The State of Texas

Executive Division
Capitol Building, 1E.8
P.O. Box 12697
Austin, Texas 78711-2697

Phone: 512-463-5770
Fax: 512-475-2761
TTY : 7-1-1
www.sos.state.tx.us

Roger Williams
Secretary of State

TO: All Interested County Officials
FROM: Roger Williams, Texas Secretary of State
DATE: March 10, 2005
RE: Best Practices Guide – Lease or Purchase Agreement and License Agreement

---

I have embarked on my 2005 County Listening Tour, and the results to date have been spectacular. The purpose of the Listening Tour was to provide a forum for county officials to sound off about some of the mandates on local counties that flow from the passage of the Help America Vote Act of 2002 ("HAVA"). And let me tell you, I have heard your concerns loud and clear, and I can sympathize with the added financial burdens that HAVA has placed on county election officials like yourselves.

As you know, the State of Texas has qualified for approximately $181 million in federal money as a result of the passage of HAVA. Each county in Texas is entitled to a portion of those federal funds based upon statistics during the 2000 federal election, including each county's voting age population expressed as a percentage of the total Texas voting age population and the number of county precincts. One of the most important provisions of HAVA that affects each Texas county is the requirement to have an accessible voting machine in each polling place in your county by January 1, 2006. We call those accessible voting machines direct recording electronic machines, or DREs. These machines are expensive, but as I said before, money is available to help pay for the cost associated with your purchase or lease of the DREs, and for training and education related to the proper use and testing of such machines.

I want all Texas counties to be HAVA-compliant by the January 1, 2006 deadline, so I have embarked on the Listening Tour to find out ways in which I may be able to help facilitate your compliance with HAVA before the deadline. One of the constant refrains that I continue to hear from small to mid-size counties is that purchasing or leasing decisions have to be made in advance of, and funding from the counties would take place before, funds were actually reimbursed to the counties through our grants process. This obviously causes counties pain from a cash-flow perspective.

The second constant complaint that I heard from you is that because HAVA is so nebulous, and the technical requirements mandated for DREs so ill-defined, that counties were hesitant to make a purchasing or leasing decision to go with a particular vendor, especially since the federal government has not yet issued recommendations on voting system standards as mandated by HAVA.

I want to offer a solution to both of these problems. Below you will find a Best Practices Guide that you can use in your negotiations with particular vendors to solve some of the complex legal and accounting issues that arise from choosing a vendor. The Best Practices Guide is intended to give you the legal firepower you need when making your procurement decision, and your ultimate execution of a contract, with your selected vendor.

This Best Practices Guide is just that – *only a guide*. You will certainly want to be in touch with your own finance, accounting, purchasing and legal advisors before making a procurement decision, and especially during the negotiation and execution of a definitive purchase or lease agreement with a vendor.

BEST PRACTICES GUIDE

(LEASE OR PURCHASE OF DRE SYSTEM AND LICENSE OF ASSOCIATED SOFTWARE)

Please use this Best Practices Guide in the event that you wish to lease or purchase the DREs required to become HAVA-compliant before the January 1, 2006 deadline.

For purposes of the Guide below, "*customer*" shall mean your county, and "*supplier*" shall mean the vendor that you choose to go forward with. There are two components to leasing or purchasing any DRE – the lease or purchase of the hardware and entering into a license agreement for the software. The trickier of these two phases clearly involves the license agreement from the supplier. We will spend time discussing a variety of the pitfalls that can occur when negotiating license agreements with third parties. In addition, we will discuss the procurement process generally, and discuss the top-line cost/benefit discussion of leasing versus purchasing a DRE voting system.

First, the lease vs. purchase decision is a threshold business decision that each county must make on the front end of this procurement. Obviously, because of the lack of definitive rules and regulations promulgated by EAC with respect to HAVA, the more conservative approach would be to take a "wait and see" attitude, not bind your county into a major commitment now, and negotiate some type of leasing arrangement with the supplier (at least until HAVA becomes a little more well defined). This conservative approach may not be for everyone, especially since this is a onetime allotment of funding from the federal government. Accordingly, some counties may choose to go ahead with a direct purchase of all the hardware and a license agreement for all the software. Or, a county may choose a "lease to buy" option, in effect, combining both of the aforementioned options.

Whichever way that you choose to obtain the hardware associated with DRE equipment, SOS is going to work very hard to make sure that you have the necessary funds directly in hand prior to your hard cost expenditure.

Please use this Guide in any manner you see fit. I want you to know that my agency and my employees are available to answer any questions you may have concerning the procurement and negotiation process with your selected vendor. Contact information for those directly responsible for aiding in these efforts is contained at the bottom of this Guide.

TABLE OF CONTENTS

PROCUREMENT

The Uniform Grant Management Standards (UGMS)

Be sure to use the county procurement procedures and regulations, provided that the procurement conforms to applicable laws and the standards identified in Chapter III (State Uniform Administrative Requirements for Grants and Cooperative Agreements), Subpart C, Section 36 of the Uniform Grant Management Standards. Attachment A on page 14 contains the text of those regulations.

Suggested Procurement Guidelines

The majority of the following information is taken from the Texas Building and Procurement Commission's ("TBPC') website and should be considered suggestions, not a mandate. **Be sure to involve your local purchaser at the onset of the process.**

A. Identify Need

1. The goals of the technology or project should be defined at the beginning of the project or technology acquisition process. In this case, the need is acquisition of HAVA-compliant voting equipment. However, there are variations of systems. For example, does the county wish to create a 100% DRE voting system or a hybrid system comprised of DREs and precinct-level optical scan devices?

2. A clear statement of expectations for the project or the technology should be included in the specifications that are developed and provided to the vendors.

B. Document Requirements

1. Do not unnecessarily limit competition.

2. Clearly and accurately describe the goods/services to be purchased.

3. When appropriate, include a statement of the work to be performed, minimum performance requirements, evaluation factors, specific features, service requirements, delivery dates, and terms.

4. Determine the appropriate procurement method. Table 1 outlines in general terms the various methods of procurement. Also consult paragraph (d) in Attachment A of this document. Again, it is important to discuss your options with your county purchaser.

Table 1

Procurement Method	Use When	Advantages	Disadvantages
Competitive Bids (Invitation for Bids)	Lots of competition exists. The product or service is available from more than one source.	Award process is simpler. Award is made to the lowest responsive, responsible bidder providing the best value to the State.	Defined specifications may be difficult to develop. Does not encourage innovative solutions.
Competitive Proposals (Request for Proposals, Request for Offer)	When factors other than price are evaluated. When negotiations are desired. Vendor is expected to provide innovative ideas.	Allows factors other than price to be considered. Allows for customized proposals suggesting different approaches to the same business need. Allows for negations in order to obtain the best value for the state.	Lead times for procurement are much greater. Evaluations are more complex and subjective.
Request for Information	There is insufficient information to write specifications for any procurement method.	Provides information to prepare a complete bid or proposal document. Allows the business community to have input into the agency's solicitation document based on current industry practices and market factors.	Lengthens the procurement process.

C. Identify Potential Vendors

1. When possible at least three vendors should be solicited.

2. Factors which may influence the selection of vendors/products include applicable law, industry reputation, HUB status, recommendations of professional technical consultants, user recommendations, and specifications.

D. Contact Vendors

1. Selected vendors should be provided with a written copy of the requirements. This can be done via the mail, e-mail or in separate face-to-face meetings with each selected vendor. Regardless, contact methods should be consistent and be documented.

2. If a vendor declines to be included and the total number of vendors drops below three, selection of another vendor should be attempted.

3. It should be explained clearly to vendors that the procurement process is an interactive negotiation process. Each vendor should be provided with the same information including the specifications, deadlines for responses, and other clarifying information.

4. Free exchange of dialogue should be conducted with each vendor until the entity has a complete understanding of the vendor's offer, and the vendor has a complete understanding of the entity's need.

5. Entity personnel that conduct negotiations with vendors should be trained in negotiation and preferably skilled in the process. The process of negotiation can be beneficial to the state and the vendor if conducted properly.

6. Vendors may be required to fill out standard forms or spreadsheets for evaluation purposes. Use of standard forms in the evaluation process may facilitate an objective analysis of the offerings and may be useful as backup documentation.

7. In addition to (but not in replacement of) the minimum requirements, vendors may propose enhancements or innovations.

8. Everything within each offer must be kept confidential until the award is final. Good judgment should be used in determining what information from any vendor's offer may be revealed to other vendors. **NOTE:** It is an unethical practice to allow vendors to "auction" their prices using this process. "Auctioning" is when vendors are required to be against each other for pricing competition.

E. Receive Initial Responses

1. Each vendor should understand that missing the deadline for submission will result in the removal of that vendor from further consideration unless the established deadline for the initial responses is delayed by a formal notice given to all vendors.

F. Evaluate Responses and Negotiate

1. Provide feedback to each vendor concerning their proposal. Have the vendor clarify missing or confusing information.

2. Negotiate for the best prices, products, services and terms as applicable.

3. Establish the deadline for all vendors to submit a "best and final" offer.

G. Select the Best Value

1. Maintain records of all pertinent information to document the evaluation and selection process.

2. Maintain appropriate confidentiality.

3. If the purchase is "open ended," continue to negotiate prices and terms with the successful vendor:

- Keep informed of trends in technology and pricing. Obtain quotes from other vendors on like goods and services. Use these quotes to evaluate goods, services and prices from the selected vendor on an ongoing basis.

- Ensure that the selected vendor passes along price changes immediately, and that the vendor works continuously with the entity to enhance service, products, and pricing.

Texas Building and Procurement Commission's Cooperative Purchasing Program

One option is to utilize the Texas Building and Procurement Commission's Cooperative Purchasing Program ("Co-Op"). Created by legislation in 1979, the TBPC Co-Op Program offers members a unique opportunity to purchase goods and services from state term contracts and the CISV Catalog Purchasing Program. Using these services through TBPC will meet your competitive bidding requirements. If you are not a member or wish to obtain additional information, please contact Co-Op staff at coop@tbpc.state.tx.us, or by phone at 512-463-3368.

The purpose of the CISV Purchasing Program is to allow for qualified entities (state agencies and political subdivisions) to purchase automated information systems products and /or services in an efficient, cost effective, and competitive procurement method. This includes voting equipment. To obtain more information about the CISV Purchasing Program, please contact CISV staff at cisv@tbpc.state.tx.us, or by phone at 512-463-3459.

LICENSE AGREEMENT

Section 1. Recitals

The opening paragraph of a license agreement, as with most agreements, addresses routine matters such as the date of the agreement and identification of the parties (names, addresses, etc.). The recitals should provide a statement of key issues, and in particular the bargaining position of the parties, which define the background and context in which the particular supplier was selected and the business needs of the customer.

Note critical points in the recitals. For instance, the customer has no existing system, or has an existing non-HAVA-compliant system, and is implementing a new HAVA-compliant system sponsored by the supplier. The recitals should state that the supplier is providing more than a copy of a software program – it is providing a business solution. This is most effectively done by incorporating the supplier's response to the customer's request for proposal. The recitals should also introduce the concept of integration by stating that the customer has acquired or is acquiring "A Recommended Hardware Configuration" and that the supplier has furnished "Software and Hardware Requirements" (which should be detailed in an exhibit), thereby further establishing the change of position being undertaken by the customer and the integrated nature of the bargain.

Finally, the recitals should show that the customer's change of position is in reliance upon the expertise of the supplier to not only acquire the Recommended Hardware Configuration and the supplier's software, but also the implementation of the business solution.

Comprehensive recitals such as those below are often difficult to negotiate because the supplier will certainly be concerned that general statements such as these could be construed broadly by a court against the supplier. Usually the supplier counters that the customer is ultimately responsible for the

selection of the solution, and that the supplier could not possibly be responsible for the information included in its proposals.

Section 2. License

The language contained in the License section is the key clause that actually grants specific license rights. A license is a limited use right, and the law generally presumes that any right not expressly granted is reserved by the licensor. Therefore, the granting clause must protect the full range of the customer's rights to use the software. Typically, a customer will want to be comprehensive in specifying the key terms for a customer's undisturbed right to use the software: a paid-up, irrevocable, worldwide, perpetual license to use the software on any CPU and for any business purpose of customer. Most often a license is also nonexclusive, meaning the supplier has and will license the software to third parties. It should be borne in mind that if the software is customized or specially developed, additional considerations regarding ownership, exclusivity, and other issues should be carefully considered.

The rights of a licensee are also defined by what is licensed. The definition of Licensed Software can be tailored to the customer's specific needs by stating that it consists of all software provided by the supplier including the specific software that is the business solution for the customer.

Section 3. Title

The license agreement recognizes that the supplier is the owner of the software. This is appropriate, since a well-drafted license will give a customer all of the rights it will need for its use of the software. Additionally, ownership is the legal vehicle through which the supplier will be held responsible for its obligations, such as indemnifications and warranties.

Section 4. Authorized Users

Authorized Users gives the supplier something by making a general statement of the customer's obligation to limit use of the software, but then takes it back by giving the customer broad rights for those people who are defined as "*authorized users*" — employees, agents, consultants, outsourcers, and contractors. A customer should think of the situations that may require use of a program by third parties and then ensure that its counsel and consultants are aware of those situations so that they can be taken into account in this section.

Section 5. Delivery and Installation

The supplier should be responsible for shipping and risk of loss. Risk of loss should pass only upon Final Acceptance, a term you will want to define in your agreement that occurs after successful acceptance testing of the software. The customer should also seek a provision here that allows the customer to delay shipping and installation (each at no cost to customer) for up to 90 days for both delivery and installation, thereby giving the customer a window of up to 180 days to implement delivery and installation. Such a provision is another example of how to build flexibility into an acquisition, especially when the customer is putting together a system and not simply adding application software.

Section 6. Payment

This is one of the areas were we have heard the "cash-flow" concerns of the counties loud and clear. Because payment of HAVA funds from our office is made on a reimbursement basis after your procurement decision and contract have been executed, it is important to remain as flexible as possible with this term. Generally, suppliers expect partial payments at four different milestones: delivery,

installation, preliminary testing, and final testing. The Guide suggests that no progress payments be made until final testing is completed. This will have the benefit of pushing out the time in which final payment is due to supplier, thereby allowing our office to process your request for payment during the interim between contract execution and final acceptance testing. Customers may consider making the earlier progress payments based on achieving some of the milestones above, but should not commit to anything unless they are sure that they have otherwise received their reimbursement from our office.

Section 7. Invoicing

Invoicing is another area where a customer can build in enough flexibility to ensure that SOS reimbursement funds are received prior to suppliers receiving payment, thereby solving the "cash-flow" problem. The Guide suggests that customers provide for 60 day net invoicing – in other words, no payments are required until 60 days following receipt of any invoice. In addition, it is wise to provide that the customer is required to pay only undisputed invoices. This is an important contractual right that allows the customer to maintain a control position during performance. If the supplier protests unilateral withholding of payment by the customer, a fallback position would be to state that the payment will be made unless disputed "in good faith" by the customer. You will also want some additional assurance that if a dispute develops, that the supplier remains under an obligation to continue performance even when there is a dispute.

Section 8. Documentation and Training

Documentation is often defined as something as simple as a user manual. The Guide suggests that documentation also include several additional provisions: (i) a requirement for product overview and step-by-step procedures (in addition to any on-line help desk functions); (ii) the delivery of sufficient copies and the ability to use those copies as need by the business; (iii) a representation and warranty that the documentation is sufficient to allow appropriately skilled people to use, modify, and enhance the software; (iv) the extension of the warranty to modifications and upgrades; and (v) a requirement to provide documentation for any third-party software.

The Guide also suggests that the supplier be required to notify the customer of, and allow the customer to participate in user groups, bulletin boards, and other on-line services. As these services become more accepted, the customer can take advantage of them and perhaps use them to negotiate lower maintenance fees.

It is also suggested that the supplier be required to provide hands-on training at the customer's site, at the supplier's expense. Specific training suggestion should include, but not be limited to, the following:

> The supplier shall provide extensive training programs on all phases of the voting system(s). The training shall provide State, county, and local election personnel with sufficient training in order to operate the DRE system without continuous support by the supplier. Supplier shall provide a maximum of five (5) training classes per program (e.g. voting unit, election management system, ballot creation and layout software) for customer for initial contract period and each renewal period exercised. Dates for training sessions will be mutually agreed upon between customer and supplier.
>
> The training should also include, but shall not be limited to, the following topics:
>
> - Training on the use of the ballot creation and layout software, if applicable;
> - Programming of tabulators;

- Preparation of tabulators including set up and pre-election testing;
- Election day and early voting operations from the opening to the closing of the polls;
- Printing of zero counts before the polls open;
- Processing of voters, early voting ballots, and provisional ballots;
- Use of central counting station functions;
- Troubleshooting to solve temporary problems;
- Hot points for system errors;
- Safeguards to prevent and detect tampering;
- Tabulation of results;
- Electronic transmission of election results;
- Printing, designing and reformatting election reports;
- Methods of ensuring the accuracy of precinct results;
- Use of battery backup feature(s);
- Taking a malfunctioning piece of equipment out of service;
- Full understanding of the audit procedures;
- Conducting a recount;
- Records preservation; and
- How and when to place service calls.

The supplier should also represent that it will assist county and local election officials (if requested) in conducting comprehensive training for election judges and clerks for their various precincts prior to the primary and general elections in the first year of use.

Section 9. Maintenance and Support

The strategy of some suppliers is to bundle license or use rights with maintenance such that the customer becomes totally committed to the supplier's maintenance.

The Guide suggests that you attempt to de-link maintenance from any other license or use right, separating the product from the service. You should also seek to require the supplier to provide maintenance as long as the customer pays the fees. Again, control and flexibility should be part of the customer's bargain. The Guide also suggests that you make clear that contract maintenance begins at the end of the warranty period. Often, suppliers allow the maintenance period to overlap the warranty period, even though they amount to the same service level.

Response times for service calls at and around election times are obviously critical. We suggest that you incorporate, at a minimum, some type of heightened response before, during, and immediately following election periods. We suggest something similar to the following:

- An "election period" begins 30 days prior to any election day and continues through the 30th day after an election day. Service shall be available Monday through Saturday, 7am to 7pm during an election period. Telephone responses to service calls on any election day and during an early voting period shall not exceed 1 hour. On-site response shall not exceed 1 hour in urban areas and 3 hours in rural or remote areas; and

- Service calls required other than during an "election period". Service and support shall be available Monday through Friday, 8am to 5pm, local time. Telephone responses to service calls shall not exceed 4 hours. On-site response shall not exceed 4 hours in urban areas and 8 hours in rural or remote areas.

Other suggestions specific to support personnel include the following:

- Be well trained and experienced in the maintenance and repair of direct recording electronic voting systems, and capable of replacing malfunctioning equipment in the polling place;

- Have reliable dedicated transportation of sufficient size to accommodate the transport of voting equipment;

- Be prepared, on election day and during the early voting period, to replace voting equipment that cannot be repaired within two hours following arrival at the polling location at which the equipment is used;

- Maintain, on election day and during the early voting period, a reasonable supply of spare parts and components necessary to repair malfunctioning equipment and return it to service; and

- Have cellular telephones or other means of real time communication, on election day and during the early voting period, so that they may be dispatched to polling locations that are experiencing system malfunctions.

A number of structures can be used for response times, including categories of severity, chain-of-command reporting, measurement of response times over extended periods, maintaining and providing access to electronic bulletin boards, and e-mail communications.

Service Tracking and Reporting requires the supplier to track service calls made under the maintenance program. This information becomes valuable to the customer when the customer negotiates a renewal of services based upon the effectiveness of training.

Most suppliers also condition continuing maintenance services upon the customer's having installed the most current release of the software, arguing that they do not want to be obligated to support different release levels. The customer may want to provide that it can decline to implement enhancements or new releases if those programs interfere with the customer's intended usage or operating environment.

A common problem for software users, even when they pay for maintenance, is that there is seldom an effective remedy in the event of a supplier default. The supplier's sole obligation usually is to re-perform the service until they get it right. The Guide suggests that the customer provide for liquidated damages for a system-down time that is caused by any product supplied by the supplier. Customers should expect solid resistance to such a proposal from the supplier.

Section 10. Warranties

The Guide suggests a comprehensive list of warranties that protect the customer in the event that the business solution of the software does not perform as promised. These warranties should include, at a minimum, the following:

Warranties as to:

- functions and features;
- performance;
- compatibility;
- conformance to specifications;
- configuration;
- pass-through of third-party warranties;
- government consents (if needed);
- infringement;
- past success; and
- supplier capability.

The customer may not be able to get warranties for all of these items, but this is a comprehensive list of the most appropriate warranties to seek. Some provisions are worth additional mention. From an overall concept standpoint, the warranties discussed above are meant to work end-to-end from the date of final acceptance through the date of commencement of maintenance services, which do not begin (and the customer does not pay for) until after the warranty period. The customer should seek to ensure that it receives the same coverage during the warranty period as provided under the maintenance agreement, including response times. As a remedy for breaches of the any of the foregoing warranties, customer should provide for a refund of all fees in the event that the software fails to meet that particular warranty.

Section 11. Most Favored Nation Clause

Suppliers do not like clauses that provide "most favored customer" (MFC) status to the customer. Under such a clause, the supplier agrees that the customer will have terms and conditions no less favorable than the supplier has offered to any other customer. Note that this provision is not limited to financial terms. A well drafted MFC clause requires the supplier to notify the customer of any more favorable contract and to refund any savings resulting from the MFC clause, and the agreement is automatically amended to include more favorable positions. Usually, a supplier will only grant a customer MFC status when either (a) the supplier is starting up and is willing to give up financial terms to get a product in the marketplace; or (b) the customer will likely be the most preferred licensee of the software and the business relationship is too important to lose.

Section 12. Modifications

One of the major complaints that I heard on my Listening Tour was that because HAVA is so ill-defined: "How do I [county] ensure that my software meets or exceeds federal standards that may change in the future." The Guide provides an answer to this complaint. In the "Modification" section of the license agreement, you need to make a couple of things very clear.

- The right of the supplier to make modifications is stated, but it is also clear that modifications are part of what is already licensed under the agreement, and not a new product (with a corresponding license fee); and

- The Contractor shall perform the following:

  - Make system modifications as deemed necessary by contractor, state, county, or local election official, *or any modification due to new requirements or standards mandated by Federal or State laws at no additional cost to the customer.*;
  - Any unit or system modifications (regardless of the basis for the modification) must be certified by the Office of Secretary of State ("*SOS*") before release;

- Obtain re-certification from SOS in time to comply with applicable State and Federal administration and election timelines;
- Apply supplier-opted modifications to all previously-installed systems at no cost to the customer when a system is covered by an existing maintenance agreement; and
- Supplier shall notify entities if 3rd party software upgrades are required. The purchase of any upgrades of 3rd Party software will be a responsibility of the customer.

Section 13. Miscellaneous

There are a number of other provisions specific to all contracts that could be mentioned here, including indemnification and limitations on liability, assignment provisions, insurance requirements, confidential and proprietary information provisions, taxes, authority issues, etc. that are outside the scope of this memorandum. An attorney well-versed in basic contract law will be able to help you with all of the various miscellaneous provisions.

By providing you this Guide, my hope is that you get some idea about the kinds of terms and conditions that you can ask for, and receive, from the vendors that you choose to go forward with. In particular, I wanted to be able to offer a contract solution to the two issues that I continued to hear about on my Listening Tour concerning cash-flow difficulties and federal standard representations.

My staff and I stand ready to help you in anyway that we can. I am encouraged by your efforts to be compliant with HAVA before the January 1, 2006 deadline. But we can do better. The money is there for you to meet the requirement of one DRE in each polling place. You now, with this Guide, have some idea of the types of terms and conditions that you can ask for in the contract with your selected vendor. Now the rest is up to you.

Please feel free to contact my Chief of Staff, Benjamin M. Hanson, or my HAVA Grants Manager, Dan Glotzer, with any questions, comments or concerns with respect to this Guide, or more generally if you have any questions concerning the reimbursement process that we have put in place for HAVA. Ben can be reached directly at (512) 475-2813, or via e-mail at bhanson@sos.state.tx.us. Dan can be reached at (512) 463-9861, or via e-mail at dglotzer@sos.state.tx.us.

ATTACHMENT A

Uniform Grant Management Standards (UGMS) Procurement Regulations

____.36 Procurement

(a) States. When procuring property and services under a grant, a state will follow the same policies and procedures it uses for procurements from its non-federal funds. The state will ensure that every purchase order or other contract includes any clauses required by federal statutes and executive orders and their implementing regulations. State or local laws which impose more stringent requirements on purchases or contracts made by a subrecipient must be followed. State agencies should consult Title 10, Texas Government Code and the Texas Building and Procurement Commission Procurement Manual for applicable procurement laws and procedures. Other grantees and subgrantees will follow paragraphs (b) through (i) in this section.

(b) Procurement standards.

(1) Grantees and subgrantees will use their own procurement procedures which reflect applicable state and local laws and regulations, provided that the procurements conform to applicable federal law and the standards identified in this section. Grantees of the state that choose to use the Texas Building and Procurement Commission's cooperative purchasing program will be presumed to have met state bid requirements.

(2) Grantees and subgrantees will maintain a contract administration system which ensures that contractors perform in accordance with the terms, conditions, and specifications of their contracts or purchase orders.

(3) Grantees and subgrantees will maintain a written code of standards of conduct governing the performance of their employees engaged in the award and administration of contracts. See Section ____.14, Subsection (a) (1) and Chapter 171, Local Government Code, for additional ethics provisions. No employee, officer or agency of the grantee or subgrantee shall participate in the selection, or in the award or administration of a contract supported by federal funds if a conflict of interest, real or apparent, would be involved. Such a conflict would arise when:

(i) The employed, officer or agent,

(ii) Any member of his immediate family,

(iii) His or her partner, or

(iv) An organization which employs, or is about to employ, any of the above, has a financial or other interest in the firm selected for award. The grantee's or subgrantee's officers, employees or agents will neither solicit nor accept gratuities, favors or anything of monetary value from contractors, potential contractors, or parties to subagreements. Grantee and subgrantees may set minimum rules where the financial interest is not substantial or the gift is an unsolicited item of nominal intrinsic value. To the extent permitted by state or local law or regulations, such standards of conduct will provide for penalties, sanctions, or other disciplinary actions for violations of such standards by the grantee's and subgrantee's officers, employees, or agents, or by contractors or their agents. The awarding agency may in regulation provide additional prohibitions relative to real, apparent, or potential conflicts of interest.

(4) Grantee and subgrantee procedures will provide for a review of proposed procurements to avoid purchase of unnecessary or duplicative items. Consideration should be given to consolidating or breaking out procurements to obtain a more economical purchase. Where appropriate, an analysis will be made of lease versus purchase alternatives, and any other appropriate analysis to determine the most economical approach.

(5) To foster greater economy and efficiency, grantees and subgrantees are encouraged to enter into state and local intergovernmental agreements for procurement or use of common goods and services.

(6) Grantees and subgrantees are encouraged to use federal and state excess and surplus property in lieu of purchasing new equipment and property whenever such use is feasible and reduces project costs.

(7) Grantees and subgrantees are encouraged to use value engineering clauses in contracts for construction projects of sufficient size to offer reasonable opportunities for cost reductions. Value engineering is a systematic and creative analysis of each contract item or task to ensure that its essential function is provided at the overall lower cost.

(8) Grantees and subgrantees will make awards only to responsible contractors possessing the ability to perform successfully under the terms and conditions of a proposed procurement. Consideration will be given to such matters as contractor integrity, compliance with public policy, record of past performance, and financial and technical resources.

(9) Grantees and subgrantees will maintain records sufficient to detail the significant history of procurement. These records will include, but are not necessarily limited to the following: rationale for the method of procurement, selection of contract type, contractor selection or rejection, and the basis for the contract price.

(10) Grantees and subgrantees will use time and material type contracts only—

(i) After a determination that no other contract is suitable, and

(ii) If the contract includes a ceiling price that the contractor exceeds at its own risk.

(11) Grantees and subgrantees alone will be responsible, in accordance with good administrative practice and sound business judgment, for the settlement of all contractual and administrative issues arising out of procurements. These issues include, but are not limited to source evaluation, protests, disputes, and claims. These standards do not relieve the grantee or subgrantee of any contractual responsibilities under its contracts. Federal or state agencies will not substitute their judgment for that of the grantee or subgrantee unless the matter is primarily a federal or state concern. Violations of law will be referred to the local, state, or federal authority having proper jurisdiction.

(12) Grantees and subgrantees will have protest procedures to handle and resolve disputes relating to their procurements and shall in all instances disclose information regarding the protest to the awarding agency. A protester must exhaust all administrative remedies with the grantee and subgrantee before pursuing a protest with the federal agency. Reviews of protests by the federal agency will be limited to:

(i) Violations of federal law or regulations and the standards of this section (violations of state or local law will be under the jurisdiction of state or local authorities) and

(ii) Violations of the grantee's or subgrantee's protest procedures for failure to review a complaint or protest. Protests received by the federal agency other than those specified above will be referred to the grantee or subgrantee.

(c) Competition.

(1) All procurement transactions will be conducted in a manner providing full and open competition consistent with the standards of Section ____.36. Some of the situations considered to be restrictive of competition include but are not limited to:

(i) Placing unreasonable requirements on firms in order for them to qualify to do business,

(ii) Requiring unnecessary experience and excessive bonding,

(iii) Noncompetitive pricing practices between firms or between affiliated companies,

(iv) Noncompetitive awards to consultants that are on retainer contracts,

(v) Organizational conflicts of interest,

(vi) Specifying only a "brand name" product instead of allowing "an equal" product to be offered and describing the performance of other relevant requirements of the procurement, and

(vii) Any arbitrary action in the procurement process.

(2) Grantees and subgrantees will conduct procurements in a manner that prohibits the use of statutorily or administratively imposed in-state or local geographical preferences in the evaluation of bids or proposals, except in those cases where applicable federal statutes expressly mandate or encourage geographic preference. Nothing in this section preempts state licensing laws. When contracting for architectural and engineering (A/E) services, geographic location may be a selection criteria provided its application leaves an appropriate number of qualified firms, given the nature and size of the project, to compete for the contract.

(3) Grantees will have written selection procedures for procurement transactions. These procedures will ensure that all solicitations:

(i) Incorporate a clear and accurate description of the technical requirements for the material, product, or service to be procured. Such description shall not, in competitive procurements, contain features which unduly restrict competition. The description may include a statement of the qualitative nature of the material, product or service to be procured, and when necessary, shall set forth those minimum essential characteristics and standards to which it must conform if it is to satisfy its intended use. Detailed product specifications should be avoided if at all possible. When it is impractical or uneconomical to make a clear and accurate description of the technical requirements, a "brand name or equal" description may be used as a means to define the performance or other salient requirements of procurement. The specific features of the named brand which must be met by offerors shall be clearly stated; and

(ii) Identify all requirements which the offerors must fulfill and all other factors to be used in evaluating bids or proposals.

(4) Grantees and subgrantees will ensure that all prequalified lists of persons, firms, or products which are used in acquiring goods and services are current and include enough qualified sources to ensure maximum open and free competition. Also, grantees and subgrantees will not preclude potential bidders from qualifying during the solicitation period.

(d) Methods of procurement to be followed.

(1) Procurement by small purchase procedures. Small purchase procedures are the relatively simple and informal procurement methods for securing services, supplies, or other property that do not cost more than $100,000 in the aggregate. If small purchase procurements are used, price or rate quotations will be obtained from an adequate number of qualified sources. As of April 2000, the federal small purchase threshold had risen to $100,000. However, the State of Texas Building and Procurement Commission "informal" procurement threshold was $15,000. State agencies should consult Title 10, Chapter 2156, Texas Government Code and the Texas Building and Procurement Commission Procurement Manual for applicable laws and procedures governing procurement. Municipalities should consult Chapter 252, Texas Local Government Code. Counties should consult Chapter 262, Texas Local Government Code. In case of conflicts between A-102 and state law involving state funds, state law will prevail.

(2) Procurement by sealed bids (formal advertising). Bids are publicly solicited and a firm-fixed-price contract (lump sum or unit price) is awarded to the responsible bidder whose bid, conforming to all the material terms and conditions of the invitation for bids, represents best value to the state. The sealed bid method is the preferred method for procuring construction, if the conditions in Section ____.36 (d) (2) (i) apply. State agencies should consult Title 10, Chapter 2156, Texas Government Code and the Texas Building and Procurement Commission Procurement Manual for applicable laws and procedures governing

procurement. Municipalities should consult Chapter 252, Texas Local Government Code. Counties should consult Chapter 262, Texas Local Government Code. In case of conflicts between A-102 and state law involving state funds, state law will prevail.

(i) In order for sealed bidding to be feasible, the following conditions should be present:

(A) A complete, adequate, and realistic specification or purchase description is available;

(B) Two or more responsible bidders are willing and able to compete effectively for the business; and

(C) The procurement lends itself to a firm fixed price contract and the selection of the successful bidder can be made principally on the basis of price.

(ii) If sealed bids are used, the following requirements apply:

(A) The invitation for bids will be publicly advertised and bids shall be solicited from an adequate number of known suppliers, providing them sufficient time prior to the date set for opening the bids;

(B) The invitation for bids, which will include any specifications and pertinent attachments, shall define the items or services in order for the bidder to properly respond;

(C) All bids will be publicly opened at the time and place prescribed in the invitation for bids;

(D) A firm fixed-price contract award will be made in writing to bidder(s) whose bid(s) represent best value to the state. Where specified in bidding documents, factors such as discounts, transportation cost, and life cycle costs shall be considered in determining which bid is lowest. Payment discounts will only be used to determine the low bid when prior experience indicates that such discounts are usually taken advantage of; and

(E) Any or all bids may be rejected if there is a sound documented reason.

(3) Procurement by competitive proposals. State agencies should consult Title 10, Chapter 2156, Texas Government Code and the Texas Building and Procurement Commission Procurement Manual for applicable laws and procedures governing procurement. Municipalities should consult Chapter 252, Texas Local Government Code. Counties should consult Chapter 262, Texas Local Government Code. In case of conflicts between A-102 and state law involving state funds, state law will prevail. The technique of competitive proposals is normally conducted with more than one source submitting an offer, and either a fixed-price or cost-reimbursement type contract is awarded. It is generally used when conditions are not appropriate for the use of sealed bids. If this method is used, the following requirements apply:

(i) Requests for proposals will be publicized and identify all evaluation factors and their relative importance. Any response to publicized requests for proposals shall be honored to the maximum extent practical;

(ii) Proposals will be solicited from an adequate number of qualified sources;

(iii) Grantees and subgrantees will have a method for conducting technical evaluations of the proposals received and for selecting awardees;

(iv) Awards will be made to the responsible firm whose proposal is most advantageous to the program, with price and other factors considered; and

(v) Grantees and subgrantees may use competitive proposal procedures for qualifications-based procurement of architectural/engineering (A/E) professional services whereby competitors' qualifications are evaluated and the most qualified competitor is selected, subject to negotiation of fair and reasonable compensation. The method, where price is not used as a selection factor, can only be used in procurement of A/E professional services. It cannot be used to purchase other types of services though A/E firms are a potential source to perform the proposed effort. State agencies must comply with Chapter 2254, Texas Government Code, which governs professional and consulting services.

(4) Procurement by noncompetitive proposals is procurement through solicitation of a proposal from only one source, or after solicitation of a number of sources, competition is determined inadequate.

(i) Procurement by noncompetitive proposals may be used only when the award of a contract is infeasible under small purchase procedures, sealed bids or competitive proposals and one of the following circumstances applies:

(A) The item is available only from a single source;

(B) The public exigency or emergency for the requirement will not permit a delay resulting from competitive solicitation.

(C) The awarding agency authorizes noncompetitive proposals; or

(D) After solicitation of a number of sources, competition is determined inadequate.

(ii) Cost analysis, i.e., verifying the proposed cost data, the projections of the data, and the evaluation of the specific elements of costs and profit, is required.

(iii) Grantees and subgrantees may be required to submit the proposed procurement to the awarding agency for pre-award review in accordance with paragraph (g) of this section.

(e) Contracting with small and minority firms, women's business enterprise and labor surplus area firms.

(1) The grantee and subgrantee will take all necessary affirmative steps to assure that minority firms, women's business enterprises, and labor surplus area firms are used when possible. State agencies should consult the Texas Building and Procurement Commission Procurement Manual and individual agency requirements for historically under-utilized businesses (HUB) procedures. Awarding agencies may require subrecipients to adhere to state HUB requirements.

(2) Affirmative steps shall include:

(i) Placing qualified small and minority businesses and women's business enterprises on solicitation lists;

(ii) Assuring that small and minority businesses, and women's business enterprises are solicited whenever they are potential sources;

(iii) Dividing total requirements, when economically feasible, into smaller tasks or quantities to permit maximum participation by small and minority business, and women's business enterprises;

(iv) Establishing delivery schedules, where the requirement permits, which encourage participation by small and minority business, and women's business enterprises;

(v) Using the services and assistance of the Small Business Administration, the Minority Business Development Agency of the Department of Commerce, and the Texas Building and Procurement Commission;

(vi) Requiring the prime contractor, if subcontracts are to be let, to take the affirmative steps listed in paragraphs (e) (2) (i) through (v) of this section.

(f) Contract cost and price.

(1) Grantees and subgrantees must perform a cost or price analysis in connection with every procurement action including contract modifications. The method and degree of analysis is dependent on the facts surrounding the particular procurement situation, but as a starting point, grantees must make independent estimates before receiving bids or proposals. A cost analysis must be performed when the offeror is required to submit the elements of his estimated cost, e.g., under professional, consulting, and architectural engineering services contracts. A cost analysis will be necessary when adequate price competition is lacking, and for sole source procurements, including contract modifications or change orders, unless price reasonableness can be established on the basis of a catalog or market price of a commercial product sold in substantial quantities to the general public or based on prices set by law or regulation. A price analysis will be used in all other instances to determine the reasonableness of the proposed contract price.

(2) Grantees and subgrantees will negotiate profit as a separate element of the price for each contract in which there is no price competition and in all cases where cost analysis is performed. To establish a fair and reasonable profit, consideration will be given to the complexity of the work to be performed, the risk borne by the contractor, the contractor's investment, the amount of subcontracting, and the quality of its record of past performance, and industry profit rates in the surrounding geographical area for similar work.

(3) Costs or prices bases on estimated costs for contracts under grants will be allowable only to the extent that costs incurred or cost estimates included in negotiated prices are consistent with federal cost principles (see Section ____.22). Grantees may reference their own cost principles that comply with the applicable federal cost principles.

(4) The cost plus a percentage of cost and percentage of construction cost methods of contracting shall not be used.

(g) Awarding agency review.

(1) Grantees and subgrantees must make available, upon request of the awarding agency, technical specifications on proposed procurements where the awarding agency believes such review is needed to ensure that the item and/or service specified is the one being proposed for purchase. This review generally will take place prior to the time the specification is incorporated into solicitation document. However, if the grantee or subgrantee desires to have the review accomplished after a solicitation has been developed, the awarding agency may still review the specifications, with such review usually limited to the technical aspects of the proposed purchase.

(2) Grantees and subgrantees must on request make available for awarding agency pre-award review procurement documents, such as requests for proposals or invitations for bids, independent cost estimates, etc., when:

(i) A grantee's or subgrantee's procurement procedures or operation fails to comply with the procurement standards in this section; or

(ii) The procurement is expected to exceed $100,000 and is to be awarded without competition or only one bid or offer is received in response to a solicitation; or

(iii) The procurement, which is expected to exceed $100,000, specifies a "brand name" product; or

(iv) The proposed award over $100,000 is to be awarded to other than the apparent low bidder under a sealed bid procurement; or

(v) A proposed contract modification changes the scope of a contract or increases the contract amount by more than $100,000.

(3) A grantee or subgrantee will be exempt from the pre-award review in paragraph (g) (2) of this section if the awarding agency determines that its procurement systems comply with the standards of this section. State agencies should consult Title 10, Chapter 2156, Texas Government Code and the Texas Building and Procurement Commission Procurement Manual for applicable laws and procedures governing procurement, including specific dollar thresholds and their associated requirements. In case of conflicts between A-102 and state law involving state funds, state law will prevail.

(i) A grantee or subgrantee may request that its procurement system be reviewed by the awarding agency to determine whether its system meets these standards in order for its system to be certified. Generally, these reviews shall occur where there is a continuous high-dollar funding, and third party contracts are awarded on a regular basis;

(ii) A grantee or subgrantee may self-certify its procurement system. Such self-certification shall not limit the awarding agency's right to survey the system. Under a self-certification procedure, awarding agencies may wish to rely on written assurances from the grantee or subgrantee that it is complying with these standards. A grantee or subgrantee will cite specific procedures, regulations, standards, etc., as being in compliance with these requirements and have its system available for review.

(h) Bonding requirements. Chapter 2253, Subchapter B, Sec. 2253.021, Texas Government Code, requires governmental entities entering into contracts with a prime contractor for public works projects in excess of $100,000 to require a performance bond in the amount of the contract. For public works contracts in excess of $25,000, governmental entities must execute with the contractor a payment bond in the amount of the contract. These bonds must be executed by a corporate surety authorized to do business in Texas, a list of which may be obtained from the State Insurance Department. It is the responsibility of the grantee or subrecipient to ensure that other applicable state laws governing construction are followed. For construction or facility improvement contracts or subcontracts exceeding $100,000, the awarding agency may accept the bonding policy and requirements of the grantee or subgrantee provided the awarding agency has made a determination that the awarding agency's interest is adequately protected. If such a determination has not been made, the minimum requirements shall be as follows:

(1) A bid guarantee from each bidder equivalent to five percent of the bid price. The "bid guarantee" shall consist of a firm commitment such as a bid bond, certified check, or other negotiable instrument accompanying a bid as assurance that the bidder will, upon acceptance of his bid, execute such contractual documents as may be required within the time specified. State agencies should consult with the Texas Building and Procurement Commission for applicable laws and procedures governing construction.

(2) A performance bond on the part of the contractor for 100 percent of the contract price. A "performance bond" is one executed in connection with a contract to secure fulfillment of all the contractor's obligations under such contract.

(3) A payment bond on the part of the contractor for 100 percent of the contract price. A "payment bond" is one executed in connection with a contract to assure payment as required by law of all persons supplying labor and material in the execution of the work provided for in the contract.

(i) Contract provisions. Contracts must contain provisions in paragraph (i) of this section. Federal agencies are permitted to require changes, remedies, changed conditions, access and records retention, suspension of work, and other clauses approved by the Office of Procurement Policy. State agencies are permitted to require changes, remedies, changed conditions, access and records retention, suspension of work, and other clauses required by state law.

(1) Administrative, contractual, or legal remedies in instances where contractors violate or breach contract terms, and provide for such sanctions and penalties as may be appropriate. (Contracts other than small purchases).

(2) Termination for cause and for convenience by the grantee of subgrantee including the manner by which it will be effected and the basis for settlement. (All contracts in excess of $10,000).

(3) Compliance with Executive Order 11246 of September 24, 1965 entitled "Equal Employment Opportunity," as amended by Executive Order 11375 of October 13, 1967 and as supplemented in Department of Labor regulations (41 CFR Part 60). (All construction contracts awarded in excess of $10,000).

(4) Compliance with the Copeland "Anti-Kickback" Act (18 U.S.C. 874) as supplemented in Department of Labor regulations (29 CFR Part 3). (All contracts and subgrants for construction or repair).

(5) Compliance with the Davis-Bacon Act (40 U.S.C. 276a to a-7) as supplemented by Department of Labor regulations (29 CFR Part 5). (Construction contracts in excess of $2,000 when required by federal grant program legislation).

(6) Compliance with Sections 103 and 107 of the Contract Work Hours and Safety Standards Act (40 U.S.C. 327-330) as supplemented by Department of Labor Regulations (29 CFR Part 5). (Construction contracts awarded by grantees and subgrantees in excess of $2,000, and in excess of $2,500 for other contracts which involve the employment of mechanics or laborers).

(7) Notice of awarding agency requirements and regulations pertaining to reporting.

(8) Notice of awarding agency requirements and regulations pertaining to patent rights with respect to any discovery or invention which arises or is developed in the course of or under such contract.

(9) Awarding agency requirements and regulations pertaining to copyrights and rights in data.

(10) Access by the grantee, the subgrantee, the federal grantor agency, the Comptroller General of the United States, the State of Texas or any of their duly authorized representatives to any books, documents, papers, and records of the contractor which are directly pertinent to that specific contract for the purpose of making audit, examination, excerpts, and transcriptions.

(11) Retention of all required records for three years after grantees or subgrantees make final payments and all other pending matters are closed.

(12) Compliance with all applicable standards, orders, or requirements issued under section 306 of the Clean Air Act (42 U.S.C. 1857(h), section 508 of the Clean Water Act (33 U.S.C. 1368), Executive Order 11738, and Environmental Protection Agency regulations (40 CFR Part 15). (Contracts, subcontracts, and subgrants of amounts in excess of $100,000.)

(13) Mandatory standards and policies relating to efficiency which are contained in the state energy plan issued in compliance with the Energy Policy and Conservation Act (Pub. L. 94-163).