Understanding an Operating Agreement and Its Amendments

Issue:
This brief explains the function of the Operating Agreement, how it is used during the verification process, and how it is amended.

(For purposes of this brief, the regulations when referring to Service-Disabled Veterans applies equally to Veterans; applicant refers to the business entity applying for verification; and participant refers to a business entity that has already been verified.)

The Regulations:

13 C.F.R. § 125.11 provides:

Veteran owned small business concern means a small business concern:

(1) Not less than 51 percent of which is owned by one or more veterans or, in the case of any publicly owned business, not less than 51 percent of the stock of which is owned by one or more veterans; and

(2) The management and daily business operations of which are controlled by one or more veterans. All of the provisions of subpart B of this part apply for purposes of determining ownership and control.

13 C.F.R. 125.12(b) provides “[i]n the case of a concern which is a partnership, at least 51% of aggregate voting interest must be unconditionally owned by one or more service-disabled veterans. The ownership must be reflected in the concern’s partnership agreement.”

13 C.F.R. 125.12(c) provides “[i]n the case of a concern which is a limited liability company, at least 51 % of each class of member interest must be unconditionally owned by one or more service-disabled veterans.”

13 C.F.R. 125.13(a) provides “[c]ontrol by one or more service-disabled veterans means that both the long-term decisions making and the day-to-day management and administration of the business operations must be conducted by one or more service-disabled veterans (or in the case of a veteran with permanent and severe disability, the spouse or permanent caregiver of such veteran).”

13 C.F.R. 125.13(c) provides “[i]n the case of a partnership, one or more service-disabled veterans (or in the case of a veteran with permanent and severe disability, the spouse or permanent caregiver of such veteran) must serve as general partners, with control over all partnership decisions.”

13 C.F.R. 125.13(d) provides that “[i]n the case of a limited liability company, one or more service-disabled veterans (or in the case of a veteran with permanent and severe disability, the spouse or permanent caregiver of such veteran) must serve as managing members, with control over all decisions of the limited liability company.”

What This Means:
Subpart B as referred to in 13 C.F.R. § 125.11 is saying that anywhere in the regulations where the term Service-Disabled Veteran is used, it is equally applicable to Veterans for purposes of determining eligibility.

An Operating Agreement should address the ownership and control requirements found under 13 C.F.R. § 125.12(a) and 13 C.F.R. §§
125.13(a) and (d).

An Operating Agreement is an agreement among members of a limited liability company (LLC) or partners in a partnership that governs the financial interests, affairs, and the rights and duties of the members to each other and non-members. Some states do not require LLCs to have Operating Agreements; however, without an Operating Agreement or comprehensive articles of organization, CVE will be unable to determine Veteran control.

Other than in the case of a single member - member managed LLC, CVE will require an applicant to provide an Operating Agreement. CVE does not consider letters of explanation as official documentation to establish ownership or control, in the case of an LLC. In all cases, Partnerships must provide a Partnership or Operating Agreement.

CVE is unlikely to find that a firm is eligible for inclusion in the VIP database when there is no Operating Agreement and there are several owners. CVE relies on each business concern to provide information that can be used to understand day-to-day management and long-term decision making.

**Amendments to Operating Agreements**

Typically, Operating Agreements may only be amended through specified processes and are therefore not generally subject to alteration or amendment solely by meeting minutes. In most cases, operating agreements are amended by (1) an addendum (executed by the LCC membership) or (2) a complete rewrite of the document that incorporates the proposed amendments. Once executed by the members, the amended operating agreement will then be the controlling document which governs ownership and control of the LLC.

CVE considers the ability to amend the Operating Agreement to be a business decision that the Veteran(s) must unilaterally control. Therefore, if the Operating Agreement contains a provision that requires the approval of the non-Veteran member(s) in order to amend the Operating Agreement, CVE will generally find that the Veteran has not demonstrated control as required by the regulation.

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**VA Office of Small and Disadvantaged Business Utilization**

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