

Disadvantaged Business Enterprise Programs-the Legal Landscape—A Brief Outline

I. ORIGINS OF DISADVANTAGED BUSINESS ENTERPRISE PROGRAMS

A. Origin:

1. 1958 Small Business Act §8(a) required assistance to “socially and economically disadvantaged” small businesses
 - Small Business Administration (SBA) used §8(a) to obtain contracts
 - from federal agencies and subcontract to firms that agreed to locate in/near “ghetto” areas and provide jobs to disadvantaged residents
2. 1969 Executive Order 11458 (Nixon)
 - Created Office of Minority Business Enterprise (OMBE)
 - Directed federal agencies to promote and assist MBEs
3. 1971 Executive Order 11625 (Nixon)
 - Extended mission of OMBE to include provision of technical managerial assistance to MBEs
4. 1977 Public Works Employment Act
 - First time numerical goals appeared for MBE participation in federal contracts, directing 10% of procurement be expended with MBEs
5. 1978 Amendments to §8(a)
 - Authorized SBA to enter into contracts w/other fed. agencies and sub-contract to small businesses owned by “socially and economically disadvantaged individuals”
 - Applied presumption of social disadvantage to Blacks, Hispanics, and Native Americans
6. Minority Small Business Contracting Program, §8(d)
 - Codified presumption of disadvantage
 - Recipients of major federal contracts required to negotiate with procuring agency subcontracting plans with percentage goals for MBEs and other small socially and economically disadvantaged businesses
7. 1980 Congress adds Asian Pacific Americans to list of disadvantaged persons
 - who qualify under 8(a) and 8(d)
8. 1983 Executive Order 12432
 - Directed each federal agency w/substantial procurement or grant making authority to develop a Minority Business Enterprise development plan
9. 1988 Business Opportunity Development Reform Act:
 - Directs president to set annual, govt.-wide procurement goals
 - At least 20% for small businesses; and
 - At least 5% for businesses owned by disadvantaged persons
10. 1990 Clean Air Act Amendment

- Required fair share 10% participation of MBEs and WBEs in contracts made by sub-recipients (states, counties, etc.) of EPA funding
 - In 1998, amended so that each sub-recipient could set its own fair share goal
 - In 2003, EPA changed its MBE/WBE program to a DBE program, more consistent w/Adarand and the USDOT program. EPA began accepting DBE certification for its program
11. 1997 Small Business Reauthorization Act
- Increased overall small business procurement goal to 23%;
 - Maintained 5% goal to disadvantaged MBEs; and
 - Established a 5% goal to small women-owned enterprises (federal-agency-wide)

II. TRANSPORTATION PROGRAMS

- A. 1980-US Department of Transportation (USDOT) regulations establish a minority and women's business enterprise program for highway, airport and transit projects
- B. 1982-Congress enacts Surface Transportation Assistance Act
1. Requires a minimum of 10% of the funds be expended w/small businesses owned and controlled by "socially and economically disadvantaged individuals"
- C. 1987-Surface Transportation and Uniform Relocation Assistance Act
1. Continued 10% expenditure requirement
 2. Added non-minority women to statutory definition of "socially and economically disadvantaged individuals"
- D. 1991-Intermodal Surface Transportation Efficiency Act of 1991 (ISTEA) + Transportation Equity Act for the 21st Century (TEA=21)
1. Continued the 10% DBE set-aside provision
- E. 1998-Transportation Equity Act for the 21st Century (TEA-21) enacted as Public Law 105-178
1. Continued 10% goal within USDOT
 2. Authorized the Federal surface transportation programs for highways, highway safety, and transit for the 6-year period 1998-2003
 3. Regulations
 - 49 CFR Sec. 26.21; all recipients of FHWA and most FTA/FAA must set DBE goals and plan in order to receive funding
 - 49 CFR Sec. 26.81; all DOT recipients in a given state must participate in a Unified Certification Program (UCP)
- F. 2005 Safe, Accountable, Flexible, Efficient Transportation Equity Act: a Legacy for Users (SAFETEA-LU) enacted
1. Extended 10% DBE goal through FY2009

III. JUDICIAL RESPONSES TO DBE PROGRAMS

A. Challenges to DBE programs often allege unconstitutional discrimination in violation of the 14th Amendment

B. Evaluation of 14th Amendment challenges - levels of scrutiny

1. Rational basis/lowest level; distinction involves:

- legitimate exercise of government power; and
- government actor has a rational basis for making distinction

2. Strict scrutiny/highest level; classification must be:

- legitimate exercise of governmental power;
- justified by a “compelling governmental interest”;
- “narrowly tailored” to serve the compelling interest, and
- the “least restrictive means” available to achieve it

C. Major Cases

1. ***Fullilove v. Klutznick***, 448 U.S. 448 (1980): Court defers to Congressional redress of past discrimination

- Challenge to MBE provision of Public Works Employment Act, requiring recipients of federal grants for local public works projects to use 10% of federal funds to procure services or supplies from MBEs
- Requirement was ‘to the extent feasible’
- Waiver available
- Court applied 2-part analysis -
 - ❖ Remediating present effects of past discrimination was within the *scope of Congressional spending power* when accomplished by placing conditions on use of funds
 - ❖ Limited, flexible use of race/ethnic criteria was *narrowly tailored* means of achieving goal
- Despite application of narrowly tailored test, opinion does not state level of scrutiny used or discuss whether program serves compelling govt. interest

2. ***City of Richmond v. J.A. Croson***, 488 U.S. 469 (1989): state and local govts. are limited to redressing discrimination w/in their own jurisdictional borders.

- EP challenge to municipal requirement that at least 30% of the dollar value of contracts be subcontracted to MBEs
- Court applied strict scrutiny
- Distinguished local governments’ power to redress discrimination within their borders from Congress’ power to remedy general societal discrimination.
- Concluded that City failed to present a compelling interest for

remedying discrimination because there was no evidence that it had discriminated against MBEs

1. **Adarand Constructors:** series of interconnected cases on MBE preferences
 - Adarand I: **Adarand Constructors, Inc. v. Pena**, 515 U.S. 200 (1995);
 - ❖ Contractor challenged the constitutionality of “a race-conscious subcontracting compensation clause” (SCC) that awarded incentive payments to prime contractors whose subcontracts with DBEs exceeded 10% of total contract value
 - ❖ Court rejected **Fullilove**, stated that strict scrutiny was appropriate
 - ❖ Remanded to District Ct. for strict scrutiny analysis
 - Adarand II: **Adarand Constructors, Inc. v. Pena**, 965 F. Supp. 1556 (D. Colo. 1997);
 - ❖ District Court determined Congress had a compelling govt. interest in redressing discrimination, but
 - ❖ concluded that DOT incentive program was not narrowly tailored because benefits were available to all minorities regardless of disadvantage and would exclude disadvantaged whites
 - ❖ Enjoined enforcement of program
 - Post-Adarand II;
 - ❖ Adarand sues state of Colorado, challenging its use of DBE programs
 - ❖ CO modifies its regulations, requiring all DBE contractors to certify disadvantage
 - ❖ Adarand becomes certified as DBE under new regs.
 - ❖ 10th Circuit Court of Appeals rejects government’s appeal as moot because Adarand is a DBE
 - ❖ SCt reverses 10th Circuit decision, concluding that case is not moot because Adarand’s DBE certification is suspect and he may need further judicial protection
 - ❖ SCt remands to 10th Circuit
 - Adarand III: **Adarand Constructors, Inc. v. Slater**, 228 F. 3d 1147 (10th Cir. 2000);
 - ❖ 10th Cir. Court considered constitutionality of original and revised programs
 - ❖ reversed District Court’s injunction against future implementation of DOT’s DBE program in CO

- ❖ Agreed with District Court’s conclusion that SCC system of financial incentives in Adarand I was not narrowly tailored, but concluded that new DBE program, as revised under the post-Adarand DOT regulations, was constitutional

IV. POST ADARAND

A. Regulatory Changes; new USDOT regulations include

1. Overhauling agency’s DBE goal-setting process/eligibility requirements
2. Shifting program’s focus to achieving a “level playing field”
3. Requiring states and transit authorities to base their DBE participation goals
on demonstrable evidence
4. Requiring states to meet maximum feasible portion of their DBE goals using
race-neutral measures
5. Requiring states and transit authorities to submit their DBE participation goals to USDOT for approval on an annual basis
6. Requiring state and transit authorities to create and maintain a bidders list and develop/participate in a statewide unified certification program

(“UCP”)

B. Judicial Decisions;

1. Since Adarand, lower courts have concluded that govt. has compelling interest in adopting affirmative action programs
 - But, lack of judicial consensus re: “narrowly tailored” test
 - Whether states or localities must independently justify the use of racial preferences to implement federal mandates w/in their individual jurisdictions?
2. *Sherbrooke Turf, Inc. v. Minn. Dep’t of Transp.*, 345 F.3d 964 (8th Cir. 2003) and *Gross Seed Co. v. Dep’t of Transp.*, 345 F.3d 964 (8th Cir. 2003);
 - Under revised USDOT regulations and TEA-21, Minnesota and Nebraska state highway departments established specific goals for the award of federally-funded contracts to DBEs
 - 8th Cir. agrees with 10th Cir. conclusion in Adarand III that Congress had satisfied showing of compelling interest to remedy race discrimination in federal highway contracting
 - Court holds that neither Minnesota DOT nor Nebraska road dept. was required to make an independent showing of compelling interest and that program was narrowly tailored as implemented at the state level
3. *Western States Paving Co., Inc. v. Washington State Dep’t of Transp.*, 407 F.3d 983 (9th Cir. 2005);

- 9th Cir. ruled that TEA-21's MBE and WBE preferences for highway contractors were facially valid
 - Govt. had a compelling interest in ensuring that federal funding was not distributed in way that reinforced effects of public/private discrimination w/in transportation-related construction
 - TEA-21's racial preferences were narrowly tailored to further that interest b/c revised DOT regs. prohibited use of quotas and required state to meet its maximum goal by using race-neutral means
 - Strikes down state's implementation program as not being sufficiently narrowly tailored to further Congress' remedial objectives
 - Ct. concludes that remedy requires showing of *actual* discrimination
 - Note: in the wake of this ruling, Caltrans adopted race-neutral policy
b/c it could not show sufficient evidence that minority groups had suffered disc. in the state's contracting industry.
4. ***Rothe Dev. Corp. v. U.S. Dept. of Def.***, 262 F.3d 1306 (Fed. Cir. 2001): imposes heavier burden on fed. govt. to demonstrate necessity for minority contracting preferences.
- Ct. declined to uphold §1207 of the National Defense Authorization Act of 1987
 - Provision establishes a 5% participation goal for DBEs in Dept. of Defense contracts, incorporates §8(a) presumption of racial disadvantage and authorizes Dept. of Defense to apply a price evaluation adjustment of 10% to attain 5% goal
 - Ct. held that district court's standard of review was too deferential, concluding that proper inquiry was whether a 'strong basis in evidence' supported Congress' conclusion that discrimination existed
 - 'Mere listing' of evidence before Congress when it enacted original statute was insufficient
 - Detailed statistical information regarding existence of disc. in 1992 necessary to find reauthorized §1207 constitutional
 - Govt. must also produce evidence of pre-enactment discrimination

V. STATE AND LOCAL GOVERNMENT RESPONSES

- A. To survive legal challenges, state and local race-conscious DBE programs must;
1. Be justified by studies that are based on statistically valid samples; Examples of Washington, Illinois, and Maryland disparity studies
 2. Include an assessment of the qualifications and availability of DBEs in the specific jurisdiction;
 3. Incorporate race-neutral alternatives; and

4. Avoid being overly burdensome by incorporating waivers and good faith provisions
- B. State plans adopted to enforce federal requirements: cts. have not resolved whether different fact-finding standards apply.
- C. Scan of state MBE, WBE, and DBE programs (including USDOT and state funds)
1. Trend from 1995 to the present
 2. Race-conscious program strategies: mandated sub-contractor participation; preference bid discounts; preference bid ranking points.
 3. Race-conscious programs – Maryland, Texas, Massachusetts, North Carolina, Indiana, Colorado, and Pennsylvania
 4. Hybrids – Ohio and Minnesota
 5. Race-neutral initiatives – Florida, Delaware, Missouri, Arizona, and Washington. Do they work?
 6. Update on Michigan
 7. Targeted business services, including financing programs and legal services
- D. A brief look at local race-/gender-neutral programs in California and Washington
1. Los Angeles and OBE
 2. San Francisco – moving forward with targeted vendor outreach
 3. King County and Seattle Public Schools