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**Comptroller General
of the United States**

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

Decision

Matter of: B.H. Aircraft Company, Inc.

File: B-295399.2

Date: July 25, 2005

Daniel V. Kearns for the protester.

Michael P. Chiffolo, Esq., and Benjamin G. Perkins, Esq., Defense Logistics Agency; and John W. Klein, Esq., and Laura Mann Eyester, Esq., Small Business Administration, for the agencies.

Richard P. Rector, Esq., and Eliza P. Nagle, Esq., DLA Piper Rudnick Gray Cary US LLP, for General Electric Company, an intervenor.

Paul N. Wengert, Esq., and Michael R. Golden, Esq., Office of the General Counsel, GAO, participated in the preparation of the decision.

DIGEST

Protest that agency's bundling of requirements for spare parts for aircraft engine violated the Small Business Act and Competition in Contracting Act of 1984 is denied where agency has established measurably substantial benefit to government from consolidating spare part purchases under a single contract, and established that the single contract otherwise is necessary to meet agency needs.

DECISION

B.H. Aircraft Company, Inc. (BHA), a small business, protests the consolidation of consumable parts for the F404 engine into a single performance-based logistics (PBL) supply chain management contract covering more than two thousand national stock numbers (NSN), under request for proposals (RFP) No. SP0412-05-R-0181, issued by the Defense Logistics Agency (DLA). BHA holds a current contract to supply parts that will be covered by the PBL, and seeks to compete for additional F404 parts. BHA contends that the bundling involved in the PBL contract violates the Competition in Contracting Act of 1984 (CICA) and the Small Business Act.

We deny the protest.

As described by DLA, the procurement will allow the agency to "reunite the currently fragmented F404 consumable parts supply chain and improve support to the

warfighter.” DLA Post-Hearing Comments at 1. The anticipated contract with General Electric is valued at \$300 million.¹ There is no dispute that this procurement concerns bundling of requirements that will affect many small businesses, including the protester.² Specifically, the protester holds an existing contract for consumable parts that will be consolidated under the PBL contract. Protest at 5.

Federal Acquisition Regulation (FAR) § 7.107 states that “[b]undling may provide substantial benefits to the Government. However, because of the potential impact on small business participation, . . . the agency must conduct market research to determine whether bundling is necessary and justified.” Under the FAR, market research may indicate that bundling is necessary and justified if an agency or the Government would derive measurably substantial benefits. As relevant here, the FAR provides that the measurably substantial benefits must be equivalent to 5 percent of the estimated contract value or \$7.5 million, whichever is greater. FAR § 7.107(b)(2). In this case, the threshold would be \$15 million based on 5 percent of the \$300 million estimated value of the contract with General Electric.

The FAR further provides that when the proposed acquisition strategy involves substantial bundling, the acquisition strategy must:

- (1) Identify the specific benefits anticipated to be derived from bundling;
- (2) Include an assessment of the specific impediments to participation by small business concerns as contractors that result from bundling;
- (3) Specify actions designed to maximize small business participation as contractors, including provisions that encourage small business teaming;
- (4) Specify actions designed to maximize small business participation as subcontractors (including suppliers) at any tier under the contract, or order, that may be awarded to meet the requirements;

¹ DLA issued a sole-source justification on the basis that only General Electric, which is the original equipment manufacturer of the F404 engine, could provide the needed supplies and services. Agency Report (AR), Tab 18, Justification for Other than Full and Open Competition, at 1.

² The agency provided notice of the planned bundling to small business concerns, each of which had supplied DLA with one or more of the NSNs covered by the PBL within the preceding 3-year period. Contracting Officer Statement at 6. The agency indicates 1,349 NSNs were purchased from small businesses, and that 259 small businesses had supplied at least one NSN during a recent 3-year period. AR, Tab 8, Market Research Memorandum, at 4.

(5) Include a specific determination that the anticipated benefits of the proposed bundled contract or order justify its use; and

(6) Identify alternative strategies that would reduce or minimize the scope of the bundling, and the rationale for not choosing those alternatives.

FAR § 7.107(e)

As a part of acquisition planning specified in FAR § 7.107, DLA prepared a “rough order of magnitude”³ business case analysis (ROM BCA), comparing the status quo to a PBL contract. Under the PBL contract, the contractor would draw down DLA’s parts inventory to a target of a 120-day parts reserve by providing required logistical support, sourcing, and supply. The ROM BCA anticipated that parts demand would remain constant, the contractor’s prices would be comparable to historical pricing obtained by DLA, the contractor would charge 3 percent for its services, that obsolescence would run at 3.7 percent, and that the cost of money would be 3.7 percent, for a total inventory carrying cost of 7.4 percent annually. AR, Tab 6, ROM BCA, at 9-10. Based on the anticipated reduction in inventory from current levels to a 120-day parts reserve made feasible by the contractor’s knowledge of the F404 engine, control of the supply chain and efficiencies made possible by the PBL contract, the DLA analysis concluded that DLA would produce a measurably substantial benefit of \$28.3 million over 5 years, an amount well above the amount necessary to justify bundling the parts consolidation under a single contract. Additionally, the ROM BCA anticipated a one-time inventory drawdown savings of \$147.9 million.⁴ Contracting Officer’s (CO) Statement at 4. The ROM BCA was based on an analysis of data for 2,639 NSNs because historical data on the remaining NSNs was not available. AR, Tab 6, ROM BCA, at 9.

DLA reports that the planned consolidation of consumable parts requirements under the PBL will generate other important benefits to the government by increasing the availability of needed parts, reducing the incidence of inventory obsolescence, and reducing the volume of purchases for stock by reducing the inventory to a smaller size—a 120-day parts reserve level. Id.

³ Although DLA used the term “rough order of magnitude” in the analysis, it explains that the term reflects the use of estimates because “that’s generally the term within the agency, DLA, that we use to distinguish where you have most of the data you need versus where you have to rely on estimates and judgments.” Hearing Testimony of DLA Senior Operations Research Analyst at 1:36 p.m.

⁴ DLA emphasizes that this one-time savings, while quantifiable, was not considered in determining whether the bundling met the threshold. Declaration of DLA Senior Operations Research Analyst, at 2.

Although DLA initially identified 3,431 NSNs as F404 consumable parts to be covered under the contract, DLA has since determined that 665 of those NSNs were already being provided under a separate Navy PBL contract, leaving 2,766 NSNs for which the contractor will provide logistical support services. Of those, DLA indicates that it will source and supply 312 “mainly competitive small business NSNs,” for which General Electric will supply only logistical support, leaving 2,454 NSNs for which General Electric will provide logistical support, sourcing, and supply. CO Statement at 11.

The record shows that prior to proceeding with the solicitation, DLA fulfilled its obligation to seek the views of the Small Business Administration (SBA), through its procurement center representative, regarding the anticipated bundling. See 15 U.S.C. § 644 (2000); FAR § 7.107. Initially the SBA objected to the bundling as unjustified, and pursued an appeal to reverse the bundling. Ultimately, however, the SBA withdrew its appeal and agreed to the bundling with certain conditions intended to promote and preserve small business participation for these parts, which were memorialized in writing between the SBA and DLA.⁵ AR, Tab 14, Defense Department Form 70, at 2.

BHA first objects that the assumptions made in the ROM BCA are unreasonable and that the savings are overstated. Principally, BHA argues that the obsolescence factor used by DLA is too high because the F404 engine is relatively mature.⁶ Protester’s Comments at 3. The agency responds that it uses the figure of 3.7 percent obsolescence as “an agency-wide rule of thumb or grand average that we use for this sort of assessment. We don’t have an obsolescence rate specific to any program.”

⁵ Our Office invited the SBA to provide its views regarding the protest. Since the protester was not represented by counsel, our Office did not issue a protective order. Our discussion here is, therefore, necessarily general. DLA submitted a copy of the initial proposal that had been received from General Electric to our Office in camera, and provided a copy to the SBA. In its submissions to our Office, the SBA objected that the proposal from General Electric showed that DLA might not be intending to satisfy the conditions upon which the SBA agreed to the bundling. The SBA did not, however, reinstitute its appeal. Nevertheless, any potential breach of the SBA conditions is outside the purview of our Office, and is a matter to be resolved between the two executive agencies.

⁶ The significance of obsolescence to the savings is that under the PBL, DLA will have a smaller inventory to which obsolescence would occur, thus the cost of obsolescence of a smaller inventory is correspondingly less, and that difference then results in a savings to DLA in purchasing fewer parts that will ultimately become obsolete before they are used.

Hearing Testimony of DLA Senior Operations Research Analyst at 1:42 p.m.⁷ DLA indicates that, based on historical experience agency-wide, an obsolescence rate of 6 to 8 percent is the norm, so its use of the 3.7 percent rate was conservative and thus lowered the savings estimate, potentially to the protester's benefit. Declaration of DLA Operations Research Analyst, at 3. The record shows that the agency used the most accurate obsolescence figure available at the time of acquisition planning, which it believed to be a conservative figure. The protester has failed to identify a more reliable number that DLA should have used in its analysis.

BHA also objects that the transition from competitive procurement of many NSNs to the sole source PBL contract will result in higher pricing, making reliance on historical pricing unreasonable. BHA compares historical cost for one NSN, on which BHA competes directly with General Electric, to make the argument that DLA has generally paid between 21 and 30 percent less for particular NSNs when competition was held, than under sole source procurement from General Electric. Protester's Comments at 3. BHA objects that DLA's analysis fails to appropriately consider the benefits of competition.

DLA explains that it believes that for purposes of the ROM BCA, the only pricing data on which it could base its decision was the historical data, since the analysis was required to be part of acquisition planning. Testimony of DLA Senior Operations Research Analyst at 1:48 p.m. The agency also points out that BHA's contention that prices will increase under the bundled contract is based on competition for only one NSN, and does not establish that prices of the larger pool of parts will rise under the PBL. Further, DLA expects that General Electric should be able to obtain better pricing on many parts because it will be able to project the military's needs for a particular part over a longer period of time compared to DLA's shorter term buying approach. The DLA Senior Operations Analyst for this program testified that his experience under similar programs was that pricing patterns stay "within line" and are "comparable" to historical pricing. *Id.* at 1:35 p.m. DLA also advises that General Electric has a competitive process to determine which subcontractor will receive a contract award from General Electric to manufacture a part. Testimony of Supervisory CO at 12:16 p.m. To help ensure that the overall prices paid under the PBL are reasonable, the agency reports that it will analyze prices during negotiations with General Electric to ensure price reasonableness and will examine pricing for "cost drivers," such as demand for individual items and "outliers," items that have a significant, unexplained pricing difference compared to historical pricing.⁸ DLA

⁷ In resolving this protest, our Office conducted a hearing during which testimony was provided by various agency witnesses familiar with the procurement decisions at issue in this protest. The testimony was recorded and the references in the decision are to the time of the testimony.

⁸ The procurement is being conducted as a commercial item acquisition under FAR Part 12. Hearing Testimony of Supervisory CO at 10:18 a.m..

Post-Hearing Comments at 1; Hearing Testimony of Supervisory CO at 12:15 p.m. In short, DLA believes that it has mechanisms in place that will ensure that the overall price General Electric charges for supplies will not increase significantly from historical pricing. Based on the record, we conclude that the agency has demonstrated a reasonable basis for relying on historical pricing in its analysis, notwithstanding the protester's objections, especially since the analysis that the agency is required to conduct occurs at the acquisition planning stage, before pricing has been obtained from the contractor.

BHA also objects that, even if DLA has justified the decision to bundle the requirements, DLA has failed to reasonably accommodate small businesses through other means, as required by FAR § 7.107(e); see also 13 C.F.R. § 125.2(d)(7) (2005). In these circumstances, the acquisition strategy must specifically consider and adopt means by which the agency could maximize small business participation as prime contractors in a manner consistent with its need for cost savings and efficiency. Teximara, Inc., B-293221.2, July 9, 2004, 2004 CPD ¶ 151 at 12. BHA objects that the SBA and DLA agreed to a small business subcontracting goal that is less than the DLA overall goal, and that the alternative of having General Electric provide logistical support while DLA procured the parts, would result in more small business contracting opportunities. Protester's Comments at 4-5. DLA responds that it did address small business concerns. The record shows that DLA has agreed to retain sourcing of some small business-suitable NSNs in order to accommodate small businesses. CO Statement at 8; Hearing Testimony of Supervisory CO at 10:39 a.m. Further, the record shows that DLA and the SBA have agreed to a number of specific actions to promote and preserve small business opportunities in this program. These include requiring General Electric to meet a higher small business subcontracting goal than DLA has historically met for these parts and to remove certain parts that were procured from 8(a) contractors from the General Electric contract. SBA Comments at 4. Finally, DLA explains that the PBL contract represents a comprehensive and unified logistics support package that will result in economies of scale and efficiency that is not available if DLA were to retain significant portions of the procurement responsibilities. AR, Tab 8, Market Research Memorandum, at 5; Hearing Testimony of Supervisory CO at 10:38 a.m. The record reasonably supports the conclusion that the acquisition planning process reasonably addressed the need to accommodate small businesses; the protester has failed to show that DLA could go further without affecting its ability to achieve savings and efficiency.

BHA next argues that the real motivation for bundling is in violation of CICA because it is, in essence, a failure by DLA to properly plan for its requirements, and that this failure does not justify a restriction on competition. BHA maintains that the NSNs for which DLA has properly planned are the ones for which DLA has retained sourcing, while bundling those that it has not planned properly, along with other NSNs for which DLA has no anticipated requirements during the term of the PBL contract. Protester's Comments at 6. The agency explains that the essence of the PBL is to unify the supply chain for F404 consumable parts to an extent that DLA cannot, and also explains that General Electric, by virtue of being the original

equipment manufacturer, is able to achieve savings through efficiency and planning that DLA currently cannot expect to achieve. AR, Tab 8, Market Research Memorandum, at 4-5; Hearing Testimony of Supervisory CO at 11:42 a.m.

CICA generally requires that solicitations permit full and open competition and contain restrictive provisions and conditions only to the extent necessary to satisfy the needs of the agency. 10 U.S.C. § 2305(a)(1) (2000). Since “bundled” (or “consolidated”) procurements combine separate, multiple requirements into one contract, they have the potential for restricting competition by excluding firms that can furnish only a portion of the requirement. Phoenix Scientific Corp., B-286817, Feb. 22, 2001, 2001 CPD ¶ 24 at 5. Because of the restrictive impact of bundling, we will sustain a protest challenging a bundled solicitation, unless the agency has a reasonable basis for its contention that bundling is necessary. Id. at 10; National Customer Eng’g, B-251135, Mar. 11, 1993, 93-1 CPD ¶ 225 at 5. CICA and its implementing regulations require that the scales be tipped in favor of ensuring full and open competition, whenever concerns of economy or efficiency are being weighed against ensuring full and open competition. EDP Enters., Inc., B-284533.6, May 19, 2003, 2003 CPD ¶ 93 at 4. Nevertheless, bundling may serve to meet an agency’s needs where the agency reasonably determines that consolidation will result in significant cost savings or efficiencies. Teximara, Inc., supra, at 6.

Here, the agency reasonably explains that the bundled PBL is the only means by which it can alleviate shortages of parts, increase availability of needed parts, and maintain the military readiness of the aircraft. AR, Tab 18, Justification for Other than Full and Open Competition, at 2, 6. The agency explains that the PBL represents a comprehensive logistics support package--a single contractor will control the various logistical support elements including multiple suppliers and producers, production lines, and transportation resources to ensure that the consumable parts needed by the military are available when needed. Id. We find the agency’s justification reasonably supported by the record.⁹

The protest is denied.

Anthony H. Gamboa
General Counsel

⁹ Although BHA also objects to the inclusion of NSNs in the PBL contract for which DLA does not expect to have a requirement during the 5-year term of the contract, the protester does not allege that any of the NSNs that it seeks to supply is so classified, and therefore BHA is not an interested party because it would not be in line for an award of a contract even if we were to sustain its protest on this basis. Four Winds Servs., Inc., B-280714, Aug. 28, 1998, 98-2 CPD ¶ 57.