

STATE OF NEW YORK
OFFICE OF THE STATE COMPTROLLER

In the Matter of the Bid Protest filed by
Sunoco, Inc. (R & M) with respect to the procurement
of a contract for the operation of fuel service
facilities on the New York State Thruway Authority
Request for Proposals No. 5C036

Determination of
Bid Protest
SF- 20060176

August 16, 2006

This Office has completed its review of the above-referenced procurement conducted by the New York State Thruway Authority (hereinafter the "Authority") and the bid protest filed by Sunoco, Inc. (R&M) (hereinafter "Sunoco") with respect thereto. As outlined in further detail below, we have determined that the grounds advanced by Sunoco in its bid protest form a sufficient basis to overturn the Authority's award of a contract to Lehigh Gas Corporation (hereinafter "Lehigh") and, as a result, we are returning the proposed Lehigh contract unapproved.

BACKGROUND

On October 17, 2005, the Authority issued Request for Proposal No. 5C036 (hereinafter "RFP") for the operation of twenty-nine (29) fuel service facilities on the New York State Thruway.

The term of the existing contractual arrangement for operation of thirteen (13) of these facilities (Groups 1-4, then currently operated by Exxon-Mobil) was scheduled to expire on May 31, 2006. The contract for sixteen (16) other fuel service facilities (Groups 5-9, operated by Sunoco) was scheduled to expire on September 30, 2006.

Three proposals were received and were opened on January 27, 2006. Sunoco and Lehigh each submitted a proposal providing for operation of all twenty-nine (29) fuel service facilities.¹

The proposal submitted by Sunoco was rated highest by the evaluation committee, because the committee found that Sunoco's proposal offered the best value to the Authority. The award of the contract to Sunoco was approved by the Authority on

¹ A third proposer, Wilson Farms, submitted a proposal for operating four (4) facilities in the Rochester/Buffalo area (Group 9).

March 16, 2006, and contract negotiations ensued. Drafts of the contract were exchanged and reviewed by the parties, but no final agreement was reached on all contract terms.

On May 4th, having not yet successfully negotiated a contract with Sunoco, the Authority's Board held a regularly scheduled Board meeting, at which the Board adopted a resolution authorizing the Authority to enter into two ten year contracts with Lehigh, one for the operation of the thirteen (13) fuel service facilities (Groups 1-4) for which the existing contract was scheduled to expire on May 31st, and one for operation of twelve (12) of the fuel service facilities (Groups 5-8) for which the existing contract was scheduled to expire on September 30th.²

Also on May 4th, Sunoco learned that the Authority Board had authorized the Authority to enter into negotiations with Lehigh. These negotiations culminated in the Authority's execution of a contract with Lehigh on May 11, 2006 for operation of the facilities in Groups 1-4.

On May 19, 2006, Sunoco filed a protest with the Authority pursuant to the Authority's Vendor Protests policy, contending that:

- Sunoco's proposal had presented the best value to the Authority
Sunoco and the Authority were in agreement on all financial terms of the contract, with only one remaining issue outstanding, with respect to which Sunoco had offered several alternatives and had requested the Authority to similarly provide alternatives
- while acknowledging that the RFP had provided the Authority with the ability to negotiate simultaneously with multiple proposers, under the circumstances the Authority acted arbitrarily and capriciously by abruptly terminating contract negotiations with Sunoco

On June 7, 2006, the Authority issued a Notice of Decision, denying the protest and concluding that ". . . the Authority did not act arbitrarily and capriciously in terminating contract negotiations with Sunoco in conjunction with RFP No. 5C036 on May 4, 2006."

On June 16, 2006, Sunoco filed a protest (the "Protest") appealing the Authority's decision to this Office.

² As of the date of this determination, the Authority has not yet submitted a contract or contracts for Groups 5-9 for OSC approval.

Procedures and Comptroller's Authority

The Authority was established by Public Authorities Law Sections 350 et.seq. While that law does not give OSC general authority to approve Authority contracts, in 1950, the year that the Authority was created, its Board passed a Resolution requesting OSC to "audit the funds of the Authority in the same manner as funds of a regular State agency are audited." This resolution has consistently been interpreted and applied by both the Authority and OSC to include contract approval, and Appendix A of the proposed contract with Lehigh provides that the contract will not be effective unless and until it is approved by the Comptroller. (See Matter of Worth Construction Company, Inc. v. Hevesi et al. (___ A.D. 2d ___, 2006).

Applicable Statutes, Regulations and RFP Provisions

Section 354(10) of the Public Authorities Law gives the Authority the power "to construct, reconstruct or improve on or along the thruway system in the manner herein provided, suitable facilities for gas stations, restaurants, and other facilities for the public, or to lease the right to construct, reconstruct or improve and operate such facilities; such facilities shall be publicly offered for leasing for operation, or the right to construct, reconstruct or improve and operate such facilities shall be publicly offered under rules and regulations to be established by the authority . . ."

The Authority has promulgated the following regulation which is applicable to this procurement:

§ 106.1 Awarding of leases

Gas stations, restaurants and other facilities under the jurisdiction of the Thruway Authority shall be publicly offered for leasing prior to initial occupancy. Specific terms and conditions, including prerequisites and procedures for bidding, shall be set forth in a public proposal for each facility. When, in the judgment of the board of the Thruway Authority, it shall be in the best interests of the public, the Thruway Authority and its bondholders, several facilities may be offered for bidding as a unit. (21 NYCRR 160.1).

Article IV of the RFP for this procurement described the method by which proposals were to be evaluated by the Authority. Section 4.1 provides:

An Evaluation Committee comprised of Authority staff will review and evaluate each of the properly submitted written proposals. The purpose of the evaluation process, which will be conducted as set forth in this Article, is twofold: (1) to examine the responses for compliance with this RFP, and (2) to identify the proposals that will provide the best value to the Authority pursuant to the criteria set forth in Section 4.3. The evaluation process may also include, in the

Authority's sole discretion, reference checks, oral presentations, Facilities inspections and/or interviews with selected Proposers.

Section 4.3 of the RFP prescribed the evaluation criteria:

The Evaluation committee will evaluate each proposal using the criteria for selection set forth below, not necessarily in priority order:

- Economic Analysis
- Quality, Variety and Methodology of Services
- Maintenance
- Proposer Experience/Qualifications

Section 4.5 of the RFP, captioned "Selection of Proposer(s)", provided:

The Authority, as best suits its interests, may at any time enter into Contract negotiations with more than one Proposer. The Authority will notify those Proposer(s) so selected for Contract negotiations. The Authority shall not be bound in any way to a Proposer until a formal written Contract has been duly executed by the Authority and approved by the New York State Office of the State Comptroller.

Therefore, it is clear that this procurement necessarily entailed a "public offering" to determine which proposer would provide "best value" to the Authority. While the Authority reserved the right to negotiate a contract with more than one proposer, we do not believe that this provision would permit an award to a proposer other than the proposer providing best value, except where the Authority was unable to negotiate a contract with the best value proposer.

Protesting Party

The protestor, Sunoco, is one of the entities that submitted a proposal in response to the RFP.

ANALYSIS OF BID PROTEST

Basis of Sunoco Protest

The thrust of the Sunoco bid protest is the protestor's contention that the Authority acted arbitrarily and capriciously (i) by failing to notify Sunoco that May 4, 2006 was the deadline for concluding contract negotiations, and (ii) by undertaking contract negotiations with a proposer that did not offer the best value to the State.

There is no question that the Authority determined in the first instance that the Sunoco proposal offered the best value to the Authority.

It appears from a review of the procurement record that the parties' failure to come to an agreement on one specific contract provision was the primary basis upon which the Authority decided to break off contract negotiations with Sunoco (thereby triggering the award of the contract to Lehigh and the resulting Sunoco bid protest). The disagreement stemmed from the Authority's insistence on contract language in strict accordance with the following language of the RFP:

2. Term of Agreement – The Proposal must clearly identify the Contract term which shall be for a minimum of 10 (ten) years and shall not exceed 20 (twenty) years inclusive of any permitted renewals. Renewals will not be permitted if the contractor is in default at the time of renewal or if in the Authority's sole discretion the contractor has demonstrated a pattern of non-compliance to the contract. (Emphasis supplied).

The Authority's April 14, 2006 contract draft contained the following provision:

Section 2.03 Renewal Term(s) of This Agreement

(a) Subject to the approval of the Authority, the Operator may renew this Agreement for two (2) additional five (5) year terms, provided that:

(ii) The Operator is not in default of any of the terms and conditions of this Agreement from the date such notice [of the Operator's election to renew] is given through and including the date upon which such renewal is to take place, and, in the Authority's sole discretion, the Operator has not demonstrated a pattern of non-compliance with the provisions of this Agreement at any time during the initial, or previous, whichever is applicable, term of this Agreement. (Emphasis supplied).

Sunoco, in a revised draft of the Agreement which it submitted to the Authority on April 21, 2006, addressed this issue as follows:

Section 2.03 Renewal Term(s) of This Agreement

(a) Subject to the approval of the Authority, the Operator may renew this Agreement for two (2) additional five (5) year terms, provided that:

- (2) The Operator is not in default of any of the material terms and conditions of this Agreement from the date such notice is given through and including the date upon which such renewal is to take place, the Operator has not demonstrated a pattern of non-compliance with the material provisions of this Agreement at any time during the initial, or previous, whichever is applicable, term of this Agreement.”³ (Emphasis supplied).

Sunoco was concerned that the contract language, as originally proposed by the Authority, could be construed to grant the Authority the discretion to decline a renewal option for a “pattern of non-compliance” based upon trivial technicalities, which neither separately nor in the aggregate would rise to the level of a material breach of the Agreement. Thus, says Sunoco, the Authority’s language would have converted the renewal option into a provision permitting unilateral non-renewal without just cause. Sunoco’s proposal had committed the company to provide a capital investment of \$30,000,000 within the first four years of the contract term,⁴ and there would be insufficient time for Sunoco to recover these costs if the contract terminated at the end of ten years.

The Authority did not agree to the language of Sunoco’s April 21st draft on this point.

³ We believe it to be noteworthy that the Authority’s April 14, 2006 draft of the Agreement provided, in the section dealing with contract termination, that the Authority would have the right to terminate the Agreement in its entirety or as it applied to one or more fuel service facilities, (i) upon thirty (30) days written notice for any failure by the Operator to perform or comply with any non-monetary covenant, term condition or obligation under the Agreement, and (ii) on ten (10) days written notice for any failure by the Operator to perform or comply with any monetary covenant, term, condition or obligation. In its April 21, 2006 Agreement draft, Sunoco proposed that this clause be modified to provide that the Authority’s contract termination rights be limited, in each instance, to Sunoco’s failure to perform a material covenant, term or condition, for which Sunoco would be provided with notice and a reasonable opportunity to cure the failure. It appears from correspondence received from the Authority in the course of this Office’s review of the contract (i.e. a June 20, 2006 letter from the Authority’s Director of Purchasing) that the Authority may have been willing to accept this change in the termination section had contract negotiations with Sunoco gone forward. In any event, while the Authority has noted that this issue was outstanding at the time it decided to terminate negotiations with Sunoco, it has not emphasized this issue as a key factor in its decision. It is not apparent why the Authority would be unyielding in its position on the unacceptability of Sunoco’s “materiality” proposal with respect to contract renewal provisions, but would entertain accepting that concept in the context of contract termination. Indeed, if anything, it would be supposed that the reverse would be the case in that, unlike contract renewal terms, the termination provisions are effective throughout the entire contract term.

⁴ The capital improvements to be funded with this investment consisted primarily of (i) the addition of new services (including sixteen (16) new convenience stores; enlarged kiosks; new, state-of-the-art fuel dispensing equipment; and increased fueling capacity), (ii) the completion of all capital upgrade work required in the RFP, and (iii) \$7.2 million in environmental upgrades. Sunoco argues that in the event of a premature cessation of the contractual relationship for some reason other than Sunoco’s material default (such as a decision by the Authority to preclude Sunoco from exercising its renewal options) Sunoco would be placed in the unfavorable and unfair position of not being able to recoup its capital investment during the contract term.

A review of the procurement record demonstrates that Sunoco subsequently proposed a number of alternative business terms, reflected in revised contract language offered to the Authority, in an effort to reach an agreement with the Authority on the contract renewal terms. None of these alternatives proved to be acceptable to the Authority.

The Authority's Response to the Protest

The grounds articulated by the Authority in its June 7, 2006 Notice of Decision in support of its determination to proceed to contract negotiations with Lehigh, and unilaterally terminate contract negotiations with Sunoco, is that May 4, 2006 was, in the Authority's view, the drop dead date for conclusion of negotiations, and that fact had been communicated to Sunoco well in advance. It is the Authority's position that, in view of the critical need to continue uninterrupted and reliable fuel services for the public traveling on the Thruway, the Authority had to reach an agreement with a proposer on all essential contract terms by May 4th in order to obtain necessary Board approval on that date, and that it acted rationally in doing so by taking up contract negotiations with Lehigh.

One of the existing contracts for provision of fuel services (i.e., the contract for the thirteen stations making up Groups 1-4) was scheduled to expire on May 31, 2006 and, in light of the facts that (i) Board approval was necessary for execution of a new contract to take effect on June 1st, and (ii) May 4th was the only Board meeting scheduled prior to that date, the Authority believed that timing was critical in order to prevent interruption of the operation of the fuel service facilities.

To establish that it provided Sunoco with adequate notice of its position that May 4th was the crucial date by which contract negotiations had to be concluded, in its Notice of Decision the Authority relies on an April 14, 2006 e-mail from its counsel to Sunoco's counsel, which accompanied the Authority's initial draft of the Agreement. The e-mail is quoted below in its entirety:

Attached for your review is the draft Contract, along with Appendix A.

Other Exhibits are being prepared and will be sent to you shortly.

Please note that the attached draft is being reviewed by others here at the Authority and is subject to any comments I may receive.

In light of the upcoming Authority Board Meeting scheduled for May 4, 2006, it would be helpful to have your comments, and those of others at Sunoco, Inc. (R & M), by the middle of next week. (Emphasis supplied).

We look forward to hearing from you.

In addition, the Authority notes that, in the RFP, it had reserved the right to pursue simultaneous negotiations with more than one proposer. Section 4.5 of the RFP provided that “[t]he Authority, as best suits its interests, may at any time enter into Contract negotiations with more than one Proposer . . . The Authority shall not be bound in any way to a Proposer until a formal written contract has been duly executed by the Authority and approved by the New York State Office of the Comptroller.”

Since the RFP provisions had put all proposers on notice of the possibility that the Authority would be negotiating with more than one proposer at a time, and, according to the Authority, Sunoco knew or should have known that May 4th was the key date, the Authority contends that there was a rational basis for the manner in which the procurement was conducted in this respect, and that the Authority did not act arbitrarily or capriciously.

DISCUSSION

Legal Basis to Terminate Negotiations with Best Value Proposer

As noted previously, the Authority was required by Section 354(10) of the Public Authorities Law to award this contract through a public offering. This provision does not require that the contract be awarded solely on the basis of which proposal provides for the greatest revenue to the Authority. It does, however, in our view require that the Authority undertake a competitive process designed to determine either the proposer providing the greatest revenue to the Authority or the proposer providing the best value to the Authority, and to award the contract to the winning proposer in accordance with the process it adopted, subject only to being able to negotiate a contract with such proposer and the Authority finding such proposer to be responsible.⁵

Where an agency is required by statute to award a contract on a competitive basis (whether the basis is price or best value), it is our opinion that it cannot, consistent with such statutory requirement, terminate negotiations with the winning proposer lightly. Rather it can only do so where two criteria are met.

First, where the agency finds certain contractual terms proposed by the proposer unacceptable, it must clearly and unambiguously advise the proposer in writing: (i) that such terms are unacceptable, (ii) what terms will be acceptable, and (iii) that if the proposer is not willing to agree to the terms acceptable to the Authority by a specific date, which under the circumstances is reasonable, it will terminate negotiations and proceed to negotiate a contract with the next highest ranked proposer. Secondly, assuming that such notice is provided, it must be determined that the term or terms over

⁵ Even if Section 354(10) did not require such a competitive process, this Office would normally require such a process as a condition to our approval of the contract.

which the agency breaks off negotiations must reasonably justify the award of the contract to a proposer not determined to provide best value.

Adequacy of Notice

Prior to May 4th, Sunoco was clearly aware of the fact that the then current contract for at least some of the fuel service facilities was scheduled to expire on May 31st and that there was at least one significant open issue on which the parties had not reached agreement. It is also clear that Sunoco had been informed of the fact that there was a Board meeting scheduled for May 4th. However, it does not appear from a review of the procurement record that Sunoco was ever informed in advance that the May 4th date was, from the Authority's point of view, the deadline for execution of a contract setting forth all agreed-upon terms.

We find no evidence in the procurement record that the Authority ever clearly and unambiguously advised Sunoco in writing that May 4th was a drop dead date by which Sunoco would have to agree to the Authority's proposed terms. The Authority's April 14, 2006 e-mail, cited in the Authority's Notice of Decision, in no way provided such notice. Rather, it simply noted that in light of the upcoming Board meeting on May 4th, "it would be helpful to have your comments . . . by the middle of next week." [Emphasis supplied]. The Authority has, in its June 20, 2006 correspondence to this Office responding to questions posed by the OSC Bureau of Contracts regarding the procurement, indicated that the Authority advised Sunoco on April 28th that: it was important to have a contract in place by the end of May; that the contract would need to be approved by the Attorney General's Office and by the Office of the State Comptroller; that, as such, time was of the essence; and that an issue concerning automatic round-up of prices would be a deal breaker for which the Authority "asked for an answer [apparently on that issue] by the close of business that day." This communication, which was not referenced in the Authority's Notice of Decision or in any other prior communication, was, apparently, not in writing and was certainly not clear and unambiguous. The Authority's subsequent actions in continuing negotiations with Sunoco through May 4th (by which date Sunoco had agreed to drop the rounding-up issue), would indicate that the Authority did not regard any communication which occurred as imposing a drop dead date. Indeed, in response to an audit question from the OSC Bureau of Contracts asking whether Sunoco was ever advised of a drop-dead date, the Authority stated that it "elected not to formally cease negotiations with Sunoco until an agreement with the second proposer was in place."⁶

⁶ It is irrelevant whether, as the Authority has asserted, the Authority advised Sunoco early in negotiations that negotiations were not going well. What was required, in our view as outlined above, was that the Authority advise Sunoco in writing, not only that things were not going well, but also that the open issues needed to be resolved by a date certain.

In the absence of any clear and unambiguous notice to Sunoco that pending issues had to be resolved prior to a stated, reasonably necessary, date, we are not satisfied that the Authority could validly award to, and execute a contract with, the second ranked proposer, Lehigh.⁷ Therefore, we are upholding the protest on this basis.

Materiality of Sunoco's Proposed Addition to the RFP Provision on Contract Renewal Terms

As noted above, we have concluded that Sunoco's protest should be upheld based upon the failure to provide adequate notice to Sunoco. This will require that we return the proposed contract with Lehigh unapproved, with directions to resume negotiations with Sunoco. We recognize, however, that the Authority could then provide Sunoco with a drop dead date and, if Sunoco were not willing to concede on pending issues, it is likely that we would be required to consider a new protest from Sunoco, arguing that the open issues do not justify terminating negotiations with the best value proposer. Therefore, we believe it is appropriate that we provide some guidance with respect to our present views on this point.

As noted previously, Sunoco originally proposed the alternative of adding language in the contract renewal terms paragraph which would have conditioned Sunoco's right to renew on the company's not being in default of any of the "material" terms and conditions of the Agreement, and on the company not having demonstrated a pattern of non-compliance with the "material" provisions of the Agreement. Subsequently, Sunoco proposed at least two other alternatives, one of which would have provided for an original term of fifteen years, with a single five year renewal option for Sunoco, and which would have conditioned such option to renew on the company's not being in default of any of the terms and conditions of the Agreement, and on the company not having demonstrated a pattern of non-compliance with the provisions of the Agreement - without the addition of the word "material". Under these circumstances, and in light of the significant difference in the best value scores given by the Authority to Sunoco and Lehigh, we are not presently satisfied that the terms in dispute would reasonably have justified breaking off negotiations with the best value proposer, and awarding the contract to another proposer not determined to provide best value.

⁷ The Authority terminated contract negotiations with Sunoco in early May, not only with respect to the service facilities for which the then existing contract was scheduled to expire on May 31st, but also with respect to the facilities whose contract was not going to expire until September 30th. In response to a question posed by the OSC Bureau of Contracts as to the Authority's justification for terminating negotiations so far in advance of the current contract's September 30th expiration date, the Authority responded that "[b]ecause of Sunoco's position and proposed changes to the draft contract covering 29 sites, a conclusion was drawn that an agreement with Sunoco for any group could not be reached without deviating from the terms of the RFP or deviating significantly from Sunoco's original proposal." We are not persuaded, by this explanation, that the Authority had a reasonable basis for not continuing negotiations for the contract that would replace the one expiring on September 30th, since ample time remained for negotiating mutually acceptable terms.

It is of note that a provision of the contract which the Authority entered into with Lehigh differed from the contract that the Authority proposed to Sunoco, in that the Authority included the concept of materiality in the termination section of the Lehigh contract. Section 6.01(e) of the contract offered to Sunoco gave the Authority the right to terminate the contract “. . . (e) Upon ten (10) days written notice, if in the Authority’s judgment the sum of default notices issued under Section 6.01(a) or the number of occasions the Authority’s exercises its rights under Article 20 hereof reflects a pattern and practice of non-compliance by the Operator with this Agreement.”

The wording of Section 6.01(e) of the Lehigh contract is identical, except that the word “material” is inserted before the word “pattern”, thus indicating that, at least in this instance, the Authority recognized that the remedy of termination could not be invoked for trivial deficiencies in the contractor’s performance.⁸

We note that the record before us suggests that there were a number of other open issues between the Authority and Sunoco at the time contract negotiations were terminated. The record does not offer substantial detail regarding the significance of these issues. We are, therefore, unable to address at this time whether those issues, either individually or collectively, would warrant termination of contract negotiations. We note, however, that the communications between the Authority and Sunoco give no indication that any of these open issues were deal breakers – although the Authority has subsequently suggested in its July 31st letter to the Bureau of Contracts that such issues could cumulatively have warranted termination of negotiations.

Conclusion

Based on the foregoing, we are upholding Sunoco’s protest and returning the proposed Lehigh contract to the Authority unapproved. The Authority should resume negotiations with Sunoco in an attempt to reach agreement on final contract language, unless the Authority decides, in light of this Determination, that it is in the best interests of the Authority to rebid.

We note, however, that on August 14, 2006, the Authority received a protest from Consumers Petroleum of Ct. (“Consumers”) alleging that, due to various defects in the Authority’s handling of the procurement process, Consumers was effectively precluded from submitting a proposal for this procurement. This protest is still pending with the Authority, and any adverse determination would be subject to appeal to this Office. If,

⁸ We note that the Authority has suggested that it was legally precluded from agreeing to the language originally suggested by Sunoco - presumably on the theory that such a change would constitute a material change from the RFP and Sunoco’s proposal. We do not agree, and, in fact, it is not uncommon for this Office to approve contract language requested by a contractor, inserting a materiality or reasonableness standard with respect to certain rights reserved to the State, where such language had not expressly appeared in the RFP. Indeed, if the insertion of such language were, in fact, a material change, the insertion of the language with respect to termination rights in the Agreement with Lehigh, would have been legally prohibited.

based upon such protest by Consumers, it is determined that the procurement process was seriously flawed, the Authority would be required to conduct a new procurement.

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