

DECISION

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

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97200

FILE: B-182882

DATE: June 12, 1975

MATTER OF: Wheeler Brothers, Inc.

DIGEST:

Parts procurement IFB clause which provides that, under cost-reimbursement segment of contract, contractor will not be able to furnish parts to Government at price which includes markup from affiliates is unduly restrictive and unreasonably derived, since provision would reduce likelihood that contractor would buy from affiliates and ASPR guidelines recognize affiliates entitlement to recover more than cost in comparable situations where there is price competition as clause contemplates.

The subject protest concerns invitation for bids (IFB) F65501-75-0-9030, which was issued by Elmendorf Air Force Base for a contractor-operated on-base automotive parts store (COPARS).

Award is to be made to the responsive, responsible bidder who submits the lowest total price for price listed auto parts and operation of the COPAR store during the estimated number of nonduty hours.

The contract also will require the successful bidder to supply nonprice listed items "* * *" at the contractor's net invoice cost after prompt payment discount and any applicable prorated share of supplier's volume rebate, plus the service charge shown below plus transportation charges. The amount of the monthly service charge paid will be determined by the amount of the contractor's net invoice cost after prompt payment discount as follows:

"MONTHLY DOLLAR COST

\$ 100.01 -	\$ 500.00
500.01 -	1,000.00
1,000.01 -	2,000.00
2,000.01 -	3,500.00
3,500.01 -	5,000.00
5,000.01 -	6,500.00

SERVICE CHARGE

\$ 50.00
100.00
200.00
300.00
400.00
500.00

"MONTHLY DOLLAR COSTSERVICE CHARGE

\$ 6,500.01 - 8,000.00	\$ 600.00
8,000.01 - 10,000.00	700.00
10,000.01 - 12,000.00	800.00
12,000.01 - 16,000.00	1,000.00
16,000.01 - 18,000.00	1,100.00
18,000.01 - 20,000.00	1,200.00
20,000.01 - AND OVER	1,300.00"

Clause SP J-18b of the original IFB stated that:

"b. Sales or transfer of parts between a parent company and/or subsidiaries or affiliates in which the COPARS contractor (or principals of the company) has a financial interest, which increases the price to the Government beyond the price which the COPARS contractor would normally expect to pay if the item was purchased at the best price obtainable elsewhere in the market place, is prohibited. In cases which involve the sale or transfer of parts between a parent company and/or subsidiaries or affiliates which the COPARS contractor (or principals of the company) has a financial interest, the Contractor will furnish proof that any item(s) was purchased at the best price obtainable elsewhere in the market place, when deemed necessary by the Contracting Officer."

However, per IFB amendment No. -M01, dated November 20, 1974, clause SP J-18b was deleted in its entirety and replaced by a new clause. SP J-18 now reads in pertinent part:

"SP J-18. OBTAINING NON-PRICE LISTED (NPL) PARTS.

"a. Except as provided in SP J-15c, the COPARS contractor will procure all NPL parts from the manufacturer, or from the highest level in the manufacturer's distribution system which he has access to which will provide the lowest price that is obtainable by the COPARS contractor in the normal course of business. When determined necessary by the Contracting Officer, the contractor will be required to provide evidence that the supplier of NPL parts is in fact an authorized member of the manufacturer's distribution system. The contractor's proposed source of supply, and estimated cost, must be approved by the Contracting Officer prior to obtaining parts when the estimated price

of any one item exceeds \$500 or a group of items to a single source is estimated to exceed \$1,000.

"b. In cases which involve the sale or transfer of parts between a parent company and/or subsidiaries or affiliates which the Contractor (or principals of the company) has a financial interest, the affected NPL parts will be furnished to the Government without any mark-up in the net cost of the item from the supplier to the contractor or the affiliate. The contractor shall furnish proof that any item(s) was furnished to the Government at the net invoice cost to the Contractor or affiliate, when deemed necessary by the Contracting Officer. It is not the intent of the contract to allow either the contractor or any affiliate involved in the performance of this contract, to realize a monetary profit from (or increase the cost of) NPL parts being furnished to the Government under this contract. (See Part I, Section B, Para 10 concerning required affidavit. Also, see E-2, SPJ-1; and SPJ-22 concerning payment for NPL parts)

"c. In order to satisfy the requirements of SP J-18a and b above, the Contracting Officer may require the Contractor to furnish a minimum of two proposed sources of supply (before purchase) for one item estimated to exceed \$500 or a group of items to a single source estimated to exceed \$1,000, for approval. * * *"
(Emphasis added.)

Wheeler Brothers, on behalf of itself and its affiliate, Murdock Enterprises Incorporated, protests against the inclusion of clause SP J-18b, as amended, contending that the clause is unduly restrictive of competition. Indeed, it is stated that if SP J-18b, as amended, is utilized, should Wheeler Brothers be the successful bidder, it would effectively be precluded from buying NPL parts from Murdock since Murdock's profit would not be an allowable cost to the prime contract. This fact would occur even though Murdock's price (even including profit) for a given item might have been the lowest price at which Wheeler Brothers could have obtained the part.

The protester thus contends that SP J-18b, as amended, will cause the Government to pay more for NPL parts in that a prime contractor (such as Wheeler Brothers) would not necessarily be able to obtain a given part at the lowest price available if the lowest price was quoted by an affiliate. The results of SP J-18b, as amended, it is contended, are that affiliate suppliers are essentially eliminated as potential sources of supply while in return the Government may pay the same or, more likely, higher prices for NPL parts.

The Air Force states that the NPL portion of the contract is essentially a cost-reimbursement segment of what otherwise is a fixed-price contract. It states that since the NPL portion is not evaluated and there is no basis for competition in the NPL portion of the solicitation, it cannot be restrictive of competition.

We do not agree. By disallowing from the prime's cost the profit of potential subcontractor materialmen who happen to be affiliates of the COPARS operator, competition for the supply of NPL parts has been lessened since it would reduce the likelihood that a COPARS operator would buy from its affiliate under those circumstances. Similarly, it is not likely that an affiliate supplier would sell to the COPARS operator at cost if it had an established practice of charging a profit.

While it must be recognized that almost every clause placed in an IFB may in some way be restrictive of competition, the question presented here is whether clause SP J-18b, as amended, is unduly restrictive of competition. In that connection:

"Our Office has consistently stated that specifications should be drawn to maximize competition. B-178158, May 23, 1973; B-172006, June 30, 1972. Moreover, we will not interpose our judgment for that of the agency's even when competition is reduced '* * * unless there is clear and convincing evidence that the agency opinion is in error and that a contract awarded on the basis of such specifications would, by unduly restricting competition * * *, be a violation of law.' (Emphasis added.) 40 Comp. Gen. 294, 297 (1960); B-178158, supra; see 49 id. 156 (1969) and 17 id. 554 (1938). * * *" Winslow Associates, 53 Comp. Gen. 478 (1974).

Clause SP J-18b, as amended, sets out the method for determination of prices. Accordingly, we agree with the agency that the cost principles of ASPR § 15-000, et seq., are not directly applicable. The agency does, however, state that "such principles do provide guidelines in determining the appropriateness of allowing or disallowing affiliate profit on sales or transfers between affiliates."

ASPR § 15-205.22 (1974 ed.) states in pertinent part:

"(e) Allowance for all materials, supplies and services which are sold or transferred between any division, subsidiary or affiliate of the contractor under a common control shall be on the basis of cost incurred in accordance with this Part 2, except that when it is the established practice of the transferring organization to price interorganization transfers of materials, supplies and services at other than cost for commercial work of the contractor or any division, subsidiary or affiliate of the contractor under a common control, allowance may be at a price when:

"(i) it is or is based on an 'established catalog or market price of commercial items sold in substantial quantities to the general public' in accordance with 3-807.1(b)(2); or

"(ii) it is the result of 'adequate price competition' in accordance with 3-807.1(b)(1)a and b (i) and (ii), and is the price at which an award was made to the affiliated organization after obtaining quotations on an equal basis from such organization and one or more outside sources which normally produce the item or its equivalent in significant quantity;

provided that in either case:

"(1) the price is not in excess of the transferor's current sales price to his most favored customer (including any division, subsidiary or affiliate of the contractor under a common control) for a like quantity under comparable conditions, and

"(2) the price is not determined to be unreasonable by the contracting officer."

The agency contends that, in a circumstance such as the one here presented, the exception stated in ASPR § 15-205.22(e)(ii) is not applicable because if the affiliate's price to the contractor was the result of adequate price competition and award was made to the affiliate after obtaining quotations on an equal basis from the affiliate and one or more equivalent sources, then the item would or should have been included in a price list.

The agency also states that, in effect, SP J-18b, as amended, reflects the agency's view that there is neither an established catalog nor market price for the item nor "adequate price competition" for nonprice listed parts. We note, however, that SP J-18c recognizes that the contractor may be required to submit a minimum of two proposed sources for any item exceeding \$500 or group of items exceeding \$1,000. Moreover, "adequate price competition" is defined in ASPR § 3-807.1(b) (1974 ed.) as follows:

"(1) Adequate Price Competition.

"a. Price competition exists if offers are solicited and (i) at least two responsible offerors (ii) who can satisfy the purchaser's (e.g., the Government's) requirements (iii) independently contend for a contract to be awarded to the responsive and responsible offeror submitting the lowest evaluated price (iv) by submitting priced offers responsive to the expressed requirements of the solicitation. Whether there is price competition for a given procurement is a matter of judgment to be based on evaluation of whether each of the foregoing conditions (i) through (iv) is satisfied. * * *


Accordingly, we do not share the agency's view that the cost principles would not allow affiliate profit as an allowable cost in like circumstances where applicable.

We also note the philosophy expressed in ASPR § 3-806(b) (1974 ed.) that:

"(b) Profit or fee is only one element of price and normally represents a smaller proportion of the total price than do such other estimated elements as

labor and material. While the public interest requires that excessive profits be avoided, the contracting officer should not become so preoccupied with particular elements of a contractor's estimate of cost and profit that the most important consideration, the total price itself, is distorted or diminished in its significance. Government procurement is concerned primarily with the reasonableness of the price which the Government ultimately pays, and only secondarily with the eventual cost and profit to the contractor."

SP J-18b clearly has a desirable and legitimate purpose--to insure the reasonableness of prices charged for the NPL items. However, we believe that the ultimate effect of the clause is negative. It does not assure the reasonableness of the NPL price; but it tends to reduce competition by discouraging the lowest possible prices on the price listed parts from firms with supplier affiliates who would not be able to take advantage of the affiliate's competitive position with respect to NPL items. Under these circumstances, we must conclude that this provision of the IFB is unreasonable derived and unduly restrictive. Therefore, it is recommended that appropriate action be taken to amend the noted restrictive requirements of SP J-18b.


Deputy Comptroller General
of the United States