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Comptroller General
of the United States

Washington, D.C. 20548

# Decision

**Matter of:** Cavalier Computing; System Planning Corporation

**File:** B-244697; B-244697.2

**Date:** November 12, 1991

Michael L. Gardner for Cavalier Computing, and Charles F. Hengels and Duncan Stevens for System Planning Corporation, the protesters.
John E. Boehmke, Thomson Financial Networks, for Securities Information Center, an interested party.
George Conril Brown, Esq., Eric Rosenberg, Esq., and Ilene F. Citrin, Esq., United States Securities and Exchange Commission, for the agency.
Roger H. Ayer, Esq., and James A. Spangenberg, Esq., Office of the General Counsel, GAO, participated in the preparation of the decision.

**DIGEST**

Award decision that significantly relied on the awardee's relative financial stability--a specific request for proposals (RFP) evaluation factor--is not reasonable and reflects unfair treatment of offerors, where the decision was based on financial information submitted by the awardee, that was unrelated to the awardee's capabilities and which did not comply with the RFP requirement to submit audited financial statements, and where one offeror's financial stability was significantly downgraded because its compliance with the requirement subjected it to a more critical review and another offeror's financial stability was downgraded because of its failure to submit audited statements.

**DECISION**

Cavalier Computing and System Planning Corporation protest the award of a contract to the Securities Information Center (SIC) division of Thomson Financial Networks, Inc. (TFN) under request for proposals (RFP) No. SECHQ1-90-R-0014 issued by the United States Securities and Exchange Commission (SEC) for the operation of the SEC's Lost and Stolen Securities Program.[1] Under different ownerships,

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[1]The program is authorized by the Securities Exchange Act of 1934, as amended, to curb organized crime's trafficking in stolen and counterfeit securities. See 121 Cong. Rec. 6,185

SIC has operated the program since it began in 1977. The protesters object to the SEC's evaluation of the protesters' and awardee's proposals as well as the SEC's award selection.

We sustain the protests.

The RFP, issued on August 31, 1990, solicited for a no-cost-to-the-government contract[2] for 1 year with 4 option years. The RFP required offerors to provide technical and management proposals, and "[i]nclude audited financial statements for the last [2] fiscal years, including interim statements for the current year."

As amended, the RFP provided for the evaluation of proposals in three areas (technical, management and business). For purposes of evaluation, technical and management factors carried a combined relative weight of 75 percent and business factors a relative weight of 25 percent. Relevant evaluation criteria of the three factors are listed in descending order of importance as follows:

> "**Technical Factors**
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> . . . . .
>
> (a) Design, develop, test, implement, operate and maintain a computerized data base of lost, stolen and counterfeit securities . . . .
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> . . . . .

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(1975). The more than 23,000 participating entities, financial institutions (brokerage houses and banks) and others, use the program to (1) report the theft and loss of negotiable securities (stocks and bonds), and (2) to inquire as to the true ownership of securities coming into their possession. The program contractor maintains a computer data base of lost, counterfeit, and stolen securities based on financial institution reports and inquiries. When an inquiry matches the identifying number of a previously reported lost security (this is referred to as a "hit"), the program contractor provides the inquirer with the identity of the entity that reported the particular security as lost. The "hit" may also be reported to the Federal Bureau of Investigation.

[2]The contract is similar to a concession contract in that the contractor provides services to the public at no cost to the government. The contractor charges the public user fees for program services that reimburse the contractor's start-up and operating costs.

(k) . . .

**Management Factors**

. . . . .

(a) Experience in implementing similar collection and dissemination data systems.
(b) Financial stability of the company.
(c) Available company facilities and resources.

. . . . .

(f) . . .

**Business Factors**

. . . . .

(a) Proposed fees--Reasonableness and fairness of proposed fee structure . . . .
(b) Cost realism."

The SEC received proposals from the protesters and SIC by the March 15, 1991, closing date. SIC was the highest rated offeror followed by Systems Planning Corporation and Cavalier. All three proposals were included in the competitive range. On May 3, the SEC conducted discussions with the three offerors and requested that best and final offers (BAFO) be submitted by May 14. While all three offerors improved their scores as a result of discussions, their respective positions in the competitive ranking remained the same.

On June 26, the SEC awarded the contract to SIC. Cavalier protested the award on July 3. Systems Planning Corporation waited until after it received a debriefing from the SEC on July 12 to file its July 18 protest. On July 16, the SEC authorized performance of the contract based on a determination that it was in the best interest of the government to continue performance notwithstanding the protest.

The evaluation of proposals is a matter within the discretion of the contracting agency since that agency is responsible for defining its needs and the best method of accommodating them. Information Sys. & Networks Corp., 69 Comp. Gen. 239 (1990), 90-1 CPD ¶ 203. Offers must be evaluated on the basis stated in the solicitation, however, Everhart Appraisal Serv., Inc., B-213369, May 1, 1984, 84-1 CPD ¶ 485, and agencies must adhere to the stated criteria or inform all offerors of any changes made in the evaluation scheme. Cobro Corp., B-228410, Dec. 16, 1987, 87-2 CPD ¶ 600. In reviewing the evaluation of offerors' proposals, we do not reevaluate the proposals; instead, we examine the agency's evaluation to ensure that it was reasonable and in accord with stated criteria. Id.

The evaluation and source selection documents reveal that a primary discriminator used in the selection process was in the management area, particularly with regard to offeror financial condition.[3] Financial stability--a specific RFP evaluation factor--was said to be a key concern in the award decision because the no-cost-to-the-government nature of this contract required the contractor to rely totally on itself and program users for the funds necessary for timely performance.[4] We sustain the protests because we find that the source selection decision was not reasonably based and offerors were not treated equally in the evaluation of this aspect of their proposals.

In the initial evaluation of System Planning Corporation's proposal, the evaluators remarked that its proposal showed "a sound financial position." The SEC treated the firm's financial statements as unaudited, however, because it had elected to delete the notes from the audited statements that were submitted with its initial proposal. After the SEC requested audited financial statements in negotiations, System Planning Corporation complied, submitting as part of its BAFO the financial statements complete with notes. The notes caused the SEC to question "whether confidence can be placed in [its] ability to provide the necessary funds in a timely manner."[5] This was a noted deficiency in System Planning Corporation's BAFO.

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[3]In appropriate circumstances, as here, where the solicitation expressly apprises offerors, financial condition may be used to assess the relative merits of individual proposals. E.H. White & Co., B-227122.3; B-227122.4, July 13, 1988, 88-2 CPD ¶ 41.

[4]The contractor has to have sufficient funds of its own to purchase computer systems, develop software, acquire secure facilities, and hire and train personnel. Ultimately, the contractor would be reimbursed when program participants pay their user fees.

[5]The notes caused the SEC several concerns, particularly a concern that System Planning Corporation's accounts receivable constituted an unusually large portion of current assets albeit they were "due primarily from the U.S. Government."

The SEC downgraded Cavalier's initial proposal and BAFO under the financial stability subfactor because Cavalier's submission "constituted a near total failure to demonstrate financial stability." Specifically, Cavalier provided neither RFP-required audited financial statements nor background information on itself as a firm. After the SEC raised the issue of financial stability during negotiations, Cavalier submitted with its BAFO the unaudited financial statements of several persons affiliated in its proposal effort who would join Cavalier should it receive the award. In evaluating Cavalier's BAFO, the evaluators noted Cavalier's use of "innovative state-of-the-art technology"[6] but were concerned by the software's uniqueness since it was being offered by "a small enterprise with limited capital, inasmuch as such a design may be difficult to transfer."[7] The SEC also questioned Cavalier's ability to finance its computer equipment purchases during the start-up phase of the contract.

The SEC, while initially evaluating SIC highly in almost every area, also expressed serious reservations concerning SIC's financial situation. SIC's proposal included the unaudited statement of TFN (of which SIC is a division) indicating that TFN was financially sound. The SEC was concerned by SIC's failure to provide the required audited financial statements because the SEC believed TFN had suffered "substantial losses" for 2 of the last 3 years and has a "negative retained deficit." The evaluators

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[6]Cavalier proposed a completely automated software package for the program based on Cavalier's proprietary software design written in the ANSI C programming language. Cavalier notes that the SEC reserved the right to require offerors to perform a benchmark (i.e., an operational capability demonstration including "C2" level security capabilities) of their proposed software. There also was a relatively short timeframe between contract award and the start of performance. Consequently, Cavalier had written the necessary software, and on June 18 offered to demonstrate it prior to the SEC's June 26 award to SIC.

[7]The operating system software (i.e., the software that accesses the program's reports and inquiries database, and generates reports for users from information in that database) is the property of the program contractor. The database software (i.e., the software record of reports and inquiries) belongs to the SEC and is standardized so that it can be transferred to succeeding program contractors. It is not clear why the SEC would have been concerned with transferring Cavalier's operating system "to a subsequent vendor in event of unforeseen emergencies or the routine termination of the contract."

understood that TFN's ultimate parent, which it believed was the Thomson Corporation (TC), was very strong financially, but SIC had provided no information concerning TC's financial condition. The SEC's BAFO request to SIC asked for audited financial statements for 2 years and an interim statement for the current fiscal year.[8]

SIC, in its BAFO response, referenced "the strong technical and financial backing of our company" and provided not the requested audited TFN financial statements but instead TC's audited financial statements.[9] This was justified on the ground that "[TFN] is a wholly owned subsidiary of [TC]." SIC enclosed a letter from a TFN officer explaining that TFN is wholly owned by Thomson U.S., Inc. (TUSI) "and ultimately" by TC. The letter indicated that SIC could not furnish the RFP-required audited statements for TFN because it was not the practice of TC's auditors to audit TFN--TC's auditors merely performed an "accounting review" of TFN as a part of their overall audit of TC.

The BAFO evaluation of SIC's proposal reads:

> "[T]he panel requested and has received financial statements of [TC], the parent of TFN. These statements show a strong financial position and net income after taxes of over . . . annually."

The BAFO evaluation also indicates that this submission satisfied the SEC's concerns about TFN's substantial losses over 2 of the last 3 years. The SEC advises that SIC's submission of the TC audited statements met the RFP requirement.[10]

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[8]The record shows that the evaluators expected SIC to provide audited financial statements for both TFN and TC.

[9]In its comments on the protest, SIC advises that it submitted the TC audited financial statements to "show that the information provided for the subsidiary, TFN, was materially accurate" and not to indicate that TC's assets were available to support TFN's performance of the contract.

[10]The SEC reasoned that:

> "The relevant inquiry is whether SIC's BAFO satisfied those requirements, which it did. As noted, SIC is an unincorporated division of TFN. The audited financial statements of TFN's parent corporation, [TC], were submitted to the Commission in connection with the contract. No financial statements were submitted in the name of SIC because it is an unincorporated division of TFN."

Our review of the TC audited financial statements shows that they contain no mention of TFN or TFN's finances. We made further inquiries in response to the protests to ascertain how far removed TC was in the Thomson corporate hierarchy from TFN and to ascertain if better information was available.

On October 24, we received further information to the effect that TFN's direct parent is Thomson Organization Holdings, Inc. (TOHI), that TOHI's direct parent is Thomson Holdings, Inc. (THI), and that THI's direct parent is TUSI.[11] We were at the same time furnished THI's audited financial statements, which characterize THI as an "indirect," wholly-owned subsidiary of TC. THI's audited financial statements are significantly less favorable than the TC financial statement on which the SEC assessed SIC's financial stability. No audited financial statements for SIC or TFN have been provided.

Based on our review of the record, it is apparent that the SEC has no reasonable basis for its source selection that was significantly based upon relative financial condition, and that, in the matter, the offerors were not evaluated on a fair or equal basis.

The record shows that the SEC's main concern with accepting SIC's proposal was its financial condition because of known recent financial difficulties. The SEC relied upon TC's audited statement submitted in SIC's BAFO to abate its concerns about SIC's financial stability. It appears that the SEC believes that this was the best available audited information; that TC, a financially stable corporation, was a more direct parent of TFN and SIC than it actually was; and that TC may have been "financially backing" SIC. The financial statements of the more proximate parent company of TFN and SIC (although available) were not provided to the SEC until this protest, and show a significantly less favorable financial picture. No audited statements for TFN or SIC were provided as required by the RFP.

Under the circumstances, had the SEC insisted on audited financial statements and been given a truer picture of TFN's (or even THI's) financial capabilities, the selection decision might have been different, given the SEC's significant concerns over TFN's financial stability and the

[11]A summary of the chain of organization, in ascending order of importance, is as follows: SIC, TFN, TOHI, THI, TUSI, and TC. On August 28, 1991, SIC furnished a letter from Thomson Information/Publishing Group (TI/PG) advising that TFN is a TI/PG company. We surmise that TI/PG may exist at a level above TUSI and below TC.

stated importance of this matter in the source selection documentation. Moreover, while the agency relied on the audited statements of TC, there is no indication that it accepted financial responsibility for SIC or for this contract, and it is unclear on what basis the SEC could rely on those statements to satisfy its concerns about TFN's financial situation, particularly given how the other two competitors were evaluated. Compare Hardie-Tynes Mfg. Co., 69 Comp. Gen. 359 (1990), 90-1 CPD ¶ 347, aff'd, B-237938.2, June 25, 1990, 90-1 CPD ¶ 587 (agency can consider parent company support of subsidiaries in making a responsibility determination where there is an agreement from the parent company to provide support).

As noted, System Planning Corporation was not accorded the same treatment that SIC received vis-a-vis the audited financial statement requirement. The fact that System Planning Corporation submitted an audited financial statement made it more vulnerable to criticism and down-grading than SIC was from its sanitized unaudited submission. Indeed, this more critical evaluation of its financial statements resulted in an evaluated weakness in financial stability. Cavalier was also treated unequally since its most notable deficiency was based on its failure to provide audited financial statements.

In sum, the record indicates that the award selection was based on the unequal and unfair evaluation of System Planning Corporation's and Cavalier's proposals as compared to how SIC's proposal was evaluated. See Secure Servs. Tech., Inc., B-238059, Apr. 25, 1990, 90-1 CPD ¶ 421; J.M. Cashman, Inc., B-233773, Apr. 14, 1989, 89-1 CPD ¶ 380. The SEC effectively waived for SIC a material RFP requirement that "audited financial statements" of an offeror be provided.[12] Without an audited financial statement or other evidence, the SEC has no reasonable basis for its conclusion that SIC was in "strong financial condition." In fact, the agency's final evaluation of SIC's financial condition rested on information that, as far as the record discloses, is unrelated to SIC's known financial difficulties or its capability to perform the contract. As indicated above, given the SEC's significant concern with SIC's and the other offerors' respective financial stability

[12]Generally, the preparation of audited financial statements is a very costly undertaking that discloses a firm's actual financial position and operations to recipients of the audited statements. See generally Allied Production Mgmt. Corp., Inc., B-236227.2, Dec. 11, 1989, 89-2 CPD ¶ 534. That is of course why some agencies and persons insist on such statements and may be why such an audited statement is not prepared for TFN.

in the evaluation and source selection documentation, this unequal and unfair evaluation affected the selection decision. Consequently, System Planning Corporation's and Cavalier's protests are sustained on this point.[13]

Accordingly, we are recommending that the SEC reevaluate the proposals in light of the RFP requirements to determine what information is necessary to satisfy its concerns and to fairly evaluate the proposals, conducting discussions and requesting new BAFOs, if necessary. If the reevaluation, in accordance with the stated evaluation criteria and RFP requirements, yields a winner other than SIC, the SEC should terminate SIC's contract for the convenience of the government and make award to the winning offeror. Cavalier and System Planning Corporation are entitled to recover their costs of filing and pursuing the protests, including reasonable attorneys' fees. 4 C.F.R. § 21.6(d) (1991). Cavalier and System Planning Corporation should submit their claims for protest costs directly to the SEC. 56 Fed. Reg. 3759 (1991) (to be codified at 4 C.F.R. § 21.6(e)).

The protests are sustained.

Milton J. Socolar

for Comptroller General
of the United States

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[13]Cavalier and System Planning Corporation have asserted numerous other grounds of protest that are either untimely or do not give rise to a meritorious protest. For example, the protesters challenge the SEC's acceptance of SIC's self-certification that it was providing a "C2" level of protection (a measure of computer security against improper access) contending that certification should be by the government agency that normally is charged with providing such certifications, and that SIC's proposed equipment could not meet that agency's standards. The RFP expressly allowed self-certification, and SIC's proposal contained a self-certification and a description of how SIC's equipment met the requirement, upon which the SEC reasonably found SIC's equipment met the RFP's requirement. Additionally, System Planning Corporation claims to have offered lower fees to program participants than SIC. However, this claimed advantage appears to be significantly conditioned on the SEC's extension of the initial contract term, which would allow it to amortize its start-up costs over a longer period. Since the contract period would have to be varied to accept System Planning Corporation's proposal, we find reasonable the SEC's evaluation of its cost.