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Comptroller General
of the United States

United States Government Accountability Office
Washington, DC 20548

Decision

Matter of: Eagle Home Medical Corporation

File: B-298478

Date: October 13, 2006

Gerald H. Werfel, Esq., Pompan, Murray & Werfel, PLC, for the protester.
Merilee Rosenberg, Esq., Department of Veterans Affairs, for the agency.
Peter D. Verchinski, Esq., and John M. Melody, Esq., Office of the General Counsel,
GAO, participated in the preparation of the decision.

DIGEST

Contracting agency reasonably rejected protester's proposal based on determination that its low price was unreasonably high where price was 39 percent higher than government estimate, which was primarily based on price of recently negotiated contract extension with incumbent contractor.

DECISION

Eagle Home Medical Corporation (EHMC) protests the rejection of its proposal as unreasonably high-priced under request for proposals (RFP) No. 247-0260-06, issued by the Department of Veterans Affairs (VA) to provide home oxygen services and supplies at the William Jennings Bryan Dorn Veterans Affairs Medical Center in Columbia, South Carolina.

We deny the protest.

On May 22, 2006, VA issued the RFP as a HUBZone (historically underutilized business zone) small business set-aside. Offerors were requested to propose fixed prices for 20 different contract line items (CLIN), covering various oxygen cylinders, liquid oxygen, and compressed air items, for a 1-year base period, with 4 option years. Award was to be made to the offeror submitting the lowest-priced, technically acceptable proposal.

VA had been receiving these services and supplies from Medical Comfort Systems, Inc. (MCS), under a contract awarded on January 1, 2001. In October 2005, near the end of the last option year of that contract, the agency negotiated a 6-month

extension (from January 2006 through June 2006) with MCS at prices approximately 2 percent higher than the final option year prices.

VA received two proposals by the June 15 closing date, including EHMC's, which was the lowest-priced. After evaluating the proposals, the agency determined that EHMC's total price of \$5,013,000 (with a net present value of \$4,315,479) was unreasonably high, and thus ineligible for award; the proposal so greatly exceeded the government's estimate of \$3,595,002¹ (with a net present value of \$3,104,309) that meaningful discussions were not possible. The agency then proceeded to cancel the solicitation.

EHMC challenges the agency's determination that its price was unreasonably high, noting that its price was lower than both the prices VA has paid for the same services under a previous contract, and the cost guidelines utilized by the Medicare program for home oxygen services.

A determination concerning price reasonableness is a matter of administrative discretion involving the exercise of business judgment by the contracting officer; therefore, we will question such a determination only where it is unreasonable. The Right One Co., B-290751.8, Dec. 9, 2002, 2002 ¶ 214 at 3.

The agency formulated the government estimate based primarily on the prices it was currently paying under the 6-month contract extension negotiated in October, but increased the price for CLIN 1—for oxygen concentrators, which formed the largest single segment of the contract—from \$60 (the extension price) to \$90.² Even with this 50-percent increase in the CLIN 1 price, as noted, EHMC's price exceeded the estimate by 39 percent. Notwithstanding that there may have existed other price measures that would have been more favorable to EHMC, comparison of prices to a government estimate is a legitimate means of determining price reasonableness. See Bahan Dennis, Inc., B-249496.3, Mar. 3, 1994, 94-1 CPD ¶ 184 at 3 (cancellation based solely on comparison to the government estimate was reasonable). This is particularly the case here, since the estimate was largely based on prices currently being paid under an existing contract.

EHMC asserts that the estimate was too low and did not constitute a proper basis for determining price reasonableness. Specifically, EHMC argues that, since the prior contract was awarded to MCS on January 1, 2001, and since the prices in that

¹ It appears from the record that the estimate should have been calculated as \$3,595,000—that is, \$719,000 per year for 5 years. However, this minor discrepancy is immaterial to our decision.

² MCS's contract priced CLIN 1 at \$90 for the base year and first 3 option years of its contract, and at \$60 for the final option year.

contract remained constant throughout the base year and 4 option years, those prices--which were reflected in the 6-month extension and, thus, the estimate--were not an accurate reflection of the current cost of oxygen equipment and services. We disagree.

While EHMC is correct that the prices in the 6-month extension were similar to those under the preceding contract, this fact in no way diminishes their validity for purposes of determining price reasonableness. Since the prices in the 6-month extension were negotiated in October 2005, and MCS was actually performing the work at the negotiated price when the RFP was issued, we see no reason why the agency could not accept those prices as representative of the current market price. The protester has not shown that the agency failed to consider market conditions or other extenuating circumstances that rendered the negotiated price an invalid basis for comparison. Moreover, the agency did not merely rely on the extension prices; rather, as noted above, it increased the estimate for CLIN 1, the largest segment of the work under the RFP, 50 percent above the fourth option year price under MCS's contract.

Regarding CLIN 1, although MCS was performing at a unit price of \$60 (and, as noted, had been performing at that price during the fourth option year of its contract), the contracting officer (CO) explains that the 50 percent upward adjustment was based on his discussions with another contracting official who had contacted other VA medical centers to obtain prices. CO's Statement, Sept. 21, 2006, at 2. The \$90 unit price also closely reflected offerors' prices under the same CLIN for the 2001-05 contract--offerors there proposed level 5-year pricing (except for MCS's reduced fourth year option price) of \$90, \$93, and \$95. Protester's Comments, Sept. 26, 2006, exh. 1. Thus, while the \$90 unit price was similar to prices from proposals that were submitted in 2000, those proposals essentially reflected the offerors' views that prices would not increase significantly through 2005. Against this backdrop, given MCS's willingness, as of January 2006, to perform CLIN 1 at a substantially lower price, the agency certainly had ample reason to believe that \$90 did not understate the current market price.

The protester also argues that the estimate was flawed in that it did not provide for inflation over the life of the contract. However, while the estimate apparently was based on level pricing (\$719,000) for the base and 4 option years, as already discussed, under the prior contract each of the offerors proposed level pricing over the 5 contract years. Id. Furthermore, while the protester maintains that some significant inflation factor should be applied to each contract year, we note that the protester itself only proposed to increase prices in 2 of the 4 option years. The protester also has failed to provide any evidence establishing that cost increases for home oxygen services and supplies are, or should be, expected to occur over the

contract term. We therefore are not persuaded that inflation should have been factored into the government estimate.³

Finally, the protester points to the fact that the agency and MCS negotiated a price for a 6-month interim contract (to begin after expiration of MCS's 6-month extension in June 2006) that was substantially higher than the extension price or the estimate, as evidence that its price was not excessive. EHMC notes that the price--\$583,914 for 6 months--on an annualized basis (\$1,167,828), is significantly higher than EHMC's base year price of \$951,000. The agency asserts that the interim contract price was high and did not reflect the market, because MCS, as the incumbent, was the only firm in a position to provide a continuity of oxygen supplies; the agency agreed to the high price only because it had no bargaining power. The agency further explains that MCS was motivated to charge a high rate because it had become aware that the new requirement would be set aside for HUBZone small businesses, and that it therefore would be unable to compete for the requirement. CO's Statement, Sept. 21, 2006, at 1. Given the agency's apparently unfavorable position in negotiating the interim contract, we conclude that the interim contract prices were not relevant to the agency's price reasonableness determination.

³ Even assuming that the agency was required to account for inflation in a manner comparable to EHMC's own approach--*i.e.*, increasing prices in 2 option years--we find EHMC was not prejudiced by the agency's actions. EHMC proposed an approximate 5.5 percent increase for option year 2, and a 5.2 percent increase for option year 3. Applying the same increases to the government estimate increases the total estimate to \$3,792,525 (that is, \$719,000 for the base year and option year 1, \$758,545 for option year 2, and \$797,990 for option years 3 and 4). Since, even with this increase, the protester's price--\$5,013,000--still would exceed the estimate by a substantial amount--\$1,220,475, or 32 percent--EHMC was not materially prejudiced by any error in this area, and this argument thus provides no basis for sustaining the protest. AEC-ABLE Eng'g Co., Inc., B-257798.2, Jan. 24, 1995, 95-1 CPD ¶ 37.

In short, we have no basis on this record to conclude that the government estimate was not reasonable.⁴ Accordingly, the agency reasonably rejected EHMC's proposal as unreasonably high-priced.

The protest is denied.

Gary L. Kepplinger
General Counsel

⁴ EHMC also asserts that the agency should have based its government estimate on a "Home Oxygen Contracts Study" prepared for VA by an outside consultant in 2002. Protester's Comments, Sept. 26, 2006, exh. 3. Had the estimate been based on the average cost per patient (\$1,640) provided in this study, with an adjustment for inflation, EHMC's price would have been in line with the estimate. This argument is without merit. VA was under no obligation to create a government estimate in the manner in which EHMC proposes; the agency was only required to use a reasonable estimate. See OMNI Gov't Servs., LP, B-297240.2 et al., Mar. 22, 2006, 2006 CPD ¶ 56 at 3. As already discussed, we find that the agency's methodology in developing its estimate was reasonable. In any case, EHMC's suggested approach to calculating the estimate appears problematic. For example, while EHMC would have the agency use the average cost per patient figure from the study, since the patient costs varied significantly depending on location, it would seem more reasonable for the agency to use the average cost for other VA patients located in South Carolina. In this respect, the study shows Charleston, South Carolina's average cost is \$759. Protester's Comments, Sept. 26, 2006, exh. 3, at 27.