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Comptroller General
of the United States

United States General Accounting Office
Washington, DC 20548

Decision

Matter of: XO Communications, Inc.

File: B-290981

Date: October 22, 2002

John E. Jensen, Esq., Jack Y. Chu, Esq., and Steven McLain, Esq., Shaw Pittman, for the protester.
David W. Burgett, Esq., Michael J. Vernick, Esq., and S. Gregg Kunzi, Esq., Hogan & Hartson, for Qwest Corporation, an intervenor.
Michael J. Ettner, Esq., General Services Administration, for the agency.
Paul I. Lieberman, Esq., and Michael R. Golden, Esq., Office of the General Counsel, GAO, participated in the preparation of the decision.

DIGEST

Agency reasonably determined that protester was nonresponsible where, in making the nonresponsibility determination immediately prior to the protester's bankruptcy filing, the contracting officer performed a detailed financial review which established that the firm's unsatisfactory and deteriorating financial condition made it an unacceptable financial risk; the contracting officer had recognized the implications of an anticipated bankruptcy filing and reasonably concluded that it was unlikely that the bankruptcy reorganization plan would significantly reduce the financial risk, and that, even if successful, the bankruptcy reorganization was itself likely to create contract performance risk.

DECISION

XO Communications, Inc. protests an award to Qwest Corporation under request for proposals (RFP) No. TQD-SC-01-1027, issued by the General Services Administration for telecommunications services for federal agencies and other authorized users in the Salt Lake City metropolitan area. XO objects to the agency's determination that XO is not a responsible prospective contractor.

We deny the protest.

The RFP, issued electronically on August 6, 2001, contemplated the award of one or more contracts for a 4-year base period with four 1-year options. The RFP provided for one award to the responsible offeror submitting the technically acceptable proposal with the lowest total offered price, and for the possible consideration of

additional awards based on the next lowest total offered price. XO and Qwest were the only offerors to submit proposals by the September 24 closing date. After a competitive range determination, the conduct of discussions, and the submission of proposal revisions, final proposal revisions were requested on February 28, 2002, and were received from both offerors on March 7. In a post-negotiation memorandum (PNM) executed on June 11, the contracting officer stated that both proposals had been evaluated as technically acceptable with fair and reasonable prices, and that XO's proposal represented the lower total offered price. However, the contracting officer recommended that award be made to Qwest, which was the only responsible offeror. The contracting officer determined that XO was not responsible on the basis of its financial condition, because XO lacked adequate financial resources to perform the contract, or the ability to obtain them. Agency Report (AR), Tab 133, PNM, at 21--22. The source selection authority adopted this recommendation and, on June 17, determined to make a single award to Qwest. The contract with Qwest was fully executed on July 9. XO was notified that it was an unsuccessful offeror on July 10, and after receiving a debriefing, timely filed this protest with our Office.

The only issue presented by this case is the propriety of the agency's nonresponsibility determination.[1] A contract may be awarded only to a responsible prospective contractor. FAR § 9.103(a). No award can be made unless the contracting officer makes an affirmative determination of responsibility; in the absence of information clearly indicating that the prospective contractor is

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[1] XO also protested the agency's determination that Qwest is responsible. Under our current Bid Protest Regulations, our Office will not review an affirmative determination of responsibility absent a showing of possible bad faith on the part of government officials or the misapplication of definitive responsibility criteria. 4 C.F.R. § 21.5(c) (2002). Because neither exception is applicable or even alleged here, this issue is not for consideration on the merits by our Office. Sprint Communications Co. LP; Global Crossing Telecomms., Inc.--Protests and Recon., B-288413.11, B-288413.2, Oct. 8, 2002, 2002 CPD ¶ __ at 4. In particular, XO's sole basis for objection is that the contracting officer failed to consider readily available current information about various ongoing investigations of Qwest pertaining to financial practices and possible criminal matters, which XO alleges raise questions as to Qwest's integrity and are relevant to determining Qwest's responsibility. In XO's view, this constitutes a violation of the requirement at Federal Acquisition Regulation (FAR) § 9.105-1(a) that before making a responsibility determination, the contracting officer shall possess or obtain information sufficient to be satisfied that a prospective contractor currently meets the applicable standards. In sum, XO does not allege bad faith; rather it simply contends that "this case involves a plain violation of the FAR, not a question of business judgment, and therefore is susceptible to reasoned review." Protester's Comments at 15. The express terms of XO's protest allegation do not provide any basis for our Office to review the agency's affirmative determination under our current regulations.

responsible, the contracting officer is required to make a determination of nonresponsibility. FAR § 9.103(b). A finding of responsibility requires, among other things, that the potential contractor have adequate financial resources to perform the contract or the ability to obtain them. FAR § 9.104-1(a). In making a responsibility determination, the contracting officer may rely on the results of a pre-award survey, and we will consider the accuracy of the survey information in reviewing whether the contracting officer's nonresponsibility determination was reasonable. Harvard Interiors Mfg. Co., B-247400, May 1, 1992, 92-1 CPD ¶ 413 at 3. Since the agency must bear the brunt of any difficulties experienced in obtaining the required performance, contracting officers are vested with a wide degree of discretion and business judgment in reaching a nonresponsibility determination, and our Office will not question such a determination unless a protester can establish that it lacked a reasonable basis. Computervision Corp., B-257141, Aug. 12, 1994, 94-2 CPD ¶ 73 at 3.

Here, the contracting officer based his nonresponsibility determination on multiple pre-award surveys (GSA Credit and Finance Surveys), filings by XO with the Securities and Exchange Commission, financial information provided directly to the agency by XO, and XO press releases and other information reported in the media. AR, Contracting Officer's Statement, at 2. In making this determination, the contracting officer shared information with and adopted the findings of the GSA contracting officer for a companion procurement for substantially similar telecommunications services for the Seattle area. That information and those findings (which are summarized below) were memorialized in an April 4, 2002, determination that XO was not responsible under the Seattle procurement.

The information that had been considered by the Seattle contracting officer included an initial pre-award survey report dated August 16, 2001, which indicated that XO had marginal financial resources. The report noted that XO had "a low ten-figure negative tangible net worth, a ten-figure deficit retained earnings, and a high ten-figure heavy debt." AR, Tab 133, PNM, at 8. In addition XO reported a high nine-figure loss in its interim June 2001 financial statements and losses at fiscal year-end 2000, 1999 and 1998, all of which appeared to exceed the sales revenues at each reporting period. Thus, it appeared that XO had never made a profit in its three years of business and the pre-award survey team found XO unsatisfactory as to finances. Id.

In November 2001, XO announced a preliminary equity investment agreement with Forstmann Little & Company (Forstmann) and TELMEX for a total investment of $800 million. GSA's pre-award survey team reviewed the documents associated with this agreement and, on December 17, 2001, issued a report finding that XO remained unsatisfactory as to finances. The investment was contingent on XO successfully completing a restructuring of its existing balance sheet and upon regulatory approvals, and the agreement term sheet mentioned a possible Chapter 11 bankruptcy filing. In addition, XO's updated submissions to GSA indicated a pending

default, and that XO had elected not to pay interest on unsecured notes as part of an overall restructuring, equity infusion and exchange offer. Id. at 9.

On January 16, 2002, XO announced that it had reached a definitive agreement for this equity investment plan. However, the investment was contingent on completion of a debt restructuring and required that XO's debt and preferred stock obligations be reduced from $6.9 billion to $1 billion. XO indicated that it had reached a forbearance agreement with the lenders under its secured credit facility until April 15 to provide XO an opportunity to reach agreement with its creditors regarding the restructuring. The pre-award survey team reviewed this information and advised the contracting officer that XO's definitive agreement did not change its financial picture. The team noted that investors might invest if debt was reduced by April 15, but that neither investor had yet financially involved itself with XO. Id.

On March 1, at the contracting officer's request, XO submitted updated financial information which acknowledged that XO had pending lawsuits, no bank line of credit, and was either in default or contemplating default on obligations. Pending lawsuits against XO in various states had increased from 27 as of December 13, 2001, to 41 as of February 28, 2002, one of which was a U.S. District Court class action suit on behalf of XO's investors, alleging that certain XO officers violated federal securities law by issuing a series of materially false and misleading statements about XO's liquidity and cash flow problems, as a result of which the price of XO common stock was artificially inflated, and that the debt restructuring agreement with Forstmann and TELMEX would result in XO common stockholders losing their equity in the corporation. In addition, XO's updated consolidated statements of operations show year-end revenues increasing by 73 percent from December 31, 2000 ($723,826.000) to December 31, 2001 ($1,258,567,000). However, the net loss identified for the same period increased by 89 percent from $1,101,299,000 to $2,086,125,000. Id.

The Seattle contracting officer also noted that the restructuring agreement with Forstmann and TELMEX faced numerous contingencies and obstacles, that XO's next alternative was to file for Chapter 11 bankruptcy reorganization, which also faced likely opposition, and that if Chapter 11 reorganization failed, XO would file for Chapter 7 bankruptcy liquidation. AR, Tab 104, Nonresponsibility Determination, at 3.

The contracting officer here considered and adopted this information from the Seattle contracting officer's nonresponsibility determination as an accurate summary relating to XO's present responsibility, and further determined that in the two months since the information had been assembled, XO's condition had continued to decline. In this regard, the contracting officer noted that in May 2002, a proposed infusion of $550 million by a different investment group had been withdrawn, concurrent with which the head of that investment group was quoted as stating that XO "is on the brink of meltdown." Id.

XO does not dispute the specifics contained in this determination, and has not contested the finding under the Seattle procurement, with respect to which XO had received notice of the nonresponsibility determination and of award to Qwest on May 14, 2002. Rather, XO alleges that the current nonresponsibility determination lacks a reasonable basis because the contracting officer failed to consider subsequent developments that were relevant and publicly reported. In particular XO points to an alternative "stand-alone" restructuring plan submitted in conjunction with a Chapter 11 bankruptcy petition that XO filed on June 17, 2002. Protest at 6-7. XO explains that this stand-alone alternative was included because Forstmann and TELMEX are seeking to terminate the investment agreement under the primary plan (the plan that was considered above by the contracting officer), which required that XO meet certain conditions that Forstmann and TELMEX have stated will not be met. Id. at 6.

This stand-alone restructuring alternative, as described by XO's press release provides for:

> the conversion of the $1 billion in loans under the secured credit facility into common equity and $500 million of pay-in-kind junior secured debt. The informal steering committee of lenders under the secured credit facility has indicated that it is prepared to support, and recommend that the lenders under the secured credit facility approve, the stand-alone restructuring subject to the preparation of definitive documentation and the completion of customary internal bank approval processes.

Protester's Comments at 6-7.

The press release further states:

> The stand-alone plan permits the Company to seek to obtain additional funding needed for its business plan by issuing common equity through a $250 million rights offering to be made to the Company's senior unsecured creditors, and to the extent that the offer is not fully subscribed . . . to the holders of the Company's subordinated debt and preferred and common stock. Additionally it permits any shortfall to be covered by up to $200 million in new senior secured loans ranking senior to the new junior-secured debt, although no agreements for this financing have been reached.

Id. at 7.

XO takes the position that the contracting officer's failure to consider the favorable impact of this stand-alone plan renders the nonresponsibility determination unreasonable because it establishes that the contracting officer failed to satisfy the

FAR requirement that information on financial resources and performance capability be obtained or updated on as current a basis as is feasible up to the date of award. Id.

In our view, this information regarding XO's possible alternative stand-alone restructuring plan under bankruptcy does not provide any basis to call into question the reasonableness of the contracting officer's nonresponsibility determination. While the CO did not take the specific June 17 bankruptcy filing and the alternative restructuring plan into account, the record establishes that he was aware that a Chapter 11 bankruptcy filing by XO was an ongoing pending possibility, and viewed this as essentially confirming his negative financial assessment without raising the likelihood of imminent financial improvement. AR, Contracting Officer's Statement, at 6. Notwithstanding XO's optimistic perspective, the possibility of reorganization under Chapter 11 bankruptcy is not, as the protester would have it, a panacea that automatically cures a nonresponsibility determination. On the contrary, while the mere fact that an offeror files a Chapter 11 petition for bankruptcy does not require a finding of nonresponsibility, a contracting officer may reasonably view bankruptcy as something other than a favorable development, and as a legitimate factor in finding the offeror nonresponsible. Global Crossing Telecomm., Inc., B-288413.6, B-288413.10, June 17, 2002, 2002 CPD ¶ 102 at 7.

Here, it is beyond dispute that the contracting officer had a reasonable basis to find XO nonresponsible prior to the bankruptcy filing. The only new element to which XO points with respect to the bankruptcy filing is the stand-alone plan. This was an alternative, fallback plan to the long promised and long-delayed Forstmann and TELMEX plan, a plan which the contracting officer, in his nonresponsibility determination, had reasonably concluded was unlikely to succeed. Further, the fallback stand-alone plan on its face depends on a series of uncertain contingencies and approvals. In this regard, it is noteworthy that to date, nearly four months after the filing, XO's bankruptcy reorganization plan has not yet been approved.

In our view, the contracting officer was not obligated to parse the financial minutiae of XO's fallback bankruptcy restructuring plan as part of his nonresponsibility determination. On the contrary, where the record reflects that the contracting officer is cognizant of the alleged effects of a proposed reorganization plan and does not reference them as part of his nonresponsibility determination, we view this as merely indicating that the contracting officer gives the plan little weight. Harvard Interiors Mfg. Co., supra, at 6. Further, where, as here, the court has not yet given approval to the plan, and there is no indication of when, or if, the court would approve any of the proposed reorganization plans, the agency may reasonably give little or no weight to the proposed plan and to any associated favorable financial projections by the offeror. Id. Accordingly, the bankruptcy filing including the

alternative stand-alone fallback restructuring plan provides no basis to call into question the reasonableness of the contracting officer's nonresponsibility determination.

The protest is denied.

Anthony H. Gamboa
General Counsel