

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

VSBC Appeal of:

Iron Shamrock, LLC,

Appellant

SBA No. VSBC-311-A

Decided: October 18, 2023

APPEARANCE

John Courtney Quinlan, Owner, Iron Shamrock, LLC, Pittsburg, Pennsylvania

DECISION¹

I. Introduction and Jurisdiction

On August 28, 2023, Iron Shamrock, LLC (Appellant) appealed a decision of the U.S. Small Business Administration (SBA), denying Appellant's application for certification as a Veteran-Owned Small Business (VOSB). SBA found that Appellant could not be certified due to issues with control of Appellant by a Veteran. On appeal, Appellant maintains the denial decision was erroneous, and requests that SBA's Office of Hearings and Appeals (OHA) reverse the denial. For the reasons discussed *infra*, the appeal is denied.

OHA adjudicates VOSB 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 August 16, 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 limited liability company (LLC), established in the state of Pennsylvania on July 18, 2017. (Case File (CF), Exhs. 44, 45.) John Courtney Quinlan, a certified veteran, holds 100% ownership of Appellant. (CF, Exhs. 49, 50, 66.)

¹ This decision was originally issued under a protective order. Pursuant to 13 C.F.R. § 134.205, OHA afforded counsel an opportunity to file a request for redactions if desired. OHA received no requests for redactions. Therefore, I now issue the entire decision for public release.

Within its application, Appellant acknowledged that it holds a franchise agreement. (CF, Exh. 47.) Appellant provided an unsigned Franchise Agreement listing Charles Schwab & Co., Inc. (Charles Schwab) as the Franchisor. The Franchise Agreement includes the following pertinent provisions:

Item 1. THE FRANCHISOR AND ANY PARENTS, PREDECESSORS AND AFFILIATES

The distinctive features of our franchise program include the following:

Supervision

· As our registered representative, investment adviser representative, and insurance representative, we will supervise your brokerage, investment advisory, and insurance activities as required by FINRA rules, SEC regulations, applicable state law, and the policies and procedures in the Confidential Manuals. The Confidential Manuals impose restrictions on your outside business activities.

[. . .]

Net Payout

· We calculate a Net Payout for you each month. The steps below explain the Revenue Rates that we apply to transactions and holdings of Schwab Products & Services and how we calculate the monthly Net Payout.

[. . .]

Types of Independent Branch Clients

[. . .]

(5) “Reassigned Advisor Clients”

In the Franchise Agreement, you agree that all of your Independent Branch Clients are deemed to be our clients and the client relationship is an asset of ours and not yours, regardless of your role in originating the client relationship. Except as stated in the Franchise Agreement, you have no other special rights or entitlements to Independent Branch Clients or other Schwab Clients.

Schwab Products & Services

· You will have the right to offer all of the Schwab Products & Services that we identify in the Confidential Manuals. “Schwab Products & Services” refers to the specific products and services that we make available and authorize during the term of the Franchise Agreement[.]

Item 8. RESTRICTIONS ON SOURCES OF PRODUCTS AND SERVICES

1. **General.** In operating the Independent Branch, you must adhere to the comprehensive standards and specifications comprising the Schwab System, including: (i) client service standards; (ii) privacy policies; (iii) appearance, design and trade dress standards for the Independent Branch; (iv) use of the Schwab Marks; and (v) minimum operating hours. By setting minimum service requirements and uniform standards, we strengthen customer confidence in the Charles Schwab® brand. We explain these specifications in the Confidential Manuals. We may revise our specifications in our discretion as frequently as we believe is necessary through written or electronic bulletins or supplements to the Confidential Manual or through communications sent or available to you on our Intranet. You must conform to all changes in our specifications at your cost within the time we allow.

2. **Schwab Products & Services.** You do not purchase Schwab Products & Services from us and resell them to Independent Branch Clients. All Independent Branch Clients are Schwab Clients. All Independent Branch Clients must maintain their accounts at Schwab and buy and sell securities and investment products through Schwab.

You will provide Non-Discretionary Investment Advice to help Independent Branch Clients with their investment decisions and process certain paperwork to complete brokerage transactions and assist Independent Branch Clients buy, hold and sell Schwab Products & Services. Schwab is the custodian of the assets held in the accounts of Independent Branch Clients and is the clearing firm for all brokerage transactions.

You must conduct all business with Independent Branch Clients through us and that business must be limited to handling brokerage transactions for Schwab Products & Services. We prohibit you from offering or selling any other securities, investments or other types of products or services. We may modify the list of approved Schwab Products & Services and the prices that we charge Schwab Clients at any time in our sole discretion and will notify you of changes through updates to the Confidential Manuals. These changes will take effect immediately unless we specify a different implementation date.

[. . .]

Item 15. OBLIGATIONS TO PARTICIPATE IN THE ACTUAL OPERATION OF THE BUSINESS

As the broker/dealer and investment adviser firm, we must supervise all securities regulatory activities at your Independent Branch. The supervision we undertake enables us to carry out our own regulatory duties to monitor your trading activities,

written and electronic communications with clients or regarding client matters, and similar interactions with clients and the public within the purview of FINRA rules and federal and state laws. This supervision also involves making unannounced site visits to your Independent Branch, contacting clients, and reviewing Independent Branch Client account records.

[. . .]

You may not hire independent contractors to work in your Independent Branch, service clients of the Independent Branch, or perform any other activities that require access to client information. We limit your employees' access to client information to conform to privacy and information security requirements.

[. . .]

Item 16. RESTRICTIONS ON WHAT YOU MAY SELL

Independent Branch Clients hold their accounts with, and purchase Schwab Products & Services from, us, not you. You may only offer Schwab Products & Services at the prices which we set. We prohibit you from offering or selling any other securities, investments, or other types of products or services.

[. . .]

NOW, THEREFORE, the parties agree as follows:

[. . .]

XIII. OPERATIONAL SUPPORT [. . .]

C. Compliance and Supervision

3. Schwab will perform all bookkeeping, processing, and related functions that are necessary or advisable in Schwab's judgment in order to complete trading operations for Independent Branch Clients including, without limitation, back-office, accounting and collection support, and acting as a custodian of Independent Branch Client funds.

(CF, Exh. 47.)

On August 1, 2023, the SBA's Director of the Veteran Small Business Certification Program (D/VSBCP), wrote Appellant and identified “numerous provisions that exceed the scope of non-Veteran control allowable.” (CF, Exh. 56.) D/VSBCP determined it could not conclude a veteran controlled Appellant and requested an “Amended and Restated Franchise Agreement addressing the issues identified.” (*Id.*) Specifically, D/VSBCP identified eight provisions in the Franchise Agreement considered restrictive: (1) common management; (2) lack

of financial separation between the Franchisor and the Franchisee; (3) Franchisor controls the core of the Franchisee's underlying business; (4) restrictions on the ability to subcontract; (5) Franchisor controls billing; (6) Franchisor owns customer accounts; (7) limitation of products and services; and (8) Franchisor controls accounts receivables and may extract deductions Net Payout. (*Id.*)

On August 12, 2023, Appellant submitted a response and asserted the Franchisor is a “highly regulated financial services” bank and as a result, “federal regulations impact[] how the franchise can operate.” (CF, Exhs. 41, 42.) Appellant asserted “[b]ecause of the highly regulated industry the franchise owner is operating in, the track record of [Franchisor] of putting the client first, and the controls the franchise owner has over operating their for-profit business, we are an excellent candidate for VA Certification.” (*Id.*)

B. Denial

On August 16, 2023, D/VSBCP denied Appellant's application for certification as an VOSB. (CF, Exh. 38.) D/VSBCP found that Appellant did not demonstrate that a Veteran holds “ultimate authority to establish and lead both the long-term decision-making and day-to-day operations of the business,” as required under 13 C.F.R. § 128.203(a). (*Id.*, at 1.)

D/VSBCP observed that Appellant is a Franchise that holds a Franchise Agreement with Franchisor, Charles Schwab. D/VSBCP inquired about control issues, and Appellant responded by stating, “the franchise ‘is in the highly regulated financial services (FINRA, SEC, NASD) and banking industry (Federal Banking regulations) as a publicly traded company . . . [and] [t]hese required federal regulations impacts [sic] how the franchise can operate.’” (*Id.*) D/VSBCP determined Appellant's response did not “cure the numerous provisions within the Franchise Agreement that limit the Veteran's control of decision-making or create scenarios where non-Veterans can control.” (*Id.*)

D/VSBCP continued by providing examples from the Franchise Agreement that demonstrate the Franchisor's control over Appellant. Specifically, D/VSBCP found issues in the Franchise Agreement with the following:

(1) Common Management; (2) Lack of financial separation between the Franchisor and the Franchisee; (3) The Franchisor controls the core of the Franchisee's underlying business including its crucial functions and ultimate product; (4) There are restrictions on who the franchisee can subcontract with; (5) The Franchisor controls billing; (6) The Franchisor owns customer accounts; (7) The limitation of products and services; and (8) The Franchisor controls accounts receivables and may extract deductions.

(*Id.*) D/VSBCP concluded that it cannot determine a Veteran holds authority over Appellant's long-term decision-making and day-to-day operations, as required under 13 CFR §§ 128.203(d); 128.203(h)(1).

C. Appeal

On August 28, 2023, Appellant appealed the D/VSBCP's decision to OHA. Appellant asserts the SBA informed Appellant that franchises are considered for certification under the program, “[w]hich is the reason the SBA requested and reviewed [Appellant's] Franchise Disclosure Document.” (Appeal at 1.) Appellant further rejects D/VSBCP's determination and asserts John Courtney Quinlan, the veteran, holds “total control of day-to-day operations which includes and is not limited to business hours, hiring and managing employees, marketing activities, and how to decide to engage clients and prospects.” (*Id.*)

Next, Appellant provides definitions of a franchise and asserts the franchisor and franchisee “work together” when submitting bids, “which is part of the joint agreement.” (*Id.*) Appellant asserts “[t]here isn't an instance where a franchisee has unfettered control of how their franchise can operate.” (*Id.*) According to Appellant, 13 C.F.R. § 128.203(a) should not be applicable if SBA were to consider franchises for VA certification. Also, 13 C.F.R. § 128.203(a) is “unduly restrictive for Veteran franchise owner's and should not be the deciding criteria” for certification. (*Id.*)

III. Discussion

A. Standard of Review

Under SBA regulations, an applicant seeking verification as a VOSB or SDVOSB “bears the burden of proof to demonstrate its eligibility.” 13 C.F.R. § 128.302(d). Eligibility is 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.” *Id.* 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.” 13 C.F.R. § 128.302(d)(1). In the event of a subsequent 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. 13 C.F.R. § 134.1111.

B. Analysis

Appellant has not met its burden that D/VSBCP's denial of Appellant's application for verified VOSB status is based upon clear error. I must therefore deny this appeal.

SBA regulations required that an eligible VOSB must be no less than 51% owned and controlled by a veteran(s). 13 C.F.R. § 128.200(a)(2). Control means a veteran oversees the “management and daily operations” of a concern. 13 C.F.R. § 128.203(a). OHA precedent has determined management and daily operations to include “marketing, production, sales, and administrative functions of the firm, as well as the supervision of the executive team, and the implementation of policies.” 13 C.F.R. § 128.102; *In the Matter of Partners in Energy, LLC*, SBA No. CVE-253 (2023); *CVE Appeal of The Hope Cos, LLC*, SBA No. CVE-204 (2021). Non-qualifying veterans must not exercise power over the concern and must not “have business

relationships that cause such dependence that the qualifying veteran cannot exercise independent business judgment without great economic risk.” 13 C.F.R. § 128.203(h)(1)(2).

Here, the D/VSBCP determined the provisions of the Franchise Agreement with Franchisor Charles Schwab interfere with Mr. Quinlan's ability to control the concern. Section II.B, *supra*. A review of these provisions confirms the D/VSBCP's determination that a non-veteran Franchisor exercises control over Appellant through control of its daily management and business operations. Section II.A, *supra*. For instance, Item 15 provides “[Franchisor] must supervise all securities regulatory activities at [Appellant's] Independent Branch” and “[Appellant] may not hire independent contractors to work in [Appellant's] Independent Branch.” Item 8.1. provides that Appellant must “adhere to the comprehensive standards and specifications comprising the [Franchisor] System” including client service standards, dress and appearance standards, privacy standards, use of Schwab marks and minimum operating hours. Item XIII.5.C.3 provides “[Franchisor] will perform all bookkeeping, processing, and related functions that are necessary or advisable in [Franchisor's] judgment.” *Id.*

Additionally, provisions in the Franchise Agreement confirm D/VSBCP's determination that Appellant cannot exercise independent business judgment. *Id.* For instance, Item 1.5 provides “all of [Appellant's] Independent Branch Clients are deemed to be [Franchisor's] clients and the client relationship is an asset of [Franchisor's] and not [Appellant's]”; Item 16 provides “[Appellant] may only offer [Franchisor] products and services at the prices which [Franchisor] set . . . [Franchisor] prohibits [Appellant] from offering or selling any other securities, investments, or other types of products or services”; and Item 8.2 provides “[Franchisor] may modify the list of approved Schwab Products & Services and the prices that [Franchisor] charge Schwab Clients at any time in [Franchisor] sole discretion and will notify [Appellant] of changes through updates to the Confidential Manuals.” *Id.* These provisions fundamentally restrict Mr. Quinlan's ability to independently operate Appellant and independently exercise business judgment. Thus, I find D/VSBCP reasonably determined “it cannot be concluded that a Veteran has final, ultimate authority to establish and lead both the long- term decision-making and day-to-day operations of the business, as required by the regulations.” Section II.B, *supra*.

On appeal, Appellant asserts that 13 C.F.R. § 128.203(a) is “unduly restrictive” and should not apply to Veteran franchise owners. Section II.C, *supra*. OHA has addressed this issue in *In the Matter of Partners in Energy, LLC*, SBA No. CVE-253 (2023). As OHA observed in *Partners in Energy*, SBA addressed the issue of affiliation based on franchise and license agreements in 13 C.F.R. § 121.301(f)(5)² in the context of size standards and affiliation

² On April 10, 2023, SBA issued a Final Rule removing 13 C.F.R. § 121.301(f)(5) from the regulation. SBA determined “[b]ecause SBA is removing the principle of control of one entity over another from its affiliation consideration, this paragraph is no longer needed.” 88 Fed. Reg. 21,074, 21,080 (April 10, 2023). In the context of lending, SBA removed the principles of control from affiliation considerations but did not remove them from the affiliation requirements in size standard regulations generally nor made any changes to VSBC regulation requirements that a veteran control the concern. While the principle of control of one organization over another is no longer considered in the context of SBA's loan programs, the principle that the

principles applicable to financial assistance programs; and consequently, SBA “limited the firms covered by this regulation to those applying for financial assistance.” *Partners in Energy, LLC*, SBA No. CVE-253 at 9. As a result, OHA determined “SBA has, by not extending the coverage of § 121.301(f)(5) to the Veteran Small Business Certification program, made it extremely difficult for any franchise business to qualify as a VOSB or an SDVO SBC.” *Id.* Thus, considering the plain meaning of 13 C.F.R. § 128.203(a), a VOSB must control the “management and daily business operations” of the concern. *Id.* Given the restrictions in the Franchise Agreement here and SBA regulation, I find the D/VSBCP reasonably determined Mr. Quinlan lacked control over Appellant due to the restrictions imposed by Franchisor Charles Schwab in the Franchise Agreement.

Based on the foregoing, the Franchise Agreement restricts Mr. Quinlan's control over Appellant's business operations and restricts Appellant from exercising independent business judgment. I thus find that D/VSBCP did not err in law or fact when he determined Appellant failed to meet the control requirements of 13 C.F.R. § 128.203(a).

IV. Conclusion

Appellant has not established that the D/VSBCP 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).

CHRISTOPHER HOLLEMAN
Administrative Judge

service-disabled veteran must control an SDVOSB remains a bedrock of the Veteran Small Business Certification Program.