

NEW YORK STATE
DEPARTMENT OF ECONOMIC DEVELOPMENT
633 THIRD AVENUE
NEW YORK, NY 10017

In the Matter

- of -

the Application of **Care Security Systems, Inc.**
for Certification as a Women-Owned Business Enterprise
Pursuant to Executive Law Article 15-A.

NYS DED File ID No. 61495

RECOMMENDED ORDER

- by -

A handwritten signature in cursive script that reads "Maria E. Villa". The signature is written in dark ink and is positioned above a horizontal line.

Maria E. Villa
Administrative Law Judge

March 13, 2019

SUMMARY

This report recommends that the determination of the Division of Minority and Women's Business Development ("Division") of the New York State Department of Economic Development to deny Care Security Systems, Inc. ("Care Security" or "applicant") certification as a women-owned business enterprise ("WBE") be affirmed, for the reasons set forth below.

PROCEEDINGS

This matter involves the appeal by applicant, pursuant to New York State Executive Law Article 15-A and Title 5 of the Official Compilation of Codes, Rules and Regulations of the State of New York ("NYCRR") Parts 140-144, challenging the determination of the Division that Care Security does not meet the eligibility criteria for certification as a WBE.

The Division denied Care Security's application for WBE certification (Exhibit 1) by letter dated July 21, 2017. Exhibit 2. As discussed below, the letter sets forth six grounds under Section 144.2 of 5 NYCRR for the denial, based upon applicant's failure to demonstrate that the women owner, Renee Schwab,¹ owns, operates and controls Care Security for certification purposes. By letter dated August 3, 2017, applicant appealed from the Division's determination to deny the application. Exhibit 3. The Division responded by letter dated November 23, 2018, providing information as to the appeal process, and notifying applicant of the hearing scheduled for December 18, 2018. Exhibit 4.

The hearing took place as scheduled on December 18, 2018. Applicant was represented by Horace Flowers, Esq., and Renee Schwab testified on behalf of applicant. Division staff was represented by Simon Wynn, Esq., and called Glenn Butler, a senior certification analyst for the Division, as a witness. The hearing was recorded, and this report cites to that recording as "Hearing Recording ('HR') at ____." The ALJ received the recording on March 1, 2019, and on that date the record closed.

Both applicant and Division staff offered exhibits, and those exhibits were marked and received into evidence. A chart of those exhibits is attached.

ELIGIBILITY CRITERIA

The eligibility criteria pertaining to certification as a women-owned business enterprise are established by regulation (see Section 144.2 of 5 NYCRR). For the purposes of determining whether an applicant should be granted or denied WBE status, the ownership, operation, and control of the business enterprise are assessed on the basis of information supplied through the application process. The Division reviews the enterprise as it existed at the time that the application was made, based on representations in the application itself, on information revealed in supplemental submissions, and if appropriate, on interviews conducted by Division analysts.

¹ The application refers to the woman owner as both "Renee Schwab" and "Dolsa Schwab." At the hearing, applicant clarified that Renee Schwab and Dolsa Schwab are the same person. HR at 01:04:50. This recommended order refers to "Renee Schwab."

STANDARD OF REVIEW

On this administrative appeal, applicant bears the burden of proving that the Division's denial of Care Security Systems, Inc.'s WBE certification is not supported by substantial evidence (see State Administrative Procedure Act § 306(1)). The substantial evidence standard "demands only that a given inference is reasonable and plausible, not necessarily the most probable," and applicant must demonstrate that the Division's conclusions and factual determinations are not supported by "such relevant proof as a reasonable mind may accept as adequate" (Matter of Ridge Rd. Fire Dist. v Schiano, 16 NY3d 494, 499 (2011) (internal quotation marks and citations omitted)).

POSITIONS OF THE PARTIES

Division

The Division argued that applicant failed to meet ownership, operational, and control requirements for certification as a woman-owned business, pursuant to Section 144.2 of 5 NYCRR. Specifically, the Division asserted that Ms. Schwab had not made a capital contribution proportionate to her equity interest in the business enterprise, as demonstrated by contributions of money, property, equipment or expertise. Exhibit 2; see Section 144.2(a)(1) of 5 NYCRR. In this regard, the Division cited the following "relevant facts" in the denial letter:

- On June 01, 2015 Mr. Abraham Schwab transferred one hundred (100) shares of common stock in Care Security Systems, Inc. ("CSSI") to Ms. Dolsa Schwab.
- On June 01, 2015 Mr. Nathan Schwab transferred two (2) shares of common stock in CSSI to Ms. Schwab.
- Following the aforementioned stock transfers, Ms. Schwab owned fifty-one percent (51%) of the outstanding common stock of CSSI and Mr. Nathan Schwab owned ninety-eight percent (98%) of the outstanding common stock of CSSI.²
- The application to certify CSSI as a WBE purports that Ms. Schwab contributed expertise to CSSI. The application did not assign a value to Ms. Schwab's purported contributions of expertise.

Exhibit 2, at 2. Furthermore, the Division maintained that Ms. Schwab did not share in the risks and profits of the business enterprise in proportion to her ownership interest, as required by Section 144.2(c)(2) of 5 NYCRR. The Division based its determination on the fact that "Mr. Nathan Schwab's combined wage compensation and distribution from CSSI during its 2016 tax year exceed Ms. Schwab's combined wage compensation and distributions from CSSI during the same period." Exhibit 2, at 3.

² At the hearing, Ms. Schwab pointed out that the denial letter incorrectly described the proportion of stock ownership. As stated in the application (Exhibit 1), Ms. Schwab owns 51% of Care Security, and Nathan Schwab owns 49%.

With respect to operation, the Division argued that Ms. Schwab did not make decisions pertaining to the operation of the business enterprise (see Section 144.2(b)(1) of 5 NYCRR). The Division cited to the following “relevant facts”:

- CSSI is primarily engaged in designing, installing, and managing commercial security systems.
- Ms. Schwab is primarily responsible for managing financial and human resources matters.
- Mr. Nathan Schwab is primarily responsible for managing significant operations of the business related to designing and installing commercial security systems.
- Mr. Abraham Schwab is primarily responsible for managing significant operations of the business related to sales and marketing.

Exhibit 2, at 3. The Division went on to assert that the woman owner of the business enterprise had not demonstrated adequate managerial experience or technical competence to operate Care Security (see Section 144.2(b)(1)(i)). Specifically, in its denial letter, the Division contended that:

- CSSI requires a business license to install and maintain security systems.
- Mr. Nathan Schwab is the qualifier for CSSI’s business license.

Id.

Finally, the Division maintained that applicant had not demonstrated that Ms. Schwab controlled CSSI within the meaning of the regulations. Specifically, the Division pointed out that corporate bylaws and other documents governing the business enterprise did not permit Ms. Schwab to make decisions without restrictions, as required by Section 144.2(b)(2). The Division reached this conclusion based upon the following facts:

- Pursuant to the June 01, 2015 meeting of the board of directors of CSSI, Ms. Schwab was appointed “Chief Executive Officer” of CSSI and Mr. Nathan Schwab was appointed President of CSSI.
- Section 5.2 of the By-Laws of Care Security Systems, Inc. (the “Bylaws”) provides that the president of CSSI “shall have general supervision of the affairs of the corporation . . .”
- The Bylaws do not provide for the office of “Chief Executive Officer.”
- Section 5.8 of the Bylaws provides that the board of directors of CSSI may create additional officer positions.
- The board of directors of CSSI has not vested any powers in the office of the “Chief Executive Officer.”

Exhibit 2, at 4. The Division also cited to Section 144.2(b)(3) of 5 NYCRR, which provides that an applicant must demonstrate control of negotiations through production of relevant documents. The Division pointed out that Ms. Schwab did not execute any of the contracts between CSSI and its clients that were provided as part of the application. Id.

Applicant

In the August 3, 2017 notice of appeal, Ms. Schwab disputed the Division's position regarding ownership, asserting that the Division "failed to inquire involving my historic contributions of labor without adequate compensation as the basis for my capital contribution and underlying basis for my ownership" in the business. Exhibit 3, at 2. In addition, Ms. Schwab stated that "to ensure continued liquidity, I as an owner decided to temporarily defer receiving a higher salary." Id.

With respect to operation, applicant stated that the majority of Care Security's revenue did not result from activities requiring a license. Exhibit 3, at 2. According to applicant, Ms. Schwab had been "a key person" in the business since 1997 and had been involved in all aspects of operating Care Security. Id. Applicant went on to state that as chief executive officer, Ms. Schwab, and not the president, exercises final authority "involving all major activities relating to the operation" of Care Security. Id. In that regard, applicant asserted that Ms. Schwab exercises "tie-breaking authority over all key activities," and that "all delegated authority to others" is subject to her approval. Id.

FINDINGS OF FACT

1. Care Security Systems, Inc. is located at 7 Hemion Road, Montebello, New York. Exhibit 1, at 1. The business was established in 1989, and designs, installs, and manages commercial security systems. Id. at 2-3.
2. Renee Schwab owns 51% of Care Security. Exhibit 1, at 3. Nathan Schwab owns 49%. Id. at 3; HR at 17:00. The application indicates that no monetary contribution was made (Exhibit 1, at 3), and states with respect to Ms. Schwab's contribution "17 years CFO before becoming CEO." Id.
3. The company's federal 2016 S Corporation Income Tax Return indicates that Care Security's officers were compensated as follows: Nathan Schwab: [REDACTED]; Abraham Schwab: [REDACTED]; and Ms. Schwab: [REDACTED]. Exhibit 18, Form 1125-E; HR at 01:17:05. The return states that Nathan Schwab's allocated share of income from the business was [REDACTED], and Ms. Schwab's share was [REDACTED]. Exhibit 18, Schedule K-1.
4. The licenses referenced in the application are held by Nathan Schwab. Exhibit 1, at 3.
5. Ms. Schwab did not sign the contracts submitted with the application. Exhibits 15, 16, and 17.

6. Ms. Schwab is the chief executive officer of Care Security. Exhibit 1, at 3; Exhibit 11. Nathan Schwab is the president of Care Security. *Id.* Care Security's corporate by-laws do not provide for the office of chief executive officer, and state that the president has general supervision of the affairs of the corporation. Exhibit 12.

DISCUSSION

Ownership

This report considers applicant's appeal from the Division's determination to deny certification to Care Security Systems, Inc. as a women-owned business enterprise³ pursuant to Executive Law Article 15-A. Section 144.2(a)(1) of 5 NYCRR requires that a woman owner's contributions to a business for which certification is sought must be "proportionate to their equity interest in the enterprise." Contributions may be in the form of money, property, equipment, or expertise.

The Division asserted that Ms. Schwab had not made a capital contribution proportionate to her 51% ownership interest. The application indicates that Ms. Schwab did not make a monetary contribution to the business, and states "17 years CFO before becoming CEO." Exhibit 1, at 3. According to applicant, the Division improperly overlooked Ms. Schwab's contributions of labor without adequate compensation.

At the hearing, Ms. Schwab explained that from 1997 to 2015, she volunteered her time and was involved in every aspect of the business. HR at 13:45. During those years, Care Security primarily installed alarm systems for residential customers. HR at 12:00. In 2015, Nathan Schwab began devoting more time to volunteer work, and his role in the business decreased, while Ms. Schwab began to increase Care Security's focus on "multi-site, enterprise-grade, high value campus environment" commercial customers. HR at 1:00. Ms. Schwab testified that when she became chief executive officer, Care Security's accountant arrived at a figure of \$ [REDACTED] to represent the value of her unpaid labor from 1997 to 2015. HR at 22:30; Exhibit 20. She went on to testify that, in lieu of paying that amount to her, the debt was converted to capital. HR at 25:45. In that regard, applicant offered a resolution of the directors (Exhibit 20), entitled "Cancellation of Corporate Loan and Addition to Stated Capital Account."

The Division noted that the application did not assign a value to the claimed expertise, and pointed out that the resolution (Exhibit 20) was not provided as part of the application. As a result, this document cannot be considered on appeal. Although Ms. Schwab testified credibly concerning her role in the business, and the valuation of her unpaid labor, this information was not before the Division. The Division's reliance upon the application as submitted was reasonable, and the Division's determination that Ms. Schwab did not make the requisite contribution was supported by substantial evidence.

³ The term "women-owned business enterprise" applies to an enterprise that meets the requisite criteria on the basis of the ownership and control of one woman or of multiple women (*see* Section 140.1(tt) of 5 NYCRR (defining a women-owned business enterprise as one that is, among other things, "at least 51 percent owned by one or more United States citizens or permanent resident aliens who are women"))).

In addition, with respect to ownership, Section 144.2(c)(2) of 5 NYCRR requires that the woman owner share in the risks and profits of the business enterprise in proportion to her ownership interest. The Division took the position that Ms. Schwab's compensation was not commensurate with her 51% ownership of Care Security.

Care Security's federal 2016 S Corporation Income Tax Return indicates that the officers were compensated as follows: Nathan Schwab: [REDACTED]; Abraham Schwab: [REDACTED]; and Dolsa R. Schwab: [REDACTED]. Exhibit 18, Form 1125-E; HR at 01:17:05. At the hearing, Ms. Schwab pointed out that although she received substantially less in salary, due to her decision to put money back into the business, she did receive a share of the income in that year. HR at 31:45 and 1:19:41. The return states that Nathan Schwab's share of income from the business was [REDACTED], and Ms. Schwab's share was [REDACTED], a difference of [REDACTED]. Exhibit 18, Schedule K-1.

Ms. Schwab testified that she chose to invest in the business rather than take a salary, and observed that in one year she increased Care Security's revenues from [REDACTED] to [REDACTED]. HR at 32:40. In 2017, she did begin taking a higher salary, and has done so ever since. HR at 33:00. Applicant noted that owners often defer income, in order to meet the expenses of the business. HR at 33:30.

Although Ms. Schwab's share of the 2016 income was greater than Nathan Schwab's, her salary was significantly below the amounts paid to Abraham and Nathan Schwab, respectively. The difference in Ms. Schwab's share of the income, versus Nathan Schwab's ([REDACTED]) does not counterbalance the [REDACTED] difference between her salary and Nathan Schwab's, and the even greater disparity ([REDACTED]) between her salary and the salary paid to Abraham Schwab. Exhibit 18, Form 1125-E. See Matter of C.W. Brown v. Canton, 216 A.D.2d 841, 843 (3rd Dept. 1995) (certification properly denied where, among other things, husband earned a disproportionate salary compared to woman owner).

In light of these facts, the Division's determination was based upon substantial evidence. Based upon the information before the analyst, it was reasonable to conclude that Ms. Schwab's share of the profits of Care Security was not proportionate to her 51% interest, as required by Section 144.2(c)(2) of 5 NYCRR.

Operation

Section 144.2(b)(1) of 5 NYCRR requires that, in order to be certified as a woman-owned business, an applicant must demonstrate that the woman owner makes decisions pertaining to the operation of the business enterprise seeking certification. At the hearing, applicant argued that Ms. Schwab was involved in the critical aspects of the business, and had tie-breaking authority with respect to key decisions. Ms. Schwab testified that she can read plans, estimate jobs, and bid on contracts. HR at 20:00. She stated that generally, she delegates to her department heads, who confer with her. HR at 38:45. Ms. Schwab testified about a job where, against her advice, a customer installed a security system that was later replaced by Care Security with a superior system. HR at 42:00. She stated that she is familiar

with every line of equipment sold by the business, and is trained on all the products Care Security sells. HR at 52:45.

On cross-examination, Ms. Schwab acknowledged that the application indicated that the only managerial operation for which she was solely responsible was managing and signing payroll. Exhibit 1, at 4-5; HR at 1:04:20. In all of the other categories, Ms. Schwab either shared responsibility with non-minority males, or her name did not appear. Exhibit 1, at 4-5; HR at 59:49-1:03:00.

In Matter of J. C. Smith, Inc. v. New York State Dep't of Economic Dev., 163 A.D.3rd 1517 (4th Dept., 2018), lv. denied, 2019 WL 690511 (2019), the court confirmed the Division's determination to deny certification because the petitioner failed to demonstrate that the women owners made decisions pertaining to the operations of the business enterprise. The court stated that "it is not irrational or unreasonable for the Division to require that a woman owner must exercise independent operational control over the core functions of the business." 163 A.D.3rd at 1519. Given the information before the Division as set forth in the application, it was reasonable for the Division to determine that most of the managerial responsibilities were shared with, or carried out solely by, non-minority males. See Matter of Northeastern Stud Welding Corp. v. Webster, 211 A.D.2d 889 (3rd Dept. 1995) (court concluded that an application for certification as a women-owned business was properly denied, reasoning that although the woman applicant performed some functions, and made some decisions on her own, significant operations were shared and still others were performed solely by non-minority males). The Division's determination was based upon substantial evidence.

The Division's denial was also based upon information in the application with respect to licensure. Specifically, Section 144.2(b)(1)(i) of 5 NCYRR requires a woman owner to demonstrate adequate managerial experience or technical competence to operate the business. In this regard, the Division pointed out that the licenses listed in the application were held by Nathan Schwab. Exhibit 1, at 3. At the hearing, Ms. Schwab testified that the licenses were for burglar and fire alarm installation, and that such installations account for only two percent of Care Security's business. HR at 47:25. Ms. Schwab explained that when the business was first started, fire and burglar alarm installation accounted for more of Care Security's work, but that has changed. HR at 47:25. Ms. Schwab testified that the majority of the business is devoted to closed circuit television and access control, for which no license is required. HR at 40:30. Although Ms. Schwab's testimony was credible, none of this information was before the Division at the time of the denial, and therefore cannot be considered.

The Division relied upon the information provided in the application, which indicated that the business required a license, and that Ms. Schwab was not the license holder. The burden is on the applicant to show that the Division's denial was not based upon substantial evidence, and on this record, the Division's determination was supported by the statements in the application.

Control

In order to obtain certification, an applicant must demonstrate that the woman owner exercises control over the business enterprise. Section 144.2(b)(2) of 5 NYCRR requires an

applicant to demonstrate that corporate bylaws and other documents governing the business enterprise permit the woman owner to make decisions without restrictions. As part of the application, Care Security submitted a copy of its bylaws. Exhibit 12. The bylaws provide for officers, including a president, one or more vice-presidents, a secretary and treasurer. Exhibit 12, ¶ 5.1. The bylaws do not provide for the office of chief executive officer. Exhibit 12; HR at 1:42:45. Nathan Schwab is the president of Care Security, Abraham Schwab is the secretary, and Ms. Schwab is the chief executive officer. Exhibit 1, at 3. According to the bylaws, the president “shall have general supervision of the affairs of the corporation.” Exhibit 12, ¶ 5.2.

The Division argued that where, as here, corporate bylaws vest authority to direct the business in individuals who are not women, the woman owner is not in control of the business enterprise. At the hearing, Ms. Schwab testified that she is not a lawyer, has no training in drafting bylaws or corporate resolutions, and refers those tasks to outside counsel. HR at 1:41:22. Applicant argued that the board of directors had the authority to designate a chief executive officer, who would have general supervision of the corporation’s affairs. HR at 1:46:30.

“The intent of the eligibility requirement at 5 NYCRR 144.2(b)(2) concerning the designation of the woman-owner as the decision maker in the corporate documents of the business is to formalize functional designations. Formalized designations, as reflected in the corporation’s by-laws, ensure that the woman-owner is in fact the decision maker of the business enterprise.” Matter of Uniforms by Park Coats, Inc., Final Order 17-40, Recommended Order, at 4-5 (June 26, 2017). In this case, the Division found that Ms. Schwab was not the president of Care Security, and that she cannot therefore make business decisions without restrictions, as required by the regulation.

The Division also asserted that applicant had not demonstrated, through production of relevant documents, that the woman owner controlled negotiations. See Section 144.2(b)(3) of 5 NYCRR. The Division noted that, of the contracts submitted with the application, none were signed by Ms. Schwab. Exhibits 15, 16, and 17. At the hearing, Ms. Schwab testified that while she negotiated and reviewed contracts, she delegated the power to sign contracts to her sales team. Nevertheless, based upon the information before the Division (specifically, the contracts submitted with the application) it was reasonable for the Division to conclude that Ms. Schwab did not control negotiations, and that the application did not satisfy the regulatory requirement of control. The Division’s determination was supported by substantial evidence.

CONCLUSION

As discussed above, applicant did not meet its burden to demonstrate that the Division’s determination to deny Care Security Systems, Inc.’s WBE application for certification was not based on substantial evidence.

RECOMMENDATION

The Division's determination to deny Care Security Systems, Inc.’s application for certification as a women-owned business enterprise should be affirmed.

Matter of Care Security Systems, Inc.

DED File ID No. 61495

Exhibit Chart

Exhibit No.	Description	Rec'd
1	September 26, 2016 application	✓
2	July 21, 2017 denial letter	✓
3	August 3, 2017 letter requesting hearing	✓
4	November 23, 2018 letter scheduling hearing	✓
5	June 28, 2017: Care Security History/Ownership	✓
6	Resume: Renee Schwab	✓
7	Resume: Nathan Schwab	✓
8	Resume: Abe Schwab	✓
9	Responsibilities of Managerial Members	✓
10	Sources of Capitalization and Investments	✓
11	Minutes of Meeting (June 1, 2015)	✓
12	By-Laws	✓
13	Office Lease	✓
14	██████████ Lease Amendment	✓
15	██████████ Contract (One State Street)	✓
16	██████████ Contract	✓
17	██████████ Contract	✓
18	2016 Form 1120S	✓
19	Employee Summary Earnings	✓
20	June 1, 2015 Resolution of Directors	✓
21	Resume: Nathan Schwab (different version than Exhibit 7)	✓
22	Employee Detail Earnings	✓
23	Account Quick Report	✓
24	Resume: Renee Schwab	✓
25	Certificates of Completion	✓
26	March 21, 2017 Line of Credit Note	✓
27	December 11, 2018 memo re: alarm license	✓
28	NYS DOS Division of Licensing Services; Business of Installing, Servicing or Maintaining Security or Fire Alarm Systems	✓
29	December 11, 2018 memo re: certifications	✓
30	December 11, 2018 memo re: signed contracts	✓
31	Excerpt of application with notation	✓
32	List of employees	✓