

STATE OF SOUTH CAROLINA)	BEFORE THE SOUTH CAROLINA
)	PROCUREMENT REVIEW PANEL
COUNTY OF RICHLAND)	
)	
IN RE:)	ORDER
)	(REVISED)
S.C. Patients' Compensation Fund)	
)	
v.)	
)	
Modus21, LLC)	Case No. 2013-5
)	
(Contract Controversy))	

On June 4, 2014, the South Carolina Patients' Compensation Fund (the PCF) filed a Motion for Reconsideration asking the Panel to reconsider its May 6, 2014 order regarding the contract controversy between it and Modus21, LLC. The PCF asked the Panel to reconsider its ruling regarding the application of Regulation 19-445.2015 to contract controversies and various factual findings. On June 5, 2014, the Chief Procurement Officer (the CPO) filed a separate Motion to Reconsider, asking the Panel to reverse its decision regarding the application of Regulation 19-445.2015 to the dispute before it. By letter dated June 17, 2014, the Panel advised the parties that it would entertain written legal memoranda on the issue of the application of Regulation 19-445.2015 to contract controversies, but that it would not revisit the factual findings complained of by the PCF. In addition, the Panel indicated that it would consider written arguments regarding "bad faith" as an element under Regulation 19-445.2015(D). After receiving and considering the written briefs of the parties, the Panel now withdraws its original order, dated May 6, 2014, and substitutes this one in its place.

This matter is before the South Carolina Procurement Review Panel (the Panel) for further administrative review pursuant to sections 11-35-4230(6) and 11-35-4410(1)(a) of the Consolidated Procurement Code (the Procurement Code). The South Carolina Patients'

Compensation Fund (the PCF) and Modus21, LLC (Modus21) have each appealed the May 9, 2013, decision by the Chief Procurement Officer (the CPO) for the Information Technology Management Office (ITMO). This case involves numerous disputes concerning the contract between the PCF and Modus21 for the replacement of the aging computer database the PCF used to run its insurance business with a new Member Management System (MMS). To aid its review, the Panel conducted a three-day hearing from December 3 through December 5, 2013. Helen F. Hiser, Esquire, and Tommy E. Lydon, Esquire, represented the PCF at that hearing. Robert D. Fogel, Esquire, represented Modus21, and William Dixon Robertson, III, Esquire, represented the CPO.

Taking into account and considering all of the testimony, the demeanor and the credibility of the witnesses; all of the evidence, stipulations, pleadings, and documents submitted by the parties; and all of the memoranda and argument submitted by the parties' counsel, the Panel hereby submits this ORDER.

Findings of Fact

I. State Term Contract for Third-Party Consulting

The contract between the PCF and Modus21 has its origins in a solicitation issued by ITMO on August 18, 2006. Record at PRP2566 – PRP2586 (Request for Proposal (RFP), Solicitation 07-S7276). Through this solicitation, ITMO sought to procure independent third party consulting services to review and develop an improvement process for governmental entities. Record at PRP2568. The Scope of Work section of the RFP provided the following overview of the services desired:

It is the intent of the State of South Carolina to solicit a Solutions-based State Term Contract(s) to allow governmental entities the ability to seek the assistance of an independent third party to better understand their current value and to develop an improvement process. This process should include financial

management, operational management, and knowledge management. The objective of this engagement will be to answer the following key questions:

1. Where does the agency stand versus similar organizations in terms of cost efficiency, staffing, and productivity?
2. How mature are the agencies [sic] key operational processes, and how do they impact the agencies [sic] cost, efficiency, and effectiveness?
3. What specific steps should the agency take to modernize the agencies [sic] portfolio, improve process maturity, and further reduce costs?
4. What specific steps should the agency take to transfer knowledge due to the high rate of retirement?

Record at PRP2575. Offerors were required to submit a Business Plan that included a “not to exceed price per hour” rate for each consultant type. *Id.* They were also asked to submit a Technical Proposal, and the RFP provided the following guidance:

Provide a Statement of Work to show the process that you will follow in assessment, analysis and reporting. This will be broad in nature considering the number of agencies under the State of South Carolina. This should include a description of the work to be accomplished and the format in which the information will be delivered. The measurement information and the assessment of both processes and services should provide a baseline for the current state of the agency and provide information to the agency for their accountability reporting. The recommendations should provide the insight the agency needs in improving services, reducing cost and developing processes for implementation.

Record at PRP2576.

Although the original RFP included a request for offerors to describe their “application development methodologies,” Record at PRP2574 (Part II, Section 3.1.3), this request was removed by the State in Amendment 1. Record at PRP2588 – PRP2589. Moreover, the RFP contained provisions limiting the scope of any contract resulting from this solicitation:

CONTRACT LIMITATIONS (JANUARY 2006): No sales may be made pursuant to this contract for any item or service that is not expressly listed. No sales may be made pursuant to this contract after expiration of this contract. Violation of this provision may result in termination of this contract and may subject contractor to suspension or debarment.

Record at PRP2581.

STATEWIDE TERM CONTRACT – SCOPE (JANUARY 2006): The scope of this contract is limited by the Bidding Schedule / Cost Proposals and by the description included in Part I, Scope of Solicitation. Sales of supplies or services not within the scope of this contract are prohibited. See clause entitled Contract Limitations.

Record at PRP2584. Thus, the RFP neither requested nor authorized software application development (i.e., writing custom software code).

The State awarded to multiple vendors, including Modus21. On December 5, 2006, Modus21 returned an executed “Master Agreement” to Shirley Coyner, the ITMO Procurement Manager conducting the solicitation.¹ Record at PRP118 – PRP130. One clause of the Master Agreement notes “This Master Agreement, together with all subordinate and other documents incorporated by reference herein, will constitute the entire agreement between the parties with respect to the subject matter herein.” Record at PRP128 (“Whole Agreement,” ¶ 25). In addition to the Master Agreement document, the documents “incorporated by reference” include statements of work, the RFP and amendments, and Modus21’s proposal. Record at PRP126 (“Order of Precedence,” ¶ 11). Moreover, Paragraph 11 provides:

[T]he terms and conditions in this Master Agreement supersede and replace the terms and conditions in the RFP and the amendments thereto. In the event of any conflicts between the Master Agreement or [sic] the items above listed, or between the items listed above themselves, the order of priority is that the Master Agreement, exclusive of the items listed above, shall take precedence over the items listed and the items listed shall thereafter take precedence over each other so that the earlier listed item would take precedence over the later listed item.

Id.

¹ In his order, the CPO found that this agreement had been prepared by Modus21 and that the procurement officer “took the extraordinary and irregular measure of executing” it. Record at PRP7. However, counsel for the CPO stipulated at the beginning of the Panel hearing that this finding had been in error. Indeed, the record before the Panel reflects that Ms. Coyner sent the Master Agreement to Modus21 for execution on November 30, 2006. Record at PRPAppendix, pages 2 – 13. Ms. Coyner’s accompanying e-mail notes that “[t]he State created a master agreement for vendors.” *Id.* at 2.

Under the terms of the Master Agreement, Modus21 was responsible for providing consulting services “on a . . . ‘not to exceed’ hourly rate basis during the term of this Master Agreement, with such method to be agreed upon in each Statement of Work (“SOW”).” Record at PRP120 (“Responsibilities of Contractor,” ¶ 2.1). For its part, the State agreed to cooperate with Modus21 by

providing [Modus21] with working space, equipment and facilities and timely access to data, information, and personnel of the State, and allow [Modus21] and the State to work productively as outlined in the SOW or project plan. The State shall be responsible for the performance of its personnel and agents and for the accuracy and completeness of all data and information provided to [Modus21] for purposes of the performance of the Services. The State acknowledges and agrees that [Modus21’s] timely performance is dependent on the State’s timely and effective satisfaction, using experienced and qualified personnel, of the State’s responsibilities under this Agreement and timely decisions and approvals of the State in connection with the Services. The failure of the State timely to meet any obligation that causes an adverse impact on [Modus21], including but not limited to a delay in the schedule or other event that requires an increase in resources by [Modus21], shall entitle [Modus21] to a change order that eliminates such adverse impact. Such change order shall be presented in accordance with Paragraph 26 of this Master Agreement, and approval of such change order shall not be unreasonably withheld. [Modus21] will promptly inform the State of any such failure that [Modus21] believes will cause any material delay, in order that the State may attempt to remedy such failure. [Modus21] shall inform the State’s Program Manager in writing of such failure (e.g. status report), describing such issues in reasonable detail to the State in order to allow the State an opportunity to minimize, or eliminate if possible, such adverse impact.

Id. (“Responsibilities of Contractor,” ¶ 2.2). Statements of Work (SOWs) were to be “developed, negotiated and mutually agreed to by the parties.” Record at PRP121 (“Statements of Work,” ¶ 4).

The Master Agreement also addressed the acceptance or rejection of deliverables in Article 5, which provided in pertinent part:

5.1 All deliverables prepared by [Modus21] must be approved in writing by the State’s Program Manager or his or her written designee that such Deliverables

comply in all material respects with the requirements of the applicable SOW, which approval shall not be unreasonably withheld.

5.2 To the extent not otherwise identified in a SOW, the State shall complete its review of a Deliverable in not more than ten (10) business days. The State shall provide [Modus21] (i) with approval of the Deliverable or (ii) with a written statement, as provided below, of the deficiencies preventing approval. Such business days shall be counted from and include the first business day following the delivery of the Deliverable to the State.

Record at PRP121.

The Master Agreement also contained provisions addressing each party's liability for damages:

10.1 [Modus21] will not be liable for any damages to the State resulting from the loss of data or use, lost profits or any incidental, consequential, or punitive damages unless said damages are the result of willful misconduct for which [Modus21] is adjudged responsible by the appropriate tribunal of competent jurisdiction. [Modus21] may be liable for personal injury or property damage caused by negligence or intentional harm for which [Modus21] is adjudged responsible by the appropriate tribunal of competent jurisdiction. However, [Modus21] retains all statutory and common law defenses as provided by South Carolina law.

10.2 The State shall not be liable for any damages to [Modus21] resulting from the loss of data or use, lost profits or any incidental, consequential, or punitive damages unless said damages are the result of willful misconduct for which the State is adjudged responsible by the appropriate tribunal of competent jurisdiction. The State may be liable for personal injury or property damage caused by negligence or intentional harm for which the State is adjudged responsible by the appropriate tribunal of competent jurisdiction, to the extent provided by law. However, the State retains all statutory, constitutional and common law defenses as provided by South Carolina law.

Record at PRP125.

II. Stipulated Facts

In accordance with the Consent Scheduling Order issued by the Panel on August 21, 2013, the parties agreed to certain factual stipulations, which are hereby adopted by the Panel and reproduced verbatim below:

1. The South Carolina Patients' Compensation Fund ("PCF") is a state agency, created "for the purpose of paying that portion of a medical malpractice or general liability claim, settlement, or judgment which is in excess of two hundred thousand dollars for each incident or in excess six hundred thousand dollars in the aggregate for one year, up to the amounts specified by the board pursuant to Section 38-79-430. The fund is liable only for payment of claims against licensed health care providers (providers) in compliance with the provisions of this article and includes reasonable and necessary expenses incurred in payment of claims and the fund's administrative expense." S.C. Code Ann. § 38-79-420.
2. The PCF operates essentially as an insurance company that provides excess medical malpractice liability coverage to participating health care providers.
3. A thirteen-member Board of Governors exercises authority over the PCF's operations, underwriting, and claims handling.
4. The PCF's day-to-day operations are managed by its executive director. Terry Coston has held the position since 2004.
5. During all relevant times hereto, the PCF staff included Ms. Coston and four others, Youlanda McKnight (who replaced Deanna Frederick), Leigh Brazell, Akhia Harvey, and Diane Carraway.
6. Prior to 2008, the PCF managed its membership, billing and claims through an Access-based database, referred to as the Legacy system.
7. Modus21 is a South Carolina corporation with its principal place of business in Mount Pleasant, South Carolina.
8. Modus21 holds itself out as an expert in the fields of system analysis and business process improvement. (CPO Dec[ision] p. 12 [PRP14]).
9. Peter Woodhull is Modus21's President and co-founder.
10. On August 18, 2006, the South Carolina Information Technology Management Office ("ITMO") issued Solicitation No. 07-S7276, which was a Request for Proposals ("RFP") for independent third party consulting services to review and develop an improvement process for State governmental entities.
11. The RFP included the following contract limitation: "No sales may be made pursuant to this contract for any item or service that is not expressly listed. No sales may be made pursuant to this contract after expiration of this contract. Violation of this provision may result in termination of this contract and may subject contractor to suspension or debarment." (PRP2581).

12. The RFP also provided that “Sales of supplies or services not within the scope of this contract are prohibited.” (PRP2584).
13. In its response to the RFP, Modus21 acknowledged that “although no application development is called for in this program, configuration management of the documents and process models is important.” (PRP2600).
14. The State awarded multiple contractors under the RFP, including Modus21.
15. The PCF first contacted Modus21 in February 2008 regarding changes to their current database and corresponding program. (PRP45).
16. In May 2008, Modus21 delivered its Process Centric Proposal to the PCF. In that document, Modus21 identified the problems with the PCF’s Legacy system as, “outdated and the service levels required to keep up with required changes is not adequate. Second, the reporting capabilities have become compromised and unable to deliver necessary information. Finally, the system is not technologically viable to [sic] for needed expansion.” (PRP81).
17. In its Process Centric Proposal, as part of the Deployment phase, Modus21 proposed to “deliver, install, and configure the new system for implementation.” The initial processes to be addressed included Membership Management, Claims Management, Underwriting & Rating, Billing & Payments, Financial, Renewals, Endorsement Process, and Settlement Process. The estimated cost for the project was \$191,044.00. (PRP85-87).
18. Modus21 provided the PCF with a Project Executive Summary dated June 1[3], 2008 that defined the scope of the project to include:

the development and implementation of a new, comprehensive Membership Management System (MMS) based upon a BPM,² process

² BPM is an acronym for Business Process Management, which Modus21’s Process Centric Proposal describes as “a collaborative approach to managing an organization’s core processes. . . . BPM software provides an open, standards-based framework that can be used to integrate external applications or application components.” Record at PRP91. For ease of reference, this order uses “MMS” to mean the BPM system Modus21 was to develop and implement for the PCF.

In his order, the CPO noted the following about a BPM system (BPMS):

A BPMS is a software based system that allows a business to define its workflow or processes in a graphical manner and the BPMS will fill in all the steps of the process in the order necessary to process the work. The BPMS software actually generates software code “behind” its interface, and the code integrates the business process models into the computerized workflow. This does require someone to define all the necessary processes with all the pertinent steps and someone with the skill set to input all that information into the BPMS. Theoretically, when used in an appropriate case, BPMS does not require manually written software coding.

Record at PRP8. Neither party challenged this particular observation in their appeal letters. The Panel hereby adopts it because it is helpful to understanding the difference between tailored configuration in a BPMS which, in a

centric solution. The new Membership Management System needs to provide numerous key functions for the PCF, including Policy Management, Claims Management, Underwriting and Rating, Financial Management (Billing and Payment Posting), Risk Management, Advanced Workflow, and Data Storage. In addition the new system will need to provide Joint Underwriting Associates [sic] (JUA) connectivity, web interaction, real time reporting capabilities, audit capabilities and document processing.

Moreover, the project scope includes the delivery, installation, set up, testing and deployment of the new system. The necessary training of end users required for successful implementation is also considered in the scope of the project. Finally, the project shall also include the transfer and migration of data from the current MTS to the new Membership Management System (MMS).

The scope of the project and priority of any additional requests or future phases outside of the above stated scope will be managed jointly by the PCF and Modus21 throughout the project lifecycle. Any and all requested changes will be handled via the Change Management process utilized by Modus21 and are subject to review and approval by both parties.

Both Terry Coston and Peter Woodhull signed the Project Executive Summary. (PRP108-109).

19. Modus21 delivered an MMS Process Specification to the PCF dated December 10, 2008. (PRP193-300). This Process Specification was signed by both Terry Coston and Peter Woodhull. (PRP300).
20. Modus21 delivered an MMS Product Specification to the PCF on February 20, 2012. (PRP301-352). The Product Specification is unsigned.

See Stipulations filed with the Panel on November 1, 2013.

III. Facts Related to Contract Performance

A. The PCF's Need for a New System and the Executive Summary

sense, generates its own software coding, and custom software coding, which is the manual writing of software code to create a particular solution. The Master Agreement between the State and Modus21 prohibits the latter, but not the former. As became abundantly clear in the testimony presented to the Panel, Modus21 understood it was offering a BPMS system which it would configure to automate the PCF's business processes. However, the PCF never completely grasped this distinction and believed it would be getting a custom solution.

Terry Coston, the PCF's Executive Director, testified at the Panel's hearing. She explained that the PCF's Legacy system, its ten-year-old Access database, was having increasing problems with runtime errors and systems lock up as the PCF added new users to the system. (Panel Tr. 63). She testified that the PCF "needed some kind of system to accommodate not only the size of our data but the functions that we provided with underwriting and membership services and claims and then accurate reporting, because the [A]ccess tables didn't give realtime reporting." (Panel Tr. 63:13 – 18). Ms. Coston explained that they initially approached ITMO about issuing a Request for Proposals (RFP), but that they learned that ITMO had "a list of companies that could meet our needs."³ (Panel Tr. 64:17 – 20). After learning about this list, the PCF contacted three or four of those companies for bids on a new system with the desired components. (Panel Tr. 64:20 – 65:1). The record before the Panel reflects that Modus21 first met with the PCF in late February of 2008 and submitted a plan to improve the PCF's business and technological processes in March. Record at PRP46; PRP50 – PRP55. Ms. Coston testified that Modus21 submitted the low bid⁴ and was "hired to build the membership management system" with the approval of the PCF Board. (Panel Tr. 65:1 – 5). Ms. Coston testified that the PCF wanted Modus21 to provide "a functioning system that would complete all of our processes and do realtime reporting." (Panel Tr. 65:13 – 15). Ms. Coston further explained that "I didn't know whether we were getting custom computer software or what. I just was – understood that

³ The "list" to which Ms. Coston refers appears to be the companies awarded under the ITMO state term contract discussed above. In his opening statement, counsel for the CPO emphasized that state term contracts are "a compromise between convenience and competition" and noted that large agencies with dedicated IT staff and project managers as well as small agencies lacking such "in-house" expertise are both able to procure needed goods and services through such contracts. (Panel Tr. 53 – 54) The Panel recognizes that state term contracts provide needed flexibility. However, the Panel is concerned that small agencies – especially those lacking not only IT staff but also procurement officers – will quickly find themselves out of their depth, particularly when purchasing software and IT consulting services. The Panel urges ITMO to consider steps it could take to limit the use of such contracts by small agencies, to limit the total amount they are authorized to purchase under such contracts, and to provide them with more "hands on" guidance and oversight when making purchases under such contracts.

⁴ Presumably, this low bid was the "Process Centric Proposal" Modus21 presented to the PCF in May 2008.

we would get a system like we had except better.” (Panel Tr. 105:22 – 25). She later admitted that she thought the PCF would be getting a computer program “designed and made” for the PCF. (Panel Tr. 106:15 – 17).

Although Ms. Coston acknowledged signing the Executive Summary, she testified that she “[did not] believe” she received a copy of the Master Agreement from ITMO prior to asking for bids. (Panel Tr. 108:11 – 12). Ms. Coston further testified that she did not understand until later in the project that Modus21 was only performing consulting services and that she would not have hired Modus21 if she had understood that. (Panel Tr. 76).

The Executive Summary signed by both parties provided that Ms. Coston would serve as Project Manager on behalf of the PCF. Record at PRP110. Ms. Coston testified that while she did not have experience managing this type of project (Panel Tr. 104), she felt comfortable performing the project manager duties as she understood them: “[to] oversee what was going on, attend the check-ins, work with the staff and work with Modus to complete, to push the project to completion.” (Panel Tr. 105:10 – 13). Ms. Coston also stated that Modus21 did not tell her at the beginning of the project that the PCF needed to have a software consultant in place. (Panel Tr. 78:23 – 79:1). In any event, she also explained that the PCF did not have access to a software consultant at the beginning of the project and thought that Modus21 would provide the project manager. (Panel Tr. 79).

B. Statement of Work 001

Work on the MMS began in June of 2008 under Statement of Work 001 (SOW 001), which both parties signed. Record at PRP131 – PRP134. SOW 001 described consulting services for the planning and analysis phases of the MMS project and covered the time period of June 1, 2008 through August 1, 2008. Record at PRP131 – PRP132. The stated goal of this

statement of work was “to assess project needs around process, architecture, and to further define scope for the replacement of the current system.” Record at PRP131. The “representative list of deliverables” for this SOW included the project plan, process analysis, and architecture feedback. Record at PRP131. Modus21 estimated that this portion of the work would require 160 hours at a cost of \$18,270.00. Record at PRP132.

Shannon Laughlin acted as Modus21’s analysis and project manager on the MMS for the PCF. Ms. Laughlin explained during the Panel hearing that her role as an analyst involved all five phases of Modus21’s methodology, but did not involve the development of software or the writing of software code. (Panel Tr. 297 – 298). In addition, as project manager, Ms. Laughlin testified that she was responsible for the project’s planning, schedule, budget and time lines; the weekly status reports; and the change management process. (Panel Tr. 298 – 299). Ms. Laughlin was primarily responsible for the work performed under SOW 001, which included capturing the PCF’s business requirements so that they could be modeled as discrete processes in the specification document. (Panel Tr. 297 – 298; 305).

Ms. Laughlin’s starting point for capturing the PCF’s business requirements was reviewing the PCF’s business rules set forth in its manual. (Panel Tr. 310). In addition, Ms. Laughlin spent time with each of the PCF’s staff members, or “subject matter experts,” to ask a series of elicitation questions designed to help her understand each person’s role within the PCF and how that role interacted with those of other staff members and with “business rules or integration points.” (Panel Tr. 311). She explained, “They’re helping me understand, you know, if there are ten steps in that process or 20 steps in that process. They’re helping me understand what occurs in what order.” (Panel Tr. 311). Ms. Laughlin then used the information she

gathered to develop process models, which were used in turn to develop the specification document. (Panel Tr. 313).

Ms. Coston testified before the Panel that she thought Modus21 performed satisfactorily under SOW 001, and that Ms. Laughlin “did a really good job with interviewing the staff.” (Panel Tr. 82). In addition to conducting interviews during this time frame, Ms. Laughlin prepared the Executive Summary (discussed in the parties’ stipulated facts at pages 8 – 9) and delivered it to the PCF on June 13, 2008. Record at PRP104 – PRP114. The abbreviated schedule in the Executive Summary indicated that deployment of the MMS would be completed by February 10, 2009. Record at PRP11. Ms. Coston indicated the PCF’s acceptance of the Executive Summary by signing it on June 17, 2008. Record at PRP107.

The record before the Panel and the testimony during the Panel’s hearing do not indicate that the PCF expressed any dissatisfaction with the deliverables under SOW 001. Moreover, the record before the Panel does not contain written rejection of any deliverable under SOW 001 during the performance period. Modus21 billed the PCF for the full amount of SOW 001, and the PCF paid Modus21 for that work.⁵

C. Statement of Work 002 and Addenda 001 and 002

The parties executed Statement of Work 002 (SOW 002) on June 23, 2008, prior to the completion of SOW 001. Record at PRP138. SOW 002 contemplates the MMS’s delivery,

⁵ The planning and analysis phases of the project apparently also included Modus21’s evaluation of various BPMS tools and vendors, and the PCF selected and purchased HandySoft’s BizFlow on August 7, 2008 at a cost of \$16,402. *See* Record at PRP1067 – PRP1083 (Client Vendor Evaluation Document, delivered to the PCF on June 25, 2008); PRP1096 – PRP1101 (HandySoft Software Licensing Agreement, signed by Ms. Coston). The Panel notes that this purchase exceeds \$10,000 and thus falls under section 11-35-1550(2)(c) of the Procurement Code. Because the PCF neither advertised nor sought competing bids for BizFlow, the PCF did not comply with the Procurement Code in making this purchase. The Panel is deeply concerned that this case represents a worst-case scenario for a small agency making significant purchases without the benefit of staff trained in state procurement rules, especially since this is not the only instance the PCF failed to comply with the Procurement Code in the course of this project. The Panel urges Procurement Services to consider how it might identify state agencies lacking dedicated procurement officers and provide them with at least minimal instruction on the Procurement Code in an effort to prevent future non-compliance.

installation, set up, and training of the PCF's staff during the time period of June 23, 2008 through March 1, 2009. Record at PRP135. Modus21 estimated it could perform these tasks in 1568 hours at a cost of \$191,044. Record at PRP136. The task description identified the following processes: "policy management, claims management, financial management, risk management, advanced workflow, data storage, risk analysis, document processing, and web interaction." Record at PRP135. This SOW included the following "representative list of deliverables," which would "be delivered to the customer during the project as they are completed":

- Project plan
- Process Specifications
- Architecture
- Weekly status reports of Modus21 project work
- Approved Functional Process Model(s) – Initial Operational Capability (IOC)
- System Architecture Document
- Revised Process Specification and Project Management Plan
- Implementation & Training Plan
- Training Guide(s)
- Transition Plan
- Project Closeout Report

Record at PRP135 – PRP136. Although SOW 002 noted that "[i]tems in this list are subject to change[] upon agreement of the parties," it clearly reflects the parties' expectation that the MMS project would be completed by March 1, 2009.

Peter Grazaitis is a senior software architect with Modus21 who began working as the technical lead and engineer on the MMS project in September of 2008. (Panel Tr. 424; 428; 433). Although Mr. Grazaitis is able to write custom software code, he testified that he does not usually do much of that because most of Modus21's projects "are business process management." (Panel Tr. 425). Mr. Grazaitis explained that a BPMS is "a tool that allows you to design and implement a business process and it leverages, they call it a palette, of different

icons” that “allows you to do integration of systems, web services, database interaction, as well as create front-end screens for people to enter data.” (Panel Tr. 424). He also testified that a BPMS does not come with predefined modules such as billing or correspondence, but that it gives you the ability to configure it to meet the customer’s needs. (Panel Tr. 428). For example, he explained that other COTS solutions, such as Google Maps or QuickBooks, could be leveraged into the overall design of a BPMS. (Panel Tr. 427). Mr. Grazaitis also stated that he did not consider using a BPMS’s palette to create screens to perform processes “in the same realm as writing a full blown application, but you could write some expressive language to achieve certain business rules and things like that.”⁶ (Panel Tr. 439).

In the fall of 2008, Mr. Grazaitis explained that he used the information gathered and entered into flow charts by Ms. Laughlin to create “the technical specification, the systems architect document, and also to implement what [Ms. Laughlin] captured in the specification, actually implement that in the tool itself.” (Panel Tr. 428). Once the PCF had chosen HandySoft’s BizFlow, Mr. Grazaitis began “actually configuring Hand[y]Soft based on the specifications, so taking that process flow and literally translating it by dropping the icons from this palette to produce an executable model.” (Panel Tr. 433). Mr. Grazaitis denied writing any custom code at this point in the project. (Panel Tr. 441).

The record before the Panel contains copies of several preliminary versions of the Process Specification and the System Requirements/System Architecture documents, which were prepared by Modus21 and delivered to the PCF for review. Record at PRP1113 – PRP1121; PRP1130 – PRP1234; PRP1245 – PRP1260. The Panel notes that these preliminary documents

⁶ This type of custom configuration prompted the CPO’s observation in his order that “the work described in SOW 002 was not what the solicitation intended to authorize.” Record at PRP11. However, as noted above at note 3, custom configuration was not expressly prohibited by the solicitation or the Master Agreement.

identified QuickBooks as an integration point for the new MMS.⁷ Record at PRP1120; PRP1146; PRP1252. In December 2008, Modus21 delivered the final versions of both the Process Specification and the System Requirements/System Architecture documents to the PCF, which included the QuickBooks integration as part of the intended architecture. Record at PRP177 – PRP300. These documents were signed and accepted by Ms. Coston in December 2008. Record at PRP182; PRP300. In addition, the record also contains a Converted Project Plan and numerous progress reports related to SOW 002. Record at PRP385 – PRP386; PRP486 – PRP522. The record before the Panel does not contain written rejection of any of these deliverables during the performance period of SOW 002. In addition, despite the MMS not going live as originally scheduled in late February of 2009, Modus21 billed the PCF in full for the work under SOW 002, and the PCF paid for that work by April 2, 2009.

Addendum 001 to SOW 002 extended the performance period through July 2009 at a cost of \$3,600. Record at PRP139. The extension added 120 hours for “changes within the scope of the project” related to reporting. *Id.* Addendum 002 further extended the performance period of SOW 002 through December 2009 at a cost of \$3,600. Record at PRP141. This addendum was also related to reporting. Although included in the Executive Summary, the Panel finds that SOW 002 did not specifically account for reporting functionality in its task description. Furthermore, the Panel finds that the PCF did not reject in writing any of the deliverables during these performance period extensions. Modus21 billed the PCF in full for these addenda, and the PCF paid for that work.

D. Fall of 2008 through March 2009

⁷ The significance of this will be addressed in Section D below.

Beginning in the late fall of 2008 and continuing through the end of SOW 002's performance period on March 1, 2009, Modus21 delivered pieces of the new MMS as they were completed to the PCF for testing. Indeed, Mr. Woodhull testified that Modus21 had installed the MMS's Initial Operating Capability on a server in the PCF's offices in February 2009. (Panel Tr. 567). Witnesses for both sides testified before the Panel that it was during this time frame that the project started to experience difficulties. Although Ms. Laughlin and Mr. Grazaitis testified that the MMS was on track to go live as scheduled in February 2009, Ms. Coston and Akhia Harvey, the PCF's billing coordinator, were troubled by the way the processes worked during testing. (Panel Tr. 110; 164). Another sticking point was Modus21's plan to use QuickBooks, which was already installed on Ms. Coston's computer, to perform accounting functions within the MMS.⁸ Ms. Coston testified that she used QuickBooks "to record money coming in and money going out," not to produce bills or post payments. (Panel Tr. 117). Sometime in December 2008 or January 2009, the PCF ultimately decided not to expand the use of QuickBooks in the manner proposed by Modus21. *See* Record at PRP409 (Modus21 January 7, 2009 customer check-in presentation referencing decision not to leverage QuickBooks); PRP984 (March 9, 2009 e-mail from Ms. Coston which acknowledges a "misunderstanding" with regard to QuickBooks). As a result of this decision, the parties agreed that Modus21 would develop a custom accounting system for the MMS.

E. Statement of Work 003

Although it was not signed by both parties until April 24, 2009, Statement of Work 003 (SOW 003) covers the performance period beginning March 19, 2009, through June 1, 2009.

⁸ The Panel received considerable testimony from both sides regarding the meanings of "accounting" and "billing and posting." This testimony clearly revealed that communication between Modus21 and the PCF staff left much to be desired and that there were instances of misunderstanding throughout the project. The Panel finds that both parties contributed to the confusion.

Record at PRP142 – PRP146. This statement of work estimates the need for an additional 968 hours of work at a cost of \$54,208.⁹ Record at PRP144. The task description in SOW 003 states that “Modus21 shall allocate resources to support the *development* and implementation of new requirements” in the MMS. Record at PRP142 (emphasis added). The components and processes listed under the task description include items related to claims and quoting.¹⁰ Record at PRP142. The deliverables under SOW 003 included updates to the project plan and process specification, weekly status reports, and Initial Operational Capability. Record at PRP143. Modus21 billed the PCF in full for this statement of work, and the PCF paid Modus21 for that work.

Mr. Grazaitis admitted during the Panel hearing that he began “a heavy amount of coding” during March and April of 2009, especially with regard to the accounting solution for the MMS. (Panel Tr. 446 – 449). All of the Modus21 employees who testified before the Panel understood that custom coding was not allowed under the state term contract. Mr. Woodhull, Modus21’s CEO, explained that Modus21 ultimately “wanted the project to be successful. We were trying to make the customer happy.” (Panel Tr. 575). Although Ms. Coston maintained that she did not understand that Modus21 could not write custom software code under the state term contract until much later, she confirmed that the PCF also desired project completion. (Panel Tr. 87 – 88). However, it was clear from her testimony and from e-mails in the record

⁹ This price reflects a discounted hourly rate for the services of Ms. Laughlin and Mr. Grazaitis in SOW 003, resulting in a savings to the PCF of \$50,664. See Record at PRP432 (Modus21 February 27, 2009, Update to the PCF Board); PRP985 (March 5, 2009 E-mail from Ms. Coston acknowledging discount); Record at PRP836 – PRP841 (Modus21 Invoices referencing discount for SOW 003).

¹⁰ Although the CPO expressed skepticism about these insurance related functions not being included in the scope of the prior statement of work, SOW 002, Ms. Coston acknowledged that the quoting system was a new process not included in the Legacy system and that the claims process represented an “update and upgrade” in an e-mail to PCF board members on March 5, 2009. Record at PRP985. This e-mail asked for authorization of the additional expenditure of \$54,208. Record at PRP984.

that she understood that Modus21 was proposing a custom solution by March 2009. Record at PRP984.

Because the task description in SOW 003 refers specifically to development and because Mr. Grazaitis admitted that the majority of his coding was done during the performance period of SOW 003, the Panel concludes that the work done on this statement of work was outside the scope of the state term contract. Nonetheless, the Panel also finds that both parties entered into SOW 003 out of a desire to make the project work – Modus21 wanted a positive reference from Ms. Coston and was willing to work at a discounted rate,¹¹ and Ms. Coston did not want to abandon the project for which the PCF had already invested a substantial sum.¹² Furthermore, the Panel finds that both parties were aware that custom coding was being performed, especially with regard to the accounting solution. The Panel declines to make a specific finding that the PCF threatened litigation during this period of time as alleged by Modus21 because the testimony before it was contradictory. However, the Panel does find that the PCF exerted pressure on Modus21 to modify the MMS from what was originally proposed to a system that would perform as anticipated by the PCF and include additional functionality.

F. Statement of Work 004 and Addendum 001

¹¹ Modus21 also contends that it provided approximately \$600,000 worth of work for which it did not bill the PCF. In support of its position, Modus21 introduced time sheets before the Panel through the testimony of Modus21's Chief Financial Officer, John Oliver. Record at PRP2314 – PRP2565. Although the time sheets themselves contain internal inconsistencies, the Panel finds that other contemporaneous documents in the record (e.g., invoices, e-mails and Modus21 presentations) substantiate Modus21's contention that the PCF was not billed for all of the work Modus21 actually performed.

¹² The Panel observes that testimony from both parties indicated regret that one side or the other did not end the engagement once it became apparent that the MMS originally proposed by Modus21 was not going to operate as the PCF expected. Termination at this point would have saved time, money, and frustration for all concerned, but unfortunately did not occur. Although the Master Agreement required vendors to report monthly usage to ITMO, the record before the Panel does not include those reports, and Modus21's Peter Woodhull admitted that Modus21 did not comply with this requirement throughout the entire project. (Panel Tr. 588) In order to prevent future occurrences, the Panel urges ITMO to consider more stringent oversight of time and materials contracts, perhaps requiring reporting from using agencies as well, particularly as the "not to exceed" limit is approached on a given statement of work.

Statement of Work 004 (SOW 004). covered a performance period of July 1, 2009, through December 31, 2009, at a cost of \$67,440. Record at PRP148 – PRP149. One of the deliverables for SOW 004 was “updated source code.” Record at PRP147. On December 16, 2009, Ms. Coston signed Addendum 001 to SOW 004 that extended the period of performance through May 31, 2010 for “the development of reports.” Record at PRP151. Addendum 001 carried an additional cost of \$6,085. *Id.* In its post-trial brief to the Panel, Modus21 has conceded that SOW 004 involved custom coding and was outside the scope of the state term contract. Post-Trial Brief of Modus21, LLC, dated January 13, 2014, at 10 – 11; 13. The PCF paid Modus21 in full for the work performed under SOW 004 and Addendum 001.

G. Statement of Work 005 and Addendum 001

The parties entered into Statement of Work 005 (SOW 005) on March 15, 2010, which obligated Modus21 to provide an estimated 240 hours of deployment and post-production support for the MMS during the performance period of April 1, 2010 through September 30, 2010. Record at PRP152. The estimated cost of SOW 005 was \$20,520. Record at PRP153. The deliverables for this statement of work were weekly progress reports. PRP152. The Panel finds that these progress reports detail primarily data migration and integration work which was within the scope of the state term contract. Record at PRP620 – PRP621. There is no evidence before the Panel that the PCF rejected any deliverables under SOW 005 during the performance period. Modus21 billed the PCF and was paid in full for the work under SOW 005.

The parties also executed Addendum 001 to SOW 005 on March 15, 2010, which called for the “development of reports” through an estimated 45 hours at a cost of \$2,785. Record at PRP156. The Panel finds that this development work was outside the scope of the state term contract. The PCF has paid Modus21 in full for the work under Addendum 001 to SOW 005.

G. Statement of Work 006

Statement of Work 006 (SOW 006) was signed by the PCF on July 20, 2010 to authorize additional post-production support of 480 hours at a cost of \$41,040 from July 1, 2010 through June 30, 2011. Record at PRP157. The deliverables were weekly status reports. *Id.* The Panel finds that these status reports detailed work related to data migration and integration work that was within the scope of the state term contract. Record at PRP622 – PRP652. There is no evidence before the Panel that the PCF rejected any of these deliverables in writing during the performance period. Modus21 billed for the work performed under SOW 006, and the PCF has paid in full for that work.

H. Statement of Work 007

Statement of Work 007 (SOW007) covered the performance period of January 1, 2011 through March 31, 2011 and was signed by Ms. Coston on January 18, 2011.¹³ Record at PRP161 – PRP164. SOW 007 called for 400 hours at a cost of \$41,040 for “migration preparation, deployment, and post-migration support” and involved the migration of data stored in the Legacy system’s Access database. Record at PRP161. The deliverables were weekly status reports which are included in the record before the Panel and which the Panel concludes were within the scope of the state term contract. Record at PRP653 – PRP680. There is no evidence before the Panel that the PCF rejected any of these deliverables during the performance period. Modus21 billed the PCF in full for the work under SOW 007, and the PCF has paid for that work.

I. Statements of Work 008, 009, and 010

¹³ The Panel notes that the performance periods for SOWs 005, 006, and 007 include some overlap. However, the issue of that overlap was not brought up in testimony before the Panel, and the record itself contains no explanation. Nonetheless, the Panel finds that the deliverables under these statements of work were within the scope of the state term contract and that the PCF indicated acceptance of the additional work by signing the SOWs.

Statement of Work 008 (SOW 008) was signed by Ms. Coston on December 6, 2011 for an unspecified amount of consulting hours during the performance period of December 1, 2011 through December 31, 2011. Record at PRP165. One of the deliverables under SOW 008 was “All source code generated or modified.” *Id.* Modus21 billed the PCF \$275.50 for this performance period. Record at PRP876. Statement of Work 009 (SOW 009) covered the performance period of January 1, 2012 through January 31, 2012 and also contained a reference to source code. Record at PRP169. Modus21 billed the PCF \$751.25 for this performance period. Record at PRP877. Similarly, Statement of Work 010 (SOW 010) covered the performance period of February 1, 2012 through February 29, 2012 and referenced source code as a deliverable. Record at PRP173. Modus21 billed the PCF \$12,225.75 for this performance period. Record at PRP878.

SOWs 008, 009, and 010 were all entered into during the time that the PCF had engaged Jeff Stanley, an IT consultant, in an effort to resolve the continuing issues the PCF was having with the MMS, which had finally gone live in April of 2011.¹⁴ All three SOWs openly refer to coding, and Modus21 has conceded, both in the hearing before the Panel and in its post-trial brief, that these SOWs exceeded the scope of the state term contract. Modus billed the PCF in the amounts listed above, and the PCF paid those amounts in full.

J. Mitigation Efforts

Ms. Coston testified that even after the MMS went live in April of 2011, the PCF staff was continuing to use the Legacy system to verify bill data and because they did not trust the MMS. (Panel Tr. 95). She also explained that “We never really got the full picture until the decision was made in April 2011 to go live. And at that point, we had the processes in place, but

¹⁴ Mr. Stanley’s engagement will be discussed more fully below.

they were riddled with stops that stopped the process from being complete.” (Panel Tr. 111). In July 2011, the PCF engaged the services of Jeff Stanley of J A Stanley and Associates to conduct an independent review of the project and make recommendations about getting the project back on track.¹⁵ Mr. Stanley testified before the Panel that when he began working with the PCF “there was general non-user acceptance due to inaccuracies of the system and project fatigue.” (Panel Tr. 254). Mr. Stanley worked with the PCF and Modus21 to try to resolve issues he compiled into a stop-work list during the late fall of 2011 and early winter of 2012. (Panel Tr. 264 – 265). Mr. Stanley testified that Modus21 made a good faith attempt to correct the issues identified in the stop-work list. (Panel Tr. 288). However, Mr. Stanley ultimately concluded that the MMS could not be fixed. Record at PRP718 – PRP724; (Panel Tr. 268). Contrary to the CPO’s finding in his order, the PCF seeks to recover from Modus21 the amounts paid to Mr. Stanley.

In November of 2011 the PCF contracted with Team IA, Inc., under a separate state term contract for electronic document management systems, or EDMS. Phil Hunt, a consultant with Team IA testified before the Panel that during the course of setting up the PCF’s document imaging system he had conversations with Mr. Stanley and PCF staff members about looking at some of the problems they were having with the MMS. (Panel Tr. 197). Mr. Hunt initially looked at helping the PCF with the reporting and calculation issues it was still experiencing with the MMS in January despite Modus21’s efforts on the stop-work list. (Panel Tr. 198 – 199).

¹⁵ The CPO found that Mr. Stanley’s final bill was \$16,325.12, but a copy of that bill does not appear to be included in the record before the Panel. Mr. Stanley confirmed in his testimony before the Panel that his bill for July 2011 through February 2012 was for just over \$16,000. Because the amount of Mr. Stanley’s services exceeded \$10,000, the PCF violated section 11-35-1550 of the Procurement Code because it failed to advertise or seek competitive bids. The PCF’s position that it did not anticipate that Mr. Stanley’s fees would exceed \$10,000 does not excuse this violation.

The PCF and Team IA ultimately entered into a SOW¹⁶ under the state term EDMS contract to fix the reporting issues in January 2011, and had billed the PCF \$17,226 through the end of March 2012.¹⁷ Record at PRP816 – PRP818. The PCF has not sought to recover this amount from Modus21.

Mr. Hunt testified that the MMS he observed in late 2011 and early 2012 is “essentially a custom written application that’s using a workflow tool for some parts of it.” (Panel Tr. 204 – 205). He also opined that he was “not in favor of the way BizFlow is implemented in this project.” (Panel Tr. 244). However, Mr. Hunt conceded that he was not in a position to evaluate the MMS as it existed in March 2009. (Panel Tr. 245 – 246). Mr. Hunt drafted a report evaluating the MMS in which he concluded that the MMS was unsalvageable.¹⁸ Record at PRP774 – PRP811.

Testimony from Mr. Hunt and Ms. Coston confirmed that the PCF and Team IA eventually entered another agreement under the state term EDMS contract whereby Team IA built and installed a third system, the Patients’ Compensation Fund Application (PCFA). (Panel Tr. 125 -126; 238). This system was a custom application for the PCF and cost over \$500,000. (Panel Tr. 126). The Panel finds that this custom application, which went live in October 2013, was outside the scope of the EDMS contract. Although Mr. Hunt denied using any of the MMS code to build the PCFA, he acknowledged that he did “dive very deep into the MMS data model

¹⁶ The record before the Panel does not contain a copy of this SOW.

¹⁷ The Panel notes that this work, which also involved custom coding, was outside the scope of the state term EDMS contract. It is also noted that this scope violation was one of the bases for which the PCF sought reimbursement in its March 28, 2012 letter.

¹⁸ Mr. Woodhull admitted that the MMS as it existed in 2012 when Mr. Hunt was evaluating it was a “Frankenstein.” (Panel Tr. 584). However, he emphasized that the 2012 MMS was vastly different from the system Modus21 installed in February 2009 which worked, but “we were asked to take it apart and put it back together in completely different ways that it was never intended to be.” (Panel Tr. 585). Both Mr. Woodhull and Mr. Grazaitis testified before the Panel that the PCF ultimately did not want a process based system such as the one they described in their original proposal. (Panel Tr. 460; 585).

for migration from the MMS data into the PCFA” to figure out “how we get out that system into the PCFA.” (Panel Tr. 237).

Modus21 delivered the final version of its Product Specification document to the PCF on February 29, 2012. Record at PRP301 – PRP352. This document was not signed by either party. The parties did not enter into any subsequent statements of work.¹⁹ On March 28, 2012, counsel for the PCF sent a letter to Modus21 indicating the PCF’s intention to terminate the MMS contract and demanding Modus21 “reimburse [the PCF] for the cost it incurs to repair and/or complete portions of the MMS that were part of the contract between them.” Record at PRP2114. Counsel also included a check in the amount of \$10,663.75 as payment for work billed under the final statement of work, SOW 010. *Id.* The PCF did not offer to return any deliverables it received during the course of the MMS project. Indeed, testimony before the Panel confirmed that the PCF was still using portions of the MMS during the transition phase to the PCFA at the time of the Panel’s hearing in December 2013. However, witnesses for both parties acknowledged that the MMS did not function perfectly.

Conclusions of Law

Section 11-35-4230 of the Procurement Code provides the exclusive means to resolving a controversy between the State and a contractor concerning a contract solicited and awarded under the Procurement Code, and either party to the contract may file a written request for resolution. S.C. Code Ann. § 11-35-4230 (2011). The CPO’s order notes that the PCF

¹⁹ The performance period of the final statement of work, SOW 010, ended on February 29, 2012. Record at PRP173.

requested²⁰ the resolution of a contract controversy between itself and Modus21, that he received pre-trial briefs from each party, and that he conducted a two-day hearing prior to issuing his order. Record at PRP3.

Both the PCF and Modus21 have appealed the CPO's decision to the Panel pursuant to section 11-35-4410(1)(a), which charges the Panel with the responsibility "to review and determine *de novo*" such decision. S.C. Code Ann. § 11-35-4410(1)(a) (2011). In previous contract controversy cases, the Panel has observed that the CPO's order holds no precedential value and that "the Panel is not bound by any aspect of it" in conducting a *de novo* hearing. *In re: Protest of McCrory Constr. Co.*, Panel Case Nos. 1994-13 & 1995-7 at 2 – 3 (May 29, 1995); *see also In re: Protest of M.B. Kahn Constr. Co.*, Panel Case No. 1995-13 at 7 (January 18, 1996) ("[T]he Panel's *de novo* hearing allows the Panel to evaluate the evidence presented and render a decision. The Panel rejects any suggestion that the Panel is bound by the decision of the Architect [interpreting the contract specifications] or the CPO.") Therefore, in accordance with Panel practice, the Panel heard anew those issues identified in the parties' Joint Statement of Legal Issues²¹ filed with the Panel on September 5, 2013, and allowed the parties to present additional evidence on them.²²

A contract controversy under section 11-35-4230 of the Procurement Code is in essence a breach of contract claim. In this case, the PCF claims that it paid Modus21 in excess of \$460,000.00 for an MMS which "does not provide many basic functions that were included in the initial project summaries and are key to [the] PCF's operations." Record at PRP2114. The

²⁰ The record before the Panel does not appear to include the written request for resolution from the PCF to the CPO, although it does contain the March 28, 2012 letter from the PCF's counsel to Dan Neason of Modus21 informing Modus21 of the PCF's intention to terminate the MMS contract. Record at PRP2112 – PRP2115.

²¹ This document was filed as provided by the Consent Scheduling Order issued by the Panel on August 21, 2013. The Panel finds that its review is limited to the issues identified in the Joint Statement by the consent of the parties.

²² The Panel notes that the PCF filed a motion for partial summary judgment in this case. The Panel received written briefs and heard legal argument regarding this motion at the beginning of its hearing. Deciding that there were issues of material fact that needed to be heard, the Panel denied that motion.

PCF seeks to recover all monies paid to Modus21 for “the fundamentally flawed and dysfunctional MMS,” compensation for lost staff time and the cost of hiring a consultant to conduct an independent review, and attorney’s fees. South Carolina Patients’ Compensation Fund’s Pre-Hearing Brief, dated November 22, 2013. For its part, Modus21 contends that it delivered the MMS solution as proposed, but that the PCF subsequently decided it wanted something else: a custom solution that “was not process centric, did not enforce business rules, and enabled [the PCF] to make ad hoc changes regardless of established policy.” Record at PRP2128. Thus, Modus21 asserts that the PCF bears much of the responsibility for any alleged dysfunction of the MMS. In addition, Modus21 argues it is not liable for lost staff time, the cost of the independent software consultant, or attorney’s fees under the terms of the Master Agreement.

Under South Carolina law, the primary objective in construing a contract “is to ascertain and give effect to the intention of the parties.” *Ellie, Inc. v. Miccichi*, 358 S.C. 78, 93, 594 S.E.2d 485, 493 (Ct. App. 2004) (citations omitted). The inquiry into the parties’ intention must begin with the language of the written contract itself. *Id.*, 594 S.E.2d at 493 (citations omitted). Thus, the Panel must first consider the language of the contract before it.

In this case, the written contract consists of several documents: the Master Agreement and SOWs issued under the Master Agreement; the RFP and any amendments; and Modus21’s technical and business proposals and clarifications dated September 23, 2006. Record at PRP126. As previously noted, the Master Agreement takes precedence over the other documents in the event of conflicts between them. Generally speaking, the Master Agreement obligated Modus21 to perform consulting services²³ for the PCF as described in the parties’ SOWs on a

²³ The term “consulting services” is not defined in the RFP or the Master Agreement. Moreover, the Master Agreement does not address the issue of whether the writing of custom software code (i.e., “application

“not to exceed” hourly rate basis. In turn, the PCF was to cooperate with Modus21 by “providing timely access to data, information and personnel of [the PCF],” “be[ing] responsible for the performance of its personnel and agents and for the accuracy and completeness of all data and information,” and completing its responsibilities “using experienced and qualified personnel.” As previously noted, the Master Agreement also provided that the PCF was to approve deliverables or provide written notice of any deficiencies to Modus21 within ten days of receipt. If deficiencies were noted, the PCF had ten days to review “corrective actions or changes made to the deliverable . . . and notify [Modus21] in writing of acceptance or rejection.”

I. Statement of Work 001

As discussed above, SOW 001 encompassed the planning and analysis phase of the MMS project. As an initial matter, the Panel finds that the work described in SOW 001 was within the scope of the state term contract and affirms the CPO’s finding on this issue. While not disputing the CPO’s finding that the work under SOW 001 was within the scope of the state term contract, the PCF has appealed the CPO’s findings that it accepted the deliverables under SOW 001 and that Modus21 was entitled to retain the \$18,270 the PCF paid it for SOW 001. Specifically, the PCF contends that it expressed dissatisfaction with the deliverables, that it did not accept the deliverables, and that it provided notice of deficiencies with the deliverables as soon as it learned of them. The Panel disagrees for the following reasons.

First, the Panel observes that the testimony of Ms. Laughlin and Ms. Coston established that Ms. Laughlin worked closely with the PCF staff during the time of this SOW to capture the PCF’s business requirements and to produce process models. Moreover, Ms. Coston testified

development”) is permitted in the scope of these consulting services. However, Amendment 1 of the RFP excludes “application development” from the RFP’s scope of work, and Modus21 acknowledged this limitation in its proposal. Thus, the Panel agrees with the CPO’s conclusion that writing custom code was not allowed on the MMS project.

that Ms. Laughlin did “a really good job” and that she was satisfied with Modus21’s performance on this SOW. Second, the PCF apparently paid Modus21 in full for this SOW.²⁴ Third, the record does not contain any timely, written notification rejecting the deliverables that complies with the express terms of the Master Agreement. Thus, the Panel concludes that Modus21 is entitled to retain the \$18,270 it was paid under Statement of Work 001.

II. Statement of Work 002 and Addenda 001 and 002

The Panel finds that the work described in this SOW was within the scope of the state term contract and affirms the CPO’s finding on this issue. The PCF argues that it notified Modus21 of deficiencies in the deliverables as soon as it became aware of them. The Panel acknowledges that the record before it is replete with e-mails from the PCF’s staff alerting Modus21 about various bugs and issues during the testing of MMS components. However, none of these e-mails specifically notified Modus21 that the PCF was rejecting any of the system components in accordance with the terms of the Master Agreement during this performance period. Modus21 billed the PCF in full for SOW 002, and the PCF paid Modus21 for this work. Therefore, the Panel concludes that the PCF accepted the work performed under SOW 002, and affirms the CPO’s finding in that regard. The Panel also affirms the CPO’s finding that the PCF waived any breach of SOW 002 by accepting the deliverables and paying in full. *See e.g., L. D. Powell Co. v. Levy*, 136 S.C. 387, 134 S.E. 415 (1926) (sale of goods); *Southern Coal Co. v. Rice*, 122 S.C. 484, 115 S.E. 815 (1923). Thus, the Panel concludes that Modus21 is entitled to retain the \$191,044 it was paid under SOW 002.

²⁴ The Panel notes, as did the CPO, that Modus21 did not consistently bill against a specific SOW or addendum. The Panel also notes that the PCF’s accounting contained in the Record is no more helpful in determining what amounts were paid for which work. Thus, with the exceptions of SOW 008, SOW 009, and SOW 010, the Panel has chosen to use the amounts listed in the various SOWs and addenda to determine the amounts Modus21 is entitled to retain and those it is obligated to return. For SOW 008, SOW 009, and SOW 010, the Panel has chosen to use the amounts listed in the Modus21 invoices for the time periods corresponding with these statements of work. *See* Record at PRP165 – PRP176.

The CPO found that Addenda 001 and Addenda 002 to SOW 002 lacked consideration because Modus21 was already obligated to provide reporting functionality under SOW 002. The Panel disagrees and finds that the evidence before it establishes that the reporting functionality desired by the PCF was not included in SOW 002. In other words, the Panel finds that the scope of work was changed by adding the reporting component. In addition, the addenda were presented to the PCF in writing and were approved by Ms. Coston. Therefore, the Panel concludes that these addenda satisfy the requirements of section 11-35-310(4)²⁵ of the Procurement Code and that Modus21 is entitled to retain the \$7,200 it was paid under Addenda 001 and 002 to SOW 002.

III. Statements of Work 003 through 010

As discussed above, the work performed under SOWs 003; 004 and Addendum 001; 008; 009; and 010 involved the delivery of custom software coding and exceeded the scope of the state term contract. This work was not competitively bid and represented a material change to the contract. The Panel recognizes the public contracting rule that prohibits the making of material modifications to contracts entered into under a competitive bidding statute. *Kenai Lumber Company, Inc. v. LeResche*, 646 P.2d 215 (Ak. 1982); *Matter of: LDDS WorldCom*, B-266257 (Comp. Gen.), 96-1 CPD P 50, 1996 WL 51207; *cf.* S.C. Code Ann. § 11-35-3070 (architectural, engineering, or construction changes). As a result, the Panel concludes that Ms. Coston, the PCF Board, and the ITMO procurement officer all lacked the authority to engage Modus21 to write custom software code. The Panel also concludes that Modus21 was well aware of the prohibition in the state term contract against writing custom software code. *Cf. In re: Protest of Technology Solutions, Inc.*, Panel Case No. 2001-3 (September 14, 2001) (wherein

²⁵ Section 11-35-310(4) defines “change order” as “any written alteration in specifications, delivery point, rate of delivery, period of performance, price, quantity, or other provisions of any contract accomplished by mutual agreement of the parties to the contract.” S.C. Code Ann. § 11-35-310(4) (2011).

the Panel found a vendor failed to prove that an “emergency” contract had been ratified by an agency and was not entitled to payment because the vendor relied on the representation of an IT employee who lacked the authority to bind the government). Therefore, the Panel finds that SOWs 003; 004 and Addendum 001; 008; 009; and 010 were unauthorized contracts.

In his order, the CPO applied Regulation 19-445.2015 in determining how to address the statements of work outside the scope of the state term contract. S.C. Code of State Regulations, Reg. 19-445.2015 (2011). The CPO specifically applied subsection (D) of the regulation, which provides:

Upon finding after award that an award is in violation of law and that the recipient of the contract acted fraudulently or in bad faith, the appropriate chief procurement officer shall declare the contract null and void unless it is determined in writing that there is a continuing need for the supplies, services, information technology, or construction under the contract and either (i) there is no time to re-award the contract under emergency procedures or otherwise; or (ii) the contract is being performed for less than it could be otherwise performed. If a contract is voided, the State shall endeavor to return those supplies delivered under the contract that have not been used or distributed. No further payments shall be made under the contract and the State is entitled to recover the greater of (i) the difference between payments made under the contract and the contractor’s actual costs up until the contract was voided, or (ii) the difference between payments under the contract and the value to the State of the supplies, services, information technology, or construction it obtained under the contract. The State may in addition claim damages under any applicable legal theory.

S.C. Code of State Regulations, Reg. 19-445.2015(D). Thus, to proceed under this provision of the regulation, two elements must be established: (1) that an award has been made in violation of law, and (2) that the contract recipient acted “fraudulently or in bad faith.” The Panel has agreed in part with the CPO that certain statements of work were unauthorized contracts because they involved custom coding. Thus, the first element under Regulation 19-445.2015(D) has been satisfied.

The CPO found that the second element was also met because Modus21 knowingly performed work outside the scope of the state term contract and that it did so for purposes of financial gain. Modus21 has appealed this finding of bad faith, arguing that it performed work outside the scope of the Master Agreement at the insistence of the PCF and that it did so openly and with the knowledge of the PCF, as evidenced by Ms. Coston's signatures on these statements of work. Moreover, Modus21 argues that the CPO's finding that it was motivated by financial gain failed to take into consideration the numerous hours it worked at no charge.

"Bad faith" is not defined by the Procurement Code. However, both the South Carolina Supreme Court and the South Carolina Court of Appeals have quoted from Black's Law Dictionary when considering the issue:

Bad faith. The opposite of "good faith," generally implying or involving actual or constructive fraud, or a design to mislead or deceive another, or a neglect or refusal to fulfill some duty or some contractual obligation, not prompted by an honest mistake as to one's rights or duties, but by some interested or sinister motive. Term "bad faith" is not simply bad judgment or negligence, but rather it implies the conscious doing of a wrong because of dishonest purpose or moral obliquity; it is different from the negative idea of negligence in that it contemplates a state of mind affirmatively operating with furtive design or will.

Black's Law Dictionary 72 – 73 (Abridged 5th Ed. 1983); *see, e.g., State v. Griffin*, 100 S.C. 331, 333, 84 S.E. 876, 877 (1915); *Estate of Carr ex rel. Bolton v. Circle S Enterprises, Inc.*, 379 S.C. 31, 42 – 43, 664 S.E.2d 83, 88 – 89 (Ct. App. 2008). Adopting this definition, the Panel finds that "bad faith" under Regulation 19-445.2015(D) requires more than a determination that work was performed outside the scope of the original agreement; there must also be some showing of "dishonest purpose" or "furtive design." Based on the record before it and all of the testimony heard over the course of three days, the Panel finds that Modus21 did not act out of a "dishonest purpose" or "furtive design," but rather out of a desire to satisfy its customer and to complete the project successfully. Therefore, the Panel finds that the second element of

subsection (D) is not met and reverses the CPO's decision to the extent it relied on that provision of the regulation.

The Panel must now consider whether any other provision contained in the regulation can resolve the dispute between the parties. Subsection (C) governs the termination of an unlawful or unauthorized contract not accompanied by fraud or bad faith on the part of the contract recipient. Regulation 19-445.2015(C) provides that a settlement claim by the contract recipient after the State terminates a contract may either be "made in accordance with the contract" or "made on the basis of actual costs directly or indirectly allocable to the contract through the time of termination" if the contract does not contain termination provisions. S.C. Code of Regulations, Reg. 19-445.2015(C). In the instant case, Modus21 has been paid in full for all of the statements of work, and it is the State, not Modus21, seeking "settlement." Therefore, the Panel finds that subsection (C) is not helpful to the resolution of this contract controversy and cannot be reasonably applied under the circumstances.

Nonetheless, the Panel finds that the unauthorized contracts uncovered during the course of these proceedings may be addressed by the contract controversy statutory provision itself. Section 11-35-4320 of the Procurement Code provides that the CPO "may award such relief as is necessary to resolve the controversy as allowed by the terms of the contract or by applicable law." S.C. Code Ann. § 11-35-4320 (2011). Based on this statutory provision, the Panel finds that the CPO acted properly in declaring SOWs 003; 004 and Addendum 001 to SOW 004; 008; 009; and 010 null and void under the prohibition against material modifications to contracts executed under a competitive bidding statute. Thus, the Panel affirms his decision requiring

Modus21 to return all amounts²⁶ paid to it under these statements of work. *Cf. Service Management, Inc. v. State Health and Hum. Svcs. Fin. Comm'n*, 298 S.C. 234, 238, 379 S.E.2d 442, 444 (1989) (“A private party has no right to public funds received as a result of the unauthorized conduct of a government employee.”).

With regard to SOWs 005, 006, and 007, the Panel finds that these statements of work, contrary to the CPO’s ruling, were within the scope of the state term contract. Moreover, the PCF never rejected any deliverables under these statements of work during their performance periods. Thus, the Panel concludes that Modus21 is entitled to keep the amounts the PCF paid to it under SOWs 005, 006, and 007. However, the Panel also concludes that Addendum 001 to SOW 005 called for development work which was outside the scope of the state term contract. Accordingly, Modus21 is directed to return the \$2,785 it received under this addendum.

IV. The PCF’s Claims Seeking Recovery of Mr. Stanley’s Fees, Lost Staff Time, and Attorney’s Fees and Costs

In its appeal to the Panel, the PCF also sought compensation for lost staff time, recovery of the fees it paid to Mr. Stanley, and recovery of attorney’s fees and cost. The Panel finds that these damages are not recoverable under the terms of the Master Agreement and denies the PCF’s request to recover these damages.²⁷ Record at PRP125 ¶ 10.1.

Conclusion

In conclusion, for the reasons stated herein, the Panel hereby affirms the CPO’s ruling in part and reverses the CPO’s ruling in part.

²⁶ Under the Panel’s determination, the following amounts shall be returned to the PCF: \$54,208 for SOW 003; \$73,525 for SOW 004 and Addendum 001; \$275.50 for SOW 008; \$751.25 for SOW 009; and \$12,225.75 for SOW 010.

²⁷ The Panel also notes that it does not believe Mr. Stanley’s fees would have been recoverable in any event as they were paid in violation of the Procurement Code.

IT IS SO ORDERED.

SOUTH CAROLINA PROCUREMENT REVIEW PANEL

BY: 
C. BRIAN MCLANE, SR., CHAIRMAN

This 9th day of September, 2014.

Columbia, South Carolina