

**United States Small Business Administration
Office of Hearings and Appeals**

SIZE APPEAL OF:

Industrial Support Service, LLC,

Appellant,

Appealed From
Size Determination No. 06-2014-067

SBA No. SIZ-5576

Decided: July 10, 2014

APPEARANCES

James F. Nagle, Esq., Meghan A. Douris, Esq., Oles Morrison Rinker & Baker LLP,
Seattle, WA, for Appellant

DECISION

I. Introduction and Jurisdiction

On May 13, 2014, the U.S. Small Business Administration (SBA) Office of Government Contracting, Area VI (Area Office) issued Size Determination No. 6-2014-067, finding that Industrial Support Service, LLC (Appellant) is not an eligible small business for the U.S. Army Corps of Engineers (USACE) Solicitation No. W9127N-14-R-001 because it exceeded the applicable size standard.

Appellant contends the size determination is clearly erroneous, and requests that SBA's Office of Hearings and Appeals (OHA) reverse the size determination and find Appellant to be a small business for the instant procurement. For the reasons discussed *infra*, the appeal is denied, and the size determination is affirmed.

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

II. Background

A. Solicitation and Protest

On December 20, 2013, USACE issued Solicitation No. W9127N-14-R-001 (RFP) seeking a contractor to provide repair work for the Dalles Lock and Dam Powerhouse Tailrace

Gantry Crane Rehab.

The Contracting Officer (CO) assigned the RFP as a set-aside for small business concerns, and assigned North American Industry Classification System (NAICS) code 238290, Other Building Equipment Contractors, with a corresponding \$14 million annual receipts size standard.

On March 18, 2014, the CO notified all unsuccessful offerors that Appellant had been the successful offeror selected for award. On March 28, 2014, BCI Construction USA, Inc. (BCI) an unsuccessful offeror, filed a protest with the CO, claiming that Appellant was not an eligible small business concern because it was affiliated with K&N Electric Motors, Inc. (K&N), Intermountain Electric, Inc. (IME) and Schmidlkofer Family, LLC (SFL).¹

On April 3, 2014, the Area Office notified BCI that its protest would be dismissed. However, that same day, the Area Office Director notified Appellant that pursuant to 13 C.F.R. § 121.1001(a)(1)(iii), the Director was protesting the small business size status of Appellant.

B. Size Determination

On May 13, 2014, the Area Office issued its size determination finding Appellant is not a small business concern for the solicitation at issue, and its assigned NAICS code.

The Area Office found Mr. John Schmidlkofer is the sole owner of Appellant and owns no interest in K&N or IME. Size Determination at 4. In its response to the protest, K&N submitted federal tax returns showing that its gross receipts for 2010, 2011, and 2012 exceed the \$14 million size standard associated with this solicitation. *Id.* at 5. The Area Office notes Messrs. Gerald Schmidlkofer, Robert Schmidlkofer, Steven Schmidlkofer and Ms. Janet Schmidlkofer own K&N. Mr. Gerald Schmidlkofer is Mr. John Schmidlkofer's father, Messrs. Robert and Steven Schmidlkofer his brothers, and Ms. Janet Schmidlkofer his sister. *Id.*

The Area Office considered IME's organization. IME is owned by the same individuals as K&N. However, IME did not provide any financial information to the Area Office. As a result, the Area Office drew an adverse inference that IME's financial information would not be favorable to Appellant and assumed that IME also exceeds the \$14 million size standard associated with the solicitation at issue. *Id.* The Area Office concluded K&N and IME are affiliated based on their shared ownership.

Next, the Area Office sought to analyze whether Appellant was affiliated with K&N or IME based on familial identity of interest, 13 C.F.R. § 121.103(f). The Area Office noted that in the past, OHA has found there is a rebuttable presumption that family members have identical interests causing them to be treated as one. Because Appellant did not establish that Mr. John Schmidlkofer is estranged from his family, the Area Office proceeded to determine whether Appellant could rebut the presumption of identity of interest by showing there is a minimal, or

¹ The Area Office found that IME is a trade name of SFL, and K&N Industrial Equipment is a trade name of K&N.

no, business relationship between Mr. John Schmidlkofer and his family.

The Area Office states no common management exists between Appellant and K&N and IME. Mr. John Schmidlkofer sold his interest in K&N in 2011 as well as resigned from his role as director and officer. Additionally, Mr. John Schmidlkofer never held any interest in IME, Appellant does not share any facilities, equipment or employees with K&N or IME and Appellant never received any financing or bonding from K&N or IME. *Id.* at 6-7.

However, the Area Office found there are strong economic ties between Appellant and K&N and IME. In 2011, 2012, and 2013, Appellant's sales to K&N represented 89%, 44%, and 34%, respectively, of Appellant's gross sales. *Id.* at 7. In reviewing Appellant's proposal, the Area Office found that over 25% of the contract will be subcontracted to K&N, and an undisclosed portion of it to IME. The Area Office rejected Appellant's arguments that it is not controlled by K&N or IME, and that the concerns operate in different lines of business. The Area Office observed that Appellant and K&N “work together on dam projects similar to the instant contract with [Appellant] doing the electrical work and K&N providing the engineering, manufacturing, fabrication [sic] installation of the equipment.” *Id.* at 8.

Appellant failed to show the Area Office it could rebut the presumption of identity of interest. Further, based on Appellant's failure to provide financial information on IME, the Area Office applied the adverse inference rule and determined IME's financial information would not be in Appellant's favor. The Area Office thus concluded that IME was an other than small business, and that Appellant was affiliated with K&N and IME. The Area Office thus found Appellant was not an eligible small business for this procurement.

C. Appeal Petition

On May 29, 2014, Appellant filed its appeal of the size determination with OHA. Appellant argues the Area Office erred in finding Appellant affiliated with K&N and IME.

Appellant argues the Area Office erred by ignoring factors that show a clear fracture between Appellant and its affiliates. Appeal at 11. Appellant maintains that the minimal business relationship between Appellant and its affiliates is sufficient to show a fracture and rebut the presumption of the identity of interest. *Id.* at 12; citing *Size Appeal of GPA Technologies, Inc.*, SBA No. SIZ-5307 (2011). Appellant states that past OHA decisions have supported the rebuttal of a presumption of identity of interest based on the following factors: “(1) the firms having different facilities; (2) having different locations; (3) being in different lines of business; (4) having different customers; (5) no common ownership interests; (6) no negative or positive control between the concerns; and (7) neither firms giving or receiving any financial, technical, or bid bond assistance from the other. *Id.* at 13; citing *Size Appeal of B.L. Harbert Int'l, LLC*, SBA No. SIZ-4525, at 8 (2002); *Size Appeal of Bob Jones Realty Co.*, SBA No. SIZ- 4059, at 5 (1995); and *Size Appeal of Maria Elena Torano & Assocs.*, SBA No. SIZ-4010 (1995).

Appellant acknowledges it is subcontracting 31% of the instant procurement to K&N, but asserts the Area Office should not have considered this such a major factor because it was the first time Appellant had used K&N as a subcontractor on a government procurement. *Id.* at 14.

Appellant adds that because affiliation is always based on control, the totality of the circumstances here show that neither K&N nor IME have the power to control Appellant.

Appellant argues that the small percentage of Appellant's revenues deriving from its relationship with K&N “offers no basis on which to conclude that one firm can control the other.” *Id.* at 15. Appellant contends Mr. John Schmidlkofer's sale of his interest in K&N in 2011, the absence of his family members among Appellant's owners or managers, the different lines of business between Appellant, K&N, and IME, the separate facilities, and the nonexistent common management or financial assistance establish a clear fracture between the concerns is ignored by the Area Office, which instead focused solely on the 34% of revenues Appellant received from its relationship with K&N. *Id.*

Lastly, Appellant argues the Area Office erred finding Appellant and IME affiliated based on the adverse inference rule. Appellant asserts that its lack of access to IME's financial records, based on having no relationship with IME, allowed it to only provide a contact point at IME in order for the Area Office to obtain the requested information. Appellant states the Area Office did not contact Ms. Janet Schmidlkofer in order to request information on IME. *Id.* at 18. Appellant notes that no financial relationship exists between itself and IME, and that all the documents provided to the Area Office “shows beyond a doubt that there is no affiliation between IME and [Appellant] under the proper totality of the circumstances analysis.” *Id.*

III. Discussion

A. Timeliness and Standard of Review

Appellant filed its appeal on the fifteenth day after its receipt of the Size Determination. Therefore, the appeal is timely. 13 C.F.R. § 134.304(a).²

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

B. New Evidence

OHA's review is based upon the evidence in the record at the time the Area Office made its determination. *Size Appeal of Taylor Consultants, Inc.*, SBA No. SIZ-4775, at 10-11 (2006). As a result, evidence that was not previously presented to the Area Office is generally not admissible and will not be considered by OHA. *E.g.*, *Size Appeal of Maximum Demolition, Inc.*,

² The size determination is dated May 13th, and the appeal recites that Appellant received it on May 13th. The Appeal is dated May 29th, and was filed on that date, which on the face of it would make the appeal untimely. Nevertheless, the Area Office records confirm the Area Office actually transmitted the size determination on May 14th, and so the appeal is timely.

SBA No. SIZ-5073, at 2 (2009) (“I cannot find error with the Area Office based on documents the Area Office was unable to review.”). New evidence may be admitted on appeal at the discretion of the administrative judge if “[a] motion is filed and served establishing good cause for the submission of such evidence.” 13 C.F.R. § 134.308(a). The proponent must demonstrate, however, that “the new evidence is relevant to the issues on appeal, does not unduly enlarge the issues, and clarifies the facts on the issues on appeal.” *Size Appeal of Vista Eng’g Techs., LLC*, SBA No. SIZ-5041, at 4 (2009). Here, Appellant's proffered new evidence is either documentation already in the record, or declarations that could have been submitted to the Area Office, and were not. I therefore EXCLUDE the proffered new evidence.

C. Analysis

Here, the Area Office found Appellant affiliated with K&N and IME based on an identity of interest between family members. The applicable regulation states:

Affiliation may arise among two or more persons with an identity of interest. Individuals or firms that have identical or substantially identical business or economic interests (such as family members, individuals or firms with common investments, or firms that are economically dependent through contractual or other relationships) may be treated as one party with such interests aggregated. Where SBA determines that such interests should be aggregated, an individual or firm may rebut that determination by showing that the interests deemed to be one are in fact separate.

13 C.F.R. § 121.103(f).

In the past, OHA has interpreted this regulation as creating a rebuttable presumption that family members have identical interests and must be treated as one person. *See, e.g., Size Appeal of McLendon Acres, Inc.*, SBA No. SIZ-5222, at 6 (2011); *Size Appeal of US Builders Group*, SBA No. SIZ-5519 (2013); *Size Appeal of Knight Networking & Web Design, Inc.*, SBA No. SIZ-5561 (2014). In these types of cases, the common interests are viewed as causing the parties to act in unison, and thus should be treated as one person. *Size Appeal of DooleyMack Govt. Contracting, LLC*, SBA No. SIZ-5085, at 6 (2009). Nonetheless, the challenged firm can rebut the presumption of identity of interest by showing there is “a clear line of fracture among the family members.” *Size Appeal of Carwell Products, Inc.*, SBA No. SIZ-5507, at 8 (2013) (citing *Size Appeal of Tech. Support Servs.*, SBA No. SIZ-4794, at 17 (2006)). This fracture may exist when the family members have no business relationship or involvement with each other's business concerns, or if the family members are estranged. *Id.*; *Size Appeal of Hal Hays Constr., Inc.*, SBA No. SIZ-5217, at 6 (2011). Additionally, OHA has stated “that a minimal amount of business or economic activity between two concerns does not prevent a finding of clear fracture.” *Id.*; citing *RBG Group, Inc.*, SBA No. SIZ-5351, at 7 (2012). Some of the factors to consider in examining whether a clear line of fracture exists includes: whether the firms share officers, employees, facilities, or equipment; whether the firms have different customers and lines of business; whether there is financial assistance, loans, or significant subcontracting between the firms; and whether the family members participate in multiple businesses together. *Size Appeal of GPA Techs.*, SBA No. SIZ-5307, at 8-10 (2011); *Hal Hays*, SBA No.

SIZ-5217, at 6-7; *Size Appeal of Jenn-Kans, Inc.*, SBA No. SIZ-5114, at 8 (2010); *McLendon Acres*, SBA No. SIZ-5222, at 6; *Size Appeal of Grantco Pacific, Inc.*, SBA No. SIZ-5205, at 5 (2011).

In this case, the Area Office determined there was no clear fracture between Mr. John Schmidlkofer and the concerns owned by his father and siblings, K&N and IME. The Area Office found that because Appellant and K&N's business relationship over the years 2011-2013 accounted for 89%, 44%, and 34%, respectively, of Appellant's gross sales, no clear fracture existed to rebut the presumption of affiliation. In addition, Appellant acknowledges it will be subcontracting 31% of the instant procurement to K&N. This is a significant portion of the contract, and it demonstrates that Appellant and K&N have a significant business relationship. Based on these facts, the Area Office could reasonably determine Appellant had not shown that a clear line of fracture existed between itself and K&N. Appellant failed to show there was no considerable business involvement between Appellant and K&N. This relationship continues to exist today based on the 31% of the work K&N is scheduled to subcontract for the instant procurement.

The situation here is analogous to the one found in *Knight Networking & Web Design, Inc.*, SBA No. SIZ-5561 (2014). In *Knight*, OHA found that where the protested concern derived at least 22.67% of its revenues, as well as a plan to subcontract 16% of the procurement at issue, from its affiliate, which was owned by a family member, the protested concern did not establish a clear fracture to rebut the presumption of affiliation. *Knight Networking & Web Design, Inc.*, SBA No. SIZ-5561, at 6 (2014). Further, *Size Appeal of RGB Group, Inc.*, SBA No. SIZ-5351 (2012) found that where a challenged firm and its alleged affiliate are owned by family members, and the challenged concern plans on subcontracting 25% of the procurement at issue, that fact was "by itself, arguably sufficient to find no clear line of fracture," even if no other business ties had been shown. *RGB*, SBA No. SIZ-5351, at 7. Here, Appellant is planning on subcontracting over 25% of the instant procurement to K&N, but also has been depended on K&N for at least 34% of its revenues between 2011-2013. Appellant attempts to argue the situation here is in line with *Size Appeal of GPA Techs., Inc.*, SBA No. SIZ-5307, at 6 (2011), where OHA failed to find affiliation based on a familiar identity of interest. However, in *GPA Techs., Inc.*, the challenged firm and its alleged affiliate had a very minimal business relationship, with one subcontract representing less than 5% of the challenged firm's revenues, and less than 1% of the alleged affiliate's revenues.

Next, Appellant maintains the Area Office erred by not focusing its affiliation inquiry into whether K&N had the power to control Appellant. This argument is one previously considered by OHA in similar situations. However, as in the past, OHA has stated the regulation creates the presumption of an identity of interest between family members which arises "not from the degree of family members' involvement in each other's business affairs, but from the family relationship itself." *Size Appeal of SP Tech., LLC*, SBA No. SIZ-5319, at 5 (2012); *Size Appeal of Trailboss Enterprises, Inc.*, SBA No. SIZ-5564 (2014). Thus, "concerns owned by close family members are presumed affiliated, and the burden then shifts to the challenged firm to rebut that presumption." *Knight Networking & Web Design, Inc.*, SBA No. SIZ-5561, at 6 (2014).

Lastly, Appellant attempts to argue the Area Office improperly found Appellant and IME affiliated based on the adverse inference rule. Based on federal tax returns provided to the Area Office, K&N exceeds the \$14 million size standard associated with this solicitation. Appellant is therefore other than small solely on the basis of its affiliation with K&N. I therefore need not consider Appellant's argument that the Area Office erred in drawing an adverse inference in finding IME to be an other than small business.

Appellant has therefore failed to meet its burden of proving that the size determination was based on an error of fact or law. Accordingly, I must deny the instant appeal.

IV. Conclusion

Appellant has not demonstrated that the size determination is clearly erroneous. Accordingly, the appeal is AFFIRMED, and the size determination is DENIED. This is the final decision of the Small Business Administration. *See* 13 C.F.R. § 134.316(d).

CHRISTOPHER HOLLEMAN
Administrative Judge