

**United States Small Business Administration
Office of Hearings and Appeals**

IN THE MATTER OF:

Alaka'i Consulting & Engineering, Inc.

Petitioner

SBA No. BDP-285

Decided: May 13, 2008

APPEARANCES

Guy P. Ontai, Chief Executive Officer, Alaka'i Consulting & Engineering, Inc., *pro se*,
Mililani, Hawaii, for Petitioner.

Lara H. Hudson, Esq., Office of General Counsel, Small Business Administration,
Washington, D.C., for the Agency.

DECISION AND REMAND ORDER

ARKOW, Administrative Law Judge:

I. Introduction and Jurisdiction

On February 21, 2008, Alaka'i Consulting & Engineering, Inc. (Petitioner) timely appealed a Small Business Administration (SBA) determination denying Petitioner entry into the 8(a) program. The SBA found the socially disadvantaged individual who owns and controls Petitioner failed to establish he is economically disadvantaged because his net worth exceeds \$250,000 and his two-year average adjusted gross income exceeds \$200,000. Petitioner claims that the SBA's conclusion is arbitrary, capricious, and contrary to law. I find that the SBA failed to exclude the assets and income of Petitioner's owner's spouse in its calculations. Further, the SBA failed to show how it calculated Petitioner's owner's net worth. Thus, the case must be remanded to the SBA to reexamine its calculations, excluding all of the spouse's assets and income, and explain these calculations.

This appeal petition is decided under the Small Business Act of 1958, 15 U.S.C. § 631 *et seq.*, and 13 C.F.R. Parts 124 and 134.

II. Issue

Whether the administrative record demonstrates the SBA made an erroneous factual finding or a mistake of law in its calculations of Petitioner's owner's net worth and average

adjusted gross income. *See* Small Business Act, § 8(a)(9)(C), 15 U.S.C. § 637(a)(9)(C); 13 C.F.R. § 134.406(e).

III. Facts

On September 8, 2006, Petitioner applied for admission into the 8(a) program. Administrative Record (AR), Ex. K. Petitioner states it is owned and controlled by Mr. Guy Ontai, and he is socially and economically disadvantaged. AR, Ex. L.

A. Average Adjusted Gross Income for 2005 and 2006

Mr. Ontai's joint 2005 Federal Income Tax Return (Form 1040) shows adjusted gross income of \$245,852. AR, Ex. K1. Mr. Ontai's spouse's 2005 Wage and Tax Statement (Form W-2) shows she earned \$62,258 in wages in 2005. AR, Ex. I.

Mr. Ontai's joint 2006 Federal Income Tax Return (Form 1040) shows adjusted gross income of \$236,070. AR, Ex. C5. Mr. Ontai's spouse's 2006 Form W-2 shows she earned \$58,316 in wages in 2006. AR, Ex. C6.

B. Net Worth

Mr. Ontai's SBA Form 413 (Personal Financial Statement) reflects he owns four pieces of real estate. AR, Ex. G2. Property A is Mr. Ontai's personal residence that he valued at \$600,000, with a mortgage balance of \$466,800. Property A is jointly owned with Mr. Ontai's spouse. Property B is located in Marina, California and Mr. Ontai listed its present market value at \$400,000, with a mortgage balance of \$271,000. Property B is jointly owned with Mr. Ontai's spouse. Property C is located in Golden, Colorado, and Mr. Ontai valued the property at \$96,000, with a mortgage balance of \$95,800. Property C is jointly owned with Mr. Ontai's wife. Property D is located in Honolulu, Hawaii, and Mr. Ontai valued it at \$200,000, with a mortgage balance of \$150,800. Property D is jointly owned with Mr. Ontai's mother. AR, Ex. G2.

IV. SBA Determinations

On October 4, 2007, the SBA denied Petitioner's 8(a) application. AR, Ex. C. The SBA found Mr. Ontai was not economically disadvantaged because his average adjusted gross income for 2005 and 2006 was \$241,881, placing Mr. Ontai in the top two percent of U.S. taxpayers. Further, Mr. Ontai's adjusted net worth (\$268,381) exceeded the regulatory threshold of \$250,000 for finding economic disadvantage. The SBA also concluded it was not able to determine whether Mr. Ontai complied with the ownership and control requirements for 8(a) certification. AR, Ex. C.

On November 23, 2007, Petitioner requested reconsideration of the SBA's denial. AR, Ex. B. On December 27, 2007, the SBA denied Petitioner's reconsideration request because Mr. Ontai's net worth after adjustments was still above \$250,000 and his average two-year income still exceeded the income threshold for economic disadvantage. AR, Ex. A.

The SBA questioned Mr. Ontai's valuation of his real estate, and the extent of his liabilities. The SBA stated that its search of comparable real estate values for his properties indicated the properties were more valuable than reported by Mr. Ontai.

Petitioner appealed that denial on February 21, 2008.

V. Discussion

The only substantive issue to be resolved in this matter is whether the SBA properly concluded that Mr. Ontai was not economically disadvantaged and, thus, Petitioner was ineligible for 8(a) certification. Economic disadvantage is established with evidence showing that the ability of a socially disadvantaged individual "to compete in the free enterprise system has been impaired due to diminished capital and credit opportunities as compared to others in the same or similar line of business who are not socially disadvantaged." 13 C.F.R. § 124.104(a). The SBA evaluates claims of economic disadvantage by examining the socially disadvantaged individual's personal financial condition, "including personal income for the past two years ..., personal net worth, and the fair market value of all assets, whether encumbered or not." 13 C.F.R. § 124.104(c). The SBA determined Mr. Ontai's personal income and net worth exceeded the SBA's regulatory criteria for being considered economically disadvantaged.

A. Average Adjusted Gross Income for 2005 and 2006

In evaluating Mr. Ontai's income for the two years prior to Petitioner's application, the SBA concluded in its initial determination that his average adjusted gross income for 2005 and 2006 was \$241,881. The SBA did not indicate in its reconsideration denial if it made any adjustments to this figure, instead stating that Mr. Ontai's income "still exceeds the income thresholds...." AR, Ex. A. It is apparent that the SBA did not exclude any of Mr. Ontai's spouse's income. Mr. Ontai's joint tax return shows adjusted gross income in 2005 of \$245,852 and \$236,070 in 2006. Thus, the average adjusted gross income shown on his joint tax returns for 2005 and 2006 was \$240,961.

Mr. Ontai's wife's income, however, was \$62,258 in 2005 and \$58,316 in 2006. The SBA should have excluded all of Mr. Ontai's spouse's income from its calculations. *See Matter of Anil Verma Associates, Inc.*, SBA No. MSB-536 (1996) (holding the SBA may not use a non-disadvantaged spouse's income in evaluating economic disadvantage). It did not do so.

Only excluding Mr. Ontai's wife's wages, Mr. Ontai's adjusted gross income for 2005 is, at most, \$183,594, and his adjusted gross income for 2006 is, at most, \$177,754.¹ Thus, Mr. Ontai's two year average adjusted gross income is, at most, under \$181,000. This is well below \$200,000 or the top two percent of all U.S. taxpayers, which is the threshold used by the SBA to determine economic disadvantage.

¹ I have not excluded other joint income, such as interest on joint investments, in these calculations. Thus, Mr. Ontai's adjusted gross income for 2005 and 2006 should be even lower.

B. Net Worth

The SBA's determination of Mr. Ontai's net worth is deficient. First, the initial determination concludes Mr. Ontai's net worth is \$268,381. The reconsideration determination questions the value of his real estate and liabilities. Yet the SBA does not reassess the net worth, provide Petitioner with the details of its calculations, or its new calculation of Mr. Ontai's net worth.

Second, the SBA's reconsideration determination indicates the SBA conducted its own examination into the value of Mr. Ontai's real estate by comparing the values of neighboring properties, but does not enumerate these values in its determination.

Third, it appears the SBA did not take into account that the real estate and other assets were jointly owned and attributed their full value to Mr. Ontai. Also, it did not take into account joint liabilities in its calculations. *See generally Superior Piping, Fabricators & Erectors, Inc.*, SBA No. BDP-220 (2005).

Finally, the SBA's scant assessment of Mr. Ontai's net worth deprived Petitioner of adequate notice of the basis for the SBA's determination and thus a meaningful opportunity to address the SBA's concerns in its appeal.

VI. Remand Required

It is "clearly apparent" from the AR that the SBA made both an erroneous factual finding by miscalculating the assets and income of Mr. Ontai, and a mistake of law by failing to exclude assets and income attributable to someone other than the Petitioner's disadvantaged owner. 13 C.F.R. § 134.406(e). Accordingly, remand is required. *Id.*

VII. Conclusion

The case is REMANDED to the SBA for further consideration and a new initial determination of Petitioner's eligibility for the 8(a) program that is consistent with this Decision and Remand Order. The SBA should review the existing record, including evidence in the appeal petition. Evidence need not be resubmitted, and the SBA may request additional evidence from Petitioner.

The SBA is ORDERED to follow the procedures mandated by 13 C.F.R. §§ 124.204-206.

The SBA is FURTHER ORDERED to issue, serve, and file its new initial determination with the Office of Hearings and Appeals (OHA) no later than thirty (30) days from the date of this Decision and Remand Order.

If the SBA declines the application, the SBA is FURTHER ORDERED to treat the decline as an initial decline and afford Petitioner the right to request reconsideration and submit

additional information and documentation to support its request.² 13 C.F.R. § 124.205. The SBA must also afford Petitioner the right to appeal the SBA determination without requesting reconsideration within the time periods prescribed by 13 C.F.R. § 124.206.

The SBA's determination must show how the SBA calculated Mr. Ontai's average adjusted gross income, including what income was excluded. In determining Mr. Ontai's net worth, the determination must show the SBA's calculations, how it treated joint property, how it valued property if that valuation differs from that of Mr. Ontai, and the actual figure it calculated for Mr. Ontai's net worth.

The parties should continue their settlement discussions. The SBA is ORDERED to report on the status of settlement negotiations no later than May 23, 2008.

I retain jurisdiction over this matter during the period of remand.

RICHARD S. ARKOW
Administrative Law Judge

² If the SBA certifies Petitioner, it should file and serve OHA a notice of certification.