United States Small Business Administration
Office of Hearings and Appeals

SIZE APPEAL OF: Level Access, Inc., Appellant, Appealed From Size Determination No. 02-2018-220	SBA No. SIZ-5939 Decided: July 17, 2018

APPEARANCES

Jeffery M. Chiow, Esq., Lucas T. Hanback, Esq., Stephen L. Bacon, Esq., Rogers Joseph O'Donnell, P.C., Washington, D.C., for the Appellant

Susan Warshaw Ebner, Esq., Sean D. Lee, Esq., Jacqueline R. Scott, Esq., Fortney & Scott, LLC, Washington, D.C., for Deque Systems, Inc.

DECISION[1]

I. Introduction and Jurisdiction

On April 16, 2018, the U.S. Small Business Administration (SBA) Office of Government Contracting, Area II (Area Office) issued Size Determination No. 02-2018-220, concluding that Level Access, Inc. (Appellant) is not a small business. Appellant contends that the size determination is clearly erroneous, and requests that SBA's Office of Hearings and Appeals (OHA) reverse or remand. 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 received the size determination on April 17, 2018, and filed the instant appeal within fifteen days thereafter, so the appeal is timely. 13 C.F.R. § 134.304(a). Accordingly, this matter is properly before OHA for decision.

[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 requests for redactions and considered such requests in redacting the decision. OHA now publishes a redacted version of the decision for public release.

II. Background

A. Solicitation and Protest

On October 6, 2017, the U.S. Department of Veterans Affairs, Technology Acquisition Center, in Eatontown, New Jersey, issued Request for Proposals (RFP) No. VA118-18-R-0143 for Section 508 Accessibility Compliance Scanning and Services. The Contracting Officer (CO) set aside the procurement entirely for small businesses, and assigned North American Industry Classification System (NAICS) code 541512, Computer Systems Design Services, with a corresponding size standard of $27.5 million average annual receipts. Proposals were due October 23, 2017. Appellant and Deque Systems, Inc. (Deque) submitted timely proposals.

On January 18, 2018, the CO announced that Appellant was the apparent awardee. On January 24, 2018, Deque filed a size protest against Appellant with the CO. Deque alleged:

> [Appellant] is a front for and therefore affiliated with Booz Allen Hamilton ("BAH"), its ostensible subcontractor in the procurement, and/or JMI Equity, which has a 40% ownership interest in [Appellant] and is actively involved in its management, and [Appellant] is not eligible for award.

(Protest at 1.) Deque also alleged affiliation with The Carlyle Group through both BAH and JMI Equity. (*Id.* at 5.)

Deque stated it had learned on October 11, 2017 that BAH had teamed with Appellant on this procurement and provided in its protest public information that BAH is a large concern. (*Id.* at 4-5; Encl. 1 (Decl. of [xxx] ¶ 6); Encl. 3 and 4.) Deque provided a press release announcing JMI Equity's strategic growth investment in Appellant. (*Id.* at 6-7 and Encl. 5.) The CO forwarded Deque's protest to the Area Office for review.

B. Protest Response

On February 19, 2018, Appellant responded to the protest allegations and submitted to the Area Office its completed SBA Form 355, its proposal, Federal income tax returns, corporate documents, and other material. Appellant's tax returns for the years 2014 — 2016 show that its average annual receipts do not, by themselves, exceed the applicable $27.5 million size standard.

Appellant assumed its present form as a result of various transactions occurring in April 2017. At that time, JMI Equity Fund VIII-A, L.P. and JMI Equity Fund VIII-B, L.P., two investment funds acting through their common general partner, JMI Associates VIII, L.L.C. (collectively JMI Equity), invested in Appellant. A Capitalization Table shows each shareholder's fully-diluted ownership of Appellant's stock. The largest shareholders are:

JMI Equity	48.2738%
Timothy Springer	30.2820%
Shanti Atkins	[xxx]%

(Capitalization Table printed Feb. 16, 2018; *see also* SBA Form 355, response to question 4.) Except for one other individual, who owns just under 2% of Appellant, all other shareholders own less than [xxx]% of Appellant's stock.

Under Appellant's Stockholders Agreement, the Board of Directors consists of up to two Directors nominated by the Investors, up to two Stockholder Directors nominated by qualifying stockholders other than the Investors, and one Independent Director nominated by the Investors and "reasonably acceptable" to the other qualifying stockholders. (Stockholders Agreement § 5.1.) The term "Investors" is defined as JMI Equity Fund VIII-A, L.P. and JMI Equity Fund VIII-B, L.P. (*Id.* § 1.2.) A quorum for action by the Board of Directors is a majority, including at least one Investor Director and one Stockholder Director. (*Id.* § 5.6.) Any Director may call a meeting with 24 hours' notice to the others. (*Id.*) If there is no quorum at a meeting for failure of at least one Stockholder Director to be present, the Directors who are present may adjourn to another meeting time at least 48 hours later, and at this reconvened meeting a quorum may be established without either Stockholder Director present. (*Id.*) There are currently four Directors on the Board: one Investor Director, two Stockholder Directors, and the Independent Director. (SBA Form 355, response to question 6.)

In its response to Deque's protest, Appellant denied the ostensible subcontractor allegation, arguing that its proposal shows that Appellant will perform two-thirds of the work, including all primary and vital requirements, and that Appellant will manage the effort. (Cover Letter at 1.) Appellant provided detailed argument supporting its position that BAH is not an ostensible subcontractor. (Protest Response at 8-12.)

Regarding The Carlyle Group, Appellant asserted that it is public knowledge that The Carlyle Group once held majority ownership in BAH as part of a "take private" transaction, but has since divested this position. (*Id.* at 7.) Likewise, Appellant argued, Deque's allegation of affiliation between The Carlyle Group and JMI Equity, based on a sale, from the one to the other, of stock in a third company, is meritless. (*Id.* at 8.)

Appellant also denied affiliation with JMI Equity and made several arguments in support of this position. First, Appellant argued, JMI Equity is exempt from affiliation under 13 C.F.R. § 121.103(b) because it is a "venture capital operating company" under 29 C.F.R. § 2510.3-101(d). (*Id.* at 5.) In support, Appellant offered a declaration from a JMI Equity official asserting this status.

Regarding affiliation through stock ownership, Appellant noted that JMI Equity owns less than 50% of Appellant's voting stock on a fully-diluted basis, and maintained that JMI Equity's ownership position is not large compared to other outstanding voting blocks of stock. (*Id.* at 5-7.) More specifically, Appellant claimed that its employees, including Mr. Springer, "own the next largest block of shares, which collectively amount to [xxx]% of the total outstanding shares on a fully diluted basis." (*Id.* at 5.) According to Appellant, the employees "are aligned as a cohesive voting block with common interests." (*Id.* at 5 fn.2.)

As for common management affiliation, Appellant contended that JMI Equity holds only one of Appellant's four filled Board of Director seats. (*Id.* at 5-6.)

C. Size Determination

On April 16, 2018, the Area Office issued Size Determination No. 02-2018-220 concluding that Appellant is not a small business. The Area Office found that Appellant is not in violation of the ostensible subcontractor rule. (Size Determination at 2-5.) In addition, there is no affiliation between Appellant, BAH, and The Carlyle Group. (*Id.* at 5-6.) Turning to the question of affiliation with JMI Equity, the Area Office determined that the exemption from affiliation at 13 C.F.R. § 121.103(b)(5)(i) for venture capital operating companies does not apply here, because Appellant is not seeking assistance under the Small Business Investment Act. (*Id.* at 8.)

Regarding stock ownership, the Area Office rejected the notion that, because JMI Equity owns less than 50% of Appellant, the two concerns cannot be affiliated. (*Id.* at 6.) Further, the Area Office determined, stock owned by individual employee shareholders "is not a block". (*Id.* at 6-7.) The Area Office instead compared JMI Equity's stock ownership with that of the next single largest shareholder, Mr. Springer, and concluded that JMI Equity's ownership is large relative to Mr. Springer's, citing to ratios established in OHA's previous decisions on minority stock ownership. (*Id.* at 7.) Because JMI Equity is deemed to control Appellant through its large minority ownership position, the two companies are affiliated under the size regulations. (*Id.* at 7-8.)

Although the Area Office stated that it need not address the issue of control of Appellant's Board of Directors, it noted that JMI Equity has the voting power to choose three of Appellant's five directors. (*Id.* at 8.) In calculating Appellant's size, the Area Office found that Appellant had provided its own tax returns, but not those of its affiliate JMI Equity. The Area Office therefore drew an adverse inference that the missing information would have shown that Appellant is not a small business under the size standard associated with this procurement. (*Id.* at 9-10.)

D. Appeal

On May 2, 2018, Appellant filed the instant appeal. Appellant contends that the Area Office made two clear errors in its determination. First, in its analysis of stock ownership, the Area Office did not consider the stock of Appellant's employees as a single block under the identity of interest rule in 13 C.F.R. § 121.103(f) and *Size Appeal of MPC Computers, LLC*, SBA No. SIZ-4806 (2006). (Appeal at 8.) Appellant insists that "the employees should have been treated as one party because they are all economically dependent on their employment relationship with [Appellant]." (*Id.* at 9.) Had the Area Office treated the employees as one party and aggregated their interests, the comparison between Appellant's two largest stockholders would have set JMI Equity's 48.27% ownership against the employees' [xxx]% combined ownership (or [xxx]% counting only current employees), rather than against Mr. Springer's individual ownership of 30.27%. (*Id.* at 8-10.) As a result, JMI Equity's block would not have been "large" compared to the next largest block, and there would have been no affiliation through stock ownership. (*Id.*)

Second, in applying an adverse inference against Appellant, the Area Office erred in not first having made a specific request that Appellant produce the desired information. (*Id.* at 10-11.) This omission was prejudicial, Appellant maintains, because the combined average annual receipts of Appellant and JMI Equity are below the applicable $27.5 million size standard. (*Id.* at 11.) Appellant points to, on the one hand, the Form 355 instructions, which require the protested concern to submit information on alleged affiliates within a tight timeframe and, on the other hand, the "vaguely-defined legal standard" for determining who these affiliates are based on stock ownership, citing to *Size Appeal of Forterra Systems, Inc.*, SBA No. SIZ-5029, at 8 (2009), where OHA had made a similar observation. (*Id.* at 12-13.) In any event, it is improper to apply an adverse inference before the additional information is requested. (*Id.* at 15.)

As relief, Appellant asks that OHA reverse the size determination and conclude Appellant is a small business for this procurement, or remand the matter to the Area Office for further review and a new size determination. (*Id.* at 8.)

E. Deque's Response

On May 23, 2018, Deque responded to the appeal. Deque argues that there is no identity of interest among Appellant's employees beyond their association with Appellant, and thus no basis for treating the stock of Appellant's employees as a unified block when analyzing stock ownership. (Response at 7-8, citing *Size Appeal of [Drug Applicant]*, SBA No. SIZ-5362 (2012).) Therefore, the Area Office correctly compared JMI Equity's stock holding to that of the next largest stockholder, Mr. Springer, and correctly found that, because JMI Equity's holding is large relative to Mr. Springer's, JMI Equity controls Appellant through stock ownership. (*Id.* at 8-10.) According to Deque, Appellant's affiliation with JMI Equity, although clearly established through stock ownership, is also clearly established through JMI Equity's control of Appellant's Board of Directors. (*Id.* at 4-5.)

Regarding the Area Office's application of an adverse inference against Appellant, Deque contends that Appellant had sufficient notice to submit JMI Equity's information, citing instructions on the SBA Form 355, which require the protested concern to provide information on all affiliates "whether acknowledged or not". (*Id.* at 15.) Further, Deque's protest clearly alleged affiliation with JMI Equity and thus Appellant should have provided the required information on JMI Equity. (*Id.* at 12-13.) Instead, Appellant assumed the risk of an adverse inference by not producing the information. (*Id.* at 17.)

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 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

Having reviewed the record and the arguments of the parties, I agree with Deque that Appellant has not shown clear error in the size determination. As a result, this appeal must be denied.

Appellant's principal argument on appeal is that the Area Office should have found that Appellant's employees share an identity of interest under 13 C.F.R. § 121.103(f), and should have treated the employees' stock as a single block, separate from the JMI Equity block, based on OHA's decision in *Size Appeal of MPC Computers, LLC*, SBA No. SIZ-4806 (2006). Appellant's argument, though, is unpersuasive for two reasons.

First, the instant case bears little similarity to *MPC Computers*. The challenged firm in *MPC Computers* submitted evidence, including a declaration from the company's President, establishing that the company's managers shared an identity of interest through their "long association and common goals under difficult circumstances". *MPC Computers*, SBA No. SIZ-4806, at 7-8. Further, there was an adversarial relationship between certain shareholders in *MPC Computers*, which contributed to the finding of discrete shareholder blocks. *Id.* Conversely, in the instant case, Appellant presented no evidence, beyond mere assertion, to support its claim of an identity of interest among Appellant's employees. *See* Section II.B, *supra*. The absence of supporting evidence is problematic for Appellant because, as the challenged firm, it was Appellant's responsibility to convince the Area Office that Appellant is a small business. 13 C.F.R. § 121.1009(c). Moreover, unlike the challenged firm in *MPC Computers*, Appellant here offered no rationale for treating Appellant's employees as a separate block apart from Appellant's other shareholders. Section II.B, *supra*. Notably, the identity of interest regulation, 13 C.F.R. § 121.103(f), does not contemplate that an identity of interest will arise merely because individuals share a common employer.

Second, even if Appellant could show that the instant case is analogous to *MPC Computers*, more recent OHA decisions have distinguished *MPC Computers* and significantly narrowed its scope with regard to the issue of identity of interest. In *Size Appeal of Cypress Pharmaceutical, Inc.*, SBA No. SIZ-5078, at 5 (2009) (PFR), OHA concluded that "the identity of interest analysis in *MPC Computers* was merely dicta", and warned that "litigants appearing before OHA should not rely on [*MPC Computers*]" because "it is unlikely that the identity of interest analysis in that case will apply to any future case." OHA further explained that "[t]he identity of interest rule [in *MPC Computers*] is only applicable where there is evidence that the parties whose shares are to be aggregated have common investments or similar ties *beyond their interests in the concern at issue* that require them to be treated as one party." *Id.* at 6 (emphasis in original). Similarly, in *Size Appeal of [Drug Applicant]*, SBA No. SIZ-5632, at 9 (2012), OHA reiterated that the identity of interest analysis from *MPC Computers* had been "rendered a nullity" by *Cypress Pharmaceutical*. OHA instead applied *Cypress Pharmaceutical* and found no identity of interest because "there is no evidence that the [individuals in question] have any common interests beyond [the challenged firm]." *Id.* In the instant case, Appellant does not address these more recent OHA decisions, and has not attempted to show that Appellant's employees share any common interests beyond their joint association with Appellant itself.

Accordingly, Appellant has not demonstrated that the Area Office committed any error by declining to find an identity of interest among Appellant's employees. Because the Area Office correctly did not aggregate the stock of Appellant's employees into a separate block, it follows that JMI Equity holds "a block of voting stock which is large compared to other outstanding blocks of voting stock", and thus controls Appellant and is affiliated with Appellant under 13 C.F.R. § 121.103(c)(1). *E.g., Size Appeal of Civitas Group, LLC*, SBA No. SIZ-5424 (2012).

Appellant also argues that the Area Office erred in drawing an adverse inference against Appellant, but this argument too is meritless. As Deque emphasizes in its response to the appeal, Deque's protest specifically alleged affiliation between Appellant and JMI Equity, and this allegation was highly plausible given JMI Equity's substantial ownership and managerial interests in Appellant. As a result, Appellant was on notice that JMI Equity was a likely affiliate, and should have produced information about JMI Equity's annual receipts and other affiliates with the initial submission to the Area Office. Absent such information, it was appropriate for the Area Office to apply an adverse inference concerning JMI Equity's size. 13 C.F.R. §§ 121.1008(d) and 121.1009(d). Appellant also suggests that failure to produce information about JMI Equity was harmless because the combined receipts of Appellant and JMI Equity do not exceed the size standard for the subject procurement. Even assuming that JMI Equity itself is small, though, such an argument overlooks that Appellant would be affiliated not only with JMI Equity alone, but also with other concerns, such as other portfolio companies, in which JMI Equity holds controlling interests. *E.g., Size Appeal of WisEngineering, LLC*, SBA No. SIZ-5908 (2018). Because the Area Office was not provided sufficient information to determine what other concerns, if any, are controlled by JMI Equity, Appellant's failure to produce the requested information was not harmless.

Lastly, it is worth noting that, even if Appellant were not affiliated with JMI Equity through stock ownership, the record strongly suggests that Appellant would be affiliated with JMI Equity on alternate grounds. For instance, JMI Equity appears to exercise affirmative or negative control over Appellant's Board of Directors through provisions in the Stockholders Agreement, which may give rise to affiliation under 13 C.F.R. § 121.103(a)(3) and (e). I agree with the Area Office, though, that it was unnecessary to explore these issues in detail, given that Appellant was already found to be affiliated with JMI Equity through stock ownership.

IV. Conclusion

Appellant has not demonstrated that the size determination is clearly erroneous. 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