

BEFORE THE
MARYLAND STATE BOARD OF CONTRACT APPEALS

Appeal of SUBURBAN UNIFORM COMPANY)
DIVISION OF BIG BOYS' ARMY & NAVY) Docket No. MSBCA 1053
STORES, INC.)
Under DGS Request to Bid No. P11322)

March 19, 1982

Small Business Set-Aside Statute - Affiliates — The term affiliate as used in Art. 21, Md. Ann. Code, § 8-101(b) of Maryland's small business set-aside statute was intended to have its ordinary meaning since the Legislature used the term without limitation. The term affiliate thus means a company effectively controlled by another or associated with others under common ownership or control.

Small Business Set-Aside - Affiliates — Companies are affiliated on the basis of common ownership and control pursuant to Maryland's small business set-aside statute, where a bidder's officers have a majority interest and control in a second concern.

Construction of Regulations — An agency's interpretation of a regulation it is charged with administering is entitled to controlling weight where the agency's interpretation is not plainly erroneous or inconsistent with the regulation's language.

Small Business Set-Aside Statute - Criteria — Under Art. 21, Md. Ann. Code, § 8-101 and COMAR 21.01.02.62, the bidder was not a small business entitled to the five percent preference where its gross annual sales and that of its affiliate exceeded the maximum \$1,000,000 annual gross sales amount allowed by the agency's regulations for qualifying as a small business.

APPEARANCES FOR THE APPELLANT:

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APPEARANCES FOR THE INTERESTED PARTIES:

Balco Uniform Cap Corporation

Marion P. Krampf
Baltimore, Maryland
Robert Friedlander
Baltimore, Maryland

R. J. Uniform Company

APPEARANCES FOR THE RESPONDENT:

Varda N. Fink
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OPINION BY MR. KETCHEN

This timely appeal has been taken from a final decision issued by Mr. Robin J. Zee, the Assistant Secretary for Operations at the Maryland Department of General

Services (DGS) and the procurement officer in this dispute. This final decision denied Appellant's claim that it was entitled to a five percent preference as provided for under Maryland's small business set-aside program.¹ Appellant maintains that it is entitled to that preference and asks this Board to so find. Since DGS already has awarded a contract to Balco Uniform Cap Corporation (Balco), Appellant further requests that we both order DGS to terminate that contract and require them to award a new contract to Appellant as the lowest responsive and responsible bidder under DGS Request to Bid No. P11322.

I. FINDINGS OF FACT

A. Pre-Award Procedures

On September 28, 1981, DGS issued a request for quotations (RFQ) for the supply of guard uniforms to several state correctional facilities. This RFQ provided that eligible small businesses would be accorded a five percent preference, pursuant to Art. 21, Md. Ann. Code, § 8-101 and COMAR 21.11.01.01.²

Bids were opened on November 3, 1981. Of the six bids received, the following are considered most pertinent to this appeal:

Balco	\$156,326.00
R. J. Uniform Company	\$159,819.75
Appellant	\$160,781.90

Since DGS did not apply the five percent preference to any bid received under this procurement, Balco was identified as the apparent low bidder.

B. Appellant's Bid Protests

On November 6, 1981, Appellant filed a protest with the DGS procurement officer asserting that Balco was not entitled to a five percent small business preference. In a final decision issued on November 17, 1981, the DGS procurement officer sustained Appellant's bid protest and confirmed that Balco had not been granted the five percent small business preference. On November 20, 1981, Appellant appealed this decision to the Board, alleging that it then was entitled to the five percent preference and the contract award. Since this issue had never been presented to the procurement officer for decision, it was remanded to DGS for appropriate consideration. Following a hearing on this matter on December 16, 1981, the procurement officer ruled, on January 20, 1982, that Appellant also was not entitled to a five percent preference. The basis for this decision was that Appellant's gross sales when

¹Maryland's procurement Act requires DGS to accept the lowest responsive and responsible small business bid in designated small business set-aside procurements if that bid does not exceed by five percent the bid received from the lowest responsive and responsible bidder which is not a small business. Art. 21, Md. Ann. Code, § 8-101(f); COMAR 21.11.01.01B(3). (8:9 Md. R. S-139 (May 1, 1981)).

²8:9 Md. R. S-138-39 (May 1, 1981).

considered with those of its alleged affiliate, The HUB of Southern Maryland (HUB), exceeded Maryland's small business criteria of one million dollars in annual sales.³

C. Business and Financial Relationship Between Appellant and the HUB

Appellant is a corporation whose stockholders and officers are as follows:

<u>Stockholder</u>	<u>Office</u>	<u>% of Corporate Stock Owned</u>
Mr. Warren Michelson	President	46.1
Mr. Baird Michelson	Vice-President	3.8
Mrs. Ruth Michelson	Comptroller	50.1

Each of these stockholders devotes essentially all working hours to the Appellant corporation. Approximately 92%⁴ of Appellant's sales are wholesale. Remaining sales are through a small retail outlet in Westminster, Maryland.

The HUB is a subchapter S corporation whose stockholders and officers are as follows:

<u>Stockholder</u>	<u>Office</u>	<u>% of Corporate Stock Owned</u>
Mr. Warren Michelson	President	33.34
Mr. Baird Michelson	Vice-President	33.33
Mr. David Grossman	Vice-President & Sec-Treas.	33.33

Mr. Grossman is the General Manager of the HUB and devotes all of his working time to this operation. Warren and Baird Michelson occasionally visit the store but do not play a role in its daily management. The HUB is predominantly a retail, department store outlet.

While a small amount of inventory is traded between the two businesses, these exchanges are handled as cash transactions. There have been no loans from one corporation to the other, although Warren and Baird Michelson have co-signed for loans along with Mr. Grossman on behalf of the HUB.

The annual sales of each corporation for the most recent fiscal year prior to this procurement were:

³COMAR 21.01.02.62 (8:9 Md. R. S-12 (May 1, 1981)).

⁴Although Appellant's accountant did testify that 98% of Appellant's sales were wholesale, the actual sales figures presented at hearing show 92%.

	<u>Wholesale</u>	<u>Retail</u>	<u>Total</u>
<u>Appellant</u>			
(FY January 1, 1980- December 31, 1980)	\$857,489.38	\$74,404.87	\$931,894.25
<u>The HUB</u>			
(FY February 1, 1980- January 31, 1981)	\$71,497.23	\$351,687.23	\$423,184.46
(Appellant's Exhibits 1 and 2)			

II. DECISION

Whether Appellant is entitled to a five percent small business preference is dependent upon the proper application of Maryland's Small Business Act⁵ and its implementing regulations.⁶ As set forth in § 8-101(b) of the Act, small business criteria were to be established in the following manner:

- "(1) The Secretary⁷ shall adopt rules and regulations specifying the criteria for qualification as a small business.
- "(2) The criteria shall include a maximum number for employees and a maximum dollar volume computed on annual sales and receipts of a bidder and all its affiliates. The maximum number of employees and maximum dollar volume may vary from industry to industry to the extent necessary to reflect different characteristics. However, with respect to maximum number of employees, a manufacturing business may not employ more than 250 individuals. With respect to maximum dollar volume, a wholesale business may not have annual sales in excess of \$2,500,000 for its most recent fiscal year and a retail business or business selling services may not have annual sales and receipts in excess of \$5,000,000."

⁵See Art. 21, Md. Ann. Code, § 8-101 1981 Repl. Vol.).

⁶See COMAR 21.11.01 (8:9 Md. R. S-138 (May 1, 1981)).

⁷The "Secretary" means the Secretary of General Services, the Secretary of the Department of Transportation, or the President of the University of Maryland.

The criteria ultimately decided upon were promulgated prior to this procurement and appear in COMAR 21.01.02.62⁸ as follows:

"'Small Business' means a firm which meets the following criteria:

- A. It is independently owned and operated;
- B. It is not a subsidiary of another firm;
- C. It is not dominant in its field of operation;
- D. Its wholesale operations did not employ more than 50 persons, and its gross sales did not exceed \$1,000,000 in its [sic] most recently completed fiscal year;
- E. Its retail operations did not employ more than 25 persons, and its gross sales did not exceed \$500,000 in its most recently completed fiscal year;
- F. Its manufacturing operations did not employ more than 100 persons, and its gross sales did not exceed \$500,000 in its most recently completed fiscal year;
- G. Its service operations did not employ more than 100 persons, and its gross sales did not exceed \$500,000 in its most recently completed fiscal year; and
- H. Its construction operations did not employ more than 50 persons, and its gross sales did not exceed \$2,000,000 in its most recently completed fiscal year."

In order to resolve the instant dispute, it first is necessary to determine whether Appellant and the HUB are affiliates within the meaning of § 8-101(b)(2) of Maryland's Small Business Act. Appellant contends that it is not affiliated with the HUB in that each operates independently, maintains separate books of account, and has no financial tie to the other. DGS argues, however, that common ownership in the two corporations makes them affiliates.

The cardinal rule of statutory construction is that statutes always should be construed to effectuate the Legislature's intent. Welsh v. Kuntz, 196 Md. 93, 75 A.2d 343, 345 (1949). Since the Legislature utilized the term, "affiliates" without limitation, we conclude that its ordinary meaning was intended. Compare Atlantic Gulf and Pacific v. Dept. of Assessments & Taxation, 252 Md. 173, 179, 249 A.2d 180, 185 (1969). Accordingly, the term affiliate must refer to "a company effectively controlled by another or associated with others under common ownership or control." Webster's Third New International Dictionary of The English Language Unabridged (1976). This also is the definition applied by DGS in determining qualifications for small businesses.

⁸8:9 Md. R. S-12 (May 1, 1981).

In determining what constituted common ownership and control, DGS looked to the Federal Small Business Act⁹ and its implementing regulations for guidance (Tr 51). These regulations provide, in pertinent part, that:

"Concerns...are affiliates of each other when either directly or indirectly (1) one concern controls or has the power to control the other, or (2) a third party or parties controls or has the power to control both. In determining whether concerns are independently owned and operated and whether or not affiliation exists, consideration shall be given to all appropriate factors, including common ownership, common management and contractual relationships." 13 CFR § 121.3-2(a). (DGS Exh. 1).

Factors incident to common control also are set forth in 13 CFR § 121.3-2(a) which provides that:

"(i) Nature of Control. Every business concern is considered as having one or more parties who directly control or have the power to control it. Control may be affirmative or negative and it is immaterial whether it is exercised so long as the power to control it exists.

* * *

(vi) Control through common management. A concern is considered as controlling or having the power to control another concern when one or more of the following circumstances are found to exist, and if it is reasonable to conclude that under the circumstances such concern is directing or influencing or has the power to

⁹The Federal Small Business Act, as enacted prior to Maryland's Small Business Law, provides that:

"For the purposes of this Act [15 U.S.C.S. §§ 631 et seq.], a small business concern shall be deemed to be one which is independently owned and operated and which is not dominant in its field of operation. In addition to the foregoing criteria the Administrator, in making a detailed definition, may use these criteria, among others: Number of employees and dollar volume of business. Where the number of employees is used as one of the criteria in making such definition for any of the purposes of this Act [15 U.S.C.S. §§ 631 et seq.], the maximum number of employees which a small business concern may have under the definition shall vary from industry to industry to the extent necessary to reflect differing characteristics of such industries and to take proper account of other relevant factors." 15 U.S.C.S. § 632 (July 18, 1958, P.L. 85-536, § 2[3], 72 Stat. 384).

direct or influence, the operation of such other concern.

- (A) Interlocking management. Officers, directors, employees, or principal stockholders of one concern serve as a working majority of the board of directors or officers of another concern."

Pursuant to these standards, DGS then determined that Warren and Baird Michelson's majority interest and control in the HUB, when considered along with their respective positions as officers of Appellant corporation, was sufficient to affiliate the two businesses. This conclusion was not unreasonable under the foregoing Federal guidelines. See Springfield White Castle Co. v. Foley, 230 F. Supp. 77, 78 (W.D., Mo., 1964).

In enacting the Maryland Small Business Act, the Legislature accorded considerable discretion to the procuring agencies to develop and apply criteria for qualifying small business concerns. Although certain criteria have been promulgated for use in this regard, regulations never have been published which specifically address the factors for consideration in determining whether an affiliation exists between businesses. Nevertheless, we are satisfied that DGS, in consistently applying the Federal guidelines, has employed a reasonable standard for such determinations. In Maryland, where an agency is given discretionary authority, and the exercise of that discretion is not unreasonable or fraudulent, neither the Board nor the courts may interfere. Solon Automated Services, Inc., Docket No. MSBCA 1046, p. 22 (January 20, 1982); Biddison v. Whitman, 183 Md. 620, 624, 625 (1944); Hanna v. Board of Education of Wicomico County, 200 Md. 49, 51, 87 A.2d 846, 847 (1952). Accordingly, the DGS procurement officer's decision that Appellant and the HUB are affiliates must be sustained.

We now turn to the issue of whether Appellant, together with its affiliate, qualified as a small business. In this regard, Maryland's Small Business Act requires the DGS procurement officer to compute the "... annual sales and receipts of a bidder [Appellant] and all its affiliates" and compare that total to the qualification criteria established by the Secretary of the Department of General Services for small businesses. See Art. 21, Md. Ann. Code, § 8-101(b)(2). The pertinent qualification criteria is set forth in COMAR 21.01.02.62 as follows:

"Its [the small business firm's] wholesale operations did not employ more than 50 persons, and its [the small business firm's] gross sales did not exceed \$1,000,000 in its most recently completed fiscal year..."

Appellant's gross sales, as set forth in its tax return, were \$931,894.25. The HUB's gross sales were \$423,184.46. The DGS procurement officer, on this basis, concluded that since the combined annual sales of Appellant and the HUB exceeded \$1,000,000 for the most recent fiscal year prior to this procurement, Appellant did not qualify as a small business. Appellant argues, however, that since the combined: wholesale sales did not exceed \$1,000,000, it did qualify as a small business and was entitled to the five percent preference.

When interpreting an administrative regulation, great deference is given to the interpretation of that regulation by the agency charged with its administration. Mountain States Telephone and Telegraph Co. v. United States, 204 Ct. Cl. 521, 499 F.2d

611 (1974). Where the administrative interpretation is not plainly erroneous or inconsistent with the language of the regulation, it is entitled to controlling weight. Udall v. Tallman, 380 U.S. 1, 16-17 (1965). Here DGS is one of the agencies charged with the administration of the Small Business Act. Art. 21, Md. Ann. Code, § 8-101(a)(2). The evidence further establishes that DGS consistently has interpreted this regulation as referring to gross annual sales rather than wholesale sales (Tr 118). Since this interpretation is not inconsistent either with COMAR 21.01.02.62 or § 8-101(b)(2) of the Maryland Small Business Act which speak to the annual or gross sales of an entire firm, the DGS interpretation must prevail. Accordingly, given that the combined annual sales of Appellant and its affiliate did exceed \$1,000,000 in the most recent fiscal year prior to this procurement, the decision of the DGS procurement officer, denying small business status and a preference to Appellant, must be sustained. Compare American Electric Company v. United States, 270 F. Supp. 689 (D. Hawaii 1967).

For the foregoing reasons, this appeal is denied.