Do Local Governments Have to Bid Computer Software Contracts?

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Like many public and private entities, local governments in North Carolina increasingly depend on computers to conduct their business. Investments in information technology, including computer software, hardware, and related services, are costly and complicated. Rapid innovation and development of new products make it difficult for many local governments to maintain the expertise necessary to evaluate available products before investing in new systems. Local governments therefore must rely on independent consultants and suppliers of information technology products to help develop and evaluate computer systems that meet their needs.

Purchases of information technology range from simple acquisition of personal computers and prewritten software products available "off the shelf" to contracts for integrated systems involving programs designed to meet a particular need. Many purchases fall somewhere between these extremes, involving specialized software that already has been developed but must be "configured," or modified slightly, to fit the environment of each successive purchaser. Local government officials have inquired whether competitive bidding requirements apply to any or all of these contracts.

No North Carolina case has addressed that question. This article analyzes how a court might apply the bidding statutes to local government contracts for purchase of computer software, drawing analogies to similar inquiries under the sales tax law and the Uniform Commercial Code (UCC) and to cases from other states.[1] It concludes that a North Carolina court probably would rule that prewritten computer software delivered on a tangible medium is within the scope of North Carolina's competitive bidding statutes but a contract to design custom software is not. The article goes on to discuss several statutory exceptions to the bidding requirements that may apply to certain computer software contracts. Finally it describes some approaches to obtaining bids on computer software

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within the statutory framework. The article concludes that, although it is possible to purchase computer software using a competitive process that complies with North Carolina's legal requirements, that process may lack the flexibility required to obtain the best value at the best price to meet local governments' growing needs for information technology.

Interpretation of the Competitive Bidding Statutes

Local governments must obtain sealed, competitive bids for the purchase or lease-purchase of "apparatus, supplies, materials, or equipment" estimated to cost $30,000 or more.[2] They must receive informal bids for purchases costing from $5,000 to $30,000.[3] The first question to be addressed, then, is whether computer software falls within the scope of the statutes.

The North Carolina courts rarely have had occasion to interpret the scope of the competitive bidding laws over the sixty-five years since they were first enacted. The leading case is *Mullen v. Town of Louisburg*,[4] decided in 1945, in which the court faced the question of whether the bidding requirements applied to the purchase of electricity. The court held that they *did not* apply. The ruling turned on the fact that because of government regulation of electrical rates, the bidders were not able to name their price. In effect, there was no open market for competitive pricing, so conducting a competitive bidding process would have been futile.[5]

Although the *Mullen* case involved a narrow set of facts, the court discussed the meaning of the statute before reaching its holding. The terms "apparatus, materials, and equipment," the court observed, denoted particular types of *tangible personal property*. Although the term "supplies" might be open to broader definition, the court chose to confine the meaning to property of "like kind and nature," given the term's use in conjunction with the other three terms.[6]

On the basis of the *Mullen* case, then, computer software is subject to competitive bidding if it is characterized as, or considered to be, tangible personal property. Certainly most software has a tangible, physical form—from the off-the-shelf variety that one can buy in a box, to the customized form that a vendor may install directly as part of a larger, multifaceted computer system. On the other hand, computer software contracts often include a service component, and computer software also represents intangible forms of property.

Computer Software as a Service

North Carolina's competitive bidding laws apply to tangible personal property but *not* to service contracts. There is no exception in the laws for service contracts; they simply do not fall within any of the categories of contracts listed in the statutes.[7]

There are two theories under which computer software contracts could be characterized as services and thus not subject to bidding. Under one analysis the software itself could be considered a service as opposed to a tangible good. Also, it could be argued that the bidding laws do not apply to contracts that involve a service component in addition to the software.

Software as a Service

No North Carolina case has addressed the issue of whether software is considered tangible property or a service in the bidding context. The state's sales tax law, however, defines "computer software" as tangible personal property that is subject to taxation. The definition of "tangible personal property" includes "computer software delivered on a storage medium, such as a cd-rom, a disk, or a tape."[8] The statute contains an exemption, however, for "custom computer software," which is software "written in accordance with the specifications of a specific customer."[9] The statute further qualifies the definition by specifying that custom computer software does not include "prewritten software that can be installed and executed with no changes to the software's source code other than changes made to configure the hardware or software."[10]

These definitions appear to be aimed at distinguishing computer software transactions in which the service of designing a custom program predominates, from those in which the product already has been developed and is commercially available. Although significant personal effort goes into the development of many computer software products, once a product is available in a tangible form, it is no longer characterized as a service. In the case of prewritten software requiring configuration, the tax code implies that the amount of personal service involved is incidental.[11]

The same distinction appears in court rulings addressing whether computer contracts are subject to Article 2 of the UCC, which applies only to transactions in "goods."[12] One court, concluding that

computer software should be characterized as goods under the UCC, analyzed the issue this way:

> Computer programs are the product of an intellectual process, but once implanted in a medium are widely distributed to computer owners. An analogy can be drawn to a compact disc recording of an orchestral rendition. The music is produced by the artistry of musicians and in itself is not a "good," but when transferred to a laser-readable disc becomes a readily merchantable commodity. Similarly, when a professor delivers a lecture, it is not a good, but, when transcribed as a book, it becomes a good.[13]

A majority of courts considering the issue have held that transactions involving prewritten computer software constitute sales of goods and are within the scope of the UCC.[14] Later this article discusses a proposal to revise the UCC, prompted by concerns about treating computer software contracts and licenses like sales of other goods (see "Computer Software as Intangible Property or License," page 31). Despite many questions about what rights accompany software licenses, however, courts generally have held that prewritten software represents a tangible product.

Although the sales tax law and the UCC are separate from the competitive bidding laws and exist for different purposes, all three sets of laws apply to tangible personal property. A court might draw on the definitions in the sales tax law and rulings under the UCC to conclude that previously developed computer software is tangible personal property and is subject to the bidding requirements whereas a contract to develop custom computer software is a service and not within the scope of the bidding statutes.

Contracts Combining Tangible Property and Services

Many local government contracts involve the purchase of both tangible personal property and one or more services. For example, the purchase of equipment may include installation or maintenance. Computer software contracts often involve similar combinations of tangible products and services. In each of these situations, to determine whether bidding is required, it is necessary to determine which aspect of the contract is predominant or more significant.[15]

North Carolina courts have recognized in contexts other than computer software that the predominance of a service component is significant in determining whether competitive bidding is required.[16] Courts also have used this analysis in determining whether contracts involving both goods and services are subject to the UCC.[17] To determine what aspect of a contract is predominant, a court may consider whether the bulk of the cost is for the service or for the tangible goods. An alternative approach is to consider whether the primary benefit to the contracting unit derives from the knowledge and the expertise of individuals or whether their contribution is incidental.

Although no North Carolina court has addressed this issue in a case involving bidding of computer software, courts in other states have. A series of cases from New York illustrates how courts in that state have analyzed whether a computer software purchase involves primarily services or products. New York bidding law contains an exception for purchasing services "which require scientific knowledge, skill, expertise and experience."[18] A New York court applied this exception when

> [b]oth the RFP [request for proposals] and the undisputed facts contained in the record establish that, rather than a group of physical articles of electronic hardware, [the governmental agency] primarily was seeking the design of a computer system which would provide prompt, efficient, cost-effective computer services to satisfy its growing and increasingly complex needs for the next five years. Such a design required the employment of the highest skills in the field of computer science. Vendors were allowed considerable discretion in the RFP in proposing the hardware and software components of the system, and they were also encouraged by [agency] officials to be innovative and flexible in meeting the required specifications in their design proposals.[19]

The court reasoned that the agency clearly was seeking the *design* of a computer system to meet its specific needs. Another court had reached similar results in two earlier cases, one involving a computer-data-control system for off-track betting[20] and one involving a security system and service.[21] The service exception applied because the contract involved "inextricable integration of scientific and technical skills used in conjunction with electronic hardware and software."[22]

In another New York case, however, the court found that a computer system contract did not involve a substantial service component and did not fall within the service exception to bidding. The court based its decision on these facts:

> [T]he City *knew* the specific type of computer equipment it needed to meet its needs[,] . . . had conducted its own study of its computer needs and hired an independent consultant to perform a capacity study. . . . The proposers had little discretion under the RFP in selecting the hardware or software. The RFP did not

invite innovative design proposals for a computer system. The only services which the RFP called for were installation and maintenance, services which accompany many machine purchases.[23]

North Carolina courts might use a similar analysis in determining whether particular contracts involve services predominantly, or services inextricably involved in the total system being purchased, versus services incidental to the purchase. In the New York cases, the court seemed to be influenced by the amount of discretion that the bidders had in preparing their proposals. In addition, the court weighed heavily the extent to which the city would need to exercise discretion in choosing among the proposals, because the New York bidding statute, if it applied, allowed consideration of price only. As noted later, North Carolina's bidding laws allow consideration of factors in addition to price, so that issue might be less important if a case arose in this state. Furthermore, a court might conclude that the bidding laws apply even when the bidders have significant discretion in developing their bids, on the theory that the bulk of the expense consists of the hardware and the software.[24]

Local governments might urge the North Carolina courts to adopt the reasoning in the *Burroughs* case, described earlier, that when a local government relies on a vendor to design a computer system to meet its needs, the design services provided by the vendor predominate. In such a case, the argument might run, the court should treat the transaction as a service whether or not the cost of the hardware and the software represents the bulk of the expense. This argument has practical significance because the designer/vendor of an integrated computer system may not guarantee that the desired performance will be achieved if the computer hardware and software are purchased from and installed by different suppliers. Without further interpretation or clarification from the North Carolina courts, however, local governments run the risk of a challenge if they fail to use competitive bidding in these situations.

Computer Software as Intangible Property or License

As noted earlier, computer software not only has a tangible form but also consists of intangible property interests. The unique design of each computer software program (including everything from the source code to the graphic display that appears on the screen) is recognized as "intellectual property"—a form of intangible property that is protected by copyright and trade secret laws. To maintain this protection, computer software companies sell their products under a *license*, which usually limits the use of the products to the actual purchasers and restricts the products' resale, reproduction, or alteration.

Some have argued that the interest obtained under a computer software license is sufficiently limited that it is more like a lease than a purchase and, as such, should not be considered to be within the scope of the bidding statutes. (Because the bidding laws explicitly refer to "purchases," they are generally understood not to apply to lease contracts.Thus a lease of computer software, as opposed to a purchase of it, is not subject to the bidding laws. A lease with an option to purchase, however, is subject to the competitive bidding requirements.)[25]

. . . assume that computer software contracts are subject to the competitive bidding requirements unless the contracts are for custom software. . . .

In cases arising under the UCC, courts have struggled to develop a consistent body of law on the threshold question of whether a software license is a contract for the sale of goods. Although some cases hold that a license is simply not a sale,[26] courts in other cases have concluded that computer software licenses can represent the conveyance of a tangible product, despite the restrictions on the use of the product imposed under the license and the copyright laws. As one court has noted, "We treat licenses as ordinary contracts accompanying the sale of products, and therefore as governed by the common law of contracts and the Uniform Commercial Code."[27]

To make matters even more complicated, courts are not bound by parties' characterization of a transaction as either a lease, a sale, or a license. Instead, courts evaluate the actual character of the transaction. Thus a court may conclude that a contract involves a sale, even when the transaction is called a lease or a license, if it appears to give the buyer ownership of a copy:[28] "If a transaction involves a single payment giving the buyer an unlimited period in which it has a right to possession, the transaction is a sale. In this situation, the buyer owns the copy regardless of the

label the parties use for the contract."[29] Many computer software contracts, then, may involve the sale of an object embodying work that is protected by copyright, or they may involve a license for limited use of protected material but no ownership of any tangible product.

Concerns about inconsistent court rulings on the characterization of computer software contracts, and about the consequence of applying the UCC to these unique transactions, have prompted a proposed revision to the UCC. A new Article 2B would establish separate rules for software contracts (whether or not they are characterized as licenses) and licenses of information. The commentary to a recent draft of the new article notes as follows:

> [These] transactions whether licenses or sales are subject to either express or implied limitations on the use, distribution, modification and copying of the software. These limitations are commercially important because (unlike . . . newspapers and books) the technology makes copying, modification and other uses easy to achieve and essential to even permitted uses of the software. . . . [A]s a relatively new form of information transaction involving products with distinctive and unique characteristics, no common law exists on many of the important questions with reference to publisher and end user contracts regardless of whether a transaction constitutes a license or sale of a copy.[30]

It is unclear whether the unique aspects of computer software contracts that evoked the proposed revision to the UCC would influence a court's analysis of whether computer software is subject to bidding. The UCC addresses issues of contract formation and rights of the parties under the contract once it has been formed. The competitive bidding laws are designed to promote fairness and competition in public contracting and to conserve public funds.[31] The limitations that a seller places on the use of computer software may not bear on the policies promoted by bidding. As noted in the conclusion to this article, however, the unique aspects of computer software transactions suggest a need for more flexibility in the competitive process.

Until changes in the law are actually enacted, most courts will recognize that a transfer of tangible property can occur even when it is accompanied by or characterized as a license. *Local governments should assume that computer software contracts are subject to the competitive bidding requirements unless the contracts are for custom software design or development.* Before submitting a computer software contract to bidding, however, local governments should examine whether any of the statutory exceptions to bidding apply.

Exceptions to Bidding: Sole Sources and Piggybacking

Two relatively new exceptions in the competitive bidding laws may apply to certain computer software purchases: sole sources and piggybacking.

Sole Sources

The sole-source exception contained in G.S. 143-129(f) applies to purchases when "performance or price competition is not available; when a needed product is available from only one source of supply; or when standardization or compatibility is the overriding consideration." Purchases made under this exception must be approved by the governing board. The sole-source exception is fairly broad and may apply to several common computer software purchasing situations.

Purchase of upgrades to existing computer programs often will be within the scope of the sole-source exception. Usually the upgrade will be available only from the company that produced the original system. However, even if a government needs a particular make or brand, there may be more than one supplier, and in such a case the sole-source exception does not apply. For example, upgrades to products produced by Microsoft are available from numerous retail sources. Many software programs commonly used by local governments, however, are designed for specific functions unique to their operations (tax collection, financial accounting, geographic information systems, and so forth). Once a local government chooses to purchase and install a particular system, upgrades and modifications to that system are generally available only from the original provider or its successor. In these cases the sole-source exception applies.

The sole-source exception also may apply to the initial purchase of computer software. Some computer software needs may be met by only one supplier. Applying the sole-source exception to the purchase of a new computer program is more troublesome than applying it to an upgrade, however. For example, local government officials want to purchase a new software system to handle finance and purchasing operations, including accounts payable, encumbrance accounting, issuance of purchase orders, and related functions. Numerous computer programs can

complete these tasks, but they vary in the way they do it, in the types of equipment they require—indeed, in hundreds of ways, depending on the detail of the comparison. On some level, each system is unique, and each may be available from only one source. The local government officials decide that one particular system best meets their needs. Would this purchase fall within the sole-source exception?

Using the sole-source exception in the situation just described probably is not appropriate. As a general rule, if the market offers multiple products that address a particular local government's need, the unit should seek competitive bids. Many local government officials would rather not conduct a competitive process once they have identified a product that best meets their needs. They may be concerned that once they receive bids, they will have to purchase the lowest-priced product, or they may prefer negotiating with a single provider—an option not available under the bidding laws. As discussed later, however, although the competitive bidding process lacks flexibility and does not permit negotiation, it does allow local governments to purchase the best, as opposed to the lowest-priced, computer software for their particular needs.

A difficult issue in using the sole-source exception to purchase computer software arises when the contract includes both hardware and software. In most cases, even if the software is available from only one source, the hardware is available from multiple sources. The software vendor may require, or the local government desire, that the software be delivered installed on the hardware. In some cases a vendor may refuse to honor the warranty on the software if it is installed on hardware that is purchased separately. Application of the predominant-aspect rule described earlier suggests that if the hardware represents a substantial proportion of the total cost, the local government should divide the contract and separately seek bids on the hardware, or it should let the entire contract for bidding, even though the software is available from only one source. This common problem simply does not have a clear or practical solution under the competitive bidding laws as currently written.

Piggybacking

Another exception to the bidding requirements allows local governments to purchase from a contractor who has previously contracted with another public agency. Often referred to as the "piggybacking" exception, G.S. 143-129(g) provides that a local government may purchase an item without submitting the purchase to competitive bidding if another public agency (any local or state government in the country, or any federal agency) contracted to purchase the item within the previous twelve months and if the contractor is willing to sell the same product at the same price. The statute requires that the previous agency have entered into the original contract following a public-bidding procedure similar to that required of local governments in North Carolina. The statute also requires that the governing body approve the contract at a regular meeting after ten days' public notice. No action is required of the agency that issued the original contract.[32]

Although North Carolina bidding statutes allow consideration of quality, performance, and time, the lack of flexibility to tailor proposals after receiving bids may limit local governments' ability to obtain the best proposal.

Under this exception a local government may purchase computer software that another public agency has purchased without repeating the competitive bidding process as long as the prior contract is less than twelve months old. This time limitation may reflect a concern that after twelve months the prices or the competition available in the market may be sufficiently different that a new bidding process should be conducted.

A subtle limitation on the use of this exception arises if the local government wishes to modify the product purchased under the prior contract. For example, a public agency has purchased a computer system. A North Carolina local government desires to purchase that system under the piggybacking exception, but the vendor must modify it to suit the local government's needs. The purchase may violate the requirement that it be the same product that was purchased by the other agency. It is impossible to identify what specific types of changes would be deemed so significant that the purchase would no longer represent the same product previously purchased. If necessary adaptations would result in more than a nominal price increase, it might not be safe to assume that use of the exception would be upheld if challenged.[33]

Bidding of Computer Software Purchases

Computer software purchases that do not fall within an exception and do not constitute service contracts are subject to the competitive bidding requirements. This means that if the local government estimates the contract to cost $30,000 or more, it must place an advertisement in a newspaper of general circulation in the area. The advertisement must identify when and where the bids will be opened, describe when and where interested bidders can obtain specifications, and state that the governing board reserves the right to reject any and all bids. The statutes require bid and performance bonds, but these may be waived by the governing board or by the manager or purchasing officer to whom waiver authority has been delegated.[34] A waiver of bonds should occur before bids are received, and the specifications should clearly indicate whether or not bonds are required. The statutes also require that bids be awarded to the "lowest responsible bidder, taking into consideration quality, performance, and the time specified in the proposals for the performance of the contract."[35] No minimum number of bids must be obtained unless a local policy requires it.[36]

For contracts in the informal range ($5,000–$30,000), the statutes simply require that the local unit obtain bids.[37] No advertisement is required, and, again, no minimum number of bids must be obtained unless a local policy requires doing so. Nonetheless, the local government should contact at least two potential suppliers to obtain quotes because it would be difficult to argue that "bids" were sought if only one supplier was solicited. As noted earlier, if only one supplier is available, the sole-source exception may apply.[38] The standard for awarding informal contracts is the same as that for awarding formal contracts.

Use of Requests for Proposals (RFPs) in Computer Software Purchases

Despite the fact that most computer software contracts involve tangible personal property, seeking bids on computer software purchases is not like seeking bids on purchases of vehicles or office supplies. The main difference is that in many cases it is difficult, if not impossible, to prepare detailed specifications of the product to be purchased. This difficulty is not unique to computer software purchases, however, and there are approaches to specification writing that can be used to invite competition even when the details of the product are not known or when various types of products will meet the unit's need.

A commonly used approach to purchasing computer software or computer systems is a request for proposals, or RFP. Although the North Carolina bidding laws do not use the term RFP, the procedure is commonly used by other jurisdictions, and by North Carolina local governments for procuring services, which are not subject to competitive bidding requirements. An RFP usually contains a "performance" specification, which describes a desired function or outcome without specifying in detail how a vendor is to accomplish it. This process relies on the vendor's expertise, and the vendor's proposal sets out the method and the supplies necessary to perform the desired function or service. A request or an invitation for bids (RFB or IFB), on the other hand, is generally understood to be the solicitation document used in a sealed-bid procedure. An IFB typically contains detailed specifications of the item to be purchased, and bids that do not offer the item as specified must be rejected as nonresponsive. North Carolina local governments usually use this type of specification in a formal-bidding procedure.

No North Carolina case has addressed the question of whether local governments may use an RFP format with a performance specification and still comply with state bidding requirements. But cases from other states, discussed in the following paragraphs, suggest that they can. Also, the formal-bidding statutes do not limit the local unit's discretion in preparing specifications, nor do they specify the type of solicitation the unit must use. The local government must advertise and receive sealed bids at a public bid opening, but the sealed bids can be in any format designed by the local unit, as long as the specifications do not unjustifiably restrict competition.[39]

The main concern with using an RFP in formal bidding stems from the difficulty in comparing and evaluating the proposals. Unlike most formal bids, proposals for computer systems can be quite voluminous and often contain a wide range of options. When bidders submit proposals with varying approaches, it may be difficult to evaluate whether the bids are responsive (that is, whether they meet specifications)[40] and to determine which is the "lowest responsible bidder." In one case a Massachusetts court held that the use of "problem-oriented specifications" instead of definite specifications did not satisfy the applicable bidding statute.[41] On the other hand, courts in several

cases from other jurisdictions have upheld this approach, as well as the local government's discretion in selecting the best overall proposal even if it was not the lowest-priced offer.[42]

In a case arising in Georgia, a state whose legal standard for awarding contracts is similar to North Carolina's, the court upheld the use of an RFP process to purchase a computer system under the bidding statute. The court affirmed that the law allows the local government to compare proposals that vary in approach and to select the approach that best meets its needs:

> No Georgia case has held against the proposition that the lowest responsible bidder may be passed over if it is determined that a higher bidder has a decidedly better product given the specifications. . . . The county retains some discretion to consider its needs in evaluating the bids.[43]

This case is consistent with North Carolina precedent holding that the statutes do not always require awarding the contract to the lowest-dollar bidder.[44]

Lack of Flexibility in the Bidding Process

The previous discussion demonstrates that it is technically possible and legally permissible to insert some flexibility into the formal-bidding process using performance specifications and allowing a wide range of proposals as bids. A typical RFP process, however, contains elements that are *not permitted* under the formal-bidding statutes. In these respects the bidding laws lack flexibility and may hinder the local government in obtaining the best computer systems at the best price.[45]

After receiving RFPs, the parties might wish to negotiate and then modify the proposal so that it would more completely meet the needs of the unit. In some cases these modifications would change the price originally offered in the bid. Although not specifically prohibited in the bidding statutes, this type of negotiation is inconsistent with the basic tenets of competitive, sealed bidding. Under a sealed-bid process, the bidders are required to submit a complete proposal, and material modifications to bids (especially to bid prices) or deviations from specifications could be challenged as unfair to other competitors.

The legal concern with fairness under competitive bidding laws makes sense, and it can readily be applied when the IFB contains detailed specifications and when the bidders offer similar products. However, when products offered vary significantly from one another (for example, when vendors take different approaches in response to a performance specification), it is more difficult to apply a legal standard designed to establish a level playing field. In these situations, after the local government has determined through competition which proposal offers the most desirable approach, tailoring of the preferred product may not do injustice to the competitive process. Nonetheless, current law does not allow the local government to make any material modification to a proposal after its submission and before the award of a contract.

Recognizing the need for flexibility in purchasing computer software, the Legislative Research Commission's Committee on Information Technology has recommended legislation that would allow state agencies to use a "best value" procurement method for contracts involving the purchase of information technology.[46] At the time of this writing, the proposed legislation (H.B. 1357) does not apply to local governments. The best-value procurement method specifically authorizes consideration of multiple factors in awarding information technology contracts, including the total cost of acquiring, operating, maintaining, and supporting the product over its projected lifetime; the technical merit of the vendor's proposal; the vendor's past performance; and the likelihood that the vendor can perform the requirements stated in the solicitation on time, with high quality, and in a manner that accomplishes the stated business objectives.[47] Information technology is defined in the proposed legislation to include "electronic data processing and telecommunications goods and services, microelectronics, software, information processing, office systems," and related consulting and design services.[48]

The committee's proposed legislation also authorizes a "solution-based solicitation" method for procurements of highly complex information technology. This is similar to the performance specification approach discussed earlier.

In support of its recommendation, the committee notes as follows:

> Information technology is more complex, more volatile, and often considerably more expensive than most commodities purchased by the State, and therefore should be acquired differently. In many cases State agencies seek a technology solution to a business problem, but are unsure of exactly what that technology solution might be. In such cases it is not appropriate to use the traditional means of selecting

> contractors, whereby the requirement is expressed in terms of detailed technical specifications and the lowest bid which meets specifications receives the award. It is more appropriate to evaluate vendors' proposals and select a contractor on the basis of "best value," meaning the best tradeoff between price and performance, where quality is considered an integral performance factor.[49]

The report notes that the existing competitive bidding laws applicable to state agencies do not prohibit consideration of factors in addition to price. (As noted earlier, the legal standard that applies to local governments similarly allows consideration of factors in addition to price.) The committee found, however, that the technique often is not used in situations when it might be. The need for expertise in employing the best-value procurement method prompted the committee to call for training in addition to specific legislative authority.[50]

Other public agencies already have established more flexible competitive procedures for procurement of information technology.[51] Charlotte obtained local legislation in 1993 to exempt the city from competitive bidding for the purchase of telecommunication, data-processing, and data-communication equipment, supplies, and services. The local act created a new provision in the city's charter authorizing the city to use a flexible competitive process for these purchases that includes the option to negotiate.[52] Tennessee has enacted a statute authorizing the use of a two-step sealed-bidding procedure.[53] The procedure calls for prices and technical information to be submitted and evaluated separately. The Tennessee statute allows the state to obtain additional information from bidders to facilitate evaluation of technical proposals, and it appears to allow adjustment of both technical and price bids if necessary to meet performance requirements.

A similar type of flexibility is provided in the Model Procurement Code for state and local governments, developed by the American Bar Association. The code, which has not been adopted in North Carolina, allows for a procedure called "competitive sealed proposals," combining a sealed, competitive process with the flexibility of an RFP process.[54] The competitive sealed-proposal process allows discussions for clarification after proposals have been opened and allows changes in proposals. Precautions must be taken under this procedure to treat the offerors fairly and to ensure that information gleaned from competing proposals is not disclosed to the other offerors.[55]

These modified competitive procedures provide the flexibility that seems particularly important to develop computer software contracts that are both cost-effective and responsive to the specific needs of the governmental agency. Although the North Carolina bidding statutes allow—indeed require—consideration of quality, performance, and time, the lack of flexibility for local governments to tailor proposals after they receive bids may limit the local governments' ability to obtain the best proposal. Further, it may tempt units to avoid seeking competition altogether, even when avoidance is not clearly authorized.

Notes

1. The Uniform Commercial Code is a set of uniform laws that have been enacted in substantially the same form in every state. The laws are designed to modernize the law of commercial transactions and to provide uniformity and continuity of basic legal issues involved in commercial transactions in order to facilitate interstate commerce. In North Carolina the UCC can be found in Chapter 25 of the General Statutes.

2. N.C. Gen. Stat. [hereinafter G.S.] § 143-129.

3. G.S. 143-131.

4. Mullen v. Town of Louisburg, 225 N.C. 53, 33 S.E.2d 484 (1945).

5. In light of the impending deregulation of the electrical supply industry, this case no longer may be a reliable statement of the application of the bidding requirements to the purchase of electricity.

6. *Mullen*, 225 N.C. at 58, 33 S.E.2d at 487.

7. Construction or repair services are covered by the bidding laws, and contracts for architectural, engineering, or surveying work are subject to the procedures in G.S. 143-64.31, -64.32.

8. G.S. 105-164.3(20).

9. G.S. 105-164.13(45).

10. G.S. 105-164.13(45).

11. *See* International Business Mach. Corp. v. Director of Revenue, State of Missouri, 765 S.W.2d 611, 612 (1989) (holding that computer software was subject to sales tax and was neither a service nor customized because modifications from product available in catalog were minimal).

12. G.S. 25-2-102, -2-105.

13. Advent Sys. Ltd. v. Unisys Corp., 925 F.2d 670, 675 (3d Cir. 1991) (holding that computer software contract involved sale of "goods" and was covered by UCC). *See also* Architectronics v. Control Sys., 935 F. Supp. 425, 431, n.5 (S.D.N.Y. 1996) (holding that agreement to write software was not subject to UCC).

14. *See* Andrew Rodau, "Computer Software: Does Article 2 of the Uniform Commercial Code Apply?" *Emory Law Journal* 35 (1986): 853; NMP Corp. v. Parametric Technology, 958 F. Supp. 1536, 1542 (N.D. Okla. 1997).

15. For further discussion of the "predominant aspect" rule for interpreting the competitive bidding statutes, *see* Frayda S. Bluestein, *A Legal Guide to Purchasing for North Carolina Local Governments* (Chapel Hill, N.C.: Institute of Government, The University of North Carolina at Chapel Hill, forthcoming 1998), 22–23.

16. *See* Plant Food Co. v. Charlotte, 214, 22–23 N.C. 518, 522, 199 S.E. 712, 715 (1938) (holding that contract for removal of sludge from waste treatment system was service contract rather than sale of city property).

17. Batiste v. American Home Prod. Corp., 32 N.C. App. 1, 6, 231 S.E.2d 269, 272, *disc. rev. denied*, 292 N.C. 466, 233 S.E.2d 921 (1977).

18. Pacificorp Capital v. New York City, 741 F. Supp. 481, 485 (S.D.N.Y. 1990).

19. Burroughs Corp. v. New York State Higher Educ. Serv. Corp., 458 N.Y.S.2d 702, 704 (N.Y. App. Div. 1983).

20. American Totalisator Co. v. Western Regional Off-Track Betting Corp., 396 N.Y.S.2d 301 (N.Y. App. Div. 1974). *See also* Autotote Ltd. v. New Jersey Sports and Exposition Auth., 427 A.2d 55 (N.J. 1981) (holding that service exception applied to contract for computer system for racetrack involving complex computer network designed to tabulate and categorize bets and to calculate payoffs for each race, including staff of technicians, operators, and on-call engineers).

21. Doyle Alarm Co. v. Reville, 410 N.Y.S.2d 466 (N.Y. App. Div. 1978).

22. *American Totalisator*, 396 N.Y.S.2d at 302.

23. *Pacificorp*, 741 F. Supp. at 485.

24. *See* Neilson Business Equip. Center v. Monteleone, 524 A.2d 1172, 1174 (Del. 1987) (holding that turnkey purchase of computer system in which hardware and software were combined before sale and then installed was predominantly sale of goods, and UCC applied).

25. G.S. 160A-19.

26. *See* Microsoft Corp. v. Harmony Computers & Elec., 846 F. Supp. 208, 212 (E.D.N.Y. 1994).

27. *See* ProCD, Inc. v. Zeidenberg, 86 F.3d 1447, 1450 (7th Cir. 1996) (enforcing terms of shrink-wrap license under UCC).

28. *See* Applied Info. Management v. Icart, 976 F. Supp. 149, 154 (E.D.N.Y. 1997) [citing Raymond Nimmer, *The Law of Computer Technology* (Boston: Warren, Gorham, and Lamont, 1992), sec. 1.18(1), p. 1-103].

29. *Applied Info. Management*, 976 F. Supp. at 154. Determining whether the buyer owns a copy is significant for application of the "first sale" doctrine of copyright law and for determination of the uses the buyer can make of the product without infringing on the intellectual property rights of the seller or the licenser. *See* 17 U.S.C. §§ 117, 109 (1996 & Supp. 1998).

30. Henry Beck, "Uniform Commercial Code Article 2B—Licenses," National Conference of Commissioners on Uniform State Laws, Jan. 20, 1997 Draft, pp. 54–55, in Practicing Law Institute, *Patents, Copyrights, Trademarks, and Literary Property*, 478 PLI/Pat 103.

31. *Mullen*, 225 N.C. at 58–59, 33 S.E.2d at 487.

32. For a sample notice and answers to commonly asked questions about the piggybacking exception, *see* Frayda S. Bluestein, "Interpretations of the 'Piggybacking' Exception to North Carolina's Formal Bidding Requirements," *Local Government Law Bulletin*, no. 85 (June 1998); available on the Internet at http://ncinfo.log.unc.edu/purchase/piggy.htm.

33. The statute does allow the contractor to provide the product at a more favorable price or on more favorable terms.

34. G.S. 143-129(c), (a).

35. G.S. 143-129(b). For a more detailed discussion of the formal-bidding requirements, *see* Bluestein, *A Legal Guide*.

36. The three-bid requirement in state law (G.S. 143-132) applies only to construction or repair contracts. Some local governments may have policies requiring three bids for purchase contracts.

37. G.S. 143-131.

38. Public officials have observed that applying the sole-source exception to an informal bid may be more cumbersome than seeking bids because the exception requires approval by the governing board, which is not otherwise necessary for contracts in the informal range. For informal contracts it may be sufficient to seek competition and, if none is available, simply to document the efforts and explain the lack of competition, rather than proceed under the sole-source exception.

39. Sperry Corp. v. Patterson, 73 N.C. App. 123, 124, 135 S.E.2d 642, 644 (1985).

40. For a case discussing the legal standard for evaluating "responsiveness," *see* Professional Food Serv. Management v. North Carolina Dep't of Admin., 109 N.C. App. 265, 426 S.E.2d 447 (1993).

41. Datatrol, Inc. v. State Purchase Agent et al., 400 N.E.2d 1218 (Mass. 1980).

42. Burroughs Corp. v. Division of Purchase and Property, 446 A.2d 533 (N.J. Super. 1981); Municipal Leasing Corp. v. Fulton County, Georgia, 835 F.2d 786, *aff'd*, 849 F.2d 516 (11th Cir. 1988).

43. *Municipal Leasing Corp.*, 835 F.2d at 789–90.

44. Kinsey Contracting Co. v. City of Fayetteville, 106 N.C. App. 383, 416 S.E.2d 607, *pet. for disc. review denied*, 332 N.C. 345, 421 S.E.2d 149 (1992).

45. *See generally* Margaret E. McConnell, "The Process of Procuring Information Technology," *Public Contracting Law Journal* 25 (1996): 379.

46. Legislative Research Commission, Information Technology Committee, *Interim Report to the 1998 Session of the 1997 General Assembly* [hereinafter *IT Report*], Raleigh, N.C., May 11, 1998, p. 14.

47. *IT Report*, app. D, p. D-1.

48. *IT Report*, app. D, p. D-1.

49. *IT Report*, p. 14.

50. *IT Report*, pp. 14–15.

51. *See* McConnell, "Procuring Information Technology," 385–89.

52. *See* Charter of the City of Charlotte, subch. E, § 9.85 (1993 N.C. Sess. Laws ch. 196).

53. TENN. CODE ANN. § 12-3-203(a) (1992).

54. Model Procurement Code for State and Local Governments [hereinafter MPC] § 3-203 (Am. Bar Ass'n 1979).

55. MPC, Commentary to § 3-203, at p. 22.