**1230.1604 OWNERSHIP.**

Subpart 1. **Determination of ownership.** In determining whether the qualifying participants in a business own the business, all the facts in the record will be viewed as a whole, including the origin of all assets and how and when they were used in obtaining the business. All transactions for the establishment and ownership, or transfer of ownership, must be in the normal course of business, reflecting commercial and arms-length practices.

Subp. 2. **Eligibility.**

A. To be an eligible socially and economically disadvantaged or veteran-owned small business, a business must be at least 51 percent owned by socially and economically disadvantaged individuals or veterans, respectively.

(1) In the case of a corporation, socially and economically disadvantaged individuals or veterans, respectively, must own at least 51 percent of each class of voting stock outstanding and 51 percent of the aggregate of all stock outstanding.

(2) In the case of a partnership, 51 percent of each class of partnership interest must be owned by socially and economically disadvantaged individuals or veterans, respectively. The ownership must be reflected in the business partnership agreement.

(3) In the case of a limited liability company, at least 51 percent of each class of member interest must be owned by socially and economically disadvantaged individuals or veterans, respectively.

B. To be an eligible economically disadvantaged area business, if the business is not located in an economically disadvantaged area, the business must be at least 51 percent owned by individuals who reside in an economically disadvantaged area.

Subp. 3. **Proof of contribution.**

A. The business's ownership by qualifying individuals, including their contribution of capital or expertise to acquire their ownership interests, must be real, substantial, and continuing, going beyond pro forma ownership of the business as reflected in ownership documents. Proof of contribution of capital should be submitted at the time of the application. When the contribution of capital is through a loan, there must be documentation of the value of assets used as collateral for the loan.

B. Insufficient contributions include a promise to contribute capital, an unsecured note payable to the business or an owner who is not a qualifying individual, mere participation in a business's activities as an employee, or capitalization not commensurate with the value of the business.

C. The qualifying owners must enjoy the customary incidents of ownership, and share in the risks and be entitled to the profits and loss commensurate with their ownership interests, as demonstrated by the substance, not merely the form, of arrangements. Any terms or practices that give a nonqualifying individual or business a priority or superior right to a business's profits, compared to the qualifying owner or owners, are grounds for denial.

D. Debt instruments from financial institutions or other organizations that lend funds in the normal course of business do not render a business ineligible, even if the debtor's ownership interest is security for the loan. For example:

(1) if an individual pays $100 to acquire a majority interest in a business worth $1,000,000, the individual's contribution to capital would not be viewed as substantial;

(2) if a 51 percent qualifying owner and a nonqualifying 49 percent owner contribute $100 and $10,000, respectively, to acquire a business grossing $1,000,000, this may be indicative of a pro forma arrangement that does not meet the requirements of item A; and

(3) if a qualifying owner of an applicant business spends $250 to file articles of incorporation and obtains a $100,000 loan, but makes only nominal or sporadic payments to repay the loan, this type of contribution is not of a continuing nature.

Subp. 4. **Securities and assets.** All securities that constitute ownership of a business shall be held directly by a qualifying owner. Except as provided in this subpart, no securities or assets held in trust, or by any guardian for a minor, are considered as held by a qualifying individual in determining the ownership of a business. However, securities or assets held in trust are regarded as held by a qualifying individual for purposes of determining ownership of the business if:

A. the beneficial owner of securities or assets held in trust is a qualifying individual, and the trustee is the same or another such individual; or

B. the beneficial owner of a trust is a qualifying individual who, rather than the trustee, exercises effective control over management and policy making or daily operational activities of the business. Assets held in a revocable living trust may be counted only in the situation where the same qualifying individual is the sole grantor, beneficiary, and trustee.

Subp. 5. **Contributions.** The contributions of capital or expertise by the qualifying individuals to acquire ownership interests must be real and substantial. Examples of insufficient contributions include a promise to contribute capital, an unsecured note payable to the business or an owner who is not a qualifying individual, or mere participation in a business's activities as an employee. Debt instruments from financial institutions or other organizations that lend funds in the normal course of business do not render a business ineligible, even if the debtor's ownership interest is security for the loan.

Subp. 6. **Contribution requirements.** The following requirements apply to situations in which expertise is relied on as part of a qualifying individual's contribution to acquire ownership.

A. The owner's expertise must be:

(1) in a specialized field;

(2) of outstanding quality;

(3) in areas critical to the business's operations;

(4) indispensable to the business's potential success;

(5) specific to the type of work the business performs; and

(6) documented in the records of the business. These records must clearly show the contribution of the owner's expertise and its value to the business.

B. The individual whose expertise is relied upon must have a significant financial investment in the business.

Subp. 7. **Business interests or other assets.** For purposes of determining ownership, all interests in a business or other assets obtained by the individual under the following circumstances will be deemed as held by a qualifying individual:

A. as the result of a final property settlement or court order in a divorce or legal separation, provided that no term or condition of the agreement or divorce decree is inconsistent with this part; or

B. through inheritance, or otherwise upon the death of the former owner.

Subp. 8. **Gift or transfer interest.**

A. For purposes of determining ownership, all interests in a business or other assets obtained by the individual as the result of a gift, or transfer without adequate consideration, are not held by a qualifying individual if they were obtained from any nonqualifying individual or nonqualifying business that is:

(1) involved in the same business for which the individual is seeking certification, or an affiliate of that business; or

(2) engaged in an ongoing business relationship with the business, or an affiliate of the business, for which the individual is seeking certification.

B. To overcome this determination and permit the interests or assets to be counted, the qualifying individual must demonstrate, by clear and convincing evidence, that:

(1) the gift or transfer to the qualifying individual was made for reasons other than obtaining certification; and

(2) the qualifying individual actually controls the management, policy, and operations of the business, notwithstanding the continuing participation of a nonqualifying individual who provided the gift or transfer.

Subp. 9. **Marital assets.** The division must apply the following rules in situations in which marital assets form a basis for ownership of a business.

A. When marital assets, other than the assets of the business in question, held jointly or as community property by both spouses, are used to acquire the ownership interest asserted by one spouse, the ownership interest in the business is deemed to have been acquired by that spouse with the spouse's own individual resources, provided that the other spouse irrevocably renounces and transfers all rights in the ownership interest in the manner sanctioned by the laws of the state in which either spouse or the business is domiciled. A greater portion of joint or community property assets will not be counted toward ownership than state law would recognize as belonging to the qualifying owner or the applicant business.

B. A copy of the document legally transferring and renouncing the other spouse's rights in the jointly owned business or community assets used to acquire an ownership interest in the business must be included as part of the business's application for certification.

Subp. 10. **Factors used to determine ownership.** The following factors shall be considered in determining the ownership of a business. A contribution of capital is not regarded as failing to be real and substantial, and a business shall not be found ineligible, solely because:

A. a qualifying individual acquired the individual's ownership interest as the result of a gift, or transfer without adequate consideration, other than the types specified in subpart 8;

B. there is a provision for the cosignature of a nonqualifying spouse on financing agreements, contracts for the purchase or sale of real personal property, bank signature cards, or other documents; or

C. ownership of the business in question or its assets is transferred for adequate consideration from a nonqualifying spouse to a qualifying spouse. In this case, particularly close and careful scrutiny shall be given to the ownership and control of a business to ensure that it is owned and controlled, in substance as well as in form, by a qualifying individual.

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