



Comptroller General
of the United States

Washington, D.C. 20548

Decision

Matter of: Pearl Properties
File: B-249524
Date: November 17, 1992

Michael J. Reardon for the protester.
Sharon Matthews Swain, Esq., Department of Housing and Urban Development, for the agency.
Tania L. Calhoun, Esq., and Christine S. Melody, Esq., Office of the General Counsel, GAO, participated in the preparation of the decision.

DIGEST

The apparent low bid on a contract for a 1-year base period and four 1-year options was properly rejected as materially unbalanced where there is a large decreasing price differential between the prices bid for the base and first option years, and the prices bid for the last 3 option years, and where the bid does not become low until the final option year, thereby raising a reasonable doubt that the bid would result in the lowest actual cost to the government.

DECISION

Pearl Properties protests the rejection of its bid as materially unbalanced and award of a contract to Ricardo Real Estate under invitation for bids (IFB) No. 9-92-051, issued by the Department of Housing and Urban Development (HUD) for real estate management services for single family properties located in Richmond, Virginia.

We deny the protest.

The IFB was issued on April 3, 1992, and contemplated award of a fixed-price, indefinite-quantity services contract for a 1-year base period with up to four 1-year options.¹ The services required under the Real Estate Asset Manager (REAM) contract included inspection, re-keying, winterization, and maintenance of properties assigned to the contractor. The

¹With regard to the expected quantities, the IFB stated that for any year the contract was effective a minimum of 5 properties would be assigned; the total number of properties to be managed under the contract would not exceed 200 properties per month in the period of 1 year.

IFB informed bidders that, for each year of the contract, the agency anticipated assigning between 95 and 100 HUD-owned properties in the first month; it expected to assign an additional 5 to 7 HUD-owned properties in each following month. For each year of the proposed contract, bidders were asked to supply a price that would reflect full compensation for performance of all services for each property assigned. Under the contract, the contractor becomes eligible to receive 30 percent of the price when the property is advertised for sale and the remaining 70 percent of the price when the sale closes.

The IFB included the standard "Evaluation of Options" clause, set out at Federal Acquisition Regulation (FAR) § 52.217-5, which advises bidders that the government will evaluate bids on the total price for the base requirement and all options; the IFB also included the standard clause, set out at FAR § 52.214-10, which cautions that a bid may be rejected as nonresponsive if the prices bid are materially unbalanced between line items, and which defines a materially unbalanced bid as one based on prices significantly overstated in relation to cost for some work and significantly less than cost for other work, and where there is a reasonable doubt that the bid will result in the lowest overall cost to the government.

The agency received 11 bids by bid opening on April 16; the three lowest eligible bids were priced as follows:²

	<u>Pearl</u>	<u>Ricardo</u>	<u>Forsythe</u>
Base Year	\$837	\$700	\$655
1st Option	717	500	575
2nd Option	458	550	575
3rd Option	451	575	575
4th Option	451	600	575
Total	\$2,914	\$2,925	\$2,955

Upon evaluation, though Pearl's aggregate bid was low, the contracting officer was concerned that the large pricing differential between the prices Pearl bid for the base year and first option year, and the prices it bid for the last 3 option years, indicated an unbalanced bid. She found that Pearl's prices for the last 2 option years were 46 percent lower than its price for the base year. She also found that Pearl's base year price of \$837 per unit was significantly higher than the government estimate of \$532 per unit; Pearl's base year price was the second highest price submitted for that year of the contract. Because it believed that Pearl's prices for the last 3 option years

²The apparent low bidder at bid opening was determined to be nonresponsive and ineligible for award.

were significantly less than cost in relation to what it termed an inflated or overstated price for the base year and first option year, the agency rejected Pearl's bid as unbalanced and made award to Ricardo on July 8; this protest followed.

An examination of bid unbalancing has two aspects. First, the bid must be evaluated mathematically to determine whether each item carries its share of the cost of the work specified for that item as well as overhead and profit. If the bid is based on nominal prices for some of the work and enhanced prices for other work, it is mathematically unbalanced. Second, the agency must determine whether award to a bidder that has submitted a mathematically unbalanced bid will result in the lowest overall cost to the government. If award to a party that submits a mathematically unbalanced bid may not result in the lowest overall cost to the government, the bid is materially unbalanced and cannot be accepted. QMSERV Corp., B-237691, Mar. 13, 1990; 90-1 CPD ¶ 271.

Pearl asserts that its bid is not unbalanced. The protester first contends that the government's cost estimate is incorrect. In addition, Pearl justifies its pricing structure by explaining that its implementation plan for REAM contracts has a higher start-up cost during the initial years because its approach is based on a sophisticated and detailed training program development process and because it establishes "state-of-the-art" communications and data processing systems; Pearl also asserts that there are significant facilities and staffing costs in the early stages of the project since Pearl is not currently operating in Richmond.

A large price differential between base and option periods, or between one option period and another, may be prima facie evidence of unbalancing. Professional Waste Sys., Inc.; Tri-State Servs. of Texas, 67 Comp. Gen. 68 (1987), 87-2 CPD ¶ 477. Here, the average anticipated quantities required are the same throughout the entire contract period, and Pearl's price for the 1-year base period is 46 percent higher than the price it bid for the last 2 option years. In contrast, the base period prices of the two next lowest bidders are between 12 and 18 percent higher than their prices for the last 2 option years. Further, Pearl's price for the first option year is 37 percent higher than its prices for the last 2 option years, while the second low bidder's price for the first option year is 13 percent and 16.5 percent lower than its prices for the last 2 option years, respectively; the third low bidder submitted the same price for all 4 option years. Moreover, Pearl's average price for the base period and the first option year is \$777; its average price for the last 3 option years is \$453--a

difference of 42 percent. In contrast, the differences between the other bidders' average prices for the base period and the first option year and their average prices for the last 3 option years are between 4 and 6.5 percent.

In addition, the agency estimates that, for each year of the contract, 100 properties will be assigned in the first month and 7 additional properties will be assigned in each following month, for a total of 177 properties per year. Using that estimate, which the protester does not dispute, Pearl's bid would not become the low aggregate bid until the eleventh month of the fourth option year.³

Pearl argues that the government's cost estimate of \$535 per property is based on formulas that are inappropriate for a REAM contract, and that the resulting cost estimate is "naive" and "unsubstantiated." The agency asserts that it prepared this cost estimate using averages based on statistics currently available to it for the services required under other REAM contracts; the protester does not rebut this assertion and we have no basis upon which to find the government's cost estimate unreasonable.

Pearl's explanation for its pricing methodology--that it has a higher start-up cost during the initial years due to a detailed training and program development process and must set up facilities in Richmond--is no more than an admission by Pearl that it submitted a front-loaded bid. While the protester may have a legitimate business concern for so structuring its bid, such a rationale is immaterial so long as the agency obtains reasonably-priced bids from responsible firms that are willing to accept the risks inherent in pricing each element of their bid to carry its proportionate

	<u>Pearl</u>	<u>Ricardo</u>	<u>Forsythe</u>
Base Year	\$148,149 ($\837×177)	\$123,900 ($\700×177)	\$115,935 ($\655×177)
1st Option	\$126,909 ($\717×177)	\$ 88,500 ($\$500 \times 177$)	\$101,775 ($\575×177)
2nd Option	\$ 81,066 ($\$458 \times 177$)	\$ 97,350 ($\$550 \times 177$)	\$101,775 ($\575×177)
3rd Option	\$ 79,827 ($\$451 \times 177$)	\$101,775 ($\575×177)	\$101,775 ($\575×177)
4th Option	\$ 79,827 ($\$451 \times 177$)	\$106,200 ($\600×177)	\$101,775 ($\575×177)
Total	\$515,778	\$517,725	\$523,035

If the prices attributable to the last 2 months of the final option year (14 properties at the fourth option year price) are subtracted from these totals, the low aggregate bid belongs to Ricardo, at \$509,325; Pearl's bid is \$509,464.

share of the total cost of the work. Westbrook Indus., Inc., 71 Comp. Gen. 139 (1992), 92-1 CPD ¶ 30; Crown Laundry and Dry Cleaners, Inc., B-208795.2; B-209311; Apr. 22, 1983, 83-1 CPD ¶ 438.

Whatever business reasons are offered to justify a particular bid, the government may not pay more for an item or service than its reasonable value. See Riverport Indus., Inc., 64 Comp. Gen. 441 (1985), 85-1 CPD ¶ 364, aff'd, B-218656.2, July 31, 1985, 85-2 CPD ¶ 108; Edgewater Mach. & Fabricators, Inc., B-219828, Dec. 5, 1985, 85-2 CPD ¶ 630. Thus, while start-up costs may be factored into a base period price so that a front-loaded base price does not automatically mean that the bid is unbalanced, the base period price may not carry a disproportionate share of the total contract price. Westbrook Indus., Inc., supra; Applicators, Inc., B-215035, June 21, 1984, 84-1 CPD ¶ 656. In cases where a contractor would have no use for equipment following contract performance, it may allocate the equipment cost to the base period of performance since, if options are not exercised, the contractor would not recover its cost of performance. Id. In other cases, equipment and start-up costs are expected to be apportioned over the evaluated contract period, i.e., including the option periods.

Here, Pearl relies on a general description of its purported start-up costs to explain why its prices for the base and first option year are significantly higher than its prices for the remaining 3 option years. Specifically, Pearl states that it:

" . . . has a higher startup cost during the initial years because the essence of our technical approach is based upon a very sophisticated and detailed training and program development process and the establishment of state of the art communications and data processing systems. In addition since we are not currently operating in the Richmond area there are significant facilities and staffing costs in early stages of the project."

Pearl has provided no other explanation of its costs or how it calculated its bid. To the extent that the costs referred to by Pearl include equipment (i.e., "communications and data processing systems"), Pearl makes no claim that it would have no use for its systems if the options were not exercised. The remainder of the claimed costs appear to constitute routine start-up costs. By including these costs in its prices for the base year and first option year so as to recoup them fully in the first 2 years of the contract, Pearl has attempted to shift the risk from itself to the government that contract performance might not extend

to 5 years. The government is under no obligation to accept that risk, particularly where other bidders, such as Ricardo, have accepted that risk and evidently structured their bids in light of it. Accordingly, under these circumstances, we think the contracting officer properly could view the protester's bid as mathematically unbalanced. Westbrook Indus., Inc., supra.'

A bid is materially unbalanced and must be rejected if there is a reasonable doubt that an award based on the mathematically unbalanced bid will result in the lowest overall cost to the government. OMSERV Corp., supra. We have found such reasonable doubt to exist in the following instances: where a bid does not become low unless all options are exercised and uncertainty exists whether the options will be exercised, see G.L. Cornell Co., B-236930, Jan. 19, 1990, 90-1 CPD ¶ 74; and where payments made under a contract awarded pursuant to a grossly unbalanced bid would amount to improper advance payments. See Nebraska Aluminum Castings, Inc.--Second Recon., B-222476.3, Nov. 4, 1986, 86-2 CPD ¶ 515. The agency argues that both of these instances exist here.

The agency reports that prior to the recent institution of the REAM contract concept, the Area Management Broker (AMB) contract concept was utilized for property management. The agency explains that six AMB contracts, still in their basic years, were recently resolicited without the exercise of their options to comply with the new REAM format. While the agency states that, at this time, it expects to exercise all options on this contract, it further states that it is possible that a change from REAM to another format would occur if HUD determined that the REAM concept was not efficient or cost-effective.


In cases involving extreme front-loading and where the mathematically unbalanced bid does not become low until the end of the final option year, the bid should not be accepted because, despite the agency's initial intent to exercise the options, intervening events could cause the contract not to run its full term, resulting in inordinately high cost to the government and a windfall to the bidder; in other words, there is reasonable doubt that the mathematically unbalanced

'Pearl's contention that HUD has awarded contracts where option year prices are significantly lower than those quoted by Pearl is not relevant to the award in this case, since each procurement is a separate transaction and agency action under one procurement does not affect the propriety of the agency's action under a different procurement. See Barnes Elec. Co., Inc., B-228651, Oct. 2, 1987, 87-2 CPD ¶ 331.

bid would ultimately provide the lowest cost to the government. Westbrook Indus., Inc., supra; Applicators, Inc., supra; Crown Laundry and Dry Cleaners, Inc., supra. Here, Pearl does not become the low bidder until the eleventh month of the final year of the 5-year contract, if all options are exercised. Thus, we think the agency had sufficient reason to doubt that acceptance of Pearl's bid would actually provide the lowest cost to the government, and therefore it properly rejected the bid as unbalanced. Westbrook Indus., Inc., supra; Professional Waste Sys., Inc.; Tri-State Servs. of Texas, supra.

Since we have determined that rejection of Pearl's bid was proper because it will not become low unless all options are exercised and uncertainty exists whether all the options will be exercised, we need not reach the issue of whether the acceptance of Pearl's bid would have been tantamount to allowing an advance payment.

The protest is denied.


James F. Hinchman
General Counsel