



U.S. Department
of Transportation
**Federal Highway
Administration**

Kockne Wick *Dust* *Star*
Cef

Memorandum

312 Mohawk Building
708 S.W. Third Avenue
Portland, Oregon 97204

Subject: Rejection of Unbalanced Bids

Date: July 29, 1987

From: M. Eldon Green
Regional Administrator

Reply to
Attn. of: HEO-010.2

To: DIVISION ADMINISTRATORS

Mr. B. F. Morehead, Juneau, Alaska (HDA-AK)
Mr. J. T. Coe, Boise, Idaho (HDA-ID)
Mr. D. E. Wilken, Salem, Oregon (HDA-OR)
Mr. P. C. Gregson, Olympia, Washington (HDA-WA)

Assistant Regional Counsel Lawrence Hanf has recently prepared the attached position paper regarding the rejection of unbalanced bids. The conclusion is basically that unbalanced bids are not allowed under the following circumstances:

1. If there is a specific clause in the contract prohibiting unbalanced bidding and the Government can show that the bid was mathematically unbalanced; or
2. If the contractor grossly front-end loads its bid so as to amount to an advance payment or an interest-free loan; or
3. If the unbalancing of the bid on an option contract or an estimated quantities contract with an unreliable estimate, creates a reasonable doubt that the apparent low bid will actually result in the lowest cost to the Government.

We have evaluated his paper and fully endorse the conclusion. The FHPM 6-4-1-6 requires the FHWA evaluate the unit bid items for reasonable conformance with the engineers estimate. Bids with extreme variations from the engineers estimate or other bids received, or where obvious unbalancing of unit prices has occurred, should be thoroughly evaluated by the FHWA and brought to the SHA's attention for further review and discussion before concurrence in award. In the event of potential bidding irregularities the Division Administrator must take appropriate steps to protect the Federal interest.

In addition a closer evaluation of the engineers estimate and bid prices prior to award can lead to a reduction in claims, change orders and contract disputes, as well as bring about improvements to the estimating process.

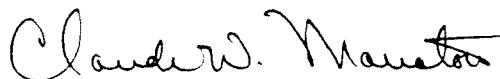
During the next few months the Divisions should evaluate the bidding and estimating practices in their State. When irregularities are noted, appropriate actions should be taken by the Division and SHA to protect the Government interest. Also for your information we have attached copies of recent actions taken in Region 4 and 6 on this subject.

July 29, 1987

We will be especially interested in seeing comments of your observations or findings when reported in the next scheduled prequalification and bidding review for your SHA.

If we can be of any assistance to the Division during your review please don't hesitate to contact this office.

Attachment



Claude W. Manaton, Director
Office of Engineering and Operations

cc:  R. Hurst (HHO-32)
L. Hanf (HRC-010)



U.S. Department
of Transportation
**Federal Highway
Administration**

Memorandum

Room 312 Mohawk Building
708 S. W. Third Avenue
Portland, Oregon 97204

Subject: Rejection of Unbalanced Bids

Date: July 24, 1987

From: Assistant Regional Counsel

Reply to
Attn of HRC-010

To: Mr. Frank Baldwin
Contract Development Engineer (HDF-17.11)
Western Direct Federal Division

Lance Hanf recently prepared the attached paper regarding rejection of unbalanced bids. In sum, the paper concludes that unbalanced bids are not allowed under the following circumstances:

1. there is a specific clause in the contract prohibiting unbalanced bidding and the Government can show that the bid was mathematically unbalanced;
2. the contractor grossly front-end loads its bid so as to amount to an advance payment or an interest-free loan;
3. the unbalancing of the bid on an option contract or an estimated quantities contract with an unreliable estimate creates a reasonable doubt that the apparent low bid will actually result in the lowest cost to the Government.

In addition, unbalanced bids can lead to unnecessary claims in those instances where the quantity of an unbalanced high priced item underruns or the quantity of an unbalanced low priced item overruns.

Given the above, let's start reviewing low bids to see whether they are unbalanced and should be rejected either for being grossly front-end loaded or because there is a reasonable doubt that they will result in the lowest cost to the Government.

James F. Zotter

James F. Zotter

Attachment

cc: John Rippley (HRC-08) w/attach
John Kraybill (HRC-06) w/attach
David Ortey (HRC-09) w/attach
John Price (HB-OR) w/attach
Jim Sorenson (HEO-010.2) w/attach



U.S. Department
of Transportation
**Federal Highway
Administration**

Memorandum

Room 312 Mohawk Building
708 S. W. Third Avenue
Portland, Oregon 97204

Subject Unbalanced Bids

Date June 10, 1987

From Attorney Advisor

Reply to
Attn of HRC-010

To: Mr. James F. Zotter
Assistant Regional Counsel (HRC-010)

There are numerous reasons why a contractor may want to unbalance its bid on a contract solicitation.

One reason a contractor might unbalance its bid is to get more of the funding at the beginning of the project. The contractor does this by overpricing the work done early on in the project. This is called "front loading" the contract.

Another reason a contractor might unbalance its bid is if it thinks that a particular item will be used more than the solicitation estimates. Thus, the contractor will maximize its profit by overpricing this item. Likewise, if its an option contract where the contractor feels the options will not be exercised, the contractor will maximize its profit by bidding higher for the base project and significantly discounting the option part of the contract.

Moreover, one can discount anticipated underruns to achieve being awarded the contract, or overprice difficult to control items, like watering, to maximize profits.

Since we generally don't have option contracts in the Federal Highway Administration, we are mostly concerned with estimated quantity contracts.

Often contractors will front load their bids so that they will get paid more money at the start of their work. In Matter of: Nebraska Aluminum Casting, Comp. Gen. B-222476.3, November 4, 1986, the contractor inflated the first article prices over 1,000 times greater than the unit price: \$22,510 as opposed to \$19.17. The Comptroller General held that this bid was "grossly" front loaded, and thus should be considered an unresponsive bid and may be rejected. Moreover, the court said:

"Even though the solicitation at issue here may have contained no express notice cautioning bidders that first article pricing should reflect only reasonable production and testing costs, the rejection of Nebraska Aluminum

Casting is required in order to maintain the integrity of the competitive system." Id.

The Comptroller General went on to hold that grossly front-loaded bids are a per se violation. Id.

The leading case in the front-loading area is Matter of: Riverport Industries, 64 Comp. Gen. 441 (1985). Here the Comptroller General held that if the bid is front loaded, regardless if it is the lowest bid, it "should be viewed as materially unbalanced since acceptance of the bid would result in the same evils as an advance payment. An advance payment is prohibited by law." Id.

"Gross" front loading is a fact question. For example, 2.6 percent more for the first items is not gross front loading in Matter of: Kidde, Inc. Weber Aircraft Division, Comp. Gen. B-223935 (1986), whereas 36 times more for the first items is considered grossly front loaded and hence an unresponsive bid. Matter of: Islip Transformer & Metal Co., Comp. Gen. B-225257 (1987).

A contract may be unbalanced for more than one reason. For example, a contractor could "front load" the contract and also unbalance other items to gain an extra profit or the initial contract award. In short, an unbalanced contract could be "front loaded" as well as unbalanced for other reasons.

As mentioned before, there are numerous reasons to unbalance bids. There are two types of contracts which attract unbalanced bids: estimated quantity contracts and option contracts. Unlike the contract problem of front loading, these unbalanced bids are generally unbalanced to reap profits on overruns or gamble on underruns. Also, unlike the problem of front loading, there is no per se prohibition of unbalancing bid items.

There are two types of unbalanced bidding: mathematically unbalanced bids and materially unbalanced bids.

It is widely held that there is no per se prohibition of mathematically unbalanced bids. A mathematically unbalanced bid has been described this way:

"A bid is mathematically unbalanced if the bid is structured on the basis of nominal prices for some work and inflated prices for other work; that is, each element of the bid must carry its proportionate share of the total cost of work plus profits." Matter of: Howell Construction, Comp. Gen. B-225766 (1987)

For example, if there is similar work being done in two time periods and there's a large price differential, this is prima

facie evidence that a bid is mathematically unbalanced. Matter of: USA Pro Co., Comp. Gen. B-220976 (1986).

However, as mentioned previously, mathematically unbalanced bids are not per se prohibited. Evidence of a mathematically unbalanced bid is, however, the first step in proving a bid is materially unbalanced. A bid which is materially unbalanced is defective and thus can be voided by the court. A materially unbalanced bid has been defined as:

"A bid is materially unbalanced if there is a reasonable doubt that award to the bidder submitting the mathematically unbalanced bid will result in the lowest ultimate cost to the Government. Consequently, a materially unbalanced bid may not be accepted." Matter of: Crown Laundry and Dry Cleaners, Comp. Gen. B-208795.2, April 22, 1983.

One situation in which materially unbalanced bids are encountered is a solicitation which has a base period of work and then an option period thereafter. In this case, the bid is evaluated for the total cost - base plus option years. In Matter of: Crown Laundry & Dry Cleaners, supra (1983), the contractor had bid its base year prices substantially higher than the second option year. The court said:

"The contracting officer also found the bid to be materially unbalanced, observing that Crown's price would not become low until well after the second option was exercised and that, therefore, a reasonable doubt existed that Crown's bid would ultimately be the most advantageous to the Government." Id.

In each procurement, it is a fact question as to whether the unbalanced bid will result in the lowest ultimate cost to the Government. Matter of: Solon Automated Services, Comp. Gen. B-206449.2 (1982). Therefore, each case must evaluate the facts to determine whether there is a reasonable doubt that the bid will be the lowest cost to the Government. The further the contract must go into the option period to achieve the lowest bid, the more superseding events could alter the exercise of the option period. Consequently, this creates a reasonable doubt that the unbalanced bid will actually be the lowest. Compare Matter of: Jimmy's Appliance, Comp. Gen. B-205611 (1982).

When evaluating unbalanced bids using the "reasonable doubt" test, if the unbalanced bid only becomes lowest in the option year, one also must calculate how much in cost savings the unbalanced bid has over the balanced bid. The greater the cost savings with the unbalanced bid, the more likely it will result in the lowest ultimate cost to the Government. For example, in Matter of: Jimmy's Appliance, supra, (1982) the unbalanced bid became lowest

in the first option year and the cost difference was 44 percent from the next lowest bid. Since the burden of proof is on the party protesting the contract, to void the unbalanced bid contract one must prove that there is "reasonable doubt" that the unbalanced bid will result in the lowest cost to the Government. Given the facts in Matter of: Jimmy's Appliance, the court found the burden of showing a "reasonable doubt" was not met and allowed the unbalanced bid contract to stand. In contrast to Matter of: Jimmy's Appliance, supra (1982), in Matter of: Howell Construction, supra, the bid only became lowest in the fourth month of the second option year, and the price was only 10 percent less than the next lowest bid, allowing the court to find that there was a "reasonable doubt" that Howell's bid would actually be the lowest to the Government.

To have an unbalanced bid, the bid must have items which are overstated as well as understated. This is because if you only had understated items creating the unbalance, a change in quantity would not economically hurt the Government or create a "reasonable doubt" that the unbalanced bid would result in the lowest cost to the Government.

In Matter of: Impsa International, Comp. Gen. B-221903, June 2, 1986, the low bidder had bid the installation items very low. In denying the protest, the court said:

"There are no pricing variables involved in this IFB, such as estimated quantities or option periods, through which Allis-Chalmers, by enhancing its equipment prices, could recoup any losses occasioned by underbidding the installation items . . . Rather, the agency is purchasing a complete hydroelectric power system on a lump-sum, firm-fixed-price basis, and, therefore, we see no possibility that acceptance of Allis-Chalmers' bid will ultimately prove not to be in the Government's best economic interest." Id.

Like the problem with option contracts, estimated quantity contracts can be a problem with unbalanced bids. In Matter of: TRW, Inc., 61 Comp. Gen. 99 (1981), the Navy solicited bids for 48 labor and material line items. Bids were evaluated by estimating quantities over the contract term, but there was also a clause for "any unforeseen growth". One contractor submitted a mathematically unbalanced bid, bidding low the large estimates of labor-intensive items and high on the smaller items. The quantities were estimated on only a historical period of one year and also could be changed by the "any unforeseen growth" clause. Therefore, the court allowed the rejection of the mathematically unbalanced bid, reasoning that:

". . . the Navy's estimates cannot be relied upon to overcome the effects of a mathematically unbalanced bid . . . We believe that it may also be materially unbalanced, since - although it has been evaluated as low - it may not actually result in the lowest cost to the Government. Under these circumstances, we believe the bid must be rejected."

One way to avoid the problems of unbalanced bids is to put a clause in the contract prohibiting unbalancing bids. However, it is important to be explicit in the wording. For example, in North Virginia Van Company v. U.S., 3 Cl. Ct. 237 (1983), GSA tried to use an amendment to the solicitation which would avoid the problem of unbalanced bids. The clause said "prices must be quoted on each item in the bid schedule to be considered for award, (i.e., 'o', no change, N/C and N/A will be considered unresponsive)." However, this clause did not mention under or over estimating items. Since some contractors submitted unbalanced bids while others did not, the court voided the contracts because of the ambiguous language. The court did note, however, that "contractors are entitled to know how their bids will be evaluated; they cannot effectively compete when the standards for judgment exist only in the contracting officer's head".

This shows the importance of having clear and explicit language in the contract if one wants to avoid certain types of bids.

In conclusion, where the contract solicitation has unknowns such as estimated quantities or option provisions, and there is an unbalanced bid, if the Government or another interested party can show there is a "reasonable doubt" that bid will result in the lowest cost to the Government, the unbalanced bid may be voided. If the bid is grossly front loaded, the bid may be voided. The best way to avoid the unbalanced bid problem, however, is to put explicit language in the solicitation prohibiting the use of unbalanced prices on items.

If the solicitation includes language which prohibits unbalancing bids, the unbalanced bid may be rejected as nonresponsive, and the remedy is to award the contract to the next lowest responsive bidder.

In the Matter of: TRW Incorporated, supra, the court rejected a bid as materially unbalanced and said, "and [we] therefore recommend that award be made to the next lowest evaluated bidder who has submitted a mathematically balanced bid." (Emphasis added) In the same vein, in Matter of: SMC Information Systems, Comp. Gen. B-224466 (1986), the plaintiff successfully brought an action to overturn its rejected bid and was awarded the contract. The contract had been given to the second lowest bidder. Again, this suggests that if a bid is correctly rejected, the award goes to the next lowest responsive bidder. If more than one bid is

materially unbalanced, each of those bids will be rejected and cannot be awarded the contract under the solicitation. Matter of: Edgewater Machine & Fabricators, Inc., Comp. Gen. B-219828 (1985).

Moreover, in the situation of grossly front-loaded bids, the bid may be rejected as nonresponsive even though the solicitation does not explicitly prohibit unbalanced bids. Matter of: Islip Transformer & Metal Co., Comp. Gen. B-225257 (1987); Matter of: Nebraska Aluminum Casting, Inc., second request for reconsideration, B-222476.3 (1986); Matter of: Edgewater Machine & Fabricators, Inc., supra (1985). Again, in this situation the contract would be awarded to the next lowest responsive bidder.

The other remedy the Government can use is to cancel the solicitation in its entirety and reissue the solicitation. For example, in the Matter of: Edward B. Friel, Inc., 55 Comp. Gen. 231 (1975), the contract was canceled and reissued. In Friel it was determined that the estimated quantities were defective, so depending on how one calculated the estimates, one would get different low bidders. Therefore, it was determined that there was a "reasonable doubt" that an award to any of the bidders would result in the lowest overall cost. Id. Further, to award the contract using a new estimate to evaluate the bids "would be contrary to the open and public nature of advertised procurement procedures and to the requirement that the IFB inform all bidders of the objective factors upon which they are to submit their bids and on which their bids are to be evaluated." Id.

To cancel a solicitation, the Government must show a cogent and compelling reason. In the context of canceling an IFB, at least two factors are involved: "(1) whether the best interests of the Government would be served by making an award under the subject solicitation and (2) whether any bidder would be treated in an unfair and unequal manner if an award was made under the IFB." Matter of: Government Contractors, Inc., Comp. Gen. B-219411.2 (1985); Matter of: North American Labs of Ohio, 58 Comp. Gen. 724 (1979); Matter of: Friel, Inc., supra (1975).

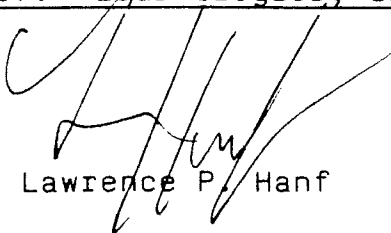
Applying these factors in the Friel case, the Government's best interest was served in canceling a defectively estimated solicitation, and to award the contract using new estimates would be unfair to the other bidders who relied on the information in the contract.

However, simply because a contract does not explicitly prohibit unbalanced bidding and the contract is deficient in some way, that does not create a per se cancellation. Each case must rest on its own facts. As the Friel case said:

"For instance, even in a case where the agency believed the IFB's purchase description to be materially deficient,

our office found no cogent and compelling reason to support the cancellation where bidders had offered to meet the Government's actual requirements and the cancellation was believed to damage the integrity of the competitive bidding system. See 52 Comp. Gen. 285 (1972). In Matter of: Joy Manufacturing Company, 54 Comp. Gen. 237 (1974), 74-2 CPD 183, the agency canceled an IFB and proposed to resolicit because it desired to add additional specifications. However, it appeared that the low, responsive bid had offered an item which might meet the additional specifications which were proposed to be added. In these circumstances, our office held that acceptance of the low bid--if it were found to meet all of the Government's actual needs--would work no prejudice to the other nonresponsive bidders."

In conclusion, if the bid is grossly front loaded, the bid may be rejected and the next lowest responsive bid may be selected. If the solicitation prohibits unbalancing bids, an unbalanced bid may be considered nonresponsive and thus rejected. Again, the next lowest responsive bid may be selected. If, however, an IFB fails to explicitly prohibit unbalancing the bid and the Government can show a cogent and compelling reason to cancel the solicitation, the appropriate remedy is to cancel the solicitation rather than reject the unbalanced bid and award the contract to the next lowest responsive bidder. Matter of: T.L. James & Co., Inc., 64 Comp. Gen. 848 (1985); Matter of: Lear Siegler, Inc., Comp. Gen. B-205594.2 (1982).



Lawrence P. Hanf

which bids or offers are being considered for award. If, after examination, the contracting agency believes that the solicitation's estimate is a reasonably accurate representation of actual anticipated needs, then the mathematically unbalanced low bid may be accepted.

On the other hand, in cases where the contracting agency concludes after examination that the solicitation's estimate is not a reasonably accurate representation of actual anticipated needs, we have indicated that the solicitation should be canceled. 55 Comp. Gen. 231, 237 (1975).

Under the Comptroller General's reasoning, a mathematically unbalanced bid merely calls into question the estimated contract quantities. If the estimated quantities are valid, no harm is done to the competitive bidding process. If the estimated quantities are inaccurate, the solicitation should be canceled (as opposed to rejecting the unbalanced bid). The Comptroller General considers the ultimate lowest cost to the Government to be the primary criteria.

State highway departments may have more discretion in dealing with unbalanced bids due to their specifications. The 1984 AASHTO Guide Specification at section 102.07(e) provides that proposals may be rejected "if the Department determines that any of the unit bid prices are significantly unbalanced to the potential detriment of the Department." This would appear to allow the consideration of more factors than those normally examined by the Comptroller General.

As a practical matter, few, if any, bids are truly mathematically balanced (i.e., every single bid item carrying its proportionate share of costs). It is, therefore, not feasible to reject all unbalanced bids. Some standard of materiality or significance must be applied. If the standard permits too much discretion, it could open the competitive bidding system to favoritism. If the standard is too broad, excessive litigation and uncertainty could be the result. As a general rule, the competitive bidding system works best with the least subjective decision making. Encouraging States to reject bids based on subjective decisions that they are "unbalanced" could lead to other abuses and increased litigation.

As suggested in the briefing paper, the first approach should be to examine what is causing the unbalanced bidding. If contractors are bidding too high on mobilization, the specifications should be altered to reduce the accelerated payment for mobilization or to limit mobilization to a fixed percentage of the contract. If low bids on certain items (e.g., traffic control) are adversely affecting contract performance, the solution could be to designate a mandatory unit price for those items.

Except in those instances where an unbalanced bid meets the Comptroller General's test of being "materially unbalanced" because of inaccurate quantity estimates, rejection of bids should be a solution of last resort.

JOHN M. RIPPLEY

John M. Rippley

Attachment

cc: ROJones-Chron File
JMRippley-Chron File
yc: HRC-File
pc: HAD-File
JMRippley:jv:06/16/87 (unbalanced bids)

Subject: Alabama Project IR-59-2(77)
Etowah County

Date June 24, 1987

From: Division Administrator
Montgomery, Alabama

Reply to
Attn of: HDA-AL

To: Mr. Leon N. Larson
Regional Federal Highway Administrator (HRA-04)
Atlanta, Georgia

The attached correspondence and documents all relate to a project for which bids were opened on May 29, 1987.

The apparent low bidder's unit price of \$90 per linear foot for horizontal drain was ten times the engineer's estimate and also ten times the second and third low bidders' prices for the same item. The State failed to check the quantity of the item during the preaward review and recommended concurrence in award of contract. During the area engineer's review of the State's request for concurrence in award, the quantity of longitudinal drain was checked and a substantial error found. The PS&E quantity of 2200 feet should have been 6500 feet. Using the \$90/lin. ft. unit price, this item would overrun \$387,000 which exceeds the difference between the first and third low bidders.

The State was advised that we would not concur in the award and that it would be necessary to correct the PS&E and readvertise the project.

This information is provided so that you and the Washington office may be informed should the contractor or members of Congress raise questions about my action. I have already received a telephone inquiry from Mr. Tom Morgan of Congresswoman Marilyn Lloyd's office.

The apparent low bidder, Wright Brothers Construction Co., Inc. of Charleston, Tennessee, submitted an unbalanced bid on borrow excavation on project APD-471(9) in the July 1986 letting. That bid was eventually awarded after a thorough check of quantities was made.

JOE D. WILKERSON

Joe D. Wilkerson

Attachments

cc:
Washington (HHO-1)

*Joe - It does not look to check
the bid award*