

June 12, 2017

Reference Number: 17-0025

Janice Salais  
Acting Chief, Certification Unit  
Office of Business and Economic Opportunity  
California Department of Transportation  
1823 14th Street MS 79  
Sacramento, CA 95811-7189

Dear Ms. Salais:

Epic Land Solutions (ELS) appeals the California Unified Certification Program's (CUCP)<sup>1</sup> removal of the firm's certification as a Disadvantaged Business Enterprise (DBE) under the rules of 49 C.F.R. Part 26 (the Regulation). CUCP decertified ELS because it concluded that the owner had demonstrated an ability to accumulate substantial wealth and therefore is not reasonably considered to be economically disadvantaged under the Regulation. The U.S. Department of Transportation, Departmental Office of Civil Rights (the Department) remands under §26.89(f)(4) for clarification of matters likely to have a material effect on the outcome.

Specifically, the Department directs CUCP to ascertain how much of owner Holly Rockwell's joint adjusted gross income (AGI) is properly attributed to her, as opposed to her spouse, under California law, and further develop its ability to accumulate substantial wealth (AASW) rationale. We direct CUCP to conduct such further proceedings as it sees fit<sup>2</sup> in furtherance of these objectives and to either restore certification or issue a new decertification letter not later than August 30, 2017. If CUCP issues a new decertification letter, it must fully explain the reasons for its decision and cite specific evidence from the record in support. *See* §26.87(g).

#### *Procedural and Factual Background*

Caltrans proposed to decertify ELS in a Notice of Intent (NOI) issued on December 29, 2015, on the grounds that its owner, Holly Rockwell, is no longer economically disadvantaged. *See generally* §§26.87(f)(1), 26.67(b)(1)(ii)(A). In reaching this conclusion, the NOI cites as factors those found at §§26.67(b)(1)(ii)(A)(1) (owner's average AGI over preceding three years exceeds

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<sup>1</sup> The applicable certifier is the California Department of Transportation (Caltrans), a member of CUCP.

<sup>2</sup> Further proceedings may or may not include a new hearing. If CUCP should choose to start decertification proceedings over again with a new personal net worth (PNW) statement and Notice of Intent, it must offer ELS an opportunity to respond to that NOI. Based upon our analysis of the record, however, we do not believe CUCP needs to start the process anew or to have another hearing. CUCP must determine (and articulate why) what part of reported joint AGI is properly Ms. Rockwell's, which is a matter that CUCP did not specifically decide when it "concur[red] with the financial analysis conducted by Caltrans." Notice of Decertification (Oct. 14, 2006) at 1.

**REDACTED**) and (6) (fair market value of owner's assets exceeds **REDACTED**).<sup>3</sup> ELS responded to the reasons articulated in the NOI with Ms. Rockwell's Affidavit, which was presented at a CUCP hearing on July 26, 2016.<sup>4</sup> On October 14, 2016, CUCP sent ELS its notice of decertification (NOD). The NOD cites only the AGI factor of §26.67(b)(1)(ii)(A)(1). The NOD also recites CUCP's conclusions that the numbers demonstrated ample access to capital and credit.

The NOI states, "The PNW dated November 30, 2014, listed **REDACTED** in personal assets, **REDACTED** in personal liabilities for an adjusted net worth of **REDACTED**."<sup>5</sup> The NOI thus concedes that Ms. Rockwell's PNW is below the §26.67(a) limit.

However, the NOI rebuts Ms. Rockwell's presumption of disadvantage under §26.67(b)(1)(ii)(A) (PNW statement and supporting documentation demonstrate AASW). Specifically, the NOI rebuts items based on factors nos. 1 and 6 of that subsection, which are, respectively, AGI exceeding **REDACTED** and total asset values exceeding **REDACTED**.<sup>6</sup> Concerning factor no. 1 (AGI), the NOI states both that Ms. Rockwell's 2012-14 average AGI is **REDACTED** and that her personal compensation plus her share of other gross income from all sources totals **REDACTED**. The first number exceeds **REDACTED** while the second does not. CUCP used the higher number when it issued the NOD, which decertified based in part on AGI grounds. NOD at 1 ("Caltrans correctly calculated your adjusted gross income (AIG) to be **REDACTED** The NOD does not explain why CUCP chose the higher number as "the average adjusted gross income of the owner" under §26.67(b)(1)(ii)(A)(1) (emphasis added).

Concerning factor 6 (total assets), the NOI adds its revised values for Ms. Rockwell's primary and vacation residence to the reported values for an IRA account,<sup>7</sup> stocks and bonds, and cash.<sup>8</sup>

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<sup>3</sup> Citing facts rather than the subsections themselves, Caltrans explained that the computed levels of AGI and total assets, combined with putatively resulting access to capital and credit, rendered Ms. Rockwell wealthy by any reasonable standard.

<sup>4</sup> Notably, ELS failed to challenge Caltrans' computation of Ms. Rockwell's AGI. Rather, the rebuttal focused on the validity of the underlying Personal Financial Statement (PFS) and the accuracy of Caltrans' interpretations of particular line-items on the PFS.

<sup>5</sup> Stated assets minus stated liabilities in fact totals **REDACTED**. The NOI provides no explanation of what adjustments were made to bring the PNW figure under the \$1.32 million cap.

<sup>6</sup> Proper reporting of a loan from Ms. Rockwell to ELS is also in dispute. The correct way to report the loan on the Department's PNW statement (see Regulation, Appendix G) is as an asset, specifically on the line that erroneously reads "Loans to Shareholders & Other Receivables." The line should read Loans from Shareholders and Other Receivables, as loans from (and repayable to) shareholders constitute assets in the nature of receivables. This point is simply instructional because CCUP did not use the shareholder loan in its computation of total assets under §26.67(b)(1)(ii)(A)(6). Further, CUCP failed to include in its total assets computation the value of ELS, which notwithstanding appellant's argument to the contrary, is fully includible in the §26.67(b)(1)(ii)(A)(6) computation. The §26.67(a)(2)(iii) exclusions apply by their terms to "determining an individual's net worth;" they do not apply for purposes of the AASW calculation of §26.67(b)(1)(ii)(A)(6) "total fair market value of the owner's assets." (Emphasis added.)

<sup>7</sup> The correct calculation of IRA holdings for AASW (versus PNW) purposes is (the business owner's share of) full

The NOD, however, does not rely on §26.67(b)(1)(ii)(A)(6) total asset values for its conclusion that Ms. Rockwell has shown an ability to accumulate substantial wealth.

Finally, the NOI also relies on an unlisted factor, which the Regulation expressly permits. That factor is that ELS generates substantial gross and net income to which its owner has access. The NOI also notes that the firm has substantial assets and retained earnings over the period 2012-2014. The point of this latter observation is not well articulated, but we infer that Caltrans argues that Ms. Rockwell has access to the firm's assets and earnings. The NOI concludes "you obviously have access to substantial income and credit facilities." We need not consider this factor further, however, because the NOD does not cite it in support of CUCP's decision to decertify.

The NOD relies exclusively on Ms. Rockwell's AGI (and high PNW, another unlisted factor) in decertifying for Ms. Rockwell's AASW:

Caltrans correctly calculated your adjusted gross income (AIG) to be **REDACTED**. An AIG of this amount combined with your personal net worth of **\$REDACTED** affords you access to capital and credit not accessible by disadvantaged individuals as defined by 49 CFR, Part 26. The fact that the personal financial data was reported on a form other than that issued by the Department of Transportation does not in any way render the data invalid. Furthermore, no subsequent financial data to dispute that which was submitted has been presented. Therefore, the data reviewed by Caltrans to make its determination is valid. (NOD at 1.)

ELS appealed the decertification to the Department on November 30, 2016 (Appeal). The Appeal makes four main arguments:

1. Caltrans' investigation was not authorized under the Regulation.
2. Caltrans used the incorrect PNW form as the basis to decertify ELS.
3. Caltrans used outdated information and miscalculated Ms. Rockwell's PNW.
4. Caltrans' analysis of Ms. Rockwell's ability to accumulate wealth is flawed.

### *Discussion*

1. *Caltrans' investigation was not authorized under the Regulation.*

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asset value. The §26.67(a)(2)(iii) exclusions apply, by their terms, only "[i]n determining an individual's net worth," not for the separate and distinct §26.67(b)(1)(ii)(A) AASW determination, which has no exclusions.

<sup>8</sup> It is unclear that Caltrans took into account only Ms. Rockwell's shares of these assets, which appear to be community property in California. Caltrans seems instead to have used full value of the assets (in the case of the real property, the value estimates are from websites that provide real estate valuation information) rather than Ms. Rockwell's half.

Section 26.87(b) *requires* a certifier to initiate decertification proceedings when there is reasonable cause to believe that a certified firm is ineligible, based on “new information that comes to [its] attention.” It does not matter that this new information comes, as ELS argues, in a previously completed certification review described in §26.83(h).<sup>9</sup> Under §26.83(h)(2), a certifier may review a firm’s eligibility at any time it is “appropriate in light of changed circumstances.” Section 26.83(h) does not temporally limit a certifier’s authority under §26.87(b) to notify the firm that it proposes to decertify. Thus, the appellant’s estoppel argument based on its having “passed” CUCP’s 2014-2015 certification review is unavailing. The Regulation not only authorized CUCP to propose decertification; under the circumstances, it required it.

*2. Caltrans used the incorrect PNW form as the basis to decertify ELS.*

It is undisputed that Caltrans used an outdated form to calculate Ms. Rockwell's PNW. It used the PFS form that pre-dates the current PNW form. The current form became the required form on November 3, 2014. 79 Fed. Reg. at 59566 (Oct. 2, 2014). ELS submitted the old form dated November 30, 2014. This was under a month after the new form was required, in our view well within any reasonable transition period. We find that the use of the former PFS form, which included the same assets and liabilities information as the new PNW form does (albeit differently arranged), was harmless error under §26.89(f)(3). On the record before us, the fact that Ms. Rockwell reported her net worth calculations on the old form did not result in fundamental unfairness to the appellant or substantially prejudice the appellant’s opportunity to present its case. The NOI clearly apprised ELS of CUCP’s eligibility concerns, and the appellant in fact mounted vigorous rebuttals at the state level and in this federal appeal.

*3. Caltrans used outdated information and miscalculated Ms. Rockwell's PNW.*

Normally, the PNW calculation is not germane to a decertification based on the AASW. CUCP did not base its action on excess PNW within the meaning of §26.67(a)(2)(i).<sup>10</sup> In fact, it concluded that Ms. Rockwell had “personal net worth of **REDACTED**,” which is below the PNW cap. NOD at 1. CUCP based the decertification primarily on the AASW ground under §26.67(b)(1)(ii), and not the PNW ground under §26.67 (b)(1)(i) for rebutting the presumption of disadvantage. Section 26.67(b) makes clear that AASW is a separate and distinct rebuttal ground from excess PNW, although CUCP cited high PNW as an auxiliary ground for its conclusion. In fairness to the appellant, we choose not to consider CUCP’s stated high PNW factor. The result

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<sup>9</sup> ELS argues that its 2015 request for certification in additional work codes was a “pretext” for Caltrans to conduct a new certification review. This argument is unavailing. Caltrans, under the Regulation and as we explain in accompanying text, was free to conduct a new review based on “changed circumstances” whenever it saw fit. As for the delimiting language in §26.71(n) (“you must not require that the firm be recertified or submit a new application for certification”), we do not read the record to show that Caltrans did either. Caltrans instead appears simply to have reconsidered whether the owner continued to be disadvantaged.

<sup>10</sup> The November 30, 2014 PFS that Ms. Rockwell provided in fact shows her net worth to be **REDACTED** Administrative Record at 100.

is that only the AGI factor is before us in determining whether CUCP properly decertified because of Ms. Rockwell's AASW.

As for the PFS information being “outdated,” we note that there will always be some lag between the date that an owner provides financial data and the date that a certifier makes conclusions based upon it. In this case, the lag time was one year.<sup>11</sup> We have no evidentiary basis for concluding that the delayed decision resulted in “unfairness” to the appellant; the delayed decision actually benefitted the firm by allowing it to retain its certification for an additional year. Moreover, there is no showing that the delay “substantially prejudiced” the appellant’s opportunity to present its case, within the meaning of §26.89(f)(3). Accordingly, the argument that the PFS information was one year old at the time of the NOI is not a ground for reversal.<sup>12</sup> A PNW statement, by its nature, is a snapshot as of its date of financial circumstances that are subject to change. Requiring a new one on the literal eve of each UCP decision is simply an unworkable rule not contained in the Regulation.

#### 4. *Caltrans' analysis of Ms. Rockwell's ability to accumulate wealth is flawed.*

Since we concluded in the preceding section that the only AASW factor properly before us in this appeal is Ms. Rockwell’s high AGI, it is important that we analyze the correct figure in determining whether Caltrans proved, as it must do under §26.87(d), that Ms. Rockwell is no longer fairly regarded as disadvantaged—in other words, that her overall financial situation demonstrates AASW.

ELS first objects to Caltrans’s use of the AASW rule at all. ELS’s argument, however, is simply that the Regulation “make[s] it clear that new rules were meant to be permissive rather than mandatory.” Appeal at 8. We agree that the Regulation *permits* Caltrans to use the AASW rule to determine whether Ms. Rockwell has AASW. We further note that the AASW rule, as opposed to the factors listed at §26.67(b)(1)(ii)(A)(1)-(6), is not new. It is a 2014 incorporation directly into the Regulation of what had been pre-existing formal Department guidance. Only the stated factors are new. ELS first objection, accordingly, is ineffective. The overall test remains whether the totality of the business owner’s financial circumstances demonstrates AASW. *See generally* 16-0166, *Global Engineering Solutions* (Mar. 31, 2017) at n.8; *see also* 15-0113, *ADF Industries, Inc.* (Jan. 8, 2015) at 2 (AGI is a *factor*, not a self-contained rule that itself rebuts economic disadvantage).

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<sup>11</sup> Appellant states that Caltrans received the Nov. 30, 2014 PFS in December 2014. Appeal at 6. Caltrans proposed to decertify in December 2015. The record does not reveal why Caltrans waited a year before proposing decertification. Although one year can make a substantial difference in the reporting of PNW, an owner’s PNW generally *increases* over time as asset values tend to increase and debt tends to be repaid. A more recent financial statement may well not benefit the appellant.

<sup>12</sup> The information was two years old at the time ELS appealed to the Department and nearly two and one-half years old at the time of this remand. Aging of operative information is an unfortunate corollary of litigation.

We are concerned that the NOD fails to analyze more than one listed factor in concluding that Ms. Rockwell has AASW. The Regulation, in our view, contemplates a more complete analysis of the owner's overall financial circumstances. We therefore remand to CUCP for further development of its AGI argument (and, at its discretion, high PNW—which the NOI raises) and explicit consideration of the total assets factor cited in the NOI.<sup>13</sup>

Second, ELS objects to Caltrans's calculation of Ms. Rockwell's AGI:

If an agency decides to make use of the rule, one of the criteria that the rule asks agencies to review is whether the average adjusted gross income of the owner over the most recent three year period exceeds **REDACTED**. Here, Caltrans calculates that Mrs. Rockwell's adjusted gross income from ELS was **REDACTED**, yet, somehow, Caltrans concluded that the accumulation of wealth rule applied.

Caltrans reached this conclusion by improperly taking into account Mrs. Rockwell's husband's income. The General Instructions to the DOT's PFS form states that an individual's PNW includes "only his or her own share of assets held separately, jointly, or as community property" with her husband. According to Caltrans, Mrs. Rockwell's compensation from ELS was **REDACTED**. Caltrans goes on to argue that her average gross income over the past three years (2012, 2013, and 2013) was **REDACTED**. The million dollar figure takes into consideration Mrs. Rockwell's husband's income. No provision in the regulations governing the DBE program gives Caltrans the ability to attribute Mr. Rockwell's income to Mrs. Rockwell. (Appeal at 8.)

We agree that the NOD leaves unclear how Caltrans determined Ms. Rockwell's income to be **REDACTED** rather than **REDACTED** (or some other number). Ms. Rockwell's share of total reported (joint) AGI consists of her entire salary or draw from ELS, plus her share of ELS's flow-through income under California law, plus her one-half share of other items of income Caltrans identified. We remand for CUCP to clarify what income properly pertains to Ms. Rockwell under the Regulation and under California law. This potentially outcome determinative matter is simply unclear in the NOD.

Third, ELS argues that the company's financial health is immaterial to Ms. Rockwell's AASW:

In making its argument that Mrs. Rockwell has the ability to accumulate wealth, Caltrans' letter also inexplicably refers to the Company's gross earnings, total assets and retained earnings over the past three years. However, section 49 CFR § 26.67 refers to the owner's status as a socially and economically disadvantaged individual. Economic disadvantage is based on the individual's ability to accumulate wealth not the business's ability. Using the Company's ability to accumulate wealth would completely go against

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<sup>13</sup> The Department has determined that where an owner has high levels of liquid assets, a total assets value of substantially under \$6 million may nevertheless indicate AASW. See 14-0143, *Tiare Enterprises, Inc.* (July 27, 2015) (Hawaii UCP proved owner not fairly regarded as economically disadvantaged under pre-2014 Regulation change AASW guidance).

the mandate that Caltrans "exclude an individual's ownership interest in the applicant firm". *See* 49 CFR § 26.67 (a)(2)(iii)(A). (Appeal at 9.)

Section 26.67(b)(1)(ii)(A) states that the certifier "may consider factors" other than those listed in the provision's subsections. The company's financial health may well be an appropriate factor to consider under §26.67(b)(1)(ii)(A), provided that the certifier explains how the company's financial position gives the owner the ability to accumulate substantial wealth. This inquiry is not foreclosed by the §26.67(a)(2)(iii)(A) exclusion, as again, the exclusions pertain only for purposes of computing an owner's formal PNW, not for analyzing an owner's AASW. This paragraph has mainly instructional value going forward, however, since the current NOD does not rely on the financial health of ELS.

The NOD, for purposes of this appeal, relies entirely on the proper computation of Ms. Rockwell's AGI as a factor in determining that she has shown AASW. We are not prepared to affirm exclusively on that ground when the record indicates confusion about how much of the reported AGI belongs to Ms. Rockwell.<sup>14</sup> *See generally* §26.89(f)(4).

### *Conclusion*

We close the current appeal in our files and remand the matter for further proceedings consistent with the instructions in this letter. We direct CUCP first to determine how much of the reported AGI belongs to Ms. Rockwell and to explain better how her AGI demonstrates AASW. Second, CUCP should consider whether Ms. Rockwell's total assets (including only her ownership share of those assets) indicate AASW. As noted above, CUCP may conduct or not conduct such further proceedings as it chooses in furtherance of these objectives.<sup>15</sup> CUCP must complete its analysis and either restore certification or issue a new, more fully reasoned NOD by August 28, 2017.

This decision is administratively final and not subject to petitions for review. Thank you for your continued cooperation.

Sincerely,

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<sup>14</sup> ELS should have raised its objections to Caltrans's computation of AGI at the state-level hearing. Had CUCP had the benefit of such a rebuttal, then the reasoning for the attribution of most of the reported AGI to Ms. Rockwell might be clearer.

<sup>15</sup> The NOI placed ELS on notice that Caltrans considered AASW factors (1) (AGI above **REDACTED** and (6) (total assets exceeding \$6 million) and high PNW (an unlisted factor) as grounds for concluding that Ms. Rockwell is not economically disadvantaged. The NOI also provided ELS the opportunity to challenge these grounds in writing or in person. Accordingly, those grounds remain viable in the case of a new NOD. ELS in fact challenged these grounds before an impartial decisionmaker within the meaning of §26.87(e), and CUCP provided written notice of its decision under §26.87(g). Accordingly, CUCP has complied with the procedural requirements for decertification. Our decision to remand does not require CUCP to repeat any of these steps except the last, namely drafting a new Notice of Decision (restoration or removal of certification) that fully explains the action and complies with the instructions above concerning proper application of the operative eligibility rules.

Samuel F. Brooks  
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cc: ELS