

Trusts

Issue: How can a firm be eligible if the Veteran owner establishes a Trust?

The Regulations

38 CFR § 74.3

- An applicant or participant must be at least 51 percent unconditionally and directly owned by one or more veterans or service-disabled veterans.
- (a) Ownership must be direct. Ownership by one or more Veterans or service-disabled Veterans must be direct ownership. An applicant or participant owned principally by another business entity or by a trust (including employee stock ownership plans [ESOP]) that is in turn owned by one or more veterans or service-disabled veterans does not meet this requirement. However, ownership by a trust, such as a living trust, may be treated as the functional equivalent of ownership by a veteran or service-disabled veteran where the trust is revocable, and the veteran or service-disabled veteran is the grantor, a trustee, and the sole current beneficiary of the trust. For employee stock ownership plans where 5 or fewer persons who are individuals, estates, or trusts own 50 percent or more of the total combined voting power of the corporation, the employee plan will be determined to be “excluded stock” and eligible parties must control 51 percent or more of the combined voting power of the corporation. For employee stock ownership plans where greater than 5 persons who are individuals, estates, or trusts own 50 percent or more of the total stock, eligible parties must control 51 percent or more of the combined voting power of the corporation, including the ESOP stock.
- (b) Ownership must be unconditional. Ownership by one or more veterans or service-disabled veterans must be unconditional ownership. Ownership must not be subject to conditions precedent, conditions subsequent, executory agreements, voting trusts, restrictions on assignments of voting rights, or other arrangements causing or potentially causing ownership benefits to go to another (other than after death or incapacity). The pledge or encumbrance of stock or other ownership interest as collateral, including seller-financed transactions, does not affect the unconditional nature of ownership if the terms follow normal commercial practices and the owner retains control absent violations of the terms. In particular, CVE will evaluate ownership according to the following criteria for specific types of small business concerns.

What This Means

- In order for a trust to satisfy the ownership requirements of 38 CFR § 74.3, the trust must meet certain legal requirements:
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 - The trust must be revocable.
 - The Veteran or service-disabled Veteran must be the grantor, a trustee, and the sole current beneficiary of the trust.
 - Documentation must be provided which makes it clear that all of these requirements have been met. The Trust Agreement must be provided, if ownership is based on a Trust.
- Because the trust must be revocable, the Veteran must be able to take back full control of the trust property at any time. While there can be more than one trustee, the Veteran must be a trustee and the sole current beneficiary. To be the sole current beneficiary, the Veteran must receive the full income or other distributions from the trust property.

- Having named beneficiaries who will receive benefits or distributions from the trust property only after the Veteran's death does not conflict with the regulation, as the firm would no longer be eligible.

Excerpts from Current Denial Letters

- "CVE is unable to conclude that you satisfy the ownership requirements of 38 CFR Part 74. You supplied the "First Amendment to the Declaration of Trust Establishing The XXX. Revocable Trust". You did not supply the original trust agreement. The amendment identifies you as the Grantor and Trustee, but the document does not identify you as the sole current beneficiary of the trust. 38 CFR § 74.3(a) does allow for ownership through a trust, but only when the trust is, "revocable, and the Veteran or service-disabled Veteran is the grantor, a trustee, and the sole current beneficiary of the trust." The supplied documentation indicates that your children shall be the beneficiaries, and without the original document, CVE is unable to conclude that you meet the requirement of direct ownership outlined in 38 CFR § 74.3(a)."
- "According to corporate documentation you own your percentage of the company through a trust. 38 CFR § 74.3(a) states that, "...a...trust, may be treated as the functional equivalent of ownership by a veteran or service-disabled veteran where the trust is revocable, and the veteran or service-disabled veteran is the grantor, a trustee, and the sole current beneficiary of the trust." You supplied a document entitled "First Restatement of the YYY Revocable Trust Agreement." This document shows that the trust is revocable, and that you are the grantor and the trustee. However, you are not the sole current beneficiary. The trust lists ZZZ and AAA as the beneficiaries of the trust. For these reasons CVE is unable to conclude that you meet the ownership requirements set forth in 38 CFR § 74.3."
- "You supplied an Operating Agreement for your company. Exhibit A of the Operating Agreement states that The VVV Irrevocable Trust owns 51% of the company. While 38 CFR § 74.3(a) does allow for ownership through a trust it requires that the trust be "...revocable, and the Veteran or service-disabled Veteran is the grantor, a trustee, and the sole current beneficiary of the trust." This trust is not revocable. Therefore CVE is unable to conclude that the trust meets the requirements, and that you own 51% of the company as is required by 38 CFR § 74.3."