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**United States General Accounting Office  
Washington, DC 20548**

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## **Decision**

**Matter of:** SAMS El Segundo, LLC

**File:** B-291620.3

**Date:** February 25, 2003

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Eric J. Marcotte, Esq., and Scott A. Schipma, Esq., Winston & Strawn; and Mark R. Hartney, Esq., Allen Matkins Leck Gamble & Mallory, for LA Air Force Base SMC, LLC, an intervenor.

John D. Inazu, Esq., and James A. Harley, Esq., Department of the Air Force, for the agency.

Louis A. Chiarella, Esq., and Christine S. Melody, Esq., Office of the General Counsel, GAO, participated in the preparation of the decision.

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### **DIGEST**

1. Reasonableness of agency's evaluation of offerors' proposed costs or prices is governed by the type of contract to be awarded.
  2. Protester's challenge that contracting agency improperly evaluated the prices proposed by the selected offeror is denied where the record shows that the evaluation was reasonable and consistent with the stated evaluation criteria.
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### **DECISION**

SAMS El Segundo, LLC (SES) protests the selection of LA Air Force Base SMC, LLC (Kearny) under a request for proposals (RFP) issued by the Space and Missile Systems Center (SMC), Air Force Space Command, Department of the Air Force, for the Systems Acquisition Management Support (SAMS) project.<sup>1</sup> SES argues that the agency's evaluation of Kearny's cost proposal was improper.

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<sup>1</sup> SES was alternatively known and referred to during the selection process as "Mar Ventures." Likewise, LA Air Force Base SMC, LLC, a joint venture comprised of Kearny Real Estate Company, Catellus Development Corp., and Morgan Stanley Real Estate Fund, was alternatively known and referred to during the selection process as "Team SMC," or "Kearny."

We deny the protest.

## BACKGROUND

Section 2861 of the Floyd D. Spence National Defense Authorization Act for Fiscal Year 2001 (the Act), Pub. L. No. 106-398, 114 Stat. 1654 (2000), authorizes the Secretary of the Air Force to convey, by sale or lease, all or part of the real property at Los Angeles Air Force Base (LAAFB), California; the Act also provides that the only consideration that the Air Force can receive for the conveyed real estate is “the design and construction on [unconveyed] property . . . of one or more facilities to consolidate the [SMC] mission and support functions.” As originally enacted, the statute also established that if the consideration received by the Air Force (i.e., the value of the facility constructed) exceeded the value of the real property conveyed, then the agency could “lease back” the facility from the developer for a period up to 10 years, with the Air Force taking title to the facility at the end of the lease period. Id. § 2861(c).

On July 17, 2001, the Air Force issued an RFP for the SAMS project. The initial RFP stated, in broad terms, the agency’s desire to exchange up to 57 acres of LAAFB real property for approximately 580,000 square feet of office space.<sup>2</sup> Phase I RFP at 3. The RFP also informed offerors that the selection process for the SAMS project would occur in three phases. In Phase I, the Air Force intended to select no more than five offerors who demonstrated the highest probability of success.<sup>3</sup> In Phase II, in which offerors were to submit detailed business and technical proposals for the actual execution of the SAMS project, the Air Force intended to select the offeror proposing the best value to the agency. Phase I RFP, app. D, SAMS Source Selection Process, at 4. In Phase III, the agency planned to conduct final negotiations with the selected offeror to finalize the remaining financial contingencies and to complete the administrative details of implementing all agreements for award to the selected offeror. The solicitation established that the Phase III negotiations would be

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<sup>2</sup> The RFP specified the parcels of real property that the Air Force planned to convey: approximately 42 acres in El Segundo, California (known as Area A); approximately 13 acres in Hawthorne, California (known as the Lawndale Annex); and approximately 3.7 acres in Sun Valley, California (known as the Armed Forces Radio and Television Service Broadcast Center). In return, the successful offeror would construct the new SAMS facilities on the remaining portion of LAAFB—approximately 52 acres in El Segundo, California (known as Area B). Phase I RFP at 4; see also Pub. L. No. 106-398, § 2861(a).

<sup>3</sup> The Phase I selection decision was based on two evaluation factors, in descending order of importance: past performance and preliminary project concept. Phase I RFP at 14.

“administrative in nature and [would] not encompass issues that affect the basis for the [Phase II] source selection decision.”<sup>4</sup> Id.

Six offerors submitted proposals in response to the Phase I RFP. Among the Phase I offerors selected by the Air Force for participation in Phase II were SES and Kearny.<sup>5</sup>

On January 24, 2002, the Air Force issued the Phase II RFP for the SAMS project, with its modified objective of exchanging up to 57 acres of LAAFB real property for approximately 560,000 square feet of office space at no additional cost. It is the competition under this solicitation that is the subject of this protest. The solicitation notified offerors that the basis for the Phase II selection decision would be “best value,” based on the integrated assessment of the evaluation factors, and could involve the tradeoff of cost and noncost factors. Phase II RFP at 9. The RFP identified the following evaluation factors, in descending order of importance, and subfactors, of equal importance within each factor:

1. Cost to the Air Force <sup>6</sup>	
2. Financial Strategy	
3. Facility Capability	
	A. Building Core and Shell
	B. Tenant Improvements
	C. Integration with Area B Facilities
4. Project Management	
	A. Project Execution Plan
	B. Project Management Team
5. Proposal Risk	
6. Past Performance	

Id. at 9-10. The solicitation expressed the relative importance of the cost factor by stating:

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<sup>4</sup> If, for whatever reason, the Air Force and the selected offeror were unable to complete Phase III negotiations within 90 days, then the agency could either reschedule the milestones or select a new offeror. Id.

<sup>5</sup> A third offeror selected by the agency for participation in Phase II, Lennar/Barker Pacific LLC, withdrew from the competition prior to the Phase II selection decision.

<sup>6</sup> The cost factor did not evaluate the total cost of the SAMS project, but rather, the additional cost to the Air Force (*i.e.*, the possible need to expend appropriated funds) over and above the value of the conveyed land in order to acquire the required facility. Agency Report (AR), Nov. 27, 2002, at 5; Contracting Officer’s Statement at 1. Accordingly, the parties also refer to cost as “cost gap,” or “gap.”

Affordability of the project is a major consideration of this source selection. The goal is to achieve no additional cost to the Air Force. Therefore, affordability is defined as the combination of “cost to the Air Force” and “financial strategy” employed by an offeror, which minimizes the additional funds the Air Force would have to provide.

NOTE: Funding for the SAMS project is not currently available; neither has it been programmed in the Air Force budget. Any requirement for funding, in addition to the land to be conveyed, is unattractive from a budgetary perspective.

Id. at 13.

Although termed “cost to the Air Force,” the agency contemplated that the cost gap set forth in an offeror’s Phase II proposal would in fact become the basis of a fixed-price contract between the selected offeror and agency for the construction of the proposed SAMS facility through Phase III administrative negotiations. The solicitation informed offerors that resolution of the Phase III administrative details and execution of the real estate agreements were contingent upon satisfactory evidence that the successful offeror had, among other things, “[o]btained a firm commitment for both construction and permanent financing, on the terms set forth in the Successful Offeror’s [Phase II] proposal . . . .” Phase II RFP, app. D, SAMS Source Selection Process, at 16. Additionally, at a hearing that our Office conducted on the protest, the person who served as both the Air Force chief evaluator and SAMS project manager testified that the Phase III negotiations would result in a fixed-price relationship between the parties, such that the agency’s liability was limited to the selected offeror’s Phase II cost gap. Hearing Transcript (Tr.) at 76-81.

Kearny and SES also both understood that an offeror’s proposed Phase II cost gap would subsequently become the basis of a fixed-price contract between the selected offeror and the Air Force. As part of its financial plan for the SAMS project, Kearny’s proposal was premised on the fact that the Air Force’s payment liability was limited to the offeror’s proposed cost gap. See AR, Tab 7, Kearny Final Proposal Revision, Vol. I, Executive Summary, at 4, Vol. II, Cost and Financial Strategy, at 2. Likewise, SES’s proposal stated, “SES proposes a Guaranteed Maximum Price format to offer the Air Force the benefits of a fixed-price contract as required under the solicitation . . . .” and “SES agrees to undertake the project at the specified price, and agrees that subject to [various land use and financing contingencies], SES guarantees the project performance at the stipulated cost.”<sup>7</sup> Supplemental AR, Tab 3, SES Final Proposal Revision, Executive Summary, at I-2.

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<sup>7</sup> While the proposals of both SES and Kearny use the expression “guaranteed maximum price (G-Max),” a construction industry term that refers to the maximum (or ceiling) cost for performing a specified project, see Agency’s Post-Hearing

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SES and Kearny each submitted initial Phase II proposals by the March 25 closing date, and final proposal revisions by the August 6 closing date. An Air Force source selection evaluation team (SSET) evaluated and rated the proposals as to the financial strategy, facility capability, project management, and past performance factors utilizing a color-coded descriptive rating system: blue (exceptional, or high confidence), green (very good, or significant confidence), yellow (satisfactory, or confidence), and red (marginal, or little confidence). Phase II RFP, app. D, SAMS Source Selection Process, at 9-12. The RFP also established that the proposal risk factor would be rated as high, moderate, or low, and that the cost factor would be evaluated for “completeness,” “reasonableness,” and “realism.” *Id.* at 12-14.

As set forth above in the discussion of the unique statutory framework of the SAMS project transaction, the Act established that if the value of the office facility to be constructed exceeded the value of the LAAFB real property conveyed, then one means by which the Air Force could overcome the cost gap was to “lease back” the facility from the developer for a period up to 10 years.<sup>8</sup> During Phase II, the Air Force observed that SES had submitted an alternate proposal in which the offeror’s financial strategy was contingent upon a 30-year leaseback period. On July 26, the Air Force formally suggested to the congressional representative for the district in which LAAFB is located certain “technical corrections” to the original Act, to include permitting a leaseback period of up to 30 years. AR, Tab 39, Letter from Air Force to Offerors Regarding Proposed Legislative Changes, at 2. At the time of both the agency’s final evaluation of proposals and the Phase II selection decision, however, the statutory changes sought by the Air Force for the SAMS project had yet to be enacted into law.<sup>9</sup>

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Comments at 5, the parties agree that the cost gap set forth in an offeror’s Phase II proposal would become the basis of a fixed-price contract between the selected offeror and agency as a result of Phase III administrative negotiations. Tr. at 85-86; Protester’s Comments, Jan. 23, 2003, at 16; Intervenor’s Post-Hearing Comments, Jan. 17, 2003, at 2, 5. The possibility that the agency would benefit from any actual contract performance cost savings would thus arise only if such an arrangement were set out in an offeror’s proposal, and was not required by the terms of the solicitation.

<sup>8</sup> Although not expressed in the Act, other options available to the Air Force to overcome a cost gap were to make total payment using appropriated funds to the selected offeror upon the completion of construction, or to reduce the size of the SAMS facility to be built.

<sup>9</sup> On December 2, subsequent to both the Air Force’s selection of Kearny and SES’s filing of its protest, the president signed into law the Bob Stump National Defense Authorization Act for Fiscal Year 2003, Pub. L. No. 107-314, 116 Stat. 2458 (2002),

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On August 20, the SSET briefed the agency source selection advisory council (SSAC) as to its evaluation and ratings of the proposals of Kearny and SES, which were as follows:

		<b>Factor</b>				
		Cost <sup>10</sup> (in millions)	Financial Strategy	Facility Capability	Project Management	Past Performance
<b>SES</b>		\$29 (10 yr lease) \$13 (30 yr lease)	Blue	Blue	Blue	Blue
	Risk (10 yr lease)		Moderate	Low	Low	N/A
	Risk (30 yr lease)		High	Low	Low	N/A
<b>Kearny</b>		\$13 (10 yr lease)	Green	Blue	Blue	Blue
	Risk		Moderate	Low	Low	N/A

AR, Tab 9, Briefing to the SSAC, at 15.

The SSET chairman informed the SSAC of his view that both offerors had submitted exceptional proposals that were substantially equal in terms of non-cost factors. AR, Nov. 27, 2002, at 7, Contracting Officer's Statement at 7; Tr. at 72. At the conclusion of the briefing, the SSET recommended that the agency's selection decision be based on existing statutory authorization, and therefore, that Kearny should be selected, as its cost gap was manageable and not contingent on potential legislative amendments. AR, Tab 9, Briefing to the SSAC, at 20-21.

On August 23, the SSAC (and SSET) briefed the agency source selection authority (SSA). While accepting the SSET's evaluations and ratings of the offerors' proposals, the SSAC chairman recommended the selection of SES contingent on enactment of 30-year leaseback authority (by the end of fiscal year 2002), and the selection of Kearny if the legislation did not pass.<sup>11</sup> AR, Tab 10, Briefing to the SSA, at 31, 33, 35.

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section 2841 of which revised the Act so as to permit leasebacks for up to 30 years for the SAMS project.

<sup>10</sup> The overall cost gaps for each proposal were rounded down to the nearest whole number as part of the SSET's briefing. Tr. at 191-94. Specifically, the cost gaps, which included a \$2 million management reserve, were \$13.1 million for Kearny's proposal, \$13.3 million for SES's 30-year lease proposal, and \$29.9 million for SES's 10-year lease proposal.

<sup>11</sup> The SSAC chairman believed that SES's superior design aesthetics for the SAMS facility, particularly a stand-alone conference center, made SES the best value

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The SSA did not immediately make a decision, believing that the selection of the recommended proposal, SES's 30-year leaseback proposal, would be premature and unsupported based on existing legislation. AR, Tab 43, SSA E-Mail Messages, at 1-2; Tr. at 217-18.

Subsequent to the briefing and prior to a source selection decision being made, certain events transpired. SES's proposal had included the idea of "swapping" a portion of one LAAFB-conveyed parcel for a slightly larger adjacent tract of land occupied by the Federal Aviation Administration (FAA).<sup>12</sup> On September 13 and 24, SES notified the contracting officer that the FAA land swap had fallen through, in whole or in part, because of the FAA's security concerns. AR, Tab 48, SES Letter Regarding FAA Land Swap; Tab 50, SES Clarification Letter Regarding FAA Land Swap. Consequently, the Air Force determined that the cost gap for SES's alternative proposals had increased to \$14.4 - \$14.9 million for the 30-year leaseback option, and \$30.9 million for the 10-year leaseback option. Additionally, as of the end of fiscal year 2002, Congress had yet to enact any change in SAMS project leaseback authority. As a result of the revision to SES's cost gap, and the fact that amended statutory authorization for the SAMS project had yet to be obtained, the SSAC chairman informed the SSA that he had changed his recommendation and now recommended the selection of Kearny. Tr. at 460-61.

On September 30, the SSA determined that the proposals of Kearny and SES were essentially equal as to all noncost factors, and that Kearny's proposal represented a lower overall cost to the Air Force. Based on an integrated assessment of all evaluation factors, the SSA determined that Kearny's proposal represented the best value to the Air Force. AR, Tab 12, Source Selection Decision, at 4. SES then protested to our Office.

#### EVALUATION OF KEARNY'S PROPOSAL AS TO COST

In its original and first supplemental protests, SES raised numerous issues that could be grouped into two categories. First, SES alleged in various ways that the agency's evaluation of Kearny's proposal, other than as to cost-related factors, was improper. Second, SES alleged that the agency's source selection decision was unreasonable and not in accord with the RFP's stated award scheme. We recently issued a decision denying these protests. SAMS El Segundo, LLC, B-291620, B-291620.2,

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among offerors that were otherwise equal as to cost and noncost factors.  
Tr. at 60-62, 244.

<sup>12</sup> SES planned to exchange 2 acres of conveyed LAAFB land, improved by SES with a single level 250-stall parking deck, to the FAA in return for 4 acres of FAA land, for a net value increase of \$1.6 million. Supplemental AR, Tab 3, SES Final Proposal Revision, Cost and Financial Strategy, at II-7.

Feb. 3, 2003, 2003 CPD ¶ \_\_. In a second supplemental protest, SES argued that the agency's evaluation of Kearny's proposal as to cost-related factors was unreasonable and inconsistent with the RFP's stated evaluation criteria. It is this second supplemental protest that is the subject of this decision.

The evaluation of proposals, including the evaluation of an offeror's proposed cost or price, is a matter within the contracting agency's discretion, since the agency is responsible for defining its needs and the best method for accommodating them. See U.S. Textiles, Inc., B-289685.3, Dec. 19, 2002, 2002 CPD ¶ 218 at 2. In reviewing a protest against an agency's evaluation of proposals, our Office will not reevaluate proposals, but instead will examine the record to determine whether the agency's judgment was reasonable and consistent with the stated evaluation criteria and applicable procurement statutes and regulations. See Shumaker Trucking & Excavating Contractors, Inc., B-290732, Sept. 25, 2002, 2002 CPD ¶ 169 at 3; Hydraulics Int'l, Inc., B-284684, B-284684.2, May 24, 2000, 2000 CPD ¶ 149 at 14. A protester's mere disagreement with the agency's judgment does not establish that the evaluation was unreasonable. C. Lawrence Constr. Co., Inc., B-287066, Mar. 30, 2001, 2001 CPD ¶ 70 at 4.

The reasonableness of an agency's cost or price evaluation is directly related to the financial risk that the government bears because of the contract type it has chosen. When an agency evaluates proposals for the award of a fixed-price contract, in which the government's liability is fixed and the contractor bears the risk and responsibility for the actual costs of performance, see Federal Acquisition Regulation (FAR) § 16.202-1, the analysis of an offeror's price need only determine that the price offered is fair and reasonable to the government (i.e., price reasonableness), and focuses primarily on whether the offered price is higher--as opposed to lower--than warranted. See CSE Constr., B-291268.2, Dec. 16, 2002, 2002 CPD ¶ 207 at 4; WorldTravelService, B-284155.3, Mar. 26, 2001, 2001 CPD ¶ 68 at 4 n.2. By contrast, when an agency evaluates proposals for the award of a cost-reimbursement contract, in which the government bears the risk and responsibility to pay the contractor its actual allowable costs regardless of the costs proposed by the offeror, see FAR § 16.301-1, the agency's analysis must also determine the realism of the offeror's proposed costs and what the costs are likely to be under the offeror's technical approach, assuming reasonable economy and efficiency (i.e., cost realism).<sup>13</sup> See

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<sup>13</sup> Likewise, a realism analysis is not ordinarily part of an agency's price evaluation because of the allocation of risk associated with a fixed-price contract. AST Env'tl., Inc., B-291567, Dec. 31, 2002, 2002 CPD ¶ 225 at 2. To the extent an agency elects to perform a price realism analysis in the competition for a fixed-price contract, its purpose is not to evaluate an offeror's price but to assess an offeror's risk or to measure an offeror's understanding of the solicitation's requirements. Id.; ENMAX Corp., B-281965, May 12, 1999, 99-1 CPD ¶ 102 at 9.

Pueblo Env'tl. Solution, LLC, B-291487, B-291487.2, Dec. 16, 2002, 2003 CPD ¶ 14 at 13; PADCO, Inc.--Costs, B-289096.3, May 3, 2002, 2002 CPD ¶ 135 at 5.

Our review of the record, including the written proposals, the pleadings, and testimony taken during the hearing in this matter, provides us no basis to find the agency's evaluation here was unreasonable or otherwise objectionable. We preface our discussion by briefly describing the contractual nature of the SAMS transaction and Kearny's proposal as to cost-related factors.

As set forth above, the SAMS project solicitation contemplated a three-phase selection process in which the cost gap set forth in an offeror's Phase II proposal would become the basis of a fixed-price contract between the selected offeror and the agency for the construction of the proposed SAMS facility through Phase III administrative negotiations. Specifically, during the Phase III "due diligence" period the selected offeror would determine if the various assumptions and contingencies encompassed within its proposal (e.g., obtaining entitlements for the specified uses of the conveyed properties, finalizing tax allocation and financing agreements with local municipalities) would be achieved.<sup>14</sup> Tr. at 78. Additionally, if the selected offeror determined that the land values and/or financing mechanisms it proposed in Phase II would not result in the anticipated overall funding amount, thereby creating a larger cost gap in comparison to the costs of construction, the offeror could either "absorb" the increased cost difference by increasing its equity contribution to the SAMS project or withdraw from the arrangement; the solicitation did not permit renegotiation of the cost gap. Id. at 79, 87; Phase II RFP, app. D, SAMS Source Selection Process, at 16. How the selected offeror attained the overall funding amount and cost gap as proposed in Phase II was solely the responsibility and the risk of the offeror. Tr. at 129-30. Quite simply, while the agency's Phase II source selection decision essentially constituted no more than "an agreement to agree," Tr. at 81, the Air Force's financial liability for the SAMS transaction project became determined (i.e., fixed) with the Phase II selection decision.

The Phase II RFP established three criteria for the evaluation of offerors' cost proposals--"completeness," "reasonableness," and "realism"--which the solicitation defined as follows:

Completeness: All information/data required to support the proposed financial strategy has been provided. Assumptions and estimates on which the strategy is based are clearly identified.

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<sup>14</sup> If the contingencies specified in its proposal could not be achieved, then the offeror had the right to withdraw from the arrangement. Tr. at 78.

Reasonableness: Cost estimates, financing terms, and financial projections are fully justified and supported and are considered fair under current market conditions.

Realism: Cost estimates and financial projections are compatible with proposed scope of effort and operations reflect reasonable economy and efficiency.

Phase II RFP, app. D, SAMS Source Selection Process, at 13-14. The RFP did not require the agency to perform a probable cost analysis or otherwise adjust an offeror's proposed cost gap as part of its evaluation. *Id.* Additionally, given the unique nature of the SAMS transaction--the simultaneous conveyance of real property in exchange for the acquisition of an office facility--the agency's evaluation here extended to "both sides" of an offeror's cost gap and examined not only an offeror's proposed construction costs, but also the various funding sources that the offeror contemplated as part of its financial strategy.

Kearny's final proposal revision included a 10-page cost and financial strategy, together with approximately 25 supporting exhibits, that described the amounts, assumptions, terms, conditions, contingencies, and calculations for its financial plan. In addition to the estimated value of the land which the agency would convey as part of the SAMS project transaction, the funding of Kearny's financial strategy was based on benefiting from tax increment financing, in the form of a Department of Housing and Urban Development (HUD) Section 108 loan, as well as a Brownfields Economic Redevelopment Initiative grant.<sup>15</sup> The SSET evaluated the individual elements as proposed in Kearny's financial strategy in determining that the offeror's overall cost gap was \$13 million, which was computed as follows:

<b>Costs &amp; Funding Sources</b>	<b>Amounts (in millions)</b>
Total Project Costs	\$115.5
Funding Sources-- Land Values	\$54.7
--Tax Increment Financing	\$47.7
--Brownfields Grant	\$2
-- <b>Total</b>	\$104.4
Cost Gap (Project Costs minus Funding Sources)	\$11.1
AF Management Reserve	\$2
Gap with AF Management Reserve	\$13.1

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<sup>15</sup> Tax increment financing refers to use of incremental, or additional, tax revenue (e.g., sales taxes, property taxes) that a development project would generate as the method by which to repay the loans used to finance the project's initial development. HUD Section 108 loans and Brownfields grants are explained later in this decision.

AR, Tab 9, Briefing to the SSAC, at 13.

As set forth above, following the evaluation of proposals, the SSA determined that Kearny's proposal represented the best value to the Air Force because of its lower overall cost among technically equal proposals. In his source selection decision, the SSA stated, "For the Cost factor, I evaluated the realism and reasonableness of the proposed amounts and established a probable cost for each offeror." AR, Tab 12, Source Selection Decision, at 1. The SSA acknowledges that he adopted the SSET's evaluation of Kearny's cost proposal and did not conduct his own independent assessment.<sup>16</sup> Tr. at 476, 493.

SES argues that the Air Force's evaluation of Kearny's cost proposal was both unreasonable and an improper departure from the stated evaluation criteria. Specifically, SES argues that, contrary to the RFP's cost evaluation criteria, the Air Force failed to conduct a proper evaluation of the realism and reasonableness (and as represented in the source selection decision, the probable cost) of Kearny's proposed cost. SES also argues that the Air Force improperly gave Kearny cost evaluation credit for various "artificially inflated" gap closure initiatives and simultaneously failed to assign a proposal risk rating of "high" to Kearny's financial strategy. According to SES, had the Air Force properly adjusted Kearny's cost gap upwards, then SES would have been selected as the best value offeror because of its lower cost gap. We disagree.

#### Nature of the SAMS Contractual Transaction

We are unpersuaded by the assertion underlying protester's various arguments--that because the Phase II selection decision did not itself create a fixed-price contract, the agency was required to perform cost realism and reasonableness analyses here. Protester's Comments, Jan. 23, 2003, at 1, 4-7. As previously detailed, the SAMS project transaction was to result in a fixed-price contract between the Air Force and the selected offeror, and it was the Phase II source selection decision that would determine the amount of the government's financial liability. Notwithstanding the "cost" and "cost gap" terminology, the agency's analysis of the amounts proposed by the offerors was, appropriately, in the nature of a price analysis, which, as defined by the RFP, was tailored to the unique nature of the SAMS project.

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<sup>16</sup> The Air Force also acknowledges that, contrary to the language of the source selection decision, no probable cost analysis was conducted as part of the evaluation of proposals. Tr. at 253-54. We find that there was neither a requirement nor a need for the agency to perform a probable cost analysis here; as discussed below, the SAMS project transaction was fixed-price in nature and the solicitation did not call for a probable cost analysis.

Again, when contemplating the award of a fixed-price contract, an agency need only analyze an offeror's price for reasonableness, see CSE Constr., supra, which the solicitation here defined as "fair under current market conditions." Phase II RFP, app. D, SAMS Source Selection Process, at 14. As applied to the SAMS transaction, the purpose of a price reasonableness review was to determine whether the offeror's "total project costs" were higher than warranted, and conversely, whether the offeror's planned funding sources were lower than warranted. Similarly, while the agency made a discretionary decision to conduct a realism analysis in its solicitation for the award of a fixed-price contract, see OMNIPLEX World Servs. Corp., B-291105, Nov. 6, 2002, 2002 CPD ¶ 199 at 9, the Phase II RFP stated that the agency's analysis here would focus on whether the "cost estimates, financing terms, and financial projections [were] compatible with [the] proposed scope of effort and operations reflect reasonable economy and efficiency."

We also find that the agency's "price" evaluation criteria, as defined by the RFP, were consistent with the multi-stage source selection process for the SAMS project transaction. It is important to reiterate that the Phase II evaluation of proposals would itself not result in a contract between the selected offeror and the Air Force. Instead, it was to be followed by the Phase III due diligence period in which the selected offeror would determine if the various contingencies within its proposal, when it was but one of several potential developers for the project, were achievable when it became the exclusive offeror selected by the Air Force. Therefore, the purpose of the agency's analysis of the amounts proposed by the offerors, especially with regard to planned funding sources, was to guard against the selection of an offeror whose unrealistic financial proposal subsequently prevented the offeror from successfully concluding the Phase III due diligence period.<sup>17</sup> Tr. at 82. For that reason, the agency's analysis of the amounts proposed by both Kearny and SES in Phase II was to determine if the individual elements comprising each offeror's financial strategy were also reasonable and achievable.

#### Reasonableness of Agency's Evaluation

SES contends that the agency's analysis of Kearny's proposed amounts, specifically, the \$47.7 million HUD Section 108 loan and \$2 million Brownfields grant, was unreasonable in light of various artificially inflated gap closure initiatives: (1) the unrealistic assumption that the City of El Segundo would agree to forgo all incremental tax revenue; (2) the total proposed HUD Section 108 loan amount which both the overall number of jobs and the actual number of new jobs planned by Kearny did not support; and (3) the proposed Brownfields grant as a gap-closing

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<sup>17</sup> The risk to the Air Force if the selected offeror's financial plan proved unworkable was not that it would have to accept a larger cost gap; the risk to the agency was the loss of time associated with having to then conduct Phase III negotiations with a second offeror. Tr. at 81-82, 129-30.

measure when it would be used for the repayment of the HUD loan. Based on our review of the record, including testimony by the agency evaluators at the hearing on the protests conducted by our Office,<sup>18</sup> we find the agency's analysis of Kearny's proposal unobjectionable.

Created by the Housing and Community Development Act of 1974 and administered by HUD, the Community Development Block Grants (CDBG) program is a major source of federal financial aid to cities and urban counties. 42 U.S.C. § 5301(c) (2000). The broad purpose of the CDBG program is to improve the quality of urban life, particularly for people of modest financial means, through better housing and enhanced economic opportunity. One specific aspect of the CDBG program is the HUD Section 108 loan guarantee program. 42 U.S.C. § 5308(a); 24 C.F.R. § 570.700 *et seq.* (2002). It allows local governments to transform a small portion of their CDBG funds into federally guaranteed loans large enough to pursue physical and economic revitalization projects that can renew entire neighborhoods. HUD Section 108 loans provide communities with a source of financing for economic development, housing rehabilitation, public facilities, and large-scale physical development projects. See <http://www.hud.gov/offices/cpd/communitydevelopment/programs/108/index.cfm>.

The size of a HUD Section 108 loan that an eligible applicant (*e.g.*, cities and urban counties) may apply for and receive is dependent upon numerous variables and qualifications. Among the variables, the ones relevant to this protest are (1) the amount of incremental taxes that would be generated by Kearny's proposed development project and available for repayment of the HUD Section 108 loan, and (2) the number of new jobs that Kearny's development project would generate for low- and moderate-income individuals.

As part of its tax increment financing plan (the \$47.7 million HUD Section 108 loan), Kearny estimated that the amount of incremental tax revenue that would be generated from the planned commercial and residential development of the conveyed properties was a total of \$4.3 million annually. AR, Tab 7, Kearny Final Proposal Revision, Vol. II, Cost and Financial Strategy, at 6. In determining this amount, Kearny analyzed the sales projections per square foot of retailers who expressed interest in opening stores on the conveyed property (*e.g.*, Ikea, Fry's Electronics, Kohl's Department Store), the sales taxes that would result therefrom, and "expanded" these numbers into future values when the sales taxes would

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<sup>18</sup> Post-protest explanations that provide a detailed rationale for contemporaneous conclusions, as is the case here, simply fill in previously unrecorded details, and will generally be considered in our review of the rationality of evaluation and selection decisions, so long as those explanations are credible and consistent with the contemporaneous record. Jason Assocs. Corp., B-278689 et al., Mar. 2, 1998, 98-1 CPD ¶ 67 at 6.

actually occur.<sup>19</sup> Kearny's proposal explained that a pledge of the incremental property, sales, and utility taxes by Los Angeles County and the cities of El Segundo and Hawthorne in support of a HUD Section 108 loan would generate net bond proceeds of \$47.7 million. *Id.* at 7. Kearny's proposal also stated that while it had previously taken into consideration a deduction of \$300,000 from incremental tax revenues by the City of El Segundo for services, it deleted the City of El Segundo "hold back" from its final proposal. *Id.*

In evaluating Kearny's proposal as to cost and financial strategy factors, the SSET realized that Kearny's tax increment financing plan included the assumption that the City of El Segundo would forgo all incremental tax revenues. The SSET in fact noted, "The El Segundo City staff is not comfortable with the city reimbursements dropping from \$300K to 0. Although this may be feasible, El Segundo needs to make this decision, and \$3-4 [million] of the \$47.7 [million HUD Section 108 loan] may be in jeopardy." Supplemental AR, Tab 4, Evaluation Assessment 240, Sept. 4, 2002. At the same time, the person who served as both the SSET chief evaluator and SAMS project manager met with the mayor of the City of El Segundo, who expressed his willingness to forgo all incremental tax revenues in order to enhance the viability of the SAMS project.<sup>20</sup> Tr. at 122-23. The mayor also determined that no hold back of incremental tax revenue was necessary because the proposed development would not necessitate additional municipal services (e.g., fire protection, police protection). Tr. at 122, 127. As the El Segundo mayor, "being the one who runs the city," had essentially overruled the city staff here, the SSET determined that Kearny's assumption that all incremental tax revenue was available to support repayment of the HUD Section 108 loan was a reasonable one. Tr. at 125, 127-28. We see no reason to conclude that the agency's determination in this regard was unreasonable.<sup>21</sup>

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<sup>19</sup> SES does not challenge Kearny's gross incremental tax revenue estimates.

<sup>20</sup> The City of El Segundo mayor also made similar comments publicly; to the Homeowners Association of El Segundo, he stated that "we need to do what we have to do to make this project viable and save our Air Force Base, and if that means giving up the revenue, I'm willing to give up all the revenues." Tr. at 126.

<sup>21</sup> SES also protests the agency's unequal treatment of offerors with respect to the evaluation of the amount of incremental tax revenue that the City of El Segundo would withhold or forgo: while Kearny's final proposal assumed that the city would forgo all incremental taxes, SES's proposal estimated that the city would withhold \$330,000 of incremental taxes annually. We find SES's protest on this ground untimely because SES knew or should have known of this basis for protest when it received the initial agency report on November 27, and failed to protest this issue within 10 days thereof. 4 C.F.R. § 21.2(a)(2) (2002). In any event, the fact that competing offerors made different assumptions about an aspect common to their proposals does not by itself constitute unequal treatment by the contracting agency.

Also as part of its tax increment financing plan, Kearny's proposal set forth how it would meet the job creation and benefit tests applicable to HUD Section 108 loans. See 24 C.F.R. § 570.208(a)(4), § 570.209(b)(2), (3). Kearny estimated that a total of 1,322 new jobs primarily benefiting low- and moderate-income persons would be created as part of its development plan. Supplemental AR, Tab 21, Briggs Letter to Kearny, Aug. 15, 2002, at 1. In making this determination Kearny examined national standards for job creation for retail businesses such as the ones that had expressed interest in opening stores on the conveyed property. Kearny's proposal also explained how its planned HUD Section 108 loan met the applicable benefit test. Specifically, based upon an overall loan amount of \$47.7 million and the estimated 1,322 new jobs, the loan amount per new job created averaged \$36,082. This amount met the regulation's "individual activity standards" of not more than \$50,000 per new job created, and "virtually met" the regulation's "aggregate standards" for all Los Angeles County CDBG projects of not more than \$35,000 per job created. *Id.* at 2.

The SSET also examined this aspect of Kearny's proposal in assessing the offeror's proposed tax increment financing amount. In its evaluation worksheets the SSET noted:

HUD will grant \$35,000[] for every 1 job generated in the project. The Offeror projects 1322 jobs will be created which will only generate \$46.3 [million]. So already their HUD projection [of \$47.7 million] is too high, but it could be even lower if their estimate of the number of jobs created is too high. After talking with HUD officials, they are concerned that such companies as Fry's and Ikea may just be transferring jobs when closing down their stores at their current location, instead of creating new jobs. A job transfer contributes little if any money available for the grant.

Supplemental AR, Tab 4, Evaluation Assessment 240, Sept. 4, 2002. The agency evaluators in fact met with and talked to both HUD and Los Angeles County officials on multiple occasions to aid in the agency's evaluation of Kearny's proposed HUD Section 108 loan. Tr. at 273, 428. While the Air Force had consultants with some relevant experience here, the SSET relied heavily on the opinions of HUD officials involved in the actual review and approval of Section 108 loans as proposed by Kearny. *Id.* at 282-83. Notwithstanding their concerns regarding new (versus transferred) jobs, HUD officials informed the SSET of their belief that both Kearny's estimated job creation and the resulting \$47.7 million HUD Section 108 loan amount appeared reasonable.<sup>22</sup> *Id.* at 274, 277. The SSET then determined that while there was risk associated with Kearny's tax increment financing strategy (thereby resulting

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<sup>22</sup> HUD officials also mentioned that the SAMS project would probably qualify for Section 108 loans based on job retention of Air Force and aerospace jobs within the South Los Angeles Bay area. Tr. at 274, 281.

in a “moderate” risk rating as to Kearny’s financial strategy), there were also many different combinations that would result in the overall amount proposed, and found Kearny’s proposal in this regard reasonable. *Id.* at 274-75, 280-81. Once again, while SES may disagree with the agency’s judgment regarding this aspect of Kearny’s proposal, we see no basis to question it. The agency’s decision was based on a full consideration of information relevant to the assumptions underlying Kearny’s proposal, and, in an appropriate exercise of its judgment, the agency concluded that this aspect of the proposal was reasonable.<sup>23</sup>

In addition to the HUD Section 108 loan, Kearny’s financial strategy also included a \$2 million Brownfields grant. A “brownfield site” refers to “real property, the expansion, redevelopment, or reuse of which may be complicated by the presence or potential presence of a hazardous substance, pollutant, or contaminant.” 42 U.S.C.A. § 9601(39)(A) (2002). Administered by HUD, Brownfields Economic Redevelopment Initiative grants are federal funds whose general purpose is to assist states and local communities with the economic redevelopment and reuse of brownfield sites. Brownfields grants can be used in a number of ways: they can be used to pay various predevelopment costs (e.g., demolition expenses) of a HUD Section 108-funded project, as a loan loss reserve in lieu of CDBG funds, to reduce the loan’s interest rate, or to establish a debt service reserve. AR, Tab 7, Kearny Final Proposal Revision, Vol. II, Cost and Financial Strategy, exh. S, Briggs Letter to Kearny; <http://www.hud.gov/offices/cpd/communitydevelopment/programs/108/index.cfm>.

As part of the initial Phase II proposal, Kearny’s cost and financial strategy stated, generally, that up to \$2 million of Brownfields grant funds were available and could be used by local municipalities to provide a “cushion” for the interest payments on HUD Section 108 loans. AR, Tab 7, Kearny Initial Proposal, Vol. II, Cost and Financial Strategy, at 6. The imprecise nature of Kearny’s proposal here was a subject of the discussions that the agency held with the offeror. Tr. at 311-13, 321. The SSET was also aware that how the \$2 million Brownfields grant would be utilized would affect the offeror’s cost gap. Specifically, if the grant was used as a reserve for the project’s HUD Section 108 loan, then it should not be used in computing the offeror’s cost. By contrast, if the grant was used by the offeror to pay predevelopment costs, then it could be counted in computing the offeror’s cost gap.

While Kearny’s final proposal revision did not alter its original proposal’s narrative language, the exhibits attached to the offeror’s cost and financial strategy indicated that the \$2 million Brownfields grant would not be used for the repayment of the HUD Section 108 loans but instead would be used by Kearny to pay predevelopment

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<sup>23</sup> While SES also protests that the Air Force failed to evaluate an alternative tax increment financing plan (consisting of revenue bonds) proposed by Kearny, we need not address this challenge in light of our conclusion that the agency’s evaluation of Kearny’s HUD Section 108 loan financing plan was reasonable.

expenses. AR, Tab 7, Kearny Final Proposal Revision, Vol. II, Cost and Financial Strategy, at 7, exh. T, Kearny Detailed Sources and Uses of Funds, exh. V, Kearny Statement of Operating Sources and Uses of Funds. Additionally, during discussions the offeror informed the agency of its intent to use the Brownfields grant for the demolition of existing structures on the conveyed LAAFB parcels. Tr. at 314. Based both on Kearny's representations during discussions and the exhibits included with the offeror's final proposal revision, the SSET determined that Kearny's financial strategy planned on the use of the Brownfields grant for predevelopment costs. Id. at 313-14, 321.

Based on its consideration of Kearny's proposal as a whole, we think it was reasonable for the agency to interpret the proposal as offering to use the Brownfields grant for predevelopment costs. Consequently, we find the agency's subsequent determination to count Kearny's \$2 million proposed Brownfields grant in the computation of the offeror's cost gap was also reasonable and consistent with the RFP's evaluation criteria.

In sum, having determined that the agency's evaluation of Kearny's proposal as to the cost factor (as well as financial strategy risk) was reasonable and consistent with the stated evaluation criteria here, we find no basis to disturb the resulting Air Force source selection decision for Phase II of the SAMS project.

The protest is denied.

Anthony H. Gamboa  
General Counsel