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**Comptroller General
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**United States Government Accountability Office
Washington, DC 20548**

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Decision

Matter of: Veolia Water North America Operating Services, LLC

File: B-291307.5; B-298017

Date: May 19, 2006

Kenneth A. Martin, Esq., for the protester.

Robert E. Little, Jr., Esq., Department of the Navy, for the agency.

Guy R. Pietrovito, Esq., and James A. Spangenberg, Esq., Office of the General Counsel, GAO, participated in the preparation of the decision.

DIGEST

1. In negotiated procurements for privatization of utility system assets, protester has not shown that the agency erred in determining that 10 U.S.C. § 2688(f)(2) prohibited the conveyance of utility assets under a proposed scheme in which the protester would contract to operate and maintain the utility system assets and would not retain title in the assets, but would simultaneously transfer title in the assets to an unrelated third party which the agency was required to acknowledge as the primary obligor for the purchase price of the assets.

2. Protest requesting GAO's recommendation based upon a promissory estoppel theory of detrimental reliance by the protester upon alleged actions of the agency that are not grounded upon an asserted statutory or regulatory violation will not be considered because the Competition in Contracting Act of 1984 only authorizes GAO to decide bid protests concerning alleged violations of a procurement statute or regulation.

DECISION

Veolia Water North America Operating Services, LLC protests the conduct of negotiations by the Naval Facilities Engineering Command (NAVFAC), Department of the Navy, under request for proposals (RFP) No. N62470-00-R-3602, issued by NAVFAC's Atlantic Division to competitively select parties for the privatization (including the transfer of title to private parties) of potable water and wastewater collection utility systems in North Carolina, Virginia, and West Virginia (collectively

known as “Utility Privatization Area C”)¹ and under RFP No. N62467-00-R-1802, issued by NAVFAC’s Southern Division to conduct a competition for the privatization of potable water and wastewater collection utility systems in Mississippi, Louisiana, Texas and Florida (collectively known as “Utility Privatization Area E”).² Veolia complains that NAVFAC rejected, after significant time and expense by Veolia, a third-party ownership of the utilities approach (explained below), which was suggested by NAVFAC and upon which basis Veolia’s proposals were selected after the competition for exclusive negotiation with the agency.³ Veolia contends that NAVFAC improperly rejected Veolia’s proposals based upon an erroneous determination that Veolia’s proposed contract structure to acquire the utility assets violated the statute governing the conveyance of those assets.

We deny the protests.

BACKGROUND

The RFPs, issued October 29, 1999 and March 17, 2000, offered for sale potable water and wastewater collection utility systems at a number of facilities. Specifically, offerors were informed that

[t]he purpose of this solicitation is to select an Offeror(s) for the purpose of privatizing utility systems specified herein. Privatization is the conveyance of the utility system ownership to a private entity who will be responsible for the operation, maintenance and capitalization of the infrastructure for the foreseeable future and for the provision of safe and reliable utility services to the Department of the Navy in exchange for reasonable compensation.

¹ Utility Privatization Area C was identified as including 16 different installations and 58 different utility systems. RFP No. 3602, at 4. Offerors were not required to propose for all solicited installations and utility systems and multiple awards could be made.

² Utility Privatization Area E was identified as including 11 different installations and 60 different utility systems. RFP No. 1802, at 4. Offerors were not required to propose for all solicited installations and utility systems and multiple awards could be made.

³ Veolia’s protest under RFP No. 3602 was filed on February 10, 2006, and is referred to in this decision as the Veolia I protest; Veolia’s protest under RFP No. 1802 was filed on February 23, 2006, and is referred to as the Veolia II protest.

RFP No. 3602, at 2; RFP No. 1802, at 2. Service standards and requirements were identified to ensure that the Navy's operational requirements for potable water and wastewater collection would be satisfied. See RFP No. 3602, at 15; RFP No. 1802, at 13-15.

Each solicitation noted that authority for utility privatization was provided by 10 U.S.C. § 2688 and that statute, among other things, imposed certain economic tests that must be met in order for such a transaction to be consummated. In addition, offerors were cautioned that all privatization actions must be approved by the Secretary of the Navy and that there was no guarantee that a privatization agreement would be executed. RFP No. 3602, at 4; RFP No. 1802, at 4. In this regard, the RFP stated that

[s]hould the Department be unable to reach a mutually acceptable agreement with the best value source, it reserves the right to terminate discussions and open discussions with the next most highly rated source or reopen negotiations with all qualified sources.

RFP No. 3602, at 23; RFP No. 1802, at 22.

The RFPs provided for a "best value" source selection process to choose the offeror that would enter negotiations with the Navy for the purchase of the utility assets. Offerors were informed that "[d]uring discussions, [NAVFAC] will determine if proposals satisfy the criteria of statute 10 U.S.C. [§] 2688 and inform Offerors thereof." RFP No. 3602, at 10; RFP No. 1802, at 9. Offerors were further informed that proposals found to be within the competitive range would be "checked to ensure the economic criteria of 10 U.S.C. [§] 2688 are still satisfied" and that, if at any time during discussions with the best-value offeror, NAVFAC "determined that terms and conditions could not be successfully finalized or that the Offeror would be unable to comply with the economic requirements of [the statute], the privatization action will be terminated." RFP No. 3602 amend 6, at 6-7; see RFP No. 1802, at 9.

RFP No. 3602--Veolia I Protest

NAVFAC's Atlantic Division received proposals from four offerors, including Veolia.⁴ Veolia's proposal and two others were included in the competitive range, and discussions were conducted with these firms. With respect to Veolia's proposal, NAVFAC informed Veolia that its offer to acquire the agency's utility assets for \$1 for each system was not acceptable and would not satisfy the requirements of 10 U.S.C.

⁴ Veolia's proposal was actually submitted in the name of U.S. Filter Operations Systems, Inc. After receipt of proposals, U.S. Filter Operating Systems, Inc. changed its name to Veolia. See Veolia I Protest at 1 n.1. We refer to the protester as Veolia throughout the decision.

§ 2688. During discussions, Veolia informed NAVFAC that the firm could not agree to purchase the agency's utility assets for what the agency believed to be "fair market value" because "Veolia could not book that much debt without compromising its financial standing and ability to attract capital for its other operations." Veolia I Protest at 7. NAVFAC suggested to Veolia that the firm consider the use of a trust or similar entity to own the utility system assets. See Veolia I Document Chronology, Tabs 16 and 17 (handwritten notes of June 6, 2003 meeting between Veolia and the Navy).⁵

On June 30, 2003, Veolia submitted a proposal clarification to the Navy in which Veolia stated that "[a]s an alternative to [Veolia's] offer of \$1.00 per [contract line item] to acquire the U.S. Navy's facilities at Navy Area C, [Veolia] is considering a 'Fair Market Value' offer, provided that we are able to team with an unaffiliated real estate trust or other third party to acquire the facilities." Id., Tab 22, Veolia Proposal Clarification Response, at AT-1-1. Further discussions were conducted regarding Veolia's proposal to have the utility assets acquired by a third party, with which Veolia would enter into a lease for the use of the utility assets in the performance of a separate operation and maintenance service contract with NAVFAC. On September 25, 2003, Veolia submitted another proposal clarification in which Veolia identified the National Center for the Employment of the Disabled (NCED), a non-profit entity with approximately \$700 million in annual revenue, as the third party that Veolia proposed would purchase the utility system assets. Id., Tab 35, Veolia Supplemental Proposal Clarification Responses, at AT-1-1.

On December 22, 2003, Veolia was selected as the best value offeror for the purpose of entering due diligence negotiations with NAVFAC for the purchase of the utility assets. NAVFAC concluded that Veolia offered a more advantageous technical approach and a more favorable and less risky pricing structure than that of the next highest rated offeror. See American States Utilities Servs., Inc., B-291307.3, June 30, 2004, 2004 CPD ¶ 150 at 3-4. Among other things, NAVFAC noted that Veolia had

submitted a proposal with a 50 year service contract with a 25 year fixed price with economic adjustment and third party ownership. With assets belonging to the [NCED], they would lease the facilities to [Veolia] under an operating lease. [Veolia] has also included an option in which they acquire the assets for Replacement Cost New Less Depreciation.

Veolia I Agency Report (AR), Tab 4, Source Selection Decision, at 4.

On February 10, 2004, Veolia and NAVFAC began negotiations for the privatization of some 34 utility systems in Utility Privatization Area C. Veolia I Protest at 10.

⁵ Veolia submitted Veolia I and Veolia II document chronologies for the record.

Although Veolia offered, as an option, to directly purchase the utility assets if NAVFAC financed the purchase, the parties' negotiations focused on Veolia's offer of a third party ownership arrangement to acquire the utility system assets, although the details of that arrangement continued to change.⁶

By letter of November 5, 2004, NCED informed the contracting officer for RFP No. 1802 (Veolia II) that NCED intended to form a non-profit subsidiary for the purpose of purchasing the government's utility system assets, stating that "[a]s payment for the purchase price, the new not for profit subsidiary will execute a promissory note secured by a first lien on the Utility Assets." NCED also informed NAVFAC that NCED would not become a party to the sales transaction nor would NCED be willing to issue a promissory note or other guarantee to NAVFAC related to the purchase price. Veolia II AR, Tab 25, NCED Letter to the NAVFAC, Nov. 5, 2004. The contracting officer for RFP No. 3602 was apparently apprised of NCED's intention to form a non-profit subsidiary to acquire the utility system assets.

On February 28, 2005, the source selection authority (SSA) for RFP No. 3602 endorsed a business clearance memorandum (BCM), stating the following recommendation:

The Source Selection Authority has previously determined that [Veolia] provided the best value offer of those received for the water and wastewater systems for the Hampton Roads area. The Navy has negotiated an agreement that meets the economic tests required by 10 U.S.C. [§] 2688 and will improve the water and wastewater service provided to the base without the Navy undertaking unreasonable risks. For these reasons, it is recommended that authority to seek Secretarial Approval to award this contract to [Veolia] be provided.

Veolia I AR, Tab 10, Veolia I BCM, at 15.

The BCM's recommendation was based upon Veolia's offer that the National Center for the Employment of the Disadvantaged (NCED II), a newly formed subsidiary of NCED, would purchase the utility system assets from NAVFAC for \$120 million under a 25-year promissory note and that NAVFAC would hold a lien on the

⁶ At least by June 24, 2005, Veolia had rescinded its offer to accept direct ownership of the utility system assets, even though it had not formally modified its proposal. See Veolia I Document Chronology, Tab 214, Veolia Letter to the NAVFAC, June 24, 2005; Veolia I AR at 13. In its comments on the agency report, Veolia states that, as of December 2003, the Navy knew that Veolia "would not accept direct ownership of the Navy's utility assets if that meant [Veolia] would have to record . . . debt on its books." Veolia I Comments at 3.

property, as improved, during the payment period. Veolia's offer provided that NCED II and Veolia would enter into a "use agreement," under which Veolia would lease the use of the assets; pursuant to this agreement, Veolia would pay a monthly rent to NCED II equal to "the cost of debt payments to NAVFAC for purchase of the assets [\$747,280 per month to be paid the Navy by NCED II as a credit to the service charges under the service contract--thus, Veolia's obligations to NCED II under the use agreement equaled/offset NCED II obligations to the Navy to be paid as a credit against Veolia's charges to the government under the service contract] and the fee to hold title and administer the Use Agreement [\$10,417 per month]." Under this offer, Veolia and NAVFAC would enter into a service contract for a 25-year base term and a 25-year option term for the operation, maintenance, repair and renewal of the assets at a fixed-monthly-price with an economic price adjustment provision, with the credit set out above to the service charges for NCED II's purchase of the assets. Id. at 10-11.

Although the Veolia I BCM did not identify as unreasonable the risk posed by Veolia's third-party ownership offer, the BCM nevertheless documented a number of business risks that were viewed as being inherent in Veolia's offer, including that NCED II was newly formed for the specific purpose of acquiring the Navy's utility system assets. In this regard, the BCM noted that NCED II may later be determined to be a for-profit entity, which could adversely affect the Navy's risk under the business arrangement. The BCM also noted that NCED II's corporate charter indicated that if NCED II was dissolved, the entity's board of director would dispose of the assets to another unnamed non-profit entity. The BCM further noted that there could be significant risk to NAVFAC if Veolia and/or NCED II failed to perform and the Navy was required to reclaim ownership of the assets. Id. at 14-15.

In accordance with the Navy's standard procedures, the Veolia I BCM was submitted to NAVFAC's headquarters in Washington, D.C. for approval.⁷ Following submission, additional information was requested from Veolia with respect to a number of questions, including whether there were any potential tax liability issues associated with the third-party ownership arrangement and what Veolia's position would be if NCED II was determined to be a for-profit entity. Veolia was requested to provide documentation from any "independent (legal or accounting or IRS [Internal Revenue Service]) determination party which offers an opinion that the proposed third party arrangement [would] pass IRS scrutiny." Veolia I Document Chronology, Tab 197, E-mail from NAVFAC to Veolia, Apr. 19, 2005.

Thereafter, NAVFAC and Veolia had a number of meetings at NAVFAC's headquarters discussing Veolia offer. See id., Tabs 207 and 213, Handwritten Notes

⁷ Under the Navy's procedures, business clearances for utility privatization are provided to NAVFAC's Assistant Commander for Acquisition for his review and approval. See Hearing Transcript (Tr.) at 9-10, 26-27.

of Meetings on May 5 and 24, 2005. By letter dated June 24, 2005, Veolia provided further information to NAVFAC's headquarters regarding its current proposal structure and explaining why it believed this structure was compliant with 10 U.S.C. § 2688; Veolia also informed the agency that

[a]s requested by the Navy, we have investigated the alternative structure that would have Veolia . . . accepting title to the facility assets directly and then transferring the title to the assets to NCED II. Our review of the accounting pronouncements . . . has determined that this structure will not preclude the requirement to record the facility assets and corresponding debt on Veolia[']s . . . books. This structure of inserting Veolia . . . into the title chain and then attempting to extinguish any associated liability by transferring the title to NCED II would be viewed as a form over substance transaction.

Id., Tab 217, Letter from Veolia to NAVFAC, June 24, 2005, at 2. Veolia further stated that the firm had structured a third-party ownership arrangement to avoid recognizing on its "books" the debt associated with the purchase of the assets and again indicated that Veolia would not enter into a contract that resulted in Veolia recording the assets and associated debt. Id. at 1-2.

On July 15, 2005, NAVFAC's Assistant Commander for Acquisitions informed Veolia that the firm's proposed third-party arrangement was inconsistent with the requirements of the solicitation and 10 U.S.C. § 2688; that privatization of these assets with Veolia could not be finalized; and that therefore NAVFAC considered Veolia's proposal withdrawn from the competition. NAVFAC's Dismissal Request, Tab 5, Letter from NAVFAC to Veolia, July 21, 2005. On July 29, NAVFAC's Assistant Commander for Acquisitions and Veolia had another telephone conversation, in which the Assistant Commander expressed a preference for a "conventional two-party deal." Tr. at 15-16. Based upon NAVFAC's interpretation of this telephone conversation, NAVFAC, by letter dated July 29, rescinded its earlier notification that Veolia's proposal was withdrawn from further consideration under the solicitation.⁸ NAVFAC's Dismissal Request, Tab 6, Letter from NAVFAC to Veolia, July 29, 2005.

⁸ The parties disagree with respect to what was said during NAVFAC's and Veolia's July 29 telephone conversation and whether Veolia agreed to a "conventional" two-party ownership arrangement. While we do not resolve this issue, it is apparent from the contemporaneous record that the agency believed that Veolia had agreed to offer a conventional two-party ownership arrangement and that this was the reason NAVFAC agreed to further consider Veolia's proposal. See Navy Dismissal Request, Tabs 7 and 8-1, Internal NAVFAC E-mails, July 29, 2005.

Thereafter, Veolia offered an ostensible two-party arrangement in which Veolia would take ownership of the utility assets directly from the Navy and then would “simultaneously transfer[] ownership of the assets to the third party, NCED[]II.” Under this arrangement, Veolia’s payment of the agreed fair market value price for the assets would again take the form of a reduction in the Navy’s payments to Veolia for operation and maintenance services under the services contract. With the immediate sale of the assets to NCED II, Veolia and NCED II would execute a promissory note, which would “reflect NCED[]II’s payment obligation to Veolia . . . and its primary obligor status to repay the utility assets purchase price debt obligation to the Navy.”⁹ As a part of this deal, Veolia requested that the Navy acknowledge and authorize Veolia’s sale of the assets to NCED II and also agree “to accept NCED II as its primary obligor for its recovery of the purchase price debt with Veolia . . . retaining secondary obligor status on that debt.” Veolia I Document Chronology, Tab 234, Veolia’s Revised Deal, Aug. 5, 2005, at ES-3-5.

This new arrangement was the subject of further discussions by Veolia and NAVFAC, with each party preparing proposed contract documents. On October 3, Veolia submitted revised contract documentation to the Navy with the notation that the Navy’s proposed contract documents failed to acknowledge the agency’s “commitment to accept [Veolia’s] conveyance of the Utility Assets to NCED[]II,” which Veolia termed a material aspect of the transaction, and that the Navy had not clearly agreed that NCED II would be the primary obligor. *Id.* Tab 241, Veolia Letter to NAVFAC, Oct. 3, 2005.

By letter of November 16, NAVFAC informed Veolia that “[s]enior NAVFAC management has reviewed and considered the detail points in [Veolia’s] letter of October 3, 2005.” Considering the “constraints imposed by the authorizing legislation” and “the risks and benefits as well as potential cost avoidance,” NAVFAC found

[d]uring the course of examining each of the proposed documents, it became obvious that, despite efforts to accommodate all concerns, the basic flaw of the concept--the non-recognition of debt--could not be overcome in a manner acceptable to [NAVFAC], *i.e.*, one that does not require our participation or implied endorsement.

⁹ Veolia and NCED II would also enter a use agreement under which Veolia would pay NCED II a facilities use fee and an annual administrative fee for the use of the assets in Veolia’s performance of its service contract with NAVFAC. *See* Veolia I Document Chronology, Tab 242, Draft Use Agreement, at 3-4. As with the three-party agreement previously proposed by Veolia, NAVFAC would not be a party to the use agreement.

Accordingly, NAVFAC informed Veolia that “further pursuit of privatization involving an artificial non-recognition of debt is imprudent and not in the interest of either Veolia or the Navy.” Veolia I AR, Tab 11, NAVFAC Letter to Veolia, Nov. 16, 2005.

The decision to reject Veolia’s proposal to acquire the utility assets and immediately sell them to NCED II was made by NAVFAC’s Assistant Commander for Acquisition based upon the advice of his immediate acquisition and legal staff. Tr. at 28-29, 40. In this regard, the Assistant Commander accepted the advice of his legal advisor that 10 U.S.C. § 2688 would not permit NAVFAC to enter a transaction in which Veolia would operate and manage the utility system assets but that those assets would be simultaneously sold by the government through Veolia to an unrelated entity. Tr. at 12-13, 20. In addition, the Assistant Commander concluded that the deal offered by Veolia was “more risk, that I was willing to sign the Government up for.” Tr. at 13, 20-21, 81-83; see also Declaration of Assistant Commander for Acquisition, Apr. 12, 2006, at 3, in which the Assistant Commander concluded:

My reaction from a business perspective was to doubt the wisdom of permitting Veolia, a multi-billion dollar, publicly-traded corporation, to lay off its debt to the United States on a closely-held, shell corporation with no assets. My advisors told me that I had no authority to take such action, but even if I did, I would not have incurred that extra risk to close this deal.

Following additional discussion between the parties to clarify the agency’s decision and to confirm that Veolia would not consider offering a “standard two party approach,” Veolia filed an agency-level protest of the rejection of its proposal. On January 31, 2006, NAVFAC denied Veolia’s agency-level protest. Veolia I Document Chronology, Tab 255, Agency-level Protest Decision, Jan. 31, 2006. This protest followed.

RFP No. 1802--Veolia II Protest

NAVFAC’s Southern Division received proposals from 10 offerors, including Veolia. All offerors were included in the competitive range and received discussions. Veolia II AR, Tab 4, Source Selection Evaluation Board Report, at 6, 19. Veolia was again informed by NAVFAC that its offer to purchase the utility system assets for \$1 per system was unacceptable. Veolia responded that the “Navy’s utility assets had no real market value” and that Veolia “had offered \$1.00 in response to an Army privatization solicitation for Schofield Barracks which the Army accepted as compliant with 10 U.S.C. § 2688.” Veolia II Protest at 5. Because the Navy continued to question the acceptability of Veolia’s purchase offer of \$1 per system, on July 22, 2003, Veolia submitted a revised proposal, in which the firm offered, as an alternative, to team with an unaffiliated real estate trust or other third-party entity to acquire the assets. See e.g., Veolia II Document Chronology, Tab 22-M, Final Proposal Revision, at V-I-1-1.

On September 9, 2003, NAVFAC informed Veolia that the agency would not consider or accept Veolia's offer to purchase the utility assets for \$1 per system. Veolia II Protest at 6. Accordingly, on October 7, Veolia revised its proposal to offer, as an alternative, a third-party ownership arrangement, under which NCED would directly purchase the utility assets from NAVFAC and Veolia would lease the use of the assets from NCED; Veolia would enter into a separate service agreement with NAVFAC to provide operation and maintenance services. See e.g., Veolia II Document Chronology, Tab 25 P, Final Proposal Revision (Clarifications), at V-I-ES-4, FPR-C-V-I-C-1. Further discussions were conducted, and a final revised proposal was received from Veolia.

On December 13, Veolia was selected as the best value offeror for the purpose of entering negotiations with the Navy with respect to the utility systems at three facilities. Veolia II AR, Tab 14-1, Source Selection Board Report, at 3. Thereafter, Veolia and NAVFAC conducted negotiations for the privatization of utility systems at these facilities.¹⁰ Although Veolia had proposed to either directly purchase the utility assets or, as an alternative, to have a third party purchase the assets, as was the case for RFP No. 3602, the parties' negotiation here too focused upon Veolia's third-party ownership offer.

As noted above, by letter of November 5, 2004, NCED, Veolia's proposed third-party purchaser, informed the contracting officer that NCED intended to form a non-profit subsidiary for the purpose of purchasing the government's utility assets. In that letter, NCED stated that it would not become a party to the transaction nor would it be willing to issue a promissory note or other guarantee related to the purchase price. Veolia AR, Tab 25, NCED Letter to NAVFAC, Nov. 5, 2004. Subsequently, Veolia informed NAVFAC that its proposed third-party purchaser of the utility systems assets would be NCED II, a newly formed subsidiary of NCED.¹¹

¹⁰ On September 16, 2004, Hurricane Ivan severely damaged the water and wastewater facilities at Naval Air Station Pensacola, and this facility (which was one of the facilities at which Veolia proposed to purchase the utility assets) was removed from the negotiations. Veolia II AR at 4.

¹¹ Internal agency e-mail traffic indicates that at some point in January 2005 NAVFAC was aware that NCED would not be the third-party owner and that some "new" business entity would be proposed. These documents highlight the frustration of NAVFAC's Southern Division that "it has been an effort to obtain clarity and documentation concerning this 'deal.' Now that we finally have sufficient documentation to make a decision the documents contain terms that place the Navy in a high business risk position if the terms are agreed to as written." Veolia II AR, Tab 31, Internal NAVFAC E-mail, Jan. 21, 2005.

On March 15, 2005, the SSA for RFP No. 1802 endorsed a BCM that recommended against entering a contract with Veolia to privatize the utility system assets for the two facilities for which Veolia was still competing under this solicitation.¹² Veolia II AR, Tab 33, BCM, at 2. The BCM's recommendation was based upon the conclusion of NAVFAC's Southern Division that Veolia's proposed third-party ownership structure was too risky and violated the requirements of 10 U.S.C. § 2688. Among other things, the agency found that under Veolia's proposed contract neither Veolia nor NCED II would have any obligation to pay for the assets in the event the Navy discontinued payments to Veolia under the service agreement.¹³ The BCM also noted that "[t]he Government is paying an administration fee to NCED[II] for the sole purpose of providing a means for [Veolia] to avoid showing debt on its books." The BCM also questioned whether NCED II would ultimately be determined to be a non-profit entity, given that no documentation had been provided to show how NCED II's ownership of the Navy's assets would satisfy IRS's filing requirements for tax-exempt non-profit entities, and that an adverse IRS determination could subject the government to "financial and legal risk." *Id.* at 14.

In accordance with the Navy's standard procedures, the BCM was submitted to NAVFAC's headquarters for approval. On November 22, 2005, NAVFAC agreed with the SSA's recommendation rejecting Veolia's third-party ownership offer for utility privatization in Area E. This decision was based upon the earlier decision of NAVFAC's Assistant Commander for Acquisition rejecting Veolia's similar deal for utility privatization in Area C. Tr. at 71-72. By letter of December 19, NAVFAC informed Veolia that the agency considered the risks and benefits of accepting Veolia's privatization offer to be unacceptable and that the agency concluded that "further pursuit of privatization involving an artificial non-recognition of debt is imprudent and not in the interest of either Veolia or the Navy." Veolia II AR, Tab 44, Letter from the Navy to Veolia, Dec. 19, 2005. Veolia filed an agency-level protest

¹² Veolia states that after November 2004 "the Navy essentially ceased all communications with Veolia" concerning privatization of the utility system assets under RFP No. 1802. Veolia II Protest at 9.

¹³ Under the proposed three-party agreement, Veolia was not a party to the conveyance of the assets to NCED II; NCED II had no obligations under the service agreement between Veolia and NAVFAC; and the government was not a party to the use agreement between Veolia and NCED II. In addition, the agreement stated that "'each party's payment obligation shall be wholly or partially suspended in the amount equal to the Purchase Money Monthly Payment until such time as the Government fully restores the withheld payments or credits.' Simply stated, the reciprocal flow of credits and the obligation to pay for the asset is suspended if the Government withholds payment on the service contract." AR, Tab 33, Veolia II BCM, at 15. The agency found that there was no indication that NCED II had any plans to pay for the assets or the necessary funds to do so. *Id.* at 16.

challenging the rejection of its offer. *Id.*, Tab 45, Veolia Agency-level Protest, Jan. 3, 2005. NAVFAC denied Veolia's agency-level protest on February 7, 2006. *Id.*, Tab 46, Agency-level Protest Decision, Feb. 7, 2006. This protest followed.

ANALYSIS

Authority to Convey Utility Assets

As indicated, NAVFAC, in rejecting Veolia's proposal, not only considered the deal to be too risky, but determined that it violated 10 U.S.C. § 2688. Veolia protests that NAVFAC's rejection of Veolia's proposals to purchase the utility assets and simultaneously transfer them to a third-party was arbitrary and capricious because nothing in 10 U.S.C. § 2688 or any other law or regulation precludes the sale of the agency's utility assets to an unrelated third party. Veolia I Protest at 19; Veolia II Protest at 13, 15. Veolia asserts that, because 10 U.S.C. § 2688 does not legally bar the arrangement offered by Veolia, NAVFAC must reconsider its rejection of its proposal, as the Assistant Commander for Acquisition testified he would do. Veolia's Hearing Comments at 16-17, citing, Tr. at 163 ("Basically, if it was later determined that the legal advice that I relied on for purposes of compliance with the statute (10 U.S.C. § 2688) was in error, then I would be very comfortable and feel I have a responsibility to go back and look at the other series of data points that caused me to make a decision with this change in data point relative to the statute compliance and make a new decision.").

NAVFAC's authority to privatize the water/wastewater system assets is provided by 10 U.S.C. § 2688, which allows the secretary of a military department to convey a utility system to a municipal, private, regional, district, or cooperative utility company or other entity so long as it is in the long-term economic interest of the government and satisfies certain other conditions. Further, section 2688 provides that "[i]f more than one utility or entity . . . notifies the Secretary concerned of an interest in a conveyance . . . the Secretary shall carry out the conveyance through the use of competitive procedures." 10 U.S.C. § 2688(b); see Virginia Elec. and Power Co.; Baltimore Gas & Elec. Co., B-285209, B-285209.2, Aug. 2, 2000, 2000 CPD ¶ 134 at 2.

Here, NAVFAC argues, among other things, that Veolia proposed arrangement, under which a third party (NCED II) would immediately acquire the utility assets and under which Veolia requested that NAVFAC agree to accept NCED II as the primary obligor for repayment of the purchase price of the assets, violates 10 U.S.C. § 2688(f)(2).¹⁴ That provision, which is entitled "Additional terms and conditions," provides:

¹⁴ This section was redesignated as 10 U.S.C. § 2688(g)(2) by section § 2823(c)(1) of the National Defense Authorization Act for Fiscal Year 2006. See Pub. L. No. 109-163, 2005 U.S.C.C.A.N. (119 Stat.) 3136, 3515.

The Secretary concerned shall require in any contract for the conveyance of a utility system (or part of a utility system) under subsection (a) that the conveyee manage and operate the utility system in a manner consistent with applicable Federal and State regulations pertaining to health, safety, fire, and environmental requirements.

NAVFAC contends that the plain language of this provision requires “the conveyee [of the assets]—selected competitively—to operate and manage the system.” See NAVFAC Reply to Veolia I Comments at 9-10. NAVFAC also notes that 10 U.S.C. § 2688(c) provides that consideration for the sale of utility assets may take the form of either a lump sum payment or “a reduction in charges for utility services provided by the utility or entity concerned to the military installation at which the utility system is located,” which the NAVFAC asserts also demonstrates that the conveyee and the entity operating and managing the utility system assets must initially be the same party. Here, in NAVFAC’s view, although Veolia could as the owner of the assets sell the assets to another party, subject to NAVFAC’s approval, entering an arrangement under which Veolia would receive title to the assets for the express purpose of simultaneously transferring them to an unrelated third party, who NAVFAC would have to expressly recognize as the primary obligor for payment of the purchase debt, was tantamount to a conveyance by NAVFAC of the assets to a party that would not be operating and managing the assets, and that such an arrangement would be in violation of 10 U.S.C. § 2688(f)(2). *Id.* at 2, 10, 12.

Veolia disagrees with the Navy’s interpretation of 10 U.S.C. § 2688, arguing that nothing in that statute “precluded a ‘conveyee’ of a utility system from contracting with a service provider to manage and operate the utility system conveyed; and this is exactly what Veolia disclosed would happen in this case.” Veolia’s Hearing Comments at 16.

In matters concerning the interpretation of a statute, the first question is whether the statutory language provides an unambiguous expression of the intent of Congress.¹⁵ If it does, the matter ends there, for the unambiguous intent of Congress must be given effect. Chevron U.S.A. Inc. v. Natural Res. Def. Council, Inc., 467 U.S. 837, 842-43 (1984). If, however, the statute is silent or ambiguous with respect to the specific issue, deference to the interpretation of an administering agency is dependent on the circumstances. Chevron, 467 U.S. at 843-45; United States v. Mead Corp., 533 U.S. 218, 227-39 (2001). Where an agency interprets an ambiguous provision of the statute through a process of rulemaking or adjudication, unless the

¹⁵ Perhaps the most fundamental principle of statutory construction is that words in a statute must be given their ordinary meaning whenever possible. See Walters v. Metro. Educ. Enters., Inc., 519 U.S. 202, 207 (1997).

resulting regulation or ruling is procedurally defective, arbitrary or capricious in substance, or manifestly contrary to the statute, the courts will defer to this agency interpretation (called “Chevron deference”).¹⁶ Mead, 533 U.S. at 227-31; Chevron, 467 U.S. at 843-44. However, where the agency’s position reflects an informal interpretation, “Chevron deference” is not warranted; in these cases, the agency’s interpretation is “entitled to respect” only to the extent it has the “power to persuade.” Gonzales v. Oregon, 126 S. Ct. 904, 914-15 (2006), citing Skidmore v. Swift & Co., 323 U.S. 134, 140 (1944); see Mead, 533 U.S. at 226-27.

Here, we find that, though the plain language of 10 U.S.C. § 2688(f)(2) appears to preclude the direct conveyance of utility system assets to an entity that will not be operating and maintaining the assets in accordance with federal and state laws and regulations, the statute does not address the precise question presented here. That is, the statutory language does not clearly answer whether the sale of the assets to Veolia and a simultaneous resale of the assets by Veolia to NCED II is prohibited. We have not found any legal decisions or other precedent addressing this issue, nor have the parties identified any. We have also reviewed the legislative history for this statute and find nothing in the legislative history that indicates the intent of Congress with respect to the question before our Office.¹⁷

As noted above, NAVFAC argues that Veolia’s final proposed arrangement would have Veolia receiving title to the utility assets for the express purpose of “simultaneously” conveying the assets to NCED II, and that this final arrangement required the agency to, in advance, recognize and approve the conveyance of the assets to NCED II and to recognize NCED II as the primary obligor of purchase price of the assets. NAVFAC convincingly argues that this ostensible two-party

¹⁶ There are exceptions to the rule whereby the absence of authority for an agency to use formal administrative procedures to interpret laws does not alone bar this level of deference. Mead, 533 U.S. at 231 n.13, citing NationsBank of N.C., N.A. v. Variable Annuity Life Ins. Co., 513 U.S. 251 (1995) for the example that the deliberative conclusions of the Comptroller of the Currency as to the meaning of banking laws are deserving of this higher level of deference due to the Comptroller’s specific authority to enforce such laws.

¹⁷ Paragraph (f)(2) (now designated (g)(2)) was added to 10 U.S.C. § 2688 by section 2813 of the National Defense Authorization Act of Fiscal Year 2001. See Pub. L. No. 106-398, 2000 U.S.C.C.A.N. (114 Stat.) 1654, 1654A-419. A House Conference Report for this provision merely states that the House recedes to a Senate amendment with an amendment that “would also direct the secretary concerned to require the conveyee or awardee of the utility system to manage and operate the utility system consistent with federal and state regulations pertaining to health[,] safety, fire, and environmental requirements.” H.R. Conf. Rep. No. 106-945, at 918 (2000), reprinted in 2000 U.S.C.C.A.N. 1516, 1737.

arrangement was essentially the same as Veolia's earlier three-party arrangement, under which the agency was requested to convey the utility assets directly to NCED II while Veolia would operate and manage the assets under a separate contract with the agency. This view is supported by contemporaneous documentation drafted by Veolia, wherein Veolia informed the agency

[t]he only difference between the original transaction approach [the three-party arrangement] and the one Veolia . . . proposes now is that Veolia . . . is introduced into the chain of ownership of the Navy's utility assets

and

[b]ecause the substance of the transaction remains materially unchanged, only minor modifications to the existing transaction documents are required to reflect the revised transaction approach.

Veolia I Document Chronology, Tab 234, Veolia's Revised Deal, Aug. 5, 2005, at ES-2. In other words, in NAVFAC's view, Veolia's ostensible two-party arrangement violated the requirement in 10 U.S.C. § 2688 that assets cannot be conveyed, at the time of award, to an entity that will not be operating and maintaining the assets, in that title and responsibility in the assets will not vest in Veolia, but in NCED II.

Veolia contends that neither its originally proposed three-party structure at the time of its selection for negotiation with NAVFAC or its later two-party structure with a simultaneous conveyance of the assets to NCED II was prohibited by 10 U.S.C. § 2688.¹⁸ See Veolia I Protest at 10; Veolia's Hearing Comments at 16; see also Veolia I Document Chronology, Tab 217, Veolia Letter to NAVFAC, June 24, 2005, enclosing a legal memorandum from its outside counsel. However, the protester has not at any time during the negotiations or in its pleadings to our Office specifically addressed

¹⁸ Veolia also argues that NAVFAC admitted during negotiations that "it appears that nothing would preclude Veolia's sale of the asset to NCED II provided that Veolia remained a responsible contractor." See Veolia I Comments at 15, citing, Veolia I Document Chronology, Tab 209, NAVFAC E-mail to Veolia, May 19, 2005, transmitting "agenda points for discussion." We do not agree that this e-mail message establishes that the agency has admitted that a sale to NCED II would be permissible in any form, as Veolia apparently believes. In any event, NAVFAC makes clear that, although a conveyee under the statute may later transfer utility assets, subject to government approval, Veolia's proposed contract structure requiring a simultaneous transfer of title to NCED II by Veolia meant that NCED II was essentially receiving the assets directly from the agency while not responsible for operating and maintaining them, which in NAVFAC's view, contravened the statute.

why 10 U.S.C. § 2688(f)(2) does not preclude Veolia’s proposed contract structure, as argued by the agency.

Instead, Veolia directs our attention to other provisions of 10 U.S.C. § 2688, arguing that these other provisions indicate that a conveyance of the utility assets to NCED II is permissible. Specifically, Veolia states that the statute allows an agency to convey a utility system to a “municipal, private, regional, district, or cooperative utility company or other entity,” see 10 U.S.C. § 2688(a), and that “[i]f more than one utility or entity referred to in subsection (a) notifies the Secretary concerned of an interest in a conveyance under such subsection, the Secretary shall carry out the conveyance through the use of competitive procedures.” 10 U.S.C. § 2688(b). Veolia argues that the statute merely requires the agency to use competitive procedures for the conveyance of utility assets where more than one utility or other entity expresses interest and states that the term “other entity” in subsection (a) indicates that the agency is authorized to transfer the assets to an “entity” other than the offeror for the operation and maintenance of the utility system. See Veolia I Comments at 11.

We do not find Veolia’s interpretation reasonable either in the context of the plain language of the provisions Veolia cites or in reading the statute as a whole. Subsections (a) and (b) of the statute plainly indicate that the secretary is authorized to convey utility assets to a utility company or other entity, and that this conveyance should be effected by competitive procedures where more than one company or entity expresses interest. Neither section, either read alone or together, indicates that an agency could competitively award a contract for the operation and maintenance of the utility system assets and then convey the assets to an unrelated “entity,” as Veolia suggests. Rather, the list of utilities and “other entity” as used in subsections (a) and (b) merely identify the type of entities with which the agency may entertain the conveyance of utility system assets under the statute. When read as a whole, the statute indicates that the utility company or “other entity” to which the utility assets are conveyed must be the same company or “other entity” which will be operating and maintaining the assets.

Veolia also states that NAVFAC’s subordinate command—its Atlantic Division—did not interpret 10 U.S.C. § 2688 as prohibiting either NAVFAC’s direct conveyance of the utility system assets to NCED II or Veolia’s immediate conveyance of the utility system assets to NCED II. Veolia argues that this demonstrates that the later decision of NAVFAC’s Assistant Commander for Acquisition is arbitrary and capricious. See Veolia I Protest at 16-17.

Veolia’s argument misunderstands the grant of authority within the Department of the Navy to review and decide upon the privatization of utility system assets under 10 U.S.C. § 2688. Congress granted to the Secretary of a military department the

authority to convey utility system assets under the Secretary's jurisdiction.¹⁹ 10 U.S.C. § 2688(a). Within the Navy, the Secretary's authority to review proposed utility privatization proposals was delegated to NAVFAC's Assistant Commander for Acquisition, who is the chief of NAVFAC's contracting office. Tr. at 25-26. In turn, the Assistant Commander for Acquisition authorized NAVFAC's subordinate Atlantic and Southern Divisions to conduct the procurements, make source selection decisions, and negotiate with best value offerors. Tr. at 26. Inherent in this grant of authority by the Assistant Commander for Acquisition is the power to disagree or reverse decisions made at the lower level. See, e.g., Advanced Sciences, Inc., B-259569.3, July 3, 1995, 95-2 CPD ¶ 52 at 18-19 (inherent in the authority to appoint source selection officials is the power of higher-level officials to review source selection decisions, reverse or vacate those decisions, make new decisions, and to appoint new source selection officials). Thus, the authority of the field activities to make decisions with respect to utility privatization remained subject to review by the Assistant Commander for Acquisition through whom their authority was received. The mere fact that the Assistant Commander for Acquisition disagrees with a determination or decision made by a subordinate command does not alone demonstrate that the Assistant Commander was arbitrary or capricious; it is the Assistant Commander who holds the higher-level authority within NAVFAC to determine whether Veolia proposed contract structure is compliant with 10 U.S.C. § 2688.

In sum, since NAVFAC's argument as to why Veolia's proposal violated 10 U.S.C. § 2688(f)(2) has the "power to persuade," and in the absence of cogent argument by Veolia demonstrating that NAVFAC erred in determining that this statute prohibited Veolia's proposed contract structure, we find no basis to conclude that the agency's interpretation of the statute was in error.²⁰

Estoppel

Veolia also complains that

the Navy not only included Veolia's offer in the competitive range,
the Navy suggested the third party owner approach; directed Veolia

¹⁹ As noted, the RFPs notified offerors that all privatization actions must be approved by the Secretary of the Navy and that there was no guarantee that a privatization agreement would be executed. RFP No. 3602, at 4; RFP No. 1802, at 4.

²⁰ While NAVFAC has advanced seemingly valid reasons why Veolia's proposed contract structure was too risky to consummate in any case, we need not determine whether this position by NAVFAC was reasonable, given our agreement with NAVFAC that Veolia's proposed two-party contract structure would be a violation of 10 U.S.C. § 2688.

to adopt the approach as its primary approach; selected Veolia as its best value offeror on the basis of that approach; invited Veolia to perform due diligence; engaged Veolia in contract negotiations; reached agreement with Veolia on the terms and conditions of a contract and other transaction documents; and then arbitrarily disqualified Veolia after it spent millions of dollars responding to the Navy, all because Veolia “offered a non-recognition of debt approach.”

Veolia I Comments at 5.²¹ Veolia requests, based upon an estoppel theory, that we recommend that NAVFAC award Veolia a utility privatization contract or that NAVFAC reimburse Veolia the firm’s “bid and proposal costs” incurred in competing and negotiating for that contract under the RFP No. 3602. *Id.* at 24; Veolia’s Hearing Comments at 4.

Although Veolia describes this protest allegation as being grounded upon the doctrine of equitable estoppel, *see* Veolia’s Hearing Comments at 4, this ground of protest seems to be actually based upon the doctrine of promissory estoppel. Although the doctrines of equitable estoppel and promissory estoppel are both based upon detrimental reliance, promissory estoppel is used to create a cause of action, whereas equitable estoppel is used to bar a party from raising a defense or objection it otherwise would have, or from instituting an action which it is entitled to institute; thus, “[p]romissory estoppel functions as a sword, while equitable estoppel functions as a shield.” *See R.R. Donnelley & Sons, Co. v. United States*, 38 Fed. Cl. 518, 521 (1997). Here, Veolia asserts a detrimental reliance theory as its basis for seeking our recommendation that NAVFAC either award the protester utility privatization contracts or reimburse the protester for its proposal preparation costs; in other words, Veolia’s asserts estoppel as a cause of action upon which it seeks to receive relief from our Office and thus this protest ground must necessarily be based on the doctrine of promissory estoppel.

Under the Competition in Contracting Act of 1984 (CICA), our Office is authorized to decide bid protests “concerning an alleged violation of a procurement statute or regulation.” 31 U.S.C. §§ 3552, 3553(a) (2000). Although protests usually involve alleged violations of statutes that are indisputably procurement statutes, such as CICA, we will hear protests alleging violations of other statutes or regulations when those statutes or regulations bear directly on federal agency procurements. *See Merck & Co., Inc.*, B-295888, May 13, 2005, 2005 CPD ¶ 98 at 10-11; *see also Georgia Power Co.; Savannah Elec. and Power Co.—Costs*, B-289211.5, B-289211.6, May 2,

²¹ In its Veolia II protest, Veolia limited its protest, stating that “[t]herefore, the only issue that GAO need determine is whether or not the [third-party owner] concept is tainted by illegality,” that is, “illegal under 10 U.S.C. § 2688.” Veolia II Comments at 14.

2002, 2002 CPD ¶ 81 (protest of a utility privatization competition under 10 U.S.C. § 2688).

Here, Veolia's promissory estoppel arguments are not grounded upon an asserted violation or violations of a procurement statute or regulation, including 10 U.S.C. § 2688. Rather, Veolia's promissory estoppel arguments are founded upon allegations that NAVFAC induced Veolia to propose a contract structure that the agency, at a higher-level of review, ultimately concluded could not be accepted.²² Although Veolia disagrees with the agency's legal interpretation of 10 U.S.C. § 2688, its promissory estoppel arguments are based only upon its claimed detrimental reliance upon the agency's representations and the subsequent change of position by the agency's higher-level officials, with no assertion that the agency's actions in this regard violated any procurement law or regulation.²³ Because Veolia's promissory estoppel arguments are not founded upon an alleged violation of a procurement statute or regulation, we conclude that our jurisdiction to resolve bid protests under CICA does not encompass this cause of action. See Georgia Power Co.; Savannah Elec. and Power Co.--Costs, supra, at 8 (our determination of a statutory or

²² To the extent that Veolia complains that NAVFAC failed to inform Veolia "[d]uring discussions" that NAVFAC did not view Veolia's proposed three-party contract structure as satisfying "the criteria of statute 10 U.S.C. [§] 2688," as it asserts was required by the solicitations, see RFP No. 3602 at 10; RFP No. 1802 at 9, we find no basis on this record to fault NAVFAC's conduct of discussions with Veolia. That is, there is no indication in the record that, at the time Veolia's proposal was included in the competitive range and discussions were conducted, NAVFAC was aware that Veolia's three-party structure would violate the statute. In fact, the solicitation contemplated that whether a proposal complied with 10 U.S.C. § 2688 was subject to review by higher-level agency officials and that discussions could be concluded and the proposal rejected at any time it became apparent the proposal was not compliant with this statute. See, e.g., RFP No. 3602, at 10. Indeed, the determination by NAVFAC's Assistant Commander for Acquisition was a difficult one and was made, after some reflection, at a much later point in time as a part of his higher-level review of the field activities' recommendations. As noted, Veolia was specifically aware that the judgments and recommendations of the field activities with respect to the privatization of the utility system assets would be subject to higher-level review, see RFP No. 3602 at 4; RFP No. 1802 at 4, which, as we noted above, could result, as here, in the higher-level authority disagreeing with NAVFAC's Atlantic Division's judgment.

²³ Although, as noted above, Veolia argued that NAVFAC's rejection of its proposed two-party/three-party contract structure was based upon an erroneous interpretation of 10 U.S.C. § 2688 (an argument that we have denied above), Veolia's request for recommended relief under a promissory estoppel theory is specifically raised as an alternative basis of protest. See Veolia's Hearing Comments at 1-4.

regulatory violation is the linchpin of GAO's jurisdiction to recommend reimbursement of protest costs under CICA).²⁴

The protests are denied.

Anthony H. Gamboa
General Counsel

²⁴ The United States Court of Federal Claims has similarly found that its jurisdiction under the Tucker Act does not allow it to consider claims based solely on promissory estoppel. See R.R. Donnelley & Sons, Co. v. United States, 38 Fed. Cl. at 521.