SPO 183 – Procurement Pricing

Slide 1 – Title

Aloha everybody! My name is Sarah Allen from the Hawaii State Procurement Office and today we are talking about Procurement Pricing - A Fundamentals class on cost & pricing analysis for the Procurement Lifecycle.

This training has been loosely developed from Volume 1 of the Contract Pricing Reference Guide used by the Federal Acquisition Community. It has been designed to take you through the pricing requirements required at each stage of the Procurement Lifecycle. Understanding where each pricing piece falls within the procurement life-cycle and what your responsibilities are at that phase of the procurement is fundamental to the overall success.

All attendees were sent a copy of the Basic Pricing Class manual, and I hope you have brought it with you today, as the class is built up around this manual.

Note that the words procurement, contracting and acquisition are synonymous for this training, and can be used interchangeably.

Slide 2 – Agenda

We are going to work on the basic introduction, planning and market research over the first 40 or so minutes, and then move on to solicitation, award, contract management and closeout.

Slide 3 – Procurement Lifecycle

Let me introduce you to the procurement lifecycle. Because procurement must be seen as a holistic system. It has a beginning, a middle and an end, and all phases of it must be managed in order to assure a successful contract. Some procurements are short, quick, goods buys that will not need all the bells and whistles, but ultimately, all procurements go through this lifecycle no matter their size and complexity.

Let’s consider where cost & pricing analysis requirements fall in the lifecycle:

First, at the Procurement Planning Stage. Typically, for more complex, high visibility and/or high dollar procurements, an independent government cost estimate (or ICE) is required. This is developed over the planning and market research stage of the procurement lifecycle. Typically, planning and market research overlap each other.

You can see that cost and pricing analysis is required also at the market research stage. Here, you are looking at the market, finding information to substantiate your ICE and learning what the market range of prices and sub-pricing requirements are within the industry you are procuring. The information garnered in this stage will help you greatly when it comes to analyzing whether an offeror’s proposal is realistic and price, fair and reasonable, and also assist you in post-award contract modifications.

At the Solicitation and Award stage, you will be doing cost and pricing analysis on your offers, verifying their accuracy, determining if the proposal is realistic and evaluating your risk.

The Contract management stage will require your doing equitable adjustment analysis for change orders and burn rate reviews to manage the contract funds.

And finally, at Contract Closeout, you will be managing final payment, any deobligation of funds, and collecting lessons learned to be incorporated for the planning of the next procurement.

In a nutshell, the cycle of procurement.

Slide 4 – The Regulations

We have always had a requirement to conduct cost and pricing analysis on procurements, however, recently, the Statute now includes language that Procurement Officers make sure our procurements are priced, fair and reasonable. In addition, we need to write down that analysis in an internal memorandum for record for the contract file. There are a couple of good reasons why this is important. First, monies spent on government procurements come from the tax we pay, so it is our fiduciary responsibility to ensure we are getting the best fair and reasonable price we can within the market. Second, the State has lost court cases in the past because even though we may have used the basic calculations to determine lowest bidder, we had not conducted analysis to show the price was fair and reasonable. Third, a lot of times, we are conducting this analysis, but we just aren't writing it down. Remember, cost and pricing data can be requested for any procurement over $100,000 if the Procurement Officer needs to validate the price for the contract.

Slide 5 – What is Fair and Reasonable Pricing?

What is Fair and Reasonable pricing? Price is defined as the amount the buyer pays for a product or service. However, it is important to remember that, if prices do not cover supplier costs and provide a profit, losses will occur. When a contract is priced below cost, performance risk increases. The contractor must finance contract performance with funds from other sources and contractor default is a real possibility.

Slide 6 – Identify Government's Pricing Objectives

When buying for the Government, your primary pricing objective for all contract actions is to acquire supplies and services from responsible sources at fair and reasonable prices.

Slide 7 – Fair and Reasonable

The term "fair and reasonable price," implies two tests:

1. What is fair?
2. What is reasonable?

What Is Fair? Buyers and sellers may have different perceptions on what price is fair.

1. Fair to the Buyer. To be fair to the buyer, we want to pay a fair market value of contract deliverable, delivered by a well-managed, responsible firm using reasonably efficient and economical methods of performance plus a reasonable profit.
2. Fair to the Seller. To be fair to the seller a price must be realistic in terms of the seller's ability to satisfy the terms and conditions of the contract.

Risk of Prices Unfair to the Seller. Why should you care if a low offer is unrealistic? Because an unrealistic price puts both parties at risk. The risk to the Government is that the firm -- to cut its losses -- might:

- Cut corners on product quality;
- Deliver late;
- Default, forcing a time-consuming re-procurement; or
- Refuse to deal with the Government in the future or be forced out of business entirely.

A fundamental aspect of this concept is that we as Procurement Officers, are the business leaders and facilitators between our customer (the department or division who needs the goods/services/construction), and the contractor. We are in a business partnership with the seller, and we want to ensure that we aren't utilizing our power to deprive a business of their ability to continue as a going concern, and to continue growing and providing jobs to our citizens. We must always look to a win-win answer that creates positive, professional, trusted relationships.

What Is Reasonable? A reasonable price is a price that a prudent and competent buyer would be willing to pay, given available data on:

- Market conditions (supply and demand, competition), and
- All inclusive costs

Your determination of whether an offer is fair and reasonable is a matter of judgment. There is no simple formula in which you can just plug in a few values and receive a firm answer.

<u>Slide 8 – Fair and Reasonable Pricing</u>

Two notes on fair and reasonable pricing:

1. Pricing each contract separately. It is human nature to try to balance one contract against another in terms of financial results. A seller's position might be that the firm lost money on the last contract; therefore, an effort should be made to make up for that loss on the next contract. A buyer's position might be that the contractor made too much profit on the last contract; therefore, the next contract should be structured to restrict profit. While these attitudes may be understandable in a personal sense, they are not valid in Government contracting.

2. Contingencies: the Government pricing objective requires that contracts exclude contingencies that CANNOT be reasonably estimated at the time of award.

Slide 9 – What is Fair and Reasonable Pricing?

Although this class only cover price analysis, I would like to at least define the three focus areas for you here.

Slide 10 – Two Methods for Determining Price Reasonableness?

Price analysis is the process of examining and evaluating a proposed price to determine if it is fair and reasonable, without evaluating its separate cost elements and proposed profit.
When to use? Always.
Basis? Some form of comparison with other prices.

Cost analysis is the review and evaluation of the separate cost elements and proposed profit/fee.
When to use? When the offeror is required to submit cost or pricing data. In this situation, the offeror must provide complete, accurate, and current data to support all proposed costs and profit/fee.
AND/OR
When you require an offeror to submit cost information other than cost or pricing data to support your decision on price reasonableness or cost realism.

Cost realism analysis is the process of independently reviewing and evaluating specific elements of each offeror's proposed cost estimate to determine whether the estimated proposed cost elements:

- Are realistic for the work to be performed;
- Reflect a clear understanding of the requirements; and
- Are consistent with the unique methods of performance and materials described in the offeror's technical proposal.

Slide 11 – Planning and Market Research Steps 1 & 2

It could be argued that the planning part of the procurement is the most important step of the life-cycle. When I say planning, I really mean the first two steps planning and market research. These two steps are typically conducted in tandem with each other. This planning set of steps should be the longest period of time of all your milestones pre-award. Why? Because, if you take the time upfront to plan and research your procurement, the solicitation, award and actual contract management will show the benefits and the statistical likelihood of a successful contract performance jumps significantly.

What are you doing in this set of steps? You should be part of a procurement planning team, assisting the customer in defining their requirements based on the true needs as well as what is available in the marketplace. You will be determining risk expectations, strategizing on best contract type, and defining the evaluation criteria you will be using.

Decisions made in the pre-solicitation phase of the procurement process will be key factors in defining what the Government receives and the price that the Government will pay. For example, contracting decisions that:

- Increase contractor performance costs will normally increase contract price.
- Limit competition will normally increase contract price.
- Facilitate competition will normally reduce contract price.
- Increase contractor risk will normally increase contract price.

The better you understand the marketplace the better you will be able to make decisions that will enable you to meet the needs of the Government at a reasonable price.

<u>Slide 12 – Independent Government Estimate (IGE)</u>

One of the tools you should develop is a Independent Government Estimate or IGE. An IGE is a cost estimate developed by the customer/technical specialist to give the procurement team (and later the evaluation team) an idea of what cost items one should expect to see on an offeror's proposal and what a reasonable contract price should be.

Independent means that this estimate is not a cut and paste of an offeror's proposal, rather, that a government personnel or their acquisition consultant is developing based on the research that is conducted in this phase.

The manual outlook presumes the Procurement Specialist is obtaining this IGE from the customer, and gives instruction as to how much reliance you can place on this estimate. There are four major questions to consider:

1. How Was the Estimate Made?
2. What Assumptions Were Made?
3. What Information and Tools Were Used?
4. Where Was the Information Obtained?

1. How Was the Estimate Made? You must determine how each individual estimate was developed so that the other questions concerning reliability can be examined. Estimates are often based on the last unit price paid with no consideration of changes in the market situation.

2. What Assumptions Were Made? Knowing and understanding those assumptions can give you an insight into the estimator's understanding of reliable estimate development. IN PRICING, THERE ARE NO DUMB QUESTIONS! If you do not know, ask! It is your right and your responsibility!

   Let's look at one estimate example: The requester used the last price paid for an item to estimate the price for the same item 10 years later.

Assumptions. The requester has assumed that the last price paid was reasonable, and that the market situation has not changed in 10 years.

Analysis. Over a few days or weeks, it may be reasonable to assume that the price has not changed if quantity, delivery, and other factors have not changed. But in this case the last purchase was made 10 years ago. Normally, it is not reasonable to assume that the price has not changed in 10 years. Once you identify the assumptions used in estimate development, you can evaluate them and adjust for any that do not appear consistent with market realities.

3. What Information and Tools Were Used? The most successful estimators know their item. Before they make an estimate, they collect information on the product and the market for that product. Their market research may be a one-time effort or part of an on-going process that is an integral part of their normal job. Find out if the estimator is familiar with the market for the item, including:

    - Last price paid?
    - General market price changes?
    - Current commercial market price?
    - Quantity price breaks?
    - Possible substitutes?

    Estimating Analysis. Market information alone is usually not enough. The estimator must be able to apply appropriate analysis to estimate development.

    Reasoned Analysis: analysis that sets forth the known information and clearly explains how it was used in estimate development. This analysis may or may not be supported by the use of quantitative techniques.

    Quantitative Techniques. When appropriate, adjustments should be made using accepted quantitative techniques. For example, index numbers can be used to quantify price changes and adjust historical pricing data.

    Estimate Support Comparison. Estimates supported by words such as "professional judgment," but no factual data and explanations about how that professional judgment was applied, are typically of little value. Estimates based on good information and the application of appropriate quantitative techniques or reasoned analysis will generally be more accurate and easier to support throughout the procurement process. For example, in an analysis of changes in technology, which of the following techniques would be more useful in price estimation?

    Professional Judgment. "Based on my 20 years of experience as a Project Engineer and my knowledge of the product, I estimate the price of this unit at $585,000."

    This is a good start, but adding clear explanations of how the numbers are used in the estimate along with quantitative data points, offer a much more reliable estimate. For example:

Reasoned Analysis. "We are requesting new high sensitivity replacement units. A year ago, a product could not be produced with this level of sensitivity to high frequency sound. Today, units with similar sensitivity improvements are available at a 30 percent higher price than the less sensitive units they replaced. Therefore, the estimated price for this unit, $585,000, is 30 percent higher than the $450,000 price last paid for the less sensitive unit that it will replace."

4. Where was the Information Obtained?

   Some sources of information are better than others. Knowing the sources of information will make it easier for you to evaluate the reliability of the estimate.

   Emphasize Estimator Independence. While use of vendor catalogs and other methods of market research should be encouraged, estimators MUST BE DISCOURAGED FROM CONTACTING VENDORS FOR SPECIFIC QUOTATIONS. This is particularly true in sole source situations, where the Independent Government Estimate may be a primary basis for determining price reasonableness. If both the estimate and the proposal come from the offeror, there is no independent measure of price reasonableness. If the estimator must contact a vendor to better understand specifications, pricing, discounts, etc. then two very important steps must be taken:

   - First discuss the need to contact the vendor with the responsible procurement officer

   - Also, make it very clear, in writing, to the vendor that you are performing market research and need more information about the product or pricing, and that you ARE NOT REQUESTING A QUOATATION OF ANY KIND.

Slide 13 – Market Research

As a minimum, your research, should consider the following data sources.

- Historical Pricing Data For Market Research
- Published Data For Market Research
- Market Research Data From Buyers And Other Experts
- Market Research Data From Prospective Offerors
- Market Research Data From Other Sources
- Using Market Research To Estimate Probable Price

Each time you conduct market research the process will be different because of differences in Government requirements, market conditions, and other factors. The tables in your manual identifies research factors and outlines the type of questions that you should be able to answer when you complete your market research. Not all of the questions identified in the table will be valid for every procurement.

Here's some examples:

- Current Competitive Conditions – do we have multiple sellers in the market to make it competitive?
- Ownership Costs – What repair and maintenance costs will there be over the lifetime? What are the warranty terms?

<u>Slide 14 – Procurement Data Sites</u>

Paragraph 2.2.2.5 on page 43 in your manual talks to researching Government Procurement Data Sites.

<u>Slide 15 – State Websites</u>

The Hawaii State Procurement Website is a helpful way to find out what state cooperative contracts we have where you could compare pricing. The DBEDT website has valuable information on the Hawaii economy.

<u>Slide 16 – GSA Schedules</u>

Federal procurement uses the General Services Administration or GSA who manages federal cooperative contracts within multiple industries, and offer a great set of pricing data. Although Hawaii Procurement Specialists are not authorized to buy directly off the GSA contracts, they can use these contracts to get an idea of how much that product or service is being priced at the federal level. There are a couple of different ways you can access the cost information. I am going to show you some print screens of a search for goods and then services.

Starting at the GSA Library link, lets pick the “Laboratory, Scientific, and Medical” category.

<u>Slide 17 – GSA Schedules Continued</u>

Once picked you will see a range of sources, in this case from staffing services to clinical analyzer tests. Let’s pick on “Medical Equipment and Supplies”.

<u>Slide 18 – GSA Schedules Continued</u>

The Medical Equipment and Supplies source will then show a list of categories to pick from – we’ll pick “Adhesive Tapes and Bandages”.

<u>Slide 19 – GSA Schedules Continued</u>

Here you will see a list of the vendors who have a contract on GSA. There are two ways to access the pricing data from here:

First, there is the contract link, which you can click on and find not only the prices for the items, but also details on the terms and conditions of procuring those goods.

Or, you can click on the Advantage link that takes you directly to a digital marketplace, similar to an Amazon, which will give you prices of the products.

Slide 20 – GSA Schedules Continued

This is a copy of what you would see in the contract.

Slide 21 – GSA Schedules Continued

Alright, let's try that again, but this time for services. Let's click on "Scientific Equipment and Services".

Slide 22 – GSA Schedules Continued

The categories here are little more detailed. We'll pick Testing and Analysis Services.

Slide 23 – GSA Schedules Continued

Again, here you have the vendors and their respective contracts and Advantage links.

Slide 24 – GSA Schedules Continued

And this is how you would see a service hourly rate charge based on labor categories inside of the contract.

Slide 25 – FedBizOpps.gov

Another helpful site to visit is the FedBizOpps site. This site allows the Procurement Specialist to search for solicitations and awards that are similar to what we are buying and garner information that might be helpful such as specific terms and conditions, price constraints and other market information.

Slide 26 – FedBizOpps.gov

Here are some I found for Hawaii.

Slide 27 – FedBizOpps.gov

Make sure to have a look at all the options in the manual. There are a few more really great sites that can help you with your market research!

Slide 28 – Government Economic Data – Bonnie's Example

Paragraph 2.2.2.6 on Page 55 in the manual, we talk about how government economic data can assist you in your pricing market research. Here is a great example where indexes and other economic data charts were used.

Bonnie Kahakui of our office needed to determine whether or not to allow a price increase on our car rental contract. She researched several data points to come to a decision.

The first chart she looked at was the Consumer Price Index, that shows the increase or decrease in general prices – this is basically a view into how inflation is affecting our economy.

For this purpose, there was an estimated average of 1.5% increase

<u>Slide 29 – Bonnie's Example Continued</u>

Then Bonnie looked at Passenger car rental rates, showing a 2% increase in prices.

<u>Slide 30 – Bonnie's Example Continued</u>

Next, gasoline prices had dropped from Jan through April with increases back on in May.

<u>Slide 31 – Bonnie's Example Continued</u>

And new vehicle costs showed very minor deviations.

<u>Slide 32 – Bonnie's Example Continued</u>

In addition, Bonnie made a current price comparison between the competitors. Ultimately, the negotiated price showed an increase of 1-2% versus a much higher increase that was initially requested.

NEXT:
An additional tool for market research is Encouraging Early Exchanges. Potential offerors are a good source of information of market information for planning purposes. Early exchanges of information between potential offerors and members of the Government Procurement Team can identify and resolve concerns regarding the procurement strategy, the Government requirement, proposal instructions, offer evaluation criteria, reference documents, and other industry concerns.

Techniques to Promote Early of information include:

- Industry or Small Business Conferences. Many industries sponsor periodic conferences to share information on technical achievements and business practices.
- Public Hearings. Government personnel can use public hearings to disseminate information about projected Government requirements. Prospective offerors and other interested parties can ask questions and provide input to the procurement decision makers.
- One-On-One Meetings. Any meetings with prospective offerors that are substantially involved with potential contract terms and conditions should include the contracting officer.

- Requests for Information. A request for information (RFI) may be used when the Government does not presently intend to award a contract, but wants to obtain price, delivery, or other information for planning purposes. Responses to an RFI are not offers and cannot be accepted by the Government to form a binding contract. Agency approval may be required before issuing an RFI.
- Presolicitation or Preproposal Conferences. When you use a preproposal or presolicitation conference, materials distributed at the conference should be made available to all potential offerors, upon request.

<u>Slide 33 – Developing Your Price Estimate</u>

Jumping to Page 66 in the manual: Developing your Price Estimate.

Different Data, Different Estimates. As you perform your market research, you will likely find different data that could lead you to different preliminary estimates of contract price. Using the price that you paid for the item 11 months ago, your estimate might be $19,700. If you use the last price paid for the item plus 4 percent inflation your estimate might be $20,488. The catalog price for a similar item from a commercial vendor might be $19,750. The catalog price for a comparable item from a second vendor might be $19,900.

In this case an estimate of $19,750 appears most reasonable because it is based on a current catalog price.

<u>Slide 34 – Procurement Strategy</u>

A vital part of your planning and market research is your procurement strategy which includes

- Identifying your procurement team members, and
- Identifying your total life-cycle costs of the procurement

<u>Slide 35 - Who is Responsible for Determining Price Reasonableness?</u>

The manual on Page 68 talks to the kinds of expertise that should be on your Procurement Planning Team.

One of our of main jobs as procurement personnel is to act as the business leader and facilitate a smooth and successful relationship between the customer (our department or agency) and the contractor (our vendor). We must bring in all interested parties on the government side initially, to ensure all aspects of the procurement are considered from the management side as well as the customer’s point of view.

<u>Slide 36 – Procurement Strategy: Life-Cycle Costs</u>

Life Cycle Cost. Life Cycle cost is the total cost to the Government of acquiring, operating, supporting, and (if applicable) disposing of the items being acquired. Procurement costs are all costs, including contract costs, may involve research and development as well as production, delivery, and installation of the item. Operating and support costs include contract costs, associated with equipment, supplies, and services needed to operate and maintain an operational system. Disposal costs include contract costs, associated with removing equipment from service and disposing of it. Evaluations that consider life-cycle cost should also consider any significant salvage or resale value at the time of disposal. And don't forget about handover and / or surge costs. There might be a period of six months or more where the incumbent might have to work hand in hand with the new contractor on an organized handover. Also, during the contract period, there might be periods of known surge requirements that should be included into the life cycle cost.

Slide 37 – Procurement Strategy: Lease vs. Purchase

Page 74 of the manual talks to conducting a Lease vs Purchase evaluation to see if it is cheaper for the government to lease or buy. Here is an example that also includes a time value of money calculation over time.

The offer to purchase will cost the Government $146,000 at the beginning of year 1, nothing at the end of year 1, but then might receive $12,000 on the sale of the equipment at end of year 2.

The offer to lease will cost the Government just $70.500 at the beginning of year 1, and another $70,500 at the end of year 1.

In order to compare lease vs purchase we need to find the present values of the future amounts. Using the Excel formula, we find that ultimately, it is still cheaper to lease.

Slide 38 – Solicitation & Award Step 3

Responsibility. Sometimes the lowest bid is based on the false perception that this bid, over the course of the subsequent performance of the contract will actually offer the original savings. It can be false economy if there is subsequent default, late deliveries, or other unsatisfactory performance resulting in additional contractual or administrative costs.

While it is important that Government purchases be made at the lowest price, this does not require an award to a supplier solely because that supplier submits the lowest offer. A prospective contractor must affirmatively demonstrate its responsibility...
Therefore, if the low offer is significantly lower than other offers or your estimate of the should-pay price, the burden is on the offeror to affirm its ability to perform at that price.

Important: You cannot make a determination of price reasonableness based on a price comparison with an offer that is technically unacceptable or an offer submitted by a firm that is not responsible.

Slide 39 – Price Analysis

Price Analysis is: The process of examining and evaluating a “proposed price” to determine if it is fair and reasonable without evaluating its separate cost elements and profit.

Always involves some form of comparison with other prices. The basis for your comparison should be a price that has been determined a reasonable estimate of the price a reasonable person is willing to pay.

Slide 40 - Should-Pay Price

Should-Pay Price. The should-pay price, used for comparison, is the price that, in your best judgment, the Government should reasonably expect to pay for the deliverable based on available information concerning competitive offers, historical prices previously paid, validated commercial prices, pricing yardsticks, and Independent Government Estimates (IGE). Remember your should-pay price is an estimate and therefore just an approximation of the price the Government can expect to pay. Being an estimate, it is by definition inexact. So, be amenable to offers that are close to, but not exactly at, your should-pay price estimate, but investigate the reason if there is a significant variance between your should-pay price and the offered price.

During your analysis, you will need to account for the differences in the offered price to your expected price range. There might be added options included in the offer, or a perhaps the offeror has a cheaper, more innovative approach than your team had considered. Remember to consider similar characteristics to make the comparison meaningful.

Slide 41 – Price Analysis

Page 83 of the manual shows the process for making price comparisons.

Step 1 is selecting prices for comparison.
The best starting place is to look at the other proposed prices – are they from responsible sources?
Then, is the comparison between your goods and services and those found in the published price lists valid?

Step 2 is identify factors that affect comparability.
Consider what is the geographic location? For example a previously proposed price for Maui might be different to Oahu.
What is the extent of the competition? Fewer sources typically mean higher prices.
Has technology changed since the previously proposed price?
What about differing terms and conditions?

Step 3 is determine the potential impact of these factors on prices selected for comparison.
How substantial is the impact? A geographic separation between Maui and Oahu might not substantially effect the price, whereas a new technology could radically change price.

Step 4. Adjust prices selected for comparison. Remember you are looking to compare apples to apples. If you have a previously proposed price from three years ago, use an index number chart such as the

Consumer Price Index to calculate the inflation rate growth to increase the price to a more reasonable number for today. Have your technical subject matter experts give you information on trends in the industry. Use price volume analysis to adjust quantity, size and volume for comparison. Cost estimating relationships will be discussed more thoroughly in the cost analysis class.

And finally, Step 5 – Compare offered prices with adjusted prices. Consider how much reliance to place on each comparison.

Slide 42 – Price Analysis

This section covers comparability in more detail. Remember, the Procurement Officer is responsible for making the determination that the offered price is fair and reasonable and for selecting the basis for comparing that price. The basis of the proposed price and comparison prices must be analyzed and documented for the contract file.

Slide 43 – Price Analysis

Page 88 of the manual talks to how price analysis varies depending on the estimated dollar value of the contract. For example:

For micropurchases under $2,500: The administrative cost of verifying the reasonableness of the price may more than offset potential savings from the effort, so verifying price reasonableness need only be taken if you suspect or have information to indicate that the price may not be reasonable.

For small purchases, comparing competitive quotes is the preferred method for pricing these procurements. If you only receive one quote, then you would go back to the list of price analysis comparisons.

For contracts over the small purchase thresholds, then you would look at the list of price analysis comparisons. When comparing to other proposed prices, place less reliance when:
The apparent successful offeror has such a decided advantage that it is practically immune from competition.
The apparent successful offeror's price is significantly different (higher or lower) than the next rated offeror. This could indicate that there is a mistake in bid, a misunderstanding of the contract requirements, etc. In this situation, you should take steps to verify the offeror's bid and/or use another technique to analyze the price.
Government requirements permit offerors to propose widely different technical approaches to contract performance. For example, a ceramic mug and a paper cup may both meet a requirement to hold 8 ounces of coffee, but that does not mean that $1.00 price for a paper cup is reasonable because it is less than a $5 price for a ceramic mug. Even if no other offeror is proposing to provide a paper cup, the key element of your price analysis should be to compare the paper cup offer with prices paid for similar paper cups.

Slide 44 – Price Analysis Example

Commercial prices are prices being paid by the general public for a product. Here is an example of a fair and reasonable justification:

Agency is unable to join / enroll in WSCA 10-01 due to the cooperative agreement's start a year ago. HP is able to provide the HP Designjet T1200 HD Multifunction Printer for $17,913.00, Four Year Next Business Day Hardware Support for $3,827.00, and the required ink cartridges for $414.00. Amazon.com was able to provide the same printer and ink cartridges at $18,561.24 and $449.34 respectively. CDW.com's pricing was quoted at $19,795.99 and $383.94. A comparative table below displays the price of the 3 companies while supplying the warranty directly from HP as the manufacturer. Below are the quotes that support this justification.

The manual goes on to give more details on previously proposed prices and independent government estimates.

Slide 45 – Factors That Affect Comparability

Picking back up on Page 97, Paragraph 3.3 talks to identifying factors that affect comparability.

1. Market conditions change. The passage of time usually is accompanied by changes in supply, demand, technology, product designs, pricing strategies, laws and regulations that affect supplier costs, and other such factors. Look instead for prices that were established under similar terms and market conditions.

2. Variations in quantity can have a significant impact on unit price. Typically, if you buy in bulk, you should receive a higher discount, but this may not be so if the supplier cannot handle the large volume you want to order.

3. Here in Hawaii, we always need to consider geographic location. Check for differences in the level competition that may affect price comparisons. And Check freight requirements and accompanying costs. These can vary considerably, especially for chemicals and other hazardous materials.

4. Purchasing power: use price index numbers to adjust for the changing value of the dollar over time. It is fair and reasonable to expect an older proposed price would increase due to inflation eroding the real value of money.

5. Extent of competition. The last time you solicited for this good or service, you may have received only one quote. Now the environment might have changed and there will be more competition.

6. Terms and conditions include things like packaging, delivery, financing, discounts, payment terms, etc. Prices on contracts for delivery in 90 days may well be higher than those for delivery in 180 days because the contractor may have to hire additional employees or pay overtime to expedite manufacturing to meet the shorter delivery date. When the Government has other complex demands or urgent delivery requirements may cause the price to be significantly higher than usual.

7. Technology. Prices from dying industries can rise because the technologies don't keep pace with rising costs. Conversely, technological advances in growth industries can drive prices down.

8. Government unique requirements. Our state laws may require specific unique requirements that are not required in commercial market transactions. These differences will also affect price comparisons.

<u>Slide 46 – How do we know we are getting a fair and reasonable price in the following?</u>

These types of procurements or procurement actions typically require additional analysis is conducted to show the price is fair and reasonable. Even in an emergency such as a declared disaster, prices still have to be found price fair and reasonable or FEMA can refuse to pay for it.

<u>Slide 47 – Solicitation & Award: Unbalanced Bids</u>

A word on unbalance bids – moving to page 107, or section 3.7: there are times where you will received unbalanced pricing. You need to know how to recognize this and understand the risk that is involved.

Unbalanced pricing exists when, despite an acceptable total evaluated price, the price of one or more contract line items is significantly over or understated as indicated by application of cost or price analysis techniques. This can:

- Increase contract performance risk; or
- Result in payment of unreasonably high prices.

A bid is materially unbalanced IF it is mathematically unbalanced AND one of the following is true:

- There is reasonable doubt that the lowest evaluated bid will actually result in the lowest cost to the Government.
- The offer is so grossly unbalanced that its acceptance would be tantamount to allowing an advanced payment.

A bid is mathematically unbalanced IF it is based on prices that are significantly less than cost for some line items AND significantly more than cost for other line items.

<u>Slide 48 - Solicitation & Award: Price-Related Decision Process</u>

Government procurement in the pre-award phase does not allow for open negotiations to take place in the same way that it does in the commercial market. However, the Government does have a discussions phase that should require the Procurement Officer to prepare Pre-negotiation Objectives. Pre-negotiation objectives establish the Government's initial negotiation position and assist in determining whether a price is fair and reasonable.

First, you should analyze the risk of the proposed prices, and consider how realistic they may be.

Second, you should develop price positions and data points that will substantiate your positions. This is even more important during contract modification or change order negotiations. A price discussion memorandum will document your price objectives.

Slide 49 – CONTRACT MANAGEMENT AND CLOSEOUT Steps 4 & 5

And finally, we have Steps 4 & 5: Contract Management and Closeout on Pg117 of the manual.

Slide 50 – Contract Management

During the contract management phase, you will come across Requests for Equitable Adjustments, typically processed as a modification of some kind to allow for additional monies on the contract. Some of the reasons for this to occur is because of:

- Changes to government specifications
- Government delay of work
- Differing site conditions etc.,

There are two main types of modifications: bilateral where both the contractor and procurement officer sign and unilateral where only the procurement officer signs.

When you use a unilateral contract modification, the contractor must continue to perform the modified contract.
While continuing to perform, the contractor incurs actual costs related to the change. As a result the contractor's proposal for an equitable adjustment must include a combination of actual and estimated costs. Each day work is completed so actual costs change and the estimated cost for uncompleted work changes. Negotiations are like trying to hit a constantly moving target.
Each day of contractor performance reduces the possibility that you can further influence how the contractor will interpret the modified contract requirements.
Contracting officers must definitize unilateral modifications within the shortest practicable time. Contracting officers commonly perceive this requirement as additional pressure for timely settlement on them but not on the contractor.

Both the contractor and the government hold certain advantages in Equitable Adjustment Negotiation:
For example: An equitable adjustment negotiation may provide the contractor with negotiation advantages not present before contract award.

Negotiations are noncompetitive. Pricing alternatives on the original contract may have been limited by competition.

Whereas, for the government, the contractor performance must continue, so the Government is not faced with a lack of progress in meeting its needs.

A bilateral, negotiated agreement is generally a better deal for both sides because:
A unilateral contracting officer's decision may give the impression of being win/lose no matter how reasonable it is.
Disputes are long and expensive for both parties involved.
If the Government wins, the contracting officer's decision may still appear one-sided to the contractor.
If the contractor wins, it appears that the Government adopted a win/lose position and lost.

<u>Slide 51 - Contract Management</u>

Contract Funding logs and Burn Rate logs are vital to maintain an ongoing level of knowledge of how the funding for that contract is being used, how fast are we burning through our monies and what is our balance at any one time.

It is important to keep a log, especially on large complex contracts where many funding modifications are being processed. This is especially true when there is no eProcurement to accounting system available to track and view these transactions.

Here is an example of a Burn Rate Log
You will see that using a Pivot Chart will give you and your management a clear understanding of how fast the money is being spent. You should set a quarterly meeting to discuss the burn rate with the contractor to ensure you have enough funds to maintain the contract for the full year and/or obtain your deliverables before the money runs out.

<u>Slide 52 - Closeout</u>

When the government terminates partially or wholly for convenience, the contractor may be authorized to submit settlement expenses.

Commercial contract termination for convenience settlements center on determining the percentage of contract work performed prior to the notice of termination and reasonableness of charges related to the termination. The termination settlement is calculated by multiplying the contract price by the percentage of work performed and adding the reasonable charges related to the termination.

Your objective should be a settlement that compensates the contractor fairly for the work done and the preparations made for the terminated portions of the contract including a reasonable allowance for profit.

The amount payable under a settlement (not including settlement costs) must not exceed the contract price less payments otherwise made under the contract. From that amount you must deduct any disposal or other credits.

The biggest problem is often the atmosphere surrounding the termination process. While the atmosphere surrounding a new contract negotiation is one of hope and a new beginning, the atmosphere surrounding a termination is one of lost opportunities. Many times it is an atmosphere of distrust and resentment. You must not allow this atmosphere to drag you into a win/lose negotiation.

Slide 53 – Mahalo!

Thank you so much for being part of this pricing class. Please contact us if you have any specific questions. We would love to help you further. Mahalo and Aloha!