United States Small Business Administration
Office of Hearings and Appeals

IN THE MATTER OF:	
Firewatch Contracting of Florida, LLC	SBA No. VET-137
Appellant	Decided: August 1, 2008
Solicitation No. VA-101-07-IB-0039 U.S. Department of Veterans Affairs	

APPEARANCES

Victoria Johnson, Esq., Baker & Hostetler LLP, Cleveland, Ohio, for Appellant.

William L. Bruckner, Esq., Bruckner & Walker, LLP, San Diego, California, for KEVCON, Inc.

Sam Q. Le, Esq., Office of General Counsel, Small Business Administration, Washington, D.C., for the Agency.

DECISION

PENDER, Administrative Judge:

I. Jurisdiction

This appeal is decided under the Small Business Act of 1958, 15 U.S.C. § 631 *et seq.*, and 13 C.F.R. Parts 125 and 134.

II. Issue

Whether the Director for Government Contracting (D/GC) for the U.S. Small Business Administration (SBA) made a clear error of fact or law in determining that Firewatch Contracting of Florida, LLC (Appellant) is not controlled by a Service-Disabled Veteran. *See* 13 C.F.R. § 125.10(d) and 13 C.F.R. § 134.508.

III. Background

A. Protest and D/GC Determination

On January 17, 2008, the U.S. Department of Veterans Affairs, Office of Construction & Facilities Management, issued the subject sealed bid solicitation as a set-aside for Service-Disabled Veteran-Owned Small Business Concerns (SDVO SBC). The Contracting Officer (CO) opened bids, including Appellant's, on March 27, 2008. On May 13, 2008, the CO notified unsuccessful offerors that Appellant was the apparent successful offeror.

On May 13, 2008, KEVCON, Inc. (Kevcon) protested Appellant's SDVO SBC status with the CO.[1] Kevcon's protest alleged that Mr. Melvin Lowe, Appellant's service-disabled veteran owner, did not have the ability to control Appellant because Mr. Lowe resides in Ohio and Appellant is located in Florida. Kevcon also alleged that Appellant's President, Mr. Christopher Valerian, who is not a service-disabled veteran, actually controls and operates Appellant.

On June 9, 2008, the CO referred Kevcon's protest to the SBA Office of Government Contracting. On June 16, 2008, SBA notified Appellant of the protest and requested that Appellant provide a variety of documents to prove its SDVO SBC status.

On June 20, 2008, Appellant filed its response to the protest. Appellant submitted Mr. Lowe's proof of service-disabled veteran status and Appellant's corporate governance documents, including its Operating Agreement. Appellant stated that it is an LLC that was established November 1, 2006. Mr. Lowe, a service-disabled veteran, owns sixty percent of the membership interests in Appellant and serves as Appellant's Managing Member, Chief Executive Officer (CEO), and Secretary. Mr. Valerian, who does not claim service-disabled veteran status, owns the remaining forty percent of Appellant's membership interests and is Appellant's President and Treasurer. Appellant further asserted that while Mr. Lowe resides in Ohio and Appellant is located in Florida, Mr. Lowe nonetheless controls Appellant remotely through travel, telephone, email, and contact with employees at Appellant's local office in Tampa, Florida.

On July 1, 2008, the D/GC issued a determination finding Appellant was not controlled by one or more service-disabled veterans at the time of its bid and thus Appellant does not qualify as a SDVO SBC.

The D/GC found that Appellant satisfied the requirements of 13 C.F.R. § 125.9 because Mr. Lowe, a service-disabled veteran, directly and unconditionally owns at least fifty-one percent of Appellant. The D/GC found, however, that Mr. Lowe's sixty percent interest in Appellant was insufficient to overcome Appellant's supermajority voting requirements as set

[1] Kevcon also protested Appellant's size status. On June 19, 2008, the AD/GC also filed a size protest against Appellant with the SBA, Office of Government Contracting, Area III (Area Office). On July 15, 2008, the Area Office found Appellant to be other than small under the $31 million size standard. Appellant's size is not the subject of this appeal.

forth in its Operating Agreement, Section 7.1(c). Specifically, the D/GC concluded that Mr. Lowe is unable to remove officers of the company, change officer compensation, or appoint a new managing member without seeking the approval of members holding at least sixty-seven percent of the ownership interests. Accordingly, the D/GC concluded that Appellant was not controlled by one or more service-disabled veterans at the time of its offer on the instant solicitation, in violation of 13 C.F.R. § 125.10(d).

B. Appeal

On July 15, 2008, Appellant filed the instant appeal of the D/GC's determination with the SBA Office of Hearings and Appeals (OHA). Appellant contends that Mr. Lowe controls Appellant because he is able to overcome the supermajority voting requirements of Appellant's Operating Agreement. Appellant asserts that its Operating Agreement, Section 7.1(a), provides that the management and control of Appellant and its day-to-day operations is vested exclusively with Mr. Lowe. Further, Section 7.1(c) provides that Mr. Valerian, as President/Treasurer, is subject to the direction and control of the Managing Member, Mr. Lowe. Thus, Appellant maintains the Mr. Lowe is vested with exclusive control over Appellant and its officers, "effectively nullifying any need to remove the President/Treasurer by virtue of Mr. Lowe's ability to direct and control the actions of [Appellant's] officers." Appeal, at 3.

Next, Appellant argues that the Area Office incorrectly found that Mr. Lowe needs to seek the approval of Mr. Valerian to change the compensation of officers. Appellant maintains that the Operating Agreement, Section 7.1(c), states that officers shall not receive compensation and further neither the Chief Executive Officer/Secretary nor the President/Treasurer receives any compensation. Notwithstanding these provisions, Appellant contends that any future decision to compensate officers would require Mr. Lowe's consent.

Appellant also asserts the Area Office committed clear error by finding that Section 7.2 of the Operating Agreement prohibits Mr. Lowe from appointing a new managing member without a supermajority. Appellant contends that Section 7.2 addresses a situation where the managing member has died, becomes incompetent, refuses to serve, or has resigned. Appellant asserts that "[i]t is the occurrence of a legal disability, such as death or incompetence of Mr. Lowe, that would prohibit Mr. Lowe from appointing a new Managing Member, not the inclusion of a provision in the Operating Agreement addressing the replacement of the Managing Member in such event." Appeal, at 3.

Finally, Appellant maintains that it is a two-member company consisting of Mr. Lowe (Managing Member, CEO, and sixty percent owner) and Mr. Valerian (President, Treasurer, and forty percent owner) and all decisions require Mr. Lowe's consent.

On July 24, 2008, Appellant moved to supplement its appeal in light of a recent OHA decision, *Size Appeal of EA Engineering, Science, and Technology, Inc.*, SBA No. SIZ-4973 (2008) (*EA Engineering*). Appellant represented that counsel for SBA and Kevcon do not object to the motion. Because of the relevance of the case and the fact that the case had not been published prior to the filing deadline for Appellant's appeal, Appellant's motion to supplement its appeal is GRANTED. 13 C.F.R. § 134.207(b).

Appellant argues that similar to the Area Office's holding in *EA Engineering*, which was reversed on appeal to OHA, the D/GC here relied on a blanket prohibition against supermajority requirements. This blanket prohibition ignores the reality of passive investors in small businesses who require some degree of control over their investments, thus necessitating supermajority provisions in extraordinary business decisions. Appellant contends the supermajority provisions found in Sections 7.1, 7.2, and 7.3 of its Operating Agreement involve only extraordinary events comparable to the supermajority provisions that OHA found did not evince negative control in *EA Engineering*.

Appellant also maintains that the D/GC's reading of 13 C.F.R. § 125.10(d) frustrates the requirements of 13 C.F.R. § 125.9, which allow an SDVO SBC to take the form of a limited liability company so long as the service-disabled veteran unconditionally owns at least fifty-one percent of the member interest in the company. By requiring a service-disabled veteran to have control over all decisions, as set forth in 13 C.F.R. § 125.10(d), Appellant argues the D/GC is prohibiting a 49 percent investor from any control over his/her investment, even in extraordinary circumstances. Further, Appellant argues that the D/GC's interpretation of 13 C.F.R. § 125.10(d) is at odds with 13 C.F.R. § 125.10(a), and the subsections should be read together. Specifically, the definition of control set forth in 13 C.F.R. § 125.10(a) addresses control over long-term decision-making and day-to-day management and, unlike 13 C.F.R. § 125.10(d), does not specify that a service-disabled veteran control all long-term decisions.

C. SBA Response

On July 24, 2008, SBA filed its response to the appeal. SBA asserts the D/GC properly found Appellant was not controlled by a service-disabled veteran based on its Operating Agreement, which provides that a 67 percent supermajority must approve the appointment, removal, or compensation of officers, and the appointment of a new managing member. SBA argues Appellant's contention that Mr. Lowe's consent is required for all corporate decisions is irrelevant because Mr. Lowe, with only a sixty percent interest, cannot control all decisions unilaterally as required by 13 C.F.R. § 125.10(d). Instead, in order to overcome the supermajority voting requirements, Mr. Lowe would need the consent of Mr. Valerian, Appellant's co-owner, who is not a service-disabled veteran.

Additionally, SBA argues that *EA Engineering* is inapplicable as this case addressed supermajority provisions in extraordinary corporate events (altering the firm's charter or bylaws, issuing additional shares of stock, or entering into a substantially different business). In contrast, the supermajority provisions in Appellant's Operating Agreement concern management decisions that affect Appellant's daily operations and concern fundamental corporate decisions. Moreover, SBA argues that *EA Engineering* was limited to the negative control provisions in SBA's size regulations, 13 C.F.R. § 121.103(a)(3), and did not interpret SDVO SBC regulations.

Finally, SBA asserts that because Appellant has been found other than small by the SBA Area Office, Appellant is ineligible for award of the instant solicitation regardless of the outcome of this appeal. Thus, SBA asserts the appeal could also be dismissed as moot under 13 C.F.R. § 134.509(a)(4).

D. Kevcon's Response

On July 24, 2008, Kevcon filed its response in support of the D/GC's determination. Kevcon argues that Mr. Lowe was not listed as a managing member in Appellant's Operating Agreement on the date it submitted its bid (the Articles of Organization were subsequently amended), in violation of 13 C.F.R. § 125.10(d) ("In the case of a limited liability company, one or more service-disabled veterans . . . must serve as managing members. . . ."). As such, Kevcon argues Appellant was not a valid SDVO SBC at the time of its bid.

Kevcon then sets forth the various decisions as listed in Appellant's Operating Agreement that require a supermajority (67 percent) membership interest. Kevcon maintains that Mr. Lowe's sixty percent ownership interest is insufficient to overcome the supermajority requirements and thus Mr. Lowe does not control all business decisions as required by 13 C.F.R. § 125.10(d).

IV. Discussion

A. Timeliness and Standard of Review

Appellant filed its appeal petition within 10 business days of receiving the D/GC's determination, and thus the appeal is timely. 13 C.F.R. § 134.503.

The standard of review for SDVO SBC appeals is whether the D/GC's determination was based on clear error of fact or law. 13 C.F.R. § 134.508. In determining whether there is a clear error of fact or law, OHA does not evaluate whether a concern met the eligibility requirements of 13 C.F.R. §§ 125.9 and 125.10 *de novo*. Rather, OHA reviews the Record to determine whether the D/GC based her decision upon a clear error of fact or law. 13 C.F.R. § 134.508; *see Size Appeal of Taylor Consultants, Inc.*, SBA No. SIZ-4775, at 10-11 (2006) (discussing the clear error standard that is applicable to size appeals and SDVO SBC appeals). Consequently, I will disturb the D/GC's determination only if I have a definite and firm conviction the D/GC erred in making a key finding of law or fact.

B. Merits of the Appeal

Pursuant to 13 C.F.R. § 125.10(a), a service-disabled veteran must manage and control a concern's daily business operations for the concern to qualify as an SDVO SBC. In the case of a limited liability company, one or more service-disabled veterans must serve as managing members with control over *all decisions* of the limited liability company. 13 C.F.R. § 125.10(d).

Appellant is an LLC with sixty percent of its membership interests owned by its Managing Member and service-disabled veteran, Mr. Lowe. Appellant's other member, Mr. Valerian, owns a forty percent membership percentage. Appellant's Operating Agreement, Section 7.1(a), provides that the management and control of Appellant is vested exclusively in Mr. Lowe; this control, however, is constrained by Section 7.1(c), which provides:

Officers. Members holding at least 67% of the Membership Percentages may

> appoint such officers as such Members deem reasonably necessary to effectuate the purposes and the *operation* of the Company, which may include, without limitation, a Chief Executive Officer, a President, one or more Vice Presidents, a Secretary, an Assistant Secretary and a Treasurer (collectively, the "Officers") . . . The Officers, subject to the direction and control of the Managing Member, shall do all things and take all actions necessary to run the business of the Company. Each Officer shall have the duties assigned to him or her by the Managing Member and the Members. Except as determined by the Managing Member and the Members holding at least 67% of the Membership Percentages, no Officer of the Company shall receive any compensation for services rendered to the Company by such person in such capacity. Any Officer may be removed at any time, with or without cause, by the Members holding at least 67% of the Membership Percentages . . . Any vacancy in any office may be filled by the Members holding at least 67% of the Membership Percentages.

(emphasis added).

I find that Section 7.1(c) provides that Mr. Lowe cannot hire or fire the officers needed to operate Appellant without the consent of Mr. Valerian, who does not claim service-disabled veteran status, *e.g.*, Mr. Lowe cannot fire Mr. Valerian unless Mr. Valerian agrees to be fired. Nor can Mr. Lowe independently overcome the supermajority voting requirements to establish officer compensation.

Because 13 C.F.R. § 125.10(d) provides that a service-disabled veteran managing member must have control over all decisions, this member must necessarily have control over the types of fundamental decisions delineated in Section 7.1(c) (the ability to hire, fire, and set the pay for officers) as requiring a supermajority vote. The fact that Mr. Lowe's consent is required for these fundamental decisions does not alter the fact that Mr. Lowe does not have the 67 percent membership interest to control these decisions, as mandated by 13 C.F.R. § 125.10(d). Therefore, I find the D/GC did not commit clear error in concluding that Appellant's 67 percent supermajority voting requirements prevent Mr. Lowe, with a sixty percent membership interest, from controlling *all decisions* of Appellant as required by 13 C.F.R. § 125.10(d).

I also find *EA Engineering* distinguishable as that case was limited to the negative control provisions in SBA's size regulations, 13 C.F.R. § 121.103(a)(3), and did not interpret SDVO SBC regulations. Further, the controls at issue in *EA Engineering* were extraordinary (non-operational) in nature and, in contrast to the instant case, did not limit the right of the controlling interest to hire, fire, or pay corporate officers responsible for operating the company.

Accordingly, I find the D/GC did not commit clear error in finding Appellant an ineligible SDVO SBC.

V. Conclusion

Appellant has failed to establish a clear error of fact or law material to the D/GC's determination. Accordingly, the D/GC's determination is AFFIRMED and the Appeal is

DENIED.

This is the final decision of the Small Business Administration. *See* 13 C.F.R. § 134.515(a).

THOMAS B. PENDER
Administrative Judge