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Comptroller General
of the United States

Washington, D.C. 20548

:03211

Decision

Matter of: Halifax Technical Services, Inc.

File: B-246236.6; B-246236.7; B-246236.9

Date: January 24, 1994

Jacob B. Pompan, Esq., Gerald H. Werfel, Esq., and Brad C. D'Amico, Esq., Pompan, Ruffner & Werfel, and William W. Goodrich, Esq., Arent, Fox, Kintner, Plotkin & Kahn, for the protester.
Paul Shnitzer, Esq., and David Z. Bodenheimer, Esq., Crowell & Moring, for AlliedSignal Technical Services Corporation, an interested party.
George N. Brezna, Esq. and Jeffrey A. Epstein, Esq., for the agency.
Ralph O. White, Esq., Office of the General Counsel, GAO, participated in the preparation of the decision.

DIGEST

1. Contention that agency performed an unreasonable cost realism review by accepting a cap on awardee's direct costs in certain specific labor categories is denied where agency performed a reasonable evaluation of the cost proposal, both with and without the cap, and where the agency clearly understood the impact and limitations of the terms of the cap clause, which was set forth in the contract schedule.

2. Contention that cost realism review was improper for failing to reject the cost benefits of an agreement between the awardee and a representative of the union for certain of the incumbent's employees is denied where the agreement is consistent with the awardee's approach when it was the incumbent; the contracting officer sought expert advice regarding the soundness of the approach; and the cost cap clause included in the awardee's contract is not contingent upon the awardee's ability to obtain the benefits of this agreement after receiving the contract.

DECISION

Halifax Technical Services, Inc. protests the award of a contract to AlliedSignal Technical Services Corporation (Allied) under request for proposals (RFP) No. M67004-90-R-0094, issued by the U.S. Marine Corps for maintenance of assets aboard ships associated with the Maritime Prepositioning Forces (MPF). Halifax argues that the agency conducted an improper cost realism analysis of Allied's proposal, and mistakenly concluded that Allied, rather than Halifax, offered the lowest evaluated costs.

We deny the protest.

BACKGROUND

This protest involves the Marine Corps' selection of a contractor to operate the MPF program. This program was implemented to reduce deployment time for Marine Corps forces by prepositioning squadrons of ships stocked with equipment and supplies for up to 30 days of sustained combat. Separate MPF squadrons are afloat in the Atlantic Ocean, the Pacific Ocean and the Indian Ocean, ready to be deployed at any time to crisis areas throughout the world. The role of the contractor is to provide civilian maintenance crews for the MPF ships and to perform the equipment modifications and calibrations, stock rotation, inventory management, and readiness reporting necessary to ensure that the MPF is constantly prepared for deployment.

Events and Changes Since the Original Protest Decision

The procurement at issue here is a reopened competition recommended by our Office after sustaining a challenge to the Marine Corps' earlier selection of Halifax to perform these services. See Bendix Field Eng'g Corp., B-246236, Feb. 5, 1992, 92-1 CPD ¶ 227. Our prior decision recommended that the Marine Corps reopen negotiations, request best and final offers (BAFO), and, if appropriate, terminate the contract awarded to Halifax and make a new contract award. In the nearly 2 years since our Office sustained Bendix's initial protest, a number of events have delayed the Marine Corps in its attempt to conclude this procurement. These events are highlighted briefly below.

After amending the solicitation--the relevant terms of which will be set forth below--and reopening negotiations, the Corps first requested BAFOs by August 3, 1992. While evaluating the first round of BAFOs, certain union employees involved in providing these services were provided increased health and welfare benefits. As a result, the Corps found it necessary to request a second round of BAFO submissions after attempting to clarify its instructions to offerors regarding these benefits and to explain its approach to evaluating such benefits, including employee insurance coverage. Before the agency received a second round of BAFOs to address these changes, Halifax challenged the agency's intended evaluation approach in an agency-level protest, two protests to our Office (both of which were dismissed)[1] and a lawsuit filed in the Court of Federal Claims (which was subsequently withdrawn).[2]

During the negotiations, the Marine Corps also received a request from the Department of the Army for support for the Army Afloat Prepositioning Program, a program similar to the MPF program. On June 3, 1993, the contracting officer added the Army program to the solicitation as an option requirement, after providing a draft amendment to the offerors for comment. On June 30, the agency received its third round of BAFO submissions from six offerors.

The Current Evaluation

The solicitation, as amended, anticipated award of a cost reimbursement level-of-effort contract for 1 year, followed by four 1-year options. There was also an unpriced option included for the Army program. The statement of work in the solicitation specified the level of effort as 709 staffyears per year.

Potential offerors were advised at sections M-4 and M-5 of the RFP that the agency would evaluate and rate proposals in the areas of technical approach, management approach, corporate experience, and cost. Specifically, the RFP advised that the relative weights of these factors would be:

Technical and Management Approach		60 percent
Technical proposal	30 percent	
Management proposal	20 percent	
Corporate experience	10 percent	
Cost Proposal		40 percent

Section M-4 also stated that award would be made to the offeror that "can best satisfy the objectives and requirements set forth in the solicitation in a manner most advantageous to the [g]overnment." Section M-2 addressed the role of the options in the award decision: it advised that offers would be evaluated by adding the proposed cost for all options to the total price for the basic effort, but cautioned that the government would not be obligated to exercise options. The RFP further advised that cost would

[1]Halifax Tech. Servs., Inc., B-246236.4, Jan. 5, 1993, 93-1 CPD ¶ 3, and Halifax Tech. Servs., Inc., B-246236.5, Feb. 16, 1993.

[2]Halifax Tech. Servs., Inc. v. United States, Ct. Fed. Cl. No. 93-107C.

assume greater significance if offerors were determined to be technically equivalent.

Since this procurement has stretched over nearly 4 years, we need not set forth the results of each successive evaluation of proposals. However, upon receipt of the third round of BAFOs in the reopened competition--wherein six offerors participated--the results of the technical and cost evaluations showed that Allied was rated slightly higher technically than Halifax, and that its evaluated costs were lower than Halifax's, and lower than those of any other offeror. Halifax was the offeror with the second lowest evaluated costs. As a result, Allied received the highest combined technical and cost score, while Halifax was a close second.

In its review of the last round of BAFOs, the agency focused on two issues related to the proposed costs in Allied's proposal: first, Allied proposed to cap a portion of its direct labor costs at $61,782,122; second, Allied included an agreement between it and a representative of the United Steelworkers of America--the union that represents certain of the hourly employees involved in this effort--regarding the hourly rates to be paid in the event Allied received the contract. Specifically, this agreement related to a May 21, 1993, collective bargaining agreement (CBA) between Halifax and the union, and addressed the extent to which Allied would honor the terms of the CBA if Allied received the contract. Under this arrangement, Allied agreed to pay the union employees at the CBA rates until May 1994, but in lieu of the 3.5 percent annual wage escalation set forth in the CBA, Allied agreed to pay annual lump sum bonuses based on performance. Allied's labor cap and the agreement with the union were the basis for Allied's significantly lower proposed costs.[3]

In attempting to address these issues, the contract specialist contacted both the Department of Labor (DOL) and the National Labor Relations Board (NLRB) to inquire whether the agreement between Allied and the union violated either the Service Contract Act or the National Labor Relations

[3]Over the life of the contract, Allied's approach of not paying annual wage escalations--and instead paying performance bonuses--lowers the direct labor costs generated. This is true even if the same amount is paid each year in annual bonuses (3.5 percent) as would have been paid in annual wage escalations.

Act.[4] By letters dated July 29, 1993, the contracting officer confirmed the conversations with the DOL and NLRB representatives. In the letter to the NLRB representative, the contracting officer confirmed the contract specialist's understanding that there was nothing improper about the agreement. In the letter to the DOL representative, the contracting officer confirmed that:

> "You stated that it was the policy of the Department of Labor to only enforce the Service Contract Act (SCA) for one year. Additionally, you stated that there is not a violation of the SCA until it occurs. The fact that an offeror proposed to violate the SCA in 1995, if the CBA is not renegotiated, does not constitute a violation now. The Corps cannot presume that the offeror will not abide by the SCA until the violation actually occurs."

The contracting officer's letters also asked for a response by August 16 in the event the letter misrepresented the conversation.

When neither recipient responded to the July 29 letters, the contracting officer sent a second pair of confirming letters on September 3. While the DOL representative did not call or write in response to either letter, the NLRB representative did both. After conferring with the contracting officer by telephone, the NLRB representative, by letter dated September 9, explained that the issue was not clear. In his letter, after cautioning that the opinions offered were his own and could not be used as a defense to an unfair labor practice charge, the NLRB representative stated:

> "As far as the National Labor Relations Act is concerned, in my opinion, a successful bidder could adopt the predecessor's collective bargaining agreement for one year and then renegotiate in the 2nd and/or 3rd years.

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[4]Under the Service Contract Act, successor contractors generally are required to adhere to the predecessor contractor's CBA. See 41 U.S.C. § 353(c); KCA Corp., 69 Comp. Gen. 549 (1990), 90-2 CPD ¶ 1; Trinity Servs., Inc., B-215631, Dec. 3, 1984, 84-2 CPD ¶ 602. The agency's concern about whether Allied's proposal violated this general principle--together with the unusual circumstance of an offeror negotiating a prospective agreement with a union representing employees who do not work for that offeror, and the labor relations issues presented by that agreement--was the basis for the decision to seek additional guidance here.

> "However, it is a little more difficult question where the union representing the incumbent contractor's employees, promises a prospective bidder in advance that it will agree to do this if awarded the contract. If the union makes this commitment in good faith in order to best represent the employees in the bargaining unit, then in my opinion it would not be violative of the NLRA. However, I do not know without researching the issue, whether the [e]mployer could bind the [u]nion to this commitment once it was selected as contractor, and bargaining commenced.
>
> "Additionally, if the union and the prospective bidder entered into an actual collective bargaining agreement before the bidder became the [e]mployer of the bargaining unit employees, then both [u]nion and [e]mployer may be potentially liable to unfair labor practice charges."

The Marine Corps evaluated Allied's cost proposal both with, and without, the cap. At the end of the evaluation, the Marine Corps concluded that Allied's proposal would be the least expensive under either scenario. The overall numbers generated by this comparison are shown below:

COSTS IN MILLIONS OF DOLLARS[5]

	Proposed Costs	Evaluated Costs With Cap	Evaluated Costs Without Cap
Allied	$ 123.1	$ 127.7	$ 131.6
Halifax	$ 138.2	--	$ 132.9

Using the evaluation of Allied's costs without the cap, the source selection evaluation committee generated weighted technical and cost scores for each of the offerors, which are shown below:

	Technical	Cost	Total
Allied	42.80	40.00	82.80
Halifax	42.47	39.61	82.08
Company A	42.87	38.04	80.91
Company B	43.10	34.88	77.98
Company C	37.55	38.70	76.25
Company D	37.49	36.00	73.49

[5]We have omitted the cost information related to the other four offerors, all of which were evaluated higher than were Allied and Halifax.

Based on these weighted scores, the evaluation committee recommended award to Allied. The source selection official concurred on September 7, and this protest followed.

DISCUSSION

Halifax's protest, in essence, raises two challenges to the Marine Corps' conclusion that Allied's proposal offered the greatest advantage to the government because of its combination of technical merit and low evaluated costs. Halifax argues that the agency improperly accepted a cap on certain--but not all--direct labor costs that will fail to provide adequate protection against cost overruns, and that the agency improperly permitted Allied to premise its cost cap on an agreement between Allied and a union representative that may not be enforceable. In Halifax's view, these errors rendered unreasonable the agency's conclusion that Allied's proposal offered the lowest costs.

When agencies evaluate proposals for the award of a cost-reimbursement contract, an offeror's proposed estimated costs are not dispositive, because regardless of the costs proposed, the government is bound to pay the contractor its actual and allowable costs. Federal Acquisition Regulation (FAR) § 15.605(d). Consequently, a cost realism analysis must be performed by the agency to determine the extent to which an offeror's proposed costs represent what the contract should cost, assuming reasonable economy and efficiency. CACI, Inc.--Fed., 64 Comp. Gen. 71 (1984), 84-2 CPD ¶ 542. Because the contracting agency is in the best position to make this cost realism determination, our review of an agency's exercise of judgment in this area is limited to determining whether the agency's cost evaluation was reasonably based and not arbitrary. General Research Corp., 70 Comp. Gen. 279 (1991), 91-1 CPD ¶ 183, aff'd, American Mgmt. Sys., Inc.; Department of the Army--Recon., 70 Comp. Gen. 510 (1991), 91-1 CPD ¶ 492; Grey Advertising, Inc., 55 Comp. Gen. 1111 (1976), 76-1 CPD ¶ 325.

Allied's Proposed Cap

In its original and two supplemental protests, Halifax raises numerous challenges to the agency's decision to accept Allied's proposed cap on direct labor. Among other things, Halifax argues that the agency improperly failed to: (1) recognize that Allied's cap was a buy-in and only covered certain categories of direct labor; (2) understand that the cap was a cap on dollars and not rates; (3) appreciate that the cap would not generate savings until the last option period; and (4) reject Allied's approach to the proposed cap as a violation of applicable cost accounting standards. For the reasons set forth below, we see nothing unreasonable about the agency's decision to accept Allied's proposed cap on direct labor expenses.

Allied's proposal, in essence, identifies six types of employees it intends to use to perform these services. Since the purpose for the breakdown of employees by type is not relevant to this discussion, we will simply identify the employees by their labor category number, as used in the contract--i.e., labor categories 27N, 27M, 27P, 27R, 27T and 5JX. The terms of Allied's proposed labor cap, set forth in the contract schedule, explain in detail the operation of the labor cap by labor category. Specifically, the cap clause provides:

> "This contract is entered into with the agreement that [Allied] will cap direct labor dollars and annual increases proposed over the total term of the contract ([b]ase [y]ear plus four [o]ption [y]ears) based on 681 personnel at $61,782,122.00 The total direct labor ceiling cap is the sum of the following:
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> > "a. Direct labor dollars for [labor categories 27M][6], [27R], [27T], and [27P].
> >
> > "b. Merit Bonus for [27M and 27R], and Shipboard Completion Bonus for [27T].
> >
> > "c. Union Lump Sum Distribution Payment dollars for [27P] Bargaining Unit."

The cap clause included in Allied's contract also excludes the following items from the cap: (1) direct labor charges under categories 27N and 5JX; (2) all overtime charges; (3) increased charges resulting from changes in the skill mix imposed by the government; (4) any increase in staffing above 709 positions[7]; (5) special augmentation labor costs directed by the government; (6) increased labor costs associated with deployment to another area where a higher wage determination may apply; (7) costs associated with the implementation of the Army Prepositioning Program; (8) costs associated with invoking differential pay; and (9) phase-in labor dollars for labor category 27M.

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[6]Extraneous labor category descriptive information has been omitted.

[7]Both the skill mix and staffing level exclusions--i.e., exclusions 3 and 4, above--provide that only the difference in the rates will be excluded from the cap, and that an increase in these two areas will not invalidate the cap.

As an initial matter, our review of the record, including the cost evaluation of Allied's proposal both with, and without the cap, shows no basis for Halifax's suggestion that the agency misunderstood the mechanics of Allied's proposed cap. Although Halifax correctly claims that the cap here is limited and will not protect the agency from all direct labor increases, the cost realism review shows that the agency recognized this fact. For example, the agency differentiated between capped and non-capped labor categories in making adjustments to Allied's proposed costs as part of its cost realism review. In several areas where the cap did not apply, the agency made upward adjustments, suggesting that it did, in fact, understand how the cap would operate.

Our Office recently considered in detail the impact of an offeror's proposed cap or ceiling on an agency's cost realism review. In that decision, Vitro Corp., B-247734.3, Sept. 24, 1992, 92-2 CPD ¶ 202, we explained that as a general rule, the use of such caps shifts the government's risk of bearing the expense of cost overruns on cost reimbursement contracts back to the contractor. As a result, when offerors propose such caps, and no other issue calls into question the effectiveness of the cap, upward adjustments to capped costs are improper. Id. In lieu of a cost realism adjustment, a decision about an awardee's ability to perform a contract at rates capped below actual costs falls within an agency's determination of an offeror's responsibility, an affirmative determination of which we will not review absent a showing of agency fraud, bad faith or misapplication of definitive responsibility criteria. Robocom Sys., Inc., B-244974, Dec. 4, 1991, 91-2 CPD ¶ 513.

Halifax claims that the agency's decision to accept Allied's proposed cap violates the cautions against "buying-in" set forth at FAR § 3.501. As we stated in Vitro, since the effect of a cap like the one here is to convert a portion of this cost-type contract to a fixed-price contract, see Advanced Tech. Sys., Inc., 64 Comp. Gen. 344 (1985), 85-1 CPD ¶ 315, we agree that Allied's cap may be analogous to a below-cost bid or offer in a fixed-price environment. However, the FAR guidance to contracting officers does not bar an agency from accepting such an offer. Rather, the FAR states that contracting officers faced with the possibility of a buy-in must take steps to ensure that an offeror's buying-in losses are not recovered from the government through change orders or follow-on efforts. FAR § 3.501-2(a). In fact, the FAR suggests that one way to minimize such an offeror's likelihood of recovering such losses through other means is to seek a price commitment covering as much of the program as possible--something the contracting officer has done here. See FAR § 3.501-2(b)(1).[6]

Halifax's next two contentions--that the agency did not understand that the cap was a cap on dollars and not rates, and that the agency did not appreciate that the cap on dollars would not generate savings until the last option period--are not supported by the record. As an initial matter, the terms of Allied's cap clause are set forth in the contract schedule. The terms there clearly state that Allied will cap direct labor dollars at $61,782,122. The clause says nothing about rates. In addition, the agency evaluated Allied's proposal both with, and without, the cap. As stated above, the cost evaluation of Allied's proposal sets forth in detail a review of the different labor categories, and adjustments to those categories not covered by the cap.

As evidence that the Marine Corps does not understand that Allied's cap will not generate savings until the fourth option year, Halifax cites the fact that the agency's counsel argued that savings from the Allied approach will begin to accrue in May 1994. The agency's statement regarding when savings will accrue relates to the impact of the labor agreement, not the operation of the cap. Thus, the agency's position that savings from Allied's approach will begin in May 1994--the time of the first scheduled annual labor rate escalation, which Allied proposes not to pay--does not support a conclusion that the agency misunderstood how the cap will operate. In addition, even if we accept Halifax's contention that Allied will not reach its direct labor cap of nearly $62 million until the fourth option year, the argument is irrelevant. The RFP advised offerors that their offers would be evaluated with options. The RFP further advised that the decision to evaluate the base year effort together with the options did not mean that the agency was committed to awarding the options. Thus, the

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[6]Halifax also suggests that the agency's failure to request proposed costs for the option effort covering the Army program violates the FAR's cautions regarding "buying-in." Although FAR § 3.501-2(b)(2) does suggest that agencies can minimize exposure to increased costs by using priced options for additional quantities, the agency's decision not to do so here does not invalidate its selection decision, since the cost of the Army program played no role in the evaluation. In addition, any claim that the option for the Army program should have been priced and evaluated is now untimely. This contention should have been raised in response to the draft solicitation amendment, or prior to the time the agency received the third round of BAFO submissions. See 4 C.F.R. § 21.2(a)(1) (1993).

fact that Allied has proposed a cap that may have no effect until the fourth option period does not invalidate the agency's conclusion that Allied has proposed the lowest overall evaluated costs.[9]

As a final matter, we see no reason to overturn the agency's cost evaluation based on Halifax's contention that Allied's proposed operation of its cap would violate the cost accounting standards. For the purpose of analysis, we will assume that Halifax is correct in its contention that Allied's proposal failed to allocate overhead to its direct costs properly, and that its approach to allocating overhead to the capped costs would violate cost accounting standards. As Halifax admits, the record shows that the agency recognized this problem and added a significant amount of overhead to Allied's cost proposal as part of the cost realism review. Halifax does not suggest that the cost realism adjustment was improper, but argues instead that in lieu of making the adjustment, the agency should have simply rejected Allied's proposal for violating cost accounting standards.

Where the terms of a contract itself include a provision where a contractor agrees to waive certain charges--here all charges in excess of the specified cap--there is nothing improper about an agency's decision to accept the contractor's offer, even though the contractor's cost accounting disclosure statement provides that such charges will be accrued. See Raytheon Support Svcs. Co., 68 Comp. Gen. 566 (1989), 89-2 CPD ¶ 84. In short, the accrual of such costs does not translate to their recovery. See Syscon Corp., 68 Comp. Gen. 311 (1989), 89-1 CPD ¶ 249. Here, where the agency spotted the possibility of additional overhead charges on its own, and reasonably added the additional overhead to Allied's costs as part of its cost realism review, we fail to see why the agency instead should have rejected Allied's proposal. In administering the contract, the agency can take steps to safeguard the government from any attempt by Allied to recover these costs under this contract, or under any other effort. See Raytheon Support Servs. Co., supra.

Allied's Labor Agreement

Halifax's second area of protest is that the agency should have rejected any cost savings associated with Allied's agreement with a representative of the labor union

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[9]As with the Army program, if Halifax disagreed with the agency's decision to evaluate options, the time for a protest of that issue in this procurement has long since passed. 4 C.F.R. § 21.2(a)(1).

representing certain of the employees involved in this effort. For the reasons set forth below, we see no reason to overturn the agency's cost realism review in this area.

As an initial matter, the entire issue of Allied's controversial labor agreement may be irrelevant to whether the agency will benefit from the direct labor cap here. The cap clause set forth in the contract schedule is not contingent on whether Allied will be able to realize the benefit of the agreement at issue. Thus, in our view, regardless of whether Allied is able to realize the benefit of its agreement with a representative of the current union, it is nonetheless obligated to cap its costs in certain labor categories at approximately $62 million.[10]

In addition, we have found nothing in the record to suggest that the agency's consideration of and conclusion about this issue was unreasonable. First, Allied explains that when it previously performed these services for the Marine Corps--Allied was the contractor for the 5 years prior to our initial decision sustaining its protest against award to Halifax--it had a similar agreement with the union involving payment of performance bonuses instead of annual escalation increases. This previous experience lends credence to the agency's conclusion that Allied's approach will be acceptable to the employees here.

Second, the record shows that the agency went to great lengths to seek input from knowledgeable sources regarding the legality of Allied's proposed approach. As explained above, the contracting officer and his staff contacted representatives of both the DOL and the NLRB, talked with those individuals, followed up on the conversations with not one but two confirming letters, and had a further telephone conference with the NLRB representative, followed by written advice from that individual. Although the NLRB representative raised certain concerns about the agreement, quoted above, those concerns do not support a conclusion that the agency acted improperly here. The general thrust of the advice received from both sources was that, at worst, Allied might have to renegotiate the CBA to achieve the desired agreement regarding payment of bonuses.

Efforts such as those taken here to seek expert advice on complicated labor issues--and other issues--impart greater credence to an agency's evaluation, and absent circumstances

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[10]Our view of the impact of caps and ceilings on cost reimbursement contracts is tied to the expectation that in administering such contracts agency personnel will aggressively protect the government's interest in realizing the benefits of the contract. See Vitro Corp., supra.

suggesting that following such advice is unreasonable, we will uphold evaluations based on such efforts. <u>See</u> <u>PAE GmbH Planning and Constr.</u>, B-250470, Jan. 29, 1993, 93-1 CPD ¶ 81, <u>aff'd</u>, B-250470.2, July 22, 1993, 93-2 CPD ¶ 45. Given that Allied itself previously had such an agreement; that experts on the subject were not indicating that Allied's approach was clearly improper or that Allied would be unable to proceed as intended; and that the contract did not make Allied's cap contingent upon Allied's ability to secure the agreement it apparently believes it will be able to secure, we find nothing unreasonable about the agency's cost evaluation here.

The protest is denied.

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for Robert P. Murphy
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