PRICES--REASONABLE VERSUS REALISTIC

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When people speak about the price of an item, they frequently call it "unreasonable." By that is normally meant, "too high" or "not worth the price." The Federal Acquisition Regulation ("FAR") embraces this concept by requiring that in all procurements, the price must be "reasonable." See, e.g., FAR 14.404-2(f) for sealed bids (contracting officer must reject a bid if the price is unreasonable—too high) and FAR 15.402(a) for negotiated procurement (contracting officers must purchase supplies and services at fair and reasonable prices). Indeed, the definitions in FAR 2.101 say that "Pricing means the process of establishing a reasonable amount or amounts to be paid for supplies or services."

How would people describe a price that was extremely low? The term "unrealistic" is probably correct. And in fact, the Government Accountability Office ("GAO") distinguishes between a reasonable price, and a realistic price, as explained below. The distinction underlies the result in *Lilly Timber Svcs.,* B-411435.2, Aug. 5, 2015.

In *Lilly,* the Department of Agriculture sought quotes for multiple awards to plant trees in Illinois. The solicitation required that all quotes be fixed price. As part of its evaluation, the agency reviewed vendor's prices and assigned each a rating of reasonable, risky or unreasonably (low or high) based upon how far the price deviated from the government's estimate, which had been set forth in the solicitation. A reasonable rating was within 15% of the government estimate, a risky rating was between 16-30 % of the estimate, and a rating of unreasonably high or low if the price varied more than 31% from the estimate.

On one project, Lilly's price was 30% below the government estimate (risky), on two others Lilly's prices were 31% and 35% below the government estimate (unreasonably low). In making the awards, the agency concluded that Lilly's prices "created a risk of unsatisfactory performance" and denied them an award.

In sustaining Lilly's protest, the GAO noted the requirement in FAR 15.402(a) for prices to be reasonable, but pointed out that a "reasonableness" determination focuses primarily on whether the offered prices are *higher* than warranted. GAO also noted that, although not required, an agency may also provide for a price realism analysis in a fixed-price solicitation for the purpose of assessing whether a low price reflects a vendor's lack of understanding or a high risk in the vendor's approach. However, a conclusion that a price is too low generally concerns *responsibility* (the vendor's ability and capacity to successfully perform the contract at the offered price). The GAO said that for that reason, an agency may not conduct a price realism analysis without first advising vendors in the solicitation, that the agency intends to do so. In this case, the solicitation only state that reasonableness would be evaluated, and there was no evaluation criteria that told vendors that the agency would consider the realism of vendors' prices.

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The GAO also said that “because below-cost prices are not inherently improper when vendors are competing for award of a fixed price contract, firms must be given reasonable notice that a business decision to submit a low-priced quotation may be considered as reflecting on their understanding of the contract requirements or the risk associated with their approach.” Because the solicitation lacked this required notice, but relied on the agency assessment of risk related to Lilly’s low fixed prices, the GAO held that the agency’s evaluation was unreasonable.

TIPS: Some federal bidders choose to make a business decision to offer the government goods or services at a price that results in a loss to the company. As long as the contract is fixed price (not cost-reimbursement), this type of bid is perfectly acceptable, and may make sense where a company wants to break into a new line of business, or wants to retain a contract for non-monetary reasons, like publicity. The fixed price protects the government, and if the agency is afraid that the contractor cannot perform at low prices, it can simply include a “price realism” (i.e. not underpriced) evaluation factor in the solicitation. A good example of a very low price was in *Alderson Reporting Co, Inc, Ace-Federal*, B-205552, Feb. 12, 1982, 82-1 CPD ¶ 128, where the winning bid was $0.00 for all items. (“Ace's intention to have the bid evaluated at $0 cost to the Commission, not to charge the Commission any fees, and not to offer the Commission any payment. Thus, the Commission properly determined that Ace's bid was responsive.”) Although not stated there, the transcription companies were most likely going to sell the transcripts to non-governmental agencies in order to make a profit—but that was of no concern to the GAO.

In the end, agencies must always, as a matter of compliance with the FAR, determine that prices are reasonable (i.e. not too high). If they want to evaluate offerors to see if they are priced too low, the agency must state in the solicitation that this will be part of the evaluation.

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