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DECISION

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

FILE: B-186940 DATE: December 9, 1976

MATTER OF: Honeywell Information Systems, Inc.

DIGEST:

1. Statement in "fixed-price options" clause of Federal Property Management Regulations § 101-32.408-5 to effect that "separate charges" (that is, penalty to be assessed against Government for non-exercise of option rights) may be quoted in certain data processing procurements is inappropriate and misleading to potential offerors in contracts funded with fiscal year appropriations.

2. Based on rationale employed in companion decision involving similar separate charges scheme, it is concluded that protesting offeror's proposed separate charges are violative of statutory restrictions on appropriations.

3. RFP's "fixed-price options" clause failed to inform offerors that certain charges may violate statutory restrictions; state how separate charges were to be specifically evaluated in determining whether charges made offer "unbalanced;" and warn as to how charges might improperly affect Government's flexibility in substituting equipment. Discussions with offeror did not cure failures nor give any indication that charges would be evaluated as ultimately done.

4. "Separate charges" cannot logically be added to base and option prices to determine successful offeror or to determine bid "unbalancing" since both prices and separate charges will not be paid--they are alternative in nature.

5. Because of analysis of deficiencies, recommendation is made that all offerors be afforded opportunity for another round of negotiations.

Honeywell Information Systems, Inc. (Honeywell), has protested the award of a fixed-priced contract to any other offeror under solicitation No. CDPA-75-13 issued by the General Services Administration

(GSA) on June 25, 1975, for "seven firm and one optional automatic data processing systems" to function as data processing service centers for the Department of the Navy. These eight centers will replace thirty-five existing, obsolete systems located throughout the United States. The contract, which will be funded with fiscal year appropriations, would ultimately be for a period of 96 months (if all GSA's option rights under the proposed contract are exercised). Since award under the RFP has not yet been made, our discussion of the facts involved must necessarily be restricted.

The protest arises out of GSA's evaluation of certain "separate charges" contained in Honeywell's best and final proposal submitted under the RFP. For the reasons discussed below, we are recommending that all offerors be afforded an opportunity to submit revised pricing proposals.

The RFP contained the "fixed-price options" clause required to be inserted in certain RFPs for data processing equipment and related procurements by Federal Property Management Regulation (FPMR) § 101-32.408-5, 41 CFR § 101-32.408-5 (1976), which provides:

> "When the Government has firm requirements for ADPE, software, or maintenance services which exceed the basic contract period (and quantity) to be awarded, but due to the unavailability of funds the option(s) cannot be exercised at the time of award of the basic contract (although there is a reasonable certainty that funds will be available thereafter to permit exercise of the options); realistic competition for the option periods (and quantity) is impracticable once the initial contract is awarded; and it is in the best interest of the Government to evaluate options in order to eliminate the possibility of a "buy-in," the * * * [fixed-price options] clause shall be inserted in solicitation documents."

The clause, essentially, informed offerors that:

(1) Fixed prices were to be proposed for the base period requirement plus all option requirements.

(2) Option prices would be evaluated in determining the successful offeror for the expected contract life--96 months if all options are exercised.

The clause went on to say:

> "Offers will be evaluated for purposes of award by adding the total price of all optional periods and, if applicable, all stated optional quantities to the total price for the initial contract period covering the initial systems or items. Separate charges, if any, which will incur to the Government should the latter fail to exercise the options, will not be considered in the evaluation, except as stated in II.2.3. below." (Emphasis supplied.)
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> "II.2.3. Unbalanced Prices
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> "An offer which is unbalanced as to prices for the basic and optional quantities may be rejected as nonresponsive. This will include an evaluation of the separate charges, if any, which will incur to the Government should the Government fail to exercise the option. An unbalanced offer is one which is based on prices significantly less than cost for some systems and/or items and prices which are significantly overstated for the other systems and/or items."

Both Honeywell and GSA agree that certain discussions took place concerning the meaning of the "separate charges" provision of this clause prior to the submission of Honeywell's best and final offer which contained the separate charges provision giving rise to the present controversy. GSA insists that "while these discussions were proceeding, Honeywell was fully informed that any separate charges proposed must be reasonable, that they must not operate to take away the Government's option not to renew and that they represented contingent liabilities which posed certain associated funding problems with the Navy." Honeywell admits that the skeletal outline ("percent of charge not indicated") of its "best and final," separate charges provision was "discussed at length" and that the "lawyer representing GSA [at the discussions] indicated that the clause would be a Go/No Go clause based on the reasonableness of the amounts in question."

After these discussions, Honeywell submitted its best and final proposal. The company's "best and final" prices were expressly based on the assumption that the entire contract period would be 96 months. The best and final proposal also contained an "Early Lease Discontinuance Charge" ("separate charge") which, in theory,

would be payable (with certain minor exceptions) to the contractor should GSA neither purchase nor retain on rental (for a specified minimum period of months--varying with the class of equipment involved) equipment which would be "ordered and installed." The separate charge was stated to be a percentage of the remaining monthly rental charges which would have otherwise accrued to Honeywell had the items remained on rental for the number of months specified.

Honeywell's final "separate charges" were evaluated on a "worst-case basis" under the following conditions:

> "These charges shall be additive to the systems life cost.
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> "They [the charges] shall be assessed effective one year from the date of installation of both initial and augmented equipment for each system * * *."

As a result of this directive, GSA and the Navy determined that Honeywell's separate charges "created an unbalanced offer" for the following reasons:

> "If the Government failed to exercise the option to renew the contract for the initial equipment ordered, the Government, for [some] * * * equipment, would pay discontinuance charges equal to * * *, the equivalent of two years' rent. Thus, the Government, in effect, would be paying three years' rent for one year of service. These charges were considered to be significantly overstated for the initial items. * * *
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> "Honeywell's separate charges were structured on discontinuances of individual units of equipment at any time during the systems life. Thus, they were continual throughout the life of the system and at varying prices for identical equipment, discontinued within the same fiscal year. The separate charges were designed to be assessed dependent on the date of installation and the date of discontinuance.
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> "As an example, equipment installed in year two and discontinued at the end of year three would result in a larger discontinuance charge than identical equipment installed in year one and discontinued at the end of year three, even though both units were discontinued in the same year and at the same time.

> "No discontinuance charges would be assessed for any equipment installed within five years prior to the expiration of 120 months from the award date and returned to Honeywell after 120 months, while at the same time, for identical equipment installed prior to that five years and discontinued within the last five years, discontinuance charges would be assessed."

GSA also decided that Honeywell's proposed separate charges "took away all of the Government's flexibility [as to increasing or decreasing a 'configuration' and to substitute equipment]" and learned that the Navy did not have sufficient funds available for obligation to cover the estimated "5.4 million dollars in separate charges" which might be incurred in fiscal year 1977 under the Honeywell scheme. Consequently, GSA is of the position that Honeywell's offer is not properly for acceptance.

Once Honeywell became aware of GSA's evaluation and position, the company submitted its protest. The company contends that GSA improperly evaluated the separate charges contained in its best and final proposal. Alternatively, Honeywell argues that the RFP provisions concerning separate charges do not contain any indication as to how these charges are to be evaluated, and that, in any event, GSA failed, during negotiations with the company, to convey appropriate information about the proposed evaluation of the separate charges scheme.

ANALYSIS

By companion decision of today in Burroughs Corporation, B-186313, we have concluded that the statement in the FPMR "fixed-price options" clause to the effect that separate charges may be quoted is inappropriate and misleading to potential offerors on contracts funded, as here, with fiscal year appropriations. We have so concluded because, among other deficiencies, the clause does not even suggest that certain separate charges cannot be funded under statutes (31 U.S.C. § 665(a); 31 U.S.C. § 712(a) and 41 U.S.C. § 11 (1970 ed.)) imposing restrictions on the use of fiscal year appropriations.

These statutes require that contracts executed under authority of fiscal year appropriations can be made only within the period of their obligation availability and must concern a bona fide need arising within fiscal availability. Leiter v. United States,

271 U.S. 204 (1926; Goodyear Tire and Rubber Company v United States, 276 U.S. 287 (1928); 48 Comp. Gen. 497 (1969); Burroughs Corporation, supra. In order to comply with the cited precedent and similar decisions (see, for example, 36 Comp. Gen. 683 (1957); 37 id. 155 (1957)), the charge, including "separate charges," for any good or service must reasonably relate to the value of the current fiscal year requirements which have actually been performed.

In construing a similar separate charges scheme proposed by Honeywell in its contract involved in the Burroughs decision we concluded:

> "* * * It seems apparent that the separate charges present in the Honeywell contract actually represent a part of the price of the ADP requirements for future years rather than merely current needs under the contract. Honeywell's "separate charges" penalty is clearly intended to recapitalize the contractor for its investment based upon a full 60 month systems life if the Government fails to continue to use the equipment. For example, if MESA were to terminate the contract in December 1976, Honeywell, under its separate charges scheme, would be entitled, in theory, to payment of a penalty equal to 30% of Honeywell's 'monthly list price' for the discontinued system equipment multiplied by 55 months--the then remaining intended contract life. An even more egregious example could have been demonstrated had MESA terminated the contract and paid the 'separate charges' in the first few weeks or months of the contract. If the Government were liable for the [separate charges] involved, it is apparent that the Government's option 'rights' under the Honeywell contract are essentially illusory * * *."

Under the same rationale expressed in the Burroughs decision, we conclude that the present Honeywell separate charges scheme is violative of statutory restrictions on appropriations.

On the other hand, in our Burroughs decision we upheld the propriety of certain separate charges so long as payment of the charges (including any payments already made for the service) "represents the reasonable value (e.g., ADP schedule price) of the actually performed work requirements at termination."

Nevertheless, because of our conclusion that the FPMR "fixed-price options" clause, incorporated in the RFP, does not even suggest that certain separate charges may run afoul of statutory restrictions on appropriations, it is our view that the clause in the subject RFP is deficient. The clause is deficient, moreover, because it does not state how the separate charges are to be evaluated. As we stated in our Burroughs decision:

> "* * * The clause states that separate charges for failing to exercise an option are only to be considered in determining whether an offer is 'unbalanced' as to price. But, although 'unbalancing' with regard to basic prices is defined in the clause, the specific mechanism for determining whether separate charges make an offer 'unbalanced' is nowhere indicated by the clause. Nor are there any objective or common guidelines and standards in the clause by which an offeror could reasonably determine whether its separate charges made its offer unacceptable. Faced with the existing clause, offerors are clearly unable to propose separate charges with any assurance that their offers would not be rejected because of 'unbalancing.' Cf. Mobilease Corporation, 54 Comp. Gen. 242, 246 (1974), 74-2 CPD 185; Standard Services Incorporated, B-182294, April 8, 1975, 75-1 CPD 212 * * *."

Moreover, contrary to GSA's views, we do not agree that the information given to Honeywell during discussions that the separate charges must be "reasonable," or the other advice given, cured the deficiencies inherent in the "fixed-price options" clause. This advice did not give Honeywell any concrete information as to objective guidelines to be used in determining whether proposed separate charges would be reasonable. Nor did the advice convey any indication that separate charges would be evaluated as ultimately directed by GSA (namely, by adding "worst-case" separate charges estimates to systems life cost), or that separate charges might

improperly affect the Government's flexibility in substituting equipment--yet another criticism of Honeywell's final separate charges proposal. Further, it is our view that separate charges cannot logically be added to base and option prices to determine the successful offeror or to determine "unbalancing," since both these prices and the separate charges will not be paid--they are alternative in nature.

Because of this analysis, we are recommending that GSA afford all offerors another round of negotiations. Should GSA still desire to allow any offeror the opportunity of quoting separate charges, the RFP's "fixed-price options" clause should be appropriately modified to specifically inform offerors that separate charges which exceed an appropriate ceiling--e.g. schedule prices, catalog prices at contract execution, or cost data--will be cause for the rejection of an offer (thereby eliminating GSA's felt need for a "worst-case" analysis approach). Also, specific guidance should be given as to how an offeror's separate charges might improperly affect the Government's flexibility to substitute equipment.

As this decision contains a recommendation for corrective action to be taken, it is being transmitted by letters of today to the congressional committees named in section 236 of the Legislative Reorganization Act of 1970, 31 U.S.C. § 1176 (1970), which requires the submission of written statements by the agency to the House and Senate Committees on Government Operations and Appropriations concerning the action taken with respect to our recommendation.

Deputy Comptroller General
of the United States