



U.S. House of Representatives
Committee on Transportation and Infrastructure

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March 25, 2009

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SUMMARY OF SUBJECT MATTER

TO: Members of the Committee on Transportation and Infrastructure

FROM: Committee on Transportation and Infrastructure Staff

SUBJECT: Hearing on "The Department of Transportation's Disadvantaged Business Enterprises Program"

PURPOSE OF HEARING

On Thursday, March 26, 2009, at 11:00 a.m., in room 2167 Rayburn House Office Building, the Transportation and Infrastructure Committee will meet to receive testimony regarding the Department of Transportation's Disadvantaged Business Enterprises Program.

BACKGROUND

The U.S. Department of Transportation's (DOT) Disadvantaged Business Enterprises (DBE) program was established through a series of legislative initiatives to remedy past and current discrimination against minority and women-owned businesses to ensure that they are provided equal opportunity to compete for DOT-assisted highways, transit and airport contracts.

First established by regulation in 1980 as a minority and women's business enterprise program, pursuant to Title VI of the "Civil Rights Act of 1964" and other nondiscrimination statutes applicable to DOT financial assistance programs, the DBE program was later statutorily authorized in 1983 by the "Surface Transportation Assistance Act of 1982" (P.L. 97-424), primarily to aid small businesses owned and controlled by socially and economically disadvantaged individuals in the highway and transit programs.¹

In 1987, Congress passed the "Surface Transportation and Uniform Relocation Assistance Act of 1987" (P.L. 100-17), and the "Airport and Airway Safety and Capacity Expansion Act of

¹ DBE programs for women-owned businesses and the DOT's airport program continued under the original 1980 regulations. See 64 Fed. Reg. 5096 (Feb. 2, 1999).

1987” (P.L. 100-223), which expanded the statutory DBE program to include airports, airport concessions and women-owned businesses.² In 1991, Congress reauthorized the highway/transit DBE programs and, in 1992, amended the airport DBE program to include management contracts and suppliers of goods and services.³ The DBE program for highways and transit has since been reauthorized in successive surface transportation statutes.⁴

I. What is a DBE?

A firm (and its minority and women owners) seeking certification as a DBE must meet: (1) an ownership and control test, (2) a personal net worth test, and (3) a size standard.⁵ For eligibility purposes, a DBE is defined as a small for-profit business where socially and economically disadvantaged individuals own at least 51 percent of the economic interests of the entity and also control and manage the business operations of the firm.⁶ Minorities and women are presumed to be socially disadvantaged (although that presumption is rebuttable).⁷ Others may qualify as socially disadvantaged on a case-by-case basis.⁸

To be regarded as economically disadvantaged, an individual must, among other things, have a personal net worth (PNW) that does not exceed \$750,000, excluding the equity in the individual’s primary residence and the value of their ownership interest in the firm seeking certification.⁹ Individuals seeking an Airport Concessions Disadvantaged Business Enterprises (ACDBE) certification may exclude other assets that the individual can document are necessary to obtain financing or a franchise agreement for the initiation or expansion of his or her ACDBE firm (or have in fact been encumbered to support existing financing for the individual’s ACDBE business), up to a maximum of \$3 million.¹⁰

As to size, to be eligible as a DBE, a business must be an existing small business (as defined by the SBA) and must not have average annual gross receipts over the firm’s previous three fiscal years, in excess of \$22.41 million.¹¹

² Note that the airport DBE program is codified in statute and does not have to be specifically reauthorized in the same manner as the surface transportation DBE program.

³ See “The Intermodal Surface Transportation Efficiency Act of 1991” (P.L.102-240), and the “Airport and Airway Safety, Capacity, Noise Improvement, and Intermodal Transportation Act of 1992” (P.L. 102-581). For the airport concessions program, this statutory change permitted the value of contracts with, or of goods procured from, certified DBE firms to be counted toward DBE participation goals.

⁴ See the “Transportation Equity Act for the 21st Century” (TEA-21) (P.L. 105-178), and the “Safe, Accountable, Flexible, Efficient Transportation Equity Act: A Legacy for Users” (SAFETEA-LU) (P.L. 109-59).

⁵ 49 C.F.R. §§ 26.61-26.73 (2008).

⁶ 49 C.F.R. § 26.69 (2008).

⁷ For purposes of the DBE program, ethnic minorities include: Black Americans, Hispanic Americans, Native Americans, Asian-Pacific Americans, Subcontinent Asian Americans or other minorities found to be disadvantaged by the Small Business Administration (SBA). 49 C.F.R. § 26.67 (2008).

⁸ 49 C.F.R. § 26.67(d) (2008).

⁹ 49 C.F.R. § 26.67(a)(2)(ii) (2008). The \$750,000 number was originally set by the SBA in 1989 and then borrowed by DOT and applied to the surface transportation and airport contracting programs in 1999, and airport concessions in 2005.

¹⁰ 49 C.F.R. § 23.3 (2008).

¹¹ See DOT Final Rule: Disadvantaged Business Enterprise Program; Inflationary Adjustment (signed March 24, 2009)(to be published in the Federal Register).

II. How does the DBE program work?

Congress has established a national 10 percent aspirational participation goal for firms certified as DBEs with respect to surface transportation programs, airport federally-assisted contracting (i.e., procurement, construction, or professional services contracts), and airport concessions.¹²

DOT regulations require recipients of federal financial assistance (i.e., state and local transportation agencies and airport operators) that anticipate awarding prime contracts of more than \$250,000 to establish an annual aspirational DBE participation goal that reflects what DBE participation would be in the absence of discrimination.¹³ Recipients must base their goals on how to achieve a level playing field in their individual programs, regardless of the 10 percent national goal.¹⁴ These goals must be based on demonstrable evidence of the availability of ready, willing, and able DBEs relative to the DOT-assisted contracts that will be let that fiscal year (“FY”).¹⁵ It is important to note that a recipient’s goal is aspirational only; quotas and set-asides are generally not permitted.¹⁶ In addition, DOT does not assess penalties for not meeting DBE goals as long as good faith efforts are made.¹⁷

Importantly, recipients are required to use race-neutral means (i.e., without application of any criteria that favor DBEs over non-DBEs) to meet as much of their overall goal as possible. Examples of race-neutral means include: providing assistance in overcoming issues such as the inability to obtain bonding or financing; unbundling large contracts to make them more accessible to small businesses; informational and communication programs on contracting procedures and specific contract opportunities; and other business support services.¹⁸

If a recipient is unable to meet its overall DBE participation goal through race-neutral means, then the recipient must establish contract goals (which are deemed race conscious) for DBE participation.¹⁹ This means that the recipient has determined that without the use of race-conscious measures, the level playing field could not be achieved. An example of how DBE goals might be set:

[S]uppose Recipient X establishes an 11 percent overall goal for Fiscal Year 2000. This is the amount of DBE participation X has determined it would have if the playing field were level. Recipient X projects that, using a combination of race-neutral means, it can achieve 5 percent DBE participation. Recipient X then sets contract goals on some of its contracts throughout the year to bring in an additional 6 percent DBE participation.²⁰

¹² See §1101(b) of SAFETEA-LU; 49 U.S.C. §§ 47107(e), 47113 (2009).

¹³ Federal Transit Administration (FTA) or Federal Aviation Administration (FAA) recipients who reasonably anticipate awarding \$250,000 or less in prime contracts in any fiscal year are not required to develop overall DBE goals.

¹⁴ See 64 Fed. Reg. 5107 (Feb. 2, 1999).

¹⁵ DOT, in its regulations, details the type of evidence that can be used as a basis for setting goals, including: DBE Directories and Census Bureau Data, bidder’s lists, disparity studies, goals used by another recipient in similar circumstances and other alternative methods. See 49 C.F.R. § 26.45 (2008).

¹⁶ Note that DOT’s regulations do allow “set-asides” only in “limited and extreme circumstances . . . when no other method could be reasonably expected to redress egregious instances of discrimination.” 49 C.F.R. § 26.43 (2008). Neither set-asides nor quotas are permitted in the airport concessions program. 49 C.F.R. § 23.61 (2008).

¹⁷ 49 C.F.R. §§ 26.41, 26.47 (2008).

¹⁸ 49 C.F.R. § 26.51 (2008).

¹⁹ *Id.* However, contract goals may only be used for those DOT-assisted contracts that have subcontracting possibilities.

²⁰ See 64 Fed. Reg. 5112.

In addition, recipients of DOT financial assistance are required to establish a Unified Certification Program (UCP).²¹ The purpose of a UCP is to ensure that DBEs and applicants (including airport concessionaires) will have "one stop shopping" on certification matters with respect to every recipient in the state. If a business wants to be certified as a DBE, it must submit an application to the UCP for approval. A determination as to whether a firm meets the DBE criteria will be made through various means, including on-site visits, personal interviews, reviews of licenses, stock ownership, equipment, bonding capacity, work completed, resume of principal owners, financial capacity, and type of work preferred.²² Once a DBE is certified through the UCP, that certification must be honored by all recipients of DOT funds within the state; as opposed to having the DBE apply separately to each recipient with which it wants to work.²³

The DOT also has counting rules to ensure that recipients have a mechanism to verify that the work committed to a DBE at contract award is actually performed by the DBE, as well as to have appropriate mechanisms to ensure compliance with the program.²⁴ Each recipient must report to DOT semi-annually on DBE commitments and achievements for the previous 6 months and then the full year. If the actual achievements of a particular contractor's, or a recipient's, program, falls short of commitments, DOT views this as an indication that corrective action should be taken to improve program performance.²⁵ As noted above, DOT does not sanction recipients if they fall short of their overall DBE participation goal, unless the recipient has not administered its DBE program in good faith.²⁶

III. The Impact of Federal Case Law on DOT's DBE Program

In 1995, the U.S. Supreme Court's decision in *Adarand v. Peña (Adarand)*,²⁷ a contracting case dealing with the expenditure of DOT funds in the state of Colorado, set forth constitutional requirements for race and/or gender conscious contracting programs established by Congress and implemented by the DOT. The Court held that race-conscious programs were subject to a "strict scrutiny" standard of legal review. The Court stated that strict scrutiny involves a two-part analysis. First, to enact a race-conscious program, the government must have a "compelling governmental interest." Second, the Court stated that combating discrimination was a compelling interest, but race-conscious programs could only be used if they are "narrowly tailored."²⁸

It should be noted that the 1995 *Adarand* decision did not specifically determine the constitutionality of any affirmative action or government DBE program (including the DOT's DBE

²¹ 49 C.F.R. § 26.81 (2008). Recipients (i.e., state DOTs and airports and transit properties that receive funds directly from FAA or FTA) must commit in writing to participate.

²² 49 C.F.R. § 26.83 (2008).

²³ States are required to annually survey and compile a list of small and socially and economically disadvantaged business concerns within the State, and submit this list to DOT.

²⁴ See, generally, 49 C.F.R. §§ 26.37, 26.55 (2008).

²⁵ See DOT Official Questions and Answers DBE Program Regulation (49 CFR 26) (Updated Feb. 19, 2009), <http://osdbu.dot.gov/dbeprogram/dbeqna.cfm>.

²⁶ 49 C.F.R. § 26.47 (2008).

²⁷ 515 U.S. 200 (1995).

²⁸ On remand following the Court's decision in *Adarand v. Peña*, the U.S. Court of Appeals for the Tenth Circuit noted that factors to be considered regarding whether the DOT DBE program is "narrowly tailored" include: (1) the availability of race-neutral alternative remedies; (2) limits on the duration of the [DBE] certification programs; (3) flexibility; (4) numerical proportionality; (5) the burden on third parties; and (6) over-or under-inclusiveness. See *Adarand Constructors v. Slater*, 228 F.3d at 1147, 1178 (10th Cir. 2000).

program at issue in the case).²⁹ In response to the Court's decision in *Adarand*, however, the Clinton Administration undertook a review of all federal programs using race or gender as a basis for decision making. In 1998, Congress reauthorized the DBE program for surface transportation programs in TEA-21. In 1999, the DOT finalized new rules for the DBE program designed to meet the requirements of strict scrutiny and, in 2005, new rules for the ACDBE program were issued.³⁰ Circuit courts that have considered the constitutionality of the DOT DBE program since the rules were re-written have upheld the program against facial challenges.³¹

Although not a case reviewing the DOT's DBE program, there has been a recent ruling by the United States Court of Appeals for the Federal Circuit in *Rothe Development Corp. v. Dept. of Defense* (*Rothe*) declaring the Department of Defense's (DOD) 1207 Program, which is one of the programs that the DOD uses to meet its SBA goals, unconstitutional because "Congress did not have before it, at the time of the 2006 reenactment of Section 1207, a 'strong basis in evidence' for the proposition that DOD was a passive participant in racial discrimination in relevant markets across the country and that therefore race-conscious measures were necessary."³² The *Rothe* court's application of strict scrutiny in evaluating the DOD minority business program may have implications for other Federal agencies in the event of future litigation.

However, one court decision that impacted how the DOT DBE program is applied is *Western States Paving v. Washington State Department of Transportation*.³³ In this case, the United States Court of Appeals for the Ninth Circuit (9th Circuit) held that the federal DBE program was facially constitutional, but that the Washington State DOT DBE program was unconstitutional "as applied," because the Washington State DOT had not narrowly tailored the program by ensuring that it had sufficient statistical evidence to target its remedial measures. As a result of this decision, the DOT advised recipients located in the 9th Circuit to use all race-neutral goals, pending the completion of studies to assist in narrowly tailoring the use of race-conscious goals. This has negatively impacted DBE participation in those states.³⁴

For example, the FAA has compiled statistics regarding the airport DBE program following the ruling in *Western States*, which demonstrate that DBE participation was generally lower when only race-neutral means were used.³⁵ FAA collected data from airports located in 9th Circuit States for which numbers were available in both 2004 (the last year before race-conscious measures were discontinued) and 2007 (the most recent year for which data have been compiled and only race-neutral means were used). Twenty eight of those airports had race-conscious components in their 2004 goals, but had no race-conscious components in their 2007 goals. Of these 28 airports, FAA found that 18 (64 percent) had DBE participation that was significantly lower in percentage terms, in 2007 than in 2004.

²⁹ The case was remanded back to the lower courts and the program was ultimately upheld as constitutional in 2000 by the 10th Circuit in *Adarand Constructors v. Slater*. *Id.* at fn. 28.

³⁰ See 64 Fed. Reg. 5096 (Feb. 2, 1999); 70 Fed. Reg. 14508 (Mar. 22, 2005).

³¹ See, e.g., *Sherbrooke Turf Inc. v. Minn. DOT.*, 345 F.3d 964 (8th Cir. 2003); and *Northern Contracting, Inc. v. State of Illinois*, 473 F.3d 715 (7th Cir. 2007). A facial challenge is a challenge that the law is unconstitutional on its face, as opposed to unconstitutional in its application.

³² 545 F.3d 1023 (Fed. Cir. 2008).

³³ *W. States Paving Co., Inc. v. Wash. State DOT*, 407 F.3d 983 (9th Cir. 2005).

³⁴ Note that some of the recipients have completed the requisite studies and are once again using both race-neutral and race-conscious means to meet DBE aspirational program goals.

³⁵ FAA response to Chairman Costello question for the record on the DBE program (March 17, 2009); Hearing on the FAA Reauthorization Act of 2009 before the H. Subcomm. on Aviation, 111th Cong. (Feb. 11, 2009).

Airport	DBE Achievements 2004 (%)	DBE Achievements 2007 (%)
Anchorage, AK	6.9	0
Kodiak, AK	11.5	22.3
Palmer, AK	2.8	47.3
Page, AZ	20.2	0.8
Ryan Airfield, AZ	12.9	13.2
Tucson, AZ	7.0	0.8
San Francisco, CA	33.0	34.5
Fresno, CA	8.7	7.8
Palm Springs, CA	6.1	0.9
Santa Barbara, CA	2.1	0.5
Contra Costa, CA	3.6	5.4
County of San Diego, CA	6.9	4.6
Ventura, CA	10.5	40.6
San Diego County Regional, CA	11.3	4.6
Honolulu, HI	66	0
State of Hawaii	22	0
Friedman Memorial, ID	1.7	0
Gooding, ID	7.7	6.4
Pocatello, ID	9.9	15.8
Lemhi County, ID	44.2	1.9
Bert Mooney, MT	4.6	16.8
Missoula, MT	8.9	4.6
Sanders County, MT	4.1	4.8
Sidney Richland, MT	0.2	1.0
Reno Stead, NV	5.2	0
State of Nevada	10.1	8.9
Klamath Falls, OR	0.9	0.4
Portland, OR	27.9	2.0

Source: FAA, 2009.³⁶

³⁶ According to the FAA, DBE achievements are expressed in percentages of FAA financial assistance used in contracting.

In addition, the Federal Highway Administration has compiled similar data, as shown below.

State DOT	DBE Achievements 2004 (%)	DBE Achievements 2007 (%)
Alaska	6.70	8.20
Arizona	9.6	3.77
California ³⁷	10.4	6.6
Hawaii	9.0	2.0
Idaho ³⁸	4.35	14.79
Montana	5.38	5.09
Nevada ³⁹	4	0.11
Oregon	12.80	10.60
Washington	9.7	Contract goals were suspended for only one year (2005 – 2006). During that time, DBE participation was 3.6%. Upon completion of its study, goals were reinstated in 2007.

Source: DOT, Federal Highway Administration, 2009.

This recent evidence illustrates the importance of, and the continuing need for, the DBE program to ensure that minority and women-owned businesses have an opportunity to bid on DOT-assisted contracts.

³⁷ The DOT states that according to the California DOT Disparity Study (which covered 2002 – 2006), the use of DBEs on federally-assisted contracts was 9 percent from 2002 – April 1, 2006 and dropped to 4.9 percent from May – December 2006.

³⁸ According to the DOT, the FY 2007 participation number is not based on DBE participation achieved through entirely race-neutral means. It includes multiyear contracts with pre-existing DBE contract goals. The DOT notes that according to the Idaho DOT Disparity Study, DBE participation reported at 7.3 percent for the period 2002 – January 2006; DBE participation reported at 4.9 percent for the period February 2006 – December 2006.

³⁹ The DOT states that according to the Nevada DOT Disparity Study, DBE participation reported at 4 percent for the period October 1999 – September 2005; DBE participation reported at 1.3 percent for the period October 2005 – 2006.

WITNESSES

MEMBER PANEL

The Honorable James E. Clyburn
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PANEL I

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