

DECISION FOR PUBLIC RELEASE

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

IN THE MATTER OF:

Battalion, LLC

Appellant

Solicitation No. FA6712-13-R-0012

SBA No. VET-242

Decided: December 3, 2013

APPEARANCES

Jason L. Harris, Battalion, LLC, Pittsburgh, Pennsylvania, for Appellant.

Victor G. Klingelhofer, Esq., Cohen Mohr, LLP, Washington, D.C., for Douglas P. Fleming, LLC.

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

DECISION¹

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 of Government Contracting (D/GC) for the U.S. Small Business Administration (SBA) made a clear error of fact or law in determining that Battalion, LLC (Appellant) does not meet the Service-Disabled Veteran-Owned Small Business Concern (SDVO SBC) eligibility requirements. *See* 13 C.F.R. § 134.508.

¹ This decision was initially issued under a protective order on December 3, 2013. Pursuant to 13 C.F.R. § 134.205, I afforded the parties an opportunity to file a request for redactions if it desired to have any information withheld from the published decision. No redactions were proposed, and OHA now publishes the decision in its entirety.

DECISION FOR PUBLIC RELEASE**III. Background****A. Solicitation and Protest**

On May 30, 2013, the U.S. Department of the Air Force issued Request for Proposals (RFP) number FA6712-13-R-0012 seeking a contractor to repair exterior building walls. The Contracting Officer (CO) set aside the procurement entirely for SDVO SBCs, and assigned North American Industry Classification System (NAICS) code 238140, Masonry Contractors, with a corresponding size standard of \$14 million average annual receipts. Proposals were due July 2, 2013. On August 26, 2013, the CO awarded the contract to Appellant.

On August 29, 2013, Douglas P. Fleming, LLC (DPF), an unsuccessful offeror, filed a protest challenging Appellant's size and status as an SDVO SBC. DPF alleged that Appellant's majority owner, Mr. Jason L. Harris, is a full-time employee of Sota Construction Services, Inc. (SCS), a firm controlled by Appellant's minority owner, Mr. Ernest J. Sota. The CO forwarded DPF's protest to the D/GC for review.

B. Operating Agreement

On September 6, 2013, Appellant responded to the protest and submitted a copy of its Operating Agreement to the D/GC. The agreement contains the following provisions pertinent to this appeal:

2.1 Initial Date; Initial Parties. This Operating Agreement (this "Agreement") is entered into this 19th day of April, 2012, by and among the Company and the undersigned persons who, on that date, are all the Members of the Company, each of whom has executed this Agreement on his, her or its own behalf and as a Member of the Company.

...

7.1 Management by Members. As provided herein, the Company will be managed by its Members. All decisions to be made with respect to the Company shall be made pursuant to one or more Acts of the Members. Pursuant to an Act of the Members, the Members may delegate to the Managing Member responsibility for the management and conduct of the daily business operations of the Company's business.

...

8.1 Officers of the Company. To the extent that the Class A Members have elected to delegate responsibility for the conduct of certain aspects of the Company's business to officers of the

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Company in accordance with Section 7.1 hereof, the provisions of Section 8.2 and the following provisions of this Section 8.1 shall apply:

- (a) Number and Election. The Class A Members at their annual meeting shall elect a Managing Member, and may elect one or more Vice Presidents, a Secretary, a Treasurer, and such other officers and appoint such agents as the Class A Members deem appropriate.

...

- (c) Managing Member. The Managing Member shall supervise generally all of the affairs of the Company, and shall perform all duties incident to the office of Managing Member. The Managing Member shall be the chief executive officer of the Company and, subject to the control of the Class A Members, shall have management and supervision authority over and exercise general executive powers concerning all the property, business and affairs of the Company. The Managing Member shall be charged with carrying out the policies, programs, orders and resolutions adopted or approved by the Class A Members, and shall have all powers and perform all duties incident to the office of general manager, and any further powers and duties as from time to time may be prescribed by the Class A Members.

...

9.8 Quorum. For any meeting of the Class A Members, a quorum consists of a majority of the Class A Membership Unites entitled to vote on matters affecting the Company. If a quorum is present when a properly called meeting is convened, the Class A Members present may continue to transact business until adjournment, even though the departure of Class A Members originally present leaves less than a quorum.

...

(Protest File, Tab 4, at 64-80.) The Agreement was signed by Mr. Harris, with the title of Managing Member, and by Mr. Sota, as a Member.

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C. D/GC's Determination

On October 22, 2013, the D/GC issued her determination, concluding that Appellant is not an eligible SDVO SBC. The D/GC found that Mr. Harris is a veteran with a service-connected disability based on documentation from the U.S. Department of Veterans Affairs. (Determination at 4.) The D/GC further determined that Appellant met the ownership requirement set forth in 13 C.F.R. § 125.9 because Mr. Harris owns 51% of Appellant. The remaining 49% interest is held by Mr. Sota, who is not a service-disabled veteran.

Next, the D/GC examined whether Mr. Harris has the power to control Appellant. Although Appellant argued that Mr. Harris is Appellant's Managing Member, and in charge of all decisions of the firm, the D/GC was unable to substantiate these claims based on her review of Appellant's Operating Agreement and other documents submitted in response to the protest. Rather, the D/GC found "no evidence to indicate that [Mr. Harris] hold[s] the highest officer position in [Appellant] as required by SBA regulations." (*Id.* at 5.) Furthermore, Appellant failed to demonstrate that Mr. Harris is even employed by Appellant. The D/GC observed that Mr. Harris was an employee of SCS from 2011 to 2012, when he founded Appellant. (*Id.*) Mr. Harris continues to serve as a consultant to SCS, and has "been identified as a representative of SCS within the last five months at a public housing forum." (*Id.* at 5-6.) In addition, Mr. Harris earns no income from Appellant, and his recent W-2s were "issued by SCS." (*Id.* at 5.) The D/GC found that "[a]s a current employee of SCS, [Mr. Harris is] subordinate to the officers of that firm." (*Id.* at 6.) The D/GC concluded that "SCS and its officers either have control or the potential to control [Appellant]." (*Id.*)

The D/GC further noted that Mr. Sota and SCS provide Appellant with critical financial support, including the bid bonding for the procurement at issue. Further, although Appellant has funds available to begin work, the source of that funding was not revealed, and there was no record of Appellant having received any capital contributions. On these facts, the D/GC determined that Mr. Sota "has the ability to significantly influence [Appellant's] operations", in violation of 13 C.F.R. § 124.106(g)(2). (*Id.*)

Lastly, the D/GC noted that Appellant also is "dependent on Mr. Sota for office facilities." (*Id.* at 7.) Specifically, Appellant leases office space from One80 Real Estate Services (One80), an affiliate of SCS. In addition, the D/GC found no evidence that Appellant pays any rent for these facilities. (*Id.*)

D. Appeal

On October 31, 2013, Appellant filed the instant appeal. Appellant contends that the D/GC's decision is "arbitrary and capricious, not based upon the evidence and record, contrary to applicable regulations, and should be reversed." (Appeal at 1.) Appellant states that the D/GC based her decision on incorrect information. Specifically, Appellant asserts that Mr. Harris did not attend the public housing forum referenced by the D/GC, "much less as an employee of [SCS]." (*Id.* at 2.) Appellant further disputes the D/GC's conclusion that Appellant is dependent on SCS for its office space. Appellant contends that it merely receives "an affordable rate" on its

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lease because Appellant is a “struggling start-up with limited funds.” (*Id.*) Appellant adds that it is free to relocate with 30 days notice, so “Mr. Sota and [SCS] do not dictate or control [Appellant’s] location.” (*Id.*)

Appellant maintains that Mr. Harris is the only officer and the Managing Member of Appellant. (*Id.*) Appellant further asserts that Mr. Harris alone has the power to control Appellant and that Mr. Harris is in charge of Appellant’s day-to-day operations and management. Appellant characterizes Mr. Sota as a “passive investor” in Appellant. (*Id.*) Appellant maintains that it is unjust that the D/GC found Appellant to be ineligible when the U.S. Department of Veterans Affairs (VA) determined that Appellant is an eligible SDVO SBC under VA’s rules. (*Id.* at 3.)

Appellant asserts that, contrary to the D/GC’s findings, Appellant’s Operating Agreement does identify Mr. Harris as the Managing Member of Appellant. (*Id.*, citing ¶ 2.1.) Further, the agreement defines the powers of the Managing Member, and makes clear that the Managing Member is Appellant’s chief executive officer. (*Id.*, citing ¶ 8.1(c).) Conversely, the Operating Agreement does not empower Mr. Sota to take any action without Mr. Harris’s consent, and does not identify Mr. Sota as an officer because he is not one. (*Id.* at 3-4.) Appellant reasons that Mr. Harris “hold[s] the highest (and only) officer position in the company, and ha[s] control over all decisions of the limited liability company”. (*Id.* at 3.) As a result, the D/GC clearly erred in finding that Appellant does not comply with 13 C.F.R. § 125.10(d).

Appellant next maintains that Mr. Harris chose to not take income from Appellant during 2012 because the company lost money that year. (*Id.* at 4.) Appellant acknowledges that Mr. Harris was employed by SCS during the early part of 2012. However, after founding Appellant in April 2012, Mr. Harris devoted his attentions primarily to Appellant. Further, although Mr. Harris has periodically worked as a consultant to SCS after Appellant’s formation, such activities are not prohibited by regulation, and did not prevent Mr. Harris from working full-time for Appellant. (*Id.* at 5.)

Appellant also states that Mr. Harris did make a capital contribution to Appellant commensurate with his majority ownership of Appellant. (*Id.*) Appellant argues that Appellant has funds available, but asserts that a majority of those funds originated from Mr. Harris. Additionally, Appellant paid a fee for the bid bond provided by SCS, and such activity is not expressly forbidden by regulation. (*Id.* at 6.)

E. SBA Response

On November 15, 2013, SBA submitted the Protest File and SBA’s response to the appeal. SBA contends that the D/GC correctly concluded that Appellant is not an eligible SDVO SBC.

SBA argues that Appellant’s Operating Agreement states that the firm is to be run by its Members, who “may delegate to the Managing Member responsibility for the management and conduct of the daily business operations.” (SBA Response, at 6, citing ¶ 7.1.) SBA asserts that

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Appellant presented no evidence showing that a Managing Member was designated, or that Appellant's Members ceded or delegated their authority to a Managing Member. (*Id.*) As a result, the D/GC was "correct to conclude that Mr. Harris is not [Appellant's] highest officer, does not hold the position [of] Managing Member and therefore does not control the firm in accordance with SBA regulations." (*Id.*)

SBA observes that OHA has held that 8(a) Business Development (BD) and Small Disadvantaged Business (SDB) regulations may be utilized in interpreting SDVO SBC program requirements. (*Id.* at 6-7.) SBA reiterates that as an employee or consultant of SCS, Mr. Harris is subordinate to SCS's officers, which includes Appellant's minority owner, Mr. Sota. (*Id.* at 7.) Appellant has no employees or independent resources, and Mr. Harris draws no income from Appellant. Thus, SBA reasons, Appellant can be controlled by SCS and its officers.

SBA argues that the instant case is analogous to *Matter of Marine Construction, LLC*, SBA No. VET-216 (2011). In that case, OHA found that a service-disabled veteran was employed by a company that was also a minority owner of the challenged firm. OHA found that the service-disabled veteran was subordinate to the minority owner in his employment, and reliant upon that company for his personal income. SBA argues that the facts of *Marine Construction* mirror those found here, and as such, Mr. Harris cannot be found to control the long-term decision making and day-to-day operations of Appellant. (*Id.* at 9.)

SBA contends that an SDVO SBC may be controlled by another concern if that other concern provides critical financing or can significantly influence business decisions. (*Id.* citing 13 C.F.R. § 124.106(g)(2).) SBA states that Appellant never produced any documentation showing what capital contributions Appellant received. SBA explains that "[t]he record stands as it is. SBA asked for this information, and documents provided by [Appellant] do not show a capital contribution by [Mr. Harris] to the firm." (*Id.* at 10.) SBA adds that SCS guaranteed the bid bonding needed for the procurement here. SBA further asserts that Appellant's argument that its office lease is an ordinary, arm's-length arrangement is unsubstantiated because Appellant did not provide records of rent payments. (*Id.*) SBA emphasizes that Mr. Harris receives his income from SCS; that Mr. Sota owns a large minority interest in Appellant; that SCS provides office space to Appellant through One80; and that SCS provides significant financial assistance to Appellant. Taken together, SBA argues, these facts demonstrate that Appellant would be in "economic jeopardy" but for SCS and Mr. Sota's assistance. (*Id.* at 11.) SBA concludes that "Mr. Harris is beholden to SCS and Mr. Sota and is unable to make independent business decisions" on behalf of Appellant. (*Id.*)

F. DPF Response

On November 15, 2013, DPF responded to the appeal. DPF contends the D/GC's decision is correct and Appellant's arguments are meritless.

DPF argues that Appellant's Operating Agreement allows the minority owner to continue to conduct business after the majority owner has departed from a properly-called meeting. (DPF Response, at 2, citing Operating Agreement ¶ 9.8.) DPF contends this provision violates

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13 C.F.R. § 125.10(d), which requires the service-disabled veteran to have control over all business decisions.

Regarding Appellant's lease of office space, DPF states that the lease is not an arm's length arrangement because Appellant apparently made no lease payments during 2012, yet was not evicted for delinquency. In DPF's view, "the power to have [Appellant] evicted at any time gives Mr. Sota the power to control [Appellant]." (*Id.* at 3.) DPF further asserts that Appellant's response to the protest failed to provide information about the source of the funds in Appellant's bank accounts. Moreover, Appellant admits that SCS provided the bonding for the instant procurement, further supporting the D/GC's finding that Appellant relies upon SCS for critical financial support. DPF concludes that Appellant has failed to prove that the D/GC's determination is based on factual or legal error. (*Id.* at 5.)

IV. Discussion**A. Jurisdiction and Standard of Review**

SDVO SBC status appeals are decided by OHA pursuant to 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 instant appeal within ten business days of receiving the D/GC's determination, so the appeal is timely. 13 C.F.R. § 134.503. Accordingly, this matter is properly before OHA for decision.

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 (2006) (discussing the clear error standard that is applicable to both size appeals and SDVO SBC appeals). OHA will overturn the D/GC's determination only if Appellant proves that the D/GC made a patent error based on the record before her.

B. Analysis

SBA regulations stipulate that, for a small business concern to qualify as an eligible SDVO SBC, one or more service-disabled veterans must control both the long-term decision-making and the day-to-day management of the firm. 13 C.F.R. § 125.10(a). Further, if the concern is organized as a limited liability company, a service-disabled veteran must serve as managing member, with control over all of the firm's decisions. *Id.* § 125.10(d).

In this case, I must agree with the D/GC that the record does not demonstrate that Mr. Harris fully controls Appellant. According to ¶ 8.1(a) of Appellant's Operating Agreement, a Managing Member is elected at Appellant's annual meetings, but Appellant offers no evidence that Mr. Harris was ever so elected. Moreover, even if Mr. Harris had been elected Managing Member, ¶ 7.1 of the Operating Agreement makes clear that the Managing Member is empowered to conduct daily business for the company only if the Members choose to "delegate" that authority to the Managing Member through a formal act of the Members. Again, Appellant has not demonstrated, and the record does not indicate, that any such delegation actually

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occurred. Without such a delegation, Appellant is controlled by its Members, which include Mr. Sota under ¶ 2.1 of the Operating Agreement. Furthermore, although Appellant observes that ¶ 8.1(c) discusses the powers of the Managing Member, that provision applies only if a delegation has occurred under ¶ 7.1. Accordingly, because the Operating Agreement states that Appellant “will be managed by its Members” absent an act of the Members giving control to the Managing Member, I affirm the D/GC’s conclusion that Mr. Harris does not have control over both the long-term decision-making and the day-to-day management of Appellant.

The D/GC also found that Appellant’s relationship with Mr. Sota and SCS undermines Mr. Harris’s control over Appellant. Mr. Harris serves as a consultant to SCS, and appears to be reliant upon SCS for his personal income. Furthermore, Appellant received bonding assistance from SCS, and leases office space on favorable terms from an affiliate of SCS. The D/GC noted that, under SBA regulations applicable to the 8(a) BD program, a non-disadvantaged entity may be found to control a company if the non-disadvantaged entity holds an equity interest in the company and “provides critical financial or bonding support...which directly or indirectly allows the non-disadvantaged individual significantly to influence business decisions of the Participant.” 13 C.F.R. § 124.106(g)(2). It is well-settled that “SBA may apply the regulations and case law from [the 8(a)] programs to analyze the issue of control in SDVO SBC programs.” *Matter of Chevron Constr. Servs., LLC*, SBA No. VET-183, at 4 (2010). The D/GC concluded that “Mr. Sota, by way of SCS, has the ability to significantly influence [Appellant’s] operations.” (Determination at 6.)

I find no error in the D/GC’s determination. As SBA correctly observes in its response to the appeal, the instant case is highly analogous to OHA’s decision in *Matter of Marine Construction Services, LLC*, SBA No. VET-216 (2011). In *Marine Construction*, the challenged firm’s majority owner was an employee of, and dependent upon, the minority owner, which was not an SDVO SBC. There were also other business ties between the two companies. OHA affirmed the conclusion that the challenged firm did not qualify as an SDVO SBC, stating that:

[The challenged firm] is correct that the highest officer of an SDVO SBC normally is permitted to have outside employment. The problem here, though, is not merely [the service disabled veteran] has some outside employment, but that the particular employer owns 49% of [the challenged firm] and is significantly involved in [the challenged firm’s] business. The analysis would be different if [the service disabled veteran] were employed by an unrelated party which had no involvement in [the challenged firm’s] business.

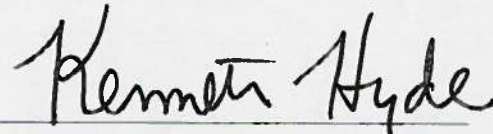
Marine Construction, SBA No. VET-216, at 6. Likewise, in the instant case, Mr. Harris is subordinate to SCS officials through his consulting arrangement, and is dependent upon SCS for his personal income. Mr. Sota holds a 49% equity interest in Appellant, and Appellant receives significant financial assistance from SCS, including bonding assistance for the contract at issue. Appellant was unable to provide the D/GC with evidence of resources or income independent of

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SCS. As in *Marine Construction*, then, the record supports the D/GC's determination that "SCS and its officers either have control or the potential to control [Appellant]." (Determination at 6.)

V. Conclusion

For the above reasons, I DENY the appeal and AFFIRM the D/GC's determination. This is the final decision of the Small Business Administration. 13 C.F.R. § 134.515(a).

A handwritten signature in black ink that reads "Kenneth Hyde". The signature is written in a cursive style with a horizontal line underneath it.

KENNETH M. HYDE
Administrative Judge