Cite as: *CVE Protest of Randy Kinder Excavating, Inc., d/b/a RKE Contractors*, SBA No. CVE-198-P (2021)

United States Small Business Administration
Office of Hearings and Appeals

CVE Protest of: Randy Kinder Excavating, Inc. d/b/a RKE Contractors, Protestor, Re: E & L Construction Group, LLC Solicitation No. 36C78621B0004 U.S. Department of Veterans Affairs	SBA No. CVE-198-P Decided: August 17, 2021

APPEARANCES

John B. Dunlap III, Esq., Erin G. Fonacier, Esq., Dunlap Fiore LLC, Baton Rouge, Louisiana, for E & L Construction Group, LLC

Peter B. Ford, Esq., Samuel S. Finnerty, Esq., Anna R. Wright, Esq., Meghan F. Leemon, Esq., PilieroMazza, PLLC, for Randy Kinder Excavating, Inc. d/b/a RKE Contractors

DECISION[1]

I. Introduction and Jurisdiction

On April 29, 2021, Randy Kinder Excavating, Inc. d/b/a RKE Contractors (Protestor) protested the Service-Disabled Veteran-Owned Small Business (SDVOSB) status of E & L Construction Group, LLC (E&L) in connection with the U.S. Department of Veterans Affairs (VA) Invitation for Bids (IFB) No. 36C78621B0004. Protestor contends that E&L is not owned and controlled by one or more Service-Disabled Veterans, and that due to substantial dependence upon a non-veteran, E&L cannot exercise independent judgment without great economic risk. For the reasons discussed *infra*, the protest is granted.

[1] This decision was initially issued under a protective order. Pursuant to 13 C.F.R. § 134.205, OHA afforded counsel an opportunity to file a request for redactions if desired. OHA received one or more timely requests for redactions and considered any requests in redacting the decision. OHA now publishes a redacted version of the decision for public release.

The U.S. Small Business Administration (SBA) Office of Hearings and Appeals (OHA) adjudicates SDVOSB status protests pursuant to 38 U.S.C. § 8127(f)(8)(B) and 13 C.F.R. part 134 subpart J.[2] Protestor filed its protest within five business days after receiving notification that E&L was the apparent awardee, so the protest is timely. 13 C.F.R. § 134.1004(a)(2)(i). Accordingly, this matter is properly before OHA for decision.

II. Background

A. CVE Verification

On October 25, 2021, the VA's Center for Verification and Evaluation (CVE) initially verified E&L as an SDVOSB and included it in the Vendor Information Pages (VIP) database of eligible firms, effective for three years. (Case File (CF), Ex. 234.) The verification letter stated that E&L "is presently, as of the issuance of this notice, in compliance with the regulation." (*Id.*, at 1.) E&L was required to report any changes that might adversely affect its eligibility within 60 days of the change. (*Id.*) On November 24, 2020, the VA informed E&L that based on the on-site examination to re-evaluate E&L's eligibility for the VIP verification program, it had been confirmed as an SDVOSB. (CF, Ex. 260.) The verification letter did not impact the date of E&L's current period of eligibility. (*Id.*) E&L was instructed to inform the CVE of any changes that would affect eligibility within 30 days of the change. (*Id.*)

B. Solicitation

On March 10, 2021, the VA issued IFB No. 36C78621B0004 (Solicitation) for a construction project at Fort Sill National Cemetery in Elgin, Oklahoma. The Contracting Officer (CO) set aside the procurement entirely for SDVOSBs and designated North American Industry Classification System (NAICS) code 237990, Other Heavy and Civil Engineering Construction, with a corresponding $39.5 million annual receipts size standard as the appropriate code.[3] Bids were due on April 22, 2021.

C. Protest

On April 22, 2021, bids were opened, and the CO announced that E&L was the lowest bidder and apparent awardee. On April 29, 2021, Protester, an unsuccessful bidder, filed the instant protest with the CO, challenging E&L's SDVOSB status.

In the protest, Protester alleges that E&L's Service-Disabled Veteran and majority owner, Christopher Esponge, does not fully control E&L under 13 C.F.R. § 125.13. (Protest, at 5.) E&L is substantially dependent on a non-veteran, and E&L cannot exercise independent business judgment without great economic risk. (*Id.*)

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[2] The regulations at 13 C.F.R. part 134 subpart J became effective on October 1, 2018. 83 Fed. Reg. 13,626 (Mar. 30, 2018).

[3] The description under the Solicitation No. 36C78621B0004 identified a $36.5 million annual receipts size standard for the NAICS code 237990. (Solicitation, at 1.) The parties do not dispute the size standard in question. As the error is harmless, further discussion is unnecessary.

More specifically, Protestor alleges that there is a presumption that the non-veteran controls E&L because E&L is co-located with Patriot Construction and Industrial, LLC (Patriot). (*Id.*, at 6.) E&L rents space to Patriot's Marine Division. Patriot is in the same line of business as E&L, i.e., the Industrial and Commercial Heavy Civil Construction business. (*Id.*) Ben LeBlanc is the 49% owner of E&L and the Chief Executive Officer of Patriot. Mr. LeBlanc, an owner, director, and officer of Patriot "owns an equity interest" in E&L. Thus, Mr. LeBlanc controls E&L consistent with 13 C.F.R. § 125.13(i)(3). Additionally, Mr. LeBlanc is both an employee and owner of E&L and the Chief Executive Officer of Patriot. Protestor argues this suggests that E&L, at a minimum, shares employees with Patriot, and shows that Mr. LeBlanc, through Patriot, exercises an undue level of control over E&L. (*Id.*, citing 13 C.F.R. § 125.13(i)(4).)

Protestor further contends that E&L remains significantly indebted to Mr. LeBlanc and his company, LeBlanc Lease, LLC (LeBlanc Lease). (*Id.*) Protestor highlights the SBA Area Office V (Area Office) Determination Case No. 05-2020-027 (Recertification Determination), noting that E&L has one Promissory Note with Mr. LeBlanc for XX and another Promissory Note with Mr. LeBlanc for XXX to be paid monthly, with interest, over X years. Here, Protestor asserts that the fact the lease and loans between the parties are committed to paper does not change the fact that Mr. LeBlanc is providing significant financial assistance to E&L. (*Id.*). Mr. LeBlanc also provides additional financial assistance to E&L by way of a personal indemnification. Protestor identifies the Area Office's prior Size Determination on E&L (No. 05-2020-019), which found affiliation between E&L and Mr. LeBlanc. Protestor states that as the Recertification Determination made no mention of any change regarding Mr. LeBlanc's indemnification of E&L, the indemnification is presumably still in place and Mr. LeBlanc continues to exert substantial control over E&L. (*Id.*) Thus, "a non-SDV who has an equity interest in E&L, "provides critical financial . . . support" to E&L, further underscoring the fact that a non-veteran controls E&L" under 13 C.F.R. §§ 125.13(i)(5) and (j).

Protestor then proceeds to list the factors that demonstrate E&L cannot exercise independent business judgment without great economic risk, such as: (1) E&L is dependent upon Mr. LeBlanc and LeBlanc Lease's financing for survival as a strong indicium of control; (2) at a minimum, there are continuing contractual relationships because of the loans and lease; (3) Mr. LeBlanc has a great interest in the success of E&L and vice versa; and (4) Mr. LeBlanc holds a substantial minority interest in E&L. (*Id.*, at 6-7.) Additionally, E&L presumably shares resources and, at least, office space with Patriot. Protestor then argues that "the "changes" that E&L made after the adverse Size Determination (e.g., removing Mr. LeBlanc as a Vice President and documenting its lease to Patriot and loans from Mr. LeBlanc and LeBlanc Lease) do not change the fact that Mr. LeBlanc, a non-veteran, exerts an impermissible degree of control over E&L." (*Id.*, at 7.) Therefore, Protestor asks OHA to find E&L cannot rebut the presumption that a non-veteran controls E&L and not eligible for inclusion in the CVE database, nor for award under the instant IFB. (*Id.*)

Finally, Protestor claims that E&L should have informed the CVE of its changed size status, when the Area Office found E&L no longer small following Size Determination No. 05-2020-019, dated April 16, 2020. (*Id.*) However, E&L did not do so until mid-May 2020 when it was time to reapply for verification, and its last certification was in October 2018. (*Id.*) Protestor

states had E&L immediately notified the CVE of its ineligibility, it'd likely have been removed from the VIP database. (*Id.*) As such, E&L should not now be considered an eligible SDVOSB, because it failed to comply with the requirements in 38 C.F.R. § 74.2(e) when it received the adverse size determination in April 2020.

With its protest, Protestor submits as exhibits the CO's post award notice to unsuccessful offerors, E&L's State of Louisiana's commercial search information, the Area Office's redacted Size Determination No. 05-2020-019, E&L's Vetbiz database profile, E&L's website team information, Recertification Determination, E&L's website service information, E&L's USAspending.gov profile information, E&L's list of contracts, and E&L's FPDS.gov profile information.

E. Response

On May 21, 2021, E&L responded to Protestor's allegations raised in the initial protest. E&L states it is not affiliated or economically dependent on Patriot, as previously determined by the Area Office's Recertification Determination issued on July 20, 2020. (Response, at 1.) E&L explains that Mr. Esponge is the founder, manager, and majority owner of E&L, while Mr. LeBlanc is a minority owner and does not hold an officer or managing position. (*Id.*, at 2.)

E&L submits background information, addressing its location, its certification by the SBA, its past performance, its business services, and its size. (*Id.*, at 2-4). Specifically, E&L provides services in the General Contracting, Construction & Project Management, as well as Design-Build and Planning. (*Id.*, at 2.) Its bonding capacity ranges from XXXXX which is contingent on the growth and success of E&L alone. E&L was founded 5 years ago and has successfully grown its business by completing successively large projects, which has increased its bonding capacity. (*Id.*)

E&L states that it owns its own building, located at 134 E. Main Street, in New Iberia, Louisiana. (*Id.*) The building includes individual suites, wherein E&L occupies Suite #2. (*Id.*) E&L purchased the building in November 2016 from Appraiser Associates. At that time, other tenants, Arceneaux Financial Services, Tammy Louvierre Insurance, and Appraiser Associates of Louisiana, were occupying existing suites. Thereafter, Appraiser Associates moved out of the building and Patriot's Marine Division moved in and opened a satellite office in the building. On April 30, 2020, Patriot executed a written lease agreement with E&L for the rental of office space for its Marine Division, which contains standard commercial lease terms and provisions. (*Id.*) Patriot pays X a month for a 1,150 sq. ft office space with a 5-year term lease. Failure to pay rent on time will be subject to late fees. Should Patriot violate any conditions of the lease, E&L can seek the remaining rent for the term of the lease or cancel the lease. (*Id.*)

E&L indicates that each office has its own individual suite, and no one shares office space. (*Id.*) Rent is based on the square footage of each office space. For example, Arceneaux Financial Services and Tammy Louvierre Insurance executed leases to E&L; the former pays X a month for a 400 sq. ft. office space, while the latter pays X a month for a 350 sq. ft. office space. E&L's building, on the Main Street in New Iberia, is a short distance from the Port of Iberia, which makes it an attractive location for all business. (*Id.*, at 3.) E&L further states that it has

created an arm's length transaction with Patriot's Marine Division and all its other tenants for the lease of space in its building. There is no reliance by one concern upon the other or any connection which would create an economically dependence based on such lease. (*Id.*)

E&L explains that last year, Protestor filed a size protest against E&L and was successful in its protest because Mr. LeBlanc, a minority owner of E&L, became a minority owner and officer of a larger company, Patriot. (*Id.*) Mr. LeBlanc did not obtain any ownership interest in Patriot until 2018, over two years after E&L's formation. Prior to his ownership in Patriot, any affiliation with Mr. LeBlanc was not an issue for SBA or SDVOSB certifications.

After SBA's finding of affiliation, E&L reorganized and ended any affiliation with Mr. LeBlanc. (*Id.*) SBA recertified E&L as a small business on July 20, 2020. Particularly, E&L adopted a new operating agreement, removing Mr. LeBlanc from any officer position as advised by SBA and from all points of contact. E&L also formalized lease and loan terms to substantiate that any interaction with Patriot or Mr. LeBlanc was an arm's length transaction. (*Id.*) E&L further states that there have been no major changes to E&L or its relationship with Mr. LeBlanc since the Recertification Determination. (*Id.*)

For past performance, E&L states that since its founding, it has provided General Contracting, Construction and Project Management, as well as Design-Build and Planning services to agencies, such as the U.S. Army Corps of Engineers, the Department of VA, the U.S. Coast Guard, the U.S. Geological Survey, and the U.S. Fish and Wildlife Service. (*Id.*) E&L also provided Project Managers/Superintendents, Quality Control Managers, and Safety Managers, which were hired for each project. Moreover, E&L has employed 5 to 6 people over the last three years, who were hired on a project-by-project basis, which included multiple dual role personnel who could act in a supervisory role as well as an operator/laborer. (*Id.*) To this end, E&L states that it has a consistent record of meeting its required self-performance goal on each of its projects. (*Id.*)

E&L further provides documentation that since its inception in 2016, it has been awarded twenty-one projects, including thirteen federal projects in the last five years, while the awarded projects have also grown in size and value. (*Id.*)

In addition to E&L's background, E&L briefly describes its size standard and Mr. Esponge's military service and spinal cord injury resulting in paralysis. (*Id.*, at 4.) After being honorary discharged, Mr. Esponge went to college, pursued Bachelor's and Master's degrees, and later founded E&L in 2016. E&L received its SDVOSB status on October 25, 2018. E&L has two full time employees, which include Mr. Esponge and Jacob Gautreau, the Project Manager and Estimator. (*Id.*) Occasionally, E&L hires part-time employees. However, E&L asserts that Mr. LeBlanc is not an employee of E&L and E&L's employees are not employed by Patriot or other entity owned by Mr. LeBlanc. (*Id.*)

Responding to the protest, E&L alleges that it has no affiliation to Mr. LeBlanc and Mr. Esponge has full control of the concern. Specifically, Mr. Esponge's full control of E&L is evidenced in the Second Amended and Restated Limited Liability Company (LLC) Operating Agreement of E&L dated April 30, 2020. (2020 Operating Agreement). E&L indicates that Mr.

Esponge is the sole Manager and principal executive officer of the company, supervising and controlling all day-to-day operations and decisions regarding future growth of E&L. (*Id.*, at 5.) As the sole Manager, Mr. Esponge has the sole authority to transact all business of the company, including the ability to expend capital, enter into agreements on behalf of E&L, open, maintain, and close bank accounts, borrow money, acquire, lease, or sell property, execute any security agreement, hire consultants and professionals, procure insurance and bonds, refinance any debt; and participate in legal proceedings of any sort. (*Id.*, citing to 2020 Operating Agreement § 3.3.) Mr. Esponge also approves members, amends the articles in the operating agreement to reflect new members, acts as liquidator, designates the principal office, calls for additional contributions, and determines distributions. (*Id.*, §§ 1.4, 1.7, 2.7, 7.1.)

Mr. Esponge is the Tax Representative with sole authority to act on behalf of E&L, controls the voting bloc, calls for special meetings, works at least 60 to 75 hours a week at E&L's office, attends all site visits for E&L's projects and all pre-construction meetings, signs all bids, contracts, contract awards, modifications and change orders, and bonding documents, and collects a salary when filling in for an absent Project Manager, Superintendent, Quality Control Manager, or Safety Manager under E&L's payroll. (*Id.*, §§ 2, 5.)

Conversely, Mr. LeBlanc does not have influence in the control of E&L in its day-to-day operations or long-term goals, does not collect a salary, and does not have the ability to perform duties affecting the overall company. (*Id.*, at 5.) At the request of Mr. Esponge, Mr. LeBlanc attends brief meetings once or twice a month. Mr. LeBlanc has no position as an officer or manager of E&L. Mr. LeBlanc may have a say in some cooperative company actions that require 100% of member approval, such as the removal of a member. (*Id.*) E&L refers to OHA case law to assert certain extraordinary actions that a minority owner may have the ability to block certain actions, which do not provide negative control to the minority owner. (*Id.*)

E&L further argues that it is economically independent. (*Id.*, at 6.) Mr. LeBlanc and Mr. Esponge, both, provided personal investments to E&L's purchase and renovation of the 134 E. Main Street building and other necessary expenses in starting the business in 2016. E&L explains that Mr. LeBlanc funded some of this investment with his own business, Leblanc Lease. These payments were not capital contributions to E&L under E&L's operating agreement, but rather personal loans to E&L. (*Id.*) Thus, E&L executed promissory notes with Mr. LeBlanc, which contain standard commercial terms and provisions found in any arm's length transaction, subject to an interest rate of X per annum. This is consistent with the current interest rates by third party lenders. (*Id.*) The terms provide that E&L must make twelve monthly payments each year, over a ten-year period. E&L will be in default of such loans if it fails to make timely payments, files for bankruptcy, admits in writing its inability to pay its debts or is subject to a conservatorship or writ attachment. After a period to cure such default, failure to pay would result in interest, penalties, and demands for collateral. (*Id.*) E&L paid off a promissory note to Mr. LeBlanc. As for the loans, E&L's debts to Mr. Esponge for XXX and to Mr. LeBlanc through LeBlanc Lease for XXX, are proportionate to their respective 51-49% ownership interests in the concern. (*Id.*) Therefore, E&L is not economically dependent upon Mr. LeBlanc, and the latter does not have the power to control E&L due to personal investments.

Furthermore, E&L asserts that Mr. LeBlanc is not a registered agent for E&L in the State of Louisiana. XXXXXXXXXXXXXXXXXXXXX. (*Id.*, at 6-7.) Moreover, E&L does not share employees, office space, equipment, or bonding and financing with any of LeBlanc's affiliated entities. (*Id.*, at 7.) E&L does not provide or receive any technical assistance with any of LeBlanc's affiliated entities. Additionally, E&L does not affiliate, align, associate, or have any business dealings with any of LeBlanc's affiliated entities. E&L indicates that many of these entities are no longer active, were never active or were created as holding companies that do not generate any revenue. (*Id.*)

E&L identifies the only "large" company that Mr. LeBlanc is associated with as Patriot, which currently provides marine services, hydro excavation, civil construction, and deep foundations. (*Id.*) E&L explains that Patriot was created on February 15, 2017. Prior to this, Mr. LeBlanc founded LeBlanc Marine, LLC (LeBlanc Marine) on September 8, 2004, and he owned X of the company. In 2018, LeBlanc Marine merged with Patriot to provide the company with a marine division. The merger was accomplished through XXXXX, which was the sole member of LeBlanc Marine. Now, Mr. LeBlanc owns a X share in XX. This X share was diluted to almost X once the companies, Patriot and XX, were merged through XXXXXX. Therefore, through LeBlanc Lease, Mr. LeBlanc currently holds a X share in XX. (*Id.*, at 7-8.)

With respect to prior subcontract projects with Patriot, E&L indicates that from the X projects that E&L has been awarded, X of which are federal awards, only two projects were subcontracted to Patriot. (*Id.*, at 8.) E&L asserts that on these projects, E&L performed the management, communication, and control portion, as well as it obtained the permits and licenses. (*Id.*) Furthermore, Patriot has provided bids to E&L for other subcontracts on other projects and was not selected as the subcontractor. In this manner, Patriot is held to the same treatment as any subcontractors that provide quotes and proposals to E&L.

The rest of E&L's response recounts why E&L is not dependent on Patriot or Mr. LeBlanc and argues that there is no good cause to find E&L ineligible as Service-Disabled Veteran in the CVE database. (*Id.*, at 9-12.) In addressing the first argument, E&L restates that Mr. Esponge is the majority owned veteran, makes sole business decisions, and fully controls the concern in its daily and long-term aspects. (*Id.*, at 9.) In response to Protestor's allegations, E&L claims OHA held that dependence is only found when the involvement of the non-veteran-owned firm is crucial to the veteran-owned firm's ability to conduct business, while E&L has ended any past affiliation with Mr. LeBlanc.

Additionally, E&L and Patriot have not entered into an agreement to conduct business on a continuing or permanent basis. Patriot does not prepare bids or assist with bid proposals for E&L, has not secured bonds for E&L, has not supplied scheduling or supervisory personnel for E&L, and has not performed the primary and vital requirement of E&L prime contract. Patriot's Marine Division is not co-located with E&L, and the former does not share employees or resources with the latter, besides being in the same building. (*Id.*, at 9-10.)

E&L relies upon OHA precedent, arguing its situation similar to cases where OHA found no evidence that a non-veteran owned entity has authority to administer and manage the SDVOSB's long term or daily business operations. (*Id.*, at 10, citing *Matter of DooleyMack*

Government Contracting, LLC, SBA No. VET-159 (2009) and *Matter of AWG Svcs., LLC*, SBA No. VET-164 (2009).)

Finally, E&L asserts that there is no good cause to find E&L ineligible as a Service-Disabled Veteran in the CVE database because E&L is presently in compliance with the SDVOSB regulations. (*Id.*, at 11.) Particularly, after SBA found E&L was affiliated with Mr. LeBlanc based on a "totality of the circumstances" standard, E&L it amended its operating agreement so that Mr. LeBlanc had no control of the concern and took further steps suggested by the SBA to memorialize the arm's length transactions with Mr. LeBlanc. (*Id.*) In May 2020, less than a month after the Area Office's size determination, E&L applied to be recertified as a small business. The SBA's certification was delayed due to the COVID-19 pandemic, and E&L was recertified as a small business on July 20, 2020. (*Id.*)

Thus, E&L explains that its failure to inform CVE was inadvertent and due to its focus on resolving the issues noted by the SBA and regaining the small business status. When E&L was not certified as a small business, it did not bid on or pursue any jobs, projects, or awards, which required a small business status or a Service-Disabled Veteran status. (*Id.*) On October 8, 2020, the CVE performed a site audit of E&L for continuing verification. (*Id.*, at 11-12.) Later, a letter from the CVE confirmed E&L's status in the VIP database.

Additionally, E&L argues that any of those issues are moot now that it is almost a year later, and there is no good cause to remove E&L from the VIP database. (*Id.*, at 12.) E&L indicates that there is no OHA precedent finding a recently verified SDVOSB ineligible due to a failure to notify the CVE of a change in circumstance without additional factors, much less because of a one-month lapse of notification. (*Id.*) Citing to OHA precedent, E&L further argues that almost all such cases involve a change in ownership, failure to respond to a direct request by the CVE, or other bad acts, which E&L has not performed or been accused of. (*Id.*, at 12-13.)

With its response, E&L submits as exhibits the State of Louisiana's certificate and documents, the 2020 Operating Agreement, commercial lease agreement between E&L and its tenants, Patriot, Tammy R. Louviere Insurance Consultants, LLC, and Arceneaux Financial Services, LLC, the Area Office's Recertification Determination, list of past performances, the CVE's verification letter as a SDVOSB dated October 25, 2018, E&L's promissory note to Mr. LeBlanc and Mr. Esponge, tax returns, Mr. LeBlanc's sworn declaration dated May 3, 2021, LeBlanc Marine's commercial search profile under the State of Louisiana, LeBlanc Marine's Amended and Restated Operating Agreement dated January 12, 2018, U.S. Industrial Holding's Capital Table, U.S. Industrial Holding's Second Amended and Restated LLC Agreement dated July 31, 2018, E&L's application to recertify as a small business dated May 15, 2020, the CVE's site visit examination letter dated October 1, 2020, the CVE's mandatory questions, and the CVE's verification of eligibility for the VIP database letter dated November 24, 2020.

F. Supplemental Protest

On June 14, 2021, after reviewing the Case File under the terms of an OHA protective order, Protestor submitted a supplemental protest. Protestor argues that the Case File bolsters its original contentions that E&L is ineligible for this award having failed to inform the CVE of a

change in circumstances and is not unconditionally owned or controlled by a Service-Disabled Veteran. (Supp. Protest, at 1-2.)

First, protestor points to the Case File and states that E&L has five operating agreements since 2016. (*Id.*, at 3.) The first operating agreement dated February 1, 2016, states that the agreement cannot be amended without the consent of Mr. Esponge and Mr. LeBlanc. Then, there are two versions of the operating agreement executed in 2018, which were not amended and restated. (*Id.*, at 3-4.) Protestor then discusses E&L's 2016 and 2018 operating agreements at length and alleges that there are clauses which limit Mr. Esponge's ability to control the company and to transfer his ownership interest which are impermissible. (*Id.*, at 4-5.) In particular, the 2018 operating agreement gives Mr. Esponge and Mr. LeBlanc full control of the management, operating, and the policy of the company as co-managing Members of E&L, equal voting power and management impasses settled through arbitration. Additionally, the 2016 operating agreement precluded Mr. Esponge from transferring his ownership interest without the express written consent of Mr. LeBlanc.

Protestor proceeds to argue that E&L was not eligible for inclusion in the CVE because none of the operating agreements in the CVE CF cure the eligibility issues discussed, *supra*. (*Id.*, at 5.) Moreover, in September 2018, E&L gave a misleading statement concerning its relationship with Mr. LeBlanc in response to the CVE's eligibility inquiries, therefore, E&L should not have been verified as an SDVOSB at any point since its admission. (*Id.*, at 6.)

Next, Protestor alleges that E&L remains ineligible for the inclusion in the CVE database as of the date of the bid and the date of the CVE protest. (*Id.*) Despite E&L's response that the 2020 Operating Agreement was in effect at the relevant time period, Protestor argues that such agreement was not included in the CVE Case File. (*Id.*, at 7.) Protestor refers to the VA's regulations and risks of SDVOSB removal from the CVE database when failing to disclose the extent to which non-veterans participate in the firm's management, failing to make required submissions or responses to CVE, and failing to inform the CVE of any such changes circumstances. Here, E&L went through a site visit and reverification process in October 2020 and was required to provide the 2020 Operating Agreement but failed to do so. (*Id.*, at 7-8.) When the CVE requested E&L's most recent meeting minutes and amended agreement, E&L provided its 2018 operating agreement, and thus, it failed to comply with the VA's regulation as cause enough for E&L's removal from the CVE database. (*Id.*, at 8.) Protestor contends that E&L's failure to comply timely resulted in it being wrongfully permitted to remain in the CVE database.

Protestor further argues that E&L does not satisfy the ownership requirement even under the 2020 Operating Agreement. (*Id.*, at 9.) Protestor relies on OHA's definition of "unconditional" ownership discussed in *In the Matter of Wexford Group Int'l, Inc.*, SBA No. SDV-105, (2009), and 13 C.F.R. § 125.11 to find impermissible limitations Mr. Esponge's ownership interest in E&L. (*Id.*, 9-10.)

Particularly, under the 2020 Operating Agreement, § 6.2 restricts Mr. Esponge's ability to sell his ownership interest in E&L by requiring him to provide a right of first refusal to E&L and in the event E&L elects not to buy all of Mr. Esponge's ownership interest, to the other members

of E&L. (*Id.*, at 10.) Further, § 6.5 precludes Mr. Esponge from retiring or withdrawing from E&L without written approval from the other members, thereby placing another impediment on his ability to exercise the full range of ownership rights. In addition, § 6.7 requires Mr. Esponge to dispose of his ownership interest in certain situations, such as when filing a petition for voluntary bankruptcy, any member must give written notice to E&L and convey to E&L that member's entire right, title, and interest. (*Id.*, at 10-11.) Failing to do so would indicate that the interest of that member in E&L will be deemed for all purposes to have been sold to E&L. Here, Protestor claims that placing such conditions on Mr. Esponge's ownership is not one of the exceptions outlined in 13 C.F.R. § 125.11, and therefore the conditions are impermissible and render E&L ineligible for the inclusion in the CVE. Protestor also identifies other impermissible limitations on Mr. Esponge's ownership, such as § 6.10 "involuntary transfer events" or "forced sale," in the event that Mr. Esponge is indicted or convicted for any felony, has committed self-dealing acts without written consent, has committed fraudulent acts, has committed a material beach to this agreement, or has been terminated. . . . " (*Id.*, at 11.)

Finally, Protestor argues that under the 2020 Operating Agreement § 11.10, E&L is not unconditionally controlled by an SDV, Mr. Esponge does not have unfettered control over the concern, and Mr. Esponge may amend the operating agreement so long as it does not affect the economic interest of any party to the agreement while all other amendments require a unanimous vote of the members. (*Id.* at 12.) Further, § 3.2 states that a successor manager will be elected upon the vote of members holding 65% of the ownership interest, which Mr. Esponge cannot satisfy on his own. (*Id.*, at 13.)

Therefore, Protestor contends that Mr. Esponge does not satisfy the SDVOSB control requirements in 13 C.F.R. § 125.13(d). Protestor makes note that amending the 2020 Operating Agreement is not one of the five "extraordinary circumstances" for which a non-veteran may have negative control pursuant to 13 C.F.R. §§ 125.11 and 125.13(m), and the regulations do not permit Mr. LeBlanc, a non-veteran, to have negative control over the Service-Disabled Veteran's ability to amend the 2020 Operating Agreement. (*Id.*, at 13.)

G. Supplemental Response

On June 29, 2021, E&L responded to the supplemental protest. E&L disputes Protestor's allegations the 2020 Operating Agreement contains impermissible conditions over Mr. Esponge's ownership and control of E&L. (Supp. Response, at 1.) First, E&L provides a history of its operating agreements in 2016, amended and restated in 2018, and once again, amended and restated in 2020. (*Id.*, at 1-2.) In 2020, the Protestor protested E&L's size status and affiliations. Then, E&L again amended its operating agreement and executed its Second Amended and Restated Operating Agreement, i.e., 2020 Operating Agreement, which SBA reviewed and approved on July 21, 2020, and thereafter recertified E&L as a small business. (*Id.*, at 2.)

E&L explains that when the CVE conducted an audit of E&L in October 2020, due to the COVID-19 pandemic, it was carried out via telephone and over the internet, as opposed to in-person. The audit required E&L to respond to a series of questions, including whether there has been any change in control, management or strategic decision-making authority of E&L, and any updates to the business documentations submitted to CVE during the last review. E&L

responded yes to both questions and noting the 49% owner was removed as a manager and vice president and is strictly an owner, while affirming of the updates to the business. (*Id.*) Mr. Esponge relayed the changes to the auditor and discussed the new operating agreement, as evidenced by the auditor's email request for the revised amended operating agreement. (*Id.*, at 2-3.) While Mr. Esponge turned over a number of documents to the auditor, he mistakenly provided the 2018 operating agreement even after informing of the recent 2020 change and 2020 Operating Agreement in response to the size protest. (*Id.*, at 3.)

As for prior operating agreements, E&L contends that the 2016 operating agreement was not in effect when the agreement was amended and restated in 2018, while the two 2018 operating agreements were no longer in effect when the 2020 Operating Agreement was executed. (*Id.*, at 3-4.) E&L further notes that under Louisiana law, limited liability operating agreements are a stand along contract that governs the parties by virtue of them signing the agreement, and Mr. Esponge and Mr. LeBlanc's 2020 Operating Agreement was correctly ratified and are the law between the parties. (*Id.*, at 4.)

E&L further contends that it is eligible for inclusion in the CVE database, because E&L informed the CVE of the changes to the operating agreement and had no reason to omit this agreement from its audit. (*Id.*) E&L states that the 2020 Operating Agreement was a "better" operating agreement in that it removed any control or affiliation issues related to Mr. LeBlanc and SBA had approved this 2020 Operating Agreement mere months before the audit. Thus, it would not benefit E&L to provide the older operating agreement. Additionally, Mr. Esponge answered all questions about the changes accurately and truthfully, informed the auditor about the new agreement, but merely and unintentionally provided the older agreement which evidenced the changes.

In response to Protestor's claims about the 2020 Operating Agreement provisions related to the withdrawal of members, filing for bankruptcy, amending the operating agreement, right of refusal, and replacement of the manager in very specific situations, E&L states that Mr. Esponge has full control and full ownership rights and direct ownership of his 51% share of E&L pursuant to the 2020 Operating Agreement. (*Id.*, at 5.) When this Protestor made a successful size protest against E&L in 2020, E&L specifically retained special counsel to draft a new operating agreement in compliance with the SBA regulations, currently referred as the 2020 Operating Agreement. This 2020 Operating Agreement was approved twice by the SBA as to form and content. First, on July 21, 2020, SBA reviewed the 2020 Operating Agreement and found that it complied with all regulations when it recertified E&L as a small business; and then, on June 9, 2021, when Protestor filed its 2021 parallel size protest. (*Id.*) In the 2021 size protest, SBA reviewed the 2020 Operating Agreement and found that it complied with all SBA regulations and dismissed the size protest. SBA further found the following:

> Certain extraordinary events, such as the removal of a member, require 100%-member approval. However, OHA has found that supermajority voting requirements for certain fundamental and extraordinary matters to protect a minority owner's investment are permissible without the finding of negative control so long as they do not restrict the day-to-day operation of the business. *See Size Appeal of BR Construction, LLC*, SBA No. SIZ-5303 (2011).

(*Id.*)

E&L contends that Mr. Esponge is the sole manager and the principal executive officer of the company, supervising and controlling day-to-day operations and decisions regarding future growth of the company. As the manager, Mr. Esponge has the authority to act alone in transacting all business of the company, while the business partner, Mr. LeBlanc, has no ability to perform duties affecting the overall operations of E&L. Mr. LeBlanc may have a say in some cooperative company actions that require 100% of member approval, such as the removal of a member, which is allowed under the regulations. (*Id.*)

E&L relies on OHA precedent concluding that situations where a minority owner may have the power to block certain extraordinary actions, do not endow the minority owner with negative control if those provisions are crafted to protect the investment of the minority shareholders and not to impede the majority's ability to control the business. (*Id.*, at 6, citing *Size Appeal of Carntribe-Clement 8AJV#l, LLC*, SBA No. Siz-5357 (2012); *Size Appeal of EA Engineering, Sci. and Tech., Inc.*, SBA No. SIZ-4973 (2008); *Size Appeal of Southern Contracting Solutions III, LLC*, SBA No. Siz-5956 (2018).) OHA also identified at least 20 acts that are considered extraordinary actions, such as amending the bylaws or operating agreements, entering into a substantially different business, issuing additional stock, changing the board, reclassifying a member's interest, approving the withdrawal of old members or the addition of new members, and filing for bankruptcy. (*Id.*, citing *Size Appeal of DHS Systems*, LLC, SBA No. SIZ-5211 (2011); *Size Appeal of Dooleymack Government Contracting*, LLC, SBA No. SIZ-5086 (2009).) Therefore, E&L maintains that the provisions of the 2020 Operating Agreement that govern the withdrawal of members, filing for bankruptcy, and amending the operating agreement are permissible.

E&L further states that other provisions highlighted by the Protestor should similarly be considered extraordinary actions, which permit a minority shareholder from protecting its investment. (*Id.*) Here, E&L is a closely held company owned by only two members. E&L's sole intent in creating the 2020 Operating Agreement was to comply with the regulations while protecting the investments of E&L by preventing another partner from being forced upon the members. (*Id.*) Moreover, 13 C.F.R. § 125.11 definition of unconditional ownership accommodates practical commercial arrangements if it prevents ownership benefits from falling into the hands of non-veterans. E&L asserts that all the provisions under the 2020 Operating Agreement are “normal commercial practices,” or essential good business practices, which protects the investment from fraud, criminal activity, or other risks while ensures the Service-Disabled Veteran's control of both, the day-to-day activities, and long-term goals of the concern.

E&L rejects Protestor's contention that the right of refusal in § 6.2 is impermissible, because the provision does not dictate pricing or force the member to sell against his or her wishes. E&L also relies on federal court interpretations of the right of first refusal in the context of bankruptcy law, finding that normal commercial rights of first refusal are not executory contracts. (*Id.*, citing to *Miles Construction, LLC v. United States*, 108 Fed. Cl. 792 (2013). Thus, if § 6.2's provision is not an executory agreement as understood under 13 C.F.R. 125.11, then it

is not an impermissible restriction on the members, including the Service-Disabled Veteran. (*Id.*, at 6-7.)

Similarly, E&L rejects Protestor's contention about the bankruptcy provision in § 6.5, because the provision does not prevent a member from declaring bankruptcy and it only precludes the bankruptcy estate from receiving the member's shares. (*Id.*, at 7.) Once the member files for bankruptcy, the shares are no longer the member's own to dispose of and the member must instead abide by the trustee's determinations. E&L explains that the commencement of a bankruptcy case "creates an estate" comprised of the debtor's property, 11 U.S.C. § 541; the trustee, through the bankruptcy court, is empowered to "use, sell, or lease" the debtor's property in the bankruptcy estate, 11 U.S.C. § 363; and the member would no longer be free under the law to dispose of or retain those shares. As the property of every business owner is automatically placed in the custody of the court upon bankruptcy, such bankruptcy provisions are standard commercial arrangements. (*Id.*)

As for § 6.10 of the 2020 Operating Agreement, this provision allows the company to buy back the shares of a member who is a bad actor and is meant to cover situations by which the entity would lose its VIP status due to lack of "good character" under 38 C.F.R. § 74.2. On the other hand, § 3.2 governs the selection of a successor manager only if Mr. Esponge is no longer the manager and the 65% vote for members to vote on a manager is only applicable for successor managers. The provisions complained by Protestor simply allow the minority member to protect his or her investment and do not impede on the majority's member right to own the company. (*Id.*) E&L further argues that SBA and OHA did not hold a first right of refusal, as such, to be in violation of the regulations. (*Id.*, at 9, citing *Matter of Alog Corp.*, SBA No. VET-285 (2020).)

In the event that OHA finds under *Wexford*'s standard that the 2020 Operating Agreement contains impermissible conditions, E&L argues that *Wexford* is no longer applicable with the promulgation of 13 C.F.R. § 125.11 and its definition of unconditional ownership. In turn, E&L cites to federal court decisions discussing unconditional ownership prior and after the promulgation of 13 C.F.R. § 125.11, to support a finding that SBA should follow this regulation or alternatively, adopt federal court interpretation of 38 C.F.R. § 74.3 and 13 C.F.R. § 124.3 wherein "normal commercial practices" were referenced. (*Id.*, at 11-12, citing *Miles* and *AmBuild Co. v. U.S.* 119 Fed.Cl. 10 (2014.))

With its supplemental response, E&L submits as exhibits SBA's 2021 Size Determination Case No. 05-2021-024, E&L's 2018 operating agreement dated September 17, 2018, a table with members' ownership interest, and an email correspondence between E&L's principal and the CVE reflecting the site examination phone call in October 2020.

H. Case File

According to the documentation in the Case File, E&L is an LLC headquartered in the state of Louisiana. (CF, Exh. 11, 244.) E&L is 51% owned by Mr. Esponge and 49% owned by Mr. LeBlanc. (CF, Exhs. 4, 5, 107-109, 118, 138, 139, 178.) Mr. Esponge is a Service-Disabled Veteran. (CF, Exh. 3.) Mr. Esponge is the sole Managing Member and President of E&L. (CF,

Exhs. 256, at 8, 24.) Mr. Esponge and Mr. LeBlanc are the only members of E&L. (CF, Exhs. 256, at 24.)

In response to inquiries from CVE during the October 2020 site visit and E&L's reverification process, Mr. Esponge disclosed a change in control and management of E&L, that "the 49% owner of E&L has been removed as a Manager and Vice President and is strictly just an owner." (*Id.*) Mr. Esponge works full-time for E&L. (CF, Exh. 256, at 4.)

The Case File includes copies of five operating agreements,[4] as most recently amended on September 17, 2018. (CF, Exhs. 10, 45, 128, 186, 198, 248.)

I. 2020 Operating Agreement[5]

E&L's 2020 Operating Agreement was executed on and effective as of April 30, 2020. This Agreement amends and reinstates the 1st Amended and Restated Agreement in full. (2020 Operating Agreement, at 1.)

Under Article 3, Management, § 3.1 states that E&L will have one manager who may also be a member of E&L, and Mr. Esponge is appointed the manager (Manager). (*Id.*, at 6.) § 3.2 further states that within 15 days following bankruptcy, insolvency, resignation, or other removal of a Manager, the remaining Members will call a meeting of the Members to elect a successor Manager. (*Id.*) The meeting will be held within 15 days after notice of the meeting at the principal office of E&L. The successor Manager will be elected upon the vote of Members holding 65% of the ownership interests. (*Id.*)

The Authorities of Manager are set out at § 3.3. It provides he will be the principal executive officer of E&L, will supervise and control all of the business of E&L and will send all required notices to Members. (*Id.*) The Manager, acting alone, will have authority to transact all business of E&L. The Manager may undertake:

> a) Expend the capital and revenues of the Company in furtherance of the Company's business;
>
> b) Enter into and execute, for and on behalf of the Company, such agreements, documents and instruments as the Manager deems necessary and/or appropriate to complete the transactions and arrangements contemplated by and/or described in this Agreement and to further the business of the Company;

---

[4] E&L executed five operating agreements that were in effect prior to the dates that OHA must examine E&L's eligibility. Despite Protestor's allegations related to these operating agreements, OHA finds them irrelevant as to the eligibility period, further discussed in the decision, *infra*. 13 C.F.R. § 134.1003(d)(1).

[5] On May 21, 2021, E&L submitted a response to the protest, along with the 2020 Operating Agreement marked as Exhibit B.

c) Open, maintain, and close bank accounts and disburse any money of the Company, including without limitation draw checks and other orders;

d) Borrow money from banks, other lending institutions or persons for Company purposes;

e) Acquire real or personal, movable or immovable, tangible or intangible property in the name of the Company, by purchase, lease, exchange, giving in payment or otherwise;

f) Execute any mortgage, encumbrance, pledge, hypothecation or other security device, and prepay, in whole or in part, refinance, increase, modify, consolidate or expend any mortgage, encumbrance, pledge, hypothecation or other security device;

g) Employ, at the expense of the Company, consultants, accountants, attorneys, brokers, management companies, escrow agents, and other professionals as the Manager deems necessary or desirable;

h) Refinance any portion or all of the debt of the Company;

i) Bring or defend, pay, collect, compromise, arbitrate, resort to legal action, or otherwise adjust claims or demands of or against the Company;

j) Lease, sell, exchange, or otherwise dispose of Company Property;

k) Purchase, at the expense of the Company, liability and other insurance and bonds to protect the Manager, the Company and the Company's property and business;

l) The adoption of a plan to liquidate or dissolve the Company; and

m) Any voluntary action that would cause a bankruptcy of the Company.

. . .

(*Id.*)

The Manager may delegate some or all of the duties and powers of their office to other persons. (*Id.*, § 3.4.) The Manager who delegates the duties or powers of an office remains subject to the standard of conduct for a Manager with respect to the discharge of all duties and powers so delegated. (*Id.*)

In terms of Restriction of Transfer, § 6.1 provides that:

a) No part of a Member's Ownership Interest Ownership Interest may be sold, exchanged, transferred, assigned, or alienated, whether voluntarily or by operation

of law, or by gift or otherwise, without the consent of the Manager, except through a transfer which meets the requirements of this Article 6. Any purported transfer in violation of any provision of this Article 6 will be void and ineffectual and will not operate to transfer any interest or title to the purported transferee.

The Agreement also includes § 6.2 Right of First Refusal.

a) If at any time a Member (the "Proposed Transferor") desires to sell for value all or any part of his Ownership Interest pursuant to a bona fide offer from a third party (the "Proposed Transferee"), the Proposed Transferor will submit a written offer (the "Offer") to sell the Ownership Interest (the "Offered Ownership Interest") to the Company on terms and conditions, including price, not less favorable to the Company than those on which the Proposed Transferor proposes to sell the Offered Ownership Interest to the Proposed Transferee. . .

b) If the Company desires to purchase all or any part of the Offered Ownership Interest, the Company will communicate in writing to the Proposed Transferor its election to purchase, which communication will state the number of Offered Ownership Interest that the Company desires to purchase and will be given to the Proposed Transferor within 30 days of the date the Company received the Offer
. . .

c) If the Company does not purchase all of the Offered Ownership Interest, the Proposed Transferor will submit a similar written offer (the "Second Offer") to sell that percentage of Offered Ownership Interest not purchased by the Company pursuant to this Section 6 (the "Remaining Offered Ownership Interest") to the other Members on terms and conditions, including price, not less favorable to the Members than those on which such Proposed Transferor proposes to sell such Offered Ownership Interest to the Proposed Transferee. Each other Member will have the absolute right to purchase that percentage of Remaining Offered Ownership Interest that is equal to the number of Remaining Offered Ownership Interest multiplied by a fraction, the numerator of which is the percentage of Ownership Interest then owned by the Member and the denominator of which is the aggregate percentage of Ownership Interest then owned by all Members other than Proposed Transferor. . .

. . .

g) The rights of first refusal provided in this Section 6.2 shall not apply with respect to sales of Ownership Interest by a Member to an Affiliate of such Member, to the Company or to other Members.

(*Id.*, at 10-11.)

§ 6.5 designates Assignees as:

a) Any Person acquiring an interest in the Company by bequest or inheritance or by a transfer permitted by this Article 6 will not become a substituted Member unless and until the conditions of Article 7 have been complied with.

b) Except as otherwise set forth herein, the death, interdiction, dissolution, seizure of an interest in the Company or bankruptcy of a Member will not result in a cessation of that Member's interest in the Company but will effectuate an assignment of that Member's interest to its successor in interest who will not become a substituted Member unless and until the conditions of Article 7 have been complied with; provided, however, that each of such transferees will be allocated the percentage of Company capital, profits, gains, depreciation deductions, losses and Net Cash Flow attributable to the interest in the Company transferred to him or it and will otherwise be treated as a partner for Federal and Louisiana income tax purposes and for purposes of the distribution of cash or other assets to him or it upon the dissolution of the Company pursuant to the Articles and this Agreement.

c) No Member or Assignee of any Member will have the right or power to receive any distribution of its interest in the Company upon his or its cessation as a Member or Assignee, notwithstanding the provisions of La. R. S. 12:1325 or any other provision of applicable law. In the event the preceding sentence is finally determined by a court of proper jurisdiction to be unenforceable, unlawful, or invalid, the amount to be paid will be equal to the Capital Account balance of the Member at the time of his or its cessation as reflected on the books of the Company.

d) No Member may retire or withdraw from the Company without the prior written approval of Members holding 100% of the Ownership Interests.

(*Id.*, at 14.)

§ 6.7 Redemption of Interest of Member consists of:

a) Prior to 180 days before the filing by any Member of a petition for voluntary bankruptcy under Chapter 7 of Title 11 of the United States Code, that Member will give written notice thereof to the Company and will convey to the Company that Member's entire right, title and interest in and to the Company and the Company will purchase same for cash equal to the greater of (i) that Member's positive Capital Account balance on the date of the conveyance (if any), or (ii) $100.

b) In the event the Member fails to give notice to the Company as provided in Section 6.2(a) and in the event a voluntary or an involuntary bankruptcy under Chapter 7 is instituted by or with respect to that Member, the interest of that Member in the Company will be deemed for all purposes to have been sold to the Company 180 days prior to the date on which the voluntary or involuntary bankruptcy or reorganization proceeding is instituted, for cash equal to the greater

> of (i) the positive Capital Account balance of that Member as of 180 days prior to the institution of those proceedings, or (ii) $100. The amount of cash will be paid to that Member's legal representative in those proceedings.

(*Id.*, at 15.)

> § 6.10 Purchase Option by Company:
>
> a) In the event a Member has i) been indicted or convicted of any felony, ii) except at arm's length, has committed self-dealing acts without the written consent of the Members, iii) has committed fraudulent acts, iv) has committed a material breach of this Agreement or any consulting, employment or other agreement with the Company; or v) terminated any consulting, employment or other agreement with the Company for any reason (each an "Involuntary Transfer Event"), the remaining Members will have the right to cause the Company to acquire some or all of the Member's Ownership Interest under the terms and conditions set forth in this Section 6.10. If the Company desires to purchase some or all of the Member's Units, the Company will deliver a written notice of its election to the Member within 60 days after the Involuntary Transfer Event, which communication will state the number of Units that the Company desires to purchase. Sale of the Units to be sold to the Company will be made at the office of the Company on the 90th day after the Involuntary Transfer Event (or if such 90th day is not a business day, then on the next succeeding business day).
>
> b) The purchase price for a Member's Ownership Interest purchased under this Section 6.10 will be the Fair Market Value of the Units as of the Determination Date. The Determination Date for purposes of this section will be the date of the Involuntary Transfer Event.
>
> . . .

(*Id.*, at 16.)

> Finally, § 11.10 Amendments states:
>
> Except as otherwise provided, this Agreement may not be amended, changed or modified in any respect without the affirmative vote of Members holding 100% of the Ownership Interests. Notwithstanding the foregoing, the Manager may modify or amend this Agreement so long as such modification or amendment does not affect the economic interest of any party hereto, and any such modification or amendment to this Agreement shall be binding on all Members.

(*Id.*, at 22.)

III. Discussion

A. Burden of Proof

As the protested firm, E&L has the burden of proving its eligibility by a preponderance of the evidence. 13 C.F.R. § 134.1010.

B. Dates to Determine Eligibility

In a CVE Protest pertaining to a procurement, OHA determines the eligibility of the protested concern as of two dates: (1) the date of the bid or initial offer including price, and (2) the date the CVE Protest was filed. *See* 13 C.F.R. § 134.1003(d)(1). Here, E&L submitted its bid on April 22, 2021, and the instant protest was filed on April 29, 2021. Section II.C, *supra*. Therefore, OHA must examine E&L's eligibility as of these dates, using the substantive ownership and control regulations in effect on each date.

Effective December 30, 2019, SBA added new language to its ownership and control regulations at 13 C.F.R. part 125, which also apply to SDVOSB procurements conducted by VA. In this case, both the date of the bid and the date of the CVE Protest are after the effective date of the new ownership and control regulations and, therefore, these new regulations apply to the substantive issues in this case.

C. Analysis

To be considered an eligible SDVOSB, a concern must be a small business that is unconditionally owned and controlled by one or more Service-Disabled Veterans. 38 C.F.R. § 74.2(a); 13 C.F.R. §§ 125.12 and 125.13; *CVE Protest of Blue Cord Design and Construction, LLC*, SBA No. CVE-100-P (2018). The control requirements for SDVOSBs are found at 13 C.F.R. part 125. *See* 38 C.F.R. § 74.4, "[c]ontrol is determined in accordance with 13 C.F.R. part 125.

Protestor's principal argument is that E&L is not fully controlled by a Service-Disabled Veteran because it is substantially dependent on a non-veteran. Specifically, Protestor alleged that E&L cannot exercise independent business judgment without great economic risk because Mr. LeBlanc has an equity interest in E&L and serves as an officer of Patriot, E&L's office is co-located with Patriot, and the two concerns are parties to a lease and loans between them. Sections II.C and II.G, *supra*. However, E&L has shown that Patriot's Marine Division is merely a tenant, leasing an office in E&L's commercial building and paying rent based on square footage. Section II.D, *supra*. Additionally, Mr. LeBlanc has a 13.6% ownership interest in Patriot with no managing role in E&L's day-to-day operations and decisions. Sections II.D, II.H, and II.I, *supra*. E&L's promissory notes to Mr. LeBlanc are paid off, and the loans to Mr. Esponge and LeBlanc Lease are proportionate to the member's respective ownership interest in the company. *Id.* Contrary to Protestor's arguments, the alleged points lack factual or legal substance, and thus, I find that E&L can exercise independent business judgment without economic risk.

In its Supplemental Protest, Protestor made further arguments that E&L never met the SDVOSB requirements because E&L had five versions of the operating agreement dating back to 2016 and 2018 with impermissible conditions on the Service-Disabled Veteran's ownership and control of the company. These arguments are irrelevant at this juncture. The dates as of which OHA must determine E&L's eligibility as an SDVO SB are the date the concern submitted its bid for the instant proposal, April 22, 2021, and the date of the protest, April 29, 2021. These are the relevant dates for this protest, and the five operating agreements which were no longer in effect as of those dates have no bearing on this case. E&L had unequivocally executed the 2020 Operating Agreement, and it took effect on April 30, 2020. Therefore, any prior operating agreement was no longer in effect as of that date, and they are consequently irrelevant for this protest. Similarly, Protestor's argument on the fact E&L had neglected to submit the latest Operating Agreement to the CVE's case file somehow renders E&L ineligible is baseless. E&L has explained its clerical error in filing, and the regulation does not provide that the absence of the Operating Agreement renders a concern ineligible. The relevant Operating Agreement is before OHA, and the decision will be based upon that.

However, the remaining issue of ownership of E&L by a non-veteran, raised by Protestor in its Supplemental Protest, must be addressed. Protestor argues that the 2020 Operating Agreement has impermissible clauses limiting the SDV's ownership and control. Protestor is permitted to raise new argument after its review of the administrative record. 13 C.F.R. § 134.1007(e).

The regulations require that an SDVO SB must be at least 51% unconditionally and directly owned by one or more Service-Disabled Veterans. 13 C.F.R. § 125.12. In *In the Matter of Wexford Group International, Inc.*, SBA No. SDV-105, at 6 (2009), OHA addressed the issue of what constituted unconditional ownership:

> In the context of 13 C.F.R. § 125.9, unconditional necessarily means there are no conditions or limitations upon an individual's present or immediate right to exercise full control and ownership of the concern. Nor can there be any impediment to the exercise of the full range of ownership rights. Thus, a service-disabled veteran: (1) Must immediately and fully own the company (or stock) without having to wait for future events; (2) Must be able to convey or transfer interest in his ownership interest or stock whenever and to whomever they choose; and (3) Upon departure, resignation, retirement, or death, still own their stock and do with it as they choose. In sum, service-disabled veterans must immediately have an absolute right to do anything they want with their ownership interest or stock, whenever they want.

Wexford, at 6.

OHA has consistently applied the *Wexford* standard. In *Matter of Veterans Contracting Group, Inc.*, SBA No. VET-265 (2017), OHA explicitly rejected the Court of Claims reasoning in *Miles* and *AmBuild*, because those cases were based upon a different Department of Veterans Affairs regulation. OHA's definition was upheld in *Veterans Contracting Group, Inc. v. United States*, 135 Fed. Cl. 316, 321 (2017). The court found that although it felt that *Wexford*

"produces draconian and perverse results in a case such as this one," it had to uphold OHA's interpretation of the regulation. *Veterans Contracting*, at 328.

In 2018, the regulations were amended to further define unconditional ownership:

> *Unconditional ownership* means ownership that is not subject to conditions precedent, conditions subsequent, executory agreements, voting trusts, restrictions on or assignments of voting rights, or other arrangements causing or potentially causing ownership benefits to go to another (other than after death or incapacity). The pledge or encumbrance of stock or other ownership interest as collateral, including seller-financed transactions, does not affect the unconditional nature of ownership if the terms follow normal commercial practices and the owner retains control absent violations of the terms.

13 C.F.R. § 125.11.

Thus, SBA later defined unconditional ownership at 13 C.F.R. § 125.11, adding the exceptions for death, incapacity, and pledges of stock as collateral if the terms follow normal commercial practices, but did not otherwise disturb the *Wexford* definition. 83 Fed Reg. 48908, 48909 (Sep. 28, 2018). OHA has further held that provisions of an Operating Agreement dealing with the bankruptcy of an owner do not render that ownership conditional. *Matter of Veterans Contracting Group, Inc.*, SBA No. VET-265, at 8 (2017).

The definition of unconditional ownership is therefore clear. The Service-Disabled Veteran's ownership of the challenged concern must be unlimited, with no restrictions whatever on their ownership, or their ability to dispose of their chares in anyway they choose. The exceptions are agreements dealing with the death, incapacity or bankruptcy of a shareholder, and the pledge of stock as collateral if the terms follow normal commercial practices. It is important to note that the exception the regulation carves out for "normal commercial practices" is limited to provisions involving the pledge of an ownership interest as collateral.

Limitations on an owner's right to sell or mortgage their interest, on who they might sell their interest to, and rights of first refusal by the concern to purchase an ownership interest all cause a concern to fail the unconditional ownership test. *Matter of Alog Corp.*, SBA No. VET-285, at 14 (2020). Relying on *Alog*, E&L pointed out that OHA did not hold a first right of refusal to be in violation of the regulations. Section II.G, *supra*. However, E&L's interpretation of *Alog* is simply wrong, as *Alog* does hold that a right of first refusal is a provision which renders ownership conditional.

E&L argued that OHA's holding in *Carntribe-Clement 8AJV#l, EA Engineering, Sci., Tech., Inc.*, and *Southern Contracting Solutions III, DHS Systems*, and *Dooleymack Government Contracting*, that certain normal commercial practices are exceptions to ownership in the context of size appeal, should apply in this case. *Id.* However, the regulations governing SDVOSB are clear about "ownership" and "exceptions," and do not allow for the type of provisions which can be characterized as the protection of minority investment in these size appeal cases, *supra*.

In the alternative, E&L argues that the adoption of 13 C.F.R. § 125.11 supersedes the *Wexford* standard, and that OHA should reconsider its rejection of the *AmBuild* and *Miles* precedents. Section II.G, *supra*. E&L then argues that this would permit the finding that any limitation on ownership that followed "normal commercial practices" did not change the unconditional nature of a Service-Disabled Veteran's ownership. However, the regulation includes the broad language in its definition of "unconditional," making clear that there must be no limits on the Service-Disabled Veteran's ownership interest. As already noted, the exceptions the regulation carves out for "normal commercial practices" are limited to provisions involving the pledge of an ownership interest as collateral. Other type of provisions which would cause a Service-Disabled Veteran's ownership to fail the unconditional test are not included.

Applying the regulations to this case, the 2020 Operating Agreement places significant limitations on Mr. Esponge's ownership. His ability to sell his ownership interest is limited by the requirement in § 6.2 that provide a right of first refusal to E&L, and if it elects not to purchase his entire interest, to other members. He may not retire or withdraw from the company, without written approval from other members under § 6.5. There are certain "involuntary transfer events" which require his to transfer his interest to E&L under § 6.10. All of which place significant limitations on Mr. Esponge's ownership of E&L.

Accordingly, I find that E&L is not at least 51% unconditionally owned by a Service-Disabled Veteran, and therefore I must GRANT the protest.

IV. Conclusion

E&L has failed to establish by the preponderance of the evidence that it is an eligible SDVOSB. The protest therefore is GRANTED. This is the final agency action of the U.S. Small Business Administration. 38 U.S.C. § 8127(f)(8)(B); 13 C.F.R. § 134.1007(i).

CHRISTOPHER HOLLEMAN
Administrative Judge