



WEBINAR

Understanding VA's and SBA's New SDVOSB Rules

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Overview

- SBA's and VA's new rules on ownership and control of SDVOSBs
- What should you do in response to the new rules?
- New VA protest and verification appeal procedures
- Recent SDVOSB cases of note

Background

- Both VA and SBA have their own SDVOSB programs
 - VA and SBA have their own rules on SDVOSB eligibility—confusing!
 - VA verifies VOSBs and SDVOSBs for VA procurements through the Center for Verification and Evaluation (“CVE”)
 - SBA does not currently verify SDVOSB status; if eligible, firms may self-certify their SDVOSB status in SAM.gov
- Previously, standards for veteran ownership and control differed between SBA and VA rules
 - VA rules have been a little more flexible
 - No flexibility under SBA rules: “all means all”

Congress Stepped In Last Year

- To try to resolve the confusion and create one unified set of rules, the 2017 National Defense Authorization Act (“NDAA”) gave sole authority to SBA for determining ownership and control of VOSBs/SDVOSBs
- The 2017 NDAA also granted SBA’s Office of Hearings and Appeals (“OHA”) the ability to hear appeals from CVE protests and verification determinations
- In response to this law, last January, SBA and VA each proposed rules to implement Congress’ direction

Final Rules Effective October 1, 2018

- SBA's and VA's new rules went into effect on October 1, 2018
- Creates new unified rules for ownership and control of VOSBs/SDVOSBs at both VA and SBA
- SBA's rules now exclusively govern ownership and control requirements for all VOSBs and SDVOSBs
 - VA's rules now refer to SBA's rules for ownership and control
 - VA's CVE is still responsible for verifying VOSBs or SDVOSBs for VA procurements—but they now do so using SBA's rules
 - Self-certification still applies outside VA...for now

Summary of What's New in SBA's Rules

- Like VA, SBA rules now permit surviving spouse to maintain SDVOSB status under certain conditions
- SBA now permits five “unanimity” or veto rights for non-veterans—but only five
- SBA added several situations that create “rebuttable presumptions” of control by a non-veteran...but SBA did not give clear guidance on how to rebut the presumptions

SBA's Rules on Unconditional Ownership

- At least 51% of the SDVOSB must be unconditionally and directly owned by one or more SDVs
- Unconditional means ownership 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
 - SBA rules recognize exceptions for death or incapacity of the SDV
 - What about rights of first refusal?
- SBA will not take community property laws into account when assessing the veteran's ownership

Pledging Ownership as Collateral

- SBA's rules recognize that using ownership as collateral does not affect its status as unconditional ownership, including seller-financed transactions
- The ownership pledge must follow normal commercial practices, and the veteran must control absent violations of the terms
 - Traditional bank financing should be considered normal commercial practices, and veteran would maintain control absent default
 - Loans from private parties are riskier and may (or may not) be considered normal commercial practices depending on the terms and surrounding circumstances



Financial Benefits of Ownership

- SBA's rules require that the veteran receives the financial benefits commensurate with his or her ownership
- This means the veteran must receive at least 51% of the annual distribution of profits, and the veteran's share of the profits must be commensurate with the veteran's ownership interest (i.e., if the veteran owns 75%, the veteran must receive 75% of the profits)
- The veteran must also receive 100% of the value of each share of stock he or she owns, if the stock is sold

Surviving Spouse

- An SDVOSB will remain eligible under the SDV's surviving spouse if:
 - Surviving spouse of deceased SDV acquires SDV's ownership
 - SDV had service-connected disability rated as 100% disabling, or the SDV died as a result of service-connected disability
 - For a CVE-verified company, it was included in the VIP database immediately prior to the veteran's death
- SDVOSB status continues until the earlier of:
 - Spouse remarries,
 - Spouse relinquishes ownership, or
 - 10 years after the date of the SDV's death

The Veteran Must Be In Control

- SBA rules require the veteran to have control over the management and daily business operations
 - Daily business operations now defined as: the marketing, production, sales, and administrative functions of the firm, as well as the supervision of the executive team, and the implementation of policies
 - This list is not exhaustive
- The veteran must also have control over long-term decision-making (except for “extraordinary circumstances”)
- For firms set up as partnerships, the veteran must control 51% of the aggregate voting interests but is no longer required to be both a general and limited partner

Rights for Non-Veterans

- Generally speaking, there cannot be any voting requirements that the veteran cannot satisfy on his or her own
 - This means the veteran's vote, alone, controls all company decisions
 - CVE applicants and participants must notify CVE of any "supermajority" voting requirements contained in corporate documents or required by state law
- However, SBA's rules now permit the company to give non-veterans a veto right over the following five "extraordinary circumstances":
 - Adding a new equity stakeholder
 - Dissolution of the company
 - Sale of the company
 - Merger of the company
 - Company declaring bankruptcy
- **Key:** SBA will not permit veto rights for non-veterans on anything other than the five extraordinary circumstances listed above

SBA May Find the Veteran Does Not Control When...

- Non-veteran is involved in management or ownership and is a current or former employer of the veteran
- Non-veteran receives the highest compensation
- SDVOSB is co-located with another firm and has some common ownership
- Sharing employees, resources, equipment, or services with another firm in the same or similar line of business, and that firm or an owner, director, officer, manager, or direct relative has equity interest in the SDVOSB
- Non-veteran has equity in the SDVOSB and provides critical financial or bonding support to the SDVOSB
- Non-veteran holds a critical license
- SDVOSB has a business relationship with a non-veteran that inhibits the veteran from exercising independent business judgment

SBA May Find the Veteran Does Not Control When...

- Non-veteran provides a loan to the veteran or SDVOSB
 - However, a loan or guaranty on commercially reasonable terms does not, by itself, give the non-veteran control
 - SBA says it will look at “other factors” but it is not clear what those will be
- Veteran does not work for the SDVOSB during what are the normal business hours for the SDVOSB’s industry
 - If your industry is “9 to 5,” and you work nights and weekends, this could be an issue

SBA May Find the Veteran Does Not Control When...

- Veteran does not live within a reasonable commute to HQ and/or job sites
 - Applies regardless of the SDVOSB's industry
 - SBA says the ability to answer emails, communicate through phone/skype, etc., is not enough
 - Unclear what SBA expects if the SDVOSB has projects around the country

Rebutting the Presumptions

- Fortunately, all of the non-veteran control circumstances discussed on the prior slides are “rebuttable presumptions” of control
- This means you can demonstrate to SBA that the veteran controls, even if these circumstances are present
- Unfortunately, SBA’s rules do not provide much guidance on how you can rebut the presumptions

What Should You Do Based on SBA's New Rules?

- Review your Operating Agreement or Bylaws to confirm they are consistent with the new rules
- If you have a minority, non-veteran partner, you can consider giving them the five permitted veto rights—but no more
- Assess your current operations to determine if you have any potential issues under the rebuttable presumptions of control by non-veterans
 - If you do, take proactive steps to rebut the presumption and document what you have done

VA's Revised Rules

- Refer to SBA's rules on ownership and control and revises definitions to have the same meaning as SBA's rules
- Helpful change for joint ventures:
 - VA's old rule required the SDVOSB partner in the JV to receive at least 51% of the JV's profits
 - New rule is consistent with SBA, which requires profit to be shared by JV partners based on the work each company performs

New Rules on CVE Protests and Appeals

- Old VA rules:
 - Appeals from CVE decisions were decided by VA
 - VOSB/SDVOSB status protests are filed with the contracting officer and were decided by VA
- New VA rules:
 - Appeals from CVE decisions go to SBA's OHA
 - VOSB/SDVOSB status protests are filed with the contracting officer and are then sent to SBA's OHA for ruling

New Rules on CVE Protests and Appeals

- Must appeal to OHA within 10 business days after adverse decision from CVE
- Must file the VOSB/SDVOSB status protest with the contracting officer within five business days after first learning the identity of the successful offeror
 - Unlike a disappointed offeror, the contracting officer may file protest challenging an awardee's CVE eligibility at any time during the life of a VA contract

Recent SDVOSB Cases

- Federal Circuit: PDS Consultants, Inc. v. United States & Winston-Salem Industries for the Blind
 - Two statutory regimes to benefit two historically disadvantaged groups: veterans (Vets First/Rule of Two) and disabled persons (JWOD/AbilityOne)
 - JWOD applies to all agencies of the federal government, Vets First applies only to VA procurements and only when the Rule of Two is satisfied
 - The requirements of Vets First take precedence over the JWOD when the two conflict

Recent SDVOSB Cases

- Court of Federal Claims: Electra-Med Corp. v. United States
 - Protest of sole source modification to VA's prime vendor contracts for medical supplies
 - COFC noted that the Supreme Court has left no doubt Vets First requires the "Rule of Two" be applied to every possible purchase made by the VA
 - COFC found that the VA violated Vets First
 - However, COFC did not issue injunction because harm to VA outweighs harm to plaintiff

Questions?

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