

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

REDACTED DECISION FOR PUBLIC RELEASE

SIZE APPEAL OF:

Core Recoveries, LLC,

Appellant,

Appealed From
Size Determination No. No. 3-2016-022

SBA No. SIZ-5723

Decided: March 21, 2016

APPEARANCES

Antonio R. Franco, Esq., Alexander O. Levine, Esq., PilieroMazza PLLC, Washington, D.C., for Appellant

DECISION¹

I. Introduction

On January 5, 2016, the U.S. Small Business Administration (SBA) Office of Government Contracting, Area III (Area Office) issued Size Determination No. 3-2016-022 concluding that Core Recoveries, LLC (Appellant) is not a small business under the size standard associated with Appellant's primary industry. The Area Office specifically determined that Appellant is affiliated with West Asset Management, Inc. (West) through economic dependence, 13 C.F.R. § 121.103(f). Appellant maintains that the size determination is clearly erroneous, and requests that the SBA Office of Hearings and Appeals (OHA) reverse. 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

¹ This decision was originally issued under the confidential treatment provision of 13 C.F.R. § 134.205. OHA received one or more requests for redactions and considered any requests in redacting the decision. OHA now publishes a redacted version of the decision for public release.

fifteen days after 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. Procedural History

On November 19, 2015, the Area Office, acting on an anonymous complaint, informed Appellant that it would investigate Appellant's size "on the belief that [Appellant] may be other than small because of [Appellant's] affiliation with [West], a large company." (Protest at 1, citing 13 C.F.R. § 121.1001(b)(9).) The Area Office observed that, in the System for Award Management, Appellant represented itself as a small business for North American Industry Classification System (NAICS) code 561440, Collection Agencies. (*Id.*)

On December 4, 2015, Appellant responded to the protest and submitted its completed SBA Form 355 and other supporting documents and information. Appellant denied affiliation with West on any grounds, stating:

[Appellant] is a national collection agency licensed in every jurisdiction in the United States. [Appellant] maintains 21 full- time staff members, its own collection system, dialer, letter vendor, and compliance management system. [Appellant] currently has [XXX] active clients, with over 150,000 debtor accounts assigned and loaded on our collection system. As of the date of this inquiry, November 19, 2015, West maintained only 1,616 accounts with [Appellant], which represented only 1.1% of [Appellant's] total account volume on that date. Additionally, as of the date of your letter, and through the date of this response, [Appellant] does not have an active contract with West.

(Protest Response at 1.)

Appellant highlighted that West holds no ownership or managerial interest in Appellant. (*Id.* at 2.) With regard to Appellant's business dealings with West, Appellant stated that:

[I]n August 2011, [Appellant] signed a contract with West (as a Department of Education subcontractor) and four months after that, in December 2011, [Appellant] received its first account placements from West. [Appellant's] active contract with West ended when the Department of Education canceled its contract with West in February 2015. [Appellant] is currently in the process of onboarding two new large clients (both are separate Department of Education subcontracting agreements), neither of which is affiliated with West.

(*Id.*)

In response to a subsequent inquiry from the Area Office, Appellant acknowledged that it had derived more than 90% of its receipts from its subcontract with West during fiscal years

2012, 2013, and 2014. (E-mail from L. Korn to T. Rogers (Dec. 17, 2015).) West represented a lesser proportion of Appellant's receipts during 2015, although still more than 70%. (*Id.*)

B. Size Determination

January 5, 2016, the Area Office issued Size Determination No. 3-2016-022 concluding that Appellant is affiliated with West through economic dependence.

The Area Office explained that the date to determine Appellant's size is November 19, 2015 — the date of the Area Office's protest letter — and proceeded to analyze Appellant's receipts for fiscal years 2012, 2013, and 2014. The Area Office found that “[d]uring fiscal years of 2012, 2013, 2014 [Appellant] earned 99.6 percent, 99.8 percent, and 94.16 percent of [its] annual receipts from West respectively.” (Size Determination at 4.) Under long-standing OHA precedent, concerns are affiliated through economic dependence when one depends on the other for 70% or more of its revenue. (*Id.*, citing *Size Appeal of Faison Office Prods., LLC*, SBA No. SIZ-4834 (2007).) Because Appellant derived more than 70% of its revenues from West during 2012, 2013, and 2014, the Area Office concluded that Appellant is economically dependent upon, and affiliated with, West. (*Id.*)

As a “further point of interest”, the Area Office noted that Appellant “reported receipts for 2015 that show that [Appellant] earned 74 percent of [its] income from West.” (*Id.*) Even during 2015, then, Appellant's revenues from West “would still be over the threshold established by the *Faison* case of 70 percent.” (*Id.*)

In reaching its decision, the Area Office did not give weight to Appellant's contentions that Appellant no longer has a contract or subcontract with West, and that Appellant's business dealings with West had declined since February 2015. The Area Office reasoned that, because the date to determine size is November 19, 2015, the only relevant years are 2012, 2013, and 2014, and any “future projections of income from West are not applicable to the size evaluation at this time.” (*Id.*)

The Area Office found that Appellant alone is a small business. (*Id.*) However, once Appellant's receipts are combined with those of West, Appellant exceeds the \$15 million size standard for NAICS code 561440.

C. Appeal

On January 20, 2016, Appellant filed the instant appeal. Appellant argues that the Area Office incorrectly determined that Appellant is economically dependent upon West.

Appellant contends that the Area Office mechanically applied the *Faison* 70% rule by computing the percentage of Appellant's revenues that historically were attributable to West, but failing to consider that the situation could have changed significantly as of the date to determine size, November 19, 2015. In particular, as Appellant informed the Area Office, Appellant's active subcontract with West ended in February of 2015, when the U.S. Department of Education terminated West's prime contract. (Appeal at 5.) Consequently, as of November 19, 2015, there

was no longer a contractual relationship between Appellant and West, and Appellant's business dealings with West were “effectively over.” (*Id.*) Appellant emphasizes that, as of the date to determine size, Appellant had [XXX] active clients and approximately 150,000 accounts, with West representing only 1.1% of Appellant's account volume. (*Id.* at 6.) Although Appellant continued to derive revenues from West as of November 19, 2015, “the contract with West was not active as of then and the only receipts being received were from accounts receivable from previous activity.” (*Id.* at 11.)

Appellant points to *Size Appeal of OBXtek, Inc.*, SBA No. SIZ-5451 (2013) in arguing that the Area Office should have considered whether Appellant was economically dependent upon West as of November 19, 2015. The key issue, Appellant asserts, “is whether, at the specific date upon which size is to be determined, an alleged affiliate actually controlled, or had the power to control, the protested concern.” (*Id.* at 7, emphasis in original.) Here, the Area Office focused on the past dealings between Appellant and West, but “rejected, out of hand, any consideration of [Appellant's] statements regarding what had happened in 2015, *e.g.*, the fact that West and [Appellant] no longer had an active contract.” (*Id.* at 9, emphasis in original.) As a result of this flawed reasoning, the Area Office was unable to “come up with a plausible explanation regarding how West can control [Appellant] through the mechanism of a terminated contract.” (*Id.* at 12.)

Appellant next argues that the Area Office improperly disregarded the fact that Appellant was a newly formed business when it first entered into its subcontract with West. OHA has recognized that mechanical application of the 70% rule unduly penalizes startup concerns based on their inability to secure multiple contracts. (*Id.* at 11, citing *Size Appeal of Argus and Black, Inc.*, SBA No. SIZ-5204 (2011) and *Size Appeal of Cherokee Nation Healthcare Services, Inc.*, SBA No. SIZ-5343 (2012).) Therefore, Appellant contends, the Area Office erred by not considering Appellant's status as a newly organized company when assessing whether Appellant was economically dependent upon West.

Appellant emphasizes that it had largely severed its business relationship with West prior to the date to determine size, and has developed “into an independent and strong business in its own right.” (*Id.* at 13.) Accordingly, the Area Office erred in finding economic dependence as of November 19, 2015. (*Id.*)

III. Discussion

A. Standard of Review

Appellant has the burden of proving, by a preponderance of the evidence, all elements of the appeal. Specifically, Appellant must prove that 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. Analysis

Appellant's principal argument is that the instant size determination should be overturned based on OHA's decision in *Size Appeal of OBXtek, Inc.*, SBA No. SIZ-5451 (2013). In *OBXtek*, the area office found affiliation through economic dependence after analyzing the challenged firm's prior three years of receipts (2009-2011). The area office did not, however, consider the relationship between the two companies as it existed on the self-certification date of February 1, 2012. On appeal, OHA explained that “because size is determined as of the self-certification date, a size determination must determine affiliation—in this case, economic dependence—as of that date.” *OBXtek*, SBA No. SIZ-5451, at 10. Although self-certification had occurred only one month after the end of fiscal year 2011, OHA found that the revenues the challenged firm derived from the alleged affiliate had sharply declined during this interval. Specifically, based on evidence submitted by the challenged firm during the size review, OHA found that “[a]s of the self-certification date, twelve of [the challenged firm's] thirteen active contracts were prime contracts with Federal agencies, and the subcontract with [the alleged affiliate] represented just 18.16%, less than one-fifth, of [the challenged firm's] revenues.” *Id.* at 11. Because the challenged firm had proven that it was no longer economically dependent upon its alleged affiliate as of the self-certification date, OHA reversed the size determination.

Appellant correctly observes that, under *OBXtek*, the Area Office should have examined the relationship between Appellant and West as of the date to determine size: November 19, 2015. Insofar as the size determination suggests that the Area Office could only review information through the end of 2014, this was error. On the other hand, the Area Office appropriately considered the fact that Appellant derived more than 90% of its receipts from West during the years before November 19, 2015. As OHA stated in *OBXtek*, “where there is such heavy dependence in the three years preceding the self-certification date, the challenged firm must persuasively demonstrate it is no longer economically dependent on its alleged affiliate, and the alleged affiliate does not have the ability to control the challenged firm.” *OBXtek*, SBA No. SIZ-5451, at 10 (citing *Size Appeal of C2G Ltd. Co.*, SBA No. SIZ-5186 (2011)).

The problem for Appellant here is that, unlike the challenged firm in *OBXtek*, Appellant did not prove that it was economically independent of its alleged affiliate as of the date to determine size. In particular, Appellant failed to submit evidence to the Area Office demonstrating that Appellant derived substantially less than 70% of its receipts from West as of November 19, 2015. On the contrary, Appellant acknowledged in its e-mail of December 17, 2015 — and the Area Office confirmed in the size determination — that West still represented well over 70% of Appellant's receipts during 2015, after having accounted for more than 90% of Appellant's receipts during each of the preceding three years. Sections II.A and II.B, *supra*. Further, while Appellant informed the Area Office that its subcontract with West was no longer “active” after February 2015, Appellant did not explain how a purportedly defunct subcontract might account for so large a proportion of Appellant's 2015 receipts. Based on this record, then, the Area Office could properly conclude that Appellant remained economically dependent upon West as of November 19, 2015.

Appellant argues that West lacked any mechanism to control Appellant in November 2015 because the subcontract between the two companies had become inactive in February 2015.

Again, though, there appears to be no dispute that Appellant continued to derive substantial revenues from West after February 2015. This is consistent with Appellant's e-mail of December 2015 acknowledging that West still comprised more than 70% of Appellant's receipts during 2015. Section II.A, *supra*. OHA has held, as a matter of law, that a firm that derives 70% or more of its revenue from another firm is economically dependent upon that firm. *Size Appeal of Faison Office Prods., LLC*, SBA No. SIZ-4834, at 10 (2007). Further, “a contractual relationship between two concerns with one heavily dependent for its revenues on another is alone sufficient to support a finding of affiliation, even if there are no other ties between the firms.” *Size Appeal of Incisive Tech., Inc.*, SBA No. SIZ-5122, at 4 (2010). Accordingly, given that Appellant apparently continued to be heavily dependent upon West for revenues as of November 19, 2015, the Area Office need not have found any additional means whereby West could control Appellant.

Appellant also argues that because it was a newly formed business in 2011, and the subcontract with West was Appellant's first, the Area Office should not have found economic dependence. This argument is meritless. It is true that OHA has recognized an exception to *Faison* in situations “where the challenged firm has only recently begun operations either initially or after a period of dormancy, and is dependent upon its alleged affiliate for only one small contract of short duration, which by itself could [not] sustain a business.” *Size Appeal of Argus and Black, Inc.*, SBA No. SIZ-5204, at 6-7 (2011). In the instant case, though, Appellant was not a startup business in November 2015, and Appellant's arrangement with West was not a small contract of short duration but rather a multi-million dollar subcontract spanning several years. Under such circumstances, OHA has declined to apply the exception set forth in *Argus and Black*. *Size Appeal of Ma-Chis Project Controls, Inc.*, SBA No. SIZ-5486, at 4 (2013).

IV. Conclusion

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

KENNETH M. HYDE
Administrative Judge