

FHWA Viewpoint of the Disadvantaged Business Enterprise Program

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The disadvantaged business enterprise (DBE) program and its predecessor, the minority business enterprise (MBE) program, have been a part of FHWA's federal-aid highway program since the early 1970s. The MBE program, early on, was integrated into the federal-aid highway program through each state's nondiscrimination affirmative action plans to ensure equal opportunity for individuals in federally assisted projects. The 1982 and 1987 federal-aid highway program reauthorization acts revamped the MBE program to the DBE program and established the clear statutory authority, which exists today. The 1982 and 1987 acts also implemented several key components of today's program, including a national 10 percent achievement goal, a precise eligibility definition, inclusion of women as a presumptive group, and uniform certification criteria. Each of these elements has significantly contributed to a program that has as its principal objective maximizing the opportunity of bona fide DBEs to participate in federally assisted contracts, while minimizing the potential of firms fraudulently trying to enter the program and failing to perform a commercially useful function. The program has shown considerable growth, especially since the enactment of a statutory goal in 1982. Since 1982, approximately \$10.3 billion of federal-aid funds have been awarded to DBEs on federal-aid highway projects.

The promotion of increased participation by minority contractors in the highway construction industry is not a recent phenomenon. Several early legislative statutes and executive orders greatly shaped and defined FHWA's DBE program. Title VI of the Civil Rights Act of 1964 forbids discrimination in the provision of benefits, services, and participation in federally assisted programs. Executive Order 11625 (October 13, 1971) required that federal executive agencies develop comprehensive plans and programs to encourage minority business participation. Finally, President Carter's Urban Policy Statement of March 27, 1978, directed all federal agencies to triple federal contracting with minority businesses and to include minority business enterprise (MBE) goals in federal assistance programs.

As far back as 1975, when FHWA issued Order 4700.1 (August 28, 1975), the agency has had an affirmative action policy to provide minority businesses with the maximum practical opportunity to participate in the federal-aid highway construction program. Guidance set forth in the 1975 order represented the agency's first extensive attempt to foster a nationwide program to develop plans and program goals, establish performance monitoring and reporting systems, and evaluate the results.

FHWA followed this order with implementing regulations under Title 23, Code of Federal Regulations (CFR), Part 230, on October 22, 1975. FHWA directed the state highway agencies' (SHAs') efforts in fulfilling the federally mandated minority business program. Several key elements of this new regulation were (a) the definition of the term minority business enterprise (MBE); (b) the requirement that SHAs take affirmative action to increase participation by minority businesses; (c) the requirement that prime contractors specify their intention to sublet any portion of the contract and, if so, take affirmative action to seek out and consider minority subcontractors; and (d) the incorporation of minority affirmative action clauses in the subcontract. The regulation defined an MBE as a business with at least 51 percent of the stock owned by minority group members.

Congress reinforced the concept of using federal financial assistance programs to promote minority businesses through enactment of the Public Works Employment Act of 1977. Section 103(f)(2) of that act contained a provision that 10 percent of the funds for local public works projects be expended with MBEs. This act, until passage of the 1982 Surface Transportation Assistance Act (STAA), was the only legislative statute mandating a specific minority business percent goal for a federally funded program.

The U.S. Department of Transportation's (DOT's) Order 4000.7A, issued on March 6, 1978, established the administrative framework for DOT's modal administrations MBE programs. DOT directed the establishment of strong affirmative action efforts to set and meet goals for increasing MBE involvement.

Recipients were required to present for approval an affirmative action program to promote MBE participation in federally assisted work. The term "good-faith effort" was first introduced in this order. Also, women were included in the definition of MBE.

DOT specified an 11-point affirmative action program for adoption by recipients. These 11 points were

1. A policy statement expressing a commitment to use MBEs in all aspects of procurement to the maximum extent feasible;
2. Appointment of a liaison officer and support staff to administer the program, noting authority, responsibility, and duties;
3. Percentage goals for the dollar value of work to be awarded to MBEs and reasonable written justification for these goals;
4. Procedures by which recipients seek affirmative action on MBE participation from major suppliers or contractors to the recipient;

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5. Where allowable under local law and appropriate to meet MBE goals, procedures to carry out an MBE set-aside program;

6. Procedures to require MBEs to be identified by name when bids are submitted and to permit their legitimacy to be ascertained;

7. Procedures to ensure known MBEs are able to compete equally by arranging solicitations, time for presentation of bids, quantities, specifications, and delivery schedules;

8. Means of assistance in overcoming barriers to program participation such as through bonding, insurance, and technical assistance activities;

9. Information and communication programs for MBE opportunity awareness;

10. Opportunities for use of minority-owned banks; and

11. To the extent necessary, methods of requiring contractors and subcontractors to comply with provisions of the program outlined.

On March 31, 1980, DOT issued implementing regulations under Title 49, CFR, Part 23, for a uniform MBE program by which firms owned and controlled by minorities and women could participate in contracts let by recipients of DOT financial assistance.

This regulation superseded all MBE regulations, orders, directives, etc., previously issued and was the first in a series of DOT regulations addressing its preference programs for ethnic minorities and women, with others to follow in 1981, 1983, and 1987.

The 1980 regulation provided the backbone of FHWA's program as it exists today. Key elements of this regulation were that it (a) defined MBE program elements that had to be implemented by recipients as a condition of federal assistance, (b) required program implementation by the modal agencies, (c) permitted contract goals to be set by recipients, and (d) required certification of the eligibility of participating firms by recipients. The regulation also adopted Section 8(a) of the Small Business Act (SBA) that defined a minority under a number of specific ethnic and cultural races as well as a general definition that also covered members of other groups, or other individuals found to be economically and socially disadvantaged by the SBA.

This regulation delegates to each modal administration the responsibility to approve the methods for determining its overall program and contract MBE goals. All programs had to be approved by August 1, 1980. Content and format of these programs were to take basically the same shape as that prescribed by DOT's Order 4000.7A. For the first time, a requirement was in effect that directed establishment of distinct and separate goals for MBEs and what became commonly known as women business enterprises (WBEs).

These early goals were generally expressed in dollar amounts. In 1980, approximately 3.4 percent of federal-aid construction funds were awarded to MBE and WBE firms.

One provision of the 1980 regulation, later rescinded by a final rule published on April 27, 1981, was the adoption of an administrative finding called "conclusive presumption." If one bidder met the MBE contract goal and offered a reasonable price, then all bidders that did not meet the goal were conclusively presumed as not exerting sufficient reasonable efforts and therefore were ineligible to receive the contract. As noted, the conclusive presumption provision was rescinded

in 1980 and replaced by one requiring contractors to make a good-faith effort.

The good-faith effort provision allowed the low bidder to receive the contract if meeting the MBE contract goal or satisfactorily demonstrating to the recipient that a good-faith effort had been made to do so. The final rule provided guidance criteria for determining what constituted good-faith effort.

In the evolution of FHWA's present DBE program, the major event was the passage of the 1982 STAA. This act was signed into law on January 6, 1983, and contained Section 105(f), which imposed the following requirement on federally assisted highway and transit projects:

Except to the extent that the Secretary determines otherwise, not less than 10 percent of the amounts authorized to be appropriated under this Act shall be expended with small business concerns owned and controlled by socially and economically disadvantaged individuals as defined by section 8(d) of the Small Business Act . . . and relevant subcontracting regulations promulgated pursuant thereto.

Section 105(f) made three substantial changes to the broad parameters of the MBE program as conceived in the 1970s. First, passage of the act for the first time provided clear statutory authority for DOT's program. Second, the act established a 10 percent goal for program participation. Finally, the definition of eligible individuals and groups was adopted from Section 8(d) of SBA. Section 8(d) provides a broader ethnic base of eligible groups and individuals. By defining participation under Section 8(d) of SBA, the act shifted eligibility criteria from minority status to disadvantaged status. The term "disadvantaged business enterprise" became the name for DOT's program. The 10 percent participation requirement applied only to ethnic minorities. Nonminority WBEs were not included but continued as eligible participants under the voluntary language established in Title 49, CFR Part 23, in 1980.

With passage of the 1982 Act and resulting program changes, DOT published implementing regulations that added Subpart D to existing 49 CFR 23 on July 21, 1983. The new regulation dealt primarily with DOT's interpretation of the congressional intent in setting a goal of not less than 10 percent and the newly defined eligibility criteria. DOT went to great lengths to repudiate any thought that the 10 percent goal for the DBE program was to be handled as a fixed set-aside or firm-quota program. The legislative history of Section 8(d) indicated that members of presumptive groups were to be conclusively considered as socially and economically disadvantaged, regardless of their actual economic situation. However, DOT's regulation included a rebuttable presumption requirement. Simply, this requirement states that belonging to one of the presumptive groups does not conclusively render an individual socially and economically disadvantaged.

A challenge provision was included in the regulation whereby recipients were required to adopt a procedure to allow anyone to challenge the presumption of being disadvantaged.

CURRENT PROGRAM IMPLEMENTATION

As the previous discussion indicates, the DBE program has changed considerably during its history. Passage of the 1987 Surface Transportation and Uniform Relocation Assistance

Act (STURAA) brought even more changes to the program. STURAA was enacted on April 2, 1987. Under this law, Section 105(f) of the 1982 STAA was replaced by Section 106(c) as the statutory authority for the DBE program. Section 106(c) required four basic changes to the DBE program:

- Women are to be presumed to be socially and economically disadvantaged individuals and, therefore, separate goals for DBEs and WBEs would no longer be permitted;
- In order to be an eligible DBE, a firm or group of firms controlled by the same individual cannot have average annual gross receipts over the preceding three fiscal years in excess of \$14 million, as adjusted by the Secretary of Transportation for inflation;
- DOT must establish uniform certification criteria for DBE firms; and
- Recipients are required to update their directories of eligible DBE firms annually, including the location of such firms.

On October 21, 1987, a final rule developed by the Office of the Secretary implementing Section 106(c) of the STURAA was published in the *Federal Register*. The final rule amended the existing DBE regulation (49 CFR 23) to include changes mandated by Section 106(c) and finalized several other changes that had been pending. Other changes included expanding the definition of "Hispanic" to include Portuguese and finalizing a change in the procedures for crediting the value of goods received from DBE suppliers toward DBE goals—raising the credit from 20 to 60 percent.

INCLUSION OF WBEs

With the addition of women as part of the presumptive group, retaining a two-goal system was no longer permissible. The legislative history of Section 106(c) clearly indicated that Congress intended DOT to adopt a one-goal system.

By memorandum dated August 26, 1987, the FHWA administrator informed each state that Section 106(c) did not allow separate DBE and WBE goals. Each state would be allowed to specify only a single DBE goal on future federal-aid contracts. This change became effective October 1, 1987.

A number of complaints have been received from WBEs and ethnic minorities claiming that the inclusion of WBEs in the definition of DBEs has resulted in one group receiving a disproportionate share of the work to the detriment of the other group. In several instances, inclusion of WBEs and designation of a single goal resulted in a disproportionate amount of work being obtained by WBEs. For example, on two large projects in Illinois (Dan Ryan expressway in Chicago and the Martin Luther King bridge in East St. Louis), WBEs accounted for approximately 65 percent of the DBE goal. This situation resulted in protests from the black contracting community and threats from the mayors of Chicago and East St. Louis to stop the projects unless black contractors received a larger share of the work.

On average, since implementation of Section 106(c), WBEs have gained an increasing share of the total DBE program.

Some states have attempted to offset any disproportionate effects of the single goal requirement by implementing some

remedial actions. These actions have included (a) maintaining separate goals on 100 percent state-funded projects to compensate for the disparity on single-goal federal-aid projects, (b) establishing higher contract goals to provide additional work for competing ethnic minority firms and women-owned firms, and (c) increasing the number of DBE set-aside contracts to provide additional contracting opportunities.

CERTIFICATION

In continuing the DBE program under Section 106(c), effective enforcement of eligibility requirements is a key part of ensuring that the program achieves its purpose. Keeping ineligible so-called "front" firms out is essential to maintaining the program's integrity and credibility.

As previously noted, Section 106(c) required DOT to establish minimum uniform criteria for the SHA to use in certifying DBEs for eligibility to participate in the federal-aid highway program. This criteria were included in DOT's final rule of October 21, 1987. Minimum certifying criteria include, but are not limited to, on-site visits, personal interviews, analysis of stock ownership, listing of equipment, analysis of bonding capacity, listing of work completed, resumes of principal owners, financial capacity, and type of work preferred.

Uniform certification criteria has had the following positive impacts on the DBE program:

- Decreased the paperwork burden on DBEs, and
- Helped eliminate so-called "fronts" by requiring verification of information.

In 1988, AASHTO's Special Committee on the DBE program released a special practices manual entitled *Guidelines for D/WBE Program Administration (I)*. This manual focuses on the results of a comprehensive survey, conducted by the committee, of critical methods and procedures in the administration of DBE programs. Suggestions are offered for what appear to be the most successful procedures on the basis of the committee's study of the overall program.

GOOD-FAITH EFFORT

STURAA did not include any provisions that would directly affect previous good-faith effort procedures. FHWA administrator R. A. Barnhart, in his memorandum of June 20, 1985, strongly urged states to implement a good-faith effort process and set realistic contract goals. Since this memorandum was issued, states have been encouraged to set realistically achievable contract goals and to establish a process that recognizes good-faith efforts to achieve such goals. A survey of SHAs revealed that at least 46 agencies use a contract award mechanism that recognizes good-faith efforts in meeting DBE contract goals.

A few states have expressed concerns about the subjective process of reviewing good-faith effort submissions that could lead to favoritism in awarding contracts. FHWA believes these concerns can be alleviated if realistic contract goals are established that can be met with legitimate DBEs.

DBE DIRECTORIES AND DBE SIZE RESTRICTIONS

These requirements have had minimal impact on the DBE program. Most states previously had DBE directories. FHWA has encouraged states to specify, during the annual updating of their DBE directories, the geographical areas where DBEs prefer to work.

The purpose of revising the size restriction is to ensure that the DBE program meets its objective of helping small minority and women-owned businesses become self-sufficient by graduating those firms that have average annual gross receipts of more than \$14 million over a 3-year period. The \$14-million ceiling includes revenues of all affiliates of the firm owned and controlled by the same individuals as well as that of the firm itself. In order to monitor this requirement properly, each state had to evaluate its DBE certification requirements. In this way, SHAs would ensure that adequate information is being collected to make this determination. However, the size restriction affected only a small number of firms.

On February 14, 1990, a notice was published by the Secretary of Transportation in the *Federal Register* adjusting the \$14-million ceiling for inflation to \$14.65 million.

CREDIT FOR MATERIAL SUPPLIERS

DOT's final rule permits 60 percent of the value of goods purchased from DBE regular dealers to be counted toward a contractor's or recipient's goal. The previous allowable amount was 20 percent. A regular dealer has been defined as a firm that owns, operates, or maintains a store, a warehouse, or

other establishment in which the materials or supplies required for the contract are bought, kept in stock, and regularly sold to the public. Dealers in bulk items such as steel, cement, gravel, and petroleum products are not required to maintain the items in stock, but they must own or operate distribution equipment.

This increase in allowable percentage should encourage a larger number of minority and women material suppliers to seek certification. DOT is planning to reevaluate the 60 percent value after several years to determine if further adjustment is necessary. The final rule also allows credit for fees and commissions earned by suppliers and haulers, who are not regular dealers, provided the amounts paid are customary in the industry.

PROGRAM IMPACTS

In recent years, the highway construction industry including both governmental agencies (i.e., FHWA, SHAs, and AASHTO) and the contracting industry [i.e., Associated General Contractors (AGC)] have undertaken several studies to assess the impact of the FHWA's DBE program on the federal-aid highway construction program. Emphasis has been on the impact of the 1982 and 1987 acts and their 10 percent goal requirements. The studies basically have concluded that the program has had and will continue to have a significant impact on the construction industry. However, the exact level or extent of the impact remained a matter of interpretation under each of the studies.

The single most prominent positive impact has been the increase in the number and dollar amount of awards to ethnic

TABLE 1 MBE AND WBE ACHIEVEMENTS AND PERCENT OF PARTICIPATION IN THE FEDERAL-AID HIGHWAY PROGRAM

FISCAL YEAR	NO. OF CONTRACT AWARDS	AWARD AMOUNT (\$1,000)	PERCENT OF TOTAL PROGRAM
1976	702	\$63,800	----
1977	751	\$71,530	----
1978	1,200	\$126,090	----
1979	1,574	\$163,700	----
1980	1,963	\$281,940	3.4
1981	5,602	\$520,081	6.1
1982	7,201	\$653,151	8.3
1983	10,952	\$974,688	8.8
1984	17,291	\$1,564,471	16.8
1985	19,359	\$1,585,417	14.1
1986	18,753	\$1,526,362	14.0
1987	16,441	\$1,525,722	14.7
1988	14,914	\$1,586,991	14.9
1989	14,277	\$1,571,889	14.4

minority and women-owned businesses presented in Table 1. The negative aspects are somewhat dependent on the source of data, but generally there has been some increase (amount not known) in the overall cost of contract administration and construction. Also, nonminority contractors in the specialty construction trades have been most singularly affected. The impact of FHWA's DBE program on the federal-aid highway program since 1976 is also presented in Table 1. The award amounts shown are the federal-aid funds only.

The figures represent the level of participation by minority and women-owned businesses in the years up to 1987, and since 1987 the amount of DBE participation in the federal-aid highway construction program. From these figures, the level and percentage of ethnic minority and women-owned businesses involvement significantly increased after passage of the 1982 STAA with the introduction of the 10 percent goal level.

SANCTIONS

Much of the focus has been on the certification process as the primary means of identifying DBE fronts and frauds and ensuring the integrity of the DBE program. Another significant area of concern must be the use of certifiable DBE firms by non-DBE prime contractors as pass-throughs in which the DBEs fail to perform any meaningful functions. Imposing

sanctions on a DBE through certification measures is not an effective means of controlling this kind of program abuse.

The lack of prosecution by the U.S. Department of Justice (DOJ) of discovered irregularities continues to frustrate many investigative bodies, e.g., the Office of Inspector General. Lack of prosecution appears to result from the need to focus limited DOT or DOJ resources in other areas such as bid rigging.

Civil sanctions at the state level, more particularly contract administration remedies, appear to offer much greater potential for swift and equitable treatment of DBE program abuse. Contract remedies that are most commonly used are assessment of monetary penalties, withholding progress payments, suspension of work, and disqualification from bidding for a specific time period.

Improved contract administration and increased reliance on administrative sanctions at the state level rather than criminal prosecutions are the most effective ways of controlling abuse of contract requirements.

REFERENCE

1. Guidelines for D/WBE Program Administration. AASHTO, Washington, D.C., 1988.

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