B-254909

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Comptroller General
of the United States
Washington, D.C. 20548

Decision

Matter of: McNeil Technologies, Inc.

File: B-254909

Date: January 25, 1994

James L. McNeil for the protester.
Mike Colvin, Department of Health and Human Services, and David R. Kohler, Esq., Small Business Administration, for the agencies.
Aldo A. Benejam, Esq., and Christine S. Melody, Esq., Office of the General Counsel, GAO, participated in the preparation of the decision.

DIGEST

1. Small business protester is an "interested party" to challenge Small Business Administration's (SBA) determination that acceptance of follow-on requirement into section 8(a) program would have no adverse impact on protester where (1) protester acquired incumbent's entire business during contract performance; (2) incumbent's contract thus transferred to protester by operation of law; (3) protester specifically challenges SBA's determination that acceptance of the follow-on requirement for 8(a) award would not adversely impact protester; and (4) protester would be eligible to compete for the follow-on requirement if SBA determines that acceptance of the requirement into the 8(a) program was inappropriate.

2. While the transfer of government contracts and claims is generally prohibited, such transfers are exempted from the anti-assignment statutes where they occur "by operation of law."

3. Although under the regulations applicable to procurements proposed for 8(a) award the Small Business Administration (SBA) presumes adverse impact to exist when a small business concern meets certain enumerated criteria, the regulations require SBA to determine whether acceptance of the procurement for 8(a) award nevertheless would have an adverse impact on other small business programs or on an individual small business, even if the factors that create a presumption of adverse impact are not present.

DECISION

McNeil Technologies, Inc., a small business, protests the determination by the Small Business Administration (SBA) to accept into the 8(a) program a follow-on requirement to provide management supportive services for the Department of Health and Human Services' (HHS) State Legalization Impact Assistance Grant program.[1] The protester argues that SBA unreasonably determined that the 8(a) award would have no adverse impact on McNeil.

We sustain the protest.

BACKGROUND

On June 30, 1990, following competition restricted to small business concerns, HHS awarded to Skyline Government Services Corporation a cost-plus-fixed-fee contract to provide the services at issue here.[2] McNeil purchased Skyline effective January 1, 1993. Skyline's contract expired September 29, 1993. Prior to the expiration of Skyline's contract, HHS offered the requirement to SBA under the 8(a) program,[3] naming the KRA Corporation as the proposed awardee.[4] In an August 23 letter, SBA informed HHS that acceptance of the requirement into the 8(a) program and award to the KRA Corporation would have no adverse impact on any small business, including McNeil. McNeil subsequently appealed that determination to SBA's Office of Hearings and Appeals (OHA), and also filed an agency-level

[1]The program provides assistance to states which may incur costs as a result of the legalization of undocumented aliens.

[2]Contract No. 233-90-0001, which was signed by "Mr. Richard Nelson, President" on behalf of Skyline. That contract will be referred to as the "HHS contract" in this decision.

[3]Section 8(a) of the Small Business Act authorizes SBA to contract with government agencies and to arrange for performance of such contracts by awarding subcontracts to socially and economically disadvantaged small businesses.

[4]HHS states that prior to that offering, it reviewed the technical capabilities of several 8(a) firms, including McNeil, and concluded that the KRA Corporation was best qualified to perform the follow-on contract.

protest with HHS. While those actions were pending McNeil filed this protest in our Office.[5]

The protester argues that SBA unreasonably concluded that acceptance of the requirement into the 8(a) program would have no adverse impact on McNeil. The protester explains that McNeil, itself a small business, purchased Skyline effective January 1, 1993. McNeil asserts that the purchase of Skyline did not affect contract performance or McNeil's small business size. McNeil contends that SBA's determination was unreasonable because the HHS contract represented approximately 58 percent of McNeil's total revenues.

DISCUSSION

Interested Party Status

HHS argues that McNeil is not an "interested party" to maintain the protest. Under the bid protest provisions of the Competition in Contracting Act of 1984, 31 U.S.C. §§ 3551-3556 (1988), only an "interested party" may protest a federal procurement. That is, a protester must be an actual or prospective offeror whose direct economic interest would be affected by the award of a contract or the failure to award a contract. See 4 C.F.R. § 21.0(a) (1993). HHS contends that since the contract was awarded to Skyline, Skyline--not McNeil--is "the actual or prospective bidder or offeror whose direct economic interest" was affected by SBA's decision to accept the requirement into the 8(a) program. According to HHS, McNeil is not the proper party to pursue this protest. We disagree.

Although the protester relies on the value of the HHS contract originally awarded to Skyline as a basis for its protest, it is clear that the protester is pursuing this action on the theory that Skyline's contract was transferred to McNeil prior to SBA's determination. McNeil's theory is consistent with SBA's position in this protest that McNeil "inherited" Skyline's contract as a result of purchasing

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[5]In a letter dated September 21, 1993, the contracting officer denied McNeil's agency-level protest. On November 10, SBA informed our Office that OHA had dismissed McNeil's appeal for lack of jurisdiction. See generally 13 C.F.R. §§ 121.1701 and 134.3 (1993). Pursuant to Federal Acquisition Regulation (FAR) § 33.104(b), the head of the contracting activity determined that urgent and compelling circumstances significantly affecting the interests of the United States would not permit awaiting our decision, and on September 30, HHS awarded the contract to the KRA Corporation.

Skyline. As will be explained further in this decision, we agree with that position.

Under the Small Business Act and its implementing regulations, SBA may not accept any requirement into the 8(a) program which "would have an adverse impact on other small business programs or on an individual small business, whether or not the affected small business is in the 8(a) program." 13 C.F.R. § 124.309(c); Korean Maintenance Co., B-243957, Sept. 16, 1991, 91-2 CPD ¶ 246. McNeil, a small business and in effect the incumbent contractor currently performing the services which are the subject of the 8(a) award, specifically challenges SBA's determination that the firm would not be adversely affected as a result of accepting the requirement for 8(a) award. The protester in essence argues that in reaching its conclusion, SBA failed to consider relevant factors such as the value of the contract to McNeil relative to its gross income, and the impact on McNeil of removing the requirement from a competitive small business program. If we were to sustain the protest, we would recommend that SBA determine whether, considering all relevant factors under the applicable regulations, acceptance of the requirement into the 8(a) program would have an adverse impact on McNeil, and if so, that the procurement not be retained in the 8(a) program. See State Janitorial Servs., Inc., B-240646, Dec. 6, 1990, 90-2 CPD ¶ 463. Since McNeil would be eligible to compete for the follow-on requirement at issue here, the protester has the requisite direct economic interest to maintain the protest.

HHS relies on our decision in Robert Wall Edge--Recon., 68 Comp. Gen. 352 (1989), 89-1 CPD ¶ 335, to argue that McNeil, as a shareholder in Skyline, is not authorized to maintain the protest.[6] McNeil is not protesting as a shareholder on behalf of Skyline. Rather, as already

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[6]In that case, Mr. Edge, under the letterhead of Robert Wall Edge, Senior Human Resource Management (SHRM), protested the award of a contract to another firm. We dismissed the protest because since neither Mr. Edge nor SHRM had participated in the procurement, he was not an interested party. In his reconsideration request, Mr. Edge argued that he had the requisite direct economic interest to protest the award because he had filed the protest in his capacity as a major shareholder in Development Research Associates (DRA), one of the offerors in the protested procurement. We affirmed the dismissal, concluding that in the absence of any evidence that Mr. Edge was authorized to act on behalf of DRA, the fact that he was the major stockholder in that firm did not establish that he was authorized to protest on behalf of DRA.

explained, McNeil is protesting on its own behalf, arguing that it is entitled to the protections afforded an incumbent small business under the applicable regulations, and that its economic interest was directly affected by SBA's decision.[7] HHS's reliance on our decision in Robert Wall Edge--Recon. thus is misplaced.

Adverse Impact Determination

SBA takes the position that since McNeil "inherited" the HHS contract when it purchased Skyline, McNeil is the incumbent small business concern for purposes of applying the adverse impact concept. SBA relies on 13 C.F.R § 124.309(c)(2), which states:

> "SBA presumes adverse impact to exist when a small business concern has performed a specific requirement for at least 24 months, it is currently performing the requirement or finished such performance within 30 days of the procuring agency's offer of the requirement for the 8(a) program, and the estimated dollar value of the offered 8(a) award is 25 percent or more of its most recent annual gross sales (including those of its affiliates)."

According to SBA, since McNeil had not been performing the contract for at least 24 months at the time HHS offered the requirement to the 8(a) program, SBA could not presume an adverse impact on McNeil under this rule. SBA further states that since the contract transferred to McNeil, Skyline was not "currently performing the requirement" at the time HHS offered the requirement to the 8(a) program. SBA could therefore not presume adverse impact on Skyline. SBA thus concludes that its determination that acceptance of the requirement into the 8(a) program would have no adverse impact on other small businesses, including McNeil, was reasonable.

Analysis

Before we discuss the adverse impact concept as it relates to the protester, we first examine the theory upon which SBA based its conclusion that the HHS contract originally awarded to Skyline transferred to McNeil. The anti-assignment statute applicable here, 41 U.S.C. § 15 (1988), prohibits all assignments of government contracts, except to

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[7]We note that McNeil's agency-level protest, OHA appeal, and protest letter filed in our Office are all on "McNeil Technologies, Inc." stationery and are signed "James L. McNeil, President."

banks, trust companies, or other financial institutions.[8] The courts and boards of contract appeals have long recognized exceptions to that prohibition where a transfer of a contract occurred by operation of law.[9] See Mancon Liquidating Corp., ASBCA No. 18304, Jan. 24, 1974, 74-1 BCA (CCH) ¶ 10,470.

While as a general rule government consent is required to avoid the ban of the anti-assignment statutes, an exception has been developed by legal interpretation with respect to

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[8]41 U.S.C. § 15 provides in pertinent part:

> "No contract or order, or any interest therein, shall be transferred by the party to whom such contract or order is given to any other party, and any such transfer shall cause the annulment of the contract or order transferred, so far as the United States are concerned. All rights of action, however, for any breach of such contract by the contracting parties, are reserved to the United States."

See also 31 U.S.C. § 3727 (1988), the companion statute applicable to the assignment of claims.

[9]For a brief historical discussion of the development of the operation of law exception, see Patterson v. United States, 354 F.2d 327 at 329-30 (Ct. Cl. 1965), where the court examined the anti-assignment statutes in the context of a claim against the United States. The court stated:

> "[T]he courts have held the following assignments or transfers to be by 'operation of law,' and exempt from the relevant statutory provision: transfers by intestate succession or testamentary disposition, Erwin v. United States, 97 U.S. 392 (1878); by consolidation or merger to the successor of a claimant corporation, Seaboard Air Line Ry. Co. v. United States, 256 U.S. 655 (1921); by judicial sale, Western Pacific R. Co. v. United States, 268 U.S. 271 (1925); by subrogation to an insurer, United States v. Aetna Casualty & Surety Co., [338 U.S. 366 (1949)]; by statutory provision to a trustee in bankruptcy, McKay v. United States, 27 Ct. Cl. 422 (1892) . . . and by voluntary assignment of all the assets of an insolvent debtor for the benefit of creditors, Goodman v. Niblack [102 U.S. 556] (1880)."

the sale of an entire business.[10] Where the transfer is incident to the sale of an entire business, the transfer is considered to have occurred "by operation of law," and the assignment is exempted from the anti-assignment statute. See Radiatronics, Inc., ASBCA No. 15133, June 19, 1975, 75-2 BCA (CCH) ¶ 11,349. Based on the record before us, we conclude that the transfer of Skyline's contract to McNeil falls within one of the recognized exceptions to the anti-assignment statute, namely, an involuntary assignment incident to the sale of an entire business.

We rely on two documents related to the transaction between McNeil and Mr. Richard A. Nelson (the sole shareholder of Skyline), a "STOCK AGREEMENT" and a "PURCHASE AGREEMENT." Under the terms of these documents McNeil is to buy all of the outstanding stock of Skyline through an exchange of all of Skyline's stock for McNeil stock, whereby Mr. Nelson is to receive a 20 percent ownership share in McNeil. The following sections of the purchase agreement are relevant to our conclusion.

Paragraph No. 2 provides that Skyline will:

> "[R]etain responsibility for its indebtedness and liabilities incurred prior to January 1, 1993 . . . except for those items which are on-going in nature, such as lease payments, subcontractor payments, and similar items. In order to accomplish this, [Mr. Nelson] will retain Skyline's cash and accounts receivable assets. Thus, Skyline will be conveyed to [McNeil] both without debt and without cash."

Paragraph No. 5 of the purchase agreement authorizes McNeil to use the business name "Skyline Government Services Corporation or any variation of it, or combination of it with other names"; paragraph No. 9, entitled "Contract Assignment," states that Mr. Nelson "shall assign or use his best efforts to obtain the assignment (or novation) of contracts to [McNeil]"; paragraph No. 10.8, entitled "Title

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[10]See Numax Electronics, Inc., 54 Comp. Gen. 580 (1975), 75-1 CPD ¶ 21 (the transfer of government contracts and claims incident to corporate mergers, and to the sale of an entire business or of an entire portion of a business is not prohibited by the anti-assignment statutes); 51 Comp. Gen. 145 (1971) (interpreting the anti-assignment statutes as inapplicable to transfers incident to the "sale or merger" of a contracting corporation or other entity). An analogous exemption applies to the transfer of proposals prior to award. See Ionics Inc., B-211180, Mar. 13, 1984, 84-1 CPD ¶ 290.

to Assets," provides that McNeil "shall at [c]losing receive good and marketable title to all of the assets . . . free and clear of any and all mortgages, pledges, liens, encumbrances, or other restrictions. All such assets shall be conveyed in 'as is' working condition."

It is clear from these documents that Mr. Nelson sold the entire business of Skyline, including its name, all of its assets--except those retained in order to fulfill the requirements of the purchase agreement quoted above--and future liabilities, to McNeil, thus merging it with that firm. The protester thus became the complete successor in interest to Skyline. See, e.g., J.I. Case Co., B-239178, Aug. 6, 1990, 90-2 CPD ¶ 108 (wholly owned subsidiary merged with its parent corporation, which became complete successor in interest, whereby parent corporation succeeded to all rights, privileges, immunities, and franchises, and all the property of subsidiary, as well as all liabilities and obligations). The fact that former Skyline employees assigned to the HHS contract continued to perform the contract after January 1, 1993, does not affect our conclusion. Skyline, if it may be said to have continued any operations at all, did so as an empty shell, without cash, assets, or liabilities, through McNeil and under McNeil's complete management and control.[11] In sum, we think that SBA reasonably concluded that for all practical purposes Skyline had merged into McNeil and had ceased to exist as a separate legal entity. SBA's conclusion that Skyline's HHS contract transferred to McNeil therefore was reasonable.

We next turn to SBA's adverse impact determination. The Small Business Act affords SBA and contracting agencies broad discretion in selecting procurements for the 8(a) program; we will not consider a protest challenging a

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[11]Our conclusion that Skyline merged into McNeil and that McNeil is the successor firm is further supported by other evidence in the record. In a letter dated January 29, 1993, for example, Mr. Nelson informed the HHS contracting officer that "effective January 1, 1993, [Skyline] merged our business operations with [McNeil]. . . . We will continue to do business under the McNeil name." Mr. Nelson further explained that "the merger of Skyline and McNeil has resulted in a combined organization of significantly expanded capabilities," and requested that HHS consider McNeil for future procurements. That letter was written on McNeil stationery and signed by "Richard A. Nelson, Vice President." After filing the instant protest, in a letter dated October 18, McNeil informed our Office that it had relocated its corporate headquarters to a new location--Skyline's former address.

decision to procure under the 8(a) program absent a showing of possible fraud or bad faith on the part of government officials or that specific laws or regulations may have been violated. San Antonio Gen. Maintenance, Inc., B-240114, Oct. 24, 1990, 90-2 CPD ¶ 326. The issue for our review in this case is whether SBA followed the applicable regulations in concluding that there would be no adverse impact on Skyline or McNeil as a result of accepting the requirement into the 8(a) program.

The first question we must address is whether SBA reasonably determined that it could not presume adverse impact to exist relative to Skyline or McNeil. As stated earlier, the regulation relied upon provides that SBA presumes adverse impact to exist when the following criteria are met: (1) when a small business concern has performed a specific requirement for at least 24 months; (2) it is currently performing the requirement or finished such performance within 30 days of the procuring agency's offer; and (3) the estimated dollar value of the offered 8(a) award is 25 percent or more of its most recent annual gross sales (including those of its affiliates). See 13 C.F.R. § 124.309(c)(2).

As discussed above, SBA reasonably concluded that Skyline had essentially ceased to exist, and that the HHS contract transferred to McNeil by operation of law as of January 1, 1993. Accordingly, we think that SBA reasonably concluded that it could not presume an adverse impact to exist as to Skyline, since that firm was not performing the HHS contract at the time HHS offered the requirement to SBA.[12]

Nor do we think that Skyline's incumbency on the HHS contract could properly be imputed to McNeil. It is undisputed that prior to its acquisition by McNeil, Skyline was a separate legal entity; Skyline was the firm that competed for the 1990 requirement; Skyline was the firm found responsible and acceptable by HHS based on that firm's resources and capabilities independent of McNeil; and Skyline actually performed the contract for more than 2 years, without any assistance from or participation by McNeil. Accordingly, we think that SBA reasonably

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[12]It is apparent that McNeil also believed that Skyline was no longer performing the HHS contract as a separate legal entity after January 1, 1993. In its appeal to OHA, the protester explained that "MCNEIL/Skyline continued to perform on the effort;" the protester made the same statement in its protest letter to our Office; and in its agency-level filing, the protester stated that "McNeil continues to perform on this effort," and that "McNeil is adversely impacted" by SBA's determination.

disregarded Skyline's performance in not presuming an adverse impact on McNeil. Further, since the transfer did not occur until there were only 9 months remaining on the contract, there was no basis for SBA to otherwise presume adverse impact to exist as to McNeil.

While SBA reasonably concluded that the criteria for presuming adverse impact were not met, we conclude that SBA nevertheless erred in its determination because SBA limited the scope of its inquiry to determining whether it should presume adverse impact. SBA's regulations require it to do more than that.

13 C.F.R. § 124.309 states:

> "SBA will not accept for 8(a) award proposed procurements not previously in the 8(a) program if any of the circumstances identified in paragraphs (a), (b), or (c) of this section exist. . . .
>
> . . . . .
>
> "(c) Adverse Impact. SBA has made a written determination that acceptance of the procurement for 8(a) award would have an adverse impact on other small business programs or on an individual small business, whether or not the affected small business is in the 8(a) program. . . .
>
> "(1) In determining whether or not adverse impact exists, all relevant factors will be considered." [Emphasis added.]

Thus, where, as here, the facts do not create a presumption of adverse impact under 13 C.F.R. § 124.309(c)(2), the regulations nevertheless require SBA to consider all relevant factors which may show potential adverse impact on a small business. In other words, the regulations do not preclude SBA from determining that a small business could be adversely affected by a decision to accept a proposed procurement into the 8(a) program where the criteria that would otherwise create a presumption of adverse impact are not met. See, e.g., Microform Inc., B-244881.2, July 10, 1992, 92-2 CPD ¶ 13 (where, absent the criteria that create a presumption, SBA examined additional relevant factors including whether loss of the contract would force incumbent into bankruptcy, affect a significant percentage of incumbent's employees, or significantly impair the value of assets incumbent purchased for the procurement).

SBA's standard "DETERMINATION OF IMPACT" form reflects the regulatory requirement. Paragraph No. 2 of that form, a copy of which appears in the record, provides:

> "2. The facts in [the] paragraph above do not create a presumption of adverse impact, but adverse impact is determined to exist for the following reasons:"

The form provides a space for SBA to document its finding. The form SBA completed for the instant procurement, however, contains the notation "N/A," (not applicable) in the space provided. SBA does not explain, and given the requirement in the regulations it is not clear how, without further inquiry, SBA determined that the quoted paragraph was inapplicable here.

In sum, the regulations clearly require SBA to go further than it did. SBA should have considered the potential impact of accepting the requirement into the 8(a) program on McNeil, even though all the factors which create a presumption of adverse impact may have been absent. To hold otherwise would undermine the purpose of the adverse impact concept, i.e., "to protect those small business concerns which are performing requirements pursuant to other small business programs from having these requirements taken away and placed into the 8(a) program for performance by 8(a) firms only." Information Dynamics, Inc., B-239893; B-239894, Oct. 1, 1990, 90-2 CPD ¶ 262 at 4. Accordingly, we find that in determining whether including this requirement in the 8(a) program would have an adverse impact on McNeil, SBA improperly failed to follow 13 C.F.R. § 124.309(c), and we sustain the protest on this basis.

RECOMMENDATION

We recommend that SBA, consistent with its regulations, properly determine whether including the requirement in the 8(a) program would have an adverse impact on McNeil. If SBA concludes that acceptance of the requirement was inappropriate, the requirement should not be retained in the 8(a) program. If that is the case, the contract awarded to the KRA Corporation should be terminated. McNeil is entitled to recover the reasonable costs of filing and pursuing its protest. 4 C.F.R. § 21.6(d). McNeil should file its claim, detailing and certifying the time expended and costs incurred, within 60 days after receipt of this decision. 4 C.F.R. § 21.6(f)(1).

The protest is sustained.

James F. Hinchman

for Comptroller General
of the United States