



Comptroller General  
of the United States  
Washington, D.C. 20548

## Decision

**Matter of:** Sabre Systems, Inc.  
**File:** B-255311  
**Date:** February 22, 1994

Robert M. Cambridge, Esq., for the protester,  
Demetria T. Carter, Esq., and Daniel Laguaite, Esq.,  
Department of the Navy, for the agency,  
Henry J. Gorczycki, Esq., Guy R. Pietrovito, Esq., and  
James A. Spangenberg, Esq., Office of the General Counsel,  
GAO, participated in the preparation of the decision.

### DIGEST

In performing a probable cost analysis for the award of a cost reimbursement contract, the contracting agency properly adjusted offerors' estimated costs of contract performance in the contract's option years to account for anticipated escalation in labor costs by applying an escalation rate to the offerors' direct labor rates.

### DECISION

Sabre Systems, Inc. protests the award of a contract to Diverse Technologies Corporation<sup>1</sup> under request for proposals (RFP) No. N00421-93-R-0008 issued by the Naval Air Warfare Center, Department of the Navy, for clerical support services. Sabre challenges the Navy's cost realism analysis.

We deny the protest.<sup>2</sup>

The Navy issued the RFP on January 15, 1993, contemplating the award of cost-plus-fixed-fee, level-of-effort contract for 1 base and 4 option years. The RFP stated that award would be made to the offeror submitting the lowest evaluated cost, technically acceptable proposal. Offerors were informed that the Navy would perform a cost realism

<sup>1</sup>Diverse Technologies was previously known as Operational Systems, Inc.

<sup>2</sup>Sabre's counsel was admitted to the protective order that was issued in this case and received access to protected material. Our decision is based in part upon protected, confidential information and is necessarily general.

analysis, and were required to submit cost data for the agency's cost realism analysis, which at a minimum was to include direct labor rates, other direct costs, indirect costs such as overhead and general and administrative expense (G&A), and escalation rates for proposed labor costs.

The RFP identified four labor categories of personnel to be provided under the contract and stated an anticipated level of effort of 51,000 hours of direct labor. The RFP also incorporated by reference the "Service Contract Act of 1965" (SCA) clause, as set forth at Federal Acquisition Regulation (FAR) § 52.222-41, which states that the contract is subject to the SCA and that employees in labor categories subject to the SCA must receive the minimum levels of compensation as determined by the Secretary of Labor on a periodic basis. All of the RFP's labor categories were identified as subject to the SCA.

Seventeen offerors submitted proposals by the closing date of March 9, 1993. Seven proposals, including Sabre's and Diverse Technologies's, were determined to be technically acceptable and were evaluated for cost realism.

In its evaluation of cost proposals, the Navy found that several offerors had not provided for escalation of labor costs, as required by the RFP. Because the contract labor categories are subject to the SCA, the Navy decided that offerors' proposed option years direct labor costs should be escalated to account for anticipated future increases in wage rates under the SCA. The Navy accepted as reasonable the labor escalation rates proposed by the offerors, and applied a 3.5 percent escalation rate to those cost proposals that failed to provide for labor escalation. The Navy then calculated offerors' probable costs of performance, with and without escalation of labor costs.

Sabre did not provide for escalation of its proposed labor costs, and the Navy applied a 3.5 percent labor escalation rate to its labor rates. Diverse Technologies provided for a labor escalation rate that was slightly higher than 3.5 percent, which, as noted above, the Navy accepted as reasonable. Sabre's and Diverse Technologies's proposed and probable costs were as follows:

<u>Offeror</u>	<u>Proposed</u>	<u>Without Escalation</u>	<u>With Escalation</u>
Diverse Tech.	\$3,834,817	\$3,543,268	\$3,818,594
Sabre	3,408,875	3,596,821	3,845,063

On October 1, 1993, the Navy awarded a contract to Diverse Technologies as the offeror with the lowest evaluated cost, technically acceptable proposal. This protest followed.

Sabre challenges the methodology employed by the Navy to compare the offerors' proposed costs, with and without labor escalation. Sabre argues that its proposed unescalated labor costs should have been compared to Diverse Technologies's escalated labor costs because Sabre did not propose labor escalation while Diverse Technologies did. Sabre alternatively argues that the Navy's calculation of Sabre's escalated costs was unreasonable because the Navy allegedly applied the labor escalation rate to Sabre's estimated indirect cost rates, such as its rates for G&A expenses and material and handling costs. Sabre also argues that the Navy improperly increased Sabre's indirect rates based upon advice from the Defense Contract Audit Agency (DCAA).<sup>3</sup>

Where, as here, an agency evaluates proposals for the award of a cost reimbursement contract, an offeror's proposed estimated costs of contract performance are not dispositive because, regardless of the costs proposed, the government is bound to pay the contractor its actual and allowable costs. FAR § 15.605(d); Amtec Corp., B-240647, Dec. 12, 1990, 90-2 CPD ¶ 482. Consequently, a cost realism analysis must be performed by the agency to determine the extent to which an offeror's proposed costs represent what the contract should cost, assuming reasonable economy and efficiency. CACI, Inc.-Fed., 64 Comp. Gen. 71 (1984), 84-2 CPD ¶ 542. Because the contracting agency is in the best position to make this cost realism determination, our review is limited to determining whether the agency's cost realism analysis is reasonably based and not arbitrary. General Research Corp., 70 Comp. Gen. 279 (1991), 91-1 CPD ¶ 183, aff'd, American Mgmt. Sys., Inc.; Department of the Army--Recon., 70 Comp. Gen. 510 (1991), 91-1 CPD ¶ 492.

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<sup>3</sup>Sabre also argues the Navy should have accepted Sabre's estimated costs of performance in its cost realism analysis because the RFP contained the standard "Limitation of Funds" clause, FAR § 52.232-22, allegedly limiting Sabre's recovery of costs under the contract to the estimated costs which it proposed. We disagree. Under the cost reimbursement contract to be awarded here, the government will pay the contractor for all allowable costs incurred; the risk of actual costs exceeding estimated costs is borne by the government. See FAR § 16.306. The limitation of funds clause limits the government's risk to the amount allotted to the contract and specifically provides for increasing the contractor's estimated cost up to the amount allotted by the government to the contract. FAR § 52.232-22(g).

Here, we find that it was reasonable to account in the cost evaluation for anticipated escalation in labor rates as applied to the offerors' proposed labor costs, given the agency's belief that labor costs would escalate, as reflected by the RFP's requirement to provide labor escalation rates. The Navy estimated that labor rates under the SCA would escalate by 3.5 percent per year, which Sabre concedes is reasonable. An agency should adjust cost proposals in its cost realism analysis to reflect the agency's reasonable projection of anticipated escalation in labor rates over the term of the contract; where one proposal includes labor escalation and another proposal excludes labor escalation, the proposals should be normalized to include anticipated labor escalation.<sup>4</sup> See General Research Corp., supra.

Sabre next argues that the agency's calculation of its escalated costs was unreasonable because the Navy allegedly applied the labor escalation rate to Sabre's estimated indirect cost rates. The record does not support this allegation.

The Navy escalated Sabre's labor rates for each labor category, including those for any proposed subcontractor personnel, by 3.5 percent for each of the option years of the contract; the agency then used the costs of direct labor produced by the escalated labor rates to calculate the related indirect costs, such as labor overhead and G&A expense. The Navy used the fixed rates for allocating these other costs which were applicable to each offeror. In the case of Sabre's proposal, the agency relied on advice from the DCAA and increased the indirect cost allocation rates proposed by Sabre; these fixed indirect cost rates, as increased in accordance with DCAA's advice, were applied uniformly throughout the agency's cost realism analysis. Contrary to the protester's arguments, Sabre's indirect rates were not escalated as were the labor rates; however, the escalation of the labor rates by 3.5 percent had the effect of increasing the actual dollar value of the indirect

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<sup>4</sup>Ordinarily, the same percentage multiplier or escalation rate should be employed in normalizing offerors' proposed labor costs. See General Research Corp., supra. Here, Diverse Technologies's price advantage would be even greater if its proposed labor costs were escalated only by 3.5 percent, rather than at its proposed slightly higher rate. We also note that Diverse Technologies's evaluated costs were lower than Sabre's, whether the firms' costs were escalated or not.

costs that were derived, either directly or indirectly, from the escalated direct labor costs.<sup>5</sup>

Sabre nevertheless argues that the dollar values of certain expenses, such as G&A and material and handling costs, should remain fixed throughout the entire term of the contract, even if the underlying labor rates are escalated for the cost analysis.<sup>6</sup> For example, with regard to labor overhead, Sabre suggests that a lower allocation percentage be used in the option years. However, Sabre did not propose either a fixed dollar value for its indirect costs or a lower overhead allocation percentage for the option years, but rather proposed a fixed percentage for each indirect cost category, based either directly or indirectly on direct labor costs. Therefore, it was proper for the Navy to recalculate the dollar value of these costs as the labor rates were escalated using the fixed allocation rates proposed by Sabre and adjusted for realism by the Navy. See Dynalectron Corp.; Lockheed Elecs. Co., Inc., 54 Comp. Gen. 562 (1975), 75-1 CPD ¶ 17.

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<sup>5</sup>For example, Sabre's overhead cost on labor was a percentage of total direct labor costs, and G&A expense was a percentage of the sum of total direct labor and labor overhead costs. As labor rates were escalated by 3.5 percent, the total direct labor costs increased. Accordingly, all of the cost allocations derived using this greater figure for direct labor costs also increased, even though the allocation percentages were fixed. Similarly, materials and handling costs allocated to administering the subcontract in Sabre's proposal were calculated using a fixed percentage of the total costs of the subcontract; thus, as the subcontractor's labor rates were escalated by 3.5 percent, the dollar value of the subcontractor's allocated costs also increased, which ultimately increased the dollar value of Sabre's materials and handling costs.

<sup>6</sup>In this regard, Sabre argues that the solicitation should have included the "Fair Labor Standards Act and Service Contract Act--Price Adjustment" clause, as set forth in FAR § 52.222-43, which provides for adjusting fixed-priced contracts for Department of Labor wage determinations made during the term of a contract. This clause applies only to fixed-price contracts, and is inapplicable here. In any event, this protest allegation concerns an apparent alleged solicitation impropriety that should have been protested prior to the submission of initial offers. 4 C.F.R. § 21.2(a)(1) (1993).

Finally, Sabre alleges that the Navy's decision to increase Sabre's proposed indirect cost allocation rates in the agency's cost realism analysis was unreasonable. However, the Navy did so on the advice of DCAA after DCAA had reviewed cost information submitted by Sabre. A contracting officer may generally rely on DCAA advice in performing a cost realism analysis absent evidence that the advice is incorrect. Delta Research Assocs, Inc., B-254006.2, Nov. 22, 1993, 94-1 CPD ¶ \_\_\_\_; NFK Eng'g, Inc.; Stanley Assocs.; B-232143; B-232143.2, Nov. 21, 1988, 88-2 CPD ¶ 497. Since Sabre has not shown the rates recommended by DCAA to be incorrect or unreasonable, we find the agency's reliance upon DCAA's suggested rates to be reasonable.<sup>7</sup>

We have checked the Navy's cost realism analysis for both Sabre's and Diverse Technologies's cost proposals and find that the agency consistently and accurately calculated the evaluated, escalated costs of each of proposal and that the cost realism analysis was otherwise reasonable. Thus, Diverse Technologies was reasonably determined to be the offeror with the lowest evaluated cost, technically acceptable proposal, and the award was proper.

The protest is denied.

*Ronald Berger*  
for Robert P. Murphy  
Acting General Counsel

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<sup>7</sup>Sabre also argues that since DCAA did not "audit" Sabre's cost information, the Navy should not have relied on this advice. This information was provided by Sabre, and, as noted above, Sabre does not allege that the information which it provided was inaccurate or unreliable. Accordingly, this provides no basis to question DCAA's rate advice.