United States Small Business Administration
Office of Hearings and Appeals

SIZE APPEAL OF: Nuclear Fuel Services, Inc., Appellant, Appealed From Size Determination No. 3-2011-114	SBA No. SIZ-5324 Decided: February 2, 2012

APPEARANCES

Stephen D. Harvey, Esq., Babcock & Wilcox Technical Services Group, Lynchburg Virginia, for Appellant

Scott Langston, Contracting Officer, U.S. Department of Energy, Aiken, South Carolina

DECISION

I. Introduction and Jurisdiction

On November 9, 2011, the U.S. Small Business Administration (SBA) Office of Government Contracting, Area III (Area Office) issued Size Determination No. 3-2011-114 finding Nuclear Fuel Services, Inc. (Appellant) other than small. On November 21, 2011, Appellant appealed the size determination, claiming it contains clear errors. For the reasons discussed *infra*, the appeal is granted, and the size determination is reversed.

SBA's Office of Hearings and Appeals (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 the instant appeal within fifteen days of receiving the size determination, so the appeal is timely. 13 C.F.R. § 134.304(a). Accordingly, this matter is properly before OHA for decision.

II. Background

A. The Prime Contract and Protest

Appellant is a subcontractor to Savannah River Nuclear Solutions, LLC (SRNS) on Contract No. DE-AC09-08SR22470 (prime contract) with the U.S. Department of Energy. Under the prime contract, SRNS performs Management and Operating (M&O) services at the Savannah River Site (SRS), in Aiken, South Carolina. *See generally* Federal Acquisition Regulation (FAR) Subpart 17.6. In January 2009, while performance on the prime contract was underway,

Appellant was acquired by Babcock & Wilcox Co. (B&W).[1] At issue in this appeal is whether the acquisition should be given effect as of July 15, 2008, the date that Appellant self-certified as a small business for Master Task Agreement No. C002341N (MTA), a subcontracting instrument between SRNS and Appellant.

Request for Proposal 071408 (RFP), which led to formation of the MTA, was issued by SRNS on July 12, 2008. Section I-9 of the RFP indicated that the procurement was set-aside exclusively for small businesses, and that "[p]roposals received from concerns that are not small business concerns will not be considered." Section I-8 of the RFP identified the applicable North American Industry Classification System (NAICS) code as 541990, All Other Professional, Scientific, and Technical Services, with a corresponding size standard of $6.5 million average annual receipts. The RFP stated, however, that:

> If [Appellant] asserts that NAICS code 325188, [All Other Basic Inorganic Chemical Manufacturing,] having a small business size standard of 1000 employees is applicable to the services that are detailed in the statement of work, a justification of this assertion must be submitted with this proposal.

(RFP at 4.)

On July 15, 2008, Appellant submitted to SRNS a partial response to the RFP, including its representations and certifications. There, Appellant stated: "[Appellant] is a small business under its primary NAICS code of 325188. [Appellant] is NOT a small business under NAICS code 541990." On July 17, 2008, Appellant submitted its price proposal to SRNS. With regard to the justification requested by Section I-8 of the RFP, Appellant stated:

> [Appellant] was included as a designated and integrated subcontractor on the SRNS team because of [Appellant's] extensive nuclear materials processing experience, much of which is similar to work conducted at SRS. Also, [Appellant] was included in the SRNS team because it was a Small Business (SB). Nuclear materials processing and the manufacture/fabrication of nuclear fuel fall under NAICS code 325188 ....[Appellant] qualifies as a NAICS 325188 small business.
>
> [Appellant] believes that the NAICS code noted above is appropriate for the primary work
>
> [Appellant] expects to be involved in at SRS which is the processing of nuclear materials.

SRNS awarded the MTA to Appellant, effective August 1, 2008. The specific services that Appellant would perform are described in individual task orders. However, the MTA generally summarizes the scope of work as follows:

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[1] For purposes of this appeal, Appellant concedes that B&W is not a small business. (Appeal at 6, n.5.)

> [Appellant] shall provide management support services or functions in the areas of nuclear materials management, nuclear materials processing and nuclear non-proliferation .... [Appellant] shall provide personnel and engineering or consulting services in the primary areas of nuclear materials management, nuclear materials processing and nuclear non-proliferation.

(MTA, Attachment B, ¶ 1.0.) The MTA further explains that:

> [Appellant] is a pre-selected first tier subcontractor for [SRNS], bringing its core competencies in the areas of chemical processing, nuclear operations, nuclear materials management & disposition and safeguards & security to support SRNS missions. [Appellant] qualifies as a small business under NAICS code 325188.

(*Id.*, ¶ 5.1.)

Following establishment of the MTA, SRNS issued, and Appellant has performed, numerous task orders under the MTA. SRNS did not assign NAICS codes to individual orders.

On August 9, 2011, SRNS requested that the Contracting Officer (CO) obtain a size determination on Appellant, explaining that Appellant's size is relevant to the issue of whether certain fees could be recovered as allowable costs under the prime contract. SRNS noted that Appellant was acquired in January 2009 by B&W, and that Appellant thereafter indicated that it was no longer a small business under NAICS code 325188.

On August 25, 2011, the CO requested that the Area Office review Appellant's size. The CO stated that "[t]he size determination, as issued by [the Area Office], will be used as an Alternative Dispute Resolution (ADR) procedure for resolving a contractual disagreement" between the agency and the prime contractor, SRNS. As attachments to the protest, the CO forwarded SRNS's August 9 letter, and Appellant's Online Representations and Certifications Application (ORCA) showing that Appellant currently does not represent itself as a small business under NAICS code 325188.

On September 6, 2011, the Area Office notified Appellant that its size had been questioned, and directed Appellant to submit additional information. The Area Office identified the applicable NAICS code as 325188, and explained that "[t]he basis for protest is that in order to qualify as a small business concern [Appellant] must be a small business and not exceed the 1000 employees [standard] for the above mentioned NAICS code."

C. Size Determination

On November 9, 2011, the Area Office issued its size determination concluding that Appellant is not a small business. The Area Office examined two issues: (1) which NAICS code applied to the MTA; and (2) whether Appellant was affiliated with B&W as of July 15, 2008, the date Appellant self-certified as a small business for the MTA.

With regard to the NAICS code issue, the Area Office noted that, according to 13 C.F.R. § 121.410, the applicable code is that which the prime contractor believes best describes the product or service being acquired by the subcontract. The Area Office noted that the prime contractor, SRNS, assigned NAICS code 541990 to the RFP which led to the MTA. The Area Office also recognized that the RFP invited Appellant to address whether NAICS code 325188 should instead be used; however, the Area Office stated that it was unable to locate any response from Appellant on this issue. (Size Determination at 3.) The Area Office then explained it conducted its own review of the MTA and the task orders issued to Appellant and found that the work primarily entailed scientific, professional, and technical services. The Area Office concluded that NAICS code 541990 would best characterize such work. In Appellant's July 15, 2008 self-certification, Appellant stated that it did not qualify as a small business under NAICS code 541990. The Area Office therefore reasoned that Appellant was not a small business as of July 15, 2008. (*Id.* at 8.)

The Area Office also examined whether Appellant was affiliated with B&W as of July 15, 2008. The Area Office found that Appellant formally agreed to be acquired by B&W on August 8, 2008 — approximately three weeks after the date of self-certification — when the parties executed a stock purchase agreement. The Area Office found, however, that Appellant and B&W had been engaged in discussions regarding potential acquisition for several months prior to July 15, 2008. Appellant invited proposals from potential buyers on September 17, 2007. B&W initially proposed to purchase Appellant by letter of October 5, 2007, and subsequently provided more detail about its proposal by letter of December 19, 2007. The Area Office found that the December 19, 2007 letter in particular showed "an evident meeting of the minds between the buyer and seller" and "support[s] a finding that [the parties] were close to finalizing the transaction." (*Id.*) The Area Office also observed that Appellant and B&W conducted numerous meetings, telephone conversations, and emails to discuss the acquisition prior to July 15, 2008. The Area Office concluded that Appellant and B&W had reached an agreement in principle to merge as of July 15, 2008. Under SBA's "present effect" rule, 13 C.F.R. § 121.103(d), SBA will treat agreements to merge or acquire (including agreements in principle) as having a present effect on the power to control a concern. The Area Office concluded that Appellant was affiliated with B&W as of July 15, 2008, because there was by that time an agreement in principle that B&W would acquire Appellant. Due to affiliation with B&W, Appellant does not qualify as a small business under either NAICS code 541990 or 325188. (*Id.* at 7.)

D. Appeal Petition

On November 21, 2011, Appellant filed the instant appeal.[2] Appellant asserts that the size

[2] With its appeal, Appellant moves to supplement the record with two new exhibits. The first exhibit is a two-page description of the work at SRS, taken from SRNS's website. The second exhibit is a copy of Appellant's July 17, 2008 justification for the use of NAICS code 325188, which the Area Office purportedly was unable to locate. Generally, new evidence is not admissible before OHA unless the party seeking to admit the evidence files a motion and establishes good cause for the admission. 13 C.F.R. § 134.308(a)(2). Here, the description of work at SRS is very brief and does not enlarge the issues on appeal. Appellant's justification for the use of NAICS code 325188 is already included in the Area Office file as part of Appellant's [*cont.*]

determination contains clear errors of fact and law.

Appellant first contends the Area Office applied the wrong NAICS code and size standard, and did so without notice to Appellant. Therefore, Appellant had no opportunity to provide evidence showing that the correct NAICS code for the MTA is 325188. Appellant argues that under 13 C.F.R. § 121.410, the prime contractor — not the Area Office — selects the NAICS code for subcontracts related to Government procurements. Appellant points out that SRNS's protest cited NAICS code 325188 as the applicable NAICS code. Further, Appellant contends its July 15, 2008 self-certification was only part of its response to the RFP, and that on July 17, 2008, Appellant submitted the justification for NAICS code 325188 as instructed by Section I-8 of the RFP.

Appellant also maintains the Area Office incorrectly invoked the present effect rule to conclude that Appellant was affiliated with B&W as of the July 15, 2008, self-certification date. Appellant contends that on July 15, 2008, the companies were still engaged in negotiations and conducting due diligence, but no agreement had yet been reached. In support of its contention that there was no agreement, Appellant discusses B&W's December 19, 2007, letter outlining conditions under which the acquisition could move forward, and quotes the Area Office's summary of that letter. Appellant cites *Size Appeal of Kadix Systems, LLC*, SBA No. SIZ-5016 (2008), to argue that because business transactions such as the one at issue here are long and complicated, and are not finalized until after lengthy negotiation over many points, the Area Office erred in applying the present effect rule in the absence of agreement.

Appellant requests that OHA reverse the size determination and conclude Appellant was an eligible small business as of the July 15, 2008 self-certification.

D. Contracting Officer's Response

On December 7, 2011, the CO filed his response to the appeal petition. The CO urges OHA to summarily dismiss the appeal. The CO states that the MTA is similar to a Blanket Purchase Agreement (BPA) and that the appropriate time to measure Appellant's size is when a task order is awarded, rather than upon award of the BPA (or the MTA). The CO further contends that Appellant has no standing to pursue this appeal because Appellant is not "adversely affected" by the size determination. The CO maintains that, regardless of the outcome of this appeal, Appellant will still receive its full fee from SRNS; the only difference is that SRNS may be unable to recover the fee as an incurred cost.

E. Appellant's Reply

On December 7, 2011, Appellant filed a Motion for Leave to Reply to New Issues Raised in the CO's Response. Appellant disputes the CO's characterization of the MTA as essentially

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proposal, and therefore does not constitute "new evidence." Accordingly, I find that Appellant has established good cause for admission of these documents. *See generally Size Appeal of Nat'l Sourcing, Inc.*, SBA No. SIZ-5305, at 8-9 (2011). Appellant's motion is thus GRANTED, and the evidence submitted with the appeal petition is ADMITTED to the record.

similar to a BPA, and argues that SRNS has not requested a new size certification with each task order. Appellant also challenges the CO's statement that Appellant is not adversely affected by the size determination. Appellant states that SRNS has advised Appellant that the MTA will be terminated if the size determination is not reversed on appeal, and attaches a letter to that effect from SRNS.

III. Discussion

A. Standard of Review

Appellant has the burden of proving, by a preponderance of the evidence, all elements of its appeal. Specifically, Appellant must prove the size determination is based upon a clear error of fact or law. 13 C.F.R. § 134.314. OHA will disturb the Area Office's size determination only if, after reviewing the record, the administrative judge has a definite and firm conviction that the Area Office erred in making its key findings of fact or law. *Size Appeal of Taylor Consultants, Inc.*, SBA No. SIZ-4775, at 11 (2006).

B. Analysis

1. Standing to Appeal

OHA has, in some instances, found that a subcontractor lacks standing to bring an appeal because the subcontractor has no direct stake in the outcome of the case. *E.g., Size Appeal of Control Systems Research, Inc.*, SBA No. SIZ-5012 (2008). Such cases, however, have involved situations where another concern — such as the prime contractor — is the challenged firm. In the instant case, Appellant itself is the challenged firm. Because Appellant's size is at issue in these proceedings, Appellant has a direct interest in the outcome of the litigation. Furthermore, Appellant has established that SRNS intends to terminate its subcontract unless the size determination is reversed. Accordingly, Appellant is adversely affected by the size determination, and has standing to pursue this appeal. 13 C.F.R. § 134.302(a).

2. NAICS Code and Size Standard

Appellant first complains that the Area Office erred in assessing Appellant's size under NAICS code 541990, with a size standard of $6.5 million. Rather, according to Appellant, the Area Office should have determined whether Appellant qualifies as a small business under NAICS code 325188, with a size standard of 1000 employees.

In explaining its decision to use NAICS code 541990, the Area Office acknowledged that Appellant's primary NAICS code is 325188, and that the underlying size protest had questioned Appellant's size under NAICS code 325188. The Area Office observed, however, that under SBA regulations, a concern is small for subcontracts which relate to Government procurements if the subcontractor "does not exceed the size standard for the NAICS code that the prime contractor believes best describes the product or service being acquired by subcontract." 13 C.F.R. § 121.410. The Area Office therefore reasoned that the applicable NAICS code "is not the subcontractor's primary NAICS code, but the NAICS code that the prime contractor believed

best described the product or service to be acquired by this procurement." (Size Determination at 2.) The Area Office found that the prime contractor, SRNS, assigned NAICS code 541990 to the RFP which eventually led to the MTA. The Area Office also conducted its own review of task orders issued under the MTA and determined that the work was better characterized by NAICS code 541990 than 325188.

Appellant counters that the Area Office never asked either SRNS or Appellant to address which NAICS code best described the work under the MTA. Appellant argues that although SRNS initially did assign NAICS code 541990 to the RFP, SRNS simultaneously invited Appellant to explain whether NAICS code 325188 should instead apply. Specifically, the RFP instructed that "[i]f [Appellant] asserts that NAICS code 325188, having a small business size standard of 1000 employees is applicable to the services that are detailed in the statement of work, a justification of this assertion must be submitted with [Appellant's] proposal." Appellant states that it provided the requested justification in its proposal, and self-certified that it was a small business under NAICS code 325188 and not a small business under NAICS code 541990. SRNS awarded the MTA to Appellant, and noted in the MTA itself that "[Appellant] qualifies as a small business under NAICS code 325188." (MTA, Statement of Work at 1.) Appellant also attaches significance to the fact that SRNS's size protest questioned Appellant's size under NAICS code 325188. Appellant argues that the protest is strong evidence that "the prime contractor here had determined that NAICS code 325188 best describes the services [Appellant] is providing." (Appeal at 2.) Finally, Appellant asserts that it had no notice that the Area Office was considering NAICS 541990, and therefore was denied meaningful opportunity to be heard on that issue.

I agree with Appellant. Under 13 C.F.R. § 121.410, the appropriate NAICS code is that which prime contractor believes best describes the products or services being acquired. Accordingly, the Area Office's opinion of which NAICS code is most suitable for the subcontract can be given little weight, particularly since the Area Office apparently reached its conclusion without even consulting the prime contractor. In addition, the record reflects that SRNS invited Appellant to explain why NAICS code 325188 should apply to the MTA, that Appellant did provide the requested explanation, and that SRNS proceeded to award the MTA to Appellant. It thus appears that SRNS accepted the justification offered by Appellant that NAICS code 325188 was the appropriate code.[3] The protest filed by SRNS questioned whether Appellant exceeded the size standard under NAICS code 325188, again suggesting that SRNS viewed 325188 as the applicable code.

The record demonstrates that SRNS considered NAICS code 325188 best described the products or services being acquired. Accordingly, the Area Office erred in assessing Appellant's size under NAICS code 541990.

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[3] As noted in the size determination, SRNS restricted the RFP to small businesses, and Appellant certified that it was a small business only under NAICS code 325188, not 541990. (Size Determination at 3-4.) Logically, then, SRNS could not have awarded the MTA to Appellant at all, unless SRNS had accepted Appellant's justification that the appropriate NAICS code was 325188.

3. Present Effect Rule

Appellant also asserts that the Area Office erred in applying the present effect rule to conclude Appellant was affiliated with B&W as of Appellant's July 15, 2008, self-certification on the MTA. Appellant points out that it did not enter into a formal Sales and Purchase Agreement with B&W until August 8, 2008, some three weeks after Appellant self-certified for the MTA.

The present effect rule provides that agreements for a merger or acquisition, including agreements in principle, have "present effect" on the power to control a concern. 13 C.F.R. § 121.103(d)(1). Stated differently, for size purposes, a merger or acquisition is effective as of the date of that an "agreement in principle" is reached, even though the merger or acquisition itself is not yet consummated. The regulation cautions, however, that "[a]greements to open or continue negotiations towards the possibility of a merger or a sale of stock at some later date are not considered 'agreements in principle' and are thus not given present effect." 13 C.F.R. § 121.103(d)(2).

In interpreting this regulation, OHA has held that it is improper to assume that, merely because a deal is complex or time-consuming, an agreement in principle must have been reached at an earlier point in the process. OHA has explained:

> The mere fact that an agreement is lengthy and complicated does not necessarily mean that there was any agreement reached prior to its execution. Many business transactions are finalized only after long negotiation over many points. While the parties may both seek an agreement, one is not final until the final contract is signed. Often, major business deals fall apart at the last minute, despite long negotiation and extensive drafting of lengthy documents .... [T]o find that an agreement in principle must have existed simply because the final document is lengthy and complex is without foundation, and a clear error.

Size Appeal of Kadix Systems, LLC, SBA No. SIZ-5016, at 6 (2008). Accordingly, OHA has affirmed the use of the present effect rule in situations where there is tangible evidence that an agreement in principle had been reached. *Size Appeal of WRS Infrastructure and Environment, Inc.*, SBA No. SIZ-5007, at 9-10 (2008) (letter of intent constituted an agreement in principle); *Size Appeal of Syro Steel Co.*, SBA No. SIZ-3800, at 10 (1993) ("[t]he 'Agreement and Plan of Merger' is, to our mind, an 'agreement in principle"'); *Size Appeal of Underwood Industries, Inc.*, SBA No. SIZ-3053 (1989) (written acquisition agreement was properly given present effect). Conversely, OHA has declined to apply the present effect rule absent specific evidence of an agreement in principle. *Size Appeal of PCCI, Inc.*, SBA No. SIZ-4531 (2003) (no agreement in principle where parties merely committed to negotiate exclusively with one another); *Size Appeal of Technology Systems Associates, Inc.*, SBA No. SIZ-3963, at 9 (1994) ("While there may have been discussions and negotiations between the parties regarding future actions to be taken, including negotiations concerning [the] proposed acquisition of Appellant, there is nothing in the record to indicate that any formal document to acquire Appellant was in existence prior to Appellant's self certification or that even a meeting of the minds had occurred.").

In this case, the Area Office concluded that an agreement in principle had been reached before the date of Appellant's self-certification. The Area Office relied in particular upon B&W's December 19, 2007 letter, which the Area Office found to represent "an evident meeting of the minds between the buyer and seller." (Size Determination at 8.) B&W's letter, however, was merely a tentative proposal to acquire Appellant. There is no indication that Appellant accepted B&W's proposal; thus, the letter cannot be considered a bilateral "agreement" between the parties. *Size Appeal of GeoSyntec Consultants*, SBA No. SIZ-4277, at 5 (1997) (offer to acquire another firm, which was initially rejected by the target company, did not establish agreement in principle). Furthermore, B&W's letter repeatedly stated that its proposal was non-binding and subject to numerous conditions, including thorough review of Appellant's business operations. Thus, the December 19, 2007 letter was not in the nature of a definitive offer that Appellant could have chosen to accept. Indeed, the very fact that negotiations between Appellant and B&W continued for another eight months after the December 19, 2007 letter suggests that the parties had not in fact reached agreement as of December 19, 2007.

The Area Office also attached significance to the fact that the December 19, 2007 letter included some discussion of potential terms of the acquisition, especially price. As Appellant emphasizes, however, it would not have been possible for Appellant to entertain B&W's offer without any mention of approximate price. (Appeal at 10.) Thus, inclusion of a proposed price does not establish that the parties had reached any agreement in principle, but rather marks the onset of more serious negotiations.

The Area Office also observed that Appellant and B&W conducted numerous meetings and teleconferences, and exchanged various draft documents, leading up to their August 8, 2008 stock purchase agreement. These communications establish that the parties were actively negotiating a potential acquisition, but the Area Office cited no specific evidence that an agreement in principle was reached. It is well-settled that "[m]ere negotiations do not constitute an agreement in principle." *Technology Systems Associates*, SBA No. SIZ-3963, at 9.

IV. Conclusion

Appellant has demonstrated that the Area Office's size determination is clearly erroneous. The Area Office incorrectly assessed Appellant's size under NAICS code 541990, rather than NAICS code 325188, the code designated by the prime contractor. Further, there is no evidence that Appellant and B&W had reached an agreement in principle regarding their merger as of the date of Appellant's self-certification. As a result, Appellant was not affiliated with B&W as of that date. I therefore GRANT this appeal and REVERSE the size determination. This is the final decision of the Small Business Administration. 13 C.F.R. § 134.316(d).

KENNETH M. HYDE
Administrative Judge