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GAO Rules That *Kingdomware* "Rule of Two" Does Not Govern Leasehold Acquisitions Conducted by GSA on Behalf of VA

By Gordon Griffin, Robert C. MacKichan Jr., and Amy L. Fuentes*

A ruling by the U.S. Government Accountability Office addressed a question that has long troubled federal real estate practitioners that the U.S. Supreme Court left unanswered in its Kingdomware v. United States *decision: Is the acquisition of a leasehold interest an acquisition of goods or services? The authors of this article discuss the ruling.*

The U.S. Government Accountability Office ("GAO") ruled[1] that the "Rule of Two" of the Veterans Benefits, Health Care, and Information Technology Act of 2006 ("VBA") does not require the U.S. General Services Administration ("GSA") to set aside for veteran-owned small businesses any lease procurements conducted on behalf of the U.S. Department of Veterans Affairs ("VA").

This ruling addresses a question that has long troubled federal real estate practitioners that the U.S. Supreme Court left unanswered in its *Kingdomware v. United States*[2] decision: Is the acquisition of a leasehold interest an acquisition of goods or services?

According to GAO, it is not, and this distinction between goods and services and leasehold interests means that the VBA does not govern the acquisition of leasehold interests by another agency on behalf of the VA.

MAJOR TAKEAWAYS

- For the first time, an adjudicative body has directly addressed the question of whether the Rule of Two in the VBA applies to GSA acquisitions of leases on behalf of the VA. According to GAO's decision

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[1] https://www.gao.gov/assets/710/703565.pdf.

[2] https://www.supremecourt.gov/opinions/15pdf/14-916_6j37.pdf.

in *Cross & Company, LLC*,[3] it does not.

- "Goods and Services," as referenced in the VBA, *does not* include leasehold interests, even when those leases require design and construction services.
- Government contractors should be aware that following the *Cross & Company* decision, agencies with independent leasing authority may determine that the Federal Acquisition Regulation ("FAR") does not apply to leasehold acquisitions.

BACKGROUND—THE VBA AND THE U.S. SUPREME COURT'S *KINGDOMWARE* DECISION

In 2006, Congress passed, and President George W. Bush signed into law, the VBA, which requires the VA to set aside procurements for veteran-owned small businesses when the Contracting Officer reasonably believes that there could be two or more small, veteran-owned business that will submit offers (the "Rule of Two"):

> Except as provided in subsections (b) and (c), for purposes of meeting the goals under subsection (a), and in accordance with this section, a contracting officer of the Department shall award contracts on the basis of competition restricted to small business concerns owned and controlled by veterans if the contracting officer has a reasonable expectation that two or more small business concerns owned and controlled by veterans will submit offers and that the award can be made at a fair and reasonable price that offers best value to the United States.[4]

The Rule of Two requires the VA to set aside procurements for veteran-owned small businesses ("VOSBs") or service-disabled veteran-owned small businesses ("SDVOSBs") when market research indicates that two or more such entities would submit offers, assuming the award can be made at a fair and reasonable price.

The VBA also contains a provision that governs certain procurements made by other agencies on behalf of the VA:

> If after December 31, 2008, the Secretary enters into a contract, memorandum of understanding, agreement, or other arrangement with any governmental entity to acquire goods or services, the Secretary

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[3] B-417971 (Comp. Gen. Dec. 20, 2019).

[4] 38 U.S.C. § 8127(d), *available at* https://uscode.house.gov/view.xhtml?req=granuleid:USC-prelim-title38-section8127#=0&edition=prelim.

> shall include in such contract, memorandum, agreement, or other arrangement a requirement that the entity will comply, to the maximum extent feasible, with the provisions of this section in acquiring such goods or services.[5]

This provision essentially states that when the VA uses another agency to procure goods and/or services on its behalf, the Rule of Two also applies, and such procurements must be set aside if the requirements of section 8127(d) are met.

For several years after the passage of the Act, the VA maintained that the Rule of Two was discretionary, and not mandatory (especially if the VA had met its set-aside goals). Many veteran-owned contractors disagreed, and GAO entertained a number of protests by contractors seeking to force the VA to set aside contracts for procurements for goods and services conducted on the GSA's Federal Supply Schedules ("FSS"). GAO sustained a number of these protests, but the VA refused to follow GAO's recommendation to set aside awards and reprocure requirements from a pool of eligible veteran-owned businesses.

After several such iterations, GAO finally indicated in *Kingdomware Technologies-Reconsideration*,[6] that it would no longer entertain these protests. GAO explained its rationale as being because of the lack of meaningful remedy available in its forum and the U.S. Court of Federal Claim's ("COFC") decision to uphold the VA's interpretation:

> Although our Office is not bound by the court's decisions, its decision in *Kingdomware*, together with the VA's position on the meaning of this statute, effectively means that protesters who continue to pursue these arguments will be unable to obtain meaningful relief. Consequently, under these circumstances, we will no longer consider protests based only on the argument that the VA must consider setting aside procurements for SDVOSBs (or VOSBs) before conducting an unrestricted procurement under the FSS.[7]

The contractor disagreed with this decision and brought a protest along the same grounds at COFC (which upheld the VA's position), the U.S. Court of Appeals for the Federal Circuit (which affirmed COFC's decision below), and finally to the Supreme Court, which ruled as follows:

> Congress' use of the word "shall" demonstrates that § 8127(d) man-

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[5] 38 U.S.C. § 8127(i).

[6] B-407232.2, Dec. 13, 2012, 2012 CPD ¶ 351, *available at* https://www.gao.gov/assets/b-407232.2.pdf.

[7] *Id.* at 3.

> dates the use of the Rule of Two in all contracting before using competitive procedures . . . Accordingly, the Department shall (or must) prefer veteran-owned small businesses when the Rule of Two is satisfied.[8]

In short, the Supreme Court sided with GAO, overruling the Federal Circuit, and in doing so, required the VA to set aside all contracts[9] meeting the Rule of Two prescribed by the VBA.

Notably, however, the question posed by the contractor in *Kingdomware* was limited to the scope of the contract at issue, which was a contract for software development services.

CROSS & COMPANY: GAO DETERMINES THAT THE RULE OF TWO IS LIMITED IN SCOPE FOR AGENCIES OTHER THAN THE VA FOR THE PROCUREMENT OF GOODS AND SERVICES

The Pre-Award Protest

In summer 2019, a VOSB protested the terms of a request for lease proposals ("RLP") issued by the GSA for the lease of space to be used as a community-based outpatient clinic ("CBOC") by the VA in the Pittsburgh, Pennsylvania, area. The protestor argued that, because the RLP did not set aside the procurement for VOSB's, the solicitation violated the VBA. Specifically, the protestor alleged that "the statutory intent of 38 U.S.C. § 8127(i) is to extend the mandatory requirements of 38 U.S.C. § 8127(d) to instances where another governmental entity is conducting the procurement on behalf of the VA."[10]

GSA defended its refusal to set aside this procurement:

> GSA first argues that the rule of two does not apply to this procurement because 38 U.S.C. § 8127(d) applies only to contracts awarded by a VA contracting officer, whereas this procurement is conducted by GSA, through a GSA lease contracting officer, and utilizing GSA's authority pursuant to 40 U.S.C. § 585. Second, GSA argues that 38 U.S.C. § 8127(i) applies only to the acquisition of goods and services, which does not include leasehold interests.[11]

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[8] 136 S. Ct. 1969, 1977 (2016).

[9] Government leases *are* government contracts. *See Forman v. United States*, 767 F.2d 875, 879 (Fed. Cir. 1985) (noting that Government leases are government contracts). Accordingly, following the U.S. Supreme Court's decision in *Kingdomware*, the Rule of Two must apply to lease acquisitions conducted by the VA on its own behalf, as noted by GAO in the *Cross & Company* decision.

[10] *Cross & Company*, *supra* note 3.

[11] *Id.*

GAO Declares the Rule of Two Is Inapplicable to GSA Lease Acquisitions

Following its statutory analysis and consideration of the parties' respective arguments, GAO unambiguously held in *Cross & Company* that the Rule of Two *does not* apply when GSA conducts a leasehold acquisition on behalf of the VA because the VBA only requires other agencies to set aside procurement for "goods and services" and leasehold interests are neither goods nor services:

> Here, we conclude that the mandatory preference in 38 U.S.C. § 8127(d) does not apply to this procurement. While the plain language of the statute establishes a mandatory preference for VOSBs and SDVOSBs, it also limits the application of the mandatory preference in subsection 8127(d) to when the VA conducts the procurement. In contrast, the conduct of a procurement by another governmental entity on behalf of the VA is addressed in subsection 8127(i).
>
> We also conclude that 38 U.S.C. § 8127(i) does not apply to this procurement because GSA is not acquiring goods or services, but is acquiring a leasehold in real property. . . .
>
> ***
>
> [W]e find that it is reasonable for GSA to interpret the statutory language in § 8127(i) to limit the application of the rule of two specifically to the acquisition of goods or services, when another governmental entity is conducting the procurement.
>
> ***
>
> [A]s the protester's arguments are not borne out by the plain meaning of unambiguous statutory language, we find that the [Act] is not applicable to GSA's procurement of real property leases here.[12]

In short, GAO held that the provision of the VBA governing procurements by agencies other than the VA (Section 8127(i) of the Act), was limited in scope to the procurement of goods and services, and that leasehold interests are neither goods nor services. Accordingly, the Rule of Two provision is inapplicable to the acquisition of leasehold interests.

IMPLICATIONS AND TAKEAWAYS FROM GAO'S *CROSS & COMPANY* DECISION

GAO's decision in *Cross & Company* has the potential for wide-ranging implications for government landlords. The FAR limits its own applicability to

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[12] *Id.* (internal citations omitted).

procurement for "supplies" and "services."[13] Given the arguable equivalence between "supplies" (in the FAR) and "goods" (in the VBA), this ruling could lead agencies with independent leasing authority to determine that the FAR does not apply to leasehold acquisitions. While GSA's General Services Acquisition Regulation ("GSAR") indicates that "[t]he FAR does not apply to leasehold acquisitions of real property,"[14] other agencies have not enjoyed the freedom to procure leasehold interests outside of the FAR's requirements, absent a use of delegated leasing authority from GSA. It remains to be seen whether this will change in the future.

Notably, however, this ruling likely has no impact on the VA's use of its independent leasing authority, nor does it likely impact the VA's use of GSA-delegated leasing authority; in both cases, because the procurement is being conducted by the VA, Section 8127(d) of the VBA and the Rule of Two will apply.

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[13] 48 C.F.R § 2.101, *available at* https://www.ecfr.gov/cgi-bin/text-idx?SID=e81ae25a9586befdfcead2ba9ac0d5f3&mc=true&node=se48.1.2_1101&rgn=div8.

[14] 48 C.F.R. § 570.101(d), *available at* https://www.ecfr.gov/cgi-bin/text-idx?SID=e81ae25a9586befdfcead2ba9ac0d5f3&mc=true&node=se48.4.570_1101&rgn=div8.