Mr. Arsenoff

Comptroller General
of the United States

Washington, D.C. 20548

Decision

Matter of: Mandex, Inc.

File: B-241841

Date: March 6, 1991

Floyd C. Stilley, Esq., for the protester.
William M. Weisberg, Esq., Wiley, Rein & Fielding, for Cortez III Service Corporation, and Ruth Y. Morrel, Esq., for DynCorp, interested parties.
Major William R. Medsger, Esq., and Robert P. Simms, Esq., Department of the Army, for the agency.
Robert C. Arsenoff, Esq., and John Brosnan, Esq., Office of the General Counsel, GAO, participated in the preparation of the decision.

DIGEST

1. Allegation that discussions were inadequate because they did not inform protester that administrative contracting officer (ACO) had to approve an advance agreement relating to a change in computing corporate general and administrative cost rates is denied where record shows that protester applied to the ACO for such approval immediately prior to discussions and where the solicitation and the procurement regulations indicate that such approval is within the ACO's authority.

2. Cost realism adjustment based on substituting certain proposed indirect cost rates predicated on an unapproved change to protester's existing method of accounting with audit-determined rates under the firm's established method of accounting was reasonable since contracting officer could not know which accounting system would be used in the event approval for the change was denied and since, at the time of award, deficiencies related to the proposed change had not been remedied.

DECISION

Mandex, Inc. a small disadvantaged business (SDB), protests the award of a cost-plus-award-fee contract to Cortez III Service Corporation under request for proposals (RFP) No. DAAD07-90-R-0005, issued by the Department of the Army for engineering, technical, and maintenance services in support of the Army Test and Evaluation Directorate at the

White Sands Missile Range in New Mexico. Mandex argues that the Army's failure to conduct meaningful discussions with regard to general and administrative (G&A) cost rates contained in its cost proposal led to an improper cost realism adjustment to its proposal.1/

We deny the protest.

The RFP was issued on January 24, 1990, contemplating the award of a 5-year contract to the offeror whose proposal was determined by the procurement contracting officer (PCO) to represent the "best buy" to the government based on an integrated assessment of technical, management, and cost factors. To be considered for award, an offer had to be determined acceptable with regard to the technical and management factors; although these "merit" factors were listed as more important than cost, cost could become determinative as proposals were rated technically equal. The RFP also provided that proposed costs would be evaluated for realism in consideration of a number of factors including "recommendations" of the Defense Contract Audit Agency (DCAA) which audited all the proposals.

Of the four initial proposals received on April 20, three were found to be technically acceptable including the protester's and the awardee's. The evaluators concluded that, despite some insignificant technical scoring differences among these offers, each offeror could perform as well as the other and recommended that the final selection decision be based primarily on cost considerations.

Mandex's initial cost proposal was premised on the use of G&A rates for each year of the contract which were based on a proposed change to its established method of accounting. According to the protester, this proposed change was necessitated by its reading of the RFP with regard to

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1/ Mandex also alleged that the awardee was not entitled to a 10 percent evaluation preference to be accorded SDBs under the RFP because, in the protester's view, Cortez was not a small business within the applicable size standard. Concurrent with our consideration of this protest, Mandex pursued a size challenge before the Small Business Administration (SBA). On February 1, 1991, Mandex's final appeal was denied as SBA determined that the awardee was a small business. Since the protester has predicated its allegation as to the improper application of the evaluation preference on the condition that it would be successful before the SBA, the allegation is academic as that agency has exclusive statutory authority to decide such matters. Bid Protest Regulations, 4 C.F.R. § 21.3(m)(2) (1990).

mandatory staffing levels for administrative support positions which the firm had historically provided through its central office and accounted for in terms of a G&A rate calculated on a corporate-wide "total cost input" (TCI) basis.2/ In the protester's view, the mandatory staffing requirements would have meant, under its then current accounting system, that it would have to both directly charge the government for the support positions as well as "double charge" through the application of its G&A rates. Accordingly, Mandex believed that it was necessary to convert its accounting system for G&A computation purposes to a "home office expense" (HOE) method, which provided for a greater degree of specificity in allocating centrally provided expenses to a given segment of business through the use of multiple G&A pools as contrasted with a single G&A pool under the TCI method.

On June 8, DCAA reported the findings of its audit of the Mandex proposal to the protester and to the PCO and outlined a number of deficiencies with regard to the manner in which the firm's cost accounting system allocated costs as a result of the proposed change. DCAA recommended that the protester remain on the TCI basis of computing its G&A rates; DCAA also calculated a set of rates based on the TCI method which were significantly higher than those contained in the proposal. Finally, DCAA instructed Mandex to submit its proposed change to the administrative contracting officer (ACO)3/ for approval prior to its further presentation in a proposal.

On June 11, Mandex applied to the ACO for approval of its proposed change to an HOE method of calculating G&A on the basis of DCAA's instruction and acknowledged in its letter that it understood that, under normal circumstances, "this change should have been first presented to you [ACO]" and that

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2/ According to the agency and DCAA, no such change was required by the RFP's terms and we find no support in the solicitation for the protester's position; however, Mandex was, of course, free to change its accounting system provided that it met the requirements of the cost principles set forth in Federal Acquisition Regulation (FAR) Part 31.

3/ Under sections G.7.1 and G.9 of the RFP, the ACO was charged with approval authority over accounting matters. See also FAR § 31.109, which states that the ACO has the authority to finally negotiate advance agreements regarding potentially questionable matters of allowability and allocability--including G&A rates--to preclude future disputes about the reimbursement of costs; this authority includes the review of an offeror's other government contracts to ensure uniformity.

DCAA would report the results of its audit to the ACO in 45 days. Mandex requested that this process be expedited in view of its need to participate in the ongoing procurement.

In reviewing Mandex's proposed G&A rates in conjunction with the DCAA recommendation, the PCO was concerned that they had been understated; as a result, on July 5, he sent the following discussion question to Mandex:

> "I acknowledge your discussions with DCAA over what the G&A rate should be. For cost realism purposes, however, I cannot accept a rate based on a proposed accounting change that has not been approved unless that rate is also a ceiling. In other words, I would accept the proposed rates as a ceiling, but you must accept the risk of getting the accounting change approved, and you must accept the additional risk the actual rate would not go up over the next five years."

Mandex responded on July 19 stating that it would consider placing a ceiling on its G&A rate in its best and final offer (BAFO), but noted that the issue might become moot since the firm anticipated "satisfactory completion of discussions with DCAA prior to your call for a BAFO."

Mandex states that it received verbal "approval" of its accounting change from a DCAA auditor on August 21. The protester also notes that the PCO received an August 9 letter from DCAA which contained "preliminary results" concerning Mandex's proposed change sent at the PCO's request in the event that the change to an HOE method was approved. Although the letter indicated that DCAA had "approved" the change and it contained G&A calculations based on the change, it also noted continuing deficiencies with the protester's cost accounting system and a need for further information and audit review.

Mandex submitted its BAFO on September 7, which noted that DCAA had approved its accounting change and contained no ceilings. Its final proposed G&A rates were based on the HOE computation method. A week later, on September 13, DCAA sent a letter to Mandex (with a copy to the PCO) indicating that the change was "acceptable" but requesting additional budgetary data and further noting deficiencies in the allocation methods used by the firm to treat indirect costs. Thereafter, on September 19, the PCO contacted a

representative in the ACO's office and was informed that no change had yet been approved.4/

The agency reports that since there was no change approved by the ACO and Mandex's BAFO contained no ceilings on its G&A rates as discussed in July, during his cost realism analysis the PCO used the only audited rates available to him--those calculated by DCAA on June 8 using the TCI method--to adjust Mandex's total proposed costs upwards by approximately $2.8 million. This adjustment alone changed the protester's competitive position from low offeror to next low and impacted the PCO's "best buy" decision which, on October 19, resulted in an award to Cortez--the low evaluated offeror.

Mandex has raised numerous arguments in protesting this cost realism adjustment to its proposed G&A rate which are essentially based on two themes: (1) discussions were inadequate because the PCO failed to disclose, and Mandex had no other reason to know, that ACO approval would be required before HOE rates would be accepted as realistic without a ceiling; and (2) since DCAA had communicated its "approval" prior to award, the need for ACO action was little more than a formality, and the cost realism adjustment was, therefore, unreasonable and not reflective of its probable costs for the contract effort since the Army had adequate assurances5/ that the firm would implement the accounting change as proposed and the agency also had legal recourse if it did not. We find Mandex's arguments to be unpersuasive for the reasons set forth below.

For cost discussions to be meaningful, the agency must generally lead offerors into areas of their proposals in need of amplification or change and provide them an opportunity to revise their proposals. In this regard, agencies are not required to specifically indicate which data they will use in performing cost realism analyses. See Jonathan Corp., B-230971, Aug. 11, 1988, 88-2 CPD ¶ 133. When an agency evaluates proposals for the award of a cost reimbursement

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4/ This fact was confirmed after award by the ACO in an October 29 letter to the PCO which notes that, even as of that time, there were remaining deficiencies involving accounting for indirect costs which affected both Mandex's current system and its proposed change and which needed to be resolved after further DCAA monitoring prior to approval.

5/ Mandex claimed that it signed a firm commitment to make the accounting change on August 7 at DCAA's request, however, it has not produced a copy of this document and DCAA unequivocally denies that such a document exists.

contract, an offeror's estimated costs are not dispositive since they may not provide valid indications of what the government is required to pay; consequently, a cost realism analysis must be performed to determine the extent to which the proposed costs represent what the contract should cost. United Eng'rs & Constructors, Inc., Stearns-Rogers Div., B-240691; B-240691.2, Dec. 14, 1990, 90-2 CPD ¶ 490. Our review of an agency's exercise of judgment in this area focuses on whether the agency's cost evaluation was reasonably based. Id.

The protester's allegation that the PCO somehow failed to disclose, and that Mandex had no other reason to know, that ACO approval of the accounting change was required is not supported by the record. The RFP itself informs offerors that the ACO's office approves changes with regard to accounting matters. Further, FAR § 31.109 provides the ACO with such authority. Mandex's assertion that DCAA approval was all that was required ignores the ACO's legal authority as well as the fact that DCAA's role is only to provide recommendations to contracting officers which they are not bound to follow. Electronic Warfare Integration Network, B-235814, Oct. 16, 1989, 89-2 CPD ¶ 356.

Most important, the record shows that Mandex knew that ACO approval, based on DCAA recommendations, was required since the protester itself applied for such approval on June 11 and asked for an acceleration of DCAA's report to the ACO. If, as Mandex seems to argue, its various preaward oral communications with the PCO and DCAA representatives created any confusion as to who had approval authority, by the terms of the RFP, Mandex was required to seek written clarification from the PCO, which it did not. See RFP section L.1.1 incorporating FAR § 52.215-14.

In light of these circumstances and in view of the fact that the July 5 written discussion question regarding G&A rates clearly communicated the PCO's concern with Mandex's proposal and gave the firm reasonable alternatives for correction, we find that discussions were adequate. Jonathan Corp., B-230971, supra.

Mandex's challenge to the reasonableness of the cost realism adjustment to its G&A rates is premised in part on an argument that, by virtue of submitting a cost proposal disclosing the accounting change to an HOE method, the government had "legally enforceable" assurances that the firm's G&A rates would not exceed the rates calculated by using that method. Mandex also questions why the adjustment was not limited to approximately $72,000, representing an amount for 1990 during which it proposed to remain on a TCI basis of computing G&A prior to switching to HOE in 1991.

The purpose of negotiating an advance agreement on the treatment of costs which are expected to be questionable is to preclude, to the extent possible, disputes during the administration of a contract, thus eliminating the need to litigate such matters. See FAR § 31.109. Advance agreements are also important when, as here, a potential contractor has other government contracts whose administration may be affected by the subject matter of such an agreement, e.g., a change in the method of computing G&A.

In this case, as of the initiation of discussions, the PCO had been advised of deficiencies in the HOE method proposed by Mandex. In our view, the PCO reasonably concluded, and adequately conveyed to Mandex, that Mandex had three alternatives: obtain approval to use the HOE method, place ceilings on its rates derived by that method, or (if it persisted in proposing costs based on that method) face the prospect of a cost realism adjustment.

As of the time Mandex submitted its BAFO and was undergoing a final cost evaluation, the record discloses that no ceilings had been offered and no ACO approval had been obtained for use of the HOE method of computing G&A. In fact, DCAA still perceived deficiencies in Mandex's indirect cost accounting system which required additional actions and monitoring to remedy.

Thus, when he performed the analysis, the PCO did not know when or if the deficiencies would be remedied and the change approved, and, perhaps more importantly, did not know what future method of computing G&A Mandex would use in the event that approval was not granted--a situation implicit in his advice during discussions as to the propriety of proposing ceilings. Since the PCO did not know what could happen in the absence of ACO approval, we are provided with no basis for concluding that the PCO acted unreasonably in adjusting Mandex's G&A rates to those which had been determined by DCAA on the basis of the long-established TCI method. United Eng'rs & Constructors, Inc., Stearns-Roger Div., B-240691; B-240691.2, supra.

Finally, as to Mandex's suggestion that the adjustment should have reasonably been limited to 1990--the only time it proposed to remain on the TCI method--we note that this too is predicated on the assumption that the firm would, in fact, use

the HOE method thereafter even if approval were not granted, an assumption that we find the contracting officer was reasonably unwilling to make as of the time of award.

The protest is denied.

Robert P. Murphy
for James F. Hinchman
General Counsel