United States Small Business Administration
Office of Hearings and Appeals

IN THE MATTER OF:	
Heritage of America, LLC	SBA No. VET-142
Appellant	Decided: November 12, 2008
Solicitation No. VA-101-07-RP-0306 Department of Veterans Affairs	

APPEARANCES

John S. Garcia, Esq., Byrne, Benesch & Villarreal, P.C., Yuma, Arizona, for Appellant.

William Bruckner, Esq., Bruckner & Walker, LLC, for Veterans Vocational Services.[1]

Christopher R. Clarke, Esq., Office of General Counsel, Small Business Administration, Washington, D.C., for the Agency.

DECISION

HOLLEMAN, 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 determination of the Small Business Administration's Director for Government Contracting (D/GC), that Heritage of America, LLC (Appellant), failed to meet the Service-Disabled Veteran-Owned Small Business Concern (SDVO SBC) ownership and control requirements was based on clear error of fact or law. *See* 13 C.F.R. § 134.508.

[1] Mr. Bruckner filed an appearance in this proceeding but, after viewing the file under a protective order, chose not to file a response to the appeal.

III. Background

A. Solicitation and Protest

On June 22, 2007, the Department of Veterans Affairs (VA), in Washington, D.C., issued Solicitation No. VA-101-07-RP-0306 to provide vocational rehabilitation and employment services to veterans with service-connected disabilities. The procurement was set aside for Service-Disabled Veteran-Owned Small Business Concerns (SDVO SBCs). On August 27, 2008, Heritage of America, LLC (Appellant), submitted its offer for this procurement.

The VA awarded the contract to Appellant on July 21, 2008.[2] On July 25, 2008, Veterans Vocational Services (VVS), another offeror, learned of the award and, on July 28, 2008, VVS filed its protest of Appellant's SDVO SBC status with the Contracting Officer (CO). VVS asserted that Appellant's qualifying veteran, Thomas Kiley, is not service-disabled; further, he is neither the President nor the CEO of Appellant.

On August 19, 2008, the CO referred the matter to the Small Business Administration's (SBA) Director for Government Contracting (D/GC) for an SDVO SBC status determination. The D/GC notified Appellant of the protest and requested various documents and a response to the protest allegations. On September 17, 2008, Appellant responded to the D/GC's request with its response to the protest allegations, documentation establishing that Patrick F. Chorpenning is a service-disabled veteran, and copies of Appellant's Articles of Organization, Articles of Amendment, Operating Agreement, minutes, tax returns, and other documents.

According to these documents, Appellant was formed as an Arizona limited liability company (LLC) on January 1, 2004. Section 5 of Appellant's Articles of Organization states, "Management of the limited liability company is reserved to the members." The Appellant's Operating Agreement, effective May 3, 2004, contains the following sections:

> 1.1.C. "Agreement" shall mean this written Operating Agreement. No other document or oral agreement among the Members shall be treated as part of or superseding this Agreement unless it is reduced to writing and it has been signed by all of the Members.
>
> 1.1.O. "Majority-In-Interest" shall mean Members owning an 80% majority of the Percentage Interests who are not in default under this Agreement.
>
> 3.2. Major Decisions. No act shall be taken or sum expended or obligation incurred by the Company or any Member with respect to a matter within the scope of any of the major decisions affecting the Company as defined below. ("Major Decisions"), unless such of the Major Decisions have been approved by a Majority-In-Interest of the Members entitled to vote. The Major Decisions shall be the following:

[2] The VA posted notice of the award on FedBizOpps on August 7, 2008.

A. Selecting depreciation and accounting methods, making elections and making other decisions with respect to treatment of various transactions for federal and state income tax purposes, . . .;

B. Determining compensation of members and whether or not distribution should be made to the Members, . . .;

C. Making any expenditure or incurring any obligation by or on behalf of the Company involving a sum in excess of $10,000.00 for any transaction or group of similar transactions, except for expenditures made and obligations incurred pursuant to a Budget theretofore approved by the Members;

D. Acquire real property;

E. Borrow money for the Company from banks, other lending institutions, the Members or affiliates of the Members; . . .

3.3. Authority of a Member. Subject to the decisions requiring the approval of a Majority-In-Interest of the Members and the provisions of this Agreement, each Member shall be authorized to act on behalf of the Company for the purpose of carrying on its day-to-day business.

7.1 Percentage Interests. The Percentage interests of the Members are as follows:

PFC Education Consulting	51 %
MCF Consulting	12 1/4 %
Heritage Consulting Services, Inc.	12 1/4 %
National Education and Training Services	12 1/4 %
Weaver	12 1/4 %

7.2 Profits and Losses. Subject to Section 7.4, each Member shall share in the Profits and Losses of the Company according to the following shares: 1/5 each.

Protest File, Ex. 3 (Operating Agreement). Section 14.5 provides that Arizona law governs. *Id.*

Appellant also submitted the notice and minutes for a meeting held in May 2008, and Articles of Amendment dated July 2008. This latter states that there are now three members of Appellant, but does not provide their current ownership interests or shares of profits and losses.

In its letter to the D/GC, Appellant stated it currently has three members: Patrick F. Chorpenning d/b/a/ PFC Education Consulting (PCF or Mr. Chorpenning); Michael C. Fugate d/b/a MCF Consulting (MCF), and Heritage Consulting Services, Inc. (HCF). In discussing the control requirements of 13 C.F.R. § 125.10, Appellant stated that Mr. Chorpenning is its President and Chief Executive Officer. Further, Appellant stated:

[a]t an organizational meeting of HOA held in or around April of 2004, in Phoenix,

> Arizona, the members elected Mr. Chorpenning to his position, thereby vesting him with all duties, obligations, and powers of the day-to-day management and administration of the Company and well as the responsibility for the Company's long-term decisions. Although no formal minutes were taken at the meeting (as no such legal requirement exist for the taking of minutes for limited liability companies), the members would agree to provide Affidavits if the SBA so requests as further documentation of this meeting.
>
> Neither the Operating Agreement, nor any other agreement, has disturbed or altered the decision made by the members at the organizational meeting to elect Patrick F. Chorpenning as their President and Chief Executive Officer for all day-to-day management and long-term decision making for the operation of the business. In HOA's Operating Agreement (like most Operating Agreements utilized by limited liability companies in general), certain *extraordinary, atypical, one-time decisions, which are not considered items of "long-term decision-making" or "day-to-day management and administration of business,"* are decisions that must be decided by 80% of the members at large. These *extraordinary, atypical, or one-time decisions* are found in Section 3.2 of the Operating Agreement, and listed as items "A" through "J." Thus, at all times, Patrick F. Chorpenning, as President and C.E.O., is responsible for all "long-term decision making" and "day-to-day management and administration of business."

Protest File, Ex. 3 (Appellant's Letter).

Appellant's 2007 Federal income tax return, Form 1065, Schedule K-1, Line J, shows four members: PFC, HCS, MCF, and Mr. Weaver. For each member, the shares of profit and loss are shown as 25%. For PFC, the share of capital is shown as 51%. For the other three members, the share of capital is shown as 16.33% or 16.34%. Protest File, Ex. 3 (Tax Return).

B. Formal Protest Determination

On September 23, 2008, the D/GC issued her formal protest determination, concluding Appellant was not an eligible SDVO SBC at the time it submitted its offer for this procurement. Although the D/GC found Mr. Chorpenning is an eligible service-disabled veteran (SDV), she also found that he failed to meet the ownership and control requirements for Appellant to be an eligible SDVO SBC.

Regarding ownership, the D/GC noted Appellant's Operating Agreement shows PFC has a 51% interest and each member has a one-fifth right to profits and losses. Next, she noted the 2007 tax return shows equal shares of profit and loss. Then, the D/GC stated SBA considers the right to share in profits and losses to be a key indicator of the true extent of an individual's ownership interest, citing 13 C.F.R. § 124.105(f). She noted, were that not the case, "a 'figurehead owner' could, on paper, be listed as the primary owner of a concern even though he or she was only entitled to nominally share in the concern's profits." The D/GC then concluded, given the discrepancy between Mr. Chorpenning's listed ownership interest (51%) and his interest in profits and losses (25%), that he did not directly and unconditionally own at least 51%

of Appellant. Therefore, Appellant did not satisfy the ownership requirement.

Regarding control, the D/GC first noted the SDV must serve as the managing member of an LLC. Then, she referenced the sections of Appellant's Operating Agreement providing that its business affairs shall be managed by the Members, that major decisions must be approved by a Majority-In-Interest of the Members, and that each Member is authorized to act on its behalf for the purpose of carrying on its day-to-day business. Mr. Chorpenning by himself does not constitute a Majority-In-Interest of the Members. He has no authority to make major decisions independently. Therefore, the D/GC concluded, Appellant did not satisfy the control requirement.

C. The Appeal

On October 6, 2008, Appellant filed the instant appeal. Appellant states that on the offer date it had four Members, and that the interest in it of each remaining member had "increased proportionately" from the earlier percentages. Appellant argues the D/GC made errors of fact and law in concluding that Mr. Chorpenning did not satisfy the SDVO SBC ownership and control requirements.

As for ownership, Appellant first asserts the D/GC made no finding contradicting the evidence in the Operating Agreement that Mr. Chorpenning has a 51% ownership interest. Second, Mr. Chorpenning's 25% share of profits and losses is not "nominal." Third, Appellant asserts the SDVO SBC ownership regulation is silent on the issue of shares of profit and loss, and it was error of law for the D/GC to have relied on 13 C.F.R. § 124.105(f), which not only governs a different SBA program, but also applies to corporations rather than LLCs.

As for control, Appellant first asserts that, as a result of the meeting in Phoenix in April 2004, Mr. Chorpenning has Appellant's highest position and has the authority to make both day-to-day and long-term decisions for Appellant. Second, the D/GC should not have limited her inquiry to the Operating Agreement. Finally, the D/GC misconstrued the term of art "major decisions" in the Operating Agreement to include the decisions covered by the control regulation. Despite OHA decisions to the contrary, some of which Appellant cites, Appellant asserts that "all decisions" must mean something other than "all decisions."

As relief, Appellant requests that I reverse and vacate the D/GC's formal protest determination and conclude that Appellant is an eligible SDVO SBC for the instant procurement. Alternatively, Appellant requests that I remand this matter to the D/GC for further investigation and a new determination.

D. The SBA Response to the Appeal

On October 15, 2008, the SBA filed its response to the appeal and the Protest File on which the D/GC based her determination. SBA asserts the D/GC correctly concluded Appellant was not an eligible SDVO SBC on the day it submitted its offer on the instant procurement.

IV. Discussion

A. Threshold Issues

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, including the Protest File, 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 which 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

1. Two Grounds for Ineligibility

In order to be an eligible SDVO SBC, a business concern must be owned and controlled by a service-disabled veteran. 13 C.F.R. § 125.8(g). It is undisputed that Mr. Chorpenning is a service-disabled veteran. The D/GC concluded Mr. Chorpenning does not own and does not control Appellant; thus, she cited two separate grounds for Appellant's ineligibility as an SDVO SBC — one based on ownership and one based on control. Program ineligibility does not require grounds based on both ownership and control, however. A ground or grounds based on either ownership or control would render a business concern ineligible for the program. *See, e.g., Matter of The Wexford Group International, Inc.*, SDV-105 (2006) (ineligibility based on ownership grounds only); *Matter of Firewatch Contracting of Florida, LLC*, SBA No. VET-137 (2008) (ineligibility based on one control ground). Accordingly, if I determine that either the D/GC's cited ownership ground or her cited control ground is valid, then her ultimate conclusion that Appellant is not an eligible SDVO SBC is also valid and must be affirmed. Based on this principle I will analyze only the cited control ground.

2. Control

The program regulations define an eligible SDVO SBC as a concern whose management and daily business operations are controlled by one or more service-disabled veterans. 13 C.F.R. § 125.8(g)(2). For a limited liability company, these regulations require that 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's Articles of Organization (Articles) do not provide for a managing member. To the contrary, they vest management in the members. Articles, § 5.

Under the governing Arizona law, where an LLC's Articles of Organization do not vest management in one or more managers, management "is vested in the members, subject to any provision in an operating agreement restricting or enlarging" those rights. Ariz. Rev. Stat. § 20-681(A). Appellant's Operating Agreement provides restrictions on certain management actions, such as determining members' compensation, spending more than $10,000 except pursuant to a budget approved by the members, and borrowing money. Operating Agreement, § 3.2. To effect these actions requires a "Majority-In-Interest," defined as 80% of the membership interest. Operating Agreement, §§ 1.1.O., 3.2.

Here, Appellant asserts Mr. Chorpenning has 51% of the membership interest,[3] but even that percentage interest is far short of the 80% that Appellant's Operating Agreement requires in order to effect any of the actions listed in Section 3.2. Thus, Mr. Chorpenning is unable to effect any of those actions himself. The regulations governing SDVO SBC eligibility, however, require that Mr. Chorpenning, as the qualifying SDV, have control over all decisions of Appellant in order to qualify it as an SDVO SBC. The only conclusion therefore, is that Appellant does not satisfy the control requirements because he cannot by himself overcome the "Majority-In-Interest" supermajority requirement.

The Office of Hearings and Appeals (OHA) has decided in similar fashion several other cases involving supermajority restrictions. *See Matter of Technical and Project Engineering,* LLC, SDV-110, at 7 (2006) (SDV with 51% interest does not satisfy control requirement where 55% interest is needed for some actions.); *Matter of IITS-Nabholz, LLC,* VET-114, at 9 (2007) (SDV with 51% is interest not in control where 75% is needed for some actions.); *Matter of CymSTAR LLC,* VET-123, at 7 (2007) (Two SDVs with 63.24% are not in control where 66% is needed for some actions.); *Matter of Firewatch Contracting of Florida,* LLC, VET-137, at 6 (2008) (SDV with 60% is not in control where some actions required 67%). I see no good reason to depart from this very consistent precedent.

Appellant contends Mr. Chorpenning is its highest officer, following the April 2004 meeting in Phoenix in which he was elected "President and Chief Executive Officer for all day-to-day management and long-term decisionmaking." Protest File, Ex. 3 (Appellant's Letter). I reject this contention. Appellant's Operating Agreement requires any agreement among the members that would be "treated as part of or superseding" the Operating Agreement to be reduced to writing and signed by all members. Operating Agreement, § 1.1.C. The Operating Agreement grants equal authority to all members to act on Appellant's day-to-day business. *Id.*, § 3.3. The Operating Agreement authorizes neither a managing member nor a President and Chief Executive Officer. Thus, the Phoenix action, intended to give Mr. Chorpenning more authority over Appellant than the other members have (as Appellant is here trying to prove), was clearly one that would have to be "treated as part of or superseding" the Operating Agreement. Such an action would not be effective at all unless put in writing and signed by all of the then-five members. Yet, the Phoenix action was never put into writing — not in 2004, and not earlier this year, when the members met in May 2008, or when they approved the Articles of Amendment in July 2008. Therefore, I conclude the Phoenix action was ineffective. Appellant

[3] I do not resolve the issue of whether Mr. Chorpenning owns a 51% interest, as Appellant claims, or 25% as the D/GC found. Either way, the analysis here has the same result.

has no highest officer, and the D/GC was correct not to look beyond the Operating Agreement for one. Further, the D/GC was correct in not taking up Appellant's offer of affidavits on the issue of the Phoenix action. Affidavits would not have cured the defect of the unwritten action.

Finally, Appellant contends that the regulation cannot mean that the SDV must be able to control "all" decisions. I must reject this contention. The regulation states that the SDV must have "control over all decisions of the limited liability company." 13 C.F.R. § 125.10(d). In its past decisions involving the SDV's lack of control over some specified decisions that require supermajority approval, OHA has consistently interpreted the "all decisions" language of the regulation strictly in accordance with its plain meaning. *See Matter of Technical and Project Engineering*, LLC, SDV-110, at 7 (2006) (decisions including changes to the firm's organization structure or financial signature authority, or hiring of executive staff); *Matter of IITS-Nabholz, LLC*, VET-114, at 9 (2007) (selling, mortgaging, or otherwise transferring company assets); *Matter of CymSTAR LLC*, VET-123, at 7 (2007). ("fundamental decisions"); *Matter of Firewatch Contracting of Florida*, LLC VET-137, at 6 (2008) (appointing, compensating, or removing officers). In each case, the fact that there were any specified decisions requiring a supermajority that the SDV could not himself satisfy rendered the firm ineligible.

Here, management decisions subject to supermajority ("Majority-In-Interest") approval include determining members' compensation, spending more than $10,000 except pursuant to a budget approved by the members, and borrowing money. I see no need to depart from OHA's consistent precedent based on the type of specified decision the SDV does not control.

Accordingly, the D/GC correctly concluded that Mr. Chorpenning, the service-disabled veteran, did not control Appellant on the date of its offer on the instant set-aside contract.

V. Conclusion

After reviewing the record, I find the written protest file supports the D/GC's SDVO SBC status determination. Appellant has failed to establish any clear error of fact or law in the D/GC's decision. Accordingly, I must DENY the instant Appeal Petition, and AFFIRM the D/GC's SDVO SBC status determination.

The D/GC's determination that Heritage of America, LLC, was not an eligible SDVO SBC at the time it submitted its offer on the instant procurement 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).

CHRISTOPHER HOLLEMAN
Administrative Judge