Cite as: *Size Appeal of The Clement Group, LLC*, SBA No. SIZ-5146 (2010)

United States Small Business Administration
Office of Hearings and Appeals

SIZE APPEAL OF:	
The Clement Group, LLC	SBA No. SIZ-5146
Appellant	Decided: July 29, 2010
Appealed from Size Determination Nos. 3-2010-75, 3-2010-76, 3-2010-91, and 3-2010-92	

ORDER REMANDING PROCEEDINGS

I. Introduction and Jurisdiction

On June 24, 2010, the Small Business Administration's (SBA) Office of Government Contracting, Area III (Area Office) issued a Size Determination for case numbers 3-2010-75, 3-2010-76, 3-2010-91, and 3-2010-92 (Size Determination) finding that The Clement Group, LLC (Appellant), is other than a small concern under the $33.5 million size standard applicable to Solicitation Nos. W91278-10-R-0012 and W91278-10-R-0014 (RFPs), which were issued by the U.S. Army Corps of Engineers, Mobile District (Corps). On July 9, 2010, Appellant filed the instant appeal of the Size Determination. For the reasons discussed below, this matter is remanded to the Area Office for further consideration.

OHA decides size determination appeals under the Small Business Act of 1958, 15 U.S.C. § 631 *et seq.*, and 13 C.F.R. Parts 121 and 134. Appellant filed its appeal within fifteen days of receiving the Area Office's dismissal, so the appeal is timely. 13 C.F.R. § 134.304(a)(1). Accordingly, this matter is properly before OHA.

II. Issue

Did the Area Office commit a clear error of fact or law in determining that Appellant is affiliated with Clement Contracting Group, Inc. under the doctrine of negative control? 13 C.F.R. § 121.103(a)(3).

III. Background

A. Facts

I find the Record establishes the following facts by the preponderance of the evidence:

1. On December 7, 2009, the Corps issued RFP No. W91278-10-R-0012 (RFP 1) for an Indefinite Delivery/Indefinite Quantity Multiple Award Task Order Contract (IDIQ MATOC)

for construction within the Mobile District's North Region Construction Program. The Contracting Officer (CO) set-aside the procurement for small business concerns and designated North American Industrial Classification System (NAICS) code 236220, with a corresponding size standard of $33.5 million. Appellant submitted its offer under RFP 1 on January 20, 2010.

2. On December 10, 2009, the Corps issued RFP No. W91278-10-R-0014 (RFP 2) for an IDIQ MATOC for construction within the Mobile District's Gulf Coast Regional Construction Program. The CO set-aside the procurement for small business concerns and designated NAICS code 236220, with a corresponding size standard of $33.5 million. Appellant submitted its offer under the RFP 2 on February 2, 2010.

3. On March 25, 2010, the CO notified all RFP 1 offerors of her intent to make award to various offerors. Among those the CO identified as successful awardees was Appellant.

4. On March 31, 2010, McClain Contracting Company, Inc. (McClain), an unsuccessful offeror under RFP 1, protested Appellant's size to the CO. The CO forwarded McClain's protest to the Area Office in a letter dated April 5, 2010, which was received by the Area Office on April 12, 2010. McClain alleged that Appellant graduated from the SBA's 8(a) Business Development (BD) program in only two years, indicating that the firm exceeds the size standard applicable to RFP 1.

5. On April 1, 2010, Reams Enterprises Inc. (Reams), an unsuccessful offeror under RFP 1, also protested Appellant's size to the CO. The CO forwarded Reams's protest to the Area Office in a letter dated April 5, 2010, which was received by the Area Office on April 12, 2010. Based upon publicly available information, Reams alleged that Appellant's average annual receipts exceed the size standard applicable to RFP 1.

6. On April 15, 2010, the Area Office notified Appellant of both the McClain protest and the Reams protest filed with regard to RFP 1. The Area Office requested that Appellant provide the documentation necessary to perform an official size determination.

7. On March 31, 2010, the CO notified all RFP 2 offerors of her intent to make award to various offerors. Among those the CO identified as successful awardees was Appellant.

8. On April 6, 2010, McClain, also an unsuccessful offeror under RFP 2, protested Appellant's size to the CO. The CO forwarded McClain's protest to the Area Office in a letter dated April 21, 2010. McClain again alleged that because Appellant graduated from the SBA's 8(a) BD program in only two years, the firm must exceed the applicable size standard.

9. On April 7, 2010, Reams, also an unsuccessful offeror under RFP 2, protested Appellant's size to the CO. The CO forwarded Reams's protest to the Area Office in a letter dated April 21, 2010. Reams reiterated its contention that Appellant's average annual receipts exceed the applicable size standard.

10. On May 6, 2010, the Area Office notified Appellant of the size protests concerning RFP 2. The Area Office again requested that Appellant provide the documentation necessary to perform an official size determination.

11. On April 20, 2010, Appellant provided substantial information in response to the protests concerning RFP 1, including a completed SBA Form 355. Over the period from June 4, 2010, through June 22, 2010, Appellant provided further information and documentation in response to the protests concerning RFP 2 as well as additional requests from the Area Office. (As a practical matter, information submitted in response to both protests is responsive to either.)

12. Information provided by Appellant establishes:

a. Appellant is an Alabama limited liability company. Clement Contracting Group, Inc. (CCG) is an Alabama corporation.

b. Mr. Craig Clement is President of and has 70% ownership interest in Appellant.

c. Mr. Craig Clement owns 7.63% of CCG. Mr. Clement's wife, Mrs. Robyn Clement, owns 41.37% of CCG.

d. Ms. Monique Hicks is President of and has 51% ownership interest in CCG.

e. Mr. Craig Clement, Mrs. Robyn Clement, Ms. Monique Hicks, and Mr. Todd Hicks are the directors of CCG.

f. CCG's by-laws define a quorum of directors, the minimum number of directors necessary to conduct business, as a majority of directors.

B. The Size Determination

On June 24, 2010, the Area Office issued the Size Determination concluding Appellant is other than small. The Area Office found Appellant to be affiliated with Clement Management Group, LLC (CMG) and BCS Group, LLC (BCS) on the basis of common ownership and common management. 13 C.F.R. §121.103(c), (e). The Area Office also found Appellant to be affiliated with S.T.A.E. Here, LLC (STAE) based on familial identity of interest. 13 C.F.R. §121.103(f).

The Area Office next found Appellant to be affiliated with CCG pursuant to the doctrine of negative control. 13 C.F.R. §121.103(a)(3). The Area Office explained that Mr. Craig Clement, President and 70% owner of Appellant, owns 7.63% of CCG. Mr. Clement's wife, Mrs. Robyn Clement owns 41.37% of CCG, giving the Clements a 49% ownership interest in CCG. Ms. Monique Hicks, President of CCG, owns the remaining 51% of CCG. Mr. Clement, Mrs. Clement, Ms. Hicks, and Mr. Todd Hicks, Vice President of CCG, all serve as directors of CCG.

The Area Office set forth a provision from Appellant's by-laws indicating that a majority of directors constitutes a quorum for the purpose of transacting business at a meeting of the Board of Directors. Based on this provision, and the fact that Mr. and Mrs. Clement are both directors of CCG, the Area Office reasoned that the Clements have the ability to prevent a quorum of directors at a Board meeting and thereby prevent the transacting of the firm's business. Thus, the Area Office concluded that the Clements hold the power of negative control over CCG.

The Area Office also determined that Appellant and CCG continue to conduct business together, further evincing affiliation between the firms. Specifically, the Area Office found that Appellant and CCG are in the same line of business (construction), CCG sold property to Appellant for a nominal sum, and CCG rents office space from Appellant for a nominal sum in the same building where Appellant conducts its operations.

Finally, the Area Office calculated the combined average annual receipts of Appellant and its affiliates and concluded that the receipts exceed the $33.5 million size standard applicable to the procurements at issue. Thus, the Area Office determined Appellant is other than a small business concern for the size standard.

C. The Appeal Petition

On July 9, 2010, Appellant filed the instant size appeal with OHA claiming that the Size Determination is based upon clear errors of fact and law. Appellant does not challenge the Area Office's findings that it is affiliated with CMG, BCS, and STAE. Appellant only challenges the Area Office's finding that it is affiliated with CCG based upon its conclusion that Mr. and Mrs. Clement have the power of negative control over CCG.

Appellant claims that Mr. and Mrs. Clement do not have the power of negative control over CCG, despite the fact that they are two of the four directors of CCG, and a majority of directors is required to conduct business. Appellant argues "the ability to control must be actual ability, not merely illusory ability." (Appeal Petition 3.) Appellant then attempts to demonstrate that Mr. and Mrs. Clement's ability to control CCG is illusory.

Appellant asserts that the Area Office erroneously failed to consider Alabama corporate law in its analysis of the negative control issue. Under Alabama law, Appellant explains, the shareholders of a firm may remove directors with or without cause unless the firm's articles of incorporation provide that directors may only be removed for cause. Ala. Code § 10-2B-8.08(a). The CCG Articles of Incorporation include no such provision. Thus, pursuant to Alabama law and the CCG by-laws, Appellant contends that Ms. Hicks, as President and majority shareholder, could remove Mr. and Mrs. Clement as directors of CCG as follows:

1. As President of CCG, Monique Hicks could call a special meeting of the shareholder of CCG upon 10 days written notice. *CCG by-laws* §§ 3.03 and 3.05. As required by Alabama law, the notice must state that at least one of the purposes of the meeting is the removal of Craig and Robyn Clement as directors of CCG.
2. At a shareholders' meeting, a quorum consists of a bare majority of the outstanding shares. *CCG by-laws* § 3.07(a). And, each share of stock is entitled to one vote. *CCG by-laws* § 3.9.
3. Solely by virtue of her ownership of 51% of the outstanding shares, Monique Hicks can control the vote and successfully remove Craig and Robyn Clement as directors

(Appeal Petition 3-4.) Appellant concludes that should the Clements ever attempt to assert control over CCG, Ms. Hicks has the sole and complete power to prevent such an attempt. Thus, Ms. Hicks has actual control over CCG.

Appellant also disputes the Area Office's finding that it and CCG conduct business together. Appellant claims the sale of the building from CCG to Appellant was not for a nominal sum. Rather, "[a]s is common in real estate transactions, the deed itself refers to consideration of $100 (so that the deed, once recorded, does not reveal the actual purchase price)." (Appeal Petition 4.) Appellant attaches a settlement statement showing the true amount of the sale. With regard to the office space CCG leases from Appellant, Appellant asserts it does not conduct any business out of that building, but uses it only for storage. According to Appellant, it is only CCG that operates out of that location. Moreover, Appellant argues the Area Office had no basis for determining that the rent paid for that space is nominal.

Appellant concludes that the Clements do not have negative control over CCG because Ms. Hicks has actual control over CCG under Alabama law and CCG's by-laws. Thus, Appellant asserts there is no affiliation between the firms and, excluding CCG's receipts from the calculation, Appellant's average annual receipts (including those of Appellant's other affiliates) are within the applicable size standard.[1] Appellant requests that OHA reverse the Size Determination.

IV. Analysis

A. Standard of Review

OHA reviews a size determination issued by an SBA area office to determine whether it is "based on clear error of fact or law." 13 C.F.R. § 134.314. In evaluating whether there is a clear error of fact or law, OHA does not consider Appellant's size *de novo*. Rather, OHA reviews the record to determine whether the Area Office made a patent error based on the record before it. It is Appellant's burden to prove that the Area Office committed an error. *Id.* Consequently, I will disturb the Area Office's Size Determination only if I have a definite and firm conviction the Area Office made key findings of law or fact that are mistaken. *Size Appeal of Taylor Consultants, Inc.*, SBA No. SIZ-4775, at 10-11 (2006).

B. The Merits

The SBA's size regulations provide that concerns are affiliated if one has the power to control the other. 13 C.F.R. §121.103(a)(1). The regulations further provide that "[c]ontrol may be affirmative or negative. Negative control includes, but is not limited to, instances where a minority shareholder has the ability, under the concern's charter, by-laws, or shareholder's agreement, to prevent a quorum or otherwise block action by the board of directors or shareholders." 13 C.F.R. §121.103(a)(3).

The Area Office concluded that Mr. and Mrs. Clement have the power of negative control over CCG because they could prevent a quorum, one of the situations specifically identified in the regulation as constituting negative control. A quorum of directors is necessary to conduct business,

[1] Appellant asserts: "There is no dispute that without a finding of affiliation between [Appellant] and CCG, [Appellant] is 'small' under NAICS code 236220 because without CCG's revenues added, [Appellant's] three-year average revenue is less than $33.5 million." (Appeal Petition 1.) The Area Office's calculations included in the Record do reflect that if CCG's receipts are deducted from Appellant's receipts, Appellant's average annual receipts would fall within the size standard.

and the CCG by-laws provide that a majority of directors comprises a quorum. Thus, the Area Office concluded that because the Clements make up one half the Board of Directors (two of four directors), they could prevent a quorum by failing to appear at a meeting, thereby preventing the firm from conducting business. Upon a reading of only CCG's by-laws, the Area Office's conclusion is understandable. However, as Appellant now points out, the operation of Alabama law under the facts and circumstances of this case renders the Area Office's conclusion legally erroneous.

Ala. Code § 10-2B-8.08(a), which applies to Alabama business corporations such as CCG, provides: "The shareholders may remove one or more directors with or without cause unless the articles of incorporation provide that directors may be removed only for cause." A review of CCG's Articles of Incorporation reveals no such provision. Thus, Appellant is correct in its conclusion that Ms. Hicks, as President and 51% shareholder, has the power to remove Mr. and Mrs. Clement should they ever attempt to control CCG by preventing a quorum. She need only call a shareholder meeting for that purpose and vote to remove the Clements. Because she is the majority shareholder of CCG, her votes would control the outcome.

I am in agreement with Appellant that negative control over a firm for the purposes of finding affiliation must include the ability to actually control the firm, not merely the illusion of control. *Cf. Size Appeal of EA Eng'g, Sci. and Tech., Inc.*, SBA No. SIZ-4973 (2008) (finding supermajority voting requirements were designed merely to protect stockholder investments and declining to find negative control under 13 C.F.R. §121.103(a)(3) because although those supermajority requirements conferred some power to negatively control certain actions of the firm, that power could not affect the firm's ability to manage and operate its business). Given that Ms. Hicks could unilaterally remove the Clements as directors of CCG, it is clear that any power the Clements may have over CCG could not affect its ability to manage and operate its business. The effect of the Alabama provision is thus to remove the illusion that the Clements could control CCG and to clarify that Ms. Hicks has the complete power to actually control CCG. Although it would have been prudent for Appellant to bring this provision to the Area Office's attention, the effect of the provision is that the Size Determination contains a clear error of law that I cannot ignore.

Accordingly, I find the Clements do not have negative control over CCG, and I must reverse that portion of the Size Determination concluding Appellant is affiliated with CCG under the doctrine of negative control. Nevertheless, my ruling does not fully resolve the question of affiliation between Appellant and CCG. As discussed above, the Size Determination also includes other indicia of affiliation between Appellant and CCG. However, because the Area Office relied upon its determination of negative control to find affiliation between Appellant and CCG, it is unclear from the Size Determination whether this other evidence was sufficient for the Area Office to find affiliation between the two concerns in the absence of negative control.

Therefore, I must remand the matter to the Area Office to fully investigate the relationship between Appellant and CCG to determine whether the other evidence of affiliation between the firms is strong enough to constitute a finding of affiliation on other grounds. If the Area Office concludes Appellant is not affiliated with CCG, it must recalculate Appellant's size, deducting CCG's receipts from its calculation of Appellant's average annual receipts.

V. Conclusion

For the above reasons, I REVERSE the finding that Appellant is affiliated with CCG based upon negative control, and I REMAND this matter to the Area Office for further consideration consistent with this Order.

THOMAS B. PENDER
Administrative Judge