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Comptroller General
of the United States

United States General Accounting Office
Washington, DC 20548

Decision

Matter of: Imaging Systems Technology

File: B-283817.3

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DIGEST

Cancellation of solicitation based on a determination that in-house performance would cost the government less than contractor performance was improper where comparison of in-house and contractor performance was neither realistic nor fair.

DECISION

Imaging Systems Technology (IST) protests the cancellation of request for proposals (RFP) No. F04606-99-R-90052, issued by the Department of the Air Force for logistics support for the Programmable Indicator Data Processor (PIDP) air traffic control and landing system. The agency cancelled the solicitation based on a determination that performing the work in-house would result in cost savings. IST, the incumbent contractor, contends that the cancellation lacked a reasonable basis because the agency failed to conduct a realistic or fair comparison of the cost of in-house and contractor performance.

We sustain the protest.

The RFP, a total set-aside for small businesses, sought proposals to furnish all necessary resources required to provide logistics support for the PIDP system and peripheral equipment. The PIDP system is a standardized automated radar display, tracking, and flight data processing system used in the provision of air traffic control services at locations identified in the RFP, including dozens in the continental United States together with others as distant as Japan and Germany.

The logistics support covered by the RFP was defined in the "Work Description Document" to include depot-level repair, software engineering support, emergency on-site technical assistance, contingency assets (spares) procurement and management, configuration management and control, and logistics information reporting during performance of the contract. Other than a relatively minor "data item," the items whose prices were to be provided in proposals and evaluated as part of the award decision were items for which fixed labor rates were to be proposed.[1] RFP § B. The evaluated prices for those items (which together represented the great majority of the offerors' evaluated price) were calculated by multiplying the proposed hourly labor rates against the RFP's estimate of the number of hours the item would be needed. Id. § M-502. Those line items were telephone technical support (for which the RFP estimated 2,400 annual hours); depot-level support (estimate: 500 annual hours); and on-site emergency technical support (estimate: 500 annual hours). Id.

The RFP was issued on June 30, 1999; proposals were due on August 31. During the course of August, the Air Force decided (for reasons not relevant here) to review the need for any of the work covered by the RFP to be performed by a contractor, rather than brought in-house at Tinker Air Force Base. That review led to the conclusion that the contractor's work was either unnecessary or could be performed by [deleted] personnel at Tinker who were already working on software support.[2] Contracting Officer's Statement of Facts at 2. Overall, the Air Force concluded that the PIDP support effort no longer represented a significant workload, that the "low level of activity over the last few years does not justify the cost of a private contractor," and that any work that did remain could be performed by Air Force personnel at Tinker as "other duties as assigned." Id. at 4. This led to a decision to cancel the RFP and bring the work in-house at Tinker. Because of delays within the Air Force, the amendment cancelling the RFP was not issued until September 14, 1999. By then, however, two firms, including IST, had submitted proposals. Because of the cancellation, the Air Force decided not to open the proposals. Id.

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[1] Some items ("over and above expenses") were to be paid at prices negotiated during performance; others (travel and materials) were to be paid on a reimbursement basis.

[2] For example, Air Force officials concluded that, while the contractor staffed a toll-free telephone number that Air Force technicians could call with questions, the technicians might be calling the number merely out of convenience, so that, without that resource, they might be able to solve the problems on their own. Contracting Officer's Statement of Facts at 2. Furthermore, an Air Force logistics management specialist performed an analysis which indicated that the toll-free number was, in any event, not being used often, with approximately 180 calls per year since 1992. Id. at 3.

IST protested the cancellation to our Office. Among the various issues raised by the protester was the allegation that the cancellation violated 10 U.S.C. § 2462 (1994), because the agency had not performed a realistic and fair comparison of the cost of in-house and contractor performance. On January 6, 2000, the Air Force advised our Office that the agency intended to take corrective action. Specifically, the Air Force wrote that it intended "to more fully analyze and document the costs that would be incurred performing the solicited services in-house in comparison to the costs that would be incurred under a contract for those same services." Because of the Air Force decision to take corrective action, our Office dismissed the protest on January 12, 2000.

In an August 29, 2000, letter (received August 31), the Air Force advised IST that the agency had performed a cost comparison and decided to stand by its decision to cancel the RFP. The letter included a copy of the cost comparison, which was dated January 6, 2000 (the same date as the Air Force's notice to our Office of the intent to take corrective action). IST filed a protest with our Office on September 11.

The protester's core allegation is that the Air Force failed to ensure that all costs considered in the comparison of in-house and contractor performance were realistic and fair. The protester contends that this failure violates 10 U.S.C. § 2462(b) and the Federal Activities Inventory Reform (FAIR) Act of 1998, 31 U.S.C. § 501 note (Supp. IV 1998), and that, more generally, the agency improperly failed to follow the cost comparison process set out in Office of Management and Budget Circular A-76, as allegedly required by 32 C.F.R. Parts 169, 169a. With respect to the cost of contracting, the protester contends that the Air Force did not calculate those costs realistically or fairly since the agency never opened and reviewed IST's proposal; the contractor costs relied on were those under the predecessor contract which, IST argues, reflected somewhat different requirements. With respect to the cost of in-house performance, the protester argues that the cost figure included in the January 6 cost comparison was neither realistic nor fair, because it assumed all the work required by the RFP could be performed by [deleted] people, when, in the protester's view, it could not. In addition, IST contends that the costs of in-house performance did not include various elements allegedly required by Circular A-76 and the FAIR Act.

The Air Force contends that our Office lacks jurisdiction to consider the protest because the cancellation took place before the proposals were evaluated or even opened. As to the merits of the protest, the agency contends that the costs considered in the cost comparison were realistic and fair.

JURISDICTION

The Competition in Contracting Act of 1984 (CICA), 31 U.S.C. §§ 3551-56 (Supp. IV 1998), which forms the statutory basis for the procurement protest system under which we review the contracting actions of federal agencies, limits our review to

consideration of objections to solicitations, cancellations of solicitations, proposed awards, and awards of contracts for the procurement of property or services, and to terminations of such awards under limited circumstances. 31 U.S.C. § 3551(1) (1994). Thus, as the Air Force acknowledges, this Office has jurisdiction under CICA to review and decide objections to the cancellation of a solicitation.

CICA provides further that the Comptroller General shall decide protests "concerning an alleged violation of a procurement statute or regulation." 31 U.S.C. § 3552. Section 2462 of title 10 mandates that Department of Defense (DOD) agencies procure goods or services from a source in the private sector under specified circumstances, rather than from an agency source; therefore it is a procurement statute. As we noted in 1998, where a DOD agency issues a solicitation, receives and evaluates bids or proposals, and awards a contract, and then cancels the solicitation to take the work in-house, CICA grants us the authority to consider a protest that the agency did not comply with the requirements of 10 U.S.C. § 2462. Pemco Aeroplex, Inc., Aero Corp., B-275587.9 et al., June 29, 1998, 98-2 CPD ¶ 17 at 5-6. In the Pemco decision, we reserved judgment on whether we would have jurisdiction where a solicitation is cancelled prior to receipt and evaluation of proposals. Id. at 6 n.2. Here, we face a variant of that question, since the solicitation was cancelled after proposals were received, but before they were opened and evaluated. We conclude that we do have jurisdiction over IST's challenge to the cancellation of the RFP. Our jurisdiction to hear protests objecting to the cancellation of solicitations is not limited by CICA to situations where the cancellation occurred after proposals had been received or evaluated. In this case, therefore, we have jurisdiction to consider the propriety of the Air Force's decision to cancel the solicitation, including whether the effect of that decision--taking the PIDP work in-house--is consistent with 10 U.S.C. § 2462.

APPLICABLE LAW

Because, as discussed above, 10 U.S.C. § 2462 is a procurement statute that applies to DOD procurements of services, such as those being procured under the RFP, we conclude that the language in that statute governs here. Section 2462 provides:

> (a) In general.--Except as otherwise provided by law, the Secretary of Defense shall procure each supply or service necessary for or beneficial to the accomplishment of the authorized functions of the Department of Defense (other than functions which the Secretary of Defense determines must be performed by military or Government personnel) from a source in the private sector if such a source can provide such supply or service to the Department at a cost that is lower (after including any cost differential required by law, Executive order, or regulation) than the cost at which the Department can provide the same supply or service.

> (b) Realistic and fair cost comparisons.--For the purpose of determining whether to contract with a source in the private sector for the performance of a Department of Defense function on the basis of a comparison of the costs of procuring supplies or services from such a source with the costs of providing the same supplies or services by the Department of Defense, the Secretary of Defense shall ensure that all costs considered (including the costs of quality assurance, technical monitoring of the performance of such function, liability insurance, employee retirement and disability benefits, and all other overhead costs) are realistic and fair.

Under this statutory language, if a private-sector source can provide services that the Air Force needs at a cost that is lower than the cost of in-house performance, the Air Force must obtain the services from the private sector, unless the Secretary of Defense determines that the services must be obtained from military or government personnel. Since no such determination was made here, the key question becomes how to compare the cost of contractor and in-house performance. Much of the balance of this decision is devoted to a discussion of whether the Air Force's actions met the statutory requirement that the costs considered in the comparison be "realistic and fair." The Air Force agrees that this is the relevant question.[3] See Air Force Response to Protester's Comments (Nov. 9, 2000) at 1.

With respect to Circular A-76, there is generally no question as to the applicability of the Circular in bid protests, because the solicitations at issue have typically committed the agency to following the Circular's provisions in conducting a public/private cost comparison. In such a case, our Office, in considering whether the agency's action complied with Circular A-76, is assessing whether the agency followed the evaluation and source selection procedures incorporated into the solicitation. See, e.g., Trajen, Inc., B-284310, B-284310.2, Mar. 28, 2000, 2000 CPD ¶ 61 at 2. Here, there is no such solicitation provision. We recognize that Circular A-76 may well be mandatory within the executive branch as a matter of policy (so that the Air Force should have followed it here).[4] See Circular A-76 ¶ 7.a. ("Unless

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[3] Regarding the FAIR Act, we need not consider its applicability here, because its requirement for realistic and fair cost comparisons is virtually identical to the language in 10 U.S.C. § 2462 requiring that the costs compared be realistic and fair.

[4] The Air Force argues that Circular A-76's cost comparison requirements do not apply where the function involves fewer than 10 full-time equivalents (FTE), which the Air Force contends is the case here. As the protester points out, however, the 10-FTE exception for conversion to in-house performance applies only if the contracting officer determines that performance is unsatisfactory or that fair and reasonable prices cannot be otherwise obtained, which the record does not indicate occurred here (other than in the sense that the Air Force viewed any contract costs

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otherwise provided by law, this Circular and its Supplement shall apply to all executive agencies . . . ."). Nonetheless, in the absence of a solicitation reference to Circular A-76, we view compliance with the Circular as a matter of following executive branch policy; thus, an alleged failure to follow the Circular does not, in and of itself, constitute a valid basis of protest.[5] See Crown Healthcare Laundry Servs., Inc., B-270827, B-270827.2, Apr. 30, 1996, 96-1 CPD ¶ 207 at 3. Accordingly, we do not consider the protester's allegations regarding the failure to comply with Circular A-76.

REALISM AND FAIRNESS OF THE COSTS AND COST COMPARISON

In order to satisfy the standard of 10 U.S.C. § 2642, the Air Force needed to calculate the costs of in-house and contractor performance realistically and fairly. We set out in detail below the concerns that we have about the agency's calculation of both in-house and contractor performance costs. In addition, we view it as implicit in the requirement for a realistic and fair cost comparison that the Air Force needed to ensure that the costs compared were for essentially the same work. Our discussion below explains why, in our view, the cost comparison here did not meet that standard.

Cost of Contractor Performance

The Air Force's January 6, 2000, cost comparison found that the average annual cost of contractor performance was $438,754 (for a 5-year total of $2,193,772).[6] This was calculated by averaging the fixed and cost-reimbursement costs paid to the contractor (excluding material costs) each year over the 5 years of the predecessor contract.

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as unreasonable in comparison with zero costs for in-house performance). Circular No. A-76 Revised Supplemental Handbook, ch. 1, ¶ C.6.

[5] While IST argues that 32 C.F.R. Parts 169 and 169a establish a regulatory requirement for cost comparisons to be conducted pursuant to Circular A-76, we see no such requirement in those regulatory provisions. Weighing against allowing an alleged violation of the Circular to create a basis of protest is the explicit language in Circular A-76 stating that the Circular and its Supplement "shall not . . . [e]stablish and shall not be construed to create any substantive or procedural basis for anyone to challenge any agency action or inaction on the basis that such action or inaction was not in accordance with this Circular, except as specifically set forth in [sections not relevant here]." Circular A-76, ¶ 7.c.8.

[6] All the numbers here are rounded to the nearest dollar.

IST contends, and we agree, that the January 6, 2000, cost comparison was unrealistic and unfair in not taking into account the price proposals that were in the Air Force's possession. Once the Air Force had received the proposals in response to the RFP (IST's and another offeror's), in our view those proposals could not fairly be ignored in the Air Force's estimate of the price of contractor performance. IST contends that its proposed prices (with unit prices multiplied by the RFP's estimated quantities) amount to a total cost to the government of an annual average of [deleted] (for a 5-year total of [deleted]). IST's proposal noted that the firm had [deleted] reduced its prices from those under the predecessor contract. Protester's Comments, exh. 6, IST Proposal, at 27.

The Air Force does not dispute any of these numbers. Indeed, the agency concedes that IST's proposed prices are "[deleted] less than the cost of the previous contract" and that, when the proposed prices are compared with the Air Force's January 6, 2000 estimate of in-house cost, this "suggests" that contractor performance would cost the government less than in-house performance. Air Force Response to Protester's Comments (Nov. 9, 2000) at 2. While the Air Force, once it learned of the protester's proposed prices, proffered other reasons to defend its cost comparison conclusion (discussed below), we view it as essentially undisputed that the Air Force's estimate of the cost of contractor performance was unrealistically and unfairly high because it failed to take into account IST's proposed prices.

Cost of In-House Performance

With respect to the calculation of the cost of in-house performance, the Air Force has changed its position during the course of the protest. The one-page cost comparison dated January 6, 2000, itself included two different ways to calculate the in-house cost. On the one hand, it stated that [deleted] in-house individuals were able to absorb the work earlier performed by the contractor in addition to the other work they were performing; because the government would have to pay those employees' salaries whether they performed the extra work or not, those were "sunk costs," so that the real cost to the government of doing the previously contracted work in-house would be zero. On the other hand, the January 6 cost comparison identified the [deleted] salaries, totaling [deleted] per year (for a 5-year total of [deleted]), thus suggesting that this figure represented the cost of in-house performance.

Regarding the "sunk cost" argument, the protester contends that the fact that there is apparently excess staff capacity at Tinker Air Force Base does not mean that the time of in-house staff at Tinker can reasonably be considered cost-free for purposes of a cost comparison. Protester's Reply to Air Force Response (Nov. 15, 2000) at 4. We agree that, in a cost comparison, the fact that current government staff may be able to absorb work without extra hiring does not justify treating the staff's time as cost-free. Instead, we believe that the agency needs to estimate the percentage of the staff's time that will be taken up performing the work and multiply that

percentage by the overall cost of the staff (if the work will take up a de minimis portion of the staff's time, as the Air Force may be suggesting, the resulting cost figure will itself presumably be minimal). Cf. Circular A-76 Revised Supplemental Handbook, ch. 2, §§ B.5, B.6.

Regarding the number of in-house personnel needed to perform the work, the protester challenges the argument that [deleted] individuals could do all of the work required by the RFP. Among other things, the protester argues that, because of the need to take into account factors such as sick leave and annual leave, it is physically impossible for [deleted] individuals to provide the telephone coverage required by the RFP (24 hours a day, 365 days a year). The protester also points out that the in-house estimate includes only salary costs (the protester identifies a series of additional costs that it alleges should have been included), and that even the salary costs are improperly assumed not to increase over the 5 years of performance. While each of these points has merit, we need not address them in detail, because, once it learned that IST's proposed prices represented a cost to the government below the salary costs of the [deleted] individuals, the Air Force essentially abandoned the [deleted] salary basis of calculating in-house performance costs. Instead, the agency proffered a series of different arguments to defend its position. We address each in turn.

First, the Air Force disclosed that it had decided to reduce the scope of work from that set out in the RFP. In particular, after IST's contract ended in September 1999, the Air Force states, the agency reduced telephone coverage from 24 hours a day, 365 days a year to 8 hours a day, 5 days a week, and approximately 260 days a year. Air Force Response to Protester's Comments (Nov. 9, 2000) at 3. While the change in the scope of work affects the nature of the cost comparison between in-house and contractor performance (discussed below), we find no basis (nor has IST suggested any) to question the realism or reasonableness of the Air Force's definition of the scope of work needed.

Second, the Air Force concluded, based on its analysis of usage over recent years, that the services covered by the RFP were needed far less than the quantity estimates in the RFP indicated. In particular, while the RFP estimated 2,400 annual hours of telephone technical support, the Air Force reports that it now has only [deleted] handling all the calls, and that [deleted] receiving only three or four calls a week, each needing responses taking from a few minutes to several hours. Air Force Response to Protester's Comments (Nov. 9, 2000) at 4. Indeed, the Air Force contends that [deleted] performing all of the work previously performed by the contractor in approximately 40 percent of [deleted] work time. Id. The Air Force calculates that 40 percent of the [deleted] will represent [deleted] in fiscal year 2000. Id. Again, while we will address below concerns raised by the inconsistency between the RFP's estimate and the Air Force's current assessment of the number of

hours of telephone technical support, we find no basis (nor has IST suggested any) to question the realism or accuracy of the current assessment.[7]

Third, the Air Force decided not to count any costs for work being performed by Air Force personnel outside Tinker. For example, while the Air Force recognizes that emergency on-site engineering technical assistance is still needed, it did not include any costs for that work, because the work is "being performed on site by the Air Force Commands who may be the owners of the systems in question, on an as needed basis." Air Force Response to Protester's Comments (Nov. 9, 2000) at 3. For the same reason, the Air Force assumes zero cost for performing preventative maintenance on computer reprogramming and other equipment on a quarterly basis and for performing equipment performance serviceability checks upon completion of maintenance action in the field. We see no basis for treating the performance of work by Air Force personnel outside Tinker as cost-free to the government; doing so is neither realistic in terms of the actual cost to the government nor fair to the private-sector offerors. The protester contends that this category includes substantial amounts of work, such as hardware maintenance and emergency service. In our view, as with the time of the [deleted] at Tinker, the amount of time to be spent by the other Air Force personnel should be estimated and calculated in terms of percentages of the salary and other costs of the Air Force personnel expected to perform the work. Cf. Circular A-76 Revised Supplemental Handbook, ch. 2, §§ B.5, B.6.

Fourth, the Air Force contends that it no longer requires performance of some of the tasks listed in the RFP. These are items not separately priced by offerors and are generally requirements premised on the work being contracted out, so that it is undisputed that the items are not needed if the work is performed in-house (for example, the RFP required that the contractor designate a program manager). The protester does not dispute this aspect of the Air Force's calculation. It should be noted, however, that the contractor does not appear to have charged the government separately for any of these items.

In sum, we conclude that the estimate of the cost of in-house performance was unrealistically low for failure to include work performed by Air Force personnel at locations other than Tinker Air Force Base. The extent of the costs missing from the Air Force figure cannot be calculated on the present record.

[7] We note that the Air Force's use of 40 percent of [deleted], assuming [deleted] 40 percent of [deleted] time on this work, is in contrast to the Air Force's earlier "sunk cost" argument, which, as explained earlier, we find unreasonable.

Fairness of the Comparison

As discussed above, 10 U.S.C. § 2462 requires that an agency's cost comparison be realistic and fair. In both its January 6, 2000, cost comparison and its subsequent calculations, the Air Force has (1) failed to realistically determine the cost of in-house performance (by failing to include in its in-house estimate costs properly allocable to the requirement) and (2) failed to reasonably calculate the cost of contractor performance (by failing to consider the prices submitted by the offerors). In addition, the comparison between in-house and contractor performance was unfair, because the Air Force failed to compare the costs on the basis of a similar level of effort.

Specifically, as the analysis above shows, there are significant areas in which the cost comparison was not based on the same work effort for the in-house and contractor personnel. Essentially, the Air Force concluded that the quantity estimates in the RFP were unrealistically high, and calculated the cost of in-house performance based on more realistic, but much lower, quantity estimates. While the Air Force vigorously defends its current assessment of how little it needs the services covered by the RFP, that defense misses the point. In our view, the Air Force is not performing the realistic and fair cost comparison required by 10 U.S.C. § 2462 when it compares the cost of contractor performance of (to take the clearest example) 2,400 annual hours of telephone technical support to the cost of in-house performance of what will apparently be at most a few hundred hours of telephone technical support a year.[8]

Because of the lack of realism in the calculation of the cost of contractor and in-house performance and the lack of fairness in the cost comparison between the two, we conclude that the agency failed to comply with 10 U.S.C. § 2462, so that the cancellation of the RFP lacked a reasonable basis. Accordingly, we sustain the protest. We recommend that, consistent with the analysis set out above, the Air Force review its estimated costs of contractor and in-house performance, as well as the comparison between the two. If the agency's assessment is that its needs have changed as much as indicated during the course of the protest, we recommend that, prior to the cost comparison, the Air Force amend the solicitation to reflect the current assessment of the agency's needs, and then solicit revised proposals. We also recommend that IST be reimbursed the costs of filing and pursing its protest,

[8] Even the reduction of coverage from 24 hours a day, 365 days a year to coverage during what are apparently ordinary business hours may well mean that the contractor's costs (and therefore presumably its proposed prices) are unnecessarily high, due to the need to pay for coverage on holidays, nights, and weekends.

including reasonable attorneys' fees. Bid Protest Regulations, 4 C.F.R. § 21.8(d)(1). IST's certified claim for costs, detailing the time spent and the costs incurred, must be submitted to the agency within 60 days after receiving this decision.

The protest is sustained.

Anthony H. Gamboa
Acting General Counsel