



**U.S. Department of
Transportation**

Office of the Secretary
Of Transportation

Departmental Office of Civil Rights
1200 New Jersey Avenue, S.E., W76-401
Washington, DC 20590

February 15, 2018

Reference Number: 17-0130

Deborah Luter, Director
Small Business Development Program
Tennessee Department of Transportation
505 Deaderick Street, Suite 1800
James K. Polk Building
Nashville, TN 37243

Dear Ms. Luter:

McFall Sod & Seeding LLC (MSSLLC), appeals the Tennessee Department of Transportation's (TDOT) April 27, 2017 decision decertifying MSSLLC as a Disadvantaged Business Enterprise (DBE) under criteria set forth at 49 C.F.R. Part 26 (the Regulation). After considering the entire administrative record, the U.S. Department of Transportation, the Departmental Office of Civil Rights, (the Department) reverses TDOT's decision and directs the agency to restore the firm's certification for the following reasons.¹

Background

Jackie McFall and her husband (deceased) formed MSSLLC in the 1980s and TDOT certified MSSLLC as a DBE on April 6, 1990. MSSLLC's eligibility status went unchallenged until TDOT moved to decertify the firm on March 23, 2017. *See generally* Notice of Intent to Decertify (NOI). TDOT stated in the NOI:

The basis for the determination can be found within the Personal Net Worth Statement for Ms. Jackie McFall, dated December 31, 2016 and submitted to our office for review. You stated that your personal residence at REDACTED Hampshire Pike, Columbia, TN 38401 has a present market value of REDACTED This is above the threshold for the program as stated in §26.67(b)(1)(ii)(A)(I): the person's assets collectively (e.g., high income level, a very expensive house, a yacht, extensive real or personal property holdings) may lead a reasonable person to conclude that he or she is not economically disadvantaged.

¹ §26.89(f)(2) provides:

If the Department determines, after reviewing the entire administrative record, that [the certifier's decision was unsupported by substantial evidence or inconsistent with the substantive or procedural provisions of this part concerning certification, the Department reverses [the certifiers] decision and directs [it] to certify the firm or remove its eligibility, as appropriate. You must take the action directed by the Department's decision immediately upon receiving written notice of it.

This amount allows the TDOT. . .to rebut your presumption of economic disadvantage, even though you have indicated on your most recent “No Change Declaration” (executed on December 30, 2016) submitted to the TDOT DBE Program that your personal net worth is less than \$1.32 million.² (NOI pp. 2–3).

The NOI stated that Ms. McFall had the right to an informal hearing within one month of the notice and that MSSLLC also could present written information and arguments. The informal hearing occurred on April 18, 2017, and TDOT issued its Notice of Decertification (NOD) on April 27, 2018. The NOD again focused on the value of Ms. McFall’s residence to conclude that the firm was ineligible. TDOT’s entire decertification rationale is as follows:

The basis for the determination involves the “fair market value” for your personal residence which is significant. The supporting documentation found within your Personal Net Worth Statement submitted to our office for review, as of December 31, 2016, lists your “Primary Residence” with a “Present Market Value” at REDACTED The panel also based its determination on additional information that was presented at the informal hearing, including information regarding your business and personal income. (NOD, p. 1).

Decision

1. In its 2014 revision of the Regulation, the Department articulated how recipients can take into account evidence that indicate assets held by an owner suggests he or she is not economically disadvantaged, even in cases where personal net worth is not mathematically above \$1.32 million. A finding that an individual has an ability to “accumulate substantial wealth,” is a permissible ground for ruling that an owner is no longer economically disadvantaged under §26.67(b)(1)(i)(A). (*See*, 79 Fed. Reg. 59566, at 59568-59569, (Oct. 2, 2014)). The Department provided an example, directly in the text, wherein a person’s assets, collectively (*e.g.*, high income level, an expansive house and real or personal property holdings) may lead a reasonable person to conclude that he or she is not economically disadvantaged. We thereby gave recipients a tool to exclude from the program someone who, in terms of overall assets, would be considered by a reasonable person to be a wealthy individual, including even someone with liabilities sufficient to bring their personal net worth under \$1.32 million. *Id.*³

² MSSLLC provided updated personal net worth statements along with MSSLLC’s annual no change affidavit from 2010–2016, although there is no regulatory requirement for a disadvantaged owner to provide these statements as a matter of course. *See generally* §26.83(j) (“affidavit shall specifically affirm that your firm continues to meet SBA business size criteria and the overall gross receipts cap of this part, documenting this affirmation with supporting documentation of your firm’s size and gross receipts submission of Federal tax returns”).

The fair market value of Ms. McFall’s personal residence remained largely unchanged throughout the previous six years. After reviewing the firm’s submissions TDOT found no issue with the firm’s continuing eligibility. *See e.g.*, TDOT No Change Acknowledgement Letter (Jan. 5, 2017). It is unclear why TDOT then took issue with the firm’s eligibility in March of 2017, which is several years after the Department’s AASW guidance was incorporated in the Regulation.

³ The Department strongly believes that “recipients must be able to look beyond the individual’s personal net worth bottom line and consider his or her overall economic situation in cases where the specific facts suggest the

Section §26.67(b)(1)(ii)(A)(I) envisions the recipient perform the following logical steps. First, if the personal net worth statement and supporting documentation demonstrates an ability to accumulate substantial wealth, the recipient may rebut the presumption of economic disadvantage, and consider factors spelled out in the rule.⁴ Second, the recipient is to conduct a proceeding following the procedures of §26.87, which includes notifying the firm of reasonable cause to remove its eligibility, offering the firm an ability to respond in writing and/or in person before an impartial decision maker, and transcribing the proceeding if one occurs. During the proceeding, it is the recipient's burden to prove its case. In a broad sense, this means the recipient is to make a reasoned case that is supported by all relevant facts that are presented to the firm in such a way that they then can make a meaningful rebuttal.

An applicant's overall business/financial success and holdings is a starting point for looking at how this success translated to a person's ability to accumulate substantial wealth; Ms. McFall's personal residence was the starting point.⁵ We agree that Ms. McFall's personal residence could be relevant to the "total fair market value" analysis of her assets (item 6 in footnote 4 below).⁶ However, the record suggests that TDOT took the personal residence at its present market value, ignoring completely any debt associated with the asset, and not mentioning any other assets or relevant factors such as income. *See* NOI, pp. 2–3. Compounding the error was the agency's reference that the value of Ms. McFall's personal residence "is above the threshold for the program as stated in §26.67(b)(1)(ii)(A)(I)." (NOI, p. 2). This misstates the provision which has no such requirement.

2. TDOT's NOI and NOD do not reference a decertification ground for removing MSSLLC's eligibility as a DBE. *See generally* §26.87(f). The NOD also based its decision on "*additional information that was presented at the informal hearing, including information regarding [Ms.*

individual is obviously too wealthy with resources indicating to a reasonable person that he or she is not economically disadvantaged." 79 Fed. Reg. 59566, at 59568-59569, Oct. 2, 2014.

⁴ The Department set forth 6 factors, however; these are non-exclusive:

- (1) Whether the average adjusted gross income of the owner over the most recent three-year period exceeds REDACTED
- (2) Whether the income was unusual and not likely to occur in the future;
- (3) Whether the earnings were offset by losses;
- (4) Whether the income was reinvested in the firm or used to pay taxes arising in the normal course of operations by the firm;
- (5) Other evidence that income is not indicative of lack of economic disadvantage; and
- (6) Whether the total fair market value of the owner's assets exceed \$6 million.

⁵ TDOT's burden is to prove Ms. McFall's *ability to accumulate substantial wealth*—not simply that a particular asset would be regarded of high value. *See* 15–0113, *ADF Industries, Inc.* (Jan. 8, 2015) at 2 (AGI is a *factor*, not a self-contained rule that itself rebuts economic disadvantage). The Department's rule presents non-exhaustive factors to take into account in assessing *ability to accumulate substantial wealth* (and whether a reasonable person would therefore consider the presumed disadvantaged owner to be economically disadvantaged). The preamble to the rule clarifies that this analysis is to be reserved only for egregious, outlying claims of disadvantage; the factors are "not intended to be a checklist." 79 Fed. Reg. 59566, at 59569 (Oct. 2, 2014) (Regulation's procedural safeguards make it "unlikely" that certifiers would attempt to rebut presumption "in all but the most egregious cases").

⁶ Ms. McFall's personal average three year adjusted income from 2014–2016 is significantly less than REDACTED

McFall's] business and personal income," which is not articulated within the NOI. NOD at 1. Under §26.87, the decertification ground, and underlying substantive rationales, should have been communicated to MSSLLC in the notice that proposed decertification. MSSLLC would have then had the opportunity for an informal hearing, at which it could respond to the reasons for the proposal to remove its eligibility.

3. Section §26.87(g) provides, in part, that a certifier "must provide the firm written notice of the decision and the reasons for it, including specific references to the evidence in the record that supports each reason for the decision." As discussed above, the NOI provided TDOT's general conclusion regarding its rebuttal of Ms. McFall's economic disadvantage, and it failed to provide any analysis to support its conclusion. Similarly, the agency's final decision (NOD) does not provide a rational basis for TDOT proving, by a preponderance of the evidence standard, that it successfully rebutted Ms. McFall's presumption of economic disadvantage.⁷ Specifically, the NOD merely restates the fair market value of Ms. McFall's residence and adds that "[t]he panel also based its determination on additional information that was presented at the informal hearing, including information regarding [Ms. McFall's] business and personal income." There are no references to the relevant evidence in the record mentioned in the NOD (or the NOI), and TDOT failed to explain why MSSLLC's submissions and arguments that the firm presented in defense of the proposed removal did not establish that she was economically disadvantaged. This is an important part of TDOT's decision that renders it deficient. It also shows that TDOT did not satisfy its burden of proof under §26.87(d)(1).

In addition, to the extent that TDOT's denial rationale is based on an example that the Department codified to accompany the AASW provision,⁸ we find that the ground/rationale is underdeveloped. The example states that:

An individual with very high assets and significant liabilities may, in accounting terms, have a PNW of less than \$1.32 million. However, the person's assets *collectively* (e.g., high income level, a very expensive house, a yacht, extensive real or personal property holdings) may lead a reasonable person to conclude that he or she is not economically disadvantaged. The recipient may rebut the individual's presumption of economic disadvantage under these circumstances, as provided in this section, even though the individual's PNW is less than \$1.32 million.⁹

The example simply reinforces the certifier's obligation to reach its AASW conclusion based on the totality of circumstances. It is not intended to be a bright line rule. The NOD fails to provide sufficient evidence, supporting facts, or further reasons to show how TDOT reached its finding that Ms. McFall's is not economically disadvantaged. Thus, TDOT's decertification rationale is

⁷ §26.87(d)(1) states that during an informal hearing the certifier "bears the burden of proving, by a preponderance of the evidence, that the firm does not meet the certification standards of this part."

⁸ MSSLLC alleges Ms. McFall built the house using insurance proceeds from her late husband's death. Appeal, p. 2.

⁹ We note that the example erroneously appears under §26.67 (b)(1)(i) (rebuttal of economic disadvantaged based on the disadvantaged owner's excess personal net worth). However, the Department intended to place the example under §26.67 (b)(1)(ii) (rebuttal of economic disadvantaged based on AASW).

not adequately presented, and it is inconsistent with the Regulation's provisions concerning AASW.

4. TDOT's informal hearing occurred on April 18, 2017, however, this was not transcribed as §26.87 requires nor was a transcription provided to the Department as required by the Regulation. *See* §26.89(d) ("When it receives an appeal, the Department requests a copy of the recipient's complete administrative record in the matter. If you are the recipient, *you must provide the administrative record, including a hearing transcript, within 20 days of the Department's request.*") (Emphasis added).

In summary, we find that TDOT's decertification was procedurally deficient because it removed MSSLLC's DBE certification without a stated §26.87(f) decertification ground, and because the NOD raised a new—vague and unspecified—rationale that was not raised in the notice proposing the firm's decertification.¹⁰ The latter error, substantially prejudiced MSSLLC.¹¹ We therefore reverse under §26.89(f)(2), and direct TDOT to place MSSLLC back on its list of certified DBEs. This decision is administratively final and not subject to petitions for reconsideration.

Sincerely,

Marc D. Pentino
Lead Equal Opportunity Specialist
Disadvantage Business Enterprise Division

cc: TDOT

¹⁰ During decertification proceedings, an independent decisionmaker that is not comprised of an office or personnel that took part in actions leading to the proposal to remove the firm's eligibility makes the final decision concerning the firm's proposed decertification. *See* §26.87(e). The decisionmaker's determination is limited to deciding whether the agency that proposed the decertification demonstrated, by a preponderance of the evidence, ineligibility pertaining to the grounds raised in the notice of intent. *See generally* 14-0144, Northgate Land Development (September 14, 2015) (certifier erred by presenting new grounds within the notice of decision and failed to prove its original ground for decertification). "The Department does not intend for §26.87 to operate as a chance for a fishing expedition that later enables a decisionmaker to examine an agency's entire historical course of action concerning a firm's certification and use facts so mined to support an action *not proposed by the initiating agency.*" 12-0240, *Grady Excavating, Inc.* (August 18, 2014) at 7. (Emphasis added).

¹¹ Decertification proceedings are intended to "provide important due process protections to the DBE firm, including the right to a full explanation of the reasons for the proposed action, the right to contest, and the right to be heard. *See* 15-0113, *ADF Industries, Inc.* (January 8, 2015) at 2. "The right to be heard must be meaningful." 15-0146, *Belle Fontaine Interests, LLC* (April 25, 2016) at 5 (discussing an applicant firm's right to contest a proposed denial of interstate certification.). Depriving a firm's right to meaningfully contest a proposed decertification is an irreparable due process violation.