NATIONAL VETERAN SMALL BUSINESS
Conference and Expo
Building Partnerships - Veterans, Businesses, and Government

Legal Lessons You Need to Know and Learn

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A Regulatory Walk Through in the Life of a SDVOSB/VOSB

Meet GI Joe

GI Joe – Hypothetical #1

- Joe is an African American, just sent home from Afghanistan due to injury
- Has VA disability rating and is a Service Disabled Veteran
- Has BS in Business Administration
- Worked in his family's large construction company before enlisting
- Has strong background in IT

Set Up Company

- Joe and two of his non-vet buddies establish a construction company LLC
- Focus on marketing VA and the Army Corps of Engineers

Does Joe's Construction Co need CVE Verification? YES

GI Joe, with his two buddies as business partners…

- Hammer out the Operating Agreement
- What are the regulatory considerations?

Regulatory Requirements

- GI Joe must own 51% of the company
  - 38 C.F.R § 74.3

- Must unconditionally "Control" the company
  - 38 C.F.R § 74.4(e) - in the case of an LLC, one or more veterans or service disabled veterans must serve as management members with control over all decisions of the LLC

- What rights do the 49% owners have to protect their investment?
  - Supermajority for major decisions? NO
  - Buy, sell agreement with right of first refusal? NO

Joe must manage day-to-day operations and…

- Does he need to be the highest paid employee? Yes
  - Unless demonstrates why someone else needs more $
  - 38 C.F.R § 74.4(g)(3)
- Who holds construction license ? Must be Joe
  - Unless CVE approves
  - 38 C.F.R § 74.4(g)(3) & 38 C.F.R § 74.4(i)(2)
- Can Joe's buddies (or third party) provide financing or bonding? Needs approval
  - 38 C.F.R § 74.4(i)(2)

Joe works everything out and becomes CVE verified, but…

- WHAT ABOUT SBA?

- Do their regulations matter? YES
  - "Small" in SDVO**<u>S</u>**B/VO**<u>S</u>**B is regulated and reviewed by SBA, and
  - Non VA SDVOSB set-asides are evaluated by SBA
  - 13 C.F.R § 121.103

- Is Certification by SBA required? NO
  - Back to square 1

SBA SDVOSB Regs

- 13 C.F.R. Part 125
  - Ownership - 13 C.F.R § 125.9
  - Unconditional Control - 13 C.F.R § 125.10
    - Matter of Heritage America, LLC, SBA No. VET-142 (2008) (in the context of decision making, the term "all" has been interpreted strictly in accordance with its plain reading)
  - Day-to-day management
  - Most highly compensated
  - Critical financing / bonding / licenses

Size and Affiliation – Hypothetical #2

- One year later, Joe's construction company is…
  - Subcontracting to his family's large company
  - Approximately 60% of revenues obtained through these subcontracts
  - Joe's company won a $3 million VA renovation contract.
  - Family's company indemnified the bond and is a subcontractor for 60% of the renovations

Question: Is Joe's company affiliated with the family owned business?

Affiliation

- Ostensible Subcontractor
- Stock Ownership
- Common Management
- Identity of Interest
  - familial relationships
  - common investments
  - economic dependence
- Negative Control
- Totality of the Circumstances

Identity of Interest 121.103(f)

- Family Members – immediate family members are presumed to act in concert (parents and children, siblings, spouses)
  - The family members must control the respective concerns in order for there to be affiliation
  - In order to rebut presumption, must show clear line of fracture, i.e., estrangement or non-involvement in each other's business affairs
  - Incobrasa, SBA No. SIZ-4557 (2003); Gallagher, SBA No. SIZ-4295 (1998).
  - Presumption rebutted - Different lines of business, different locations, minimal transactions. Bob Jones, SBA No. SIZ-4059 (1995); Harbert, SBA No. SIZ-4525 (2002); Maria Elena, SBA No. SIZ-4010 (1995); Skelton, SBA No. SIZ-2534 (1986).

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Identity of Interest 121.103(f)

- Economic dependence through contractual or other relationships
  - One concern is so dependent on another for contracts or business that its economic viability would be in jeopardy without that business. STA, SBA No. SIZ-4790 (2006).
  - 98% of firm's receipts attributable to one concern. J&R Logging, SBA No. SIZ-4426 (2006).
  - O'Donnell Construction, SBA No. SIZ-4125 (1995); Team Contracting, SBA No. SIZ-3875 (1994).

Totality of the Circumstances

- Even if a single factor is insufficient to demonstrate affiliation between businesses, the SBA will find the businesses affiliated under the totality of the circumstances when the interactions between the businesses are so suggestive of reliance as to render the businesses affiliates. Faison Office Products, SBA No. SIZ-4812, 2006.

Totality of the Circumstances

- However, the totality of the circumstances is not an independent basis for affiliation - is legally insufficient not to tie the circumstances to a type of affiliation specified in 121.103. STA Technologies, SBA No. SIZ-4790, 2006
- Concerns may not use the totality of the circumstances to defeat affiliation found through operation of one of the independent bases for affiliation. Technical Support Services, SBA No. SIZ-4794, 2006

Ostensible Subcontractor Rule

- A contractor and its ostensible subcontractor are treated as joint venturers, and therefore affiliates, for size determination purposes

- An ostensible subcontractor is a subcontractor that performs primary and vital requirements of a contract or a subcontractor upon which the prime contractor is unusually reliant

Ostensible Subcontractor Rule

- All aspects of the relationship are considered, such as contract management, technical responsibilities, percentage of subcontracted work, bonding, whether the subcontractor is the incumbent and is ineligible to submit its own offer
- A prime can be found to be affiliated with its subcontractor even where the prime will meet the applicable performance requirements (limitations on subcontracting)
- 13 CFR 121.103(h)(4)

Can Joe manage multiple companies? – Hypothetical #3

- Joe must prove he can manage and control both companies on a daily basis
  - If not, CVE will not certify 2nd company and 1st company's certification will be in jeopardy.
  - Not recommended
  - 38 C.F.R. 74.4(c)(1)

Can Joe’s second IT Company get an 8(a) Certification?

- NO
- The 8(a) regulations require that Joe manage and control the day-to-day operations of the 8(a) firm.

Mentor-Protégé – Hypothetical #4

- Joe's construction company is growing and wants to establish a Mentor-Protégé relationship to take his company to the next level.
  - Customers are the VA and Army Corps of Engineers

Which Mentor-Protégé Program?

- VA
  - Benefits:
    - VA COs will give proposal evaluation consideration to Mentor firms when utilizing evaluation factors in their contract solicitations.
    - Large business primes serving as mentors under the program may receive additional subcontracting plan credit towards a specific VA contract.
  - Negatives:
    - No affiliation exemption
    - Limited participation

Which Mentor-Protégé Program?

- DOD (includes Army Corps of Engineers)
  - Benefits:
    - Exemption from Affiliation
    - Mentors receive reimbursement for developmental assistance costs
    - Mentors may receive credit toward applicable subcontracting goals.
  - Negatives:
    - Period of performance may not exceed 3 years
      - If unusual circumstances exist, authorized extension may be granted for up to 2 more years.

Which Mentor-Protégé Program?

- Other Possibilities
  - Small Business Jobs Act allows for SBA to establish Mentor-Protégé programs for:
    - HUBZone Companies
    - SDVOSB's
    - WOSB's
  - SBA issued Semiannual Regulatory Agenda on July 7, 2011
    - Roll out expected August 2011
    - Programs will be comparable to the 8(a) program

Joint Venture – Hypothetical #5

- Joe's construction company has received its 8(a) Certification and is considering a possible joint venture for several contracts.
- What are the regulatory considerations?

Joint Venture

- Common Law Rule – joint venture is for a specific purpose, i.e., a single contract
  - Generally, ongoing entity going after multiple contracts is not a JV
- All participants in the JV are prime contractors
- General Rule – participants are affiliated for that procurement – aggregate the receipts or number of employees of all the participants. 13 CFR 121.103(h)(2).

Joint Venture

- Exceptions to aggregation requirement - JV is small if each participant is small
  - "bundled"
  - Procurements above $10 million if the size standard is employee based
  - Procurements with a value in excess of half of a revenue based size standard
  - 13 CFR 121.103(h)(3)(i)

SBA's Definition of Joint Venture

- A joint venture is an association of individuals and/or concerns with interests in any degree or proportion consorting to engage in and carry out no more than three specific or limited-purpose business ventures for joint profit over a two year period, for which purpose they combine their efforts, property, money, skill, or knowledge, but not on a continuing or permanent basis for conducting business generally.
- 13 CFR 121.103(h)

SBA's Definition of Joint Venture

- The same JV entity may receive up to 3 contract awards in a 2 year period
- JV agreement must be in writing
- JV may be formal (separate entity) or informal (not a separate entity)
- If JV is separate legal entity it may be populated or unpopulated
- The same participants can form another JV and pursue up to 3 more opportunities

SBA's Definition of Joint Venture

- Once JV receives an award clock starts ticking
- May receive more than 3 awards if firm had not received 3 awards and offer was made prior to 2 years having passed since first award
- JV must meet Limitations on Subcontracting (performance requirements) FAR 52.219-14; 13 CFR 125.6.
- For size purposes, a concern must include in its receipts its proportionate share of joint venture receipts, and in its total number of employees its proportionate share of joint venture employees. 13 CFR 121.103(h)(5).

Can Joe's 8(a) company participate in SBA's 8(a) Mentor-Protégé program and joint venture with the mentor? YES

8(a) Mentor Protégé Program

- Mentor can be large business
- Mentor can have up to 3 protégés at one time
- Protégé can have second Mentor, corresponding to an unrelated, secondary NAICS code.
- Mentor/Protégé Agreement must be approved by SBA before the firms can submit an offer on a procurement as a small business.
- SBA approved Mentor/Protégé joint ventures are small for federal subcontracts.
- SBA prohibited from approving a new Mentor/Protégé relationship within six months of the end of an 8(a) Participant's program term.

8(a) Joint Ventures

- For all contracts, the JV agreement must comply with the 8(a) JV requirements in 13 CFR 124.513(c).

- JV must meet limitations on subcontracting. For all contracts, 8(a) Participant must perform 40% of the total amount of work the JV and any of its participants will perform at the prime or subcontract level. 13 CFR 124.513(d).

  - Compliance with (c) and (d) can be challenged through a size protest. 13 CFR 121.103(h)(3)(iii).

8(a) Joint Ventures

- Competitive 8(a) procurement - determine apparent successful offeror and request eligibility determination from District Office. 13 CFR 124.507(a), (b).

- For 8(a) contracts, District Office must approve JV agreement prior to award.

- No requirement to be listed in ORCA/CCR as an approved 8(a) JV in order to be considered or eligible for award.

Thank You!

Questions?

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