

Procurement Resource Abstract



Title	Transforming Procurement for the 21st Century
Sponsoring Organization(s)	TechAmerica
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Synopsis	<p>This paper presents a consolidated view from the Information Technology (IT) industry regarding state and local government (SLG) contract terms and conditions and the contract formation process for complex IT projects. It discusses industry concerns about generic contract terms that are not well-suited to implement complex IT projects and how they are driving costs up and competition and innovation out of the SLG market. The procurement discussion is based on several demographic and financial challenges facing the public sector environment that create difficulties for SLGs to procure and deploy IT solutions including:</p> <ul style="list-style-type: none">• Increasing number of federal and state mandates with complex regulations and compliance requirements• Demographic trends in the population indicate rising demand for services and benefits• Tighter budgets, economic contraction, and competition for federal (and state) dollars suggests the rate of funding available will not grow at a rate proportional to the demand• Increasing client (beneficiaries) and citizen service expectations as a function of "commercial" experience with web-driven applications <p>The paper explains that complex IT projects truly require partnerships between the SLG customer and the contractor and how this partnership must be reflected in the contractual agreement rather than constructed from a standard contract template. This approach not only reduces associated project risks but also increases competition during all phases of the procurement process. Project risks are discussed in the context of partnership and how they should be shared between industry and SLG customers. In addition, contract terms such as intellectual rights, warranties, indemnification, liquidation damages and performance bonds are discussed as to how they can increase project risks and costs.</p> <p>There is also a discussion on how the bid requirements and RFP's contract terms are critical to pricing and cannot be independent from the cost and competitive assessment by explaining industry pricing models and cost structures and their relationship to contract terms and conditions – e.g., a company cannot produce an accurate a la carte price for a broader indemnity clause. A contract term such as this could force companies into a "no bid" situation or attach extraordinary pricing premiums thus driving the competition down and cost up for the SLG customers.</p> <p>Finally, recommendations are presented for SLGs to increase transparency to their procurement processes and discuss contract problems with industry to improve contract agreements and help determine mutual solutions. They urge SLGs to share</p>

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	their experiences and use lessons learned, as well as to consider Federal government terms and commonly-accepted commercial provisions for their IT procurements. This will improve the SLG competitive process by modernizing their procurement philosophies with thoughtful terms and conditions that protect the public interest while managing balanced, commercially-acceptable business risk with industry partners.
Topic Areas	Legal and Contracting Issues
Web Reference	[see below]

TRANSFORMING PROCUREMENT FOR THE 21ST CENTURY:

**Part I: Reforming IT Contract Terms and Conditions
to Improve Procurement Environments and
Outcomes**

presented by:

TechAmerica



March 2009

Executive Summary:

The purpose of this paper is to present input from the Information Technology (IT) industry regarding contract terms and conditions and the contract formation process for complex IT projects in the state and local government (SLG) marketplace.

In short, as discussed in this document, IT contractors have become increasingly concerned that overly prescriptive generic contract terms that are not well-suited to complex IT projects are driving competition and innovative solutions out of the SLG market and are unnecessarily driving costs up. This is neither in the best interest of governmental entities nor IT contractors.

At the outset, we would like to share some general concepts regarding the IT industry's perspective, interests and constraints regarding contract terms as these concepts provide the backdrop and inform the more specific concerns detailed in this paper.

- Complex IT projects truly require partnership between the SLG customer and the contractor and the contractual agreement should reflect that. IT system projects involve substantially more customer-contractor interaction than delivering commodity products, constructing a building or even producing a complicated manufactured device. Modern IT system projects involve melding existing technologies to existing organizations. The rules that govern their operations often require some flexibility on the part of both the technology and organization involved. To successfully complete a project, numerous inputs are required from the implementing agency. Often the end user wants a great deal of involvement in the system implementation so that the purchaser will be able to maintain the system at the end of the project implementation. Contracts that do not reflect this reality – that purport to impose all performance obligations on the contractor or not provide the contractor with adequate compensation where the end user does not timely meet its obligations – result in decisions to not bid or increased price premiums. By making contract terms match the nature of this unique type of project instead of using generic commodity or construction terms for IT projects, state and local government entities will find that they will enjoy increased competition and therefore be able to reduce costs.
- Contract terms are a critical but non-segregable input to pricing. Companies' pricing models and costing structures are based on contract terms that align with a general set of parameters. These parameters reflect input from outside auditors and insurers; consequently, they are set at the corporate level and cannot be adjusted by account or practice teams responsible for individual proposals. With very limited exceptions, contract provisions that do align with a company's contract parameters cannot be individually priced for a proposal – e.g., a company cannot produce an accurate a la carte price for a broader indemnity clause. As a result, when forced to accept non-standard contract terms, companies are forced into a "no bid" situation or attach extraordinary pricing premiums to account for potential impacts from insurers, auditors

- or other parties that conduct post-execution contract reviews that can enormously impact the company and its finances. This drives competition down and cost up for SLG customers; unfortunately, as discussed in this paper, these additional terms provide little or no benefit to the government entity in exchange for such costs.
- IT contracts need to apportion the risk of performance, not the risk of the venture. Simply by undertaking a complex IT project, an entity is incurring risk. Will the needed functionality be achieved? Will the organization adopt the new technology? Are there other unforeseen impacts that will occur? Experienced IT contractors using established technologies and methodologies help reduce those risks by bringing their expertise and seasoned skills to the table. However, while they can reduce the risk, they cannot eliminate it. Too often, contract terms required by SLG customers go beyond merely contracting out performance of a project to attempting to outsource the entire risk of the initiative. This is reflected in non-standard liability clauses, indemnity provisions and extraordinary warranties that are not commonly seen in commercial contracts. IT companies doing system implementation work understand that they have very serious obligations to their customers and that their customer's core functions are resting in their hands; however, responsible companies cannot bet their future existence on one project. While IT companies are certainly willing to accept the risk of their performance and reasonably compensate the customer where they fail to deliver, they cannot accept the entire risk of the project's success.

We understand that often papers such as this can be perceived as a "bill of complaint" or some airing of grievances. To be clear, that is not our intent at all for this document.

This document is the first in a series of papers on the subject of reforming procurement processes in public sector organizations. This paper, presented by TechAmerica's State and Local Government Board and our SLG Procurement Committee, is intended to be a constructive assessment of the critical challenges within the sphere of government procurement. As the title hints, this document focuses first and foremost on the IT contracts terms and conditions, or the "Ts and Cs;" the contract clauses that establish the legal underpinnings of any transaction between two entities. By offering an industry perspective, it is our hope that we will help our member companies and their government customers find the common ground necessary to establish more vibrant, competitive, and fair public procurements, which will support the needs of government customers and their stakeholder constituencies.

Our hope is that this paper will serve as an entry point to a dialogue between representatives from both the industry and government sides with the objective of reaching a common understanding regarding contracting principles and processes that will enhance the IT solutions available in the SLG market by reducing barriers to entry and non-value-added costs while at the same time providing strong protection to SLG purchasers and the taxpayers whose needs they represent. Based on past experience where such efforts were undertaken, we are confident that such dialogue when conducted with open minds and committed representatives on both sides can produce outcomes that tremendously benefit everyone.

State and Local Governments Face a Growing Need for IT Solutions

IT solutions and services are increasingly important to state and local government entities delivery of services to constituents. According to market analysts at INPUT, state and local government IT spending is expected to grow to \$72 billion by FY 2011, a level which eclipses even the federal government as a buyer of IT goods and services.

To add to the increasing volume of work, the scale and complexity of IT projects are compounding. Many states, as well as large counties and cities, now seek to change the way government delivers services and to transform government's interactions with constituents. State & local governments are also likely to use IT to obtain cost-savings and other efficiencies through moves to centralized IT resources, consolidated IT operations, and outsourced non-essential government functions. Increasingly, state and agency resources may not be available or sufficient for some of the business, programmatic, and technology challenges facing the public sector. Hence, state and local governments are reliant on the "best in class" solutions offered by the private sector. From replacing outmoded legacy systems to implementing "Web 2.0" technologies, states are in need of the entire array of professional services, data storage, IT infrastructure, and network services available via IT and telecommunications solutions and service providers.

There are several ongoing and emerging demographic and financial challenges in the public sector environment, which magnify the difficulties posed by deploying IT solutions for SLGs. Those include:

- Increasing number of federal and state mandates with complex requirements
- Demographic trends in the composition and needs of the population indicate rising demand for services and benefits
- Tighter budgets, caused by shrinking revenues related to a potentially prolonged period of economic contraction, and competition for federal (and state) dollars suggests the rate of funding available will not grow at a rate proportional to the demand
- Client (beneficiaries) and citizen service expectations are increasing, e.g., as a function of "commercial" experience with web-driven applications

The rising demand for IT solutions, complicated by factors such as those outlined above, has made the acquisition and deployment of timely, value-adding IT solutions and services of paramount importance to governments at all levels. Given the importance of IT in supporting government missions of all kinds, the acquisition practices and processes that allow for the purchase of IT have been subject to heightened levels of oversight and policymaking since the early-1990s, when IT emerged as a major capital investment and operating expense for SLGs.

Many observers and practitioners have become convinced that SLG IT procurement processes and practices that have taken root over the past two decades are dysfunctional and do not function as intended. In many cases, procurement processes and contract clauses deter competition for state agency business or drive up the cost of the proposed solution and/or

service to the agency and, ultimately, the taxpayer. Such instances offer evidence that IT procurement is ripe for reform and transformation.

The Case for Transformation Enabled By Information Technology

To meet the many and at times differing needs of constituents, thoughtful state and local government leaders must look to transform government through novel policy ideas and to provide the leading-edge IT services that demonstrate the value of government in the 21st century. If, however, the process of implementing the vision is outdated, antiquated or fraught with friction, then transformation will be lost, the vision muddled and the constituents ultimately ill-served. By contrast, nimble, creative and innovative procurement processes can help crystallize and focus transformative efforts in a way that enhances the chances for success.

As manual work processes have given way to information technology products and services, governments have been confronted with radically different contractual considerations. In the federal public sector marketplace, and to a lesser extent in the state and local government marketplace, acquisition reform initiatives have occurred to implement best practices of the commercial marketplace and which seek to capture the flexibility of the private marketplace to implement innovation. Today in 2009, it is obvious that these reforms must continue, and accelerate, if government is to meet the needs of the citizens.

To succeed, transformation requires a strong support network of not just committed and talented leaders but also processes and infrastructure to realize the vision. In an era where governments operate with fewer employees and constrained budgets, the achievement of transformation will very often require the participation of private industry and a commitment from industry to support key initiatives in a creative and cost-efficient fashion.

For the past decade - and perhaps longer - the drivers of state and local government procurement have created greater imbalances in the partnerships between the public and private sector and raised barriers to creative and nimble system development and implementations. In all too many SLGs, procurements have become standardized, less transparent, lacking in free and open communication and negotiation, and made tense by lack of trust between the parties. These attributes are symptomatic of increasingly prescriptive and risk-averse procurement policies. While well-intended, such policies have produced consequences which make IT innovation more challenging to state purchasers and IT vendors alike. While the degrees differ in every state and locality, there is no agency or vendor which has operated free from the impact of these trends. Results are unintended and undesirable: More "no bid" or "high bid" procurements, too much focus on low-cost bids, slow and contentious procurements, and ultimately, public buyers and users denied the latest commercial technologies and skills.

The Trouble with Terms and Conditions

TechAmerica and its member companies have, for several years, focused on one multi-dimensional piece of the procurement puzzle: IT contract terms and conditions. For those working to provide IT solutions and services to government customers, there is no procurement practice which offers more challenge, frustration, and wasted resources – with little to no connection to business value or financial reward – than the contract articles stipulating degrees of liability, levels of indemnification, the rights reserved by the parties, and all other manners of legal minutiae.

It is TechAmerica's view that inflexible IT terms and conditions developed without industry participation and support can negatively impact all parties to a procurement. For example, such terms:

- Depart from commercial realities by imposing risks and costs on vendors that are disproportionate to any potential gain, and are often outside the risk-management parameters of the vendor. A responsible vendor with significant assets may simply be unable to accept certain terms and at the same time satisfy its statutory and regulatory obligations to manage risk and deliver profitable growth to its shareholders. This can lead to situations where the only vendors participating in key local procurements are those with inadequate expertise or insufficient assets to perform. Or, more accomplished vendors will respond to unbounded risk with higher prices.
- A procuring agency's insistence on adherence to inflexible terms often discourages otherwise competitive vendors from participating in procurements, thus depriving the public of the benefit of full competition. The process of completing public procurements also is complicated when the public agency starts with "out of market" terms and a lengthy period follows where established private firms seek to bring the terms into alignment with what is acceptable in the industry. Such delays serve no one's interests.
- Even when competition does proceed, it is a practical reality that commercially unreasonable terms and conditions require vendors to take measures to minimize potential risk to a company's viability. In deciding whether to pursue a major procurement opportunity, vendors are often faced with making a "bet the business" decision or responding to the government's RFP only after devising or purchasing very robust, costly protection against excessive risk exposure. Another outcome can be that more established firms elect to become lower tier subcontractors so that their exposure is reduced.

A relationship where one party to the transaction bears all the risk is not one where, in our experience, the end result is satisfactory to either party. Nor is it a relationship that either party is likely to repeat when, as in the vendor's case, companies have fiduciary duties to their shareholders and others.

TechAmerica and its member companies support efforts to avoid these adverse results and to achieve procurement transformation and procurement policy reforms. The following section provides a brief overview of the benefits public purchasers could reap via a shift to more commercially-acceptable terms and conditions.

Benefits of Commercial Terms and Conditions

There are alternatives to onerous terms and conditions that in the end do little to protect either party. While TechAmerica recognizes that there are special needs and interests of the public purchaser that require recognition, TechAmerica advocates for the use of common, commercially- acceptable terms and conditions, whenever appropriate. Our analysis indicates that the following benefits are among those most often cited.

Decreasing cost to drive best value for the customer. To the extent that vendors accept excessively onerous and risky terms and conditions, the risks are reflected in the bid price, preventing the government customer from getting the best value for its procurement dollar.

Potentially attracting more, and better qualified, vendors to bid on projects. In some recent cases, well known vendors have reached “no-bid” decisions when considering government opportunities, not from an inability to provide the functionality desired but instead because of adverse reaction to the standard terms and conditions. By reducing or sharing risk in a balanced fashion, more vendors will pursue business in a given state or municipality. Moreover, qualified, local small and disadvantaged businesses may be more willing to pursue public sector work if they can secure balanced terms and conditions. Increasing the number of vendors will also yield better prices and more competitive choices for government departments and agencies. Where competition is more vigorous, public procurements will truly produce the best solution and value.

Expediting the procurement process. Too often, negotiations are needlessly slow, beset by changing deadlines and impasses. Terms that better conform to commercial realities will lower the need on the part of the vendor community to insist on waivers, deviations, or specially negotiated terms. By implementing an accelerated negotiation schedule that provides a specific date for negotiations to be completed by, the government client and its vendor community can proceed with delivering services to its constituents in a more timely fashion.

Aligning the government with best practices in procurement. By reforming terms and conditions, the government entity will position itself to achieve other improvements in its IT processes and practices and attain true “win-win” contracts between the government and its vendor partners. While good contract language is one way to limit the risk of project failure, sophisticated agency customers should look to continue best practices in contract scoping, developing customer specifications and requirements, and executing well on project management and administration to ensure project success.



Improving the customer-vendor relationship. An improved culture of trust and open communication between the customer and the vendor will also help create a successful outcome for state and local procurements. A public sector entity that assumes a less adversarial stance in contracting and negotiations, a stance which focuses on sharing risk and reward, and adopts a focus on partnership will benefit from a more open selection process, improved communication of ideas, and a shared interest in the success of the project. This can be achieved without sacrificing the important qualities of fairness, transparency and equity in the procurement process.

Procurement Provisions of Greatest Concern

TechAmerica would welcome the opportunity to discuss certain key terms and conditions with public sector officials and groups representing those officials. If reformed, some of the key contract terms and conditions, we believe, would greatly enhance the SLG procurement environment, and improve the likelihood of intended, optimal outcomes for the government IT customer.

1. Risk Balancing Provisions

Prudently managed companies must focus on effectively assessing and controlling economic risks by securing appropriate terms and conditions in their contracts. Limitation of liability provisions form a key mechanism for striking the appropriate balancing of financial risk between vendors and government customers. These provisions also support the broader public policy goal of corporate responsibility which is intended to protect the investments of not only thousands of individuals but also large institutional investors such as pension funds for government employees. It is well known that Sarbanes-Oxley implemented the intent of Congress that companies, particularly those that are publicly traded, must disclose to their shareholders, among other things, how risks assumed by the company may materially impact financial results and, ultimately, the value of their stock. The requirements of compliance with Sarbanes-Oxley rules reinforced this message by requiring senior corporate management to not only certify the company's financial results but also to establish a system of internal business controls designed to prevent fraud, foster reporting of accurate results and to evaluate and mitigate risk. For companies that work with governments, such controls usually involve a contemporaneous evaluation of contracts that are often material, complex, risky, long term, ever-changing, and at times adversarial.

As a result, it has become increasingly important to industry that contracts establish limits on a company's liability. Unlimited liability is simply untenable for nearly all vendors today. This topic was studied at length in 2005-2006 by the National Association of State Chief Information Officers' (NASCIO) Procurement Reform Committee – which is comprised CIO's, procurement professionals and lawyers as well as industry representatives. The resulting report is available

online¹ and contains the following statement with regard to liability clauses in public sector IT contracts:

“As a general principle, the Procurement Subcommittee recommends that both states and vendors work to determine the true risks that are associated with state IT procurement contracts and then allow the states to protect themselves against those true risks, as opposed to drafting IT contracts with unlimited liability for IT vendors. This approach is intended to improve competition for state IT contracts and is expected to result in higher quality vendor products and services at a lower cost to the states.”

In 2008, the State of Iowa undertook a study of contracting problems stemming from lack of limitation of liability in state contracts. The study widely canvassed both the vendor community and some legal experts. Highlights on the issue of limitation of liability included:

“There is no question that Iowa’s unlimited liability requirements are causing large IT vendors to decline to participate in Iowa’s state government contracting opportunities.”

“A significant consideration for vendors is the “one-sided” process and terms and conditions of the contracts in Iowa. Seemingly, all the cards are in the state’s hand, and the lack of limitation on liability is ultimately the card that drives the vendors away from the state.”

While limitation of liability may be the proverbial “straw that breaks the camel’s back,” there are other risk-balancing provisions that may cause “no-bid” decisions. Typically, problems lie in the layering of risk mitigation measures. Contracts may include language on a customer’s acceptance of the vendor’s work as a trigger for payment, requirements of high amounts of insurance with the state listed as an additional insured, performance bonds that require large cash reserves often accessible only to the largest companies, and other terms that essentially provide redundant and duplicative risk mitigation.

Performance Bonds

Performance bonds have proven particularly problematic for IT contractors. Generally speaking, the purpose of performance bonds is to pay for customer expenses related to the procurement in the event that the original vendor fails to perform. In other words, a performance bond is meant to guarantee that the project will proceed despite a defaulting vendor, not to make the government purchaser whole for all damages suffered in connection with a default.

In recent years, due to factors external to the IT industry such as the Enron scandal and the spate of bankruptcies in the telecommunications industry, the surety market has significantly

¹ https://www.nascio.org/nascioCommittees/procurement/road_to_win-win.pdf

reduced the amount and types of performance bonds available to companies. High bond amounts and bonds exceeding twelve months are especially difficult to secure. Additionally, many bond companies are now requiring that companies partially or fully collateralize performance bonds with bank Letters of Credit, substantially increasing the overall bonding cost. This means that SLGs and other buyers of services requiring high performance bond requirements will significantly limit competition because:

- Smaller companies will not have the ability to qualify for high dollar performance bonds
- All companies now have limited bonding ability, which means they must prioritize opportunities in order to conserve their ability to obtain bonds for existing and future opportunities
- Where a bond will need to be collateralized, corporate management must also evaluate the impact of reduced liquidity resulting from the collateralization in determining whether to even submit a bid for a particular IT procurement..

Even more important, the cost of obtaining any bond has risen dramatically. For example, the cost of a performance bond today can be 40 times higher than the cost of an existing bond obtained prior to the scandal period of 2002 – 2003. Companies have no choice but to pass on this additional cost (as well as any cost associated with collateralization, which can be very substantial) on to the customer (i.e., the SLG) through increased prices.

2. Intellectual property (IP) rights and related indemnity clauses.

Intellectual property rights constitute another area of concern to, in particular, information technology vendors and software suppliers. Innovation forms the lifeblood of the IT industry and has driven its astonishing growth in the US economy. To harvest the benefits of private initiative and protect shareholder value for investors, it is essential that IT firms be permitted to protect their intellectual property and be able to leverage what they learn in public and private sector work to promote future engagements. Some public sector purchasers seek too much, and threaten the economic viability of their would-be technology partners, by insisting that rights of ownership in IP are conveyed to the public purchaser if used on a public contract.

This is not a necessary approach; nor is it in the public interest. It is not necessary because the first interest of the public purchaser is the efficient and cost-effective delivery of supplies and services; this does not require acquiring ownership of private intellectual property used in such performance. Further, public agencies will not benefit from becoming potential competitors of their IT suppliers through acquisition of ownership or greater than necessary rights in the IP of their suppliers. Those suppliers will restrict what they develop and deliver and the public agency will be exposed to liabilities that are beyond its core competence and not an exposure that is prudent for a public body to accept. Moreover, in many instances, public sector customers benefit from a vendor's ability to employ and adapt intellectual property, developed in one public sector engagement for other projects.

TechAmerica advocates that SLGs carefully assess their intellectual property requirements so as to secure for them the essential rights needed to achieve project goals. In the same way, SLG

should avoid taking ownership or requiring sweeping rights such that vendors will be discouraged from using their most innovative talent, existing intellectual property. TechAmerica's view is that governments should work from a premise of acquiring no greater ownership and no more rights in IP than what is required to achieve the necessary public purpose.

3. Other Indemnification Clauses

Industry is generally prepared to provide customers with appropriately tailored indemnification provisions. For example, indemnities for bodily injury, including death, and damage to tangible real and personal property are not unusual. It is typical that these indemnities are limited to third party claims and apply to damages for which the contractor is legally liable. However, many SLGs offer terms and conditions that seek to have contractors agree to a very broad indemnity that rises to the level of strict liability. This broad indemnity is of great concern to industry because it in effect would negate any limit of liability for breach type claims that should be contained by appropriate direct damages caps and disclaimers of consequential damages.

4. Most Favored Public Entity

The Most Favored Public Entity provision seeks to require vendors to offer to the public sector customer the lowest price they may have agreed to provide to another government customer for the same product types or services. While industry appreciates the appeal of attempting to guarantee an ostensibly low price, this contractual provision is not advisable in our view for several reasons. First, we believe that public sector entities can effectively manage the procurement process to drive very competitive pricing. In our experience, the competition between vendors is often fierce and the pressure on pricing is intense. Firms are highly incented to offer the lowest possible price that meets the requirements of a specific bid – not just to offer the same price they may have agreed to on another contract. Second, while competitive pricing is extremely important, in best value procurements, the lowest price is not necessarily the winning bid. A thorough review of the vendor's value, solution, past experience and price may result in the conclusion that the price proposed – even if not the lowest in all contexts – may nevertheless be the true best value. Third, most favored entity clauses are functionally impossible to administrate especially when the vendor is a large, multi-national corporation. For example, large companies cannot effectively monitor and track literally thousands of contracts to determine which customer was offered a purported lower price than a customer that may have a contract with a most favored entity clause. Moreover, it is very difficult to decide which contracts would drive a lower price; that is, it will be extremely rare that the vendor has made the *exact* same offer to another government. Rather, there will be significant differences regarding the mix of services and products; local labor cost differences, and the terms and conditions; all of which affect pricing. As a result, governments are much more likely to gain competitive and credible pricing through a vigorously managed procurement process than they are through most favored entity terms in their contracts.

5. Warranty

A warranty is a promise or agreement by a seller of goods or services that an article or service has certain qualities. As you would expect, the seller of an ordinary commodity is willing to provide very different promises than a provider of computer software or hardware or a provider of IT services. Commercial concerns are typically prepared to provide appropriate warranties as a mechanism to protect a public sector entity from a defective service or product. However, the nature and appropriateness of these warranties will vary greatly -- depending upon whether the transaction involves the sale of (i) the generally available hardware or software of the company, (ii) services of the company or (iii) the resale by the company of a third party's hardware or software.

TechAmerica advocates that government purchasers carefully assess their warranty requirements based upon the needs of the particular procurement. Requesting warranties beyond the essential needs to achieve the project goals will impose undue risks and burdens on vendors, resulting in unnecessary price increases. We believe that the warranty and remedy provisions described above provide more than sufficient assurances that the customer will receive the benefit of their bargain.

6. Liquidated Damages

Liquidated damages are a well-established tool for enforcing satisfactory vendor performance under IT services contracts. Liquidated damage clauses allow contracting parties to specify by their mutual agreement the monetary damages that would result from a given contractual breach or performance failure, in cases where actual damages would be difficult to prove or quantify. Provisions for the assessment of billing credits in the event of a vendor's failure to maintain required service levels are typically enforced as liquidated damages.

TechAmerica recognizes that properly constructed liquidated damages clauses can be a legitimate tool for encouraging quality performance by the vendor. However we are concerned about rigid and inflexible clauses that attempt to set damage amounts unilaterally (notwithstanding the legal requirement that these amounts be determined by agreement), or where the damage amounts themselves are punitive or bear little or no proportion to the severity of the corresponding failure. Clauses that allow for multiple damage assessments to be triggered by the same event, or that do not provide an overall 'cap' on total assessments are also likely to fall outside of the vendor's acceptable risk profile.

Recommendations

Our recommendations reflect both process and substance. As a matter of process, we urge SLGs and other public sector organizations to take steps that will inform them of the problems vendors perceive with present agreements and help them assess the way in which other governments handle representative IT procurements and contract terms and conditions.

We also urge states and localities to review and consider the lessons learned from the experience of other governments. Federal terms and commonly-accepted commercial provisions should be considered, which will show the range of options and help point toward changes that may find a better balance between competing interests. As the process evolves, a key substantive event would be the adoption of a new, set of model IT contract terms and conditions. Initially, it could serve the interests of all concerned to conduct one or several procurements in which the new terms are employed and then evaluated for their effectiveness.

Over the past several years, many other governments have announced ambitious plans to improve the quality and responsiveness of many governmental services. To do so affordably with the best technology, goods and IT services that can be obtained through the competitive process, governments also need to consider modernizing their procurement philosophies by reviewing terms and conditions and developing new standards that, while respecting the public trust, nonetheless present commercially-acceptable business risk to potential public sector vendors.

About TechAmerica

TechAmerica is the leading voice for the U.S. technology industry, which is the driving force behind productivity growth and jobs creation in the United States and the foundation of the global innovation economy. Representing approximately 1,500 member companies of all sizes from the public and commercial sectors of the economy, it is the industry's largest advocacy organization and is dedicated to helping members' top and bottom lines. It is also the technology industry's only grassroots-to-global advocacy network, with offices in state capitals around the United States, Washington, D.C., Europe (Brussels) and Asia (Beijing). TechAmerica was formed by the merger of AeA (formerly the American Electronics Association), the Cyber Security Industry Alliance (CSIA), the Information Technology Association of America (ITAA) and the Government Electronics & Information Association (GEIA). Learn more at www.techamerica.org, www.aeanet.org or www.ita.org.

About TechAmerica's Public Sector Group

TechAmerica's Public Sector Group serves the wide-ranging needs of the software and systems integration industry through advocacy, member events, networking and business development, and works to provide an active voice for the information technology community.