

An hourglass-shaped graphic with a globe inside. The top bulb is dark blue, and the bottom bulb is light blue. The globe is centered in the narrow neck of the hourglass. The entire graphic is set against a white background.

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*Minority Contracting and Affirmative Action for
Disadvantaged Small Businesses: Legal Issues*

Jody Feder, American Law Division

January 19, 2007

Abstract. Since the early 1960s, minority participation "goals" have been an integral part of federal policies to promote racial and gender equality in contracting on federally financed construction projects and in connection with other large federal contracts. Federal contract "set-asides" and minority subcontracting goals evolved from Small Business Administration (SBA) programs to foster participation by "socially and economically disadvantaged" entrepreneurs (SDBs) in the federal procurement process. Minority group members and women are presumed to be socially and economically disadvantaged under the Small Business Act, while non-minority contractors must present evidence to prove their eligibility. "Goals" or "set-asides" for minority groups, women, and other "disadvantaged" individuals have also been routinely included in federal funding measures for education, defense, transportation, and other activities over much of the last two decades.

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Minority Contracting and Affirmative Action for Disadvantaged Small Businesses: Legal Issues

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January 19, 2007

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Summary

Since the early 1960s, minority participation “goals” have been an integral part of federal policies to promote racial and gender equality in contracting on federally financed construction projects and in connection with other large federal contracts. Federal contract “set-asides” and minority subcontracting goals evolved from Small Business Administration (SBA) programs to foster participation by “socially and economically disadvantaged” entrepreneurs (SDBs) in the federal procurement process. Minority group members and women are presumed to be socially and economically disadvantaged under the Small Business Act, while non-minority contractors must present evidence to prove their eligibility. “Goals” or “set-asides” for minority groups, women, and other “disadvantaged” individuals have also been routinely included in federal funding measures for education, defense, transportation, and other activities over much of the last two decades.

The U.S. Supreme Court has narrowly approved of congressionally mandated racial preferences to allocate the benefits of contracts on federally sponsored public works projects, while generally condemning similar actions taken by state and local entities to promote public contracting opportunities for minority entrepreneurs. Disputes prior to *City of Richmond v. J.A. Croson* generated divergent views as to whether state affirmative action measures for the benefit of racial minorities were subject to the same “strict scrutiny” as applied to “invidious” racial discrimination under the Equal Protection Clause, an “intermediate” standard resembling the test for gender-based classifications, or simple rationality. In *City of Richmond*, a 5 to 4 majority resolved that while “race-conscious” remedies could be legislated in response to proven past discrimination by the affected governmental entities, “racial balancing” untailored to “specific” and “identified” evidence of minority exclusion was impermissible.

Until *Adarand Constructors, Inc. v. Peña*, however, a different more lenient standard was thought to apply to use of racial preferences in federally conducted activities. The majority there applied “strict scrutiny” to a federal transportation program of financial incentives for prime contractors who subcontracted to firms owned by socially and economically disadvantaged group members. Although the Court refrained from deciding the constitutional merits of the particular program before it, and remanded for further proceedings below, it determined that all “racial classifications” by government at any level must be justified by a “compelling governmental interest” and “narrowly tailored” to that end. But the majority opinion, by Justice O’Connor, sought to “dispel the notion” that “strict scrutiny is ‘strict in theory, but fatal in fact,’” by acknowledging a role for Congress as architect of remedies for discrimination nationwide. Bottom line, *Adarand* and its progeny suggest that racial preferences in federal law or policy are a remedy of last resort, which must be adequately justified and narrowly drawn to pass constitutional muster.

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It has long been the policy of the federal government to assist minority and other “socially and economically disadvantaged” small businesses become fully competitive and viable business concerns.¹ The objective has largely been pursued through the federal procurement process by allocating federal assistance and contracts to foster disadvantaged business development. Federal assistance has taken a variety of forms, including targeting procurement contracts and subcontracts for disadvantaged or minority firms, management and technical assistance grants, educational and training support, and surety bonding assistance.

Present day set-aside programs authorizing preferential treatment in the award of government contracts to “socially and economically disadvantaged” small businesses (DBEs) originated in § 8(a) of the Small Business Act of 1958.² Initially, the Small Business Administration (SBA) utilized its § 8(a) authority to obtain contracts from federal agencies and subcontract them on a noncompetitive basis to firms agreeing to locate in or near disadvantaged areas and provide jobs for the unemployed and underemployed. The § 8(a) contracts awarded under this program were not restricted to minority-owned firms and were offered to all small firms willing to hire and train the unemployed and underemployed in five metropolitan areas, as long as the firms met the program’s other criteria.³ As the result of a series of executive orders by President Nixon, the focus of the § 8(a) program shifted from job-creation in low-income areas to minority small business development through increased federal contracting with firms owned and controlled by socially and economically disadvantaged persons.⁴ With these executive orders, the executive branch was directed to promote minority business enterprise and many agencies looked to SBA’s § 8(a) authority to accomplish this purpose.

The administrative decision to convert § 8(a) into a minority business development program acquired a statutory basis in 1978 with the passage of P.L. 95-507, which broadened the range of assistance that the government—SBA, in particular—could provide to minority businesses. Section 8 (a), or the “Minority Small Business and Capital Ownership Development” program, authorizes SBA to enter into all kinds of construction, supply, and service contracts with other federal departments and agencies. The SBA acts as a prime contractor and then “subcontracts” the performance of these contracts to small business concerns owned and controlled by “socially and economically disadvantaged” individuals, Indian Tribes or Hawaiian Native Organizations.⁵

Applicants for § 8(a) certification must demonstrate “socially disadvantaged” status or that they “have been subjected to racial or ethnic prejudice or cultural bias because of their identities as members of groups without regard to their individual qualities.”⁶ The Small Business Administration “presumes,” absent contrary evidence, that small businesses owned and operated by members of certain groups—including Blacks, Hispanics, Native Americans, and Asian Pacific Americans—are socially disadvantaged.⁷ Any individual not a member of one of these

¹ This report was originally written by Charles V. Dale, Legislative Attorney.

² 15 U.S.C. § 637(a).

³ Minority Contracting: Joint Hearing Before the Senate Comm. on Small Business and the House Subcomm. on Minority Enterprise and General Oversight of the Comm. on Small Business, 95th Cong., 2d Sess. 37 (1978).

⁴ E.O. 11652, 3 C.F.R. § 616 (1971), *reprinted in* 15 U.S.C. § 631 authorized the Office of Minority Business Enterprise created by preceding order, E.O. 11458, to provide financial assistance to public or private organizations that provided management or technical assistance to MBEs. It also empowered the Secretary of Commerce to coordinate and review all federal activities to assist in minority business development.

⁵ 15 U.S.C. § 637(a).

⁶ *Id.* at § 637(a)(5).

⁷ 13 C.F.R. § 124.105(b).

groups must “establish individual social disadvantage by a preponderance of the evidence” in order to qualify for § 8(a) certification.⁸ The § 8(a) applicant must, in addition, show that “economic disadvantage” has diminished its capital and credit opportunities, thereby limiting its ability to compete with other firms in the open market.⁹ Accordingly, while disadvantaged status under the SBA includes a racial component, in terms of presumptive eligibility, it is not restricted to racial minorities, but also includes persons subjected to “ethnic prejudice or cultural bias” who are able to satisfy specified regulatory criteria.¹⁰ It also excludes businesses owned or controlled by persons who, regardless of race, are “not truly socially and/or economically disadvantaged.”¹¹

The “Minority Small Business Subcontracting Program” authorized by § 8(d) of the Small Business Act codified the presumption of disadvantaged status for minority group members that applied by SBA regulation under the § 8(a) program.¹² Prime contractors on major federal contracts are obliged by § 8(d) to maximize minority participation and to negotiate a “subcontracting plan” with the procuring agency which includes “percentage goals” for utilization of small socially and economically disadvantaged firms. To implement this policy, a clause required for inclusion in each such prime contract states that “[t]he contractors shall presume that socially and economically disadvantaged individuals include Black Americans, Hispanic Americans, Native Americans, Asian Pacific Americans, and other minorities, or any other individual found to be disadvantaged by the Administration pursuant to § 8(a)...” All federal agencies with procurement powers were required by P.L. 95-507 to establish annual percentage goals for the award of procurement contracts and subcontracts to small disadvantaged businesses.

A decade later, Congress enacted the Business Opportunity Development Reform Act of 1988,¹³ directing the President to set annual, government-wide procurement goals of at least 20% for small businesses and 5% for disadvantaged businesses, as defined by the SBA. Simultaneously, federal agencies were required to continue to adopt their own goals, compatible with the government-wide goals, in an effort to create “maximum practicable opportunity” for small disadvantaged businesses to sell their goods and services to the government. The goals may be waived where not practicable due to unavailability of DBEs in the relevant area and other factors.¹⁴ Federal Acquisition Act amendments adopted in 1994 amended the 5% minority procurement goal, and the minority subcontracting requirements in § 8(d), to specifically include

⁸ Id. at 124.103(c).

⁹ The statute, 15 U.S.C. § 637(a)(6)(A), defines economic disadvantage to mean “socially disadvantaged individuals whose ability to compete in the free enterprise system has been impaired due to diminished capital and credit opportunities as compared to others who are not socially disadvantaged, and such diminished opportunities have precluded or are likely to preclude such individuals from successfully competing in the open market.”

¹⁰ 15 U.S.C. §§ 637(a)(5), (d). Criteria set forth in the regulations requires non-minority individuals to prove by “a preponderance of the evidence,” that they have personally experienced “substantial and chronic social disadvantage in American society” as the result of “[a]t least one objective distinguishing feature,” including “long term residence in an environment isolated from the mainstream of American society,” with a “negative impact “on his or her “entry into the business world.” “In every case ... SBA will consider education, employment, and business history, where applicable, to see if the totality of circumstances shows disadvantage in entering into or advancing in the business world.” 13 C.F.R. § 124.105(c).

¹¹ See 49 C.F.R. Pt. 23, Subpt. D, App. C.

¹² 15 U.S.C. § 637(d). See also 13 C.F.R. § 124.106.

¹³ P.L. 100-656, § 502, 102 Stat. 3887, codified at 15 U.S.C. § 644(g)(1).

¹⁴ See, e.g., 49 C.F.R. §§ 23.64(e), 23.65 (setting forth waiver criteria for the Department of Transportation).

“small business concerns owned and controlled by women” in addition to “socially and economically disadvantaged individuals.”¹⁵

Additionally, statutory “set-asides” and other forms of preference for “socially and economically disadvantaged” firms and individuals, following the Small Business Act or other minority group definition, have frequently been added to specific grant or contract authorization programs. “Goals” or “set-asides” for minority groups, women, and other “disadvantaged” individuals have routinely been part of federal funding measures for education, defense, transportation and other activities over much of the last two decades.¹⁶ Early on, Congress established goals for participation of small disadvantaged businesses in procurement for the Department of Defense, NASA, and the Coast Guard. It also enacted the Surface Transportation Assistance Act of 1982 (STAA),¹⁷ the Surface Transportation and Uniform Relocation Assistance Act of 1987 (STURAA),¹⁸ the Intermodal Surface Transportation Efficiency Act of 1991 (ISTEA),¹⁹ and the Transportation Equity Act for the 21st Century (TEA-21),²⁰ each of which contained a 10% minority or disadvantaged business participation goal on federally funded projects. TEA-21 lapsed on May 31, 2005, but was extended through FY2009 by P.L. 109-59, signed into law during the 109th Congress.²¹

The Adarand Decision and Its Progeny

Background and History of *Adarand*

Litigation surrounding racial preferences in federal contracting has followed a convoluted course since 1995, when the Supreme Court settled the constitutional parameters of the issue but avoided a decision of the merits in *Adarand Constructors Inc. v. Peña (Adarand I)*.²² By the time it returned to the High Court six years later, as *Adarand Constructors Inc. v. Mineta*, the legal and factual framework of the case was considerably altered by multiple lower court decisions and appeals, and by changes in the plaintiff’s legal standing, the details of the challenged federal program, and regulatory reforms to “amend, not end” federal affirmative action by the former Clinton Administration. To the chagrin of many legal observers, the Court in 2001 once again sidestepped the constitutional issues posed by the *Adarand* case and, after agreeing to reconsider the controversy, dismissed the appeal as “improvidently granted.” The object of the Court’s latest action—or inaction—was the Tenth Circuit’s two-part ruling in *Adarand Constructors v. Slater (Adarand III)*.²³ The federal appeals court there invalidated a federal highway program of financial incentives to promote minority and “disadvantaged” small business utilization in force

¹⁵ P.L. 103-355, 108 Stat. 3243, 3374, § 7106 (1994).

¹⁶ See CRS Report RL32565, *Survey of Federal Laws and Regulations Mandating Affirmative Action Goals, Set-asides, or Other Preference Based on Race, Gender, or Ethnicity*, by Charles V. Dale and Cassandra L. Foley.

¹⁷ P.L. 97-424, § 105(f), 96 Stat. 2097 (1982).

¹⁸ P.L. 100-17, § 106(c), 101 Stat. 132 (1987).

¹⁹ P.L. 102-240, § 1003, 105 Stat. 1914 (1992).

²⁰ P.L. 105-178, § 1101, 112 Stat. 107 (1998).

²¹ See § 1101(b) of P.L. 109-59, the “Safe, Accountable, Flexible, Efficient Transportation Equity Act: A Legacy for Users” (SAFETEA-LU), 119 Stat. 1144 (8-10-2005).

²² 515 U.S. 200 (1995).

²³ 228 F.3d 1147 (10th Cir. 2000).

at the time of *Adarand I*. But as revised and amended in 1997, the program was found to be narrowly tailored to a compelling governmental interest and passed constitutional muster.

Prior to *Adarand*, the U.S. Supreme Court had narrowly approved of congressionally mandated racial preferences to allocate the benefits of contracts on federally sponsored public works projects in *Fullilove v. Klutznick*,²⁴ while generally condemning similar actions taken by state and local entities to promote public contracting opportunities for minority entrepreneurs in *City of Richmond v. J.A. Croson Co.*²⁵ These disputes generated divergent views as to whether state affirmative action measures for the benefit of racial minorities were subject to the same “strict scrutiny” as applied to “invidious” racial discrimination under the Equal Protection Clause, an “intermediate” standard resembling the test for gender-based classifications, or simple rationality. In *City of Richmond*, a 5 to 4 majority resolved that while “race-conscious” remedies could be legislated in response to proven past discrimination by the affected governmental entities, “racial balancing” untailed to “specific” and “identified” evidence of minority exclusion was impermissible.

Until *Adarand Constructors, Inc. v. Pena*, however, a different, more lenient standard was thought to apply to use of racial preferences in federally conducted activities. The majority there applied “strict scrutiny” to a federal transportation program of financial incentives for prime contractors who subcontracted to firms owned by socially and economically disadvantaged group members. Although the Court refrained from deciding the constitutional merits of the particular program before it, and remanded for further proceedings below, it determined that all “racial classifications” by government at any level must be justified by a “compelling governmental interest” and “narrowly tailored” to that end.

There have been three distinct phases to the *Adarand* litigation. The case originated with a now-discontinued “race-conscious subcontracting compensation clause (SCC)” program conducted by the Federal Highway Lands Program of the Federal Highway Administration. The SCC did not allocate or set-aside a specific percentage of subcontract awards for DBEs or require a commitment on the part of prime contractors to subcontract with minority firms. Rather, “incentive payments” varying from 1.5% to 2% of the contract amount were paid to prime contractors whose subcontracts with one or more qualified DBEs exceeded 10% of total contract value. The program incorporated the racial presumption from the Small Business Act and regulations, in effect relieving minority group subcontractors of the burden of demonstrating disadvantaged status imposed upon non-minorities.

Suit was brought by *Adarand Constructors, Inc.*, a white-owned construction firm whose low bid on a subcontract for highway guard rails was rejected in favor of a higher bidding DBE. Both the federal trial court and the Tenth Circuit initially upheld the program by applying “lenient” judicial review—“resembling intermediate scrutiny”—rather than strict scrutiny, requiring far less remedial justification by the government. Because the program was not limited to racial minorities, and non-disadvantaged minority group members were ineligible to participate, the appeals court concluded, the program was “narrowly tailored.” In *Adarand I*, the Supreme Court reversed this first round of decisions.

²⁴ 448 U.S. 448 (1980).

²⁵ 488 U.S. 469 (1989).

The majority in *Adarand I* rejected the equal protection approach that applied “intermediate scrutiny” or some other relaxed standard of review to racial line-drawing by the Congress. “Because the “race-based rebuttable presumption” in the DOT program was an “explicit” racial classification, the Court determined, “it must be analyzed by a reviewing court under strict scrutiny,” and to survive, must be “narrowly tailored” to serve a “compelling governmental interest.” *Adarand I* undermined prior judicial holdings, which had afforded substantially greater latitude to Congress than to the states or localities when crafting affirmative action measures for racial or ethnic minorities. To “dispel the notion,” however, that “strict scrutiny is ‘strict in theory, but fatal in fact,’” the Court appeared to reserve a role for the national legislature as architect of remedies for past societal discrimination. “The unhappy persistence of both the practice and lingering effects of racial discrimination against minorities in this country is an unfortunate reality, and the government is not disqualified from acting in response to it.”²⁶ Thus, a majority of the Court appeared to accept some forms of racial preference by Congress in at least some circumstances.²⁷ No further guidance was provided, however, as to the scope of remedial authority remaining in congressional hands or the conditions for its exercise. Indeed, the Court refrained even from deciding the merits of the constitutional claim before it in *Adarand I*, instead remanding the case to the lower courts to determine the outcome.

On remand, the district court in *Adarand II* decided that the “congruence” required by the Court did not mean that federal affirmative action must be supported by the same “particularized” showing of past discrimination as state and local programs.²⁸ Rather, as national legislature, Congress was empowered to enact broad discrimination remedies based on nationwide findings derived from congressional hearings and statements of individual federal lawmakers. “Congress,” in other words, “may recognize a nationwide evil and act accordingly, provided the chosen remedy is narrowly tailored so as to preclude the application of a race-conscious measure where it is not warranted.” The DOT incentive program failed the “narrow tailoring” test, however, because it linked a race-based presumption to the award of financial “bonus[es]” to prime contractors whose choice of a subcontractor was based “only on race.” The racial presumption was found to be both “overinclusive”—in that its benefits were available to all named minority group members—and “underinclusive”—because it excluded members of other minority groups or caucasians who may share similar disadvantages. Although “more flexible” than a “rigid racial quota” or mandatory set-aside, the SCC program was tainted by the government-wide 5% goals and transportation set-asides which it implemented.²⁹

²⁶ 515 U.S. at 217.

²⁷ In their separate concurrences, Justices Scalia and Thomas, espoused a far more restrictive view that would foreclose all governmental classifications by race or ethnicity. Justice Scalia declared that “government can never have a ‘compelling interest’ in discriminating on the basis of race in order to ‘make up’ for past racial discrimination in the opposite direction.” Justice Thomas was of the view that the “racial paternalism” of affirmative action was more injurious than beneficial to minorities. “In my mind, government-sponsored racial discrimination based on benign prejudice is just as noxious as discrimination inspired by malicious prejudice. In each instance, it is racial discrimination, plain and simple.”

²⁸ *Adarand Constructors Inc. v. Pena*, 965 F. Supp. 1556 (D.Colo. 1997).

²⁹ Two aspects of the district court’s analysis of the “narrow tailoring” requirement were especially unsettling for federal small disadvantaged business programs. First, the “optional” or voluntary nature of the SCC program was not enough to save it, notwithstanding the fact that prime contractors were free to accept bid proposals from any subcontractor, regardless of race or ethnicity. The government’s failure to prevail on this issue cast a long shadow over other federal minority contracting efforts—e.g., the § 8(a) set-aside, bid or evaluation preferences, and the like—which, under the district court’s reasoning, may be viewed as imposing a “choice based only on race” at least as “mandatory” and “absolute” as the incentive payment to prime contractors in *Adarand*, if not more so. Similarly, the fact that the SCC program did not expressly incorporate any “goals, quotas, or set-asides” was not sufficient to divorce it, in the (continued...)

The Tenth Circuit in 2000 issued its decision on the merits of the controversy.³⁰ The appellate panel in *Adarand III* reversed the district court injunction against future implementation of DOT's disadvantaged business enterprise (DBE) program in Colorado. In so doing, the court of appeals considered the constitutionality of the program, both as structured at the time of the district court decision and of later revisions to DBE regulations adopted in 1997. First, it generally agreed with the district court that the SCC system of financial incentives, in effect at time of *Adarand I*, had not been narrowly enough tailored to satisfy the constitutional requirements of strict scrutiny. But after lengthy congressional hearings, the financial incentives were eliminated, and other reforms were adopted to DBE requirements imposed by DOT regulation on state and local highway aid recipients. As a result, the appeals court ultimately concluded that the DOT disadvantaged business enterprise program as currently structured—though not the former, discarded program of financial incentives—passed constitutional muster.

Initially, the appellate tribunal aligned itself with the district court's finding that the federal government had a "compelling interest" in preventing and remedying the effects of past discrimination in government contracting. And the scope of Congress's authority to act was not limited geographically or to specific instances of discrimination—as in the case of the states and localities under *Croson*—but extended "'society-wide' and therefore nationwide." The range of admissible evidence to support racial line-drawing by Congress was both direct and circumstantial, including post-enactment evidence and legislative history, demonstrating public and private discrimination in the construction industry. The court was largely dismissive of individual statements by members or from committee reports as "insufficient in themselves to support a finding of compelling interest." Congressional hearings over nearly a two-decade period, however, depicted the social and economic obstacles—e.g., "old boy networks," racism in construction trade unions, and denial of access to bonding, credit, and capital—faced by small and disadvantaged entrepreneurs, mainly minorities, in business formation and in competition for government contracts. Moreover, "disparity studies" conducted after *Croson* in most of the nation's major cities compared minority-owned business utilization with availability and "raise[d] an inference that the various discriminatory factors the government cites have created that disparity." This record satisfied the Tenth Circuit panel that Congress had a "strong basis in evidence" for concluding that passive federal complicity with private discrimination in the construction industry contributed to discriminatory barriers in federal contracting, a situation the government had a "compelling" interest in remedying.

(...continued)

district court's view, from the percentage goal requirements imposed by statutes the program was designed to implement. Those statutory provisions—the 5% minimum disadvantaged small business goal in § 8(d) of the SBA and the parallel 10% requirement in STURAA and ISTEAA—were deemed invalid for lack of narrow tailoring. In effect, the district court ruling questioned much of the federal government's statutory infrastructure for advancing minority small business participation in the procurement process by race-conscious means.

³⁰ *Adarand Constructors Inc. v. Slater (Adarand III)*, 228 F.3d 1147 (10th Cir. 2000). This court of appeals decision was preceded by an intervening appellate ruling and Supreme Court review confined to procedural questions of standing and mootness occasioned by the plaintiff's change in circumstances. After the district decision in *Adarand II*, the State of Colorado did away with the racial presumption and certified the non-minority owner of *Adarand Constructors Inc.* as disadvantaged. As a result, the Tenth Circuit dismissed the case as moot and the vacated the judgment against the government. *Adarand v. Slater*, 169 F.3d 1292 (10th Cir. 1999). The district court decision was reinstated on January 20, 2000, however, when the Supreme Court rejected the mootness finding because there was nothing to prevent the government from reviving the abandoned policy, and returned the case to the circuit court for further proceedings. *Adarand Constructors v. Slater*, 528 U.S. 216 (2000).

The appellate tribunal adopted a two-stage review of the “narrowly tailored” requirement, focusing on the DBE program both as in effect prior to 1997 and later as revised to comply with *Adarand I*. Basically, it determined that many of the constitutional flaws that defeated the program in the district court’s opinion—an outcome with which the appellate panel largely agreed—had been eliminated by the government’s regulatory reforms. In effect, the latest decision lays the old program to rest while reversing the district court’s order insofar as it would bar implementation of the revised version. The appeals court also clarified the scope of the DBE program under review. It disagreed with, and specifically reversed, elements of the district court judgment raising issues beyond the specific DBE program as applied by Colorado officials to federally funded highway procurements within that state. Because the 5% and 10% goals in the SBA and underlying transportation authorization measures “are merely aspirational and not mandatory,” they were not the reason that “Adarand lost or will lose” contracts, and any challenge to those provisions were outside the scope of the remand in *Adarand I*. Thus, any broader potential implications of the district court ruling for § 8 (a) set-asides or government-wide goals for DBE participation under the Small Business Act were largely blunted by the appellate panel.³¹

The constitutional virtues of the revised program over the pre-1996 SCC program at issue in *Adarand I* were several. First, race-neutral measures dating back to the 1958 enactment of the SBA had preceded Congressional adoption of “aspirational goals” and other affirmative action measures for minority groups in government-wide contracting. DOT had not considered such alternatives before adopting race-conscious subsidies for prime contractors who select minority subcontractors. However, this defect was cured by the revised regulations, which specifically directed recipients to exhaust race-neutral alternatives—bonding, financing, and technical assistance, etc.—before taking race into account.³² Secondly, the revised regulations incorporated the time limits and graduation requirements for participation of disadvantaged businesses in the §§ 8(a) and 8(d) programs, thereby ensuring the later program’s limited duration.³³ The court of appeals also found that the revised DOT program was more flexible than the mandatory set-asides in *Fullilove* and *Croson* because they were voluntary on the part of the prime contractors and because the post-1996 revisions adopted an express waiver.³⁴ Any use of “aspirational goals” by recipients of federal highway funds had to make “reference to the relative availability of DBEs in the market” and was restrained in other ways by the new regulations so that “there is little danger of arbitrariness in the setting of such goals....”³⁵ The burden of the revised program on third parties was mitigated by placing monetary caps on subsidies to prime contractors—limiting the incentive to hire further DBEs—and by adopting “preponderance of the evidence” for proof of

³¹ Specifically, the Tenth Circuit opinion states: “Subsection 8(a) does not involve the use of SCCs, nor has Adarand made any showing that it has been injured by non-inclusion in the § 8(a)... This case does not involve, nor has Adarand ever demonstrated standing to bring, a generalized challenge to the policy of maximizing contracting opportunities for small disadvantaged businesses set forth in 15 U.S.C. §§ 637 and 644(g), or to the various goals for fostering the participation of small minority-owned businesses promulgated pursuant to 15 U.S.C. § 644(g). Nor are we presented with any indication that Adarand has standing to challenge ... § 637d.” 228 F.3d at 1152.

³² 49 C.F.R. § 26.51(a),(b)(2000).

³³ Participation in the § 8(a) program is limited by statute and regulation to ten and one-half years, and each DBE is re-evaluated, and may be graduated from the program, based on the submission of financial and other information required annually.

³⁴ 49 C.F.R. § 2615 (2000)(allowing recipients to seek waivers and exemptions, despite the already non-mandatory nature of the program).

³⁵ The court of appeals found that the SCC had been based in part on “an ill-defined 12-15% goal apparently adopted by the Federal Highway Administration, for which “it could find no explanation in the record.” This alone would have warranted summary judgment for Adarand, it concluded.

“social disadvantage” by members of “non-presumed” groups in lieu of the former “clear and convincing” standard. Finally, the revised program avoided the constitutional vice of over- and under-inclusiveness by “disaggregating the race-based presumption that encompassed both “social” and “economic” disadvantage” in the former regulation. Thus, an individualized showing of economic disadvantage is now required of all applicants to the program, minority and non-minority alike. This change, the appeal court believed, effectively satisfied the *Croson* requirement of an “inquiry into whether or not the particular MBE seeking a racial preference has suffered from the effects of past discrimination.”³⁶

The Supreme Court Declines to Decide the Case

The U.S. Supreme Court granted *certiorari* in an appeal from the Tenth Circuit’s final decision, marking the third High Court appearance by the *Adarand* case. During oral arguments, the Justices appeared more concerned with procedural irregularities in the case, as outlined by the Justice Department, than with the substance of the constitutional claims. In essence, the government argued that *Adarand*’s legal challenge was limited to the DOT program and regulations applicable to direct procurement of highway construction on federal lands, like the contract denied, not to the separate regulatory scheme governing federal highway assistance to states. Petitioner *Adarand Constructors, Inc.*, made a parallel argument—but for a different reason—that the court of appeals misconceived the scope of the appeal. In particular, petitioner’s brief contended, the Tenth Circuit’s analysis considered revisions to DOT regulations applicable to federally assisted state and local highway projects, which are irrelevant to the separate set of rules governing direct federal procurement, thereby undermining the court’s conclusion that the SDB program was narrowly tailored. Because the race conscious aspects of the original financial incentive program had been suspended in Colorado and several other states as the result of administration reforms to affirmative action rules after *Adarand I*, counsel for the company had difficulty arguing that its client “is still unable to compete on an equal footing” or had “lost a single contract under the provisions they are now challenging.” Further complicating *Adarand*’s position, the Tenth Circuit had rejected its earlier attack upon the entire statutory framework for federal small disadvantaged business programs, a ruling not appealed to the Supreme Court. The government, therefore, contended that *Adarand*’s lawsuit had “outlived the program that provoked it,” and in oral arguments to the Justices, the Solicitor General urged the Court to dismiss the petition for *certiorari* as improvidently granted.

It came as no great surprise, therefore, that the Justices complied with the government’s request and dismissed the case.³⁷ In a *per curiam* opinion, the Court emphasized technical flaws with the present appeal, as framed during oral arguments. First, *Adarand* was challenging a by now defunct aspect of the program that the Tenth Circuit had not ruled upon, asking “whether the various race-based programs applicable to direct federal contracting could satisfy strict scrutiny.” Nor had the company sought review of those aspects of the DOT statute and regulations respecting the state and local procurement program on whose constitutionality the appeals court had spoken. Consequently, the Supreme Court declined to reach the merits of a controversy

³⁶ The current regulations impose additional requirements on applicants with regard to individualized showing: they must submit a narrative statement describing the circumstances of that purported economic disadvantage. 13 C.F.R. § 124.104(b)(1)(2000). See also, 49 C.F.R. § 26.67(b)(1)(2000)(providing a \$750,000 net worth limit for DBEs under transportation programs); *id.* § 26.65(b)(stating that businesses exceeding a certain amount of gross receipts are ineligible for the DBE program).

³⁷ *Adarand Constructors, Inc. v. Mineta*, 534 U.S. 103 (U.S. 2001).

regarding which neither the parties nor the courts below appeared to be reading from the same page.

Left unanswered, therefore, were two major questions presented by the petition for review. First was “whether the court of appeals misapplied the strict scrutiny standard in determining if Congress had a compelling interest to enact legislation designed to remedy the effects of past discrimination.” The Tenth Circuit found that Congress had a “solid basis in evidence” for concluding race-conscious action necessary based on its dissection of hearing testimony, legislative reports, and state and local disparity studies. Generally, its approach conformed to earlier rulings, which have stressed deference to congressional fact-finding under section 5 of the Fourteenth Amendment. As the national legislature, Congress may not be constrained by the same requirements of specificity in regard to regional scope and classes of individuals benefitted by race conscious programs.

But recent Court rulings parsing the scope of congressional § 5 power to override state sovereign immunity under a variety of federal civil rights laws have emphasized the need for “congruence and proportionality” of the remedy to any problem perceived by the Congress.³⁸ The ramifications of this principle for § 5 race discrimination legislation is undetermined, and questions remain. Conversely, some would argue, the affirmative grant of congressional authority to legislate remedies for equal protection violations by states conferred by § 5 is even broader than its power to place similar conditions on direct spending for federal procurements, which is limited by 5th Amendment due process.

The second aspect of strict scrutiny analysis would have required the Court to determine whether the means chosen by DOT to promote minority group participation in the federal procurement process is “narrowly tailored.” In this regard, the Tenth Circuit found that after eliminating financial bonus or subsidy, the adoption of “aspirational goals” for utilization of disadvantaged firms based on “good faith efforts,” as required by current regulations, was a more flexible and narrowly tailored alternative. That conclusion, however, has been questioned by other courts, which have found that governmentally required goal-setting, coupled with enforcement sanctions—in Adarand’s case, liquidated damages under § 8 (d)—is inherently coercive and encourages racial quotas. The Ninth Circuit, for example, has invalidated a California affirmative action statute that required bidders on state contracts to subcontract a percentage of their work to female- and minority-owned firms or document a “good faith” effort to do so.³⁹ Similarly, in *Lutheran Church-Missouri Synod v. FCC*,⁴⁰ the D.C. Circuit blurred the distinction between so-called “inclusive” and exclusive “affirmative” action. FCC regulations required broadcast license holders (1) to engage in “critical self-analysis” of minority and female underrepresentation, and (2) to undertake affirmative outreach by using minority and female-specific recruiting sources.

³⁸ See, e.g., *Bd. of Trs. of the Univ. of Alabama*, 531 U.S. 356 (2001)(Congress could not abrogate state sovereign immunity to suit for compensatory damages under Title I of the Americans with Disability Act since historical record “fails to show that Congress did in fact identify a pattern of irrational state discrimination in employment against the disabled,” and the rights and remedies provided against the state “raise the same sort of concerns as to congruence and proportionality” as found in previous cases.); *Kimel v. Florida Bd. of Regents*, 528 U.S. 62 (2000)(Applying “congruence and proportionality” standard, the Court determined that the Age Discrimination in Employment Act was not “appropriate legislation” under § 5); *United States v. Morrison*, 529 U.S. 598 (2000)(Court invalidated provision of Violence Against Women Act, providing victims of gender-motivated violence with a civil damages remedy, since even as a “prophylactic measure,” it was “overbroad” and applied uniformly throughout the nation, rather than merely in states with congressionally documented records of this type gender discrimination.).

³⁹ *Monterey Mech. Co. v. Wilson*, 125 F.3d 702 (9th Cir. 1997), reh’g en banc denied, 138 F.3d 1270 (9th Cir. 1998).

⁴⁰ 141 F.3d 344 (D.C.Cir. 1998).

Strict scrutiny was held to be appropriate and the regulations were unlawful since beyond simple outreach, their effect was to influence ultimate hiring decisions; that is, the threat of government enforcement “coerced” stations to maintain a workforce that mirrors racial breakdown of the labor area.

The Court’s disposition of the latest *Adarand* appeal means that a definitive review of federally-mandated affirmative action must be postponed to another day. That day, however, may not be too far distant. Percolating in the lower federal courts are cases that pose similar questions regarding the power of Congress to enact racial preferences in federal contracting as were bypassed by the Court’s inconclusive determination in *Adarand*.

Post-Adarand Regulatory Developments

Federal regulatory reforms put forward by the former Clinton Administration sought to “narrowly tailor” federal minority and disadvantaged small business programs in line with *Adarand*. The Justice Department in 1996 proposed a structure for reform of affirmative action in federal procurement, setting stricter certification and eligibility requirements for minority contractors claiming “socially and economically disadvantaged” status under § 8(a) and § 8(d) of the Small Business Act.⁴¹ The plan suspended for two years set-aside programs in which only minority firms could bid on contracts. Statistical “benchmarks” developed by the Commerce Department and adjusted every five years were made the basis for estimating expected disadvantaged business participation as federal contractors, in the absence of discrimination, for nearly 80 different industries. Where minority participation in an industry falls below the benchmark, bid and evaluation credits or incentives are authorized for economically disadvantaged firms and prime contractors who commit to subcontract with such firms. Conversely, when such participation exceeds an industry benchmark, the credit would be lowered or suspended in that industry for the following year. The system is monitored by the Commerce Department, using data collected to evaluate the percentage of federal contracting dollars awarded to minority-owned businesses, and relies more heavily on “outreach and technical assistance” to avoid potential constitutional pitfalls.

The Justice Department’s response to comments on its proposal, together with proposed amendments to the Federal Acquisition Regulation (FAR) to implement it, were published in 1997.⁴² Several procurement mechanisms interact with benchmark limits pursuant to the FAR regulation jointly proposed for the Departments of Defense, General Services Administration, and National Aeronautics and Space Administration. An “evaluation” credit applies to bids by non-minority prime contractors participating in joint ventures, teaming arrangements, or subcontracts with such firms, and contracting officers may employ “monetary incentives” to increase subcontracting opportunities for disadvantaged firms in negotiated procurements. “Benchmarking” by the Commerce Department is the key feature of the program, designed to narrowly tailor the government’s use of race-conscious subcontracting in line with *Adarand*. The Commerce recommendation relies “primarily on census data to determine the capacity and availability of minority-owned firms.” As explained by DOJ:

⁴¹ 61 FR 26042, Notices, Department of Justice, Proposed Reforms to Affirmative Action in Federal Procurement. (May 23, 1996).

⁴² Response to Comments to Department of Justice Proposed Reforms to Affirmative Action in Federal Procurement, 62 FR 25649 (1997).

[A] statistical calculation representing the effect discrimination has had on suppressing minority business development and capacity would be made, and that calculation would be factored into benchmarks ... The purpose of comparing utilization of minority-owned firms to the benchmark is to ascertain when the effects of discrimination have been overcome and minority-owned firms can compete equally without the use of race-conscious programs. Full utilization of minority-owned firms in [an] SIC code may well depend on continued use of race-conscious programs like price or evaluation credits. Where utilization exceeds the benchmark, the Office of Federal Procurement Policy may authorize the reduction or elimination of the level of price or evaluation credits, but only after analysis has projected the effect of such action.⁴³

Final regulations implementing Justice Department recommendations with respect to the § 8(a) business development and small disadvantaged business program were issued by the SBA in 1998.⁴⁴ The reforms include a new process for certifying firms as small disadvantaged businesses and, in place of set-asides, a price evaluation adjustment program administratively tied to the Commerce benchmarks. In the past, the government relied on self-certification for purposes of “disadvantaged” eligibility, which allowed firms to identify themselves as meeting certification requirements. Under the new procedure, SBA, or where SBA deems appropriate, SBA-approved state agencies, or private certifiers make a threshold determination as to whether a firm is actually owned or controlled by specified individuals claiming to be disadvantaged. After ownership or control is established, the application is reviewed by SBA for purposes of a determination of disadvantaged status.

The definition of social and economic disadvantage remains largely intact under the SBA regulation. Members of designated minority groups participating in disadvantaged small business programs continue to enjoy a statutory presumption of social disadvantage. They are required, however, to state their group identification and meet certification criteria for economic disadvantage and are subject to third-party challenge under current administrative mechanisms. Individuals who are not within the statutory presumption may qualify by proving that they are socially and economically disadvantaged under SBA standards. Under prior SBA § 8(a) certification standards, however, persons not members of presumed disadvantaged groups had to prove their status by “clear and convincing evidence. The revised SBA regulations ease this burden on non-minority applicants by adopting a “preponderance of evidence” rule.

U.S. Department of Transportation Revised Regulations

Similarly, USDOT responded to *Adarand Constructors* and its progeny by issuing revised regulations to implement minority set-aside provisions in current federal transportation authorization measures. The Transportation Equity Act for the 21st Century (TEA-21), as enacted by Congress in 1998, provided that

[e]xcept to the extent that the Secretary [of Transportation] determines otherwise, not less than 10 percent of the amounts made available for any program under titles I, III, and V of

⁴³ Id. at 25650-52. An interim rule incorporating proposed DOJ revisions to the FAR regulation became effective in 1998. Federal Acquisition Regulation; Reform of Affirmative Action in Federal Procurement; Interim rule with request for comment, 63 FR 52426 (1998).

⁴⁴ 63 FR 35726, 35767 (1998).

this Act shall be expended with small business concerns owned and controlled by socially and economically disadvantaged individuals.⁴⁵

One in a succession of laws dating back more than two decades, TEA-21 lapsed on May 31, 2005, but was extended by P.L. 109-59, signed into law during the 109th Congress.⁴⁶ The new law continues through FY2009 longstanding USDA policy of setting aside 10% of federal highway and surface transportation funds for small disadvantaged firms “[e]xcept to the extent the Secretary of Transportation determines” otherwise.

The revised DOT regulations track the Small Business Act in defining disadvantaged business enterprises (DBE’s), including the presumption regarding designated minority groups and women, except that any small business owner with more than \$750,000 in assets—or who is otherwise shown not to be socially or economically disadvantaged—is disqualified. Members of non-designated groups (i.e., a white male) may qualify for DBE status if the individual demonstrates social and economic disadvantage in fact.⁴⁷

Describing the 10% goal as merely “aspirational,” the regulations de-centralize administration of the DBE program by delegating implementation to state agencies receiving federal transportation funds. A two-step process is established for states to determine “the level of DBE participation [that] would [be] expect[ed] absent the effects of discrimination.”⁴⁸ First, the relative availability locally of “ready, willing, and able” DBE’s must be calculated. This baseline figure is then adjusted upward or downward to reflect other capability factors and evidence of discrimination against DBE’s drawn from statistical “disparity” studies. The final adjusted figure represents the portion of federal transportation funding that a state must allocate to DBE for that year.

A state must meet the maximum feasible portion of this goal through race- (and sex-) neutral means. Race-conscious contract goals must be applied to achieve any portion of the utilization requirement not attainable by other means.⁴⁹ Even when race-conscious measures are necessary, however, the regulations do not require that DBE goals be included in every contract—or that they be set at the same level in every contract where used—as long as the overall effect is to obtain the required DBE participation level. Prime contractors to whom a state awards federally funded transportation contracts must undertake good faith efforts to satisfy any included goal by allocating the designated percentage of funds to DBE firms.⁵⁰ States are prohibited from instituting rigid quotas that do not account for a prime contractor’s good faith efforts to subcontract works to DBEs.⁵¹

⁴⁵ § 1101(b)(1), 112 Stat. at 113.

⁴⁶ See § 1101(b) of P.L. 109-59, the “Safe, Accountable, Flexible, Efficient Transportation Equity Act: A Legacy for Users” (SAFETEA-LU), 119 Stat. 1144 (8-10-2005).

⁴⁷ 49 C.F.R. pt. 26 (2003).

⁴⁸ Id. at § 26.45.

⁴⁹ Id. at § 26.51.

⁵⁰ Id. at § 26.53(a).

⁵¹ Id. at § 26.43(a).

Post-Adarand Judicial Decisions

Federal Affirmative Action Programs

Since *Adarand*, several lower federal courts have addressed the issue of congressional authority to fashion affirmative action remedies. Courts in these cases have generally concluded from the record of committee hearings and other documentary evidence before Congress that the government had a compelling interest for the program in question. However, in applying the constitutional demand for a “narrowly tailored” remedy, there is a divergence of judicial opinion as to whether states or localities must independently justify the use of racial preferences to implement federal mandates within their individual jurisdictions.

The Supreme Court in 2004 refused to revisit issues left unsettled by *Adarand* when it denied review of the Eighth Circuit’s consolidated ruling in *Sherbrooke Turf, Inc. v. Minnesota Department of Transportation* and *Gross Seed Company v. Nebraska Department of Roads*.⁵² The *Sherbrooke* court joined the Tenth Circuit in upholding the DBE program under current DOT regulations and, beyond that, approved specific state plans to implement that program. Pursuant to TEA-21 and the DOT revised regulations, state highway departments in Minnesota and Nebraska established specific goals for the award of federally-funded contracts to DBEs. In both states, white-owned contractors had submitted the low bid on DOT funded subcontracts, but were passed over in favor of a presumptively disadvantaged minority competitor. Petitioners challenged DBE contract awards, alleging unconstitutional race discrimination and that continued enforcement of the programs would deny them the right to compete on an equal basis for future contracts. Federal district courts in both states upheld the program.

The government conceded that the federal highway DBE program, on its face and as applied, is subject to strict scrutiny because it uses a race-based rebuttable presumption to define its beneficiaries and employs race conscious remedial measures. Such governmental consideration of race is constitutional only if narrowly-tailored to further a compelling governmental interest. Neither *Sherbrooke* nor *Gross Seed* disputed that the federal government has “a compelling interest in not perpetuating the effects of racial discrimination in its own distribution of federal funds and in remediating the effects of past discrimination in the government contracting markets created by its disbursements.” Rather, petitioners argued that Congress and DOT have no “hard evidence” of widespread intentional discrimination in the contracting industry; they relied instead on a Justice Department summary of over 50 documents and 30 congressional hearings on minority-owned businesses prepared in response to the *Adarand* decision.⁵³ The Eighth Circuit nonetheless agreed with the Tenth Circuit conclusion in *Adarand* that “Congress has spent decades compiling evidence of race discrimination in federal highway contracting,” and petitioners failed to meet the burden of showing that no remedial action was necessary.

Nor were the Minnesota DOT and Nebraska road department required to independently satisfy the compelling government interest aspect of strict scrutiny review. To be narrowly tailored, however, a national program must be limited to those parts of the country where its race-based measures are demonstrably needed. “To the extent the federal government delegates this tailoring

⁵² 345 F.3d 964 (8th Cir. 2003), cert. denied 541 U.S. 1041 (U.S. 2004).

⁵³ See Appendix—The Compelling Interest for Affirmative Action in Federal Procurement: A Preliminary Survey, 61 FR 26050 (May 23, 1996).

function, a State's implementation becomes critically relevant to a reviewing court's strict scrutiny." Under the current DOT program, the opinion notes, race-conscious methods cannot be used unless race-neutral means are projected to fall short of achieving the overall goal, and racial preferences or set-asides are limited to those instances "when no other method could be reasonably expected to redress egregious instances of discrimination." In addition, because the goals for DBE participation are tied to the relevant labor markets, have built in durational limits, and are subject to "good faith" waiver and exemptions, the programs were deemed narrowly tailored on their face. Finally, the court reviewed Minnesota's and Nebraska's implementation, including each state's reliance on findings by independent consultants in setting goals for minority-owned business participation, and concluded that the DBE program was narrowly tailored as applied at the state level.

Similarly, the issue presented in *Western States Paving Co., Inc. v. Washington State Department of Transportation*⁵⁴ is whether TEA-21—which allocates 10% of certain federal transportation funds for small disadvantaged and minority contractors—is unconstitutional on its face, or as applied by the State of Washington. As discussed above, DOT regulations "presume" disadvantaged status for minority groups and women, provided the small business owner has a net worth of less than \$750,000, but members of other groups are eligible if they can demonstrate, in fact, that they are "socially and economically disadvantaged." A three-judge panel of the Ninth Circuit agreed with the Eighth and Tenth Circuits that race and sex preferences for highway contractors under TEA-21 are facially valid. The compelling interest was in ensuring that federal funding is not distributed in a manner that reinforces the effects of either public or private discrimination within the transportation construction industry. The evidence relied on by Congress and reviewed by the court demonstrated a continuing pattern of race and sex discrimination in the industry.

The court further determined that the TEA-21 racial preferences were narrowly tailored to furthering compelling federal governmental interests. In this regard, the court pointed to several factors. First, the revised DOT regulations "explicitly prohibit the use of quotas" and require a state to "meet the maximum feasible portion of [its] overall goal by using race-neutral means."⁵⁵ Where racial goals are not met, the state may yet comply with federal standards by showing "good faith efforts" to achieve its goals. Moreover, "durational limitations" imposed by the legislative reauthorization process "ensure that Congress regularly evaluates" whether continuing need exists for the minority preference program. The regulation also makes clear that the statute's 10% DBE goal is "aspirational" only, with individual state goals determined by "the realities of [each state's] own labor market" and the availability locally of qualified minority contractors.

But these findings did not shield the Washington State program from Fourteenth Amendment challenge. Because the record was "devoid of any evidence suggesting that minorities currently suffer—or have ever suffered—discrimination" in the award of transportation infrastructure contracts within Washington State, Judges O'Scannlain and Bea found that the state's implementation program "is not narrowly tailored to further Congress' remedial objectives." A narrowly tailored remedy "depends on the absence or presence of discrimination," these judges urged, and it was not enough "simply [that] the state complied with the federal program's requirements." Thus, each of the six principal minority groups identified in Washington's DBE program must be shown to have suffered contract award discrimination.

⁵⁴ 407 F.3d 983 (9th Cir. 2005), cert. denied, 126 S. Ct. 1332 (2006).

⁵⁵ 49 C.F.R. § 26.51(a).

The ruling of another post-*Adarand* appellate tribunal appears to impose a heavier burden on the federal government for demonstrating a “strong basis in evidence” to support minority contracting preferences. In *Rothe Development Corporation v. U.S. Department of Defense*,⁵⁶ the trial judge appeared to defer uncritically to congressional evidence and findings to uphold § 1207 of the National Defense Authorization Act of 1987. That statute incorporates the SBA definition of small disadvantaged business, including the racial presumption, and establishes a 5% participation goal for such entities in Department of Defense contracts.⁵⁷ The § 1207 program authorizes DOD to apply a price evaluation adjustment of 10% in order to attain the 5% goal. In effect, this means that DOD may raise the bids of non-DBEs by 10% in order to give disadvantaged entrepreneurs a preference. The statutory goal-setting provision in § 1207 was reauthorized in 1989, and again in 1992 and 2003, because DOD efforts in the initial years fell short of meeting the 5% goal. A non-minority bidder in *Rothe* sued DOD and the Department of the Air Force for violating its equal protection rights in awarding a contract to a higher bidder, International Computer and Telecommunications, Inc., because of the race of its owner, who was of Korean descent.

The U.S. Court of Appeals for the Federal Circuit rejected what it viewed as the “deferential standard of review” applied by the district court and vacated the judgment. In so doing, it advanced a different conception of both the constitutional basis for Congress’s enactment of § 1207 and the degree of scrutiny demanded. As national legislature, it said, Congress could enact race-based programs as a condition to the exercise of its Article I spending powers or pursuant to § 5 of the Fourteenth Amendment as a remedy for lingering discrimination by state and local governments. Whatever deference may be owed to congressional remedies for state equal protection violations under § 5, when legislating racial preferences in federal spending programs, Congress is restricted by the Fifth Amendment, which incorporates its own equal protection component. “Strict scrutiny is a single standard and [it] must be followed here,” said the appeals court. The proper judicial inquiry was whether a “strong basis in evidence” supported Congress’s conclusion that discrimination existed and remedial action was warranted. A “mere listing” of evidence before Congress when it enacted the original statute in 1987 was insufficient, the Federal Circuit warned. Rather, detailed statistical information regarding the existence of discrimination in 1992 was necessary to find the reauthorized § 1207 constitutional. Moreover, the government must produce evidence of pre-enactment discrimination; reports generated after the statute was enacted showing discrimination against specific groups cannot be used to prove the constitutionality of the program when enacted. The “strong basis in evidence” must have existed at the time the law was enacted if it is to survive strict scrutiny. In remanding for further proceedings, the appeals court confirmed that when it comes to race-based federal programs, there is only “one kind of strict scrutiny.”⁵⁸

⁵⁶ 262 F.3d 1306 (Fed.Cir. 2001).

⁵⁷ 10 U.S.C. § 2323.

⁵⁸ The appellate opinion underscored certain additional elements for the lower court’s review on remand. In determining whether a “compelling Government interest” justified the SDB program, the lower court must decide if the § 1207 program is “truly remedial.” This requires a determination whether the program targets present discrimination or the “lingering effects” of past discrimination. If the latter, the opinion notes, the probative currency of the evidence must be determined, as must the existence of specific evidence of discrimination against Asian Americans in the particular industry involved in this case. As to whether the § 1207 program is narrowly tailored, the Federal Circuit highlighted three areas for remand consideration. First, the trial court should conduct “a probing analysis of the efficacy of race-neutral alternatives” to the § 1207 program. Second, the court must review evidence demonstrating whether the 5% goal of SDB participation was relevant to the number of qualified, willing, and able SDBs in the industry. Finally, the lower court had to determine whether the § 1207 program was over-inclusive by “presuming” that the five groups (continued...)

On remand, the district court bifurcated Rothe's claim into a challenge to § 2323 "as applied" in 1998, when the case was filed, and a broader challenge to the statute on its face.⁵⁹ This required it to analyze both the circumstances known to Congress when the statute was reauthorized in 1992 and later when the statute was reauthorized in 2003. The evidence purporting to justify the earlier claim was viewed to be "anecdotal" and did "not demonstrate a strong basis for Congress to believe that a race based remedial program was necessary because of the lack of statistical evidence of discrimination." Despite congressional testimony and findings of racial bias in the private and public sectors affecting the award of defense contracts, this evidence lacked statistical focus on discrimination against Asian Americans, the racial classification of the company awarded the contract instead of Rothe, and the particular industry involved. The court, therefore, found that "the program, as reauthorized in 1992 and applied in 1998, was unconstitutional."

As to Rothe's claim that §2323 was facially unconstitutional, the district court determined that Congress had met its burden of demonstrating statistical evidence documenting pervasive discrimination when it reauthorized the program in 2003. Specifically, it found that "59 statistical studies from across the nation succinctly demonstrate that Congress was reacting with a strong basis in evidence." The court focused on evidence regarding all minority groups—rather than simply Asian American as in the prior "as-applied" portion of its opinion—because proof that a program can be constitutionally applied in any one set of circumstances will sustain the statute from a facial challenge. It, therefore, held that § 2323, as re-authorized in 2003, was constitutional and denied Rothe any prospective relief.

Likewise, courts have considered challenges to SBA's § 8(a) program for socially and economically disadvantaged businesses. While upholding the constitutionality of the § 8(a) program on its face, the district court in *Cortez III Service Corporation v. NASA* required federal officials "to decide whether there has been a history of discrimination in the particular industry at issue" before applying a race-based set-aside.⁶⁰ Other courts, however, have denied firms or individuals standing to challenge the racial presumption in the SBA statute and regulations on the rationale that they were disqualified from contract consideration because of inability to demonstrate "social and economic disadvantage," and not race.⁶¹

Minority Contracting By State and Local Government

With increasing frequency, state and local affirmative action programs have met with constitutional objection from courts applying strict judicial scrutiny. Several federal circuit courts have addressed the legality of racial preferences in employment and public contracting programs since the Supreme Court's ruling in *City of Richmond v. J.A. Croson*.⁶² *Croson* emphasized the obligation of state and local governments to anchor their affirmative action efforts by identifying with specificity the effects of past discrimination. This meant that the governmental entity has to have a "strong basis in evidence"—just short, perhaps, of that required to establish a "prima

(...continued)

identified in the statute were victims of discrimination.

⁵⁹ *Rothe Dev. Corp. v. U.S. Dep't of Defense*, 324 F. Supp.2d 840 (W.D.Tex. 2004).

⁶⁰ 950 F. Supp. 357 (D.D.C. 1996). See also *Klaver Constr. Co. v. Kansas Dep't of Transp.*, 211 F. Supp.2d 1296 (D.Kan. 2002).

⁶¹ See *Interstate Traffic Control v. Beverage*, 101 F. Supp. 2d 445 (S.D. W.Va. 2000); *Ellsworth Associates v. United States*, 926 F.Supp. 207 (D.D.C. 1996).

⁶² 488 U.S. 469 (1989).

facie” case in a court of law—for its conclusion that minorities have been discriminatorily excluded from public contracts in the past.

In *Croson*, a 30% set-aside for minority subcontractors adopted by the City of Richmond failed this constitutional test. First, the program was premised on a comparison of minority contractor participation in city contracts with general minority population statistics rather than the percentage of qualified minority business enterprises in the relevant geographic market. There was, moreover, no evidence of discrimination in any aspect of city contracting as to certain groups—i.e., Orientals, Indians, Eskimos, and Aleuts—who nonetheless were granted a preference under the plan. With respect to “narrow tailoring,” the 30% “quota” was deemed “too inflexible” and had been implemented by the city without any prior consideration of “race-neutral” alternatives. Finally, the “waiver” built into the Richmond plan was too “rigid” because it focused solely on minority contractor “availability” with “no inquiry into whether or not the particular MBE seeking a racial preference has suffered from the effects of past discrimination by the city or prime contractors.”

The heightened standards of proof articulated by *Croson* and further developed by *Adarand* led many states, counties and municipalities to reevaluate existing minority business enterprise programs. Judicial challenges followed, and while several race-conscious programs survived,⁶³ many others were less successful, either because they lacked a compelling remedial justification or were not sufficiently “narrowly tailored” to withstand strict judicial scrutiny. As to the former, local jurisdictions primarily sought to establish a “strong basis in evidence” with “disparity” studies depicting the extent of minority exclusion from public contracting activity within the jurisdiction, coupled with any available “anecdotal” evidence. After the Court’s 1995 *Adarand* decision, such studies were generally poorly received in the courts. Almost universally cited as the basis for judicial rejection of such statistical proof was over-reliance by the governmental unit on general or undifferentiated population data that failed to adequately reflect minority contractor availability or to account for contractor size and other factors relevant to contractor qualifications.⁶⁴ Other major faults have been failure to “narrowly tailor” the remedy—whether a minority participation goal, preference, set-aside, or other “sheltered” bidding arrangement—to any disparities revealed by statistics and anecdotal proof of discrimination;⁶⁵ the failure to properly limit the program in scope and duration;⁶⁶ the absence of a “waiver” provision;⁶⁷ or

⁶³ See, e.g., *Indianapolis Minority Contractors Ass’n v. Wiley*, 187 F.3d 743 (7th Cir. 1999); *Associated Gen. Contractors of California v. Coalition*, 950 F.2d 1401, 1416-18 (9th Cir. 1991), cert. denied, 503 U.S. 585 (1992); *Coral Constr. Co. v. King County*, 941 F.2d 910 (9th Cir. 1991), cert. denied, 502 U.S. 1033 (1992).

⁶⁴ See, e.g., *Builders’ Ass’n of Greater Chicago v. Cook County*, 256 F.3d 642 (7th Cir. 2001); *Associated Gen. Contractors of Ohio, Inc. v. Drabik*, 214 F.3d 730 (6th Cir. 2000), cert. denied, 531 U.S. 1148 (2001); *W.H. Scott Constr. Co., Inc. v. City of Jackson*, 199 F.3d 206 (5th Cir. 1999); *Engineering Contractors Ass’n v. Metro. Dade County*, 122 F.3d 895 (11th Cir. 1997), cert. denied, 523 U.S. 1004 (1998); *Concrete Works of Colorado, Inc. v. City and County of Denver*, 36 F.3d 196 (10th Cir. 1994), cert. denied 514 U.S. 1004 (1995); *O’Donnell Constr. Co. v. District of Columbia*, 963 F.2d 420 (D.C.Cir. 1992).

⁶⁵ See, e.g., *Contractors Ass’n of Eastern Pennsylvania, Inc. v. City of Philadelphia*, 91 F.3d 586 (3rd Cir. 1996), cert. denied, 519 U.S. 1113 (1997); *Associated Util. Contrs. of Md., Inc. v. Mayor of Baltimore*, 83 F. Supp. 2d 613 (D. Md. 2000); *Main Line Paving Co. v. Bd. of Educ.*, 725 F. Supp. 1349 (E.D. Pa. 1989).

⁶⁶ See, e.g., *Associated Gen. Contractors of Ohio v. Drabik*, 214 F.3d 730 (6th Cir. 2000); *Kornhass Constr., Inc. v. State of Oklahoma*, 140 F. Supp. 2d 1232 (W.D.Okla, 2001); *Webster v. Fulton County, Ga.* 51 F. Supp.2d 1354 (N.D. Ga. 1999); *Associated Gen. Contractors v. New Haven*, 791 F. Supp. 941, 948 (D. Conn. 1992).

⁶⁷ *Associated Gen. Contractors*, 214 F.3d 730. Compare *Builders Ass’n of Greater Chicago v. City of Chicago*, 298 F. Supp. 2d, 725, 740 (finding DBE plan not to be narrowly tailored where waivers were “rarely or never granted”) with *N. Contr., Inc. v. Illinois*, 2005 U.S. Dist. LEXIS 19868 (D. Ill. 2005), aff’d 2007 U.S. App. LEXIS 320 (7th Cir. 2007)(state transportation funding plan approved where flexibility assured by “the employment of individualized DBE (continued...)

neglecting first to consider race-neutral alternatives, such as bonding and credit assistance programs, to ameliorate minority underutilization.⁶⁸

The courts, however, have yet to resolve several important issues. As noted, the first relates to whether different fact-finding standards pertain to independent state or local minority contracting initiatives than to state plans explicitly adopted in aid of enforcing federal law. Notwithstanding *Croson*, decisions by three different circuit courts suggest that no independent findings may be required to established a “compelling” governmental interest where the state agency acts not on its own authority, but pursuant to federal mandate requiring remedial state or local action to counteract the effects of past or present discrimination on federally funded projects.

Compelling government interest looks at a statute or government program on its face. When the program is federal, the inquiry is (at least usually) national in scope. If Congress or the federal agency acted for a proper purpose and with a strong basis in the evidence, the program has the requisite compelling government interest nationwide, even if the evidence did not come from or apply to every state or locale in the Nation.⁶⁹

The principle here seems to be that the evidentiary record compiled by Congress to find a compelling interest for the federal program provides the factual leverage necessary to sustain supporting action at the state and local level.

Likewise, in *Western State Paving Co. v. Washington DOT*, the Ninth Circuit reviewed “as applied” challenges to state programs mandated by federal law.⁷⁰ As discussed earlier, the court followed the Eighth Circuit in finding the 10% DBE set-aside of federal transportation funds under TEA-21 facially constitutional.⁷¹ But even if Washington demonstrates compliance with TEA-21 and its implementing regulations, it must separately meet strict scrutiny to survive an as-applied challenge. Thus, the majority found that while the state does not have to re-establish a compelling state interest, it still has to show that its program is narrowly tailored. That, in turn, “depends upon the presence or absence of discrimination in the state’s transportation contracting industry.”

Washington admitted that no statistical studies were done to establish the existence of discrimination in the highway contracting industry. What arguments the state did make regarding discrimination—based on estimates of minority contractor participation in state transportation contracting—were rejected. The court concluded that those percentages proved little because they failed to account for factors affecting the capacity of minority contractors to undertake

(...continued)

goals on a contract-by-contract basis, and through the maintenance of a waiver provision to account for those situations in which achievement of the set DBE goals is not reasonably possible.”).

⁶⁸ See, e.g., *Contractors Ass’n of Eastern Pennsylvania*, 91 F.3d 586; *Associated Gen. Contractors of Ohio*, 214 F.3d 730; *Concrete Works of Colorado v. City and County of Denver*, 86 F. Supp 2d 1042 (D.Colo. 2000).

⁶⁹ *Sherbrooke Turf*, 345 F.3d 964, 970 (8th Cir. 2003), cert. denied 541 U.S. 1041 (U.S. 2004).; see also *Milwaukee County Paver Ass’n v. Fiedler*, 922 F.2d 419, 423 (7th Cir. 1991)(“If the state does exactly what the statute expects it to do, and the statute is conceded for the purposes of the litigation to be constitutional, we do not see how the state can be though to have violated the Constitution.”).

⁷⁰ 407 F.3d 983 (9th Cir. 2005), cert. denied, 126 S. Ct. 1332 (2006).

⁷¹ Generally, the court determined that Congress had a compelling interest in creating a remedial scheme to overcome effects of past discrimination in the transportation contracting industry. Further, TEA-21 was narrowly tailored to this end because it created no quotas, it is limited in duration (Congress must periodically re-authorize it), and it contains income limits to lessen the burden on non-minority firms.

contracting work; for example, DBEs could be smaller, less experienced or concentrated in a particular part of the state. Moreover, the court observed that historical minority participation on contracts with affirmative action components “does not provide any evidence of discrimination against DBEs” in a race-neutral market. Washington also lacked anecdotal evidence of discrimination, which could not be inferred from statistics alone. Finally, “even when discrimination is present within a State, a remedial program is narrowly tailored if its application is limited to those minority groups that have actually suffered discrimination.”⁷²

In a more recent ruling, *Northern Contracting Inc. v. State of Illinois*,⁷³ the Seventh Circuit reached a result similar to the Ninth Circuit’s ruling in *Western States Paving*. In affirming the district court, the Seventh Circuit “considered the question of whether the federal government’s interest in remedying discrimination in highway contracting provided sufficient justification for the state to engage in a federally mandated DBE program, and ... concluded that it did.” As a result, the only question that remained was whether the state highway contracting program was narrowly tailored to achieve this compelling interest. After reviewing the statistical evidence and evaluating the state’s compliance with federal regulations, the court determined that the state’s program was narrowly tailored and therefore passed constitutional muster.

By contrast, a more restrictive evidentiary approach is represented by a different Seventh Circuit ruling in *Builders Association of Greater Chicago v. County of Cook*,⁷⁴ a case that involved a locally adopted minority contracting program rather than a federal program. The court there held that Cook County had failed to establish a compelling interest supporting its contract set-aside program. In defense of its program, the County presented anecdotal evidence that prime contractors failed to solicit minority- and women-owned subcontractors at the same rate as similarly situated firms owned by white males. In addition, the County put forward statistical data demonstrating that a number of firms rarely or never solicit minority- or women-owned firms for subcontract work. This evidence, however, failed to persuade the court of a systematic refusal to solicit such firms for subcontract work because it was based on the practice of a mere thirteen general contractors. In affirming the decision, the appeals court also noted that the program failed to link its set-aside levels (30% minorities, 10% women) to evidence of their availability on the relevant market.

Western States Paving and related cases may have important implications for future challenges against both state and federal affirmative action programs. Under the Ninth Circuit’s rationale, while federal programs may be insulated by appropriate congressional fact-finding, state affirmative action in furtherance thereof must be supported by proof of discrimination on a state-by-state basis. Moreover, even federal programs could fall under question as the statistical foundation for their enactment becomes strained by the passage of time, perhaps necessitating renewed evidentiary justification. Meanwhile, USDOT has issued guidance concerning the effects of the *Western States Paving* decision on recipients in the Ninth Circuit.⁷⁵

⁷² Id. at 998.

⁷³ 2007 U.S. App. LEXIS 320 (7th Cir. 2007).

⁷⁴ 123 F.Supp.2d 1087 (N.D. Ill. 2000), aff’d 256 F.3d 642 (7th Cir. 2001).

⁷⁵ A notice describing DOT’s implementation of the guidance was published in the *Federal Register* on Aug. 21, 2006. 71 FR 48579. Questions and answers regarding *Western States Paving* are available on the DOT website at http://www.fhwa.dot.gov/civilrights/dbe_memo_a5.htm.

Another issue that has divided the federal circuit courts since *Croson* is whether post-enactment evidence of discrimination is sufficient to justify minority set-asides and preferences.⁷⁶ In 1996, the Supreme Court in *Shaw v. Hunt* ruled that, in the context of racial gerrymandering, a legislature must have sufficient evidence to support a racial distinction “before it embarks on an affirmative action program.”⁷⁷ *Shaw* demanded a “strong basis in evidence” for race-based governmental action, which has been interpreted by the Federal Circuit to mean that “the quantum of evidence that is ultimately necessary to uphold racial classifications must have actually been before the legislature at the time of enactment.”⁷⁸ In this view, proof that the legislature had a constitutionally permissible intent requires strong pre-enactment evidence. But the Tenth Circuit decision in *Adarand III* allowed consideration of post-enactment evidence in addition to congressional findings because the defendants had gathered it in response to the Supreme Court’s application of strict scrutiny to the statutes in question.⁷⁹ The Supreme Court recently chose not to address this and other issues when it declined an appeal from the Tenth Circuit ruling in *Concrete Works of Colorado, Inc. v. City and County of Denver*.⁸⁰

In *Concrete Works*, the federal circuit court examined a city ordinance establishing goals for participation in the construction industry by minority- and female-owned businesses. In 1990, the Denver City Council passed Ordinance 513 to promote participation by minority-owned business enterprises (MBEs) and women-owned business enterprises (WBEs) in public work projects “to an extent approximating [their] availability and capacity.” The city determined availability and capacity by conducting periodic studies of minority participation in each contract area. The Ordinance also directed the Office of Contract Compliance (OCC) to establish MBE and WBE participation goals on each individual city contract. The statutory goals for total annual expenditures were 16% for MBEs and 12% for WBEs. According to the ordinance, if the OCC established an individual project goal, all bidders had to either meet the goals or demonstrate their good faith efforts to do so. The city revised the program in 1996 and 1998, reducing the annual goals for MBEs and WBEs in construction contracts to 10% and prohibiting M/WBEs from counting self-performed work towards the goals.

Concrete Works of Colorado, a construction firm owned by a white male, sued the city in 1992, alleging that it had been denied three contracts for failure to meet the goals or to make good faith efforts, and sought injunctive relief and money damages. The city relied on three categories of evidence to demonstrate a compelling remedial purpose for the ordinance. First, major studies—in 1990, 1995, and 1997—revealed large disparities between M/WBE availability and utilization on city projects without goals. Census data revealed like patterns of minority and female underutilization as contractors and subcontractors in state-wide construction, public and private. At trial, M/WBEs also testified to discrimination they confronted in qualifying and bidding on private sector jobs, in obtaining capital and credit, in dealing with suppliers, and of harassment suffered at work sites, including physical assaults.

⁷⁶ See, e.g., *Rothe Dev. Corp. v. United States DOD*, 262 F.3d 1306 (Fed. Cir. 2001); *Associated Gen. Contrs. of Ohio, Inc. v. Drabik*, 214 F.3d 730 (6th Cir. 2000); *Eng’g Contractors Ass’n of S. Fla., Inc. v. Metro. Dade County*, 122 F.3d 895, 911-13 (11th Cir. 1997); *Contractors Ass’n of E. Pa., Inc. v. City of Philadelphia*, 91 F.3d 586, 605 n.21 (3rd Cir. 1996); *Concrete Works of Colo., Inc. v. City & County of Denver*, 36 F.3d 1513, 1520-21 (10th Cir. 1994); *Harrison & Burrowes Bridge Constructors, Inc. v. Cuomo*, 981 F.2d 50, 60 (2nd Cir. 1992); *Coral Constr. Co. v. King County*, 941 F.2d 910, 919-20 (9th Cir. 1991).

⁷⁷ 517 U.S. 899 (1996).

⁷⁸ *Rothe Dev. Corp. v. United States DOD*, 262 F.3d 1306, 1327 (Fed. Cir. 2001).

⁷⁹ *Adarand Constructors Inc. v. Slater*, 228 F.3d 1147 (10th Cir. 2000).

⁸⁰ 321 F.3d 950 (10th Cir. 2003), cert. denied, 540 U.S. 1027 (U.S. 2003).

The principal issue presented by *Concrete Works* was whether the government's statistics and other evidence established a remedial justification for racial and gender preferences in public contracting. The circuit court adopted an expansive approach, finding that "irrefutable or definitive" proof of the city's own "guilty" actions was unnecessary where the city's "passive" participation in marketplace discrimination by its spending practices was shown.

Denver's only burden was to introduce evidence which raised the inference of discriminatory exclusion in the local construction industry and link its spending to that discrimination.... Denver was under no burden to identify any specific practice or policy that resulted in discrimination. Neither was Denver required to demonstrate that the purpose of any such practice or policy was to disadvantage women or minorities. To impose such a burden on a municipality would be tantamount to requiring proof of discrimination and would eviscerate any reliance the municipality could place on statistical studies and anecdotal evidence.⁸¹

Croson's admonition against relying on "mere societal discrimination" did not apply, the opinion states, where evidence of discrimination in the industry targeted by the program is shown—whether motivated by an attitude "shared by society" or "unique to the industry" is constitutionally irrelevant. The trial court was wrong to require Denver to "show the existence of specific discriminatory policies and that those policies were more than a reflection of societal discrimination."

The trial court also faulted the city's disparity studies, in part, for failure to control for firm size, area of specialization, and whether the firm had actually bid on city contracts. Such factors were thought important because, due to their generally smaller size, M/WBE's might lack the requisite experience and qualifications, diminishing their availability and capacity to perform on city construction projects. The Tenth Circuit accepted the studies, nonetheless, reasoning that small firms can expand and contract to meet their bidding opportunities, and because size and experience are not race or gender-neutral variables. "M/WBE construction firms are generally smaller and less experienced because of discrimination." The disparities, moreover, were not shown to disappear when such variables were controlled for, or held constant, and taking the number of city bidders into account might distort the picture by including unqualified firms. Likewise, "lending discrimination" and "business formation" studies were properly relied on by the city for the "strong link" they demonstrated between disbursement of public funds and the "channeling" of those funds due to private discrimination. Private barriers precluded entry of M/WBE's into the market "at the outset" and made impossible "fair competition" for public contracts by minority firms that did submit bids.

An appeal from the Tenth Circuit ruling, filed by petitioner Concrete Works of Colorado, Inc., was denied by the Supreme Court.⁸² In an unusual move, Justice Scalia was joined by Chief Justice Rehnquist in filing a written dissent from the Court's refusal to grant *certiorari*. The dissenters argued that Denver's policy violated the standards of proof required by the Court's 1989 decision in *Croson* and "invites speculation that case has effectively been overruled." According to their view, there must be some evidence that discrimination was so pervasive that any minority business would have suffered. "Absent such evidence of pervasive discrimination, Denver's seeming limitation of the set-asides to victims of racial discrimination is a sham, and the only function of the preferences is to channel a fixed percentage of city contracting dollars to firms identified by race." In declining review, Justice Scalia opined that his fellow Justices had

⁸¹ Id. at 973.

⁸² *Concrete Works of Colorado v. City and County of Denver*, cert. denied 540 U.S. 1047 (2003).

“abandoned” their former insistence on a “strong basis in evidence,” relying instead on the “good faith” of local governments to act responsibly when using racial preferences.

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