Public Purchasing and Contracting

Included here is a draft, pre-publication version of the chapter that will appear in the forthcoming publication. This draft chapter will be edited or revised prior to final publication.

By Frayda S. Bluestein

Two significant pieces of legislation affecting public contracting were enacted during the 1997 session. This first, S.L. 1997-174 (S 891), which became effective July 1, 1997, makes numerous changes in the bidding procedures that apply to local government purchasing.[1] The enactment of these changes represents the culmination of efforts over the past several years by the Carolinas Association of Governmental Purchasing, joined this year by the North Carolina Finance Officers Association and the North Carolina League of Municipalities, to update and revise the bidding laws. The law increases statutory thresholds for certain categories of contracts, recognizes several new exceptions to the bidding requirements, and makes other changes that may be viewed best as conforming the language of the statute to reflect the way it has been applied in practice.

A second important act this session increases flexibility and autonomy in contracting for the state university system. S.L. 1997-412 (S 862) delegates significant new authority to The University of North Carolina for purchasing and construction projects.

Local Government Purchasing

Formal Bid Threshold Raised

S.L. 1997-174 (S 891) raises the formal bidding threshold in G.S. 143-129 for the purchase of apparatus, supplies, materials, and equipment from $20,000 to $30,000. This change applies to cities, counties, and other local government entities. It does not apply to local school units, which are required under G.S. 115C-552(a) to purchase all materials, supplies, and equipment under contracts approved by the Department of Administration and are therefore subject to the purchasing benchmark in G.S. 143-53.1. (Changes affecting local school purchasing under this benchmark are discussed below.) With this change in the formal bidding threshold, purchase contracts costing between $5,000 and $30,000 may be entered into using the informal procedure set forth in G.S. 143-131. S.L. 1997-174 also contains a provision that raises any dollar thresholds contained in local acts to the levels established in the new law.

1. S.L. 1997-174 is also summarized in Frayda S. Bluestein, "Changes in Local Government Purchasing and Property Disposal Laws Effective July 1, 1997," *Local Government Law Bulletin* No. 79 (June 1997).

Delegation Authorized

The formal bidding statute, G.S. 143-129, has been interpreted to require that all contracts within its scope be awarded by the governing board. In both large and small jurisdictions, this requirement has caused delay in the contracting process, particularly when the board meets infrequently. Furthermore, some boards view their role in purchasing as finished after the budgetary decisions are made, and prefer to leave to the staff the acquisition of the materials and equipment in compliance with applicable bidding procedures. S.L. 1997-174 (S 891) amends the formal bidding statute to authorize the governing board to delegate authority to the manager or chief purchasing official to (1) award contracts, (2) reject bids, (3) readvertise to receive bids, and (4) waive bid bond or deposit requirements, and performance and payment bond requirements, when waiver is authorized by law. The board may adopt a resolution to effect this delegation and may limit the delegation to contracts within a specified dollar amount or of a particular type, or impose any other conditions it deems appropriate.

It is important to note that the delegation authority applies only to contracts for the purchase of apparatus, supplies, materials or equipment. It does not apply to construction or repair contracts, which still must be awarded by the governing board if they are in the formal bidding range.

New Exceptions to Formal Bidding Requirement

S.L. 1997-174 (S 891) creates two new exceptions to the bidding requirements for purchase contracts. Until now the only exception for "sole source" purchases applied only to hospitals. S.L. 1997-174 extends a portion of that exception, which is contained in G.S. 143-129(f), to local governments generally. The exemption now authorizes local governments to purchase without bidding "when performance or price competition for a product are not available; when a needed product is available from only one source of supply; or when standardization or compatibility is the overriding consideration." Several other bases for sole source purchasing specific to hospitals are retained and continue to apply only to hospitals.

The statute imposes two procedural requirements on sole source purchases. First, the governing board must award sole source contracts that are in the formal range, even if authority to award contracts has been delegated to the manager or purchasing official under the new delegation authority discussed above. Second, the governing board must keep a record of these purchases, and that record is subject to public inspection. As a practical matter, this means that a written justification for a sole source purchase, including efforts to determine whether there is competition for the product, should be prepared and made a part of the record of the board's decision to award a sole source contract.

A second exception has been referred to as the "piggybacking" exception—a convenient shorthand, but one which turns out not to be exactly descriptive. S.L. 1997-174 adds a new section (g) to G.S. 143-129 to allow local governments to purchase from a person or entity that has, within the past twelve months, contracted with another public entity to sell the same item at the same price as is offered to the local government. The prior contract may be with the federal government, any state government or agency, or any other local government in North Carolina or elsewhere, and must have been entered into following a public, formal bid process substantially similar to the one required by North Carolina's bidding statute. Technically, it is not piggybacking that is authorized, because the local government does not piggyback on a prior contract in the sense of purchasing under that contract. Instead, the local government simply purchases directly from a vendor who is willing to extend the same terms as the previous contract under a new and separate contract with the local government.

As with the sole source exception, several procedural requirements apply to the piggybacking exception. Contracts under G.S. 143-129(g) must be awarded by the governing board, notwithstanding any prior delegation of awarding authority. The board must award the contract at a regular meeting, and must publish notice no fewer than ten days before the meeting announcing its intention to waive formal bids under this exception. This notice probably should include, at a minimum, a description of the item(s) being purchased, and also could identify the

public entity that awarded the earlier contract that is the basis for the purchase. The statute allows purchases under this exception when the responsible officials within the local government determine that it is in the best interest of the unit. This suggests that some effort should be made to determine that the price and terms offered by the supplier are as good or better than those that could be obtained through bidding.

Finally, it is important to note that both of the two new exceptions apply only to purchase contracts—not to contracts for construction or repair work—and that neither exception applies to local schools which, as noted above, are governed by a different set of purchasing laws.

Purchase with Trade-In

Local governments often trade in surplus property as part of a contract to purchase replacement property. Since there are separate procedural requirements for the purchase of property (contained in G.S. Chapter 143, Article 8), and for sale of surplus property (contained in G.S. Chapter 160A, Article 12), local governments have been required to comply with two separate procedures to effect a purchase with a trade-in. In practice, many officials simply combined the process, attempting to comply with both sets of statutes in a single procedure. S.L. 1997-174 (S 891) enacts a new statute, G.S. 143-129.7, that specifically authorizes the inclusion of a trade-in option in a formal bid for a purchase contract, exempts these sales from the separate property disposal procedures, and authorizes consideration of the trade-in price in determining the lowest responsible bidder.

Bid Bond Waiver

G.S. 143-129 requires bidders to submit bid bonds or deposits with their bids as security that they will execute a contract if it is awarded to them. Prior law authorized the governing board to waive the bid bond or bid deposit for purchase contracts estimated to cost under $100,000. S.L. 1997-174 removes the dollar limitation, extending the waiver authority to all purchase contracts. (The statute does not authorize waiver of bid security for construction or repair contracts.) As noted above, the board may exercise the waiver, or may delegate the authority to do so to the manager or chief purchasing official. Bid security may be waived either for particular contracts, or for all contracts, and after such waiver, may be imposed for particular bids if desired.

Confidentiality of Informal Bids

A common concern for purchasing officials is that when they are receiving informal bids under G.S. 143-131, bidders participating in the process inquire about the bids that have already been received. This is particularly likely when bids are solicited by telephone. Purchasing officials have never been required to disclose orally bids received by telephone, but the law has required them to keep a record of bids they receive, and those records are subject to public inspection. S.L. 1997-174 (S 891) amends G.S. 143-131 to provide that informal bids do not become public until a contract is awarded.

Unauthorized Bid Opening

G.S. 143-129 makes it a misdemeanor to open a sealed bid before the time set for opening without the permission of the bidder. Sometimes, however, envelopes containing bids are erroneously opened by local government employees, particularly if the envelopes arrive without conspicuous marking indicating that they contain bids, or when they are in overnight mail envelopes with no separate envelope inside. S.L. 1997-174 (S 891) amends the statute to make it clear that the opening of an envelope constitutes a misdemeanor only if the person opening it knows that it contains a bid.

Local Government Property Disposal

Thresholds Raised

S.L. 1997-174 (S 891) raises the threshold above which local governments are required to use competitive procedures when selling personal property. Previously, G.S. 160A-266, which applies to cities, counties, and local school units, allowed the use of the private sale procedure in G.S. 160A-267 only for personal property estimated to be worth $10,000 or less. S.L. 1997-174 raises this limit to $30,000. The act also increases from $500 to $5,000 the threshold for disposal of property using informal procedures under G.S. 160A-266(c), and simplifies the reporting requirements for property sold under these procedures. This allows local governments to dispose of property valued at up to $5,000 without action by the governing board on each transaction. The governing board must delegate authority for disposal of property under 160A-266(c), and those that have previously done so probably should adopt a new resolution specifically extending that authorization to property within the new statutory limit. Finally, a small change in wording has been made in G.S. 160A-266 to clarify that the private sale procedure generally is not available for the sale of real property.

Donation of Unclaimed Bicycles

S.L. 1997-180 (H 1050) amends G.S. 15-12(b) to authorize local law enforcement agencies to donate unclaimed bicycles to charitable organizations. Without this authorization, unclaimed bicycles must be sold by public auction. Only organizations designated as Section 501(c)(3) charitable organizations by the Internal Revenue Service are eligible to receive donations under the new law. The intent to donate property under the new law must be stated in the notice that is published under G.S. 15-12(a) which gives interested parties an opportunity to claim the property. S.L. 1997-180 is also discussed in Chapter 15 (Local Government and Local Finance).

State Agency, University, and Local School Purchasing

The threshold for formal bidding on purchase contracts for state agencies, universities, and local school units is established as the "expenditure benchmark" in G.S. 143-53.1. S.L. 1997-412 (S 862) increases the benchmark from $10,000 to an amount not to exceed $25,000. G.S. 143-53(a) has been amended to authorize the director of the Division of Purchase and Contract discretion to increase the threshold, upon the request of a local school unit, community college, or state agency, after evaluating the capabilities, staff resources, and compliance record of the requesting agency.

A separate benchmark of $35,000 previously applied to special responsibility constituent institutions of The University of North Carolina (defined in G.S. 116-30.1). S.L. 1997-412 replaces that benchmark with a new statute, G.S. 116-31.10, which authorizes the UNC Board of Governors to set the benchmark for each institution at an amount not to exceed $250,000. The statute requires that in setting the benchmark the board must consider the institution's overall capabilities (including staff resources, purchasing compliance reviews, and audit reports) and consult with the director of the Division of Purchase and Contract and the director of the budget.

S.L. 1997-412 also amends G.S. 143-53 to give the director of the Division of Purchase and Contract specific power to delegate authority and prescribe procedures for securing offers for contracts costing under the benchmark amount. The director's delegation authority extends to state agencies and departments, local schools, and community colleges, but not to UNC special responsibility constituent institutions, whose delegations will be determined by the UNC Board of Governors under the new law. Procedures established by the director must include those for contract award, protest, and advertising, and will apply to all state agencies, local schools, community colleges, and state universities (including the special responsibility constituent institutions). These changes become effective January 1, 1998. The

Office of State Budget and Management must evaluate the "effectiveness and efficiency" of the increased purchasing benchmarks and delegations and report its recommendations to the General Assembly by April 15, 2001.

S.L. 1997-412 also makes some changes in G.S. 143-52, which prescribes procedures for competitive bidding by the Division of Purchase and Contract. The statute previously required advertisement of bidding opportunities in a "newspaper of statewide circulation." The statute now allows the state to advertise in a newspaper "widely distributed in this State" or through electronic means, or both, whichever is determined to be most advantageous.

S.L. 1997-412 also amends G.S. 143-52 to provide that bid tabulations (summaries of bids prepared after the bid opening) are subject to public inspection "in accordance with rules adopted by the Secretary of the Department of Administration," and that all contract information is subject to public inspection after the award of the contract. This change probably was prompted by a recent decision in an administrative hearing in which an administrative law judge held that it was improper for the state official handling a public bid opening to disclose information about the bids (including the prices offered) before the contract was awarded.[2]

University Construction Projects

S.L. 1997-412 (S 862) delegates significant new authority to the UNC Board of Governors for construction or repair projects at universities. The act delegates to the board, for projects estimated to cost $500,000 or less, the authority to (1) negotiate design fees, and supervise the award of design and construction contracts; (2) supervise and inspect work, and obtain certification of compliance with the State Building Code on projects not requiring a registered architect or engineer; and (3) develop procedures and "reasonable limitations" governing the use of "open-end design agreements" (discussed below). The board is authorized to delegate this new authority to the constituent or affiliated institutions if they are "qualified" under guidelines established by the board. These guidelines must be reported to the Joint Legislative Commission on Governmental Operations no later than December 1, 1997, and must be approved by the State Building Commission and the governor (as director of the budget). The new authority granted under this act becomes effective January 1, 1998, and expires July 1, 2001. The act requires the Office of State Budget and Management and the State Building Commission to evaluate "the process and quality" of construction completed under the new delegation in G.S. 116-31.11, including time required to complete projects, cost savings, effect on staffing needs, and any other resulting benefits or detriments. The Office of State Budget and Management and the State Building Commission must report their findings and recommendations about whether the delegation should continue to the General Assembly by April 15, 2001.

Requirements for Selecting Design Professionals

Contracts for the design of public construction projects are subject to G.S. Chapter 143, Article 3D, which generally requires announcing the need for design services, choosing the best qualified firm from those responding to the announcement, and then negotiating an acceptable fee. G.S. 143-64.31. That article contains an exemption for state capital improvement projects under the jurisdiction of the State Building Commission that are estimated to cost less than $50,000. G.S. 143-64.34. S.L. 1997-314 (H 1006) increases the threshold for that exemption to $100,000, effective October 1, 1997 for projects for which designers are selected after that date.

In addition, S.L. 1997-412 (S 862) adds a new exemption for "open-end design agreements" estimated to cost less than $300,000 for university projects as authorized under G.S. 116-31.11

2. The case is Budd Seed, Inc. v. North Carolina Department of Administration, 96 DOA 0281 (January 22, 1997). The claimant argued that it was injured by the disclosure because an award was not made after the first round of bidding, and for the second round of bidding, the claimant's bids had been exposed and were available to competitors.

(discussed above). Although not defined in the new statutes, an open-end design agreement probably is one under which a designer is hired at a set fee to work over a period of time on various projects, as opposed to a contract for the design of a discrete project. These contracts must be publicly announced and must comply with procedures adopted by the UNC Board of Governors and approved by the State Building Commission.

Procurement Card Pilot Program

A special provision in the budget bill, S.L. 1997-443 (S 352), Section 27.1, establishes a pilot program for the use of procurement cards by state agencies, community colleges, universities, and local schools. Public agencies across the country have been making increased use of procurement cards (cards issued to public employees to be used like credit cards for small and emergency purchases). Several local governments in North Carolina have started using procurement card systems and have found them to be an efficient way to reduce paperwork and staff time involved in small purchases. According to figures released by the North Carolina Department of Administration, over 80 percent of purchase transactions are under $2,500, accounting for less than 20 percent of dollars spent. By using procurement cards, the department hopes to streamline the purchasing approval process and reduce the number of checks issued by paying a single bill for all purchases made on the procurement cards. The secretary of administration was authorized to designate up to fifteen agencies to participate in the program, including at least one state agency, one community college, two constituent institutions of The University of North Carolina, and one local school administrative unit. As of September 1, 1997, the units participating in the pilot programs are the Department of Administration, the Department of Environment and Natural Resources, the Department of Health and Human Services, East Carolina University, North Carolina A & T State University, North Carolina State University, the University of North Carolina at Chapel Hill, the University of North Carolina Hospitals, the University of North Carolina at Wilmington, Alamance Community College, Central Piedmont Community College, and Wake County public schools. All state agencies, community colleges, universities, and local schools that are not chosen to participate in the pilot program are prohibited from using procurement cards until July 1, 1998. The Division of Purchase and Contract must report to the Joint Legislative Commission on Governmental Operations on March 1, 1998 about the program, including savings realized, impact on accounting and budgeting records, and purchasing history records, as well as the effect of the program on the state's ability to track both in-state and out-of-state sales tax payments by county. The latter concern may reflect the fact that since charges made on procurement cards are accumulated in a single bill, which does not separately itemize taxes, additional efforts must be made to retrieve this information.

Local School Operational Leases

S.L. 1997-236 (S 71) authorizes local school administrative units to enter into operational leases of real or personal property for use as school buildings or school facilities. An operational lease, defined according to generally accepted accounting principles, is a lease in which the lessor obtains no ownership interest or option to obtain an ownership interest in the leased property. An operational lease is distinguished from a capital lease, which would be shown as an asset for accounting purposes; an operational lease is a pure rental agreement, and is shown simply as an expense for accounting purposes. There has been uncertainty about whether local school units had authority to enter into such leases. The new law, G.S. 115C-530, explicitly authorizes the leases, and imposes several conditions on their use. Leases for terms of three years or longer, including optional renewal periods, must be approved by the county commissioners. This approval obligates the commissioners to appropriate sufficient funds in each year of the lease to meet the payments due. The statute also requires that the school's budget resolution include an appropriation sufficient to pay the amount due under the lease in the current fiscal year, and that an

unencumbered balance remain in the appropriation sufficient to pay the sums due under the lease in the current fiscal year.

S.L. 1997-236 also changes the law to allow local schools to make improvements to leased property. Formerly, a provision in G.S. 115C-521(d) prohibited local schools from making repairs to school buildings they did not own. Contracts for repair or renovation of leased property under the new law must comply with the energy guideline requirements in G.S. 115C-521(c). In addition, they must be approved by the county commissioners if they are subject to the competitive bidding requirements in G.S. 143-129(a) (the current threshold under that statute is $100,000) and do not otherwise constitute continuing contracts for capital outlay. *See* G.S. 115C-441(c1) and 115C-426(f).

Finally, operational leases must be approved by the Local Government Commission if they meet the conditions in G.S. 159-148(a)(1)–(3) (the same conditions that apply to installment purchase contracts authorized under G.S. 115C-528). Under these statutes, contracts extending for five or more years and costing $500,000 or more will be subject to Local Government Commission approval. In a related technical correction, S.L. 1997-236 clarifies that for purposes of determining whether Local Government Commission approval is required for certain local school contracts, only the $500,000 threshold in G.S. 159-148(3) applies. The alternative threshold contained in that statute is based on a percentage of the tax base and generally has been ignored since local school units do not have taxing authority.

Contractor Claims on Construction Contracts

A series of bills was introduced this session that would make it easier for contractors to recover under various types of claims arising under construction contracts. Late in the session, two of the proposals were combined in a new bill and were enacted as S.L. 1997-489 (S 122). New G.S. 143-134.2 allows a contractor to file an action against an owner on behalf of a subcontractor even if the contractor has not paid the subcontractor for the costs or damages that are the basis for the claim. Without this law, the contractor's failure to have paid the subcontractor would be a defense to the claim. The law specifies, however, that the owner is not required to pay the contractor for any costs or damages incurred by the subcontractor until the subcontractor submits proof that the contractor has paid the subcontractor. This law probably was prompted by the decision in APAC-Carolina, Inc. v. Greensboro-High Point Airport Authority,[3] in which the North Carolina Court of Appeals held that a prime contractor did not have standing to bring the claims of its subcontractor against the owner since the subcontractor, by the terms of the contract, had no direct claim against the owner.

S.L. 1997-489 also enacts a second new statute, G.S. 143-134.3, which limits the enforcement of a "no damages for delay" clause in a construction contract. These clauses limit a contractor's remedy for delay to an extension of the time for completion under the contract. Such a clause was specifically upheld in the *APAC* case.[4] The new law includes some important qualifications. The restriction only applies to contract provisions that limit recovery for delay "caused solely by the owner or its agent," and the law makes clear that prime contractors or their subcontractors do not constitute agents of the owner for purposes of this law. This is an important provision, since it leaves open the possibility of limiting damages for delay caused by prime contractors on a multi-prime contract.

Both of these new laws became effective October 1, 1997.

3. 110 N.C. App. 664, 431 S.E.2d 508 (1993), review denied, 335 N.C. 171, 438 S.E.2d 197 (1993).

4. 110 N.C. App. 664 at 678, 431 S.E.2d 508 at 516.

Legislative Directives Relating to Construction

Several provisions in the budget bill, S.L. 1997-433 (S 352), create new directives relating to state construction.

Section 34.9 of S.L. 1997-443 enacts the Capital Improvement Planning Act as G.S. Chapter 143, Article 1A. The act calls for a comprehensive inventory of state-owned facilities, development of criteria for evaluating proposed capital improvement projects, and preparation of a six-year capital improvement plan presented to the General Assembly by the director of the budget on or before December 31 of each even-numbered year. This legislation is discussed in more detail in Chapter 2 (The State Budget).

Section 32.23 of S.L. 1997-443 directs the Department of Transportation to develop a plan for meeting its goals for participation by minority- and women-owned businesses in construction and supply contracts. The plan must be submitted to the Joint Legislative Transportation Oversight Committee and the Fiscal Research Division by December 1, 1997.

Section 8.42 of S.L. 1997-443 authorizes the State Board of Education to use funds allotted from the State Aid to Local School Administrative Units to establish a prototype school design clearinghouse established by G.S. 115C-521(e).

Agencies Exempted from State Bidding Requirements

S.L. 1997-331 (S 141) exempts the State Ports Authority and the North Carolina Seafood Industrial Park Authority from certain bidding requirements. The law amends G.S. 143B-465 to authorize the Ports Authority to avoid certain competitive bidding requirements if necessary to expedite delivery of a particular port facility. G.S. 113-315.36 was amended to allow the Seafood Industrial Park Authority to carry out the bidding requirements for purchasing and construction without being subject to the jurisdiction of the Department of Administration.

Several local governments obtained local acts temporarily exempting them from compliance with the bidding requirements that apply to local construction projects. This has been a common trend in prior years, but is noteworthy this year for the following reason. In the 1995 session, the General Assembly enacted a law that authorizes local governments and state agencies to petition the State Building Commission for approval to use alternative contracting methods, including methods other than the multi-prime contracting method required by G.S. 143-128. Some of those who supported this new process hoped that it would reduce the number of local exemptions from state bidding requirements, although the legislature did not explicitly bar such local acts when it enacted the new procedure. By enacting several new exemptions this year, the legislature has confirmed that it did not intend for the approval by the State Building Commission of alternative methods to preclude local exemptions. An important difference between the two avenues for obtaining an exemption is that the statute governing exemptions by the State Building Commission prohibits the commission from approving an exemption from G.S. 143-129, the statute that requires competitive sealed bids. Local acts, on the other hand, typically exempt the unit from complying with both G.S. 143-128, which requires multi-prime bidding, and G.S. 143-129. Acts exempting local governments from state bidding requirements generally contain expiration dates and are limited to a particular project. This year legislative exemptions were approved for the town of Yadkinville [S.L. 1997-3 (H 4)] for a sewage treatment plant project; Davie County [S.L. 1997-331 (S 141)] for a jail and law enforcement facilities project; the town of Manteo for a town hall project, and Dare County for the design and construction of a social services building and a health services building [S.L. 1997-455 (S 343)]. The Manteo and Dare County exemptions specify that if single prime bids are sought, multiple prime bids also must be sought, and that the unit may award a contract in its sole discretion. The legislature also allowed an exemption from competitive bidding for three schools in Johnston County which have been planned and designed using a “unitary system approach.” S.L. 1997-37 (H 740) allows these

schools to be built using separate prime contractors selected by negotiation, and requires the county to report to the legislature on the final cost of the projects.

Finally, it may be of interest to local governments that might seek approval from the State Building Commission for alternative contracting methods, that the composition of the commission has been changed so that it will now have local government representation. S.L. 1997-495 (S 815) amends G.S. 143-135.25(9) to replace the position on the commission formerly designated for a manager of physical plant operations with a position representing local government. The local government representative on the commission will be chosen from among nominations made by the North Carolina Association of County Commissioners and the North Carolina League of Municipalities.

Custom Computer Software Definition Refined

The question of whether particular types of computer software must be competitively bid often arises and is not directly addressed by the competitive bidding laws. The state sales tax law contains useful definitions of computer software, which is subject to sales tax, and custom computer software, which is not. This distinction is instructive in the interpretation of the competitive bidding laws, which generally apply to tangible personal property, as do the sales tax laws. S.L. 1997-370 (H 14) amends G.S. 105-164.3(20) to clarify that computer software delivered on a storage medium, such as a CD/ROM, a disk, or a tape, is subject to state sales tax. Custom computer software exempt from taxation is defined in G.S. 105-164.13 as software written in accordance with the specifications of a specific customer, including user manuals or other documentation that accompanies the sale of the software. Excluded from the definition of custom computer software, and thus subject to taxation, is "prewritten software that can be installed and executed with no changes to the software's source code other than changes made to configure hardware or software." These changes become effective October 1, 1997.