

**United States Small Business Administration
Office of Hearings and Appeals**

VSBC Appeal of:

Horizon Marketing, Inc.,
Appellant,

SBA No. VSBC-296-A

Decided: August 3, 2023

APPEARANCE

Kyle J. Johnson, Esq., Johnson & Black, LLP, Visalia, California, for Appellant

DECISION

I. Introduction and Jurisdiction

On May 16, 2023, Horizon Marketing, Inc. (Appellant) appealed a decision of the U.S. Small Business Administration (SBA), denying Appellant's application for certification as a Service-Disabled Veteran-Owned Small Business (SDVOSB). SBA found that Appellant could not be certified due to issues with Appellant's ownership and control. On appeal, Appellant maintains that the denial decision was erroneous, and requests that SBA's Office of Hearings and Appeals (OHA) reverse. For the reasons discussed *infra*, the appeal is denied.

OHA adjudicates SDVOSB status appeals pursuant to the Small Business Act of 1958, 15 U.S.C. §§ 631 *et seq.*, and 13 C.F.R. parts 128 and 134 subpart K. Appellant timely filed the appeal within 10 business days after receiving the denial notice on May 4, 2023. 13 C.F.R. § 134.1104(a). Accordingly, this matter is properly before OHA for decision.

II. Background

A. The Case File

Appellant is a corporation established in the state of California. (Case File (CF), Exh. 40, at 2.) On April 20, 2023, Appellant applied for certification as an SDVOSB, and submitted various supporting documents to SBA. According to Appellant's stock ledger, Mr. Robert R. De La Torre, a service-disabled veteran, was issued 510 of Appellant's 1,000 shares on November 9, 2022. (CF, Exh. 31.) His wife, Mrs. Yvonne A. De La Torre, a non-veteran, was issued the remaining 490 shares. (*Id.*) In a letter dated May 2, 2023, however, Appellant informed SBA that its shares were not owned directly by the De La Torres but rather held by a trust. (CF, Exh. 26.) Board meeting minutes from March 2023 indicate that Appellant has two directors, Mr. and Mrs. De La Torre. (CF, Exh. 29.)

Appellant provided a copy of its Amended and Restated Bylaws, dated April 27, 2023. (CF, Exh. 28.) The Bylaws contain the following provisions pertinent to this appeal:

Article II

Directors — Management

...

Section 2. Number and Qualification of Directors

Subject to the Articles of Incorporation, the authorized Number of Directors shall be **two (2)** until changed by a duly adopted amendment to the Articles of Incorporation if the number is fixed in the Articles of Incorporation or otherwise by an amendment to this Bylaw adopted by the vote or written consent of holders of a majority of the outstanding shares entitled to vote. Each Director shall be a natural person of full age. A Director need not be a Shareholder unless so required by the Articles of Incorporation. No reduction of the authorized number of Directors shall have the effect of removing any Director before the Director's term of office expires.

...

Section 5. Removal of Directors

Except as otherwise provided in the Articles of Incorporation or [[California state law], the entire Board of Directors or any individual Director may be removed from office within, with or without cause by the holders of shares then entitled to vote for the election of Directors; provided, however, that if a Director is elected by a voting group, only Shareholders of the group may vote to remove and if less than the entire Board is removed. A Director may not be removed if the number of votes sufficient to elect under cumulat[iv]e voting votes against the removal unless the entire Board is removed.

...

Article III

Meetings of Directors

...

Section 8. Quorum for Meetings of Directors

A majority of the total number of Directors shall be necessary to constitute a quorum for the transaction of business. Unless the Articles of Incorporation or Bylaws require a greater number, the action of a majority of the Directors present at any meeting at which there is a quorum, when duly assembled, is valid as a corporate act; provided that a minority of the Directors, in the absence of a quorum, may adjourn from time-to-time, but may not transact any business. A meeting at which a quorum is initially present may continue to transact business, notwithstanding the withdrawal of Directors, if any action taken is approved by a majority of the required quorum for such meeting. Notwithstanding anything to the contrary, ROBERT R. DE LA TOREE's attendance shall always be required to constitute a quorum for the transaction of business.

(*Id.* at 2, 6.) The Bylaws are signed by Mr. and Mrs. De La Torre. (*Id.* at 20.)

Appellant provided a copy of an “Amended and Restated Declaration of Trust” for the De La Torre Family Revocable Trust, dated February 2, 2022. (CF, Exh. 30.) The Trust document indicates that Mr. and Mrs. De La Torre are Co-Trustees. (*Id.* at 1, 4.) The Trust document further stipulates that “[t]he term ‘Trustee’ as used in this Declaration shall refer collectively to [Mr. and Mrs. De La Torre] so long as they shall serve as such Co-Trustees. . . .” (*Id.* at 5.) Section 1.02(a) of the Trust document states that “‘Trust estate’ refers to the assets presently held in the De La Torre Family Revocable Trust of November 4, 2015, together with any other assets that may hereafter be transferred or conveyed to and received by the Trustee.” (*Id.* at 2.) No other information within the Trust document, or provided by Appellant, explains what is considered trust property. Section 7.02 describes what a Trustee may do with trust property including “sell, convey, exchange, convert, improve, repair, manage, operate, and control trust property” as well as “vote and give proxies to vote any securities held by Trustee in trust pursuant to this Declaration. . . .” (*Id.* at 19-20.) Section 7.08 indicates that business interests may be part of the trust property and that a “Trustee may continue to hold interests in such closely held business entities as a part of the trust estate, and shall have all necessary powers to act in directing, controlling and managing such entities.” (*Id.* at 24.)

B. Denial

On May 4, 2023, SBA, acting through the Director of the Office of Government Contracting (D/GC), denied Appellant's application for certification as an SDVOSB. (CF, Exh. 23.) The D/GC found that Appellant did not demonstrate that one or more service-disabled veterans fully control Appellant's Board, as is required under 13 C.F.R. § 128.203(e). (*Id.* at 1.) The D/GC also found that Appellant failed to demonstrate that one or more service-disabled veterans directly own at least 51% of Appellant, as is required under 13 C.F.R. § 128.202(a). (*Id.*)

The D/GC observed that, according to meeting minutes, Appellant has two directors: Mr. De La Torre (a service-disabled veteran) and Mrs. De La Torre (a non-veteran). (*Id.* at 2.) Appellant's Bylaws require that “a majority” of directors is needed to establish a quorum. (*Id.*) The Bylaws further provide that at a meeting at which a quorum is present, an agreement

amongst a majority of directors is an act of Appellant. (*Id.*) Although the Bylaws state that the service-disabled veteran's presence is required to constitute a quorum, the non-veteran's presence is also required. (*Id.*) The D/GC concluded that Mrs. De La Torre, a non-veteran, could exert negative control over Appellant. (*Id.*)

Appellant's stock ledger indicates that Mr. De La Torre owns 510 shares of Appellant and Mrs. De La Torre owns the other 490 shares. (*Id.*) However, Appellant informed SBA that these shares were held by a trust. (*Id.*) A review of the Trust document provided by Appellant did not explain what property was held by the Trust. (*Id.*) Due to this conflicting information, the D/GC could not verify that at least 51% of Appellant is directly owned by one or more service-disabled veterans. (*Id.*) If the Trust is the owner of Appellant, Appellant would not meet the direct ownership requirement of § 128.202(a), because both Mr. and Mrs. De La Torre are Trustees and jointly control the Trust. (*Id.*)

C. Appeal

On April 20, 2023, Appellant appealed the D/GC's decision to OHA. Appellant concedes that, under its Bylaws, the presence of Mrs. De La Torre, a non-veteran, is “required to meet a majority of the Directors for a quorum and to pass an act of the Board of Directors. . . .” (Appeal at 2.) Appellant asserts, however, that Mr. De La Torre, a service-disabled veteran, “is the majority Shareholder and therefore controls whom acts as a Director of the Corporation.” (*Id.* at 1.) Furthermore, because Mr. De La Torre's attendance is also required to constitute a quorum, Appellant argues that this satisfactorily prevents Mrs. De La Torre from exerting negative control. (*Id.* at 2.)

Appellant further maintains that Mr. De La Torre directly owns 51% of Appellant. (*Id.*) Although Mr. De La Torre “transferred his 51% ownership into his revocable Trust,” the Trust document indicates that Mr. De La Torre “retains the full right and authority to transfer those shares and control those shares unilaterally.” (*Id.*) Since the Trust does not fundamentally alter Mr. De La Torre's ownership status, Appellant contends that he directly owns 51% of Appellant. (*Id.*)

III. Discussion

A. Standard of Review

When a concern seeks certification as a VOSB or SDVOSB, SBA regulations provide that:

An Applicant's eligibility will be based on the totality of circumstances, including facts set forth in the application, supporting documentation, any information received in response to any SBA request for clarification, any independent research conducted by SBA, and any changed circumstances. The Applicant bears the burden of proof to demonstrate its eligibility as a VOSB or SDVOSB.

13 C.F.R. § 128.302(d). Furthermore, “[i]f a concern submits inconsistent information that results in SBA's inability to determine the concern's compliance with any of the VOSB or SDVOSB eligibility requirements, SBA will decline the concern's application.” *Id.* § 128.302(d)(1).

On appeal to OHA, Appellant has the burden of proving, by a preponderance of the evidence, that the denial decision was based upon clear error of fact or law. *Id.* § 134.1111.

B. Analysis

I find no merit to this appeal. As he explained in his decision, the D/GC denied Appellant's application for certification for two principal reasons. First, the D/GC found that a non-veteran, Mrs. De La Torre, has the power to exert negative control over Appellant. Section II.B, *supra*. In particular, Mrs. De La Torre is one of only two directors of Appellant, and Appellant's Bylaws stipulate that “a majority” of the Board is needed in order to establish a quorum and make decisions. Sections II.A and II.B, *supra*. Second, the D/GC found that Appellant also is not at least 51% directly owned by one or more service-disabled veterans. Section II.B, *supra*. Although Appellant provided a stock ledger indicating that Mr. De La Torre was issued 51% of Appellant's stock, Appellant also informed SBA that its shares were not owned directly by the De La Torres but rather held by the Trust. Sections II.A and II.B, *supra*.

Beginning with the question of ownership, SBA regulations require that an SDVOSB must be at least 51% directly and unconditionally owned by one or more service-disabled veterans. 13 C.F.R. § 128.202(a). Ownership through a trust may be sufficient to meet this requirement, if “the trust is revocable, and qualifying veterans are the grantors, trustees, and the current beneficiaries of the trust.” *Id.* Here, the Trust document provided by Appellant repeatedly states that Mr. and Mrs. De La Torre are Co-Trustees. Section II.A, *supra*. Accordingly, the instant Trust does not fully meet the requirements of § 128.202(a), as one of the two Co-Trustees is not a service-disabled veteran. Additionally, although Appellant contends on appeal that Mr. De La Torre still retains the ability to unilaterally control his shares transferred to the Trust, Appellant points to no provisions in the actual Trust document to support this claim. Section II.C, *supra*. In fact, the Trust document appears to give equal rights over Trust property to both Mr. and Mrs. De La Torre. Section II.A, *supra*. Given the record before him, then, the D/GC could reasonably conclude that Appellant did not establish that one or more service-disabled veterans directly owns at least 51% of Appellant; as a result, denial of Appellant's application was proper. SBA regulations are clear that “[i]f a concern submits inconsistent information that results in SBA's inability to determine the concern's compliance with any of the VOSB or SDVOSB eligibility requirements, SBA will decline the concern's application.” 13 C.F.R. § 128.302(d)(1); *see also VSBC Appeal of Wigs Plus, L.L.C.*, SBA No. VSBC-278-A (2023) (D/GC appropriately denied application for certification when applicant submitted contradictory information on material issues).

With regard to the issue of negative control, the D/GC determined — and Appellant does not dispute — that Appellant's Bylaws require the presence of Mrs. De La Torre, who is not a service-disabled veteran, in order to establish a Board quorum and to make decisions. Sections

II.B and II.C, *supra*. The D/GC thus correctly concluded that a non-service-disabled veteran has the power to exert negative control over Appellant. *See* 13 C.F.R. § 128.102 (negative control “includes, but is not limited to, instances where a non-qualifying-veteran has the ability, under the concern's governing documents (*e.g.*, charter, by-laws, operating agreement, or shareholder's agreement), to prevent a quorum or otherwise block action by the board of directors or qualifying veteran owner(s).”). On appeal, Appellant suggests that any negative control exerted by Mrs. De La Torre would be illusory, because Mr. De La Torre, as Appellant's majority shareholder, could remove her from the Board. Section II.C, *supra*. This argument fails for two reasons. First, as discussed above, it is unclear whether Mr. De La Torre is in fact Appellant's majority shareholder as Appellant appears to be owned through a Trust. Second, even assuming Mr. De La Torre is Appellant's 51% shareholder, this may not be a sufficiently large ownership interest for him to unilaterally remove Mrs. De La Torre from the Board. Although Appellant's Bylaws provide for a removal of a Director, those Bylaws further state that “[a] Director may not be removed if the number of votes sufficient to elect under cumulat[iv]e voting votes against the removal unless the entire Board is removed.” Section II.A, *supra*. Given that Appellant's Bylaws provide for cumulative voting, Appellant has not demonstrated that a 51% ownership interest is sufficient to remove one of two Directors on a two-member Board.

IV. Conclusion

Appellant has not established that the D/GC committed any error of fact or law in denying Appellant's application for certification. The appeal therefore is DENIED. This is the final agency action of the U.S. Small Business Administration. 15 U.S.C. § 657f(f)(6)(A); 13 C.F.R. § 134.1112(d).

KENNETH M. HYDE
Administrative Judge