

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

SIZE APPEAL OF:

Enhanced Vision Systems, Inc.,

Appellant,

Appealed From
Size Determination No. 6-2018-079

SBA No. SIZ-5978

Decided: December 13, 2018

APPEARANCES

H. Boyd Greene, IV, Esq., Kirkland & Ellis, LLP, Washington, District of Columbia
for Appellant

Steven J. Koprince, Esq., Matthew P. Moriarty, Esq., Koprince Law LLC, Lawrence,
Kansas, Co-Counsel for Appellant

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FedBiz IT Solutions, LLC

DECISION

I. Introduction and Jurisdiction

On September 17, 2018, the U.S. Small Business Administration (SBA) Office of Government Contracting, Area VI (Area Office) issued Size Determination No. 06-2018-079 finding that Enhanced Vision Systems, Inc. (Appellant) is not a small business under the size standard associated with the subject procurement. Appellant maintains 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 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

On October 5, 2017, the United States Department of Veterans Affairs, Office of Acquisition Operations - Strategic Acquisition Center (VA) issued Request for Proposals (RFP) No. 36C10G18R0012 for video magnification closed circuit televisions for in-home use. The Contracting Officer (CO) set the procurement aside entirely for small business, and assigned North American Industry Classification System (NAICS) code 334220, Radio and Television Broadcasting and Wireless Communications Equipment Manufacturing, with a corresponding 1,250 employee size standard. Proposals were due on December 12, 2017. On January 18, 2018, Appellant was acquired by Freedom Scientific, Inc., a subsidiary of VFO Holdings BV (VFO). On July 23, 2018, the CO notified unsuccessful offerors Appellant was the apparent successful offeror.

B. Appellant's Negotiations with VFO

VFO first gained interest in acquiring Appellant in 2015. VFO initially approached Appellant regarding a potential acquisition in the Spring of 2017. (Appeal, at 3.) VFO and Appellant signed a Mutual Non-Disclosure Agreement on approximately July 20, 2017, to facilitate discussions of the acquisition. (*Id.*) In the Fall of 2017, VFO provided Appellant with a preliminary indication of interest with a price that was deemed too low by Appellant. (*Id.*) After Appellant communicated its disinterest in the proposed price, communication between Appellant and VFO temporarily ceased. (*Id.*)

On November 16, 2017, VFO sent Appellant a revised document, entitled, “Non-Binding Indication of Interest” (LOI) and a cover letter that stated in part:

Due to our desire to consummate a transaction expeditiously and to minimize the distraction to both sides, our [LOI] is contingent upon entering into an Exclusivity Period commencing on the date hereof and running for 30 business days, which should allow us time to complete our due diligence and negotiate a definitive purchase agreement.

The “Valuation and Transaction Structure” provision of the LOI outlined the breakdown of how the equity value of Appellant would be paid. It stipulated Appellant's equity value at [XXXXXXXXXX] and provided that [XXXXXXXXXX] subject to the negotiation and execution of “definitive written documentation.” (LOI, at 2.) [XXXXXXXXXXXXXXXXXXXXXXXXXXXXX] [XXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXX]. [XXXXXXXXXXXXXXXXXXXXXXXXXXXXX] [XXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXX] [XXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXX] [XXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXX].

The “Working Capital, [Representation & Warranty] Insurance Policy and Other Assumptions and Conditions” provision of the LOI addressed Appellant's indemnification obligations. VFO stated, “we are willing to limit the indemnity obligations of [Appellant] and

utilize a representation and warranty insurance policy [] as a part of the Transaction” where VFO would cover the cost. (*Id.* at 3.) This section also stated, “[t]he representations and warranties in the Transaction Agreement will provide for ‘Fundamental Representations’ limited to customary representations and warranties for ‘Organization and Standing,’ ‘Authorization,’ ‘Non-Contravention (with respect to organizational documents),’ ‘Capitalization,’ ‘Subsidiaries,’ ‘Taxes,’ and ‘Brokers.’” (*Id.*)

The “Due Diligence Requirements” provision of the LOI described the remaining confirmatory due diligence as “a) [d]etailed review of historical financial performance and operating metrics [;] b) [c]ustomary confirmatory legal & tax diligence and quality of earnings report [;] and c) [c]ustomer and partner reference calls to be made at an appropriate time, as mutually agreed by the parties.” (*Id.*)

The “Exclusivity” provision of the LOI stipulates that, for a period of 30 business days (Exclusivity Period), Appellant will not:

[D]irectly or indirectly, solicit, entertain or encourage inquiries or proposals, or submit or enter into an agreement with respect to, or negotiate or discuss with any person or entity, any Alternative Transaction. For purposes of this [LOI], “Alternative Transaction” means any (1) reorganization, dissolution or recapitalization (including any repurchase of equity) of any portion of [Appellant] in connection with a change of control of [Appellant] or any transaction prohibited by items (2), (3), (5) or (6) below[;] (2) merger, consolidation or acquisition of or involving any material portion of [Appellant][;] (3) private or public sale of any capital stock or other equity interests of any portion of [Appellant] other than in connection with employee compensation arrangements[;] (4) sale of any notes of any portion of [Appellant] or incurrence by [Appellant] of any funded debt, in each case other than in the ordinary course of [Appellant's] business consistent with past practice or in connection with a transaction permitted by item (1) above[;] (5) sale or licensing of all or any material assets of any portion of [Appellant] or any interest therein[;] or (6) any similar transaction, business combination or joint venture involving any material portion of [Appellant] or its business or assets in any form (including any debt or equity financing thereof); provided, however, that nothing in this paragraph shall limit [Appellant] from acquiring or divesting inventory in the ordinary course of business.

(*Id.* at 3-4.) The Exclusivity provision also requires Appellant to provide notice if it receives any “solicitation of information, proposal, indication of interest or other communication relating to a possible Alternative Transaction” during the Exclusivity Period. Appellant is also to provide VFO with a detailed summary regarding the nature of such communication including Appellant's response to the communication and must represent and warrant to VFO that Appellant has ceased “any and all contacts, discussions and negotiations with third parties regarding any Alternative Transaction” and ensuring that there has been no agreement as a result of those communications. (*Id.* at 4.)

The “Governing Law; Binding Effect; etc.” provision of the LOI identifies California law as the substantive law upon which the [LOI] is governed. The provision also states:

This [LOI] represents a non-binding preliminary indication of interest on our part and, except with respect to this Section entitled, “Governing Law; Binding Effect; etc.” and the immediately preceding Section entitled “Exclusivity” both of which shall be binding on the parties hereto (the “Binding Provisions”), it is not intended to create a legally binding agreement among the parties hereto, [VFO], [Appellant] or any other person (including, for the avoidance of doubt, with respect to a Transaction.) Except with respect to the Binding Provisions, no contractual obligations with respect to our [LOI] will arise until a Transaction Agreement is executed between the parties.

(*Id.*) This provision also states that the LOI “may be executed in two or more counterparts . . . all of which taken together will constitute one binding agreement with respect to the Binding Provisions between the parties hereto and their successors and assigns.” (*Id.*) The Mutual Non-Disclosure Agreement entered into by VFO and Appellant remained in full force and effect. Appellant viewed the terms of the LOI more favorably than what was previously offered, and agreed to enter negotiations, for a 30-day period, for a possible sale to VFO on November 17, 2017. (Javaheri Declaration, at ¶ 6.)

In a sworn declaration dated August 20, 2018, Bahram Javaheri, former President of Appellant, stated he believed the only commitment made or he intended to make was “to enter exclusive negotiations with VFO for a potential sale of [Appellant.]” (*Id.* at ¶ 7.) His interpretation of the LOI was that it was an “agreement to enter negotiations and a diligence process for the sale of the Company, but by no means a preliminary agreement to sell the Company.” (*Id.*)

In a sworn declaration dated August 20, 2018, Rick Simpson, Ph.D., Chief Financial Officer for VFO, stated “VFO and Vector Capital (Vector)[(majority owner of VFO)] drafted the letter of interest in a manner to let [Appellant] know that VFO was genuinely interested in an acquisition, but also to provide VFO a reasonable amount of time to conduct diligence before reaching an agreement.” (Simpson Declaration, at ¶ 8.) Further, Simpson considered the letter “only an agreement to initiate negotiations and conduct diligence.” (*Id.* at ¶ 9.) Also, “an agreement to acquire [Appellant] could have only been reached following a confirmatory diligence, and only then after meaningful business and legal negotiations.” (*Id.*)

C. Post-LOI Occurrences

Messrs. Javaheri and Simpson attest that Appellant and VFO attempted to reach an agreement throughout December 2017 in “good faith” as agreed upon in the LOI. (Javaheri Declaration, at ¶ 8; Simpson Declaration, at ¶ 11.) On December 7, 2017, Appellant submitted a proposal for the instant procurement. Mr. Simpson denies VFO had any input or discussions with respect to any business proposals prepared by Appellant, including its proposal for the instant procurement (Simpson Declaration, at ¶ 10.)

Mr. Simpson claims VFO's review of Appellant's financial reports revealed a “softness in [Appellant's] financial performance in the most recent period.” (Simpson Declaration, at ¶ 13.) As a result, Vector “would not move forward with an agreement absent additional approval by Vector's investment committee” which would require Vector providing additional capital to make an acquisition of Appellant possible. (*Id.* at ¶ 14.) Consequently, Mr. Javaheri decided to withdraw Appellant from further negotiations with VFO and Vector, having deep concerns Appellant could reach an agreement with VFO. (Javaheri Declaration, at ¶ 14.) Therefore, Appellant and VFO were unable to reach an agreement before the conclusion of the Exclusivity Period, as Messrs. Javaheri and Simpson claim negotiations reached an impasse by the end of December 2017. (Javaheri Declaration, at ¶ 12; Simpson Declaration, at ¶ 15.)

VFO contacted Appellant to restart negotiations in early January 2018 and apologized for the “misunderstanding about their need for additional reviews to further consider a transaction.” (Javaheri Declaration, at ¶ 16 and ¶ 17; Simpson Declaration, at ¶ 16.) [XXXXXXXXXXXXX] [XX]. Thus, “discussions renewed, outstanding issues were negotiated, and an investment thesis was revised for Vector's investment committee approval.” (Simpson Declaration, at ¶ 17.) Appellant and VFO reached a purchase agreement on January 18, 2018. (Javaheri Declaration, at ¶ 18; Simpson Declaration, at ¶ 18.)

D. Protest and Protest Response

1. FedBiz's Protest

On August 13, 2018, FedBiz IT Solutions, LLC (FedBiz), filed a protest alleging that Appellant is not a small business, because Appellant had already entered into an agreement to be acquired by VFO, a large business, at the time of its initial offer. This meant Appellant was affiliated with VFO and therefore other than small for the instant procurement. FedBiz argues Appellant was affiliated with VFO prior to December 12, 2017 — the date offers for the instant procurement were due. (Protest, at 3.) FedBiz cites 13 C.F.R. § 121.103(d)(1), which “makes it clear that [SBA] considers agreements to merge as having a present effect on the power of one concern to control another.” (*Id.*) Further, OHA has held that a letter of intent for one company to purchase another “will have present effect on affiliation, even if the letter of intent is not legally binding.” (*Id.*; citing to *Size Appeal of WRS Infrastructure & Environment, Inc.*, SBA No. SIZ-5007 (2018) and *Size Appeal of Q Integrated Cos.*, SBA No. SIZ-5778 (2016).)

FedBiz argued it was “evident” Appellant had an agreement in principle with VFO by the time Appellant submitted its proposal for the instant procurement based on Appellant's January 23, 2018 announcement of the acquisition and the fact that the acquisition process “will take considerably more than six weeks.” (*Id.* at 4.) Therefore, because Appellant and VFO agreed in principle prior to December 2017, their agreement should be given present effect, making Appellant affiliated with VFO at the time Appellant submitted its offer in response to the instant RFP. (*Id.*)

FedBiz contended Appellant was a large business prior to December 12, 2017 due to its affiliation with VFO and Vector as a result VFO's acquisition of Appellant. Further, VFO owns

and controls other companies, making Appellant affiliated with those companies through common ownership and an identity of interest. (*Id.* at 5.) Because VFO is owned by Vector, Appellant is also affiliated with Vector and its affiliates. The aggregated number of employees employed by Vector, VFO, and Appellant is approximately 9,850, which far exceeds the 1,250 size standard associated with the NAICS code for the instant procurement. (*Id.* at 9-10.)

FedBiz maintains Appellant was required to recertify its size status after VFO's acquisition. FedBiz argues SBA's regulations require that a contractor must recertify its size after it submits its offer if a merger, sale, or acquisition occurs prior to award. (*Id.* at 10, citing to 13 C.F.R. 121.404(g)(2)(ii)(D).) FedBiz points to the preamble to a recent revision of the rule:

For several years SBA's rules have required recertification in connection with a contract when there is an acquisition or merger involving the prime contractor. SBA never intended for the recertification requirement to not apply based on when the acquisition or merger occurred. If recertification is required for an existing contract, it should be required for a pending contract. An agency's receipt of small business credit should not depend on whether an acquisition or merger occurs the day before award of contract.

81 Fed. Reg. 34243, 34253 (May 31, 2016). FedBiz noted the confusion associated as to “whether this re-certification requirement meant an offeror would become ineligible for award if recertified after the proposal submission date as other than small, or that the offeror could receive an award but it could not be counted toward the agency's small business goals.” (Protest, at 10.) FedBiz acknowledged OHA has held that the recertification rules were to be used for the purpose of calculating the procuring agency's small business goals, not to render a contractor as ineligible for future awards under an IDIQ contract. (Protest, at 11; citing to *In the Matter of Analytic Strategies Inc.*, SBA No. VET-268 (2018).)

FedBiz argued, however, that SBA intended the rule to not only prohibit the agency from counting the award toward its small business goals, “but to render a business ineligible for set-aside work if it was no longer small as a result of a sale, merger, or acquisition.” (*Id.* at 11-12; referring to 83 Fed. Reg. 12489 (March 26, 2018).) Thus, FedBiz claimed Appellant was required to recertify its size no later than February 22, 2018, 30 days after the acquisition, which became the new date for determining its size. (*Id.* at 12.) FedBiz argues, “the sole question is whether the offeror was actually small on the date of determining size. [Appellant] was clearly large prior to the VA's announcement that it was the apparent successful offeror” and is ineligible for the award. (*Id.* at 13.)

2. Appellant's Protest Response

On August 20, 2018, Appellant submitted its response to FedBiz's protest arguing it did not have an agreement in principle with VFO at the time of its offer for the instant procurement, it was a small business at the time of its offer for the instant procurement, and the date upon which Appellant's size is determined is the date it submitted its offer for the instant procurement. (Protest Response, at 2.)

Appellant contended that OHA decisions “make clear, that ‘agreements to open or continue negotiations towards the possibility of a merger or sale of stock at some later date are not considered ‘agreements in principle’ and thus are not given present effect.” (*Id.* at 4; citing to *Size Appeal of W.I.N.N. Group, Inc.*, SBA No. SIZ-5360 (2012) and 13 C.F.R. § 121.103(d)(2).) Appellant argues the LOI “signals only tangible evidence of an agreement to continue negotiation.” (Protest Response, at 6.) Further, Appellant and VFO continued discussions through December 30, 2017 and reached a stock purchase agreement on January 18, 2018. Therefore, Appellant and VFO had not reached an agreement in principle as of the submission date for offerors, “but rather merely to continue negotiations, which should not be given present effect.” (*Id.*)

Appellant maintained its small business status, as Appellant “plainly fell within the applicable size standard announced in the VA's RFP as of [] December 7, 2017, the date it submitted its original offer to VA.” (*Id.*) Further, the SBA determines the size status of a concern, and its affiliates, as of the date it submits a written self-certification that it is small, including the price, to the procuring agency. (*Id.*, citing to 13 C.F.R. § 121.404(a).) Because Appellant was not affiliated with VFO or its owners at the time of the initial offer, the only affiliates relevant to Appellant's size status are Enhanced Vision Systems Optron (Germany) and Enhanced Visions Europe Limited (UK). (*Id.*) The total number of employees of Appellant and its affiliates as of the date of the initial offer is 102. Therefore, Appellant is “well within the employee-based size standard announced in the RFP.” (*Id.* at 7.)

Appellant dismissed FedBiz's claim that it was required to recertify its size as of February 18, 2018 under 13 C.F.R. § 121.404(g)(2)(ii)(D), as “OHA has squarely and definitively held that the recertification of size status required under SBA regulations impact only the counting of the agency's small business goals.” (*Id.* at 8, citing to *Size Appeal of Mistral, Inc.*, SBA No. SIZ-5737; also citing to *In the Matter of Analytics Strategies, Inc.*, SBA No. VET-268 (2018) as affirming this interpretation of the rule.) Appellant also contended SBA's revised language does not apply to the instant RFP, which was issued prior to the amendment's effective date of May 25, 2018. (Protest Response, at 8.)

C. Size Determination

On September 17, 2018, the Area Office issued Size Determination No. 06-2018-079 finding Appellant to be other than a small business concern for the 1,250 employee size standard applicable to this procurement.

The Area Office first determined that Appellant is affiliated with Enhanced Vision Systems Optron (Germany) and Enhanced Visions Europe Limited (UK) due to common management. (Size Determination, at 5; citing to 13 C.F.R. 121.103(a)(1).) The Area Office then discussed VFO's purchase of Appellant on January 18, 2018 under the present effect rule, dealing with agreements to merge. (*Id.* at 6, citing to 13 C.F.R. § 121.103(d).) The Area Office determined that the LOI between Appellant and VFO “does contain provisions that are binding to both parties” despite the document's title describing the LOI as “non-binding.” The Area Office identified these binding provisions as the “Government Laws; Binding Effect; etc. and “Exclusivity” provisions of the LOI. (*Id.* at 7.) The Area Office found the Exclusivity Provision

to prevent Appellant from “engaging in any activity that would in any way change the control of [Appellant].” (*Id.* at 8.) Thus, VFO had control over Appellant on December 7, 2017, the date to determine size, based on Appellant's submission of the offer for the instant procurement. (*Id.*, citing to 13 C.F.R. 121.103(a)(1).)

(*Id.* at 8.) [sic?] The Area Office highlighted that the LOI ultimately resulted in a purchase agreement signed by Appellant and VFO on January 18, 2018. (*Id.*) It then noted that under the regulations, SBA “may treat the purchase agreement as though the rights granted have been exercised,” provided certain conditions be met. (*Id.* at 8-9, citing to 13 C.F.R. 121.103(d).)

The Area Office examined the communications between Appellant and VFO leading to the execution of the January 18, 2018 purchase agreement, stating:

SBA finds it reasonable to conclude that discussions to open or continue negotiations toward the possibility of a purchase was [sic] likely held prior to or during the summer of 2017, when discussions were probably more fluid and conversational in nature.

...

While SBA has not received a copy of the initial LOI, the wording on the executed or ‘revised’ document suggests that a similar document had been initially submitted and initial due diligence performed by [VFO] was already underway, as evidenced by the reference to the aforementioned Non-Disclosure Agreement and a reference to ‘confirmatory due diligence’ requirements remaining as part of the completion of the transaction.

The executed LOI identifies specific language, in written form, that includes specific dates, a price, and certain terms, such as prohibited transactions, that would apply to [Appellant] and prevent [Appellant's] management, employees, and principals from performing certain transactions. [Appellant]'s failure to abide by such agreed-upon terms would put the purchase transaction at risk. SBA finds no indication in the executed LOI that the parties to the agreement were not acting in good faith or that the parties were not serious about successfully completing the purchase transaction.

SBA therefore, finds the executed LOI represents the final stages of an agreement in principle, as opposed to an agreement to open or continue negotiations towards the possibility of a merger at some later date.

(*Id.* at 9-10.) The Area Office concluded the conditions under 13 C.F.R. § 121.103(d)(2) which would avoid a finding of present effect did not apply.

The Area Office then reviewed *Size Appeal of WRS Infrastructure and Environment, Inc.*, SBA No. SIZ-5007 (2008), where “OHA agreed with the Area Office's decision that the LOI [] was not speculative, was intended to succeed, included terms such as price, and which ultimately

resulted in the Company's purchase, [and] was an agreement in principle.” (*Id.* at 10.) The Area Office concluded:

The executed LOI shows that the probability of the transaction is not remote. The agreement provides both parties with 30 business days (the *Exclusivity Period*) to meet certain terms and conditions during which, [Appellant] cannot solicit or entertain any other proposals to discuss or purchase [Appellant]. This indicates the seriousness of the parties to reach a final agreement. The LOI contains binding elements that are enforceable by laws under the State of California, shows the willingness of [Appellant] to desist from entertaining any offers and to allow for finalizing of due diligence for completion of a future transaction, which in this case took place shortly after, [on] January 18, 2018, five weeks after offers were due on the procurement at issue and 15 days after the *Exclusivity Period* expired. The LOI executed by [Appellant] contains a specific price, identifies due diligence requirements, limits as to management actions or ‘prohibited transactions’ that are binding on [Appellant]. As in the referenced *WRS* case, the document is not speculative in nature, provides certain binding elements, and resulted in a finalized transaction. [The Area Office] finds that conditions at 13 C.F.R. § 121.103(d)(3) do not apply to this executed LOI.

(*Id.* at 10-11) (emphasis original). The Area Office then notes the regulations do not require an agreement to be binding in order to apply the present effect rule. The Area Office found the LOI to be an agreement in principle “because conditions 13 C.F.R. § 121.103(d)(2) and 13 C.F.R. § 121.103(d)(3) do not apply.” (*Id.* at 11.) The Area Office therefore treated the purchase agreement as though the rights granted on January 18, 2018 were exercised as of December 7, 2018 and Appellant is affiliated with VFO based on common ownership under 13 C.F.R. § 121.103(a)(1) and (c)(1). (*Id.* at 11.)

The Area Office found that Appellant, on its own, is small for the 1,250 employee size standard. However, Appellant confirmed in an e-mail that “[VFO] and its affiliates would have exceeded 1,250 employees as of December 7, 2017.” (*Id.* at 12.) Therefore, Appellant is other than small for the instant procurement.

D. Appeal Petition

On October 2, 2018, Appellant filed the instant Appeal. Appellant argues the Area Office misapplied SBA regulations and OHA precedent and committed clear error in determining that the LOI was an agreement in principle. (Appeal, at 2.) Appellant argues the LOI “merely committed the parties to a limited period of exclusive negotiations — a circumstance OHA has held does not result in an agreement in principle.” (*Id.*) Further, the LOI “omitted too many important terms” to be considered an agreement in principle. Lastly, the Area Office ignored the fact that negotiations broke down several weeks after the LOI was executed, which suggests the LOI was not an agreement in principle. (*Id.*)

Appellant contends, other than the total acquisition price, the LOI did not include essential terms of the potential deal, as they were undecided. (*Id.* at 3.) For example, the LOI

discussed that the parties would [XXXXXXXXXXXXXXXXXXXXXXXXXXXX], but did not indicate what that ‘mutually beneficial structure’ might look like. (*Id.*)

Appellant also highlights the LOI only included one paragraph regarding the substantive terms of the potential transaction, referring to the “Working Capital, R & W Insurance Policy, and Other Assumptions and Conditions” provision. (*Id.* at 4.) This paragraph discussed a working capital target, but did not specify what the target would be. The paragraph also stated VFO was willing to pay for and use a “representations and warranties” insurance policy, but did not provide details about the policy. Finally, the paragraph also stated the Transaction Agreement would include certain customary representations and warranties, but did not describe what those representations and warranties would provide. (*Id.*)

Appellant also notes the LOI stated VFO would conduct “substantial due diligence,” which would include a “detailed review of historical financial performance and operating metrics” as well as “confirmatory legal and tax diligence,” conduct a quality of earnings report, and make reference calls to customers and partners. (*Id.*)

Appellant highlights that the Exclusivity provision required Appellant to inform VFO of any communications relating to an Alternative Transaction, but “did not specify any monetary or non-monetary damages in the event [Appellant] entered into an Alternative Transaction” during the Exclusivity Period. (*Id.* at 5.)

Appellant points to a paragraph in the LOI titled “Governing Law; Binding Effect, etc.” This paragraph provided the LOI would be governed by California law and that the LOI is a “non-binding preliminary indication of interest” by VFO. Only the “Governing Law” and “Exclusivity” provisions were legally binding upon the parties. The LOI is not intended to create a legally binding agreement between the parties, and no contractual obligations would arise until a Transaction Agreement was executed. (*Id.* at 5.)

Appellant refers to the affidavits of Messrs. Javaheri and Simpson in arguing Appellant and VFO were both under the impression that the LOI was an agreement to enter negotiations but not an agreement to sell or purchase Appellant. (*Id.* at 5-6.) Further, although both parties were interested in the deal, “subsequent negotiations proved very difficult” as “[b]oth sides had significant areas of concern.” (*Id.* at 6.) For example, in conducting its due diligence review, VFO “was uncertain whether it would be able to complete a deal” due to Appellant's more recent financial performance. (*Id.*) Appellant was dissatisfied with the potential equity package offered by VFO for Appellant's senior leadership. Appellant asserts there were “at least ten significant areas of disagreement” between Appellant and VFO that would need to be resolved in the final agreement. (*Id.*) In late December 2017, the parties reached a “complete impasse and negotiations abruptly stopped.” (*Id.*, citing to the Javaheri Declaration, at ¶ 12.) Appellant claims negotiations resumed in the second week of January 2018, after a “cooling off period.” (*Id.* at 7.) The parties subsequently resolved “their many remaining areas of disagreement” and executed the Stock Purchasing Agreement (SPA) on January 18, 2018. (*Id.*)

Appellant notes the final SPA provided that Freedom Scientific, Inc., (Buyer), “not VFO itself or another VFO affiliate” would purchase the equity interest in Appellant. (*Id.*) The SPA

was 63 pages long, which included an Escrow Agreement, A Rollover Agreement, Consulting Agreements between VFO and Appellant's former owners, Joinder Agreements, and a Management Unit Agreement. (*Id.*) The SPA included 26 “Seller Representations and Warranties,” (R&Ws) which is nearly four times the number included in the LOI, five additional Seller R&Ws, and 8 Buyer R&Ws. (*Id.*) The SPA imposed “detailed indemnification obligations” on the Buyer and Seller, as compared to the LOI, which only addressed a portion of Appellant's obligations. (*Id.*) The SPA provided the tax basis and allocations for the deal, a five-year confidentiality agreement, general waivers and releases, a non-compete provision, access to Appellant's books and records, tail insurance, and a release of personal guarantees in support of Appellant's office space. (*Id.* at 8.) The parties agreed that the SPA would be governed by Delaware law, unlike the LOI, and waived their right to a jury trial. (*Id.*)

Appellant argues the Area Office did not discuss many of the matters raised by Appellant's response to the protest. Specifically, the Area Office did not discuss the *W.I.N.N. Group* decision, did not discuss the difficulties associated with negotiations between Appellant and VFO, and the expiration of the exclusivity period. Appellant finds it “most striking” that the Area Office did not discuss the complete breakdown of negotiations on December 30, 2017. (*Id.* at 11.)

Appellant argues the LOI “fits, almost to a ‘T,’ the SBA's regulatory definition of an agreement that is *not* to be given present effect.” (*Id.*) (emphasis original.) Instead, the LOI was a vehicle to open or continue negotiations and not an agreement in principle to sell Appellant, as “not every agreement about a potential acquisition is given present effect.” (*Id.* at 12, citing to 13 C.F.R. § 121.103(d)(2).) Appellant argues “tangible evidence” of an agreement in principle must be present in order to apply present effect. (*Id.* at 12, citing to *Size Appeal of W.I.N.N. Group*, SBA No. SIZ-5360 (2012).) In *W.I.N.N. Group*, Appellant contends, OHA found no tangible evidence of an agreement in principle where the agreement at issue described itself as non-binding and the offer was conditioned on a due diligence review. (*Id.*) There was no tangible evidence of an agreement in principle where parties “merely committed to negotiate exclusively with one another.” (*Id.*, citing to *Size Appeal of Nuclear Servs., Inc.*, SBA No. 5324 (2018), and *Size Appeal of PCCI, Inc.*, SBA No. SIZ-4531 (2003).)

Appellant contends the SBA should not give present effect to the LOI because there were too many important unresolved matters. (*Id.* at 13, citing to *W.I.N.N. Group*, SBA No. SIZ-5360). Further, when negotiations reach an impasse, the agreement should not be treated as an agreement in principle. (*Id.*, citing to *Size Appeal of B.K. Infrastructure, Inc.*, SBA No. SIZ-2045 (1984).) Appellant argues the fact that an agreement is lengthy and complicated does not mean that there was any agreement reached prior to its execution. (*Id.*, citing to *W.I.N.N. Group*). Appellant also contends, “the mere fact that an agreement is ultimately consummated ‘cannot contradict a clear record that, at a particular point in time, the parties had not yet reached an agreement.’ Otherwise, ‘every agreement reached would be found to have existed as an agreement in principle at the earlier point in negotiations where any document was produced.’” (*Id.*, quoting *W.I.N.N. Group*, SBA No. SIZ-5360.) Further, the inclusion of a proposed price in a negotiation document does not establish an agreement in principle, but “marks the onset of more serious negotiations.” (Appeal, at 14.)

Appellant identifies multiple clear errors made by the Area Office in its determination finding the LOI to be an agreement in principle. First, there was no tangible evidence of an agreement in principle where the LOI was described as non-binding, and neither the price, nor any substantive term of the potential acquisition was binding. (*Id.* at 15.) VFO conditioned its offer on a due diligence review. Further, the Area Office indicated the fact that VFO and Appellant agreed to negotiate with each other exclusively was critical to its finding the LOI to be an agreement in principle where the regulations and OHA case law have found that such an agreement is not always an agreement in principle. (*Id.*, citing to *PCCI, Inc.*, SBA No. SIZ-4531 and 13 C.F.R. § 121.103(d)(2).)

Appellant also counters the Area Office's suggestion that the LOI created negative control of Appellant by VFO. Appellant argues negative control usually arises where a minority shareholder has the ability to prevent a quorum or otherwise block action by the board of directors or shareholders through a concern's charter, by-laws, or shareholder's agreement. (Appeal, at 15, citing to 13 C.F.R. § 121.103(a)(3). Appellant contends the Area Office provided no support for its suggestion that “an ordinary, arm's length agreement for exclusive discussions between businesses can rise to the level of negative control sufficient to cause affiliation” where most agreements between businesses involve some level of exclusivity. (Appeal, at 15-16.)

The Area Office failed to consider the many essential matters that were left unresolved by the LOI. For example, the LOI did not establish what entity would buy Appellant and did not provide information regarding the tax and legal structure of the deal. (*Id.* at 16.) In comparing the LOI to the SPA, Appellant identifies more elements not resolved at the time of execution of the LOI. The LOI did not include the large majority of representations and warranties agreed upon in the SPA. (*Id.*) The LOI did not discuss confidentiality rights, non-compete provisions, any continued liability by the former owners of Appellant, subsequent consulting agreements entered into by the former owners of Appellant, and did not include a Rollover Agreement, Joinder Agreement, or Management Unit Agreement — all of which were negotiated and agreed upon in the SPA. (*Id.* at 17.)

Appellant finds it “most striking” that Mr. Javaheri and Mr. Simpson both testified in their declarations that negotiations broke down completely on December 30, 2017 and the Area Office “did not address this compelling evidence.” (*Id.* at 17-18.) The Area Office further erred by assuming that the length and complexity of the ultimate SPA suggests VFO and Appellant had agreed upon the substantive terms of the deal prior to December 7, 2017. Thus, the Area Office made assumptions about the initial Interest Letter, a document it did not request or review, and ignored sworn statements in the record. (*Id.* at 18.)

Lastly, the Area Office erred in only focusing on the *WRS Infrastructure* decision while ignoring the *W.I.N.N. Group* decision and other highly-relevant authority like *Nuclear Fuel Services*. The Area Office “failed to even acknowledge or consider the many important differences between the facts of *WRS Infrastructure* and the circumstances here.” (*Id.* at 19.) For example, the letter in *WRS Infrastructure* was entitled a “Letter of Intent” where here, the LOI was titled, “Letter of Interest.” (*Id.*) In addition, the Letter of Intent in *WRS Infrastructure* was more detailed than the LOI, as it included not only a price, but also an escrow provision, and provisions concerning indemnification, aged receivables, confirmatory due diligence, and pre-

signing and closing conditions. (*Id.*) The letter of intent was executed after weeks of discussions where the LOI prompted discussions to begin. Also, there was no indication in *WRS Infrastructure* that many important terms remained unresolved or that negotiations between the parties had ever broken down. (*Id.*)

Appellant concludes by arguing the LOI was not a “meeting of the minds” with respect to an acquisition of Appellant, but was only an agreement to open or continue negotiations under 13 C.F.R. § 121.103(d)(2). Thus, the Area Office erred in finding the LOI an agreement in principle.

F. FedBiz's Response to the Appeal

On October 26, 2018, FedBiz filed its response to the Appeal. FedBiz argues the Appeal fails to show any clear error of fact or law by the Area Office. The Area Office reviewed all of the evidence presented in the record and correctly concluded that the LOI was an agreement in principle. (Response, at 6-7). In comparing the LOI to the letter of intent in *WRS Infrastructure*, the LOI “was not speculative, was intended to succeed, included salient terms, and resulted in [VFO]'s purchase of all the capital stock of [Appellant], free and clear of all liens.” (*Id.* at 10.)

Appellant demonstrated no clear error by the Area Office. The Area Office gave “due weight” to the declarations of Messrs. Javaheri and Simpson, however, “OHA has made it clear that it will not rely on self-serving characterizations of documents in determining whether a document is an agreement in principle or an agreement to open or continue negotiations. Rather, SBA must consider the “substance of the entire document itself.” (*Id.* at 11, quoting *Size Appeal of Telecommunication Support Services, Inc.*, SBA No. SIZ-5953 (2018).) Thus, The Area Office determined, based on the substance of the LOI and the timing of the transaction, the parties were in the final stages of an agreement in principle at the time Appellant submitted its offer for the procurement. (Response, at 11.) Further, although Messrs. Javaheri and Simpson indicated that negotiations had broken down, they submitted “no contemporaneous documentation to corroborate the declarations.” (*Id.* at 12, citing to *Telecommunications Support Services, Inc.*, SBA No. SIZ-5953 (where the appellant submitted declarations and an extensive file of emails between the parties as evidence that no agreement in principle existed between the parties).)

The Area Office properly relied on *WRS Infrastructure and Environment, Inc.*, SBA No. SIZ-5007 (2008). FedBiz contends it is the substance of a document and not a self-serving characterization, or caption of the document, which determines whether it is an agreement in principle. (*Id.* at 13.) Like the letter of intent in *WRS Infrastructure*, the LOI expressed VFO's intent to purchase Appellant. (*Id.*, quoting the LOI cover letter, “Due to our desire to consummate a transaction expeditiously and to minimize the distraction to both sides . . .”) FedBiz also points to VFO including a price in the LOI, having VFO's CEO sign the LOI, and VFO's interest in Appellant since 2015 as proof that VFO intended to purchase Appellant when the LOI was executed. (*Id.*) Further, the LOI and the letter of intent in *WRS Infrastructure* both included a purchase price and provisions concerning indemnification and confirmatory due diligence, thus “no material difference” exists between the two letters. (*Id.* at 14.) In response to Appellant's claim that the parties in *WRS Infrastructure* were in discussions for weeks prior to the execution of the letter of intent, FedBiz highlights Appellant and VFO were in discussions as early as July 2017 when the parties executed the LOI. (*Id.*) FedBiz counters Appellant's

contention that there were many unresolved terms at the time of the LOI in arguing that OHA has never indicated that the absence of some terms in an agreement or a break in discussions would lead to a conclusion that an agreement in principle was not present. (*Id.* at 14-15.)

FedBiz contends the facts in *W.I.N.N. Group* and *Nuclear Fuel Services* are clearly distinguishable from the instant matter, and the Area Office did not commit error in not relying on them. In *W.I.N.N. Group*, the parties had not reached an agreement as to price, the purchasing entity still had to complete extensive due diligence, and the subject entity was in discussions with another potential purchaser at the time of the initial letter. (*Id.* at 15-17.) Here, there was a price, VFO had already conducted most of its due diligence, and the parties entered into an exclusivity period that prevented Appellant from discussing an acquisition with another buyer. (*Id.* at 17.) Thus, the parties in *W.I.N.N. Group* were in a different stage of discussions as compared with the instant matter, and the Area Office did not commit any clear error in concluding the parties here had an agreement in principle.

The Area Office did not err in not relying on *Nuclear Fuel Services, Inc.* because the LOI was not a unilateral proposal by VFO to purchase Appellant subject to multiple conditions. Instead, the LOI submitted by VFO included definite terms that were agreed upon by Appellant. Further, in *Nuclear Fuel Services, Inc.*, OHA found the eight months between the execution of the initial offer letter and the signing of the final transaction document to indicate no agreement in principle existed at the time of the offer, whereas only eight weeks passed between the execution of the LOI and the SPA in this matter. (*Id.* at 18.) Also, an agreement in principle need not be legally binding. (*Id.* at 18-19, citing to *WRS Infrastructure, supra*, at 7-8.)

FedBiz argues the Area Office reasonably determined VFO controlled, or had the power to control, Appellant on the date Appellant submitted its proposal due to the restrictions provided by the exclusivity provision in the LOI. (Response, at 19-20.) For example, the LOI prevented Appellant from entertaining other potential buyers and from “performing ordinary tasks essential to the operation of the business.” (*Id.* at 20-21.) FedBiz points out certain provisions of the LOI which prohibit Appellant from negotiating, discussing, or entering into any debt or equity financing which involve any material portion of Appellant's business or assets. FedBiz argues OHA has held the creation of debt is “fundamental to the daily operating of a business and the ability to impede such ordinary actions results in negative control over the concern's operations.” (*Id.* at 21, citing to *Size Appeal of Carntripe-Clement*, SBA No. SIZ-5357, at 15 (2012); *Size Appeal of BR Construction, LLC*, SBA No. SIZ-5303, at 8 (2011); *Size Appeal of McLendon Acres, Inc.*, SBA No. SIZ-5222, at 6 (2011); and *Size Appeal of Eagle Pharmaceuticals, Inc.*, SBA No. SIZ-5023, at 10 (2009).) Appellant argues OHA precedent holds a stock purchase agreement that prevented the seller from taking certain actions, like incurring debts or obligations, without the buyer's consent until the stock transfer occurred afforded the buyer negative control over the seller. (Response, at 22, citing to *Dependable Courier Services, Inc.*, SBA No. SIZ-2110, at 2-3 (1985).)

FedBiz argues VFO restricted Appellant from selling any of its assistive technology or any technological enhancements, since such activities “undoubtedly involved the ‘sale or licensing of all or any material assets of any portion of [Appellant] or any interest therein,’ which is prevented by the LOI. (Response, at 23.) FedBiz claims the broad sweep of the

Exclusivity provision of the LOI prevented Appellant from making important decisions relating to the operation of its business, essentially providing VFO with control, or the power to control, Appellant. (*Id.* at 24.) Further, circumstances of negative control are described but not limited to the examples provided in the regulations, as a determination of negative control is based on an assessment of the totality of the circumstances. (*Id.*, citing to 13 C.F.R. § 121.103(a).) Appellant's statement that the LOI was only an agreement to enter into negotiations ignores the numerous restrictions placed on Appellant in its business operations. Thus, the Area Office properly found affiliation on this basis. (*Id.* at 24-25.)

FedBiz reiterates its argument in its protest regarding Appellant's failure to recertify its size 30 days from the date its size status changed when it was acquired by VFO, as required by 13 C.F.R. § 121.404(g)(2)(ii)(D). (*Id.* at 25.) FedBiz notes OHA has found the rule to only address whether agencies could count the award toward its small business goals and not causing a concern to become ineligible for award if it is acquired after offer but before award. (*Id.* at 25-26, citing to *In the Matter of Analytic Strategies Inc.*, SBA No. VET-268 (2018).) However, FedBiz further notes SBA's subsequent amendment to the rules: "SBA explained that its rules were intended to render an entity ineligible for award if it recertifies as other than small after a merger, sale or acquisition." (Response, at 26, referring to 83 Fed. Reg. 12849 (Mar. 26, 2018).) Therefore, Appellant was required to recertify its size no later than February 18, 2018 — 30 days after the January 18, 2018 acquisition, which became the new date for determining Appellant's size. (*Id.* at 27.) Thus, Appellant became a large business when it was acquired by VFO on January 18, 2018, was large before the July 19, 2018 award, and was therefore ineligible for the award for the instant procurement.

G. Appellant's Motion to Reply

On November 5, 2018, Appellant filed a Motion to Reply to the October 26, 2018 Response to the Appeal of FedBiz. Appellant argues FedBiz cites to authority that was not published at the time of Appellant's Appeal. Appellant contends FedBiz relies on *Size Appeal of Telecommunication Support Services, Inc.*, SBA No. SIZ-5953 (2018) in its Response, which was not publicly available until after Appellant filed the instant Appeal. (Appellant's Motion to Reply, at 2.) Appellant maintains a reply to FedBiz's response addressing this case would not enlarge the issues before OHA, but instead clarify them. (*Id.* at 4.) Appellant should also be allowed to respond, because FedBiz includes arguments in its response that were not addressed by the Area Office. (*Id.* at 4.)

Along with the Motion to Reply, Appellant filed a Reply to the October 26, 2018 Response of FedBiz. In the Reply, Appellant contends, FedBiz cites to recently published authority that "is directly on point and casts a stark light on the clear error of the Area Office." (Appellant's Reply, at 1.) Appellant also argues the case indicates the Area Office relied on a case that is an "outlier." (*Id.*)

Appellant argues *Size Appeal of Telecommunication Support Services, Inc.*, SBA No. SIZ-5953 (2018), is "almost directly on point" and reveals OHA's appreciation of how such acquisition negotiations have evolved since 2008, when *Size Appeal of WRS Infrastructure and Environment, Inc.*, SBA No. SIZ-5007 (2008) was decided. (Appellant's Reply, at 2-3.)

Appellant contends the facts of *Telecommunication* is “eerily similar” to the facts in this case, where the differences show how much closer the parties were to a final transaction in *Telecommunication*, as compared to the parties here. (*Id.* at 4.) For example, the letter in *Telecommunication* included a price, leaving many other terms undefined and created an exclusivity period of 30 business days for negotiation. In *Telecommunication*, the deal had been put on hold, where there was a “complete breakdown” of negotiations here. (*Id.* at 4.) Further, OHA reasoned that the final agreement in *Telecommunication* was not reached until well after the exclusivity period had expired, which was also the case here. (*Id.* at 5.)

Appellant argues FedBiz's argument requiring Appellant to recertify its size, under 13 C.F.R. § 121.404(g)(2)(ii)(D) after VFO's acquisition, is a new issue on appeal because it was not addressed in the size determination. (*Id.* at 6-7.) Appellant finds FedBiz's argument meritless and points out that the change in the regulations occurred after the date upon which Appellant's size is determined. (*Id.* at 7.) Further, Appellant argues the regulation was not intended to cause a concern to become ineligible for an award, but would prevent an agency from counting such award toward its small business goals. (*Id.* at 7-8.)

H. FedBiz's Objection to Appellant's Motion and Reply

On November 6, 2018, FedBiz filed an Objection to Appellant's Motion to Reply and its Reply to FedBiz's Response to the Appeal. FedBiz argues Appellant's Reply will only be permitted if the administrative judge directs such a reply under 13 C.F.R. § 134.309(d). (FedBiz's Objection, at 1.) FedBiz highlights Appellant waited ten days after receipt of FedBiz's Response before filing its Motion to Reply and its Reply to FedBiz's Response. (*Id.*) Therefore, Appellant has failed to act in a timely manner and to demonstrate good cause why the Reply should be permitted. (*Id.*)

FedBiz argues *Telecommunication Support Service, Inc.*, SBA No. SIZ-5953 (2018), was available two weeks prior to the close of record, allowing for Appellant to timely respond before the record closed. (*Id.* at 2.) Further, Appellant fails to show good cause why such Reply should be permitted where Appellant is simply restating its arguments already made in its Appeal. Also, just as *Telecommunication* was unavailable to Appellant, it was also unavailable to the Area Office, meaning the Area Office did not err in not relying upon it in its decision. (*Id.* at 2.)

With respect to the requirement of Appellant to recertify its size after its acquisition by VFO, FedBiz contends it raised this same argument in its size protest and Appellant addressed FedBiz's arguments in its response to the protest and should have also addressed the issue in its Appeal. (*Id.* at 3.)

III. Discussion

A. Standard of Review and Threshold Issues

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).

I GRANT Appellant's Motion to Reply, because FedBiz's Response raises issues the size determination did not address, although the issues are not new issues on appeal, because FedBiz raised them in its protest. In the interest of a complete record, I also admit FedBiz's Reply to Appellant's Motion.

B. Analysis

First, I must address FedBiz's argument that Appellant should be deemed other than small because it failed to recertify its size at least 30 days after it was acquired by VFO, as required by 13 C.F.R. § 121.404(g)(2). While the Area Office failed to address the issue, since it was an argument FedBiz raised in its protest, which was available to Appellant. Therefore, it is not a new argument raised on appeal.

Appellant argues the rule was not intended by SBA to cause a concern to become ineligible if an acquisition occurs after it certifies as small and before an award is made, but instead prohibits an agency to count the award to its small business goals. Appellant also argues that even if the rule does require a concern to recertify after an acquisition, the clarification provided by SBA addressing this point of confusion was not in effect at the time of the instant procurement and therefore does not apply to Appellant here. I agree with Appellant that it was not required to recertify its small business status for this procurement.

The rule in question states:

A concern that represents itself as a small business and qualifies as small at the time of its initial offer (or other formal response to a solicitation), which includes price, is considered to be a small business throughout the life of that contract. This means that if a business concern is small at the time of initial offer for a Multiple Award Contract (see § 121.1042(c) for designation of NAICS codes on a Multiple Award Contract), then it will be considered small for each order issued against the contract with the same NAICS code and size standard, unless a contracting officer requests a new size certification in connection with a specific order. Where a concern grows to be other than small, the procuring agency may exercise options and still count the award as an award to a small business. *However, the following exceptions apply:*

(2)(i) In the case of a merger, sale, or acquisition, where contract novation is not required, the contractor must, within 30 days of the transaction becoming final, recertify its small business size status to the procuring agency, or inform the procuring agency that it is other than small. *If the contractor is other than small, the agency can no longer count the options or orders issued pursuant to the contract, from that point forward, towards its small business goals.* The agency

and the contractor must immediately revise all applicable Federal contract databases to reflect the new size status.

(ii) Recertification is required:

...

(D) If the merger, sale or acquisition occurs after offer but prior to award, the offeror must recertify its size to the contracting officer prior to award.

13 C.F.R. § 121.404(g) (emphasis added). OHA has held that a rule pertaining to Service-Disabled Veteran-Owned Small Business Concerns (SDVO SBCs) mirroring the rule here “*does not* prohibit the procuring agency from exercising these options or issuing orders, and does not otherwise deem the concern ineligible for award” if it is no longer small due to a merger. *In the Matter of Analytic Strategies, Inc.*, SBA No. VET-268, at 16 (2018). Instead, the rule provides that agencies will not be able to count such awards and orders toward their small business goals. *Id.*

In response to the ruling in *Analytic Strategies*, SBA issued a direct final rule stating in part:

It has been brought to SBA's attention that as drafted, it is not clear which sentence or clause the final sentence is referencing. It was SBA's intent, as made clear in the proposed and final rule enacting this regulation, entitled Acquisition Process:

Task and Delivery Order Contracts, Bundling, Consolidation, 78 FR 61114 (Oct. 2, 2013), that SBA wanted the sentence and the referenced exceptions to be applied to the entirety of the preceding paragraph. 78 FR 61114, 61119-20 (Oct. 2, 2013). Therefore, SBA is adding additional language to clearly align the paragraph to the intent of the regulation. This rule is not intended to make any substantive change to the paragraphs.

...

3. Amend § 121.404 by revising the last sentence of the introductory text of paragraph (g) to read as follows:

§ 121.404 When is the size status of a business concern determined?

* * * * *

(g) * * * However, the following exceptions apply to this paragraph (g):

* * * * *

83 Fed. Reg. 12849 (Mar. 26, 2018).

This final rule took effect on May 25, 2018. The RFP was issued on October 5, 2017 and Appellant's offer was submitted on December 7, 2017. The final rule did not take effect until nearly 9 months after the RFP was issued. Therefore it is not applicable to the instant procurement. While FedBiz argues that the original rule was intended to render an entity ineligible for award in the event of a merger, sale, or acquisition, relying upon the preamble to the amended rule, OHA rejected this argument in *Analytic Strategies*, and the Agency's *post hoc* discussion in the preamble to the new regulation fails to offer a substantial enough argument to reconsider OHA's decision. Accordingly, I reject FedBiz's argument that Appellant was required to recertify its size after the acquisition by VFO.

Although Appellant is not disqualified from being awarded the procurement based on 13 C.F.R. § 121.404(g)(2), I must turn to the issue of whether the size determination is based upon a clear error of fact or law. The issue here is whether the LOI in question is an agreement in principle that must be given present effect. The controlling rule provides:

Affiliation arising under stock options, convertible securities, and agreements to merge.

(1) In determining size, SBA considers stock options, convertible securities, and agreements to merge (including agreements in principle) to have a present effect on the power to control a concern. SBA treats such options, convertible securities, and agreements as though the rights granted have been exercised.

(2) Agreements to open or continue negotiations towards the possibility of a merger or a sale of stock at some later date are not considered “agreements in principle” and are thus not given present effect.

(3) Options, convertible securities, and agreements that are subject to conditions precedent which are incapable of fulfillment, speculative, conjectural, or unenforceable under state or Federal law, or where the probability of the transaction (or exercise of the rights) occurring is shown to be extremely remote, are not given present effect.

(4) An individual, concern or other entity that controls one or more other concerns cannot use options, convertible securities, or agreements to appear to terminate such control before actually doing so. SBA will not give present effect to individuals', concerns' or other entities' ability to divest all or part of their ownership interest in order to avoid a finding of affiliation.

13 C.F.R. § 121.103(d).

The Area Office found Appellant other than small under this rule because it concluded the execution of the LOI on November 17, 2017 created an agreement in principle to merge with VFO, which must be given present effect as of the date of its execution. Therefore, the Area Office found Appellant affiliated with VFO.

In support of its determination, the Area Office relied on *Size Appeal of WRS Infrastructure and Environment, Inc.*, SBA No. SIZ-5007 (2008). There, OHA found a letter of intent to be an agreement in principle. The letter stated that “[b]ased on the review we have completed over the past several weeks and our discussions to date, WRS Holding Company is pleased to confirm its intent to purchase, directly or through an affiliate” all of the capital of the alleged affiliate. *Id.* at 1. While the letter stated it was confirming WRS's intent to purchase the entity and included a proposed price and a breakdown on how the final price would be determined, it described itself as non-binding. *Id.* at 1-2. It also included an escrow provision designed to secure payment of any indemnification obligations under the final stock purchase agreement; aged receivables; confirmatory due diligence; and the definitive stock purchase agreement, which would contain customary indemnification provisions. *Id.* at 2. The letter also provided pre-signing and closing conditions; an exclusivity clause requiring the seller not to act to encourage offers from other parties and to identify any offers from any third parties; and an integration clause. *Id.*

In *WRS Infrastructure*, OHA reviewed the letter, considered the stated price, the exclusivity clause, the parties' stated intent to execute the stock purchase agreement consistent with the letter's terms, and the fact that the parties ultimately consummated the transaction consistent with the terms of the letter. Thus, OHA found the letter to be an agreement in principle, to be given present effect. *WRS Infrastructure*, SBA No. SIZ-5007, at 8 (2008).

OHA further emphasized that in understanding the rule of attributing present effect to a document, that SBA's actions in determining the size of a protested concern “involve time-restricted procurements that cannot wait for the closing of a deal some weeks hence. That is why the rule says an agreement in principle is enough.” *Id.* at 9. OHA also held that an agreement need not be legally binding to be found to be an agreement in principle. *Id.*

All agreements leading toward an agreement to merge are not treated as an agreement in principle, requiring present effect. *See* 13 C.F.R. § 121.103(d)(2-3). Reviewing other cases applying the rule, OHA found no agreement in principle where there is no document memorializing any agreement, and the parties confirmed with the Area Office that no agreement had been reached at the time the protested concern submitted its offer for the subject procurement. *Size Appeal of Crop Jet Aviation, Inc.*, SBA No. SIZ-5933 (2018).

OHA has held that a non-binding tentative proposal that did not include a price, that was subject to numerous conditions, and where due diligence remained to be completed, and there was no indication that the letter had been accepted by the other party, was not an agreement in principle. *See Size Appeal of Nuclear Fuel Services, Inc.*, SBA No. SIZ-5324, at 8 (2012). OHA also found the fact that a final agreement was not reached until eight months after the initial proposal further suggested the proposal was not an agreement between the parties. *Id.*

In *Size Appeal of the W.I.N.N. Group, Inc.*, SBA No. SIZ-5360 (2012) OHA held that a non-binding offer that did not include a set price, did not require exclusivity, and was carefully conditioned on extensive due diligence was not an agreement in principle. The offer letter in *W.I.N.N. Group* was conditioned on an extensive due diligence examination of all contractual instruments, third party and government audit reports, rosters of employees and contractors, financial reports, and assets. *Id.* at 9. Thus, the buyer was free to withdraw from the transaction if the information found was not satisfactory. *Id.* OHA concluded the purchasing concern had “left itself too large an out [] to conclude that it has actually agreed to anything.” *Id.* at 9. In upholding the Area Office's findings that the letter was not an agreement in principle, OHA highlighted the comprehensive record that included documentation of negotiations between the buyer and seller evidencing the specific outstanding issues that remained to be resolved by the date upon which size was determined. *Id.* at 10. In addition, the seller had not accepted the terms of the letter, and was actively in negotiations with other offerors after the letter was executed. *Id.* at 10. The fact that the seller was in negotiations with another potential buyer “weigh[ed] very strongly against, indeed almost preclude[d], a finding that there was an agreement in principle. . .” *Id.* at 11.

In *Size Appeal of Telecommunication Support Service, Inc.*, SBA No. SIZ-5953 (2018), OHA found that the Area Office erred in attaching present effect to an agreement to negotiate that was subject to multiple conditions. OHA concluded the agreement in question was an “opportunity to evaluate an opportunity.” *Id.* at 10. The agreement stated it was “not intended to create a binding contract, but [was] intended to evidence the parties' mutual willingness to work together in good faith to consummate the transaction contemplated.” *Id.* at 2. The agreement set a price that was contingent upon certain assumptions and the seller meeting certain financial targets. The seller was explicitly permitted to withdraw from negotiations if the terms of the final agreement were materially adverse to the seller as compared to the agreement to negotiate. In addition, the agreement to negotiate required an extensive due diligence review be completed before a deal could be finalized. *Id.* at 10.

The parties entered into the agreement to negotiate in May of 2017, which included an exclusivity provision that ended on July 31, 2017. *Id.* at 1. While due diligence was undertaken, concern grew about the seller meeting its financial targets. The deal went “on hold” for two months while the seller worked to improve its financial performance to meet the buyer's standards, allowing the original deadline to pass without the conclusion of a deal. *Id.* at 2. The parties subsequently extended the exclusivity period to August 31, 2017. The buyer discovered additional issues with the seller's performance in August 2017, and the seller refused to extend the exclusivity period past August 31, 2017. *Id.* The alleged affiliate of the seller submitted an offer for a procurement on or before August 23, 2017, making it the date upon which size was determined. *Id.* at 1. After August 31, 2017, the seller notified the buyer that it was entertaining offers from other parties. *Id.* at 8. The parties reached a final agreement on September 14, 2018. In not finding the LOI to be an agreement in principle, OHA found “it would confound logic to hold that an agreement in principle existed at the time to determine size, yet that same agreement could fall apart after the date to determine size based on the unilateral actions of one of the parties.” *Id.* at 11.

An analysis of cases involving a potential agreement in principle are fact-intensive and rely on a review of the totality of the circumstances in order to make a final decision on whether

the document in question is an agreement in principle. Here, after reviewing the LOI, the circumstances surrounding the negotiations between Appellant and VFO, the arguments presented by Appellant and FedBiz, and applying relevant regulations and OHA case law, I find that there is tangible evidence of an agreement in principle.

Appellant asserts that the LOI should not be treated as an agreement in principle because it was only an agreement to engage in exclusive negotiations under 13 C.F.R. § 103(d)(2). However, I agree with the Area Office that it is clear Appellant and VFO began negotiations weeks and possibly months before the LOI was executed. Appellant was on VFO's radar as early as 2015. In July of 2017, the parties entered into a mutual nondisclosure agreement. In the Fall of 2017, VFO provided Appellant with a preliminary indication of interest and a potential purchase price, which Appellant rejected. The revised indication of interest, or LOI, was mutually signed and executed on November 17, 2017, only after the parties had reached an agreed upon price. The fact that one price had already been proposed and rejected before the execution of the final LOI with a price that was deemed more favorable by Appellant is a clear indication that negotiations were not prompted by the LOI, but had been underway well before the LOI was finally signed and executed by the parties.

The fact that this LOI includes a previously negotiated definite set price, without any conditions that would vary that price, supports a finding that the LOI is an agreement in principle. *See W.I.N.N. Group, Inc.*, SBA No. SIZ-5360, at 2 (2012) (finding no agreement in principle where a range of prices were presented that had yet to be negotiated); *see also Telecommunication Support Service, Inc.*, SBA No. SIZ-5953, at 2 (2018) (finding no agreement in principle where a set price was provided, “but only on the condition that the company meet certain financial targets.”) Additionally, not only had the parties agreed upon a price, they had also agreed upon the structure of the purchase price of Appellant, [XXXXXXXXXXXXXXXXXXXXX].

Appellant argues that the LOI was not an agreement in principle because it was described as “non-binding.” However, OHA has held the fact that an agreement is described as “non-binding” does not establish that it is not an agreement in principle. *See WRS Infrastructure*, SBA No. SIZ-5007 (2008) (finding an agreement in principle despite the agreement being described as “non-binding.”)

Appellant contends the LOI was not an agreement in principle because it required a due diligence review before proceeding with a final transaction agreement. However, the LOI only required a confirmatory due diligence review as opposed to a more extensive due diligence review. *See WRS Infrastructure*, SBA No. SIZ-5007, at 2 (2008) (finding an agreement in principle where the buyer only required a confirmatory due diligence review); *see also W.I.N.N. Group, Inc.*, SBA No. SIZ-5360, at 2 (2012) (finding no agreement in principle where the buyer required a due diligence review including a “review of contracts, validation of payables and receivables, indirect and fringe rates, explanation of payroll practices, explanation of outstanding debt and specific plans for resolution, and the inclusion of real and intellectual property in the sale.”) Further, in light of VFO proposing a price to purchase all of Appellant's equity, it is reasonable to conclude that at the time of the execution of the LOI, VFO had previously

completed some level of review of Appellant's valuation in order to propose the multiple purchase prices offered to Appellant.

Additionally, the results of the due diligence review here suggests the LOI was not as conditional as Appellant maintains. When the confirmatory due diligence review revealed that Appellant's financial performance was "soft," VFO did not withdraw from the LOI or require Appellant to make any improvements in its financial performance to continue negotiations. *See Telecommunications*, SBA No. SIZ-5953, at 2 (2018) (finding no agreement in principle where negotiations ceased for two months after certain unsatisfactory financial information was revealed as a result of the due diligence review to allow the seller to work to improve its financials to meet the buyer's standards.) Instead, VFO worked to ensure that the acquisition took place by seeking additional approval from its Board to confirm the deal. When Appellant was under the impression that the transaction was nearly impossible due to VFO's findings of Appellant's soft performance, VFO reassured Appellant that it was merely a "misunderstanding" and explained that all VFO would need to do to proceed with the transaction was to seek additional approval from its shareholders. In fact, when the parties reached an impasse as a result of the misunderstanding, VFO offered an olive branch to Appellant in the form of a favorable executive compensation package as a further incentive for the parties to continue negotiations.

Appellant contends the LOI should not be considered an agreement in principle because it does not contain all of the essential terms of a purchase agreement. Although Appellant provides a thorough analysis comparing the LOI to the SPA, an agreement need not rise to the level of detail provided in a final purchase agreement to constitute an agreement in principle. Instead, what is required for a finding of an agreement in principle is sufficient evidence that the parties have agreed that a transaction to merge is to take place at some time in the future. Very similar to the LOI in *WRS Infrastructure*, the LOI contained a set price, and, while it was described as non-binding, included provisions with terms describing procedure concerning escrow and indemnification, required confirmatory due diligence, and contained an exclusivity provision. Although Appellant highlights that a specific buyer was not identified here, the same was true for the LOI in *WRS Infrastructure*, where either directly or through an affiliate, the seller would be purchased by the buyer. In this case, Appellant was purchased by a subsidiary of VFO. Additionally, the buyer in *WRS Infrastructure*, like VFO, was eager to conclude the deal expeditiously, which subsequently occurred.

Appellant argues the LOI could not have been an agreement in principle because there was a complete breakdown in negotiations. However, it is not all unusual for there to be disagreements and possibly "cooling off" periods in the process of negotiating a multi-million dollar transaction. To conclude that an instance of impasse absolutely precludes a finding of an agreement in principle is a sweeping generalization that I cannot make in light of the fact-intensive nature of matters concerning contract negotiations. Furthermore, as Messrs. Javaheri and Simpson stated, the breakdown in communication between Appellant and VFO was based on a misunderstanding that had a clear solution as opposed to an issue that the parties simply could not resolve. I must also note the relatively short duration and the timing of this particular breakdown in communication, which lasted approximately 7 business days during the holiday season.

Appellant contends the Area Office erred in not analyzing *W.I.N.N. Group* in the size determination. However, the agreement in *W.I.N.N. Group* is readily distinguishable from the LOI here. There was no set price contained in the letter in question in *W.I.N.N. Group*. See *W.I.N.N. Group, Inc.*, SBA No. SIZ-5360, at 2 (2012). Instead, the buyer provided a range of purchase prices to the buyer. The LOI here provided a set price with a payment structure. In *W.I.N.N. Group*, the buyer was free to withdraw from negotiations depending on an extensive due diligence review that had yet to be completed. *Id.* at 9. There was no such explicit “out” for VFO as there was for the buyer in *W.I.N.N. Group*. Further, there was no indication that the seller in *W.I.N.N. Group* assented to the offer. *Id.* Here, both parties signed and executed the LOI. Lastly, and arguably most importantly, the seller was in active negotiations with other suitors during the time of the negotiations with the ultimate buyer. *Id.* at 2. Here, there was an exclusivity clause prohibiting such behavior and there has been no indication that Appellant violated that provision or entertained any other buyers after the exclusivity period expired. Therefore, I find that the Area Office did not err in not relying on *W.I.N.N. Group* in the size determination, because the facts in that case were significantly different from the facts in the instant matter.

Although Appellant argues *Telecommunications* is “directly on point” here, I find that the letters in question and the circumstances surrounding the negotiations are not as similar as Appellant suggests. First, in *Telecommunications*, the price was set, but was contingent upon the findings in the due diligence review, as distinct from the LOI here, which included no provisions making the set price conditional on any outcome of the due diligence. *Telecommunication Support Service, Inc.*, SBA No. SIZ-5953, at 2 (2018). Second, when concern grew regarding the financial performance of the seller, negotiations ceased until the seller could meet certain financial targets prescribed in the letter. *Id.* Only after the seller could reach those targets did negotiations resume. Appellant seeks to compare a halt in negotiations of two months in *Telecommunications*, to the break in negotiations that took place here, which lasted merely a week during the holiday season. I find that the two situations are not, in fact, similar. Although there was an exclusivity period provided in *Telecommunications*, the seller eventually refused to extend the exclusivity of their agreement and actively sought other buyers when that exclusivity period expired. *Id.* at 6. To my calculation, the SPA, here, was executed just two weeks after the exclusivity period of the LOI expired, and there has been no indication that Appellant ever entertained any buyers during or after the exclusivity period. This suggests Appellant was committed to being purchased by VFO, or one of its affiliates, even after the exclusivity period had expired, because the LOI was an agreement in principle.

I find the LOI between Appellant and VFO was an agreement in principle, which must be given present effect at the time of its execution. Thus, the LOI, an agreement for the purchase of Appellant, must be treated as if the merger took place on November 17, 2017, the date the LOI was signed and executed. See 13 C.F.R. § 121.103(d)(1). As a result, Appellant and VFO were affiliated as of December 7, 2017, the date Appellant submitted its offer for the instant procurement, and the date upon which its size must be determined. The size standard for NAICS code 334220, Radio and Television Broadcasting and Wireless Communications Equipment Manufacturing, is 1,250 employees. Appellant admitted it would be too large for the instant procurement if it were found affiliated with VFO. Therefore, Appellant is other than small for the instant procurement.

IV. Conclusion

Appellant has failed to establish that the size determination is based upon any clear error of fact or law. Accordingly, I DENY the instant Appeal, and I AFFIRM the size determination. This is the final decision of the Small Business Administration. *See* 13 C.F.R. § 316(d).

CHRISTOPHER HOLLEMAN
Administrative Judge