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The Herman Miller Decision: A Missed Opportunity and Troubling Precedent

By Roger Waldron

The U.S. Government Accountability Office recently rendered an opinion regarding a bid protest brought against a solicitation intended to implement a novel Air Force acquisition strategy which is of significant interest to the acquisition community. *See Herman Miller, Inc.*, B-407028, 2012 CPD ¶ *296 (*Oct. 19, 2012).

The decision is interesting in a number of respects, including the issues it addresses, the issues presented by the solicitation that are not addressed, and the precedent that the troubling acquisition strategy at issue (with which the Air Force is free to proceed) may set for the acquisition system generally.

A. The Facts. The solicitation in question was issued by the Air Force as part of its effort to acquire office furniture for bases throughout the continental United States (''CONUS''). According to the synopsis of the solicitation, the stated objective of the acquisition is to ''procure systems and modular furniture as well as demountable walls, to include all panels, work surfaces, storage, electric components and related accessories.'' As stated in the solicitation, the Air Force is pursuing a ''Two Tier'' strategy for acquiring relevant office furniture. Under ''Tier I,'' the Air Force will enter into contracts with furniture manufacturers. These contracts will establish not-to-exceed (''NTE'') prices for systems and modular products and services to be later procured under ''Tier II'' contracts through competitions held by CONUS users, *e.g.*, Air Force bases. The Tier I contracts also will identify a manufacturer-authorized small business ''Dealer Network'' for use by CONUS users.

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The solicitation prescribes a ''Manufacturer/Dealer Agreement'' for use by the manufacturers and dealers under the Two Tier strategy. Among other things, this agreement requires the dealer to affirm its intention to remain ''small'' for purposes of the program. This provision is wholly inconsistent with the goal/purpose of small business contracting programs, which is to encourage the growth of small businesses into larger ones.

The solicitation was issued under a Standard Form 1449, which pertains to an acquisition of ''commercial items,'' as defined in the Federal Acquisition Regulation. The solicitation calls for submission of firm-fixed prices for certain reporting activities. According to the solicitation, no furniture or other products will be purchased or supplied under the Tier I contracts. Instead, all furniture will be purchased under the Tier II contracts awarded to small business dealers.

B. The Concerns Raised by the Two Tier Strategy. The solicitation raises a variety of concerns.

First, the solicitation constrains the manner in which manufacturers may sell furniture. Applicable statutes and regulations require that federal agencies engage in ''full and open competition,'' which requires that an agency include restrictive provisions only to the extent necessary to satisfy the needs of the agency. *See* 10 U.S.C. § 2305(a)(1); FAR 11.002. Requiring that manufacturers sell their products only through certain small business dealers (rather than directly or through the manufacturers' current or ordinary dealer networks,) imposes a considerable burden on competition. The Air Force would not appear to have a need for certain types of entities (e.g., dealers) as opposed to others (e.g., manufacturers) to deliver and install furniture that meets the Air Force's needs.

It should be noted that through the Tier I contracts, the Air Force will determine which manufacturers' furniture models satisfy the agency's needs. As a result of

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the submission of NTE pricing in the Tier I proposals, which is binding on sales under Tier II, the Air Force also will have determined that the pricing for such furniture is fair and reasonable. As a result, there does not appear to be a reasonable basis to limit competition for Tier II contracts.

Under the Two Tier strategy, a manufacturer may not sell its furniture directly under a Tier II contract even though the same furniture could be offered through a dealer and thus obviously meets the government's needs. Similarly, a dealer that lacks an existing relationship with a manufacturer under a Tier I contract—even if it qualifies as a small business—could not sell the same furniture under a Tier II contract. Either of these approaches would preclude the supply of the same furniture at the same (or even lower) prices. In this era of budget pressures, that constraint is questionable.

Second, although the Air Force issued the Tier I solicitation as a ''commercial item'' solicitation, the agency was soliciting proposals from furniture manufacturers for services rather than products. The services (formation of dealer networks, monitoring of the performance of dealers, ensuring dealers submit proposals for the Tier II competitions, and reporting to the Air Force on the dealer performance) are not tasks that such companies generally perform for commercial customers, as the FAR requires for a service to qualify as a ''commercial item.'' *See* FAR 2.101.

Interestingly, roughly a month before the *Herman Miller* decision was issued, GAO sustained a protest that challenged the terms of a solicitation on the basis that the terms at issue were not consistent with ''customary commercial practice,'' as the FAR requires for the terms of a commercial item solicitation. *SeeVerizon Wireless*, B-406854,B-406854.2, 2012 CPD ¶ 260 (Sept. 17, 2012). The *Herman Miller* decision does not address or discuss the *Verizon Wireless* case or its significance to the issues presented in *Herman Miller*.

The Two Tier strategy will result in changes to contractor's commercial practices, including pricing for dealers. Because a dealer intermediary must be used, the manufacturers' sales under the Two Tier strategy might not qualify as sales to federal agencies for purposes of GSAR 552.238-75 as the sale is made by the manufacturer to a dealer rather than directly to a federal agency (which would fall within an exception to the Price Reductions clause). The Two Tier strategy thus could impose significant price ramifications for a manufacturer and, at a minimum, raises considerable uncertainty.

Third, the apparent purpose of the Two Tier acquisition strategy (over simpler and more efficient means such as use of the Multiple Award Schedule program) is to enhance small business participation. This goal could be achieved just as effectively by encouraging manufacturers to team with and use small businesses as dealers or installers where feasible under a Schedule purchase. Schedule orders, moreover, may be set aside for small businesses. The Two Tier approach will discourage competition for small business by precluding any dealers from obtaining contracts to supply furniture at bases to the extent they do not have dealer agreements of the type specified in the Tier I Solicitation.

Reliance on the Two Tier strategy to foster small business participation is problematic in another respect. Because the Tier II contracts are dependent upon the Tier I contracts, it is unclear which NAICS code should be used for the Two Tier strategy and whether it accurately reflects the nature of the underlying work. The solicitation currently uses NAICS code 337215, Showcase, Partition, Shelving, and Locker Manufacturing, which is for establishments primarily engaged in manufacturing wood and non-wood office and store fixtures, shelving, lockers, frames, partitions, and related fabricated products of wood and non-wood materials, including plastics laminated fixture tops. However, the solicitation further states that the ''Tier I contracts shall establish not-to-exceed pricing for systems and modular products and related services to be procured later at Tier II'' (at page 22). Consistent with the language found on page 22, Attachment 9 of the solicitation includes 41 pages of typical configurations for modular/systems office furniture. Moreover, the value of the modular/systems furniture to be acquired under this procurement far exceeds the dollar value of standalone wall panels. As such, the correct NAICS code for systems and modular furniture to be acquired under this acquisition appears to be 337214, Office Furniture.

Importantly, the Small Business Administration has granted a waiver from the non-manufacturer rule for NAICS code 337215. As a result, the Air Force can take credit towards its small business goals for the entire value of the Tier II contracts even if the furniture delivered under the Tier II contracts is the product of a large business. In contrast, NAICS code 337214 does not have such a waiver. It is form over substance—the ''form'' being the Two Tier structure and choice of NAICs codes to ensure maximum small business credit, and the ''substance'' being the actual work performed by the small business dealers under the Tier II contracts.

The Two Tier strategy raises a question whether the small business dealers should be deemed as affiliated with the manufacturers. Under SBA's ''ostensible subcontractor'' rule, 13 C.F.R. § 121.103(h)(4), a prime contractor and its subcontractor may be treated as affiliates if the subcontractor either performs the primary and vital requirements of the contract, or if the prime contractor is unusually reliant upon the subcontractor. Under the Two Tier strategy, the manufacturer and its dealers must work together in pursuit of the contract opportunities, and the dealer is constrained to offer pricing in accordance with the NTE pricing submitted by the manufacturer. Moreover, the Tier I solicitation requires that the manufacturer submit a ''Dealer Management Plan'' that among other things ''demonstrates how the offeror will ensure the Dealerships within the network maintain a greater than or equal to 80% request for proposal response rate for their assigned bases....'' This requirement essentially means that the manufacturers will have some negative and/or positive control over the fundamental business decision as to whether a small business dealer competes for a specific requirement or not. This control over the small business dealer's competitive decision making raises significant concerns regarding affiliation with the manufacturers.

Fourth, the Two Tier acquisition strategy also poses a significant risk of organizational conflicts of interest as manufacturers will be asked to oversee and report with regard to dealers with whom they have a financial relationship. In short, manufacturers may be akin to subcontractors under the Tier II contracts but will be required to report under the Tier I contracts with respect

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to the performance of their associated dealers (who will be contractors and prospective offerors under Tier II contracts).

The Two Tier strategy also does not address the prospect that in one or more areas, a particular dealer might sell the product lines of more than one manufacturer. The dealer thus will be in the position of electing which of various competing lines to offer at prices below the amounts established in Tier I contracts. Because supply under Tier II contracts is limited to certain small business dealers in the Dealer Network, a manufacturer could not attempt to mitigate such a conflict by requesting a different dealer to offer its product or offer the products itself. Implementation of the Two Tier strategy thus may result in dealers with conflicting interests, which could jeopardize the fairness of Tier II competitions.

Finally, the GAO decision does not address an aspect of the acquisition strategy that may be most troubling to Multiple Award Schedule (MAS) contractors and the public: the Two Tier strategy will result in considerable contract duplication with the four Tier I contracts and literally hundreds of Tier II furniture contracts with the Air Force installations nationwide. This duplication increases costs to the furniture manufacturers who already have in place MAS contracts for the furniture being sought under the Air Force solicitations.

C. The Decision. GAO did not address all of the issues identified above. This may be due to how the protest was framed. Some issues, such as contract duplication, are ones that GAO does not regularly address, although the presence of existing alternative contract vehicles may bear on whether the specified means of acquisition is unduly restrictive.

Rather than address the range of issues identified above, GAO addressed only two issues: (i) the prospect that prospective offerors may lack adequate information with which to prepare proposals due to some purported ambiguity in the solicitation and (ii) whether the Air Force had selected the correct NAICS code for the effort. In regard to the latter, GAO held that it lacked jurisdiction to review the question.

In regard to the former, GAO held that the solicitation provided sufficient information to allow manufacturers to compete on an equal basis and did not impose undue risk on them. The discussion in this regard focused on the Price Reductions clause in the MAS contracts and, particularly, the prospect that manufacturers who had dealers as their basis of award customer category would be at risk of price reductions extended to dealers under the Two Tier acquisition strategy. GAO cited the fact that the General Services Administration (''GSA'') had issued a memorandum stating that, solely for the purposes of the two-tiered procurement, GSA would forbear enforcement of the clause for vendors that request a modification from GSA.

GAO also rejected Herman Miller's argument that the RFP did not provide for meaningful consideration of price (contrary to 10 U.S.C. 2305(a)(3)(ii)) because the NTE pricing is for furniture that will not be acquired under the contracts, and the only pricing at issue is for minor program management reviews and data reporting. In rejecting the claim, GAO stated:

> These contracts also provide for promised not-to-exceed prices that will be relied upon by the manufacturer's dealers in the second tier competitions. Although Herman Miller contends that such an acquisition approach should not be permitted, it cites to no law or regulation violated by this approach. In this regard, the FAR expressly recognizes that ''if a specific strategy, practice, policy or procedure is in the best interests of the government and is not addressed in the FAR, nor prohibited by law (statute or case law), Executive Order or other regulation, that the strategy, practice, policy or procedure is a permissible exercise of authority.'' FAR § 1.102(d).

Herman-Miller, 2012 CPD ¶ 296, at *3. GAO did not address whether the pricing or any other aspect of the RFP implemented a commercial practice.

D. What the Decision Means. For reasons that are unclear, GAO did not address some of the larger questions presented by the Two Tier strategy, such as how the prescribed dealer agreement and the Tier I contracts (which call only for reporting and program management by furniture manufacturers) qualify as a ''commercial item'' under the FAR.

Because GAO did not sustain the protest, it is reasonable to expect that the Air Force will proceed to implement the Two Tier strategy. Other agencies may follow suit. Thus, there is a risk that the Two Tier strategy may proliferate, and extend to other products and services (such as information technology). The consequences may be problematic for the government and Multiple Award Schedule contractors.

Because manufacturers that would compete under the Two Tier strategy already have Multiple Award Schedule contracts under which Air Force agencies may place orders and award blanket purchase agreements, there would not appear to be any need for separate contracts to acquire the same commercial furniture. In regard to the government, administration of such contracts will require considerably more agency time and resources than reliance on the Multiple Award Schedule. Indeed, the MAS ordering procedures allow for the use of Blanket Purchase Agreements to leverage recurring requirements. The Air Force could have conducted a streamlined competition for its requirements using BPAs under the manufacturer's MAS contracts for the same furniture it is now seeking under the current open market solicitation. The MAS approach would have saved time and money while allowing the Air Force to strategically source its recurring furniture requirements.

In regard to contractors, the Two Tier strategy renders the manufacturers' Schedule contracts less valuable. The prospect of diminished sales due to contract duplication is something that contractors always must consider when negotiating pricing for Schedule contracts, which entail unique compliance burdens under the Price Reductions Clause. Moreover, the Air Force's decision to create standalone contracts that duplicate the GSA MAS program increases bid, proposal, administrative, and transactional costs for industry—costs that could have been avoided through the use of preexisting MAS contracts.

In short, contract duplication for the acquisition of commercial items increases transactional costs for government and industry—costs that ultimately are borne by the taxpayer. At the same time, contract duplication undermines the value, efficiency, and effectiveness of the MAS program for all.