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April 24, 2003

BY ELECTRONIC FILING

Marlene H. Dortch
Office of the Secretary
Federal Communications Commission
445 12th Street, S.W. Suite TW-A325
Washington, D.C. 20554

Re: In the Matter of Request for Review of the Decision of the Universal Service Administrator by International Business Machines Corporation, CC Docket Nos. 96-45, 97-21

Dear Ms. Dortch:

Please find attached a White Paper, *Review of Federal, State of Texas, and FCC E-Rate Procurement Laws and Regulations*, which we respectfully submit in support of International Business Machines Corporation's Request for Review, filed January 30, 2003 in the above-captioned proceeding.

Sincerely,

/s/

R. Michael Senkowski
Counsel for International Business Machines Corporation

Attachment

CC: William Maher
Carol Mattey
Mark Seifert
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Narda Jones

REVIEW OF FEDERAL, STATE OF TEXAS, AND FCC E-RATE PROCUREMENT LAWS AND REGULATIONS

April 2003

Prepared by

Wiley Rein & Fielding LLP

for IBM Corp.

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I.
INTRODUCTION

Wiley Rein & Fielding LLP ("WRF"), on behalf of International Business Machines Corporation ("IBM"), respectfully submits this White Paper in support of IBM's January 30, 2003 Request for Review of the Decision of the Universal Service Administrative Company (the "IBM Request for Review"). The IBM Request for Review challenges the Universal Service Administrative Company's Schools & Libraries Division's ("SLD's) denial of five funding requests submitted by the Ysleta Independent School District ("Ysleta") for Information Technology ("IT") resources and services to be provided by IBM under a systems integration contract with Ysleta.

WRF has been retained by IBM as special counsel to provide an analysis of procurement laws and regulations under Federal, State of Texas, and Federal Communications Commission ("FCC") authority. In particular, our task has been to determine what a Texas school district legally must do in selecting a service vendor if it seeks funding from the Schools and Libraries Universal Service Support Mechanism ("E-Rate"). In addition, we have provided an overview of Federal law applicable to similar procurements.

This report was prepared by the WRF Government Contracts and Communications practice areas. Rand Allen, partner and Co-Chair of the WRF Government Contracts practice and former Chair of the American Bar Association Section of Public Contract Law, has assessed the compliance of the procurement process used by Ysleta with Texas procurement law and, more generally, with Federal procurement law. In analyzing Texas law, Mr. Allen consulted with J. Timothy Brightman, an attorney with Abernathy, Roeder, Boyd & Joplin, PC, a law firm with broad experience in government, municipal, and school law in the State of Texas.

Jeffrey Linder, partner in the WRF Communications practice, has particular expertise concerning the FCC's order in *Request for Review by the Department of Education of the State of Tennessee of the Decision of the Universal Service Administrator*, Order, 14 FCC Rcd 13734 (1999) [hereinafter "Tennessee Order"]. In that case, Mr. Linder represented the appellant, Education Networks of America ("ENA"), in its successful appeal to the FCC of the Universal Service Administrator's denial of E-Rate funding for an Internet access project. Mr. Linder has assessed the impact of that case on IBM's Request for Review in the Ysleta procurement.

Accordingly, this White Paper first summarizes WRF's understanding of the procurement process by which Ysleta selected IBM as its Systems Integrator. It next examines whether that process complied with the requirements and policies of Texas procurement law. We then provide an overview of the current Federal laws and principles applicable to similar procurements. Finally, this White Paper provides our analysis based on WRF's direct experience in the Commission's *Tennessee* case.

II.
SUMMARY CONCLUSIONS

In its Universal Services Order, the FCC explained that state and local procurement officials enjoy "maximum flexibility to take service quality into account and to choose the offering . . . that meets their needs 'most effectively and efficiently.'" *Federal-State Joint Board on Universal Service*, Order, 12 FCC Rcd 8776, 9029-30 para. 481 (1997) [hereinafter "Universal Service Order"]. The Commission explicitly identified Federal "best value" procurements as an example of cost-effective purchasing and acquisition that was consistent with its E-Rate funding rules. *Id*. In so doing, the Commission deferred to the methods adopted by Federal and state legislatures to meet the challenge of allocating scarce taxpayer resources to acquire needed products and services.

Texas Procurement law mirrors the principle of best value that forms the core of Federal procurement law. Texas law instructs school districts to select from a menu of procurement methods, each of which has been deemed by the Texas legislature to be capable of providing "the best value to the school district." TEX. EDUC. CODE § 44.031(a). These procedures are tried and tested means to achieve the Commission's stated objective for the E-Rate program, cost-effectiveness, and are grounded in fundamental principles of modern procurement law, including (a) the American Bar Association ("ABA") Model Procurement Code for State and Local Governments, which has been adopted by 17 states, and (b) the Federal procurement regime identified by the Commission in its Universal Services Order. Indeed, these are the very procedures that the Commission itself must follow when awarding public contracts.

WRF concludes that the competitive procedures that Ysleta used to select IBM as its Systems Integrator fully comport with Texas procurement law. Ysleta utilized a best value

procurement process modeled on the two-phased processes prescribed for engineering and professional services by the State of Texas, the ABA Model Procurement Code, and the Federal Government. The best value regime employed by Ysleta, Texas, the Federal Government, and many other states recognizes that price must be considered along with qualitative differences in the goods and services offered for acquisition, and that purchasing officials must ultimately determine whether any qualitative advantages are worth any additional cost. Indeed, the best value concept is the result of decades-old procurement reforms that replaced an obsolete requirement that, unless an exception existed, Federal contract awards had to be based on low-cost.

The structure and objective of Ysleta's procurement process is also consistent with FCC policies articulated in its rules and decisions, particularly the Tennessee Order. WRF has identified four reasons why, consistent with the Tennessee Order, the Commission should defer to the process employed by Ysleta: (1) Ysleta followed state procurement laws that apply to all purchases of goods and services by Texas state agencies and school districts (and thus are intended to assure cost-effective procurement of billions of dollars in goods and services annually); (2) Ysleta had every opportunity and incentive to choose the most cost-effective proposal; (3) Ysleta is a sophisticated purchaser whose actions in this procurement reflect a proficiency in the application of modern acquisition methods for complex technical services; and (4) notwithstanding the clear right to do so, no competitor objected to Ysleta's procurement practices either before or after submitting a response to Ysleta's solicitation.

III.
BACKGROUND

In preparing this White Paper, WRF has reviewed the "Factual Background" sections of Ysleta's January 28, 2003 Request for Review and IBM's January 30, 2003 Request for Review. WRF has also carefully reviewed the attachments to those filings, which comprise the documentary record of the subject procurement. This section briefly highlights the pertinent facts bearing on Ysleta's compliance with Texas procurement law and general principles of Federal procurement law.

A. Technology Plan

Over the last decade, Ysleta developed a comprehensive Long-Range Technology Plan to implement its Vision—"All students who enroll in our schools will graduate from high school fluent in two or more languages, prepared and inspired to be successful in a four year college or university." The Technology Plan was approved by the State of Texas and has served as the foundation for Ysleta's participation in the E-Rate Program. Ysleta Request for Review of Ysleta Independent School District at 8, Nos. 96-45, 97-21 (filed Jan. 28, 2003) [hereinafter "Request for Review"].

The Technology Plan, as modified, served as the basis for Ysleta's E-Rate planning for Funding Year 2002. Ysleta studied the market and pricing for the products and services it believed would be necessary to implement the Technology Plan and prepared a Project Summary that identified specific equipment to be procured. Request for Review at 9-10. The Project Summary established cost estimates for these goods and services based on current market prices. In preparing its estimates, Ysleta reviewed listed prices from multiple vendors and studied the costs of similar projects approved by SLD.

B. Request For Proposals

Thereafter, on October 17, 2001, Ysleta issued a Request for Proposal ("RFP") for a "Technology Implementation and Systems Integration Partner." The stated "Purpose of the Solicitation" was the selection of a Systems Integrator "with the competence, expertise and resources necessary to assist the Ysleta Independent School District . . . in effectively introducing and applying technology throughout the District." RFP § 1.1; *id*. § 3.6. Ultimately, the Systems Integrator would "refine and support a state-of-the-art technology infrastructure that will provide world-class technology to the students and staff of the District" and assist Ysleta in "applying technology to improve student achievement and administrative practices in support of teaching and learning." RFP § 1.1; *id*. § 3.6. Specifically included within the scope of the partner's responsibilities were "all E-Rate funded projects." RFP § 1.1; *id*. § 3.6.

The RFP provided for a "two step" evaluation of proposals. In Step One, the RFP provided that Ysleta would identify the "provider deemed most qualified to arrive at a contract that will best meet the District's needs in terms of price, service, and response." RFP § 3.9; *see id.* § 1.12. In Step Two, the RFP envisioned that Ysleta would negotiate prices with the vendor selected at Step One. If the parties failed to agree to a "fair and reasonable price," RFP § 1.12, Ysleta would terminate negotiations with that vendor and conduct negotiations with the next most highly qualified vendor as determined during Step One. *See also* RFP §§ 3.8-3.9.

During Step One, offerors' proposals were evaluated and recommended to Ysleta's Board of Trustees based on an assessment of the following items:

- The technical competence of the Offeror;
- The reputation of the Offeror and of the Offeror's services;

- The quality of the Offeror's services;
- The Offeror's past relationship with the District;
- Completeness of proposal;
- Responsiveness of the proposal in meeting the District's needs; and
- Any other relevant factors.

RFP § 1.12. More specifically, the RFP identified eight evaluation criteria that focused on the vendors' potential "to infuse technology and better prepare students to be successful citizens and productive workers in the 21st century":

1. Availability and Quality of Resources;
2. Staff Development and Training;
3. Project Management/Systems Integration;
4. Technology Solutions;
5. Commitment to K-12 Education;
6. District funding considerations;
7. Pricing Model and Cost Assurances; and
8. Other Vendor Attributes.

RFP § 3.7. Under Criterion 4, the RFP provided functional performance standards rather than detailed design specifications:

> The District requires a network that will continue to provide the District with a modern, efficient and reliable network to support data and will eventually provide voice and video information transfer capabilities with and external to the member[] district buildings. Reliability and high performance are key requirements of this networking plan, as the District network continues to migrate to the base which must support the technology needs of the future.

RFP § 3.7.4. The RFP provided a nonexclusive list of the types of equipment and services to be provided under the systems integration contract, including "Physical Infrastructure Plans for building wiring, fiber optic distribution (or leasing), wiring closets, patch panels, etc."; "Logical network designs such as switches, routers, gateways, etc. including routing, protocols carried (LAN and WAN)"; "Installation of Hardware and Support"; and "Intranet and Internet access." *Id.*

Purposefully then, the RFP did not attempt to fix, in detail, the work to be performed by the Systems Integrator. Instead, Ysleta sought a vendor that would design a system to meet Ysleta's technology needs as those needs evolved: "The work itself will consist of all aspects of technology implementation for which the District desires to contract with the partner. The current technology program calls for the installation of new technology equipment, software and services on an on-going basis." RFP § 3.6. These performance standards are consistent with Ysleta's Technology Plan, which was a matter of public record available to all offerors. Request for Review at 20.

Consistent with Ysleta's use of functional performance standards rather than predetermined design specifications, the RFP provided that final pricing terms would be established in later negotiations. The RFP did not require firm fixed-price proposals because "the specific scope of work necessary for such pricing is impossible to determine." RFP § 3.7.7. Nevertheless, the RFP provided in Criterion 7, "Pricing Model and Cost Assurances," that "cost is a consideration." *Id.* The RFP stressed that "it is vitally important that The District receives value for its dollar in the other areas included in this scope of work and be able to demonstrate this to the District Board." *Id.*

To this end, the RFP required vendors to submit "a proposed schedule of hourly charges and/or other services based pricing [that the vendor] would normally use for a project of this scale." RFP § 3.7.7. Vendors' price models were required to "demonstrate throughout the life of the contract that the costs associated with this partnership are within normal and customary charges for the type of services provided." *Id.* The RFP repeatedly warned that the vendor's actual costs would be compared to the price model in the vendor's proposal, and that this information would be important to Ysleta's decision to exercise the annual options under the contract. RFP §§ 3.6, 3.7.7, 3.10.

C. Evaluation of Vendors

Ysleta received proposals from five vendors: Avnet Enterprise Solutions, Compaq, IBM Corp., I-Next, Inc., and SBC Southwestern Bell. Award Summary at 1. Each proposal was evaluated against the RFP's selection criteria, and an overall point score was prepared for each vendor. Each vendor's proposal included offeror submitted hourly rates for a variety of services and personnel. Four of the five vendors received the maximum number of points under the "Pricing Model and Cost Assurances" criterion.

IBM received the maximum number of points under each factor. Award Summary at 3. Ysleta selected IBM as the most qualified and the most likely to successfully deliver the products and services sought by Ysleta. Specifically noted was IBM's technical expertise and experience with the E-Rate program: "It has the technical expertise to advise YISD about the most cost effective routes available to complete specific projects." Award Summary at 3.

D. Contract Award

As envisioned in the RFP, Ysleta and IBM proceeded to negotiate statements of work ("SOWs") and final prices. IBM prepared a draft SOW that included prices for the services and equipment IBM proposed to provide. Ysleta reviewed these prices based on its own independent market research. This research included discussions with other equipment vendors and analysis of their pricing information. Additionally, Ysleta compared IBM's SOW with services and prices obtained by Ysleta in prior funding years and by comparable school districts.

During negotiations, Ysleta made numerous decisions to adjust and reduce the scope and cost of the work IBM would perform. Ysleta ultimately negotiated substantial reductions in price, totaling millions of dollars. Request for Review at 10.

The contract negotiated by the parties includes five statements of work for various services necessary to implement Ysleta's Technology Plan: Cabling Services, Network Electronics, Network File and Web Servers, Basic Unbundled Internet Access, and Technical Support Services. The SOWs set forth detailed specifications on the work to be performed by IBM under the contract. For example, under the Cabling Services SOW, IBM agreed to "install and test cabling in support of the adds, moves, and changes to the cabling plan at Ysleta ISD per the specification contained in Appendix C [of the SOW]." SOW (Cabling) at 5. Under this task, the SOW identified 11 subtasks, including "[p]rovide up to 3000 cable drops, and associated equipment," as well as completion criteria. *Id.* at 5-6.

Each SOW contains a "not to exceed" price, placing the risk of inefficient performance on IBM. *E.g.*, SOW (Cabling) at 13; Award Summary at 5. The contract also contains a "Procurement of Products" clause that allows Ysleta to review IBM's product pricing

information and to direct IBM to buy products from designated vendors. General Contract at 5. The contract provides that the cost of the entire contract would be the amount of SLD funding, plus a separate payment obligation of Ysleta.

E. No Challenge to the Procurement or the Award to IBM

Ysleta's E-Rate procurement potentially was subject to legal challenge in three different fora: (1) the school district itself through the Contracting Officer, (2) Texas state court, or (3) the Texas Building and Procurement Commission. *See infra* § IV.A.4. Significantly, no one, including the competitors, challenged the conduct of the E-Rate procurement, either before or after the award to IBM. *See infra* Section IV.A.4.

F. Denial of Funding

SLD denied funding for the project under the E-Rate program. In pertinent part, SLD denied Ysleta's funding requests for the work contemplated by IBM's contract because Ysleta's procurement process assertedly did not place sufficient emphasis on price competition. Additionally, SLD determined that Ysleta and IBM improperly defined the work to be procured after selecting IBM as the awardee. SLD Op. at 5-7. Central to SLD's denial was its conclusion that Ysleta failed to comply with the requirement that it select the "most cost-effective provider of service with low cost being the primary factor." *Id.* at 6; *see generally id.* at 5-7, 10. Under SLD's view of the law, school districts must "choose the most cost-effective alternative, with price being the single most heavily weighted factor." *Id.* Att. at 1 ("Warning to Funding Year 2003 Applicants and Service Providers Regarding Application Patterns That Violate FCC Rules").

IV.
DISCUSSION

A. Ysleta's E-Rate Procurement Complies Fully with Texas Procurement Law, Which Mandates the Use of Procurement Methods Designed to Obtain the "Best Value" for the School District.

1. Texas Law Expressly Endorses the Evaluation of Competitive Proposals Based on a Variety of Price and Nonprice Factors.

The Texas Education Code, §44.031, primarily governs Ysleta's award of contracts for the purchase of goods and services. Importantly, the Texas legislature amended these laws in 1995 to move from a procurement regime under which Texas school districts were required to accept the "lowest responsible bidder" on nearly all contracts to a "best value" procurement system in which low price is not necessarily determinative.[1] Today, school districts are charged with utilizing any one of nine identified procurement procedures "that provides the best value for the district." TEX. EDUC. CODE § 44.031(a). One of those methods is to issue a request for proposals, as Ysleta did here. *Id.* § 44.031(a)(3).

Contract awards in best value procurements are made using a cost/benefit analysis—a trade-off between the price offered and other features of the proposal such as quality, technical, management, and schedule to determine whether the quality advantages of a given offer are worth any associated added cost. Through best value procurements, Texas law ensures that state contracting is done in the most cost-effective manner possible. At the heart of this regime is the Texas legislature's ongoing interest in protecting the public fisc and ensuring that constituents receive value for their taxpayer dollars.

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[1] Notably, President George W. Bush signed Senate Bill No. 1, which amended Section 44.031 and which became 1995 Tex. Gen. Laws ch. 260, during his first term as the Governor of Texas on May 30, 1995.

The best value methodology employed by Texas here is not a procurement anomaly unique to that state. To the contrary, it is recognized in the ABA's 2000 Model Procurement Code for State and Local Governments ("MPC") (which forms the basis for many state and local government procurement statutes[2]) and in Federal law as one of the chief methods, if not the chief method, by which both state and Federal Governments purchase goods and services.

Like the Texas statute, the MPC provides a menu of acquisition procedures that state and local governments can use to "satisfy public needs for supplies, services, and construction at the most economical prices." MPC § 3-201 cmt. (2). Also like the Texas statute, the MPC provides for the use of Requests for Proposals (in addition to competitive sealed bids) as a "valid competitive procurement method[]." *Id.* § 3-201(b) & cmt. (3) (concerning "competitive sealed proposals"); *id.* § 3-203(2) (providing for the use of RFPs).

In discussing the use of RFPs, MPC § 3-203(7) provides:

> Award shall be made to the responsible offeror whose proposal conforms to the solicitation and is determined in writing to be the most advantageous to the [State] taking into consideration price and the evaluation factors set forth in the Request for Proposals.

See also MPC § 3-203(2) ("Proposals shall be solicited through a Request for Proposals."). Commentary to the MPC explains that this procurement method is designed to allow trade-offs between price and quality:

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[2] To date, the MPC has been adopted by 16 States: Kentucky (1979), Arkansas (1979), Louisiana (1980), Utah (1980), Maryland (1981), South Carolina (1981), Colorado (1982), Indiana (1982), Virginia (1983), Montana (1983), New Mexico (1984), Arizona (1985), Alaska (1988), Rhode Island (1989), Hawaii (1994), and Pennsylvania (1998). The MPC has also been adopted by the Territory of Guam and countless local jurisdictions. ANNOTATIONS TO THE MODEL PROCUREMENT CODE FOR STATE AND LOCAL GOVERNMENTS WITH ANALYTICAL SUMMARY OF STATE ENACTMENTS at vii-xiv (3d ed. 1996).

> [T]he quality of competing products or services may be compared and trade-offs made between price and quality of the products or services offered (all as set forth in the solicitation). Award . . . is then made to the responsible offeror whose proposal is most advantageous to the [State].

Id. § 3-203(1) cmt. (3)(a). The MPC defines "Advantageous" as connoting "a judgmental assessment of what is in the [State's] best interest. Illustrations include determining . . . (b) whether quality, availability, or capability is overriding in relation to price in procurements for research and development, technical supplies, or services . . . ." *Id.* § 3-203(1) cmt. (4).

Consistent with the MPC, the Texas Education Code affords school districts broad discretion to determine the evaluation factors upon which it may rely in awarding contracts. The Texas statute specifically identifies the following potential factors:

> (1) the purchase price;
>
> (2) the reputation of the vendor and of the vendor's goods or services;
>
> (3) the quality of the vendor's goods or services;
>
> (4) the extent to which the goods or services meet the district's needs;
>
> (5) the vendor's past relationship with the district;
>
> . . .
>
> (7) the total long-term cost to the district to acquire the vendor's goods or services; and
>
> (8) any other relevant factor specifically listed in the request for bids or proposals.

TEX. EDUC. CODE § 44.031(b); *accord* MPC § 3-203(5) & cmt. (requiring that the RFP "set forth the relative importance of the factors and any subfactors, in addition to price, that will be considered in awarding the contract.").

Both the Texas and the MPC procurement regimes therefore emphasize price as a fundamental factor in any selection decision. Nevertheless, these regimes recognize the reality that price does not exist in a vacuum. Indeed, price is meaningless without consideration of qualitative differences in the service and products offered for acquisition. Accordingly, Texas and the MPC have shifted their focus from sealed bidding, which centers on price to the exclusion of qualitative differences, towards a regime that focuses on value, *i.e.*, what prices will actually mean in terms of meeting the government's various needs for products and services.[3] The result is a procurement system that provides the products and services to meet the government's needs at the lowest overall cost.

2. Texas Law Also Endorses the Use of "Two-Step" Procurements for the Acquisition of Certain Technical and Engineering Services.

Texas procurement law also confers on school districts the discretion to utilize a two-step acquisition process for the procurement of professional and technical services. *Id.* § 44.031(f) (citing TEX. GOV'T CODE § 2254.003). Texas procurement law, in turn, prescribes a two-step process for the acquisition of professional services, which includes any services within the scope of professional engineering.[4] TEX. GOV'T CODE § 2254.003. The statute provides that in awarding professional services contracts, selection is to be made "on the basis of demonstrated competence and qualifications to perform the services." *Id.*

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[3] "There is hardly anything in the world that some men cannot make a little worse and sell a little cheaper, and the people who consider price only, are this man's lawful prey." — John Ruskin (1819-1900).

[4] The systems integration contract procured by Ysleta more closely resembles these engineering and design services than generic commercial products and services. Rather than purchasing standard products and services from an established catalog, IBM will design, build, and support an entire information infrastructure.

The two-step process is laid out in slightly greater detail in the immediate next section of the Texas Government Code. That statute instructs agencies, when acquiring professional services, to:

- "first select the most highly qualified provider of those services on the basis of demonstrated competence and qualifications"; and
- "then attempt to negotiate with the provider a contract at a *fair and reasonable price*."

Id. § 2254.004(a) (emphasis added). If the government and most highly qualified provider cannot negotiate a mutually agreeable contract, then the government is to end negotiations with that vendor and commence negotiations with the next most highly qualified provider. *Id.* § 2254.004(b). This process should continue until a contract is executed. *Id.* § 2254.004(c).

Texas's two-step process for professional and technical services provides yet another mechanism to ensure that taxpayers obtain value for their procurement dollar. This mechanism is identical to the procedure for acquisition of architectural and engineering services in the MPC. As the Commentary to Section 5-205 of the MPC explains, the two-step process is designed to secure value where the scope of the work is necessarily evolutionary and complex:

> (3) It is considered most desirable to make the qualification selection first and then to discuss the price because both parties need to review in detail what is involved in the work (for example, estimates of man-hours, personnel costs, and alternatives that the architect-engineer or land-surveyor should consider in depth). *Once parameters have been fully discussed and understood and the architect-engineer or land surveyor proposes a fee for the work, the recommended procedure requires the [State] to make its own evaluation and judgment as to the reasonableness of the fee.*
>
> (4) If the fee is fair and reasonable, award is made without consideration of proposals and fees of other competing firms. If

> the fee cannot be negotiated to the satisfaction of the [State], negotiations with other qualified firms are initiated. *Thus price clearly is an important factor* in the award of the Architectural and Engineering Services contract under this procedure. The *principal difference* between the recommended procedure for architect-engineer and land surveyor selection and the procedures used in most other competitive source selections *is the point at which price is considered*.

MPC § 5-205(3) cmts. (3)-(4) (emphasis added).

This two-step procedure recognized by both the Texas legislature and the MPC is therefore yet another acceptable method for achieving best value. Although the sequence of the process may differ in order to accommodate the highly technical and skilled services being acquired, the ultimate objective is the same: cost-effectiveness.

3. Ysleta's E-Rate Procurement Complied with Texas Procurement Law.

Based on our review of the record, we conclude that Ysleta fully complied with the strictures—as well as the objectives—of Texas law. The RFP contemplated the selection of a single Systems Integrator "to implement, refine and support a state-of-the-art technology infrastructure that will provide world-class technology to the students and staff of the District." RFP § 1.1; *see also id.* § 3.6. Part and parcel of this effort is "the installation of new technology equipment, software and services on an on-going basis." RFP § 3.6. In short, Ysleta's RFP called for technology services, including the provision and installation of technology equipment.

In accordance with the scope and type of these services, the RFP identified a two-step evaluation process that mirrors the procedures contemplated under Sections 2254.003-004 of the Texas Government Code. In Step One, Ysleta evaluated the following capabilities identified in the general procurement procedures and the professional services acquisition procedures:

- The technical competence of the Offeror;

- The reputation of the Offeror and of the Offeror's services;
- The quality of the Offeror's services;
- The Offeror's past relationship with the District;
- Completeness of proposal;
- Responsiveness of the proposal in meeting the District's needs; and
- Any other relevant factors.

RFP § 1.12. To facilitate the Step One evaluation, Ysleta identified eight weighted factors for which it requested that offerors "provide relevant responses." RFP § 3.7. These included: (1) Availability and Quality of Resources (30 points); (2) Staff Development and Training (20 points); (3) Project Management/Systems Integration (50 points); (4) Technology Solutions (20 Points); (5) Commitment to K-12 Education (20 points); (6) District funding considerations (100 points); (7) Pricing Model and Cost Assurances (25 points); and (8) Other Vendor Attributes (30 points).

In fact, Ysleta went a step further by actually considering pricing models in its initial phase. As the RFP shows, price was given essentially the same weight as Availability and Quality of Resources, Staff Development and Training, Technology Solutions, and Commitment to K-12 Education.

During Step One, Ysleta evaluated each offeror's submission in accordance with the stated evaluation criteria. IBM received a perfect 300 points from *each* Ysleta evaluator, exceeding the next closest submission by nearly 25%. Accordingly, Ysleta selected IBM as the most qualified vendor and the vendor most likely to successfully deliver the products and services sought by Ysleta. Importantly, four of the five vendors that responded to the RFP

received the maximum number of points under the "Pricing Model and Cost Assurances" criterion. Award Summary at 2. Accordingly, price was not a discriminator among the competing proposals and the relative weight of price to the other evaluation criteria had no effect on Ysleta's selection of IBM as the most qualified vendor.

Ysleta's evaluation of competitive proposals against the bases and criteria identified in the RFP is entirely consistent with Texas's objective of obtaining "the best value for the district." TEX. EDUC. CODE § 44.031(a). Indeed, many of the bases and factors identified in the RFP are specifically identified in the statute, including: price, reputation, quality, technical acceptability, and past performance.

As envisioned by the RFP in Step Two, Ysleta then proceeded to negotiate fair and reasonable prices with IBM for the SOWs to which they had agreed. Ysleta was in a good position to assess whether IBM's proposed prices were fair and reasonable. In preparing to implement its Technology Plan, Ysleta studied the market and pricing for the products and services it believed would be necessary. In response to the RFP, Ysleta received pricing models from five major private competitors. During negotiations, therefore, Ysleta was in a position to compare IBM's prices to (1) IBM's proposed rates in its pricing model; (2) the proposed rates of the other competitors; (3) commercially available price listings for the same or similar products and services; (4) Ysleta's own experience acquiring similar products and services; (5) the experience of other school districts acquiring similar products and services; and (6) the prices for similar E-Rate projects.

At all times, Ysleta was free to terminate negotiations with IBM if, for any reason, Ysleta concluded that IBM's proposed prices were not fair and reasonable. The other offerors,

including second-ranked SBC Southwestern Bell, remained ready and willing to pick up wherever IBM failed. Moreover, at all times these offerors were free to protest any apparent impropriety in the procurement process.

SLD appears to view the negotiation of these SOWs as unusual, repeatedly observing that "[t]he [SOWs] were negotiated after Ysleta selected IBM." *E.g.*, SLD Op. at 5. Far from unusual, this is the process expressly contemplated by Texas law and the MPC, which forms the basis for many state and local government procurement statutes. Many legislatures, including those of Texas and the United States, have endorsed this process as a mechanism to meet government's needs for products and services while obtaining value for taxpayers' procurement dollar. *See infra* Section IV.B.3.

More fundamentally, in denying Ysleta's funding requests, SLD expressly recognized that Texas procurement law authorizes "best value" procurements. SLD Op. at 6. Nevertheless, SLD suggested that these procedures, to the extent that price is not "the primary factor," may not ensure the cost-effective acquisition of goods and services required by FCC regulations. *Id.* at 4, 6-7 (quoting Universal Service Order, 12 FCC Rcd at 9029-30, para. 481). In drawing this conclusion, we believe that SLD has confused price with value. As reflected in the Texas Code, as well as the MPC, price need not be the determinative criterion in the solicitation of a public contract. Instead, these authorities counsel that price should be evaluated in terms of the qualitative differences among products and services offered for acquisition. Because value cannot be determined without reference to price, price is always a fundamental—or primary[5]—

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[5] In its Further Explanation, SLD relies on the term "primary" used by the Commission in its Universal Service Order. SLD Op. at 4, 6-7. In doing so, SLD appears to use "primary" according to one dictionary definition of that term: "first in importance." WEBSTER'S NEW

factor in any best value analysis. Nevertheless, the lodestar for modern procurement is not price, but value.

4. Neither Ysleta's E-Rate Procurement Process Nor Its Award to IBM Was Challenged by IBM's Competitors.

Finally, it is very important to note that Ysleta's E-Rate procurement potentially was subject to legal challenge both before and after the decision to award to IBM. Competitors for the Ysleta contract could have filed pre-award and post-award protests in any of three different fora: (1) the school district itself through the Contracting Officer, RFP § 1.15 (authorizing protests to the Contracting Officer); (2) Texas state court, TEX. EDUC. CODE § 44.032(f) (authorizing protests in state court to enjoin performance of a contract made in violation of purchasing statutes); or (3) the Texas Building and Procurement Commission, TEX. ADMIN. CODE § 111.3. [6]

Texas, like the Federal Government, relies on the actual competitors whose business interests are at stake to enforce procurement law. *See, e.g.*, *Scanwell Labs., Inc. v. Shaffer*, 424 F.2d 859, 864 (D.C.Cir.1970) (explaining that the actual competitors "are the people who will

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WORLD DICTIONARY (3d ed. 1988). As discussed *infra* in Section IV.C, the Universal Service Order ultimately focused on cost-effectiveness, leaving states "'maximum flexibility' to take service quality into account and to choose the offering." Universal Service Order, 12 FCC Rcd at 9029-30, para. 481. Moreover, the Commission has since clarified that its statement that "price should be the primary factor [does not] mean that price should be the initial determining factor considered to the exclusion of all other factors." Tennessee Order, 14 FCC Rcd at 13738, para. 8. In light of the Commission's guidance on the matter, we believe that it is appropriate to use the term "primary" according to its broader dictionary definition: "fundamental; elemental; basic." WEBSTER'S NEW WORLD DICTIONARY.

[6] This three-tiered protest system appears modeled on the federal procurement protest system, which authorizes protests to (1) federal agencies, 48 C.F.R. § 33.103; (2) the U.S. General Accounting Office, 48 C.F.R. § 33.104 and 4 C.F.R. Part 21; and (3) the U.S. Court of Federal Claims, 28 U.S.C. § 1491(b). *See also* Ysleta Request for Review at 20-21 & Ex. 11 at 8 (Duncan Affidavit) (explaining options of competitors to complain about procurement).

really have the incentive to bring suit against illegal government action, and they are precisely the plaintiffs to insure a genuine adversary case or controversy"); Robert C. Marshall *et al*., *The Private Attorney General Meets Public Contract Law, Procurement Oversight by Protest*, 20 HOFSTRA L. REV. 1 (1991) (noting that protest systems are favored over centralized government regulation because self-interested "private attorneys general" are likely to have better information than auditors about deviations from procurement statutes and regulations).

If the solicitation were unduly favorable to IBM or otherwise susceptible to manipulation, other bidders undoubtedly would have filed protests. Likewise, if other bidders believed the award to IBM did not result in acceptance of the most cost-effective proposal, they would have tried to overturn it. *See, e.g., Daniels Bldg. & Constr., Inc. v. Silsbee Indep. Sch. Dist.*, 990 S.W.2d 947 (Tex Ct. App. 1999) (granting injunction against award of contract where school district failed to properly publish time and place for submitting bids, preventing protester from competing with other bidders).

No protest was lodged against the conduct of the E-Rate procurement, either before or after the award to IBM. The vendors that competed in this procurement are among the largest and most sophisticated information technology businesses in the world. Each vendor was perfectly capable of enforcing its rights had it found any irregularity or impropriety in the procurement process. Instead, the vendors participating in Ysleta's E-Rate procurement appear to have unanimously agreed that there was no ground to challenge the competition.

B. <u>Ysleta's E-Rate Procurement Is Consistent with Federal Procurement Principles.</u>

Neither the general "best value" approach nor the specific "two-step" procurement process for the acquisition of professional services is unique to Texas. To the contrary, they are

modeled on the Federal Government's own procurement laws. Congress itself has emphasized that Federal agencies should shift away from making contract awards based on low-cost to making them based on which proposal represents the "best value" overall to the government. Indeed, the vast majority of Federal procurement dollars are awarded under the best value concept. Federal procurement law, in fact, expressly equates the concepts of "best value" and the "lowest overall cost alternative" in the context of General Service Administration ("GSA") Federal Supply Schedule ("FSS") contracts. Finally, like Texas law, Federal acquisition law expressly recognizes as "competitive"—indeed requires—the use of the two-step process where the Government is procuring services that require certain engineering and technical expertise. In short, SLD appears to have concluded that it will not fund projects utilizing procurement processes upon which the Federal Government itself relies to prudently spend taxpayers' dollars.

1. The Overwhelming Majority of Federal Government Procurements are Awarded Based on the "Best Value" Concept.

Consistent with Texas law, Federal law provides agencies broad discretion to award contracts for the procurement of goods and services to the offeror that provides the "best value" to the government under an overall evaluation of price and quality factors, such as technical excellence, past performance, and management capability. *See* 10 U.S.C. § 2305(a)(2); Federal Acquisition Regulation ("FAR") Part 15.[7] Under the FAR, "best value" is defined as "the expected outcome of an acquisition that, in the Government's estimation, provides the greatest overall benefit in response to the requirement." FAR § 2.101.

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[7] The FAR, which identifies federal procurement rules, is set forth in Title 48 of the Code of Federal Regulations.

Federal law recognizes that best value encompasses procurements in which nonprice or technical factors may be "significantly more important than cost or price." 10 U.S.C. § 2305(a)(3)(A)(iii). Nevertheless, by statute price must be an evaluation factor in every best value procurement. *Id.* § 2305(a)(3)(A)(ii). Federal procurement law, consistent with Texas law as discussed above, recognizes that price should not be evaluated without also taking into consideration the qualitative differences that prices often represent.

Price, however, always remains a primary factor in any best value source selection because the Government must affirmatively determine that the higher quality of one proposal is worth any premium that will have to be paid. This is true regardless of the relative weight initially assigned to price and nonprice evaluation factors:

> The tradeoff between cost/price and technical factors made by the selection official must still be based on the established criteria, but, *whatever the stated relative importance of the factors*, the ultimate decision will be based on an assessment of whether the difference in technical or management merit of the proposals is worth the difference in price.

JOHN CIBINIC, JR. & RALPH C. NASH, JR., FORMATION OF GOVERNMENT CONTRACTS 932 (3d ed. 1998) (emphasis added).

Importantly, the best value concept reflects a deliberate shift in procurement law away from traditional procedures that overemphasized price at the expense of quality. Historically, Federal procurement was conducted through sealed bidding, in which the Government simply describes its needs in writing and awards the contract to the lowest-price, responsive, and responsible bidder. 10 U.S.C. § 2305(b)(3); FAR Part 14. The Competition in Contracting Act of 1984 ("CICA") "ended the practice of 'favoring' the use of sealed bidding when it made sealed bidding and competitive negotiation parallel procedures for meeting the statutory

competition requirements." CIBINIC & NASH, *supra* at 505. "The purpose of negotiation is to permit agencies to use flexible procedures not permitted in the sealed bidding process. . . . Contracting by negotiation also enables the Government to use techniques which allow it to make tradeoffs between cost or price and other factors when selecting a proposal for award." *Id.* at 709-710. Today, "less than 10 percent of federal procurement dollars are spent in sealed bids." *Id.* at 505. Instead, the vast majority of those dollars are spent in negotiated "best value" procurements.

The legislative history of amendments to CICA reveals that in emphasizing the use of best value procurement methods, Congress sought to fundamentally change agencies' unwise overemphasis on cost relative to quality:

> The committee recognizes that the procurement evaluation process for professional and technical services for today's complex programs should be different from the process utilized for acquiring goods or routine services. It believes that in the acquisition process for sophisticated professional and technical services, emphasis generally needs to be placed on the quality of the services offered—including technical capability, management capability, and prior experience of the offeror. There needs, of course, to be a proper balance between price and quality of the services.
>
> The committee is aware that current regulations permit weightings favoring quality of the services and technical capabilities, but finds that in actual practice, political and institutional considerations have often resulted in the acceptance of the low bid by procurement authorities. The committee recognizes that this may occur because evaluation of service quality is more subjective than comparison of price. Justification based on price may be less subject to controversy than justification based on quality assessment. To assure the greatest benefit to the government in procuring sophisticated professional and technical services, it is essential that quality of the service be given appropriate weight related to cost and price factors.

S. REP. NO. 99-331, at 266 (emphasis added), *reprinted in* 1986 U.S.C.C.A.N. 6413, 6461-62; *see also* H.R. REP. NO. 99-1001, at 502, *reprinted in* 1986 U.S.C.C.A.N. 6529, 6513 ("The conferees generally believe that the Department of Defense places too little emphasis on the quality of the product or service provided.").

Congress has likewise emphasized that by permitting the evaluation of technical, as well as price factors, it recognizes that the best overall value to the government oftentimes will be based not just on the low-cost bidder but on technical benefits that are not easily quantified:

> [C]ompetitive negotiation procedures are used not only to allow an evaluation of cost as opposed to price, but also to allow consideration of technical factors that cannot be quantified in cost terms. While they may not be objectively quantifiable, factors such as past performance, technical capability, management capability, design, quality, and cost discipline, are important and necessary aspects of determining which contractor will provide the best product or service to the government for the money. In many instances these technical factors are more important than quantifiable lowest overall cost.

H. REP. NO. 101-665, at 300-03, *reprinted in* 1990 U.S.C.C.A.N. 2931, 3026-29. In short, non-quantifiable technical factors must necessarily be considered, along with cost, to determine which offer provides the government the "best value."

Part 15 of the FAR implements Congress's policy of cost-effectiveness with respect to negotiated procurements. Part 15 was substantially rewritten in 1997 with the express goal "to ensure that the Government, when contracting by negotiation, receives the best value, while ensuring the fair treatment of offerors." 62 Fed. Reg. 51224, 51224 (Sept. 30, 1997). While both price and quality must be evaluated in every procurement, 10 U.S.C. § 2305(a)(3)(A)(2); FAR § 15.304(c)(1)-(2), the FAR envisions a best value "continuum" in which the relative importance of price varies with quality considerations:

> For example, in acquisitions where the requirement is clearly definable and the risk of unsuccessful contract performance is minimal, cost or price may play a dominant role in source selection. The less definitive the requirement, the more developmental the work required, or the greater the performance risk, the more technical or past performance considerations may play a dominant role in source selection.

FAR § 15.101. The FAR, consonant with CICA, expressly recognizes that quality factors may be "significantly more important than cost or price" in a "best value" procurement. FAR § 15.304(e).

Again, however, regardless of the relative weight initially assigned to price as an evaluation criterion, *price is always a primary factor in a best value source selection* because every price premium must be justified by some qualitative advantage. As the FAR commands: "This process permits tradeoffs among cost or price and non-cost factors and allows the government to accept other than the lowest price proposal. The perceived benefits of the higher priced proposal *shall* merit the additional cost . . . ." FAR § 15.101(c) (emphasis added). The General Accounting Office, which is primarily responsible for enforcing Federal procurement law, has repeatedly required a reasoned tradeoff between price and nonprice factors, even where price is relatively less important in the evaluation of the proposals. *E.g.*, *ICOS Corp. of America*, 66 Comp. Gen. 246, 248, B- 225392, Feb 10, 1987, 87-1 CPD ¶ 146 ("This discretion existed notwithstanding the fact that price was the least important evaluation factor.").[8] In short, even

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[8] It is important to distinguish between the initial evaluation of proposals on one hand, and the ultimate selection of the proposal that represents the best value on the other. As explained in *ICOS*, agencies evaluate proposals by scoring or rating them against the evaluation criteria. However, unless the solicitation specifically provides that the highest-scored proposal wins, the evaluation scores are not determinative, but are instead "merely guides for decision making by the source selection official, who ha[s] the discretion to determine whether the technical advantage associated with [a] proposal [is] worth the extra cost associated with the proposal." 66 Comp. Gen. at 248.

where a school district utilizes a "best value" procurement that permits a tradeoff between cost and quality factors, cost is still a primary factor because any additional quality advantages must be evaluated as being worth the additional cost.

That does not mean, however, that best value tradeoffs must be quantified. FAR § 15.308 ("Although the rationale for the selection decision must be documented, that documentation need not quantify the tradeoffs that led to the decision."). As long as the articulated tradeoff rationale is reasonable, it will stand. *TRW, Inc. v. Unisys Corp.*, 98 F.3d 1325, 1327 (Fed. Cir. 1996) ("Thus, the [trial tribunal] may overturn the agency's [contract award] decision only if the decision has no basis in reason, even if the agency accepted a higher-cost proposal as its best value."). Indeed, the Court chiefly responsible for reviewing the Federal Government's procurement practices has construed the best value procurement regime to confer on procurement officials "broad discretion." *See Lockheed Missiles & Space Co. v. Bentsen*, 4 F.3d 955, 958 (Fed. Cir. 1993). In *Lockheed*, in fact, the Federal Circuit reviewed an award by the Internal Revenue Service of a contract for office automation systems as well as maintenance and support services—similar to the equipment and services procured by Ysleta. The Court upheld an award to a technically superior proposal that was $700 million more expensive than its chief competitor's otherwise acceptable proposal, holding that price was still an important evaluation factor. *Id.*; *see also Grumman Data Sys. Corp. v. Widnall*, 15 F.3d 1044, 1046, (Fed.Cir.1994) (upholding an Air Force decision to award a computer networking contract to an offeror despite its $33.9 million (59%) higher price).

Once the Federal Government selects the "best value" offeror, however, it must still determine that the contract price is "fair and reasonable." *See* FAR § 15.402(a) ("Contracting Officers must purchase supplies and services at fair and reasonable prices."). Where adequate

price competition exists, Federal agencies need not obtain any additional information to determine reasonableness. Otherwise, in determining price reasonableness, Federal buyers are directed to consult the very same types of information that Ysleta reviewed here:

- Information related to price (e.g., established catalog, published price lists or market prices), including information within the government;
- Information on the prices at which the same or similar items have been sold previously, including comparison of previously proposed prices and previous government and commercial contract prices with current proposed prices for the same or similar items;
- Comparison of proposed prices with independent government cost estimates; and
- Comparison of proposed prices with prices obtained through market research for the same or similar items.

FAR §§ 15.402(a); 15.404-1(b).

At bottom, the "best value" procurement concept prescribed by Texas law is the very method by which the United States spends the majority of its procurement dollars. This is unsurprising given that both Federal and state procurement law seek to protect the same interest—cost-effectiveness.

2. Federal Procurement Law Recognizes The "Best Value" Concept As Coextensive With The Concept of Procuring Goods and Services From the Lowest Overall Cost Alternative.

The procurement procedures Ysleta utilized likewise resemble those that the Federal Government follows in awarding and utilizing GSA FSS contracts. FSS contracts are entered into by GSA with multiple vendors for a wide variety of goods and services and provide a streamlined way for agencies government-wide to order products and services.

The FSS award process is legally recognized as "competitive," *see* FAR §§ 6.102(d)(3) and 8.404(a), but it does not require the comparative evaluation of vendor proposals. Rather, GSA reviews the individual vendor's commercial prices for products and labor rates for services to determine whether they are "fair and reasonable." GSA then negotiates a general discount off of the vendor's commercial prices based on the vendor's expected volume of government-wide FSS business. *See generally* FAR Subpart 8.4. The contract does not, however, contain a detailed Statement of Work for any services offered because that can be developed only by an ordering agency after it determines its particular needs for a particular order.

When an agency orders products and services from an FSS contract, Congress mandates that the order "result in the *lowest overall cost alternative* to meet the needs of the Government." 41 U.S.C. § 259(b)(3) (emphasis added). Federal procurement regulators have concluded that this mandate is fulfilled even when a *best value* procurement method is used and even when it determines that technical factors for an individual order are significantly more important than price.

Specifically, in outlining the procurement procedures that agencies must follow in placing orders, the governing regulations expressly equate the "lowest overall cost alternative" standard with the "best value" standard: "By placing an order against a [FSS contract] using the procedures in this section, the ordering office has concluded that the order represents the *best value* <u>*and*</u> results in the *lowest overall cost alternative*." FAR § 8.404(a)(1)(ii) (emphasis added). Indeed, the best value and lowest overall cost alternative standards are both met, even where technical factors are significantly more important than price, so long as the ordering agency determines that the qualitative benefits of a particular program are worth any price premium. *See* FAR § 8.404(b)(2) (identifying nonprice factors); *Computer Prods., Inc.*, B-

284702, May 24, 2000, 2000 CPD ¶ 95 (upholding "best value" evaluation scheme for an FSS order in which technical considerations were more important than price); *see also Labat-Anderson, Inc.*, 2001 WL 410356 (Comp. Gen. Apr. 16, 2001). Under FSS contracting and ordering procedures, therefore, the mandate to procure the "lowest overall cost alternative" can be met through the conduct of a "best value" procurement.

3. Texas's Two-Step Procurement Process Comports With Federal Procurement Law.

Finally, Texas's two-step procurement process, upon which the subject acquisition was modeled, is virtually identical to the Federal Government's procedures for the procurement of "[p]rofessional services of an architectural and engineering nature" ("engineering services"). 40 U.S.C. § 1102(2)(A). The Brooks Act, 40 U.S.C. § 1101-1104, declares the Government's policy "to publicly announce all requirements for architectural and engineering services and to negotiate contracts for architectural and engineering services on the basis of demonstrated competence and qualification for the type of professional services required and at fair and reasonable prices." 40 U.S.C. § 1101.

The statute requires a two-step selection process for the award of engineering services contracts. In the first step, an agency evaluation board evaluates interested firms in accordance with the applicable evaluation criteria, and holds discussions with at least three of the most highly qualified firms regarding concepts and alternative methods. 40 U.S.C. § 1103(c); FAR §§ 36.602-3 to -4. As reflected below, the evaluation criteria for the first step focus on capability and quality factors, not price:

> (1) professional qualifications necessary for satisfactory performance of required services;

(2) specialized experience and technical competence in the type of work required, including, where appropriate, experience in energy conservation, pollution prevention, waste reduction, and the use of recovered materials;

(3) the capacity to accomplish the work in the required time;

(4) past performance on government and commercial projects in terms of cost control, quality of work, and compliance with performance schedules;

(5) location in the general geographic area of the project and knowledge of the locality of the project (provided this consideration does not unduly limit the field of competition); and

(6) other evaluation criteria deemed appropriate by the agency.

FAR § 36.602-1. The evaluation board then prepares a selection report for the selection authority, ranking at least the three top firms. FAR § 36.602-3(d).

In the second step, the contracting officer solicits a proposal from the top-ranked firm and begins negotiations to obtain a fair and reasonable price. 40 U.S.C. § 1104. In determining whether an offeror's price is fair and reasonable, the agency relies on an already prepared government estimate of the cost of engineering services. 40 U.S.C. § 1104(a); FAR § 36.605. If a mutually satisfactory contract cannot be negotiated, the contracting officer terminates discussions with the top-ranked firm and solicits a proposal from the next firm on the final selection list. 40 U.S.C. § 1104(b). The contracting officer continues with this process until a satisfactory contract is negotiated. If the contracting officer exhausts the list without negotiating a mutually satisfactory contract, the agency's selection authority may direct the evaluation board to recommend additional firms. *See also* FAR Subpart 36.3 (prescribing a similar two-step method for the procurement of "design-build" contracts).

Congress established this system of competitive negotiation because it perceived significant differences between engineering services and the usual goods and services acquired by the Government. First, Congress recognized that "engineering involve[s] countless different specialties and approaches. There is also a broad variation in the expertise and the experience of firms competing for Government work." H.R. REP. NO. 92-1188, at 3. Congress concluded that, "[u]nder a procurement with the amount of fee a factor in the selection, along with qualifications and experience, each [contractor] would be under pressure to lower his fee quotation to meet competition. This, in turn, would adversely affect the quality of his design." *Id.* The two-phase process, on the other hand, "favors selection of the most skilled and responsible members of these professions." *Id.*

Second, Congress recognized that, because of the considerable cost involved in designing the project, a traditional competition with price as an initial evaluation factor "would induce [contractors] to favor the least costly design concept regardless of the impact on the quality of the plans and specifications." H.R. REP. NO. 92-1188, at 4. Under the two-step approach, on the other hand:

> [Contractors] are under no compunction to compromise the quality of the design of the level of effort they will contribute to it in order to meet the lower "fee" quotations of other [contractors]. They are free to suggest optimum design approaches that may cost more to design, but can save in construction costs and otherwise increase the quality of the building or facility to be constructed.

Id. at 3; *see also id*. at 4 ("[T]he savings would inevitably be reflected in a reduction in the [contractor's] design costs . . . which could mean high construction and maintenance costs and, generally, lower quality buildings and other facilities."). Accordingly, in deciding not to

evaluate price in Step One, Congress specifically expected that overall value would be maximized as a result of increased quality and future savings.

Congress expressly dismissed any concern that the offeror selected in Step One could manipulate the process to obtain a higher price:

> This system protects the interest of the taxpayers. Having won the competition on the basis of capability, the winning [contractor] must then negotiate his fee. He must demonstrate on the basis of projected costs that his fee is fair and reasonable. He must accept whatever adjustments the Government demands if he wishes to obtain the contract. He knows that if he holds out for an unfair or unreasonable fee, the Government will terminate the negotiations and award the contract to another [contractor] at a fair and reasonable price.

H.R. REP. NO. 92-1188, at 3.

The Federal Government has blessed, therefore, a two-step procurement process, in which price or cost is not evaluated at all in the first phase. Price is not even raised until the second phase. Nevertheless, the FAR expressly recognizes that the two-step process for procurement of engineering services is "competitive." FAR § 6.102(d)(1).

The two-step approach adopted in Ysleta's E-Rate procurement is virtually identical to the two-phase procurements approved in FAR Part 36. Ysleta first evaluated offerors to identify the vendor most qualified to deliver the products and services needed by the schools. In doing so, Ysleta focused on many of the criteria identified in FAR § 36.602-1, including professional qualifications, specialized experience and technical competence, and past performance. Indeed, Ysleta actually went a step further, evaluating the vendors' pricing models in Step One to determine whether the quoted prices were "within normal and customary charges for the type of services provided." RFP § 3.7.7.

Based on this evaluation, Ysleta identified IBM as the vendor most qualified to implement Ysleta's Technology Plan, and proceeded to negotiate a fair and reasonable price based on IBM's proposed solution to Ysleta's needs. As with engineering services, had Ysleta failed to negotiate agreeable terms with IBM, it would then have begun negotiations with the next most qualified offeror as evaluated in Step One.

As discussed above, Texas uses this two-step procedure for all professional services. TEX GOV'T CODE § 2254.003; Tex. Educ. Code § 44.031(f) (allowing school districts to use two-step procedures for the procurement of professional services). SLD specifically objected to the use of this procedure as incompatible with the FCC's objective of obtaining information technology services at the lowest overall cost. SLD Op. at 6-7. However, as the Federal regime for procurement of engineering services makes clear, the two-step process is simply another means to the same end—best value, or cost-effectiveness. Indeed, Congress determined years ago that "[t]his system protects the interest of the taxpayers," specifically by reducing future costs that inevitably result from awarding complex, highly technical projects to the lowest bidder. H.R. REP. NO. 92-1188, at 3-4.

C. The Texas and Federal Procurement Regimes are Consistent with the Policies and Objectives that the Commission has Articulated for E-Rate Procurements.

As the Commission has emphasized repeatedly, SLD has no authority to change the Commission's rules or to promulgate new rules or policies.[9] Under well-established FCC

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[9] *Changes to the Board of Directors of the National Exchange Carrier Association, Inc.; Federal-State Joint Board on Universal Service,* CC Docket Nos. 96-45 and 97-21, Third Report and Order, Fourth Order on Reconsideration, and Eighth Order on Reconsideration, 13 FCC Rcd 25058, 25067, para. 16 (1998) ("[W]e emphasize that USAC's function…will be exclusively administrative. USAC may not make policy, interpret unclear provisions of the statute or rules, or interpret the intent of Congress.").

precedent, state and local procurement officials enjoy "'*maximum flexibility*' to take service quality into account and to choose the offering . . . that meets their needs 'most effectively and efficiently.'" Universal Service Order, 12 FCC Rcd at 9029-30, para. 481 (emphasis added). The FCC's emphasis on cost-effectiveness mirrors the principle of best value in Texas and Federal procurement law. Indeed, the FCC has explicitly endorsed the best value regime used by Texas and the Federal Government.

The FCC's Rules and decisions establish that price is an important, but not necessarily determinative, factor in awarding contracts for which E-Rate funding is sought. Rather, the guiding principle is that state and local procurement officials must select the most cost-effective alternative, taking into account price, quality, and other relevant factors, and that determinations by those officials must be presumed proper absent evidence to the contrary. *See* 47 C.F.R. § 54.511(a) (expressly authorizing state and local procurement officials to "consider relevant factors other than the pre-discount prices submitted by providers"); Universal Service Order, 12 FCC Rcd at 9029-30, para. 481 (in addition to price, prior experience, past performance, personnel qualifications, technical excellence, and management capabilities are factors that form a "reasonable basis" for evaluating whether an offer is cost-effective).

As an illustration of an acceptable procurement process, the Commission specifically cited the Federal best value methodology in its Universal Services Order:

> When it specifically addressed this issue in the context of Internet access, the Joint Board only recommended that the Commission require schools and libraries to select the most cost-effective supplier of access. By way of example, we also note that the *federal procurement regulations* (which are inapplicable here) specify that in addition to price, federal contract administrators may take into account factors including the following: prior experience, including past performance; personnel qualifications,

> including technical excellence; management capability, including schedule compliance; and environmental objectives. We find that these factors form a reasonable basis on which to evaluate whether an offering is cost-effective.

Id. (citing FAR § 15.605(b)). The FAR provision cited by the Commission is currently codified at FAR § 15.304(c), which identifies the factors, including price, that are considered in a best value procurement. At the time the Universal Service Order was published, FAR § 15.605(d) (now FAR § 15.304(e), discussed *supra*) specifically contemplated solicitations in which nonprice factors are "significantly more important" that price.

The FCC further expanded on the principle of cost-effectiveness in its Tennessee Order. In that case, the Commission upheld an SLD decision granting funding for Internet access services provided by ENA, even though ENA's bid assertedly was twenty million dollars higher than the bid submitted by the protesting party, ISIS 2000.[10] The Tennessee Department of Education awarded the contract to ENA based on a finding of superior technical merit, using an RFP that afforded technological considerations more weight than cost,[11] required cost to be considered only after evaluation of non-cost factors,[12] and permitted additional negotiation with a vendor after its initial selection by the state.[13] In accordance with Tennessee procurement law, ISIS 2000 protested that award before a special review board, which affirmed the award to ENA.

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[10] ENA denied that its bid was higher, and the Tennessee Department of Education found that ISIS 2000's cost proposal was not reliable and in fact may have been far higher than ENA's proposal. The Commission noted those facts, but declined to rely on them in making its decision. Tennessee Order, 14 FCC Rcd at 13741, para. 14 n.33.

[11] The RFP provided for a maximum of 45 points for technological approach, 30 points for cost, 15 points for proposer experience, and 10 points for proposer qualifications. *See* Tennessee RFP, § 6.1, attached to Opposition of Educations Networks of America, CC Docket Nos. 96-45, 97-21, Application No., 18132, filed April 13, 1999.

[12] Tennessee Order, 14 FCC Rcd at 13738, para. 8 n.22.

[13] Tennessee RFP, note 11, *supra*, at para. 6.3.5.

It then appealed the SLD's funding decision to the FCC, which likewise found in favor of the State of Tennessee and ENA. Tennessee Order, 14 FCC Rcd at 13736-37, para. 4.

The Commission expressly approved the weighting system used by the Tennessee Department of Education. Citing the portion of the RFP that established the point values for cost and technical approach, the Commission stated that "Tennessee's request for bids indicated that the contract would be awarded to the most cost effective bidder" and declared that "the procurement process at issue here did consider price as a 'primary factor,' and required selection of the most cost-effective bid." *Id.* at 13740 para. 11. Specifically, the Commission concluded that the "primary factor" test was met by Tennessee procurement regulations, which required only that cost be evaluated and considered "to the greatest practicable extent" and the contract awarded to the most "cost-effective" bidder. *Id.*

In this regard, the Commission explained that its statement (in the Universal Service Order) that "price should be the primary factor [does not] mean that price should be the initial determining factor considered to the exclusion of all other factors." *Id.* at 13738, para. 8. Indeed, the Commission warned that "[i]nterpreting the Commission's competitive bid rules as requiring schools to select the lowest bid with little regard for the quality of the services necessary to achieve technology goals would obviate the 'maximum flexibility' the Commission expressly afforded schools." *Id.*

To provide further guidance to schools, bidders, and the SLD, the Commission then emphasized that state and local officials have every incentive to select the most cost-effective alternative and that their decisions should be presumed to comply with the Commission's rules. First, the Commission recognized that a school district has a powerful incentive to select the

most cost-effective bid, even if it has no competitive procurement requirements, since it is required to pay a portion of the cost of the funded products and services:

> [E]ven in those instances when schools do not have established competitive bid procurement processes, the Administrator generally need not make a separate finding that a school has selected *the most cost-effective bid*. Such a finding is not generally necessary because a school has an *incentive to select the most cost-effective bid*, even apart from any procurement requirements, because it must pay its pro rata share of the cost of the services requested.

Id. at 13739, para. 10 (emphasis added).

If anything, the Tennessee Order's reference to a school's obligation to pay a *pro rata* portion of the eligible services understates the true magnitude of those incentives. Even more significant than the school's *pro rata* share of eligible service costs is the school's sole responsibility to pay the full cost of the ineligible products and services that it is required to purchase in order to obtain funding for the eligible products (*e.g.*, personal computers, associated furniture, curricular software, electrical upgrades, etc.). As in the case of Ysleta, a school district's bill for associated ineligible services and products can reach into the millions of dollars[14] and can be nearly the same amount sought for eligible products and services. This co-payment obligation creates strong incentives, particularly in poorer districts, for schools to choose the most cost-effective vendor.

Second, and more fundamentally, the Tennessee Order explained that SLD "can generally rely on local and/or state procurement processes that include a competitive bid requirement as a means to ensure compliance with our competitive bid requirements":

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[14] Ysleta's obligation for associated ineligible services is approximately $15.7 million.

> [S]uch rules and practices will generally consider price to be a 'primary factor' . . . and select the most cost-effective bid. . . . *Absent evidence to the contrary in a particular case, we believe that this incentive [to select the most cost-effective bid] is generally sufficient to support a conclusion that a school has selected the most cost-effective bid* for the requested services."

Id. (emphasis added).

Accordingly, where state procurement law includes a competitive bid requirement, the Tennessee Order prohibits the SLD from second-guessing state and local procurement decisions as to the cost-effectiveness of awards "absent evidence to the contrary."[15] As we explain below, there is no such evidence. The procurement was conducted in accordance with Texas law and no one, including IBM's competitors, has challenged the conduct of the procurement or the award to IBM.

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[15] In fact, the Commission stressed in the Tennessee Order that the SLD's evaluation of cost should not conflict with state and local procurement laws, noting the Commission's competitive bid requirements "are not intended to preempt such state or local requirements." Tennessee Order, 14 FCC Rcd at 13738, para. 8 n.22 (citing 47 C.F.R. § 54.504(a)).

V.
CONCLUSION

WRF has reviewed SLD's Further Explanation and the documentary record of Ysleta's procurement and has found no "evidence to the contrary" that would deny the Ysleta award the presumption of cost-effectiveness identified in the Tennessee Order. The Commission has given state and local officials great flexibility in identifying and selecting the most cost-effective proposal for the provision of services supported by e-rate funding. As discussed above, the process followed by Ysleta has been tailored by the Texas legislature to ensure that Texans receive the best value for their taxpayer dollars. Moreover, Texas's procurement regime is grounded in core principles of Federal procurement law, which would bind the FCC if it were procuring similar services, and is reflected in the MPC, which forms the basis of many state procurement regimes.

For the following reasons, therefore, WRF concludes that Ysleta properly selected IBM as the most cost-effective vendor to act as its Systems Integrator:

First, Ysleta complied fully with Texas state procurement law**.** Texas school districts, including Ysleta, are required by statute to award contracts to the proposal that "provides the *best value* for the district." TEX. EDUC. CODE § 44.031 (emphasis added). As discussed above, one procurement method recognized as ensuring that "best value" is obtained for the Texas taxpayers is the utilization of a request for proposals. *Id.* § 44.031(a)(3). Texas also expressly provides school districts discretion to use a two-step method for the acquisition of certain technical and engineering services. TEX. EDUC. CODE § 44.031(f). Here, Ysleta's RFP contemplated the use of a two-phased procurement modeled on the procedures required for professional and

engineering services. The Texas legislature, the MPC, and Federal Procurement law all recognize this method as ensuring the cost-effective allocation of scarce taxpayer dollars.

Second, As the Tennessee Order recognized, Ysleta had a strong incentive to select the most cost-effective bid. Ysleta's obligation for associated ineligible services is approximately $15.7 million. Moreover, even with 90% funding from SLD for eligible services, Ysleta still would have to supply $2.2 million[16] of its own money, a considerable sum by any measure for a local school district.

Third, Ysleta is a sophisticated purchaser and carefully evaluated the qualifications of each of the vendors that responded to the RFP. Ysleta studied the costs of similar projects approved by SLD, including the El Paso Independent School District, independently researched current market prices for goods and services described in its Technology Plan, and prepared cost estimates for those goods and services. Moreover, after tentatively selecting IBM, Ysleta scrutinized IBM's cost proposal in light of its own independent research (including discussions with, and pricing information from, other vendors), comparisons with services and prices of comparable school districts, and the considerable experience of its in-house IT procurement experts. During negotiations with IBM, Ysleta obtained substantial reductions in price, totaling millions of dollars and negotiated the inclusion in the Contract of risk-shifting clauses, such as the "Procurement of Products" clause, permitting Ysleta to direct IBM to procure specified products from third-party vendors who can provide them more cost-effectively than IBM.

Fourth, no other vendor protested either Ysleta's solicitation or the award to IBM, as they had every right to do under Texas law. *See supra* Section IV.A.4.

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[16] Request for Review at 34.

Fundamentally, SLD confused value with price when it denied funding to Ysleta. Both the Texas and Federal procurement regimes properly emphasize price as a primary factor in any selection decision. Nevertheless, these regimes recognize the reality that price does not exist in a vacuum and cannot be properly evaluated without consideration of qualitative differences in the service and products offered for acquisition. Accordingly, Texas and Federal law direct government purchasers to focuses on value, *i.e.*, what prices will actually mean in terms of meeting the government's various needs for products and services. The result is a procurement system that provides the products and services to meet the government's needs at the lowest overall cost.