



The Comptroller General  
of the United States

Washington, D.C. 20548

## Decision

**Matter of:** The Orkand Corporation; Department of the  
Navy--Reconsideration  
**File:** B-224466.2; B-224466.3  
**Date:** January 23, 1987

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### DIGEST

On reconsideration, General Accounting Office reverses prior decision sustaining protest, on ground that agency's contracting scheme (two-step sealed bidding with subsequent negotiation of task orders) renders conventional rules of sealed bid procurement--applied in prior decision--inadequate to protect the government from risk of unsatisfactory performance at other than lowest cost, arising from bidder's failure to price all labor categories in its bid as instructed by solicitation.

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### DECISION

The Orkand Corporation and the Department of the Navy request reconsideration of our decision in SMC Information Systems, B-224466, Oct. 31, 1986, 86-2 C.P.D. ¶ 505, in which we sustained SMC Information Systems' (SMC) protest of the Navy's award of a contract to Orkand under invitation for bids (IFB) No. N66032-85-B-0018. Orkand and the Navy contend that our decision is legally erroneous on several grounds. We reverse the decision.

The IFB is the second step of a two-step, sealed bid procurement of a requirements-type contract for automatic data processing software support services. The bidding under the IFB was in the form of fixed hourly prices for several labor categories; the labor mix for each individual task is subject to negotiation at the time the task arises. The IFB required that prices be bid for each category and that each price carry its proportionate share of wages, overhead, etc. The IFB also contained several warnings concerning the structuring of bids, one of which stated the Navy's intention to prevent bidding that could result in contract costs significantly higher than evaluated costs.

SMC originally contended that the Navy improperly had rejected its low bid for: (1) bidding "NSP" ("not separately priced") for two labor categories (program manager and group

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manager); and (2) for bidding prices that were unrealistically low. We sustained the protest, finding SMC's bid acceptable despite the "NSP" bidding, because "NSP" equated with zero dollars and evidenced SMC's intent to be bound to furnish the required labor at no charge to the government. We further held that it was improper to reject SMC's bid for unreasonably low prices because, while SMC's bid appeared mathematically unbalanced, the record did not establish that it also was materially unbalanced (i.e., would result in other than the lowest cost to the government); and because there is no prohibition against a responsible firm bidding below cost. Consequently, we recommended that the Navy terminate its contract with Orkand and make an award to SMC, if SMC were found responsible and an award was otherwise appropriate. Orkand and the Navy have requested that we reconsider this recommendation.

Basically, the Navy rejected the bid because of its belief that acceptance of the bid would subject the government to unacceptable cost and performance risks during performance. On reconsideration, we agree and find the rejection properly within the contracting officer's discretion.

In reaching our prior decision, we considered the protest in the context of the conventional rules of a sealed bid procurement. On reexamination, we find these conventional rules insufficient to protect the government's interests--i.e., proper performance at the lowest cost--under the somewhat unconventional contracting method employed here. While, nominally, this was a two-step, sealed bid procurement for a fixed-price contract, the prices are fixed at the time of award only in the most technical sense. Whereas under a normal fixed-price procurement the government knows at the time of award both the exact nature of the work and its price, here only the hourly prices of the labor categories were fixed at the conclusion of the bidding. It is only after the contract award, when each requirement arises, that specific technical approaches, labor mixes, and fixed total costs are proposed and negotiated. Thus, merely making award to the low evaluated bidder may not in all instances result in satisfactory performance at the lowest cost, and the IFB instructions on the structuring of bids reflected the Navy's concern in this regard.

The contract structure here created the possibility that if discrete, proportionate prices were not established for each labor category at the time of award, the contractor could

have a cost incentive to offer to perform using other than the optimal labor mix to assure recovery of its costs. The Navy thus believed SMC would have a substantial incentive to propose skewed labor mixes to recover costs of the two "NSP" management categories (SMC priced two of the other eight categories at \$20 (senior systems analysts) and \$17 (programmers), and the remaining six at \$7, \$6 or \$5). Alternatively, the Navy feared that SMC might minimize the number of program and group manager hours on each task, and that the quality of performance would suffer as a result. The Navy also foresaw that disagreements over labor mixes could result in many disputes under the contract disputes procedure.

We discounted these Navy concerns in our original decision, citing the fact that the unpriced management labor categories' contract responsibilities seemed integral to all tasks that would arise, and the fact that under this contract structure, any contractor--no matter how it priced the labor categories--could propose labor mixes designed to maximize its contract payment. On reflection, we find merit in the Navy's concerns.

Although the program and group managers were assigned general supervisory and administrative functions which seemingly would be part of any contract task, the relevant consideration, we now recognize, is whether these managers would be made available to perform their duties fully where the contractor will not be reimbursed for their time. Also, a contractor clearly would have a significantly greater incentive to propose skewed labor mixes where only by doing so can the contractor avoid supplying labor for which it will not be reimbursed. Finally, our Office has expressed the view that it is desirable for an agency to design requirements to reduce the likelihood of disagreements that would have to be resolved under the contract's disputes clause. See Advanced Technology Systems, Inc., 64 Comp. Gen. 344 (1985), 85-1 C.P.D. ¶ 315. The Navy attempted to do so here by instructing in the IFB that all labor categories be priced.

We had occasion to restudy our position in this area in our recent decision in Computer Data Systems, B-223921, Dec. 9, 1986, 86-2 C.P.D. ¶ \_\_\_\_\_, which concerned a failure to price all labor categories under a similar Navy solicitation. There, we recognized the propriety of an agency rejecting an offer on the ground that the offeror would have a significant incentive to propose only those labor categories for which it could recover its costs. We reasoned that the government should not be compelled to accept an offer, albeit evaluated as low, that, because of its pricing structure, posed

significant risk that performance would be deficient and that the actual cost of performance would not be the lowest.

The same reasoning applies here. The Navy perceives a significant risk that, because SMC did not price all labor categories as specifically instructed by the IFB, SMC may not properly perform the contract and the actual cost of performance may not be the lowest. We believe it was proper for the Navy to consider this risk and to deny SMC the award on this basis.

Accordingly, we reverse our prior decision. By separate letter of today to the Secretary of the Navy we are withdrawing our recommendation that the contract with Orkand be terminated for the convenience of the government and that award be made to SMC.

*Milton J. Auster*

for  
Comptroller General  
of the United States