Cite as: *CVE Appeal of Holistic Serendipity LLC d/b/a Native Ceuicals Tampa.*, SBA No. CVE-242-A (2022)

United States Small Business Administration
Office of Hearings and Appeals

CVE Appeal of: Holistic Serendipity LLC d/b/a Native Ceuticals Tampa, Appellant	SBA No. CVE-242-A Decided: October 3, 2022

APPEARANCE

Zachary K. Zindler, Owner, Holistic Serendipity LLC d/b/a Native Ceuticals Tampa, Sarasota Florida

DECISION[1]

I. Introduction and Jurisdiction

On May 17, 2022, the U.S. Department of Veterans Affairs (VA) Center for Verification and Evaluation (CVE) denied an application from Holistic Serendipity LLC d/b/a Native Ceuticals Tampa (Appellant) for verification as a Service-Disabled Veteran-Owned Small Business (SDVOSB). CVE determined that Appellant did not demonstrate that it is fully controlled by one or more service-disabled veterans, as is required by 13 C.F.R. § 125.14, due to provisions in an Affiliate Agreement between Appellant and a non-SDVOSB.[2] On appeal, Appellant maintains that CVE's decision was clearly erroneous and requests that the U.S. Small Business Administration (SBA) Office of Hearings and Appeals (OHA) reverse. For the reasons discussed *infra*, the appeal is denied.

OHA adjudicates CVE appeals pursuant to 38 U.S.C. § 8127(f)(8)(A) and 13 C.F.R. part 134 subpart K. Appellant timely filed the instant appeal within 10 business days after receiving the denial notice. 13 C.F.R. § 134.1104(a). Accordingly, this matter is properly before OHA for decision.

[1] This decision was originally issued under the confidential treatment provision of 13 C.F.R. § 134.205. OHA now publishes a redacted version of the decision for public release.

[2] Effective August 22, 2022, SBA redesignated the SDVOSB ownership and control regulations, previously found at 13 C.F.R. §§ 125.11 through 125.14, as §§ 125.12 through 125.15. 87 Fed. Reg. 43,731, 43,739 (July 22, 2022). Citations in this decision are to the SDVOSB ownership and control regulations as redesignated.

II. Background

A. Affiliate Agreement

Appellant is a limited liability company (LLC) based in the state of Florida, engaged in the business of "provid[ing] alternative options to help address mental and physical health symptoms with organic hemp products." (Case File (CF), Exhs. 15, 68.) In April 2022, Appellant applied for verification as an SDVOSB and provided various requested documentation. (CF, Exh. 77.) Among other information, Appellant submitted a copy of an Affiliate Agreement between Appellant's sole owner, Mr. Zachary K. Zindler, and Native Ceuticals, LLC (Native Ceuticals), a company based in North Carolina. (CF, Exh. 82.) The Affiliate Agreement became effective May 14, 2021, and identifies Mr. Zindler as "the Affiliate" and Native Ceuticals as "the Company." (*Id.* at 1.)

The Affiliate Agreement contains the following provisions pertinent to this appeal:

[Text of the Affiliate Agreement redacted]

(*Id.* at 1, 3-4, 6-8, 11-12.)

B. Post-Review Findings Notice

On April 29, 2022, CVE issued Appellant a Post-Review Findings (PRF) Notice. (CF, Exh. 38.3.) The Notice explained that CVE had discovered issues that likely would prevent Appellant from being verified as an SDVOSB.

The Notice divided CVE's concerns into two categories. First, CVE noted that Appellant "sells hemp derived products," a type of business which may be problematic under federal law. (*Id.* at 2.) CVE stated:

> The Controlled Substance Act (CSA), 21 United States Code (USC) §§ 811 and 812, provides that Marijuana is a Schedule I Controlled Substance and is illegal. If a business concern elects to implicitly or explicitly include in its marketing material or pursues contracting opportunities relating to the production and/or endorsement of Marijuana and simultaneously applies for and becomes verified by CVE as [an SDVOSB], the VA could be seen as endorsing illegal conduct under the federal law.

(*Id.* at 1.) CVE reiterated that, because Appellant is "engag[ed] in the sale, growth, or distribution of products derived from the same genus of plant (cannabis) as marijuana," verifying Appellant as an SDVOSB "may give the appearance that the VA is endorsing a company that promotes the use of a Schedule I Controlled Substance." (*Id.*)

Second, CVE found that the Affiliate Agreement between Native Ceuticals and Mr. Zindler places numerous restrictions on his ability to control Appellant, such that Appellant

would not be able to "operate as a viable independent business entity without the support provided by Native Ceuticals (non-Veteran)." (*Id.* at 6.) CVE found that Mr. Zindler and Appellant committed to utilizing Native Ceuticals' products and business model while in the program, to include "required training, marketing, and other business processes that are created and controlled by [Native Ceuticals]." (*Id.* at 3.) CVE was troubled in particular by the following provisions of the Affiliate Agreement:

- Section 2(b) gives Native Ceuticals control over Appellant's website, and restricts Appellant's ability to operate outside a designated location or to set prices higher than the "established maximum" set by Native Ceuticals. (*Id.* at 4.)

- Sections 2(d) and 4(a) require Appellant to exclusively sell products created or approved by Native Ceuticals. (*Id.*)

- Section 4(e) prohibits Appellant from using marketing materials or methods that are not approved by Native Ceuticals. (*Id.*)

- Section 4(f) requires Appellant to adhere to Native Ceuticals' procedures and policies. (*Id.* at 5.)

- Section 4(h) prohibits Appellant from changing, altering, or modifying products or marketing materials without Native Ceuticals' consent. (*Id.*)

- Section 4(j) requires Appellant to maintain a minimum inventory of $10,000 of Native Ceuticals products at a designated territory. (*Id.*)

- Section 4(k) requires Appellant to keep product inventory in accordance with Native Ceuticals' instructions. (*Id.*)

- Section 4(p), requires, among other things, compliance with Native Ceuticals' specified interior design for a store. (*Id.*)

- Section 4(q) requires Appellant to provide any employees with an employee handbook that contains policies and procedures set by Native Ceuticals. (*Id.*)

- Section 12 is a "Competition Clause" that prohibits Appellant from being associated with a competitive business within 15 miles of the agreed territory during the duration of the agreement and for one year after the termination or expiration of the agreement. (*Id.*)

Although Appellant claimed that the Affiliate Agreement is merely a licensing arrangement that authorizes Appellant to sell products created by Native Ceuticals, CVE found that the Affiliate Agreement places numerous "restrictions on operational decision making and requires a specific business model [Appellant] must follow in selling [Native Ceuticals] products." (*Id.*) CVE concluded that because all of Appellant's revenue is derived from selling Native Ceuticals' products under the terms of the Affiliate Agreement, Appellant cannot be found to exercise independent business judgment. (*Id.*)

C. Response to PRF Notice

On May 9, 2022, Appellant responded to the PRF Notice. (CF, Exh. 100.) Appellant maintained that the purpose of the Affiliate Agreement is "strictly" to enable Appellant to sell Native Ceuticals' products and to utilize the "Native Ceuticals" brand name. (*Id.* at 1.) Native Ceuticals provides "marketing material, coaching, and [a] training program, among other things, for their product alone." (*Id.*, emphasis Appellant's.) Appellant asserted that the Affiliate Agreement is "very similar to a manufacturing agreement" where Native Ceuticals acts as a "manufacturer" that sets prices for its products and Appellant is "essentially a distributor" that sells such products. (*Id.*) The Affiliate Agreement, thus, only applies to Native Ceuticals' products and confers control over "only the product they provide." (*Id.*) Appellant claimed that because Appellant "do[es] not have a storefront" and operates out of Mr. Zindler's personal residence, Appellant "can provide any other products at [its] choosing." (*Id.*) Native Ceuticals "in no way, shape, or form, ha[s] any control over [Appellant], only the product [Native Ceuticals] provide[s] to [Appellant] which is typical for any distributor." (*Id.*)

D. Final PRF Notice

On May 12, 2022, CVE issued Appellant a Final PRF Notice. (CF, Exh. 38.4.) In the Final PRF Notice, CVE stated that, notwithstanding the additional information Appellant had provided, CVE still would be unable to verify Appellant as an SDVOSB. (*Id.* at 1.) The Final PRF Notice again detailed two main categories of issues. (*Id.*) Upon reviewing Appellant's response to the original PRF Notice, CVE, first, concluded that Appellant's line of business, *i.e.*, the sale of hemp derived products, has not changed. (*Id.* at 2-3.) CVE reiterated its concern that verifying Appellant as an SDVOSB "may give the appearance that the VA is endorsing a company that promotes the use of a Schedule I Controlled Substance." (*Id.* at 2.)

Second, CVE continued to harbor doubts as to whether Appellant's relationship with Native Ceuticals, a non-SDVOSB, causes such dependence that Appellant cannot exercise independent business judgment. (*Id.* at 9.) Specifically, Appellant acknowledged that the Affiliate Agreement confers Native Ceuticals control over the products Appellant sells, although Appellant claimed that the Affiliate Agreement does not give Native Ceuticals full control over Appellant's business. (*Id.* at 8.) CVE found that the provisions discussed in the original PRF Notice "are still in effect," and continue to grant Native Ceuticals extensive power to control Appellant. (*Id.*)

The Final PRF Notice explained that Appellant could choose to withdraw its application for verified status, and re-apply at a later time. (*Id.* at 9.) Absent such a withdrawal, CVE would issue a letter formally denying Appellant's application. (*Id.*)

E. Denial Letter

On May 17, 2022, CVE denied Appellant's application for verification as an SDVOSB. (CF, Exh. 107.1.) CVE found that Appellant's owner, Mr. Zindler, is a service-disabled veteran.

(*Id.* at 1.) However, CVE was unable to conclude that Appellant meets other eligibility requirements. (*Id.*)

CVE first explained that, under 13 C.F.R. § 124.13(i), non-service-disabled veteran persons or entities must not control an SDVOSB. (*Id.*) There is a rebuttable presumption that non-service-disabled veteran persons or entities control a firm when business relationships exist "which cause such dependence that the applicant or concern cannot exercise independence business judgment without great economic risk." (*Id.* at 1-2, quoting 13 C.F.R. § 125.14(i)(7).)

In the instant case, the Affiliate Agreement negatively impacts Mr. Zindler's ability to control Appellant, and also allows Native Ceuticals, a non-SDVOSB, to exert actual control over Appellant. (*Id.* at 7.) In CVE's view, it "does not appear that [Appellant] would be able to operate as a viable independent business entity" without Native Ceuticals. (*Id.*) Appellant attempted to rebut the presumption that Native Ceuticals controls Appellant by likening the relationship to that of a manufacturer and a "distributorship." (*Id.* at 6-7.) Appellant further claimed that because it does not have a physical storefront, it is not limited to selling only Native Ceuticals' products. (*Id.* at 6.) CVE found these arguments unpersuasive, as the large majority of the provisions of the Affiliate Agreement that CVE identified as problematic remain in effect.[3] (*Id.* at 5-7.) Specifically, Native Ceuticals still controls numerous aspects of Appellant's daily business operations pursuant to sections 2(b), 2(d), 4(a), 4(e), 4(f), 4(h), 4(j), 4(k), 4(p), and 12 of the Affiliate Agreement. (*Id.* at 6-7.) These provisions give Native Ceuticals control over matters such as Appellant's "marketing and sales strategies" and "product portfolio," which are fundamental to Appellant's business operations. (*Id.* at 7.) Because Native Ceuticals controls aspects of Appellant's daily business operations pursuant to the referenced sections of the Affiliate Agreement, Appellant and Mr. Zindler are dependent upon Native Ceuticals, and Native Ceuticals "controls or has the power to control [Appellant's] business." (*Id.*)

CVE also determined that, because Appellant "sells hemp derived products," CVE cannot verify Appellant as an SDVOSB, as doing so may create the appearance that "VA is endorsing a company that promotes the use of a Schedule I Controlled Substance." (*Id.* at 8-9.)

F. Appeal

On June 1, 2022, Appellant timely filed the instant appeal. Appellant contends that CVE erred in denying Appellant's application for verification. Appellant then addresses issues related to control by largely relying on what it claims to be "Native Ceuticals' own explanation" of provisions in the Affiliate Agreement. (Appeal at 2.)

Appellant asserts, first, that Native Ceuticals permits that "Mr. Zindler can personally sell other products as long as we [Native Ceuticals] know what it is." (*Id.*) According to Appellant, Native Ceuticals has indicated that Appellant "[a]bsolutely . . . can sell other products, once it is approved," provided that any such "non-CBD outside products . . . don't hurt Native Ceuticals

[3] CVE acknowledged that Appellant "may not be required to provide and operate pursuant to the employee handbook developed by Native Ceuticals," as indicated in section 4(q) of the Affiliate Agreement, "because [Appellant] does not have employees." (*Id.* at 6-7.)

brand." (*Id.*) Furthermore, the Native Ceuticals "approval process is not restrictive but normal under branding." (*Id.*) Given these reported remarks by Native Ceuticals, it is clear that Native Ceuticals "has no interest in disallowing [Appellant] to sell other health and wellness products." (*Id.*) Appellant argues that "[t]hough there is a brief period of time in which [Appellant] may not compete by selling other CBD brands, this is limited to a specific geographical area and [Appellant] can still rely on its other products and services to operate during this window." (*Id.*)

Next, Appellant claims that there is no requirement that it use Native Ceuticals' employee handbook or training because the Affiliate Agreement states that a sample employee handbook will be provided upon request. (*Id.* at 2-3.) As a result, Appellant "can create [its] own" handbook. (*Id.* at 3.) Appellant contends that the Affiliate Agreement was "created, in part, to provide as much aid to [Appellant] as [it] wishes to utilize." (*Id.*)

Appellant argues that it can exercise independent judgment over its marketing because Native Ceuticals has communicated: "[t]here is no requirement to solely use [Native Ceuticals'] marketing, the Affiliate can use his own as long as it doesn't hurt the [Native Ceuticals] brand. The Affiliate can also come up with his own sales strategy." (*Id.*) Appellant insists that the Affiliate Agreement should be understood as a "guide" rather than as a restrictive or binding document. (*Id.*)

Appellant claims that it can exercise independent judgment over its pricing, notwithstanding the terms of the Affiliate Agreement. (*Id.*) The provisions referenced by CVE, §§ 2(b) and 2(c), are commonplace as "nearly all distributors of manufactured products have minimum retail prices." (*Id.*) In Appellant's view, "setting minimum pricing does not pose an economic risk but only further removes the economic risk of [Appellant] selling products but not realizing a revenue." (*Id.*) In addition, although online sales of Native Ceuticals' products may be made only through Native Ceuticals' website, Appellant asserts that Native Ceuticals has indicated that "any income is funneled back to the partner." (*Id.* at 4.)

Appellant claims that it can exercise independent judgment over its interior storefront design. (*Id.*) Contrary to CVE's decision, Native Ceuticals has "clarified" that it will only provide "suggestive direction" on such matters. (*Id.*). Although "Native Ceuticals will provide a subcontracted individual to assist [Appellant] with selecting furniture that attracts the consumer to the space and creates a quality experience," Appellant "can still exercise independent judgment in selecting the specific furniture." (*Id.*)

Lastly, Appellant contends that its relationship with Native Ceuticals should only be prohibited if that relationship poses great economic risk. (*Id.*) Appellant continues:

> Indeed many other businesses have been approved by the CVE that rely on non-veteran third-parties for a variety of functions such as but not limited to manufacturing, marketing, accounting, distributing, and other business functions; no small business can exist in our interconnected world without outsourcing at least some aspect of its operations or otherwise utilizing contractual relationships to ease the burden of operations.

(*Id.*) Appellant renews its contention that Native Ceuticals drafted the Affiliate Agreement "to protect one of the brands sold by [Appellant] and to provide tools to [Appellant] to ease [Appellant]'s overall costs and operational expenses," but not to "interfere with [Appellant]'s operations or independence." (*Id.* at 5.) Appellant further asserts that "many terms contained in the Affiliate Agreement are not actually currently being enforced by Native Ceuticals." (*Id.*) As such, CVE's concerns about the Affiliate Agreement are exaggerated. (*Id.*)

With respect to the remaining issue raised in CVE's determination, that verifying Appellant may create the appearance that CVE endorses the production and sale of marijuana, Appellant argues that CVE's position is "obsolete and moot" because Appellant "does not and will never engage in the sale, growth, or distribution of marijuana or marijuana products." (*Id.* at 5-6.) Rather, Appellant "only sells products that are derived from a federally legal plant, hemp." (*Id.* at 5.) Appellant highlights that enactment of the Hemp Farming Act of 2018 "freed hemp from the controlled substance list and allowed for states to form the framework for its legal production and sale." (*Id.* at 6.) Hemp is defined as cannabis with less than 0.3% tetrahydrocannabinol (THC) concentration. (*Id.*) Appellant's products undergo "[i]ndependent third-party labs test" to ensure that "THC content falls below the federally mandated 0.3% threshold required for hemp," and Appellant also has obtained the requisite "Hemp Food Establishment Permit" from the state of Florida that authorizes Appellant to "manufacture, process, package, hold, prepare, and sell hemp extract" within that state. (*Id.* at 6-7.) Appellant also offers a letter from a hemp advocacy organization, purporting to "explain[] that the Consolidated Appropriations Acts passed since the 2018 Farm Bill bar federally appropriated agencies, such as the VA, from using federal funds to prohibit the transportation, processing, sale or use of hemp." (*Id.* at 7.)

III. Discussion

A. Standard of Review

Under VA regulations, an applicant seeking verification as an SDVOSB bears the burden of proving its eligibility. 38 C.F.R. § 74.11(d). In the event of a subsequent appeal to OHA, Appellant has the burden of proving, by a preponderance of the evidence, that the denial was based upon clear error of fact or law. 13 C.F.R. § 134.1111.

B. Analysis

Appellant has not shown that CVE erred in denying Appellant's application for verified SDVOSB status. This appeal must therefore be denied.

SBA regulations stipulate that an eligible SDVOSB must be unconditionally owned and controlled by one or more service-disabled veterans.[4] "Control" means that both the concern's daily business operations, and its long-term decision-making, are conducted by service-disabled veterans. 13 C.F.R. § 125.14(a). The regulations define "daily business operations" as including,

[4] *See* 13 C.F.R. §§ 125.13 and 125.14. These same regulations also apply to SDVOSB eligibility determinations conducted by CVE. 38 C.F.R. §§ 74.3(a) and 74.4.

but not limited to, "the marketing, production, sales, and administrative functions of the firm, as well as the supervision of the executive team, and the implementation of policies." *Id.* § 125.12. Non-service-disabled veteran individuals or entities must not control the concern. *Id.* § 125.14(i).

In the instant case, CVE determined that although Appellant's principal, Mr. Zindler, is a service-disabled veteran, he does not fully control Appellant. Section II.E, *supra*. More specifically, CVE found that the Affiliate Agreement between Appellant and Native Ceuticals, a non-SDVOSB, imposes numerous restrictions that interfere with Mr. Zindler's ability to control the daily business operations of Appellant. *Id.* CVE expressed concerns in particular that Native controls aspects of Appellant's daily business operations through sections 2(b), 2(d), 4(a), 4(e), 4(f), 4(h), 4(j), 4(k), 4(p), and 12 of the Affiliate Agreement. *Id.*

A review of the Affiliate Agreement confirms that CVE's concerns were well-founded. Section 2(d) of the Affiliate Agreement, for instance, requires that Appellant "may only carry [Native Ceuticals] products at the Store Location," and that Appellant must "not carry and/or offer to customers at the Store Location any other products or services other than those provided by [Native Ceuticals] without first obtaining approval by [Native Ceuticals] in writing, which approval shall be at the sole discretion of [Native Ceuticals]." Section II.A, *supra*. Section 4(a) similarly provides that Appellant must "not promote, market, offer, or sell any other brand of CBD products in the Store Location or any other location, including without limitation any website or e-commerce, unless approved by [Native Ceuticals] in writing, in its sole discretion." *Id.* Such restrictions fundamentally curtail the ability of Mr. Zindler, the service-disabled veteran, to independently operate Appellant, as Mr. Zindler must obtain Native Ceuticals' written consent in deciding the types of products and services Appellant may sell, and the locations and manner in which Appellant may sell them. Appellant's "daily business operations," then, including Appellant's "marketing, production, [and] sales," plainly are not solely within the control of Mr. Zindler.[5]

On appeal, Appellant contends that Native Ceuticals does not treat the Affiliate Agreement as binding, and that Native Ceuticals has no interest in interfering with Appellant's business operations. Section II.F, *supra*. While this may be true, the mere fact that Native Ceuticals chooses not to enforce the Affiliate Agreement does not establish that Native Ceuticals lacks the power to do so. As discussed above, CVE identified numerous terms within the Affiliate Agreement which give Native Ceuticals the power to control aspects of Appellant's "daily business operations," including provisions related specifically to Appellant's marketing, production, sales, and administrative functions and to the implementation of business policies. Sections II.A and II.E *supra*. Even if Native Ceuticals does not currently enforce such provisions, Appellant does not dispute that Native Ceuticals could choose to demand Appellant's compliance at any time. Accordingly, these provisions within the Affiliate Agreement improperly limit Mr. Zindler's ability to control various aspects of Appellant's daily business

[5] As CVE recognized, the Affiliate Agreement also contains numerous other problematic provisions which restrict, for example, the inventory Appellant must maintain; the pricing Appellant may charge; the business practices and policies Appellant must utilize; and Appellant's ability to compete or to conduct business in a manner perceived as detrimental to Native Ceuticals' interests. Section II.A, *supra*.

operations, and CVE did not err in denying Appellant's application for verification as an SDVOSB.

CVE also determined that Appellant is not an eligible SDVOSB under 13 C.F.R. § 125.14(i), which mandates that "[n]on-service-disabled veteran individuals or entities may not control" an SDVOSB. The same regulation further creates a rebuttable presumption that a firm is not controlled by service-disabled veterans if "[b]usiness relationships exist with non-service-disabled veteran individuals or entities which cause such dependence that the applicant or concern cannot exercise independent business judgment without great economic risk." 13 C.F.R. § 125.14(i)(7).

Again, CVE identified provisions within the Affiliate Agreement which permit Native Ceuticals, a non-SDVOSB, to control important aspects of Appellant's day-to-day management. Specifically, CVE found that sections 2(b), 2(d), 4(a), 4(e), 4(f), 4(h), 4(j), 4(k), 4(p), and 12 of the Affiliate Agreement enable Native Ceuticals to exert such control and render Appellant highly dependent upon Native Ceuticals. Section II.E, *supra*. While Appellant disagrees with CVE's assessment, Appellant has not shown that CVE's decision was erroneous or unreasonable. Appellant has not explained, for example, how provisions limiting Appellant to selling and marketing Native Ceuticals' products, at prices unilaterally established by Native Ceuticals, would not require to Appellant rely heavily upon Native Ceuticals to conduct daily business operations. Accordingly, Appellant has not shown any valid reason to disturb CVE's decision.

Lastly, Appellant challenges CVE's conclusion that verifying Appellant as an SDVOSB may create the appearance that "VA is endorsing a company that promotes the use of [marijuana] a Schedule I Controlled Substance." Section II.E, *supra*. I find it unnecessary to resolve this issue. While Appellant emphasizes that it sells only hemp products and not marijuana products, Appellant does not address Native Ceuticals' policies or practices on such matters, and under the Affiliate Agreement, Appellant lacks control over, for example, "Marketing Materials" created by Native Ceuticals. Section II.A, *supra*. The issue is immaterial in any event because, even supposing that Appellant were to prevail on this point, CVE's findings that the Affiliate Agreement improperly limits Mr. Zindler's ability to control aspects of Appellant's daily business operations would still amply justify the decision to deny Appellant's application for verification.

IV. Conclusion

Appellant has not established that CVE erred in denying Appellant's application for verified SDVOSB status. The appeal therefore is DENIED. This is the final agency action of the U.S. Small Business Administration. 38 U.S.C. § 8127(f)(8)(A); 13 C.F.R. § 134.1112(d).

KENNETH M. HYDE
Administrative Judge