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Mr. Wayne Proc. Law II

DECISION



**THE COMPTROLLER GENERAL
OF THE UNITED STATES
WASHINGTON, D. C. 20548**

FILE: B-180789

DATE: January 6, 1977

MATTER OF: Nicolai Joffe Corporation (Reconsideration)

DIGEST:

1. Portion of prior decision, holding that Maritime Administration's establishment of a minimum acceptable bid price for surplus vessels and its rejection of bids below that price was not subject to objection in view of broad discretion vested in Secretary of Commerce, is affirmed since record does not establish that agency acted arbitrarily or in bad faith. Prior holding that absence from solicitation of minimum acceptable bid price does not comport with competitive bidding requirements is modified in view of subsequent case law and absence of specific statutory requirement for disclosure of minimum price.
2. Requirement that minimum acceptable price be determined on "current" basis and that evaluation of bids not be based on speculative factors does not preclude consideration of changing and projected market conditions in establishing minimum acceptable price.

Nicolai Joffe Corporation has requested reconsideration of our decision in Nicolai Joffe Corporation, 54 Comp. Gen. 830 (1975), 75-1 CPD/204, in which we denied its protest of the rejection of bids submitted in response to invitation for bids (IFB) No. PD-X-971, issued by the Maritime Administration (MarAd), United States Department of Commerce.

The rejected bids were offers to purchase for scrap six surplus merchant vessels from the National Defense Reserve Fleet. Joffe's all or none bid of \$21.42 per ton was the highest aggregate bid received. MarAd rejected all bids for the six vessels because it determined that the bid prices were unreasonably low in light of its minimum acceptable price per ton of \$30.00. The determination of a minimum acceptable price was made after receipt and examination of bids.

In our prior decision, we found no basis to disturb MarAd's determination that the prices offered were unreasonable. However, we recommended that MarAd should determine its minimum acceptable price prior to bidding and disclose that price to bidders. Joffe contends that MarAd's determination that the bids were unreasonably priced was erroneous and made in bad faith, and requests that the solicitation be reinstated with an award made thereunder to Joffe.

B-180769

Also, both MarAd and Joffe object to the recommendation that the agency determine and disclose an acceptable price prior to the submission of bids.

MarAd's authority to conduct these sales is found in section 508 of the Merchant Marine Act of 1936, 46 U.S.C. § 1158 (1970), which reads as follows:

"If the Secretary of Commerce shall determine that any vessel transferred to the Department of Commerce, as the successor to the United States Maritime Commission, or hereafter acquired, is of insufficient value for commercial or military operation to warrant its further preservation, the Secretary is authorized (1) to scrap said vessel, or (2) to sell such vessel for cash, after appraisement and due advertisement, and upon competitive sealed bids, either to citizens of the United States or to aliens * * *."

MarAd has adopted the guidelines contained in sections 5 and 6 of the Merchant Marine Act of 1920, 46 U.S.C. §§ 864 and 865, in its disposal of these vessels. Those statutes involve the sale of vessels that will be used in commerce, not scrapped. 46 U.S.C. 864 provides:

" * * * the Secretary of Commerce is authorized and directed to sell, as soon as practicable, consistent with good business methods and the objects and purposes to be attained by this act, at public or private competitive sale after appraisement and due advertisement, to persons who are citizens of the United States except as provided in section 865 of this title, all of the vessels acquired by the commission under former sections 862 and 863 of this title or otherwise. Such sale shall be made at such prices and on such terms and conditions as the Secretary may prescribe, but the completion of the payment of the purchase price and interest shall not be deferred more than fifteen years after the making of the contract of sale. The Secretary in fixing or accepting the sale price of such vessels shall take into consideration the prevailing domestic

and foreign market price of, the available supply of, and the demand for vessels, existing freight rates and prospects of their maintenance, the cost of constructing vessels of similar types under prevailing conditions, as well as the cost of the construction or purchase price of the vessels to be sold, and any other facts or conditions that would influence a prudent, solvent business man in the sale of similar vessels or property which he is not forced to sell. * * *

The award and rejection provision of the invitation stated:

"VII. Award and Rejection of Bids. The Contracting Officer reserves the right to reject any and all bids, call for new bids, waive any informality in any bid and make such award or awards as he may deem most advantageous, or will best serve the purposes and policy of the Merchant Marine Act, 1936, as amended, or other applicable law."

In our prior decision while noting that MarAd had neither written procedures for setting a minimum acceptable price nor regulations governing sales procedures, we found "no basis to challenge the manner in which the minimum acceptable bid was established in view of the statutory discretion vested in the Secretary of Commerce." 54 Comp. Gen. at 834. We further noted, however, that a substantial majority of the ships offered for sale in a solicitation are not sold because all bids received on a given ship are regarded by MarAd as too low. For example, under PD-X-971, only 4 of 13 vessels offered were sold with the high bids on 9 rejected as too low or below MarAd's minimum acceptable bid, a 70 percent rejection rate. The immediately preceding sale (PD-X-970) had a 63 percent rejection rate. We said that this "continuing high rate of rejection must discourage competition since bidders will be reluctant to expend the time and money to prepare and submit a bid when it is likely that most of the ships offered for sale will, in fact, not be sold." 54 Comp. Gen. at 832. We went on to state our belief that:

"competition would be served by establishing in advance the minimum acceptable price per ton for each ship and providing that information in the invitation for bids. The price per

B-180769

ton established should take into consideration the current market and any particular circumstances which would warrant a minimum price above or below the market * * *." 54 Comp. Gen. at 833

We concluded that the six vessels involved in the protest should be readvertised, with the minimum acceptable price disclosed in the IFB.

Joffe's request for reconsideration is founded on its contention that whatever discretion the Secretary of Commerce may have, that discretion is subject to the legal obligation of MarAd not to reject all bids unless there is a cogent or compelling reason. In this regard, Joffe has submitted arguments that MarAd's determination that Joffe's bid was unreasonably low was clearly erroneous and made in bad faith. Moreover, Joffe contends that it can show that its bid was reasonable and that the contracting officer actually believed that Joffe's bid was reasonable because she initially contemplated making an award to Joffe.

MarAd has summarized its procedure for evaluating the acceptability of bid prices as follows:

"1. Bids are examined in terms of the recent bidding history of the coastal area in which the bidder is located. However, no tentative minimum acceptable price is determined in this step.

"Note: The coastal distinction is based on sales experience that bids from shipbreakers located on the Gulf, East and West Coasts consistently vary.

"2. If the bids received, upon examination, do not reflect the coastal bidding trend of recent invitations, an attempt to reconcile or explain this difference is made by considering the markets into which steel scrap is sold and the resulting resale profits that would likely be realized. As part of this step a tentative minimum price per ton is determined.

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B-180769

"[More specifically] bidding history and scrap market trends are used to tentatively determine a figure. As a second procedural step MarAd's shipbreaker cost and vessel inventory information is used to confirm the tentative figure or suggest possible adjustments.

* * * * *

"3. The impact of export controls on this tentative price is evaluated.

"4. Other known factors are used to confirm the tentative minimum price, such as shipbreaker vessel inventories and, on an industry-wide basis, towage and shipping costs. The effect of steps #3 and #4 is to either adjust or confirm the tentative minimum price and in many cases to explain why some bids do not reflect recent bidding trends.

"5. The minimum acceptable price is finally determined."

In the instant sale, MarAd explains:

" * * * the protester's and other bids were first found to be well below recent bidding trends on the West Coast where the six vessels were located based on the range of bids received in preceding invitations. 3/ Then a tentative minimum price of \$30.00 was determined. 4/ This figure was then analyzed in terms of both the foreign and the domestic prices that would be available for the vessels when converted to scrap. The foreign price was and has been used because * * * a large portion of the scrap derived from its surplus ships is and has been exported. 5/ The ships' value may therefore be evaluated in terms of an export value for scrap metal. The tentative price was then confirmed by export control and cost factors that apply generally to potential purchasers."

MarAd's statement included the following applicable footnotes:

3/ "In PRV-864, opened October 10, 1973, the bids ranged from \$9.50 to \$32.94 per long ton with an average for accepted bids of

B-180769

\$25.95. In PDX-967 the range was from \$11.00 to \$41.07 per ton with an average for accepted bids of \$38.83. In FDX-968 the range was from \$17.21 to \$30.27, although no ships were awarded. [This range] excluded some nominal bids of \$15.00 per ton or less."

- 4/ "The average price on ships sold in PDX-967 was \$38.83 at a time when the domestic price for scrap was \$63.00 per long ton. The February (PDX-971) price ranged above \$10.00, so a \$30.00 minimum price was tentatively chosen on this basis."
- 5/ "U.S. scrap exports increased from 6.3 million short tons in 1971 to 11.3 million in 1973 prior to the imposition of export controls. Controls will set the 1974 figure at 8.4 million short tons. See Department of Commerce Press Release No. 6-74-26, dated February 15, 1974."

Joffe contends that the explanation given above is not an accurate description of the process used by MarAd to set a minimum acceptable price for the six vessels. Joffe argues that the actual basis for rejection of its bid was set forth in a memorandum issued by MarAd's Chief, Division of Reserve Fleet, which was referred to in our prior decision as a memorandum of the meeting during which the minimum price for PD-X-971 was established. The memorandum reads in pertinent part:

"The lowest accepted price at the last bid opening (PD-X-970 opened 12/14/73) was \$30.24 per ton. Since that opening there has been an increase in the composite domestic price of No. 1 Heavy Melting Scrap Steel - from \$72.44 per ton to \$87.76 per ton (about 21%). There has been an increase in the Eastern Market price (Buffalo, Philadelphia and Pittsburgh) from \$71.00 to \$89.83 per ton (about 27%); Central Market price (Birmingham, Houston, Chicago and Cleveland) from \$75.50 to \$89.83 per ton (about 32%); and Western Market price (San Francisco, Los Angeles and Seattle) from \$70.83 to 73.83 per ton (about 4%) - [American Metal Market - 2/13/74].

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B-180789

"It has been noted that the price of scrap steel is approximately 18% higher in the Eastern Region and 26% higher in the Central Region than in the Western Region. However, from the analysis of bids in light of this situation, bids received on the * * * [6 vessels] from West Coast bidders were approximately 40% below the recommended accepted bids on the East Coast and therefore inadequate. It must be noted that in December 1973 (PD-X-987) we received approximately \$38.00 per ton for ships in the Western Region, at a time when the price of scrap steel was about \$63.00 per ton."

MarAd denies that the memorandum reflects the actual basis of MarAd's decision to reject the bids. The agency states that the award of vessels occurs only after a committee of three members of the MarAd Office of Domestic Shipping, in the presence of a member of the MarAd Office of General Counsel, develops a minimum price in accordance with the MarAd procedure described above. MarAd states that the memorandum was prepared before the committee met and contains the reasoning solely of its author and not the committee.

Joffe contends, however, that even under MarAd's established procedure, the decision to reject Joffe's bid as unreasonably low was erroneous for several reasons. First, Joffe submits that MarAd's procedure is predicated on the incorrect assumption that all surplus vessels being sold have the same value per ton regardless of their type or whether they are being sold as scrap or for nontransportation use. Joffe asserts that "the sales price of a vessel for nontransportation use is not indicative of its scrapping value." Joffe further asserts that price is effected by such things as the difficulty involved in the break-up of a particular vessel and the different types of equipment on the vessel.

Second, Joffe asserts that MarAd chose an improper measure of shipbreaking costs for the West Coast. MarAd had stated that in confirming a \$30 per ton rate as reasonable, it subtracted \$44.30 as the average shipbreaking cost for the West Coast and the \$30 per ton minimum acquisition price from a figure representing the domestic market value of scrap in order to determine if bidders could obtain a reasonable profit in the circumstances. Before the issuance of our prior decision, MarAd stated that the \$44.30 represented:

B-180789

"[t]he Office of Domestic Shipping's estimate of the present average cost, excluding bids, of scrapping a vessel in shipbreaking yards on the West Coast."

Subsequently, MarAd acknowledged that the \$44.30 figure was actually based on an estimate of one East Coast shipbreaker to which was added a 7% factor "for escalation" and a 15% factor "to cover the known higher labor costs that existed on the West Coast."

Joffe argues that this admission that \$44.30 was not an "average cost" and not based on the costs of shipbreakers on the West Coast indicates MarAd's bad faith. Moreover, Joffe points out that the use of an adjusted East Coast figure is an apparent contradiction of statements by MarAd to the effect that costs on the East Coast and West Coast cannot be compared. Joffe also suggests that the cost received from the East Coast shipbreaker reflected only direct labor charges and not overhead.

Finally, Joffe contends that MarAd acted improperly in considering potential domestic and Far East markets for scrap because of the speculative nature of those markets. According to Joffe, the domestic market is so volatile that predicting its potential levels necessarily involves a considerable amount of speculation, while the potential market in the Far East is even more speculative because of Government restrictions on the export of scrap iron. For example, Joffe points out that at the time of bid opening it had a quota of 4,000 tons for export for the first quarter of the year but that it did not know its quotas for future quarters. Joffe estimates that, if its quota were to remain constant, it would take a year and a half to export the scrap iron during which time the Far East market could change drastically.

MarAd disagrees with all of Joffe's contentions. For example, MarAd states that while it cannot verify that different equipment on various types of ships affects values, even the possibility that prices could be affected would not indicate that its evaluation was erroneous because the minimum sale price was established on the basis of scrap value alone, i. e., the vessel's lowest value to bidders, without regard to the possible higher value which a particular vessel might have because of its equipment. As for the intended use of a particular vessel, MarAd states that there is no evidence, despite Joffe's speculations,

B-180789

"* * *that vessels purchased for nontransportation use are being widely utilized or have substantial value for nontransportation purposes other than their residual scrap value. In fact, there is some evidence to suggest that nontransportation purchases, which carry no requirement to scrap the vessel within a specific time frame, are used by shipbreakers to build longterm raw material inventories."

With regard to its methodology for determining the minimum acceptable price, MarAd states that its evaluation process

"* * *assess[es] the present value of the vessels to the United States. Such present value is, and must be, determined in part on the basis [of] the ship's potential resale value over time. There are two basic reasons for this conclusion. First the sales authority directs that all relevant factors be taken into account in selling these vessels. 46 U.S.C. §§ 864 and 865. * * * As a careful seller, the United States must * * * attempt to assess the present potential of these ships as export scrap in its evaluation process because this market potential clearly affects the present value of the ships. The second reason is * * * if the statute did not require that all factors relevant to their value be considered in the vessels' sale, the agency could not responsibly administer sales in such a volatile market without considering the impact of prospective market price changes."

Moreover, MarAd states that it

"* * *knew that the vast majority of its shipbreaker bidders were purchasing its vessels for export in the rapidly ascending foreign scrap market. * * * the agency could and did rely on the rising foreign market prices for steel scrap in setting its minimum price at \$30 per long ton. * * * few if any shipbreakers were selling domestically when the bids in PD-X-971 were evaluated * * *. Rather, they were exporting scrap for about \$160.00 per long ton [the domestic price was between \$70.00 and \$80.00]."

B-1807A9

MarAd also points out that the domestic market continued to rise substantially in the months immediately following the opening of bids and that this provided a reasonable opportunity for profit for a bidder who had met the minimum price of \$30 per ton.

We have given careful consideration to the many arguments made by Joffe and MarAd, including some not deemed necessary or relevant to our disposition of this matter and which therefore are not set forth above. In so doing, we have taken into the account the various submissions considered in connection with our original decision as well as those submitted after reconsideration of that decision was requested. We have concluded, on the basis of this voluminous record, that our original decision should be affirmed in part and modified in part.

First of all, we do have some question with respect to how MarAd arrives at a minimum acceptable price. For example, we do not fully understand why, in this case, MarAd relied on an East Coast price estimate to establish a West Coast price. More importantly, since MarAd seems to concede the possibility that shipboard equipment could have an effect on the ship's value, it seems to us that MarAd's consideration of recent bidding history in tentatively determining minimum acceptable prices, without considering if the prices bid on particular ships in a prior sale might have been higher because of the value of the ships' equipment, could result in the establishment of an inflated minimum price for current sales.

Overall, however, we find that the record does not establish that MarAd acted arbitrarily or in bad faith in rejecting all bids or in establishing the minimum acceptable price. First, although MarAd and Joffe disagree as to the propriety of taking into account the type of ship being sold or the use to which it may be put when establishing the minimum acceptable price, Joffe has not conclusively established on this record that the position of MarAd, the agency charged by statute with the duty to sell ships and which in the discharge of that duty has acquired experience and expertise in the area, is incorrect. Neither has Joffe convincingly established that MarAd's failure to consider shipboard equipment rendered its minimum price determination unreasonable in this case.

Secondly, we cannot say that MarAd abused its broad discretion in considering potential foreign and domestic scrap markets. In this connection, we point out that Joffe misreads our cases dealing with surplus vessel disposal and use of speculative factors in evaluating bids. In B-16909(2), August 13, 1971, we said:

B-180789

"* * * we believe the floor price for sales to citizens should be determined on a current basis and include consideration of all relevant factors, including those specified in section 5 [48 U. S. C. 884]."

That statement was made in response to an assertion that MarAd was using a previously established floor price without regard to changed market conditions and was not meant to preclude MarAd's consideration of all currently relevant factors, including reasonably-based market projections. Although such projections may involve some degree of speculation, we do not believe that MarAd should be precluded from making those projections in light of the statutory guidelines adopted by MarAd for these sales which call for MarAd to consider "any other facts or conditions that would influence a prudent, solvent business man * * *." 48 U. S. C. § 884. Moreover, the cases cited by Joffe (e. g., 51 Comp. Gen. 645 (1972); 47 id. 233 (1967)) for the proposition that speculative factors may not be used in the evaluation of bids all involve the use of such factors to discern the low or most favorable bid and are not strictly applicable to the instant situation involving a determination of a fair and reasonable (minimum acceptable) price.

Third, even if the contracting officer initially might have contemplated making an award to Joffe--the record is not conclusive on this point--that would not establish that Joffe's bid was reasonable and that MarAd's minimum acceptable price was unreasonable. As indicated above, MarAd utilizes a committee to develop a minimum acceptable price. Since the record indicates that the price for this sale was determined after the time Joffe says the contracting officer had indicated that she was considering an award to Joffe, the contracting officer's alleged actions can only be regarded as premature and not indicative of bad faith on the part of MarAd in subsequently determining that the minimum acceptable price for the sale was \$30 per ton.

Accordingly, we affirm that portion of our decision relative to our conclusion that MarAd did not abuse its discretion in determining a minimum acceptable price.

Upon further reflection, however, we believe modification of the prior decision is warranted with respect to our conclusions regarding competitive bidding requirements. In our prior decision we noted that (1) a large number of bids are rejected as unreasonably low and that (2) a bidder who happens to bid on a vessel that must be disposed of promptly is awarded the vessel while other bidders who bid a higher price per ton on another vessel under the same solicitation may have their bids rejected as too

B-180769

low. We felt that this situation tended to undermine the integrity of the competitive bidding system and that competition would be served by establishing in advance the minimum acceptable price per ton for each ship and providing that information in the solicitation. Therefore, we concluded that the six vessels involved in the protest should be readvertised under a solicitation which disclosed the minimum acceptable price.

On reconsideration, we think it unlikely that pre-bid disclosure of the minimum price acceptable to MarAd will cure the problem at hand. The heart of the controversy concerns the reasonableness of MarAd's determination of minimum acceptable price. The protester's position is that MarAd arbitrarily rejected its high bids for these six surplus vessels because MarAd erroneously established, after receipt of bids, a single, unreasonably high, minimum sales price for the six vessels while MarAd, on the other hand, argues that the protester's bid prices for the vessels were unreasonably low. If, as the protester contends, MarAd's determination of minimum price is based on erroneous assumptions, little will be gained by requiring MarAd to disclose its minimum price prior to bidding. Thus, although pre-bid disclosure would place bidders on notice of what MarAd considers to be a minimum acceptable price and would therefore enable would-be bidders to avoid bidding in situations in which they were not interested in meeting MarAd's minimum price, it would not resolve the basic question of the reasonableness or arbitrariness of MarAd's minimum price determination.

Furthermore, subsequent to our initial decision in this case, we held that in the absence of a statute or regulation so requiring, an agency was not required to make available to bidders the appraised fair market value of land to be leased. Ramona Sutfin, B-180963, September 9, 1974, 74-2 CPD 155. Here, as in that case, and unlike situations involving the sale of Navy vessels, see 10 U. S. C. 7304(c)(1) (1970), the relevant statute contains no requirement that MarAd's appraisal be made public prior to the solicitation of bids.

Accordingly, we do not believe it appropriate for this Office to insist that MarAd disclose a vessel appraisal price in its sales solicitations and our decision is modified to that extent. However, we are still concerned, from a policy standpoint, over the high bid rejection rate and the other matters discussed in the previous decision. In view thereof, we are reiterating our recommendation, made to the Secretary of

B-180769

Commerce in connection with our prior decision, that MarAd consider taking into account the bidding history of vessels by type when making cost appraisements. We are also recommending that MarAd consider taking into account the effect of shipboard equipment on bidding levels.

In light of our concern in this area, MarAd's ship sales also will remain the subject of continuing audit interest.

Deputy


Comptroller General
of the United States