

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

IN THE MATTER OF:

ALOG Corporation,

Appellant,

Solicitation No. FA8003-19-R-A002

Department of the Air Force

SBA No. VET-285

Decided: July 21, 2020

APPEARANCES

Jerome S. Gabig, Esq., Wilmer & Lee, P.A., Huntsville, Alabama, for Appellant ALOG Corporation

Shomari B. Wade, Esq., Danielle K. Muenzfeld, Esq., Brett A. Castellat, Esq., Greenberg Traurig, LLP, Washington, District of Columbia, for Operations Services, Inc.

Edmund M. Bender, Esq., Office of General Counsel, U.S. Small Business Administration, Washington, D.C., for the Agency

DECISION<sup>1</sup>

I. Introduction

This appeal arises from a determination by the U.S. Small Business Administration (SBA) Director of Government Contracting (D/GC) concluding that ALOG Corporation (Appellant), is not an eligible Service-Disabled Veteran-Owned Small Business Concern (SDVO SBC). Operations Services, Inc. (OSI), protested Appellant's status as an SDVO SBC. For the reasons discussed *infra*, I am affirming the determination and denying the appeal.

SBA Office of Hearings and Appeals (OHA) decides appeals of SDVO SBC status determinations under the Small Business Act of 1958, 15 U.S.C. § 631 *et seq.*, and 13 C.F.R. parts 125 and 134. Appellant filed the appeal within 10 business days of receiving the

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<sup>1</sup> This decision was initially issued under a protective order. Pursuant to 13 C.F.R. § 134.205, OHA afforded counsel an opportunity to file a request for redactions if desired. OHA received one or more timely requests for redactions and considered any requests in redacting the decision. OHA now publishes a redacted version of the decision for public release

determination, so the appeal is timely. 13 C.F.R. § 134.503. Accordingly, this matter is properly before OHA for decision.

## II. Background

### A. Solicitation and Protest

On April 16, 2019, the U.S. Air Force issued Request for Proposals (RFP) No. FA8003-19-R-A002, for Expeditionary/Contingency Medical Material Services at Wright-Patterson AFB, Ohio. The Contracting Officer (CO) set-aside the acquisition entirely for SDVO SBCs and assigned North American Industry Classification System (NAICS) code 493110, General Warehousing and Storage, with a corresponding \$27.5 million average annual receipts size standard. Proposals were due May 22, 2019. (Protest File (PF), at 1064). Appellant and Operations Services, Inc. (OSI) submitted timely offers.

On May 5, 2020, the CO announced that Appellant was the apparent awardee. (*Id.*, at 18.) On May 11, 2020, OSI filed a protest challenging Appellant's SDVO SBC status. (*Id.*) OSI alleged that Appellant is not controlled by an SDV and “[t]he person holding the highest position at ALOG is apparently a revolving door.” (*Id.*, at 23.) OSI highlighted that Messrs. Smith held out conflicting public profiles and representations as to their current position for Appellant. (*Id.*) The CO forwarded the protest to the D/GC for review.

### B. D/GC's Investigation

On May 18, 2020, the D/GC notified Appellant of the protest and requested a response to the protest allegations and various supporting documents. (*Id.*, at 27-31.)

Appellant responded on June 1, 2020, asserting that it is more than 51% unconditionally and directly owned by Paul Smith and Stephen Smith, two service-disabled veterans. (*Id.*, at 136.) Appellant provided documents entitled ALOG stock certificates and ALOG stock Ledger, which indicated that Paul Smith owned [X]% of Appellant's shares while Stephen Smith owned [X]%. (*Id.*, at 137, 170.) Together, they owned [the majority]% of Appellant.

In response to OSI's protest, Appellant maintained that Messrs. Smith have managerial experience to run the company and have previously served in leadership positions prior to joining Appellant. (*Id.*, at 137.) Appellant submitted a copy of the W2 forms of its Officers and Directors for the fiscal year 2019, indicating that Stephen Smith received the highest W2 wage compared to the rest of the members. (*Id.*, at 138.) Further documentations included stock certificates, percentage of voting stock held by SDVs, Buy Sell Agreements, Shareholder Agreements, Tax returns, Articles of Incorporation, etc. (*Id.*, at 139-140.)

Appellant also submitted a Stock Purchase Agreement (Agreement) entered into and effective on November 13, 2017, by and between the “Seller,” Paul Smith, and the “Purchasers,” Stephen Smith and two other non-service disabled veterans, with promissory notes and receipt of check payments. (*Id.*, at 179-237.) The Agreement recited that the Seller was at the date of the Agreement Appellant's sole shareholder, owning [X] of the issued and outstanding shares of the

common stock. (*Id.*, at 180.) The Seller agreed to sell, and the Purchasers to purchase, in the aggregate, [a majority] of Seller's [X] shares of the common stock of Appellant. (*Id.*)

Subject to the terms and conditions in the Agreement, Stephen Smith agreed to purchase and the Seller agreed to sell and transfer to Stephen Smith [X] shares of the stock, free and clear of all liens, encumbrances, claims, assessments and restrictions of every kind for \$[X]. (*Id.*) [XX] agreed to purchase [X] shares of the stock at [X], and [XX] agreed to purchase [X] shares of the stock at \$[X]. (*Id.*, at 180-181.) The Seller would continue to be employed by Appellant, for a period of 4 years following the effective time. It was further agreed that so long as the Agreement remains in effect,

[T]he Stock now owned or hereafter acquired by a Shareholder shall not be sold, assigned, transferred, gifted, mortgaged, alienated, hypothecated or in any way encumbered or disposed of except as hereinafter provided. Except as otherwise provided herein, all recipients of any of the Stock, including but not limited to, recipients of Stock pursuant to a court order as set forth in Section 2.2 hereof, pursuant to a divorce as set forth in Section 3 hereof or pursuant to death as set forth in Section 4 hereof, shall be subject to and bound by this Agreement and the restrictions contained herein, . . .

(*Id.*, at 200.)

Particularly, the Agreement describes § 2.1 Voluntary Sale as:

Except otherwise provided in this Agreement, if a Shareholder desires to sell, assign, transfer, gift or dispose of all or any part of the shares of the Stock which he or she owns or hereafter acquires in the Corporation (hereinafter referred to as the "Offered Shares"), such Shareholder (or Trustee appointed for such Shareholder) (hereafter referred to as the "Selling Shareholder") may not offer the Offered Shares to a third party but instead shall first offer the Offered Shares for sale to the Corporation, and for sixty (60) days thereafter, the Corporation shall have the option, but not the obligation, to purchase all of, or a portion of, the Offered Shares. The Selling Shareholder, for himself or herself and such Trustee, agrees that if the Corporation shall exercise the option granted to it under this Section 2.1 then the Selling Shareholder shall sell the Offered Shares at the price and upon the terms and conditions set forth below. If the Corporation does not within the sixty (60) day period exercise the option granted to it under this Section 2.1 to purchase all or any portion of the Offered Shares, then the Selling Shareholder shall be free for a period of ninety (90) days thereafter to transfer the Offered Shares to a third party provided that such third party complies with Sections 14 and 15 hereof. After said ninety (90) day period, the Selling Shareholder must again comply with the restrictions contained herein.

(*Id.*, at 201.)

Additionally, § 6 Mandatory Redemption of Shares of Paul Smith and [XX] requires:

Notwithstanding anything to the contrary set forth herein, if either Paul Smith or [XX] is then a shareholder of the Corporation, effective December 31, 2021, the Corporation shall purchase from each of Paul Smith and [XX], and each of Paul Smith and [XX] shall sell to the Corporation, all of each of Paul Smith's and [XX]'s shares of the stock of the Corporation. The purchase price shall be determined in accordance with Section 8 of this Agreement.

(*Id.*, at 203.)

§ 14 Transfer Only to Employees also requires:

Notwithstanding anything else herein to the contrary, except for a transfer made pursuant to Section 4.2 [Sales Upon Death], a Shareholder may not transfer any of the shares of the Stock to a person who is not an employee of the Corporation.

(*Id.*, at 208.)

#### C. D/GC's Determination

On June 11, 2010, the U.S. Small Business Administration's (SBA) Director of the Office of Government Contracting (D/GC) issued the determination letter finding that Appellant was not unconditionally owned and controlled by a service-disabled veteran at the time it submitted its offer and, therefore, did not meet the SDVO SBC eligibility requirements. The D/GC first verified that Paul Smith and Stephen Smith, are service-disabled veterans, as determined by the VA, pursuant to 13 C.F.R. § 125.8. The D/GC next analyzed the issues of ownership and control. (D/GC Determination, at 3.)

Regarding ownership, the D/GC determined that Paul Smith owns [X]% of Appellant and Stephen Smith owns [X]%. However, the D/GC also found that certain provisions of Appellant's Stock Transfer Agreement imposed unacceptable conditions on Paul Smith's ownership in violation of 13 C.F.R. § 125.11. Specifically, Section 6, Mandatory Redemption of Shares of Paul Smith and [XX] required that if either was a shareholder as of December 31, 2021, they were required to sell their shares to Appellant. (*Id.*, at 4.)

Furthermore, the D/GC found Paul Smith's transfer rights are further limited by Section 14, which excludes the sale of shares to nonemployees of ALOG, and provides that “[n]otwithstanding anything else herein to the contrary, except for a transfer made pursuant to Section 4.2 hereof, a Shareholder may not transfer any of the shares of the Stock to a person who is not an employee of the Corporation.” (*Id.*)

The D/GC noted that this type of forced sale arrangement violates SBA regulations requiring unconditional ownership, creating an “arrangement causing or potentially causing ownership benefits to go to another (other than after death or incapacity).” Further, Paul Smith as SDV is obligated to sell his shares on December 31, 2021 at a price determined by the

agreement, cannot own ALOG beyond that date, is limited in his ability to sell his shares to nonemployees of ALOG (which would include a non-SDV), and the sale grants a benefit to the non-SDV seller and purchaser. (*Id.*)

The D/GC concluded that Paul Smith's ownership is not unconditional, while Stephen Smith, whose shares are directly and unconditionally owned, does not have adequate ownership interest to meet the requirement of “at least 51%” of ALOG. Thus, the D/GC found Appellant does not meet the ownership requirement set forth in 13 C.F.R. § 125.12. (*Id.*, at 5.)

As for control, the D/GC explained that 13 C.F.R. § 125.13 requires that a service-disabled veteran hold the highest officer position in the firm, possess managerial experience needed to run the concern, and be responsible for conducting the day-to-day management of the firm's business operations. The D/GC found ALOG's by-laws confirm that as combined majority SDV owners, Messrs. Smith have control over the voting of the Shareholders' meeting and ultimately the Board of Directors, Paul Smith is the CEO/Chairman responsible for Appellant's day-to-day oversight of key employees and government contract biddings, while Stephen Smith is responsible for the day-to-day business operations. The D/GC also found that Paul Smith has over [X] years of technical expertise, while Stephen Smith has [X] years of operations experience. Thus, the D/GC concluded that Appellant satisfies the control requirement under 13 C.F.R. §§ 125.13 and 125.13(i)(7). (*Id.*, at 5-8.)

Nevertheless, the D/GC concluded, based on the ownership findings, that one or more service-disabled veterans do not own or control Appellant, and, therefore, Appellant is not an eligible SDVO SBC.

#### D. Appeal

On June 22, 2020, Appellant filed the instant appeal with the SBA Office of Hearings and Appeals (OHA). Appellant contends the D/GC clearly erred in finding Paul Smith's ownership is conditional, when the language in question was a “change in ownership” provision as permitted by 13 C.F.R. § 125.12(f).

First, Appellant argues the Stock Transfer Agreement put in place a succession plan involving a change in ownership from Paul Smith to Stephen Smith, and “there is no other logical explanation for the language in the Stock Transfer Agreement obligating Paul--four years into the future--to relinquish his ALOG stock.” (Appeal, at 4.) Appellant indicates the utilization of an outside law firm to draft the Stock Transfer Agreement adds additional credence that the document is a 13 C.F.R. § 125.12(f) change of ownership agreement with an effective date of December 31, 2021. (*Id.*, at 4-5.)

Appellant contends that when read as a whole and put in factual perspective, Paul Smith began his business succession plan in November 2017, which would become fully complete on December 31, 2021 when Paul Smith surrenders all his stock. Appellant argues the D/GC erred in finding the Stock Transfer Agreement of November 13, 2017 was a “type of forced sale arrangement.” Rather it was a “change in ownership” provision as permitted by 13 CFR § 125.12(f). (*Id.*, at 5.)

Appellant also points to precedent from the Court of Federal Claims and the U.S. Supreme Court that, Appellant asserts, support the reading of 13 CFR § 125.12 and the word “generally,” authorizing exceptions to the unconditional ownership rule. Appellant further asserts the U.S. Supreme Court made clear that, “In matters of statutory construction the duty of this Court is to give effect to the intent of Congress, and in doing so our first reference is of course to the literal meaning of words employed.” (*Id.*, at 7, citing *Flora v. United States*, 357 U.S. 63, 65 (1958).) Appellant states the intent of Congress “that the Government should aid, counsel, assist, and protect, insofar as is possible, the interests of small-business concerns. . . .” (*Id.*, at 7-8, citing 15 U.S.C. § 631(a).) Appellant argues OHA created the strict definition of unconditional ownership in *In the Matter of Wexford Group Int’l*, SBA No. SDV-105 (2006), which was criticized by the Court of Claims as having “draconian and perverse results.” *Veterans Contracting Group, Inc. v. United States*, 135 Fed. Cl. 316, 321 (2017). Appellant urges OHA to “undo the harm” it caused in *Wexford*. (*Id.*, at 8, fn. 2.) Appellant alleges the general rule of unconditional ownership in 13 CFR § 125.12 must be read in the context of “should aid, counsel, assist, and protect, insofar as is possible, the interests of small-business concerns.” (*Id.*, at 7-8.) Thus, Appellant contends the “change of ownership” is recognized in 13 CFR § 125.12(f) as a legitimate purpose, enforcing an unconditional ownership rule to frustrate Appellant's change in service-disabled veterans' ownership, inconsistent with the intent of Congress. (*Id.*, at 8.)

Appellant argues that the position taken by SBA violates the absurd consequences rule. (*Id.*, citing *United States v. John C. Grimberg Co., Inc.*, 702 F.2d 1362, 1390 (1983).) Appellant further argues, “[h]ere, an absurd consequence is occurring where a Vietnam veteran who has been mentoring a Global War on Terror veteran is stymied in transitioning ownership to the younger veteran by a hyper-technical interpretation of unconditional ownership.” (*Id.*)

Appellant argues the language in the Stock Transfer Agreement on which the D/GC relied is a change of ownership provision. (*Id.*, at 9.) Thus, “[a]pplying the rule of the specific governs the general, since the language on which the OGC Decision is based to deprive [Appellant] of its SDVOSB status is a specific provision found in 13 C.F.R. § 125.12(f), then the specific provision governs over the general provision as to stock must be unconditionally owned.” (*Id.*)

Appellant concludes the D/GC's “Decision made a clear error of law by interpreting 13 C.F.R. § 125.12 as creating an absolute prohibition against counting conditionally owned stock towards a service-disabled veteran's ownership [when] 13 C.F.R. § 125.12(f) establishes an exception for change of ownership agreements.” (*Id.*)

#### E. OSI's Response

On July 1, 2020, OSI responded to the appeal. OSI argues that SBA reached the correct determination that Appellant is not a SDVO SBC because a service-disabled veteran does not unconditionally and directly own Appellant and thus, Appellant has not met the ownership requirement under 13 C.F.R. § 125.12. (OSI Response, at 4.)

OSI maintains the instant Appeal is based on the argument that 13 C.F.R. § 125.12(f) is an exception to the requirement that an SDV's ownership of an eligible SDVO SBC be unconditional. OSI argues this argument is refuted by the language in 13 C.F.R. § 125.11 defining “unconditional ownership.” (*Id.*, at 4.)

OSI contends 13 C.F.R. § 125.12(f) does not provide an exception to unconditional ownership for “Change of Ownership” Agreements. (*Id.*, at 5.) OSI asserts Appellant “makes the strained argument that because 13 C.F.R. § 125.12 contains the word ‘generally’ in the context of requiring the service-disabled veteran having unconditional ownership, then that means 13 C.F.R. § 125.12(f) acts as an exception to the requirement for unconditional ownership.” (*Id.*) However, OSI finds no reasonable reading of 13 C.F.R. § 125.12(f) that could lead to such conclusion.

OSI relies on the U.S. Supreme Court and Court of Appeals decisions, holding the primary task is to examine the relevant statute's language, to determine whether it has a plain and unambiguous meaning. (*Id.*, at 5, citing *Lamie v. United States Tr.*, 540 U.S. 526, 534 (2004) (“[the] starting point in discerning congressional intent is the existing statutory text”); *Shoshone Indian Tribe of the Wind River Reservation v. United States*, 364 F.3d 1339, 1345-46 (Fed. Cir. 2004) (the plain language of a statute is controlling)). If a statute is plain and unambiguous, and the overall statutory scheme is coherent and consistent, the court's inquiry ends, and its sole function is to enforce the statute according to its terms. (*Id.*, at 6.)

OSI argues the plain meaning is clear. The regulation provides that generally, a concern must be unconditionally and directly owned by one or more SDVs. The change of ownership provision at 13 C.F.R. § 125.12(f) states that it is possible for an SDVOSB to change ownership and maintain its status as long as one or more service-disabled veterans own and control it after the change. But that provision is in no way an exception to the rule that a concern must be unconditionally owned by a service-disabled veteran nor is it an exception to the definition of “unconditional ownership.” (*Id.*, at 7.)

While asking this Court to effectuate all provisions of this regulation, Appellant ignores 13 C.F.R. § 125.11 which defines unconditional ownership as not subject to any conditions. (*Id.*, at 7.) This definition provides three limited exceptions to the rule of unconditional ownership, i.e., agreements or conditions after death, agreements or conditions after incapacity, or the pledge or encumbrance of stock or other ownership interest as collateral in specific instances. (*Id.*) Appellant notes that a general change of ownership agreement does not fall within any of those categories.

As opposed to Appellant's reliance on 15 U.S.C. § 631(a), OSI notes that SBA does not cite to this section in promulgating 13 C.F.R. § 125.12, but to 15 U.S.C. § 657f, which provides that a contracting officer may award contracts to concerns owned and controlled by service-disabled veterans, and this is the more appropriate statute to review in analyzing the intent of the regulation. (*Id.*, at 8-9.) SBA conformed the definition of “unconditional ownership” in the same manner throughout other SBA programs, and thus, it could hardly be said that its interpretation is unreasonable. (*Id.*, at 9.)

OSI states that even if there were an exception for the change of ownership agreement, Appellant's Stock Transfer Agreement, Section 6, titled "Mandatory Redemption of Shares of Paul Smith and [XX]" and its plain language demonstrate that it is a forced sale arrangement placing limitations on Paul Smith's ownership of stock. (*Id.*, at 9-10.) The Agreement requires at § 6 that if Paul Smith holds shares on December 31, 2021, then Appellant will purchase and Paul Smith will sell those shares back to the corporation, while § 14 precludes sales of shares to non-employees of Appellant. (*Id.*, at 10-11.) OSI contends the Appeal does not dispute this, and such conditions on stock ownership violate the definition of "unconditional ownership." (*Id.*, at 11, citing 13 C.F.R. § 125.11 ("[u]nconditional ownership means ownership that is not subject to . . . arrangements causing or potentially causing ownership benefits to go to another (other than after death or incapacity)").

OSI points out the plain language in the Agreement states that if Paul Smith still owns stock on December 31, 2021, then he must sell it to the corporation, i.e., to Appellant (not Stephen Smith). (*Id.*, at 12, emphasis OSI's.) Even read in the context of the full agreement, OSI finds it irrefutable that this provision was an arrangement "causing or potentially causing ownership benefits to go to another (other than after death or incapacity)." (*Id.*) Therefore, even if a change in ownership is allowed under 13 C.F.R. § 125.12(f), and this is a succession plan designed to transfer ownership to Stephen Smith, Appellant is not absolved of its responsibility to comply with the definition of "unconditional ownership" in 13 C.F.R. § 125.11. (*Id.*, at 12.)

In response to Appellant's allegations on appeal, OSI maintains that the rules of contractual interpretation do not look at parole evidence, such as drafter's intent, if the words are unambiguous. (*Id.*, citing *Sterling, Winchester & Long, L.L.C. v. United States*, 83 Fed. Cl. 179, 183 (2008) ("If the contract is clear and unambiguous on its face, the plain and ordinary meaning of the contract controls, and the Court may not resort to extrinsic evidence to interpret it or change the terms of a contract"). Here, the words of the Agreement are unambiguous: Paul Smith must sell his shares of ALOG on December 31, 2021 if he has not already done so, which is an arrangement causing his ownership benefits to go to another. (*Id.*)

OSI then contends that Appellant's reliance on *Veterans Contracting Group, Inc. v. United States*, 135 Fed. Cl. 316 (2017) is misplaced. (*Id.*, at 12-13.) Appellant cites this case for the proposition that 13 C.F.R. § 125.11's definition of "unconditional ownership" produces "draconian and perverse results." (*Id.*, at 13, citing Appeal at 8.) The reliance on "draconian and perverse results" completely misconstrues the holding in that case and rests on a fundamental misunderstanding of the history of the definition of "unconditional ownership." (*Id.*) OSI explains that 13 C.F.R. Part 125 originally did not have a definition for unconditional control, and OHA addressed this issue in *Matter of The Wexford Group Int'l*, SBA No. SDV-105 (2006). In *Wexford*, OHA held that "unconditional" for purposes of "unconditional ownership" means there are no conditions or limitations upon the owner's right to exercise full control and ownership of the concern. (*Id.*, at 13, citing *Wexford* at 6.) In 2017, the Court of Federal Claims upheld the definition articulated in *Wexford* in *Veterans Contracting Group* and found that it was not unreasonable for SBA to rely on its own interpretation from prior case history. (*Id.*, at 14, citing *Veterans Contracting* at 328.)



Therefore, the Court indicated that it was draconian to follow the *Wexford* definition, not that the current definition under 13 C.F.R. § 125.11 was draconian. (*Id.*) OSI notes that this is especially true since the current definition of “unconditional ownership” was not in existence when *Veterans Contracting* was decided. In fact, on September 28, 2018, SBA promulgated rules, where it provided a definition for “unconditional ownership.” (*Id.*, at 14-15, citing 83 F.R. 48908, 48909 (2018) (“[] SBA is adding definitions for . . . Unconditional Ownership”).) The promulgated rules indicated, “[t]he added definitions are being adopted from SBA’s 8(a) BD regulations found in part 124.” (*Id.*, comparing 13 C.F.R. § 124.3 with 13 C.F.R. § 125.11.)

OSI asserts that the Stock Transfer Agreement, dated November 13, 2017, was not amended when OHA adhered to *Wexford*’s standard for unconditional ownership after *Veterans Contracting* was decided on August 31, 2017, when the Court of Federal Claims affirmed it on December 11, 2017, and when the final rule from SBA was promulgated on September 28, 2018. (*Id.*, at 15.) OSI contends, as a result, having counsel prepared the Agreement, in fact, demonstrates the opposite of ALOG’s assertions today—that the intended effect of this language was not a “change in ownership” agreement, but to divest Paul Smith of his unconditional ownership because §§ 6 and 14 clearly violated the definition of “unconditional ownership” under existing laws. (*Id.*, at 12-15.)

Finally, OSI requests OHA dismiss this appeal or, in the alternative deny it under 13 C.F.R. § 134.509(a)(1), because the appeal does not, on its face, allege facts that if proved to be true, warrant reversal or modification of the determination. (*Id.*, at 15-18.) OSI states that because no exception for “change of ownership agreements” exists for the “unconditional ownership” requirement, Appellant has not, on the face of this appeal, alleged facts that if proven to be true, warrant reversal or modification of the determination. To the extent that Appellant argues that SBA’s rules are too “draconian” and should include such exception, such an argument is not proper for this Court, because Administrative Law Judges (“ALJs”) are bound by properly promulgated agency regulations and OHA is not the proper forum for a challenge to the validity of a regulation. (*Id.*, at 16.)

#### F. SBA’s Response

On July 2, 2020, SBA responded to the appeal. SBA contends the D/GC’s determination was not based on a clear error of fact or law and should be upheld. (SBA Response.) The D/GC correctly found that Appellant was not an eligible SDVO SBC due to Paul Smith’s conditional ownership of Appellant, and the Stock Transfer Agreement, wherein Paul Smith sold shares of Appellant to Stephen Smith, [XX], and [XX]. (*Id.*, at 4.) Specifically, § 6, Mandatory Redemption of Shares of Paul Smith and [XX] of the Agreement was found to be a type of forced sale arrangement, violating 13 C.F.R. § 125.12. SBA regulations require that the service-disabled veteran must unconditionally own and control a small business to be eligible. (*Id.*, at 5, citing 13 C.F.R. § 125.11.)

SBA maintains Appellant’s argument that the Agreement does not violate SBA’s requirements for unconditional ownership because “unconditional ownership is not an absolute rule,” citing to the “generally” modifier found in 13 C.F.R § 125.13, is not applicable here. In fact, SBA regulations carve out limited exceptions to the requirement of “unconditional

ownership” noted in 13 C.F.R. § 125.11, which include death, incapacity, and the pledge or encumbrance of stock or other ownership interest as collateral. (*Id.*) However, these exceptions do not apply to the subject appeal.

As for Appellant's reliance on 13 C.F.R § 125.12(f), which allows for a change in ownership or business structure so long as SDVs own and control the firm after the change, SBA asserts there was no evidence in the Protest File that an SDV will own and control the firm after the change in ownership on December 31, 2021. (*Id.*, at 6.) Appellant asks OHA and SBA to infer a plan of succession that Stephen Smith will own the firm and retain eligibility after the sale based on a clause of the Agreement: “Whereas the success of the Corporation requires the active interest, support, and personal attention of the Shareholders and that for this reason it is not advisable to permit its shares of the Stock to be subject to sale on the open market.” (PF, at 200.) However, the Agreement on record does not support that inference. SBA maintains § 6 simply states that the sale must occur on December 31, 2021 and that in § 14, the shares owned by Paul Smith and [XX] must be sold to an employee. (*Id.*, at 203, 208.) SBA maintains these sections fit squarely into the type of conditional ownership SBA's regulations prohibit. That is, ownership that is subject to arrangements causing or potentially causing ownership benefits to go to another and is therefore a concern where the SDV's ownership is of that type is ineligible. (SBA Response, at 6.)

Thus, D/GC correctly concluded that Appellant is not an eligible SDVO SBC. (*Id.*) As D/GC made no error in law or fact, SBA asks OHA to affirm D/GC's determination on appeal.

### G. Additional Pleadings

On June 29, 2020, Appellant filed a motion to present new evidence. On June 30, 2020, OSI filed an opposition to Appellant's motion to present new evidence, contending that Appellant cites to the wrong authority and OHA may not admit evidence beyond the written protest file, pursuant to 13 C.F.R. § 134.512. On July 2, 2020, with its Response, the Agency opposed Appellant's motion, pointing to 13 C.F.R. § 134.512 and maintaining that OHA has rejected a concern's attempt to “cure eligibility after submission of the initial offer.” (SBA Response at 2-4, citing *In the Matter of Apex Ventures, LLC*, SBA No. VET-219 (2011); *In the Matter of Cedar Electric, Inc./Pride Enterprises, Inc., JV*, SBA No. VET-129 (2008)).

On July 2, 2020, Appellant also filed a reply to OSI's response and motion to dismiss.

## III. Discussion

### A. Standard of Review

OHA reviews the D/GC's decision to determine whether it is “based on clear error of fact or law.” 13 C.F.R. § 134.508; *see also Size Appeal of Taylor Consultants, Inc.*, SBA No. SIZ-4775, at 10-11 (2009) (discussing the clear error standard that is applicable to both size appeals and SDVO SBC appeals). Thus, I may overturn the D/GC's decision only if Appellant proves the D/GC made a patent error based on the record before him.

### B. New Evidence and Reply

Appellant submits on appeal new evidence in the form of a declaration letter from Paul Smith, executed on June 24, 2020, and a reformation stock transfer agreement, revised and restated on June 19, 2020. OHA's governing regulations provide: "The Judge may not admit evidence beyond the written protest file nor permit any form of discovery. All appeals under this subpart will be decided solely on a review of the evidence in the written protest file, arguments made in the appeal petition and response(s) filed thereto." 13 C.F.R. § 134.512. I therefore do not have the discretion to admit any new material. *In the Matter of Veterans Construction Services, Inc.*, SBA No. VET-167, at 4 (2009); *In the Matter of Apex Ventures, LLC*, SBA No. VET-219, at 5 (2011). Accordingly, the proffered new evidence is EXCLUDED from consideration.

As for Appellant's reply to OSI's response and motion to dismiss, Appellant did not submit a motion for leave to reply. The regulations do not permit a reply to a response unless the Judge, upon motion or on his or her own initiative, orders a reply to be filed and served. 13 C.F.R. § 134.206(e). Here, Appellant failed to request leave to reply to OSI's response and its reply does not contain any substantive argument beyond those already alleged on appeal. I therefore EXCLUDE Appellant's reply from the record.

### C. Analysis

Appellant has failed to prove clear error in the D/GC's determination. As a result, I must deny this appeal.

To be an eligible SDVO SBC, the regulation requires that:

Generally, a concern must be at least 51% unconditionally and directly owned by one or more service-disabled veterans.

13 C.F.R. § 125.12.

Unconditional ownership is defined as:

[O]wnership that is not subject to conditions precedent, conditions subsequent, executory agreements, voting trusts, restrictions on or assignments of voting rights, or other arrangements causing or potentially causing ownership benefits to go to another (other than after death or incapacity). The pledge or encumbrance of stock or other ownership interest as collateral, including seller-financed transactions, does not affect the unconditional nature of ownership if the terms follow normal commercial practices and the owner retains control absent violations of the terms.

13 C.F.R. § 125.11.

The regulations further provide as to change of ownership that:

A concern may change its ownership or business structure so long as one or more service-disabled veterans own and control it after the change.

13 C.F.R. § 125.12(f).

Prior to SBA defining unconditional ownership in a regulation, OHA defined unconditional ownership:

[T]he word unconditional is defined as “not limited in any way, not bound or restricted by conditions or qualifications, absolute” (citation omitted) . . . [U]nconditional necessarily means there are no conditions or limitations upon an individual's present or immediate right to exercise full control and ownership of the concern. Nor can there be any impediment to the exercise of the full range of ownership rights. Thus, a service-disabled veteran: (1) Must immediately and fully own the company (or stock) without having to wait for future events; (2) Must be able to convey or transfer interest in his ownership interest or stock whenever and to whomever they choose; and (3) Upon departure, resignation, retirement, or death, still own their stock and do with it as they choose. In sum, service-disabled veterans must immediately have an absolute right to do anything they want with their ownership interest or stock, whenever they want.

*In the Matter of Wexford Group International, Inc.*, SBA No. SDV-105, at 6 (2009).

OHA has consistently applied the Wexford standard in determining whether a particular service-disabled veteran's ownership of a concern was unconditional. *In the Matter of Veterans Construction Services, Inc.*, SBA No. VET-167 (2009); *In the Matter of Veterans Contracting Group, Inc.*, SBA No. VET-265 (2017).

OHA's definition was upheld in *Veterans Contracting Group, Inc. v. United States*, 135 Fed. Cl. 316, 321 (2017).<sup>2</sup> The court found that while *Wexford* “produces draconian and perverse results in a case such as this one,” it had to uphold OHA's interpretation of the regulation. *Veterans Contracting*, at 328. SBA later further defined unconditional ownership at 13 C.F.R. § 125.11, adding the exceptions for death, incapacity, and pledges of stock, but did not otherwise disturb the *Wexford* definition. 83 Fed. Reg. 48908, 48909 (Sep. 28, 2018).

Thus, the definition of unconditional ownership is clear. The service-disabled veteran's ownership of the challenged concern must be unlimited, with no restrictions whatever on their ownership, or their ability to dispose of their shares in any way they choose. The exceptions are agreements dealing with the death or incapacity of a shareholder, and the pledge of stock as collateral if the terms follow normal commercial practices.

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<sup>2</sup> Reviewing *In the Matter of Veterans Contracting Group, Inc.*, SBA No. VET-265 (2017).

Here, however, contrary to Appellant's argument, the Stock Transfer Agreement was clearly drafted and agreed on that Mandatory Redemption of Shares § 6 of Paul Smith and [XX] requires Paul Smith to sell all of his shares, if any, effective December 31, 2021, and the Corporation to purchase them. Transfer Only to Employees § 14 also limits the SDV's ability to transfer any of the shares of the Stock to a person who is not an employee of Appellant. As SBA indicated, there is no evidence that an SDV or Stephen Smith will own and control the firm after the change in ownership on December 31, 2021, based on the transfer of sales clause or mandatory redemption of shares requirement. It is therefore clear that the Stock Transfer Agreement places conditions on Paul Smith's ownership of Appellant, thereby creating a forced sale arrangement that violates 13 C.F.R. § 125.12.

Thus, Appellant's shareholders must not sell, mortgage, or otherwise alienate any stock except as provided in the Agreement. Should they choose to sell any of their shares, the Appellant corporation has first right of refusal. A shareholder may not transfer any stock to any person who is not an employee of Appellant. Further, if Paul Smith is still a shareholder as of December 31, 2021, he must sell all of his shares to the Appellant corporation. Paul Smith's ownership is not unconditional, but constrained by a number of restrictions upon his actions. Further, his ownership has a definite termination date. He is required to divest himself of his stock by a certain date. All of these are restrictions upon Paul Smith's ownership of his stock in Appellant, which render his ownership conditional.

Appellant's reading of 13 C.F.R. § 125.12, conditioned upon the modifier “Generally,” as a means to allow § 125.12(f) — change of ownership, to supersede the requirements for unconditional ownership, is patently flawed. Appellant is attempting to argue that § 125.12(f) is another exception to unconditional ownership. However, nothing in the text of the § 125.12(f), or its placement in the overall regulatory scheme, identifies it as an exception to the requirement of unconditional ownership. Rather, it provides that an SDVO SBC is permitted to have a change in ownership without losing eligibility. Nothing in the text of the regulation is a *carte blanche* for a corporation to effect a change in ownership by any means it chooses, without concern for the other regulatory requirements. The regulation provides for exceptions to unconditional ownership in terms of providing for a transfer of ownership in the event of death or incapacity, and for pledges of stock as collateral. Nothing in the regulation identifies any other exception to the requirement of unconditional ownership.

I further find that Appellant's argument based upon canons of statutory construction are meritless. To build upon the one word “Generally” an exception to a long clearly defined rule without any basis in the text for the argument is risible.

I find that the D/GC's decision was reasonable based on the record before him. The plain reading of the Agreement, including §§ 6 and 14, support a finding that it includes a forced sale arrangement that restricts Paul Smith's unconditional ownership of Appellant. Further, the Agreement imposes limitations on who may buy the stock, which affects Appellant's ownership by SDV. Thus, the D/GC could appropriately conclude that Paul Smith did not have unconditional ownership of his share of Appellant, and Appellant was not unconditionally owned by service-disabled veterans.

IV. Conclusion

The D/GC's determination was not based upon clear error. Thus, the instant appeal is DENIED, and the D/GC's status determination is AFFIRMED.

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

CHRISTOPHER HOLLEMAN  
Administrative Judge