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MEMORANDUM

May 9, 2012

To: The City of Charlotte, NC

Attn: Robert E. Hagemann
City Attorney

Cynthia L. White
Senior Assistant City Attorney
City of Charlotte, North Carolina

From: Franklin M. Lee, Esquire
Tydings & Rosenberg LLP

Re: The Adequacy of the Evidentiary Basis for Charlotte's Consideration of Race-Conscious Remedial Policies for Application to City Contracting and Procurement

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I. Introduction

Our law firm has been retained by the City Attorney's Office to review the methodology, findings, and policy recommendations of MGT of America, Inc. ("MGT") as reflected in its September 26, 2011, Disparity Study Update for the City of Charlotte ("Study Update"), and based upon that review, to offer an independent opinion regarding the adequacy of the evidentiary basis for the City's consideration of race-conscious remedial policies that might be appropriately applied to the City's contracting and procurement procedures. In addressing this core issue, we have been requested to also address questions raised by the City-appointed Disparity Study Advisory Committee regarding the conclusions and policy recommendations of MGT.

In undertaking this task, we have framed the issues to be addressed in Section II of this memorandum. In providing answers to these questions, Section III of this memorandum references supporting evidence, while also presenting a thorough discussion of key areas of agreement and disagreement with MGT's stated conclusions and policy recommendations, as well as special considerations for drafting remedial policies in a manner that maximizes effectiveness and minimizes legal risks. Finally, Section IV of this memorandum broadly

outlines our final conclusions and recommendations regarding a legally defensible array of appropriately narrowly-tailored policy options for the City's consideration.

II. Issues Presented

In order to justify its consideration and adoption of a race-conscious measure to remedy discrimination that affects public contracting, a local government must "identify that discrimination, public or private, with some specificity," and must satisfy a "strict scrutiny" standard under the Equal Protection Clause of the 14th Amendment by having a "strong basis in evidence for its conclusion that remedial action is necessary." Moreover, any race-conscious remedies adopted by the government must be "narrowly tailored" to address the identified discrimination. *City of Richmond v. J. A. Croson*, 488 U.S. 469, 504 (1989); *Wygant v. Jackson Bd. Of Educ.*, 476 U.S. 267, 277 (1980); and see also *H.B. Rowe, Inc. v. Tippett*, 615 F.3d 233 (4th Cir. 2010). Although gender-conscious measures to remedy the effects of gender discrimination are subjected to a somewhat lesser standard of "intermediate scrutiny" wherein the local government must demonstrate an "exceedingly persuasive justification" for such remedial policies,[1] as a practical matter, given the lack of guidance in the case law regarding the degree to which a lesser quantity and quality of evidence may be required to satisfy the intermediate scrutiny standard, an assumption that gender-conscious policies will be subjected to a similarly rigorous standard of review as is required under strict scrutiny has served as the basis for the Study Update's methodology and findings regarding evidence of gender discrimination.

Accordingly, for purposes of this review, the key issues that are presented en route to making a determination regarding the adequacy of the evidentiary basis for the City's consideration of race- and/or gender-conscious remedial policies are as follows:

A. Does the Study Update present a strong basis in evidence of ongoing effects of race- and gender-based discrimination in the Charlotte marketplace sufficient to support consideration of race- and/or gender-conscious remedies by the City?

B. Which, if any, race- and gender-neutral policy options recommended by MGT are appropriately narrowly tailored to address identified ongoing effects of discrimination?

C. What, if any, additional race- and gender-neutral policy options are appropriately narrowly tailored to remedy ongoing effects of discrimination?

D. What, if any, race- and/or gender-conscious policy options are appropriately narrowly tailored to more fully remedy ongoing effects of discrimination?

III. Discussion

A. Defensibility of MGT's Study Update Methodology

For purposes of this memorandum, we assume the Study Update provides the evidentiary basis and factual predicate upon which the City's remedial policies will be evaluated. The strength of that evidence is directly tied to the legal sufficiency of MGT's study methodology and data sources as measured against controlling legal authority. Chapter 2.0 of the Study Update

[1] *See United States v. Virginia*, 518 U.S. 515, 531 (1996).

thoroughly and appropriately summarizes the legal framework against which the strength of the evidence is to be evaluated. MGT's stated methodologies for the Study Update[2] are all appropriate and mostly in keeping with controlling legal precedents and industry standards for disparity studies. At times, preferred methodologies cannot be employed due to the inadequacy or unavailability of data sources. In such situations, the best available methodology and data is substituted, leaving open the question as to whether the resulting evidence and findings are sufficiently strong to warrant reliance upon them in drafting public policy. The answers to the questions presented in Section II largely rest upon the totality of the evidence gathered pursuant to the appropriate methodologies used by MGT in the Study Update. A full discussion of this evidence follows.

B. The Study Update Presents a Strong Basis in Evidence of Ongoing Effects of Race- and Gender-Based Discrimination Sufficient to Support the City's Consideration of Race- and Gender-Conscious Remedial Policies

The Study Update presents a compelling combination of statistical and anecdotal evidence of ongoing affects of marketplace discrimination that is sufficient to satisfy the "strong basis in evidence" standard under "strict scrutiny."

Disparity Evidence

The foundation of the statistical analysis is disparity ratios that compare the availability of M/WBE firms, by industry, within the relevant geographic market, to the utilization of such firms ("utilization" is defined as payments by the City to M/WBE prime contractors, and as payments by prime contractors to M/WBE subcontractors). MGT has defined the relevant geographic market for its statistical analysis as the Charlotte-Gastonia-Salisbury Combined Statistical Area ("CSA").[3]

MGT relied upon a "custom census" methodology in estimating the availability of M/WBE construction prime contractors, M/WBE construction subcontractors, and M/WBE A&E sub-consultants.[4] The custom census methodology was based on an independent survey of firms from the Charlotte CSA that were contained in a Dun & Bradstreet database. For all other industry segments (i.e., A&E prime consultants, professional services firms, other services firms, and goods and supplies firms), MGT calculated availability estimates based upon U.S. Bureau of

[2] MGT's stated methodologies for: (a) defining the relevant geographic for the Study Update, (b) measuring availability of ready, willing, and able minority- and women-owned businesses ("M/WBEs") in that relevant market that supply the goods and services the City is purchasing, (c) measuring the relative utilization of M/WBEs, (d) calculating disparity indices reflecting substantial and statistically significant underutilization of M/WBE firms, (e) collecting evidence of private sector discrimination and its nexus with public sector contracting, and (f) collecting anecdotal and qualitative evidence that identifies the existence and nature of discriminatory barriers adversely affecting M/WBE participation, are all founded upon guidance gleaned from the case law summarized in considerable detail in Chapter 2.0 wherein disparity studies were subjected to strict scrutiny by reviewing courts.
[3] See Study Update at p. 3-19.
[4] The custom census methodology approach was successfully relied upon by MGT in the *H.B. Rowe v. Tippett* case involving the North Carolina Department of Transportation's M/WBE program. This methodology has also been successfully relied upon in cases such as *Concrete Works v. City and County of Denver* and *Northern Contracting v. Illinois DOT.*

the Census 2007, Survey of Business Owner data.[5]

To determine MBE utilization during the study period, MGT gathered payment data from City hard copy and electronic files, and also from SBE reports maintained by Charlotte's Small Business Office. The percentage of total payment dollars that were paid to MBE firms is referred to as the MBE utilization figure.

To calculate disparity indexes for each industry segment, and for each ethnic and gender classification of firms, MGT compared the relevant availability estimate (i.e., the MBE percentage of all firms that were ready, willing, and able to provide to the City goods or services within that industry category), to the percentage of total dollars that were paid to a particular ethnic category of MBE firms over the course of the five-year study period (MBE utilization). In keeping with legal precedent and industry standards, to the extent the disparity ratio reflected that utilization of the MBE firms in an industry category was only 80% or less than their share of availability, MGT characterized such disparities as "substantial", and where feasible, then calculated t-test statistics to determine whether such substantial disparities were statistically significant. Where there is substantial disparity that is statistically significant, there is a 95% confidence level that the disparity was not the result of chance, and therefore there is a legal inference that discrimination has occurred.[6]

The Study Update's disparity analysis established that, over the past five years, there was substantial and statistically significant disparity in the underutilization of certain classifications of MBE firms in the following industry segments within the relevant marketplace[7]:

- Construction Subcontracting (African American, Hispanic American, and Native American firms)
- Architectural & Engineering Sub-consulting (African American firms)

The Study Update's disparity analysis also established that there was substantial disparity of unknown statistical significance in the underutilization of certain classifications of MBE firms in the following industry segments within the relevant marketplace:

- Construction Prime Contracts (African American, Hispanic American, Native American, and Non-minority Women-owned firms)

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[5] While not the preferred method of estimating availability in the most recent cases, the use of U.S. Census data was approved by the Third Circuit Court of Appeals in the case of *Contractors Association of Eastern Pennsylvania, Inc. v. City of Philadelphia*, 739 F. Supp 227, 6 F.3d 990 (3rd Cir. 1993). However, as MGT notes in the Study Update, U.S. Census measures of availability tend to be somewhat lower than those resulting from the custom census methodology. Accordingly, any disparities identified using the U.S. Census measure of availability may likely be somewhat understated as compared to those that would be identified using the preferred custom census approach. *See* discussion by Dr. Vince Eagan, October 11, 2011, Disparity Study Advisory Committee meeting minutes at pp. 1-2.

[6] See *Connecticut v. Teal,* 457 U.S. 440 (1982); *Contractors Association of Eastern Pennsylvania, Inc.*, 91 F.3d at 603. See also Study Update at p. 4-2. Where there is substantial disparity of unknown statistical significance, a number of courts have nonetheless established an inference of discrimination. However, such inferences are stronger where statistical significance at the 95% level can be demonstrated.

[7] Study Update at pp. 4-2 to 4-20, and pp. 7-2 to 7-3.

- Architectural & Engineering Prime Contracts (African American, Hispanic American, Native American, and Non-minority Women-owned firms)

- Professional Services Prime Contracts (Asian American and Non-minority Women-owned firms)

- Other Services Prime Contracts (Hispanic American, Asian American, and Non-minority Women-owned firms)

- Goods and Supplies Prime Contracts (African American, Asian American, and Non-minority Women-owned firms)

Anecdotal Evidence

This disparity evidence is just the beginning of the strong basis in evidence that supports the City's consideration of narrowly tailored race-conscious remedies. Multiple forms of anecdotal evidence complement the disparity evidence by helping to identify the form and nature of barriers that have resulted in the statistical disparities, and by suggesting explanations for the manner in which discrimination may have affected market outcomes.[8] The four distinct methodologies used by MGT for collecting anecdotal evidence in the Study Update included focus groups with 29 participants[9], personal interviews of 54 randomly selected business owners and City vendors selected from MGT's Master Vendor Database,[10]survey results from 155 respondents to a survey of 502 randomly selected vendors and contractors,[11]and a public hearing with 19 witnesses providing testimony.

The robust body of anecdotal evidence obtained through these multiple methodologies established several common themes in identifying recognized forms of marketplace discrimination that is adversely affecting the ability of M/WBE firms attempting to do business on City of Charlotte contracts. In some instances, alleged discrimination has been directly attributed to the City. In other instances, many forms of private sector discrimination and prime contractor discrimination have been identified that could undermine the ability of M/WBEs to be competitive in bidding on City contracts. Key findings[12] from this anecdotal evidence include the following:

- 70 M/WBE survey respondents (nearly 15% of M/WBEs surveyed) stated that the City had unnecessarily restrictive contract specifications in its bids and requests for proposals.[13]

- A non-minority female owner of a services firm stated in a focus group that her firm had received a Letter of Intent on a project and did not get the contract. She also stated that

[8] *Croson*, 489 U.S. at 509; *H. B. Rowe* at p. 15 and 17.
[9] Study Update at pp. 6-4 and 6-11.
[10] Id. at p. 6-11.
[11] Id. at p. 6-16
[12] Study Update at p. 7-14 to 7-16; see also pp. 6-12, 6-15, 6-16, and 6-19 to 6-21.
[13] Study Update at p. 6-12.

because of her reputation, other agencies outside of the City called her to bid on projects, but that she is unable to get anyone in the City to call her for bids.[14]

- An African American specialty trade contractor stated in a focus group that when the City's M/WBE program ended and the SBO Program started he stopped getting calls or any notifications of bid opportunities.[15]

- A non-minority female construction company owner stated that one of the City inspectors did not like her firm. The inspector modified the plans and instructed her firm to follow the changed plans. When the project was complete, the City said that the work was not correct as it was not in accordance with the original plans and that they did not instruct her to make those changes.[16]

- A non-minority female owner of a professional services firm stated that while construction bids only have a number (i.e., "price") attached to them, professional services contract awards with the City are based on the prequalification information and your pre-qualification is based on the amount of previous business you have done with the City. Since she cannot get prequalified, she does not spend the money responding to RFPs. She also stated, "In the end, it is going to be the same ones selected."[17]

- Several survey questions addressed discrimination and disparate treatment of vendors. The most notable responses involved firms being used for projects governed by the SBO program, but not elsewhere, being included on a bid for good faith efforts requirements and then being dropped after contract award, and being excluded from contract opportunities by an informal network of firms. Key survey findings include the following:

    - 134 M/WBE survey respondents (over 33%) affirmed that while they were used when SBE goals were applied, they seldom, or never were solicited for other contracts;

    - 103 M/WBE survey respondents (over 25% of M/WBE respondents) affirmed the existence of an informal network that excluded firms from participating in contracts;

- 76 M/WBE survey respondents (nearly 19% of M/WBE survey respondents) stated their firms were included with bids by prime contractors and were then subsequently dropped after contract award;

- 45 M/WBE survey respondents (over 11% of M/WBE respondents) stated that their firms had experienced discrimination in the private sector; 37 M/WBE survey respondents (over 9% of M/WBE respondents) expressed that their firms had experienced bid shopping (i.e., a practice wherein a prime solicits a price from a prospective sub solely for purposes of sharing it with a favored subcontractor and allowing that favored sub to

[14] Id. at p. 6-16
[15] Study Update at p. 6-19.
[16] Id. at p. 6-15.
[17] Id. at p. 6-15.

get the work if it is willing to meet the prospective sub's price); 29 M/WBE survey respondents (over 7% of M/WBE respondents) expressed that they had experienced unequal treatment in the course of bidding on and performing contracts; 25 M/WBE survey respondents (over 6% of M/WBE respondents) stated that their firms had experienced unfair denial of contract awards; 22 M/WBE survey respondents (over 5 % of M/WBE respondents) stated that they had experienced being subjected to double standards in their performance of contracts; and 22 M/WBE survey respondents (over 5% of M/WBE respondents) stated that their firms had experienced discrimination as a prime contractor bidding or proposing on Charlotte projects.[18]

- An African-American specialty trade contractor stated that the prime will squeeze your price, and that they are just asking minority firms to fill out paperwork, and then give the work to someone else.[19]

- An Hispanic American "other services" firm stated that primes used his firm's name at bid time as a subcontractor, but did not award the work to his firm. He went on to state that the prime never called to let us know they were listed for $300,000. The firm went on to say, "I never gave them a bid and I never did the work."[20]

- An African American specialty trade contractor stated that he had a Letter of Intent signed, the contract negotiated, and then the prime went with someone else.[21]

- An African American "other services" firm owner stated that we (minority business owners) are in the same spot ten years ago when it came to small black businesses.[22]

- An African American specialty trade contractor stated that the prime awards the job and starts putting obstacles in the way. The prime gave him a schedule then starts adding more work. With the additional work, the prime begins to complain that the job is getting behind. He went on to state that once the schedule gets behind they kicked him off the job. The prime then hired two white contractors to replace him. He hired an attorney but the prime told him, "You don't have enough money to fight us."

In addition, there were several overall trends that emerged from 102 anecdotal accounts that were provided subject to the survey methodology, focus groups, personal interviews, and public hearing testimony:[23]

1. There was a consensus from persons who gave testimony that although the City has a small business program, M/WBE firms are not experiencing improvement in the amount of business conducted with the City.

2. Participants overwhelmingly agree that the M/WBE program will not be successful without stringent monitoring, consistency in application, and greater accountability.

[18] Id. at p. 6-20.
[19] Id. at p, 6-22.
[20] Id. at p. 6-22.
[21] Id.
[22] Id.
[23] Id. at p. 6-24

3. The biggest procurement issues were competing with large firms and the City's bid or proposal selection process (i.e., the City's emphasis in prequalification criteria on prior experience with City contracts favors nonminority incumbent firms over M/WBEs).

4. The biggest disparate treatment discrimination issues involved firms being used for projects governed by the SBO program, but not elsewhere; being included on a bid and then being dropped after contract award; and being excluded from work by an informal network of firms.

Well-recognized forms of marketplace discrimination were identified within this vast body of anecdotal evidence:

- False reporting / fraud in good faith efforts
- Unequal access to bid opportunities
- Slow payment
- Bid shopping
- Unequal access to capital & bonding
- Unfair termination
- Exclusion from 'good old boy" informal business networks

In addition to the traditional disparity index analysis and the anecdotal evidence typical of most disparity studies, MGT's Study Update also incorporated several other methodologies that further bolstered the strong basis in evidence for determining whether race- and/or gender-based discrimination is adversely affecting market outcomes for M/WBE firms within the realm of City contracting. In particular, the Study Update included analyses of private sector market conditions and contracting patterns to determine whether the City might be a "passive participant" in private discrimination absent some remedial relief that is provided to M/WBE firms within the context of City contracting.[24]

Private Sector Commercial Construction Permitting Data ("Passive Participant" Subcontractor Disparity Analysis)

Under this methodology, MGT undertook an examination of commercial construction permitting data in the Charlotte market area to compare M/WBE subcontracting utilization rates on City contracts to the M/WBE subcontracting utilization rates in private commercial construction projects by that segment of Charlotte's construction prime contractors that also performed

[24] In *City of Richmond v. J.A. Croson (Croson)*, the Supreme Court established that a "municipality has a compelling government interest in redressing not only discrimination committed by the municipality itself, but also discrimination committed by private parties within the municipality's legislative jurisdiction, so long as the municipality has participated in the discrimination to be remedied by the program." *Croson*, 488 U.S. at 492 (1989). This argument was reinforced by the Court of Appeals decision in *Adarand Constructors v. Rodney* Slater, 228 F.3d 1147 (10th Cir. 2000). This basis for race-conscious remedial relief has become known as the "passive participant" justification that establishes a "compelling governmental interest" under the strict scrutiny standard.

private commercial construction prime contracts. The findings from MGT's examination were as follows[25]:

- Fifty prime contractors that had been awarded and performed on City contracts were also identified as having participated in private sector commercial projects, and 49 of those identified prime contractors also utilized subcontractors on their private commercial projects.

- For 42 of those 50 prime contractors, M/WBE subcontractors constituted less than 5% of the number of subcontractors they used and about 3% of the total subcontract dollars they awarded on their private commercial contracts.

- Based upon gross disparity ratios: The City is a "passive participant" in private sector discrimination wherein its tax dollars are being paid to 42 prime contractors that have substantially excluded /underutilized ready, willing, and able M/WBE subcontractors on their private commercial construction projects (i.e., 3% M/WBE subcontract utilization on private sector contracts vs. 28% M/WBE subcontract utilization on City contracts). These vast disparities in private sector commercial construction subcontracting utilization of available M/WBEs were found for all M/WBE categories: African American, Hispanic American, Asian American, Native American, and nonminority Women-owned subcontracting firms.

Given extensive anecdotal evidence reflecting that M/WBE business owners frequently complained when they were not given work on City projects after prime contractors had listed them on bid documents as being available, it is very unlikely that such M/WBE subcontractors were so busy on City contracts that they were unavailable to perform on any commercial subcontracting opportunities with these same prime contractors. Moreover, such an explanation for this vastly lower utilization of known M/WBE subcontractors on private commercial projects is even more dubious considering that private commercial contracts are not subject to open competitive bidding laws, and that negotiated pricing with private owners may frequently result in higher profit margins for the contractors on private commercial projects than what is typically obtained in the highly competitive public sector contracting realm. The "bid by invitation only" nature of private sector construction projects is also significant when considering the implications of M/WBE bidders receiving only 8.5% of prime contract dollars on private commercial construction projects as compared to 17.5% of prime contract dollars awarded on highly competitive and openly bid City of Charlotte projects.[26]

Regression Analysis of Business Formation Rates and Earnings ("PUMS" Analysis)

Further bolstering the already strong basis in evidence supporting the compelling governmental interest for considering the use of race- and gender-conscious remedies, MGT's Study Update also used two multivariate regression techniques (logistic regression and linear regression) to examine the effects of race and gender, along with other demographic and individual business owner characteristics, on business formation rates and business firm earnings. In undertaking this analysis, MGT adopted the same methodology, relevant variables, and Public Use Microdata Samples (PUMS) data source that were successfully relied upon by the City of Denver in defending its M/WBE program from constitutional challenge.[27] After controlling for numerous

[25] Study Update at pp. 5-3 to 5-18.
[26] Study Update at pp. 5-17 to 5-18.
[27] *Concrete Works v. City and County of Denver*, 321 F.3d 950 (10th Cir. 2003).

variables such as race and sex, availability of capital (i.e., home ownership, home value, unearned income, and residual income), marital status, primary language, disability, age, education level, household children, etc., in the Charlotte CSA, MGT found the following[28]:

- Nonminority males are over two times as likely to be self-employed as minorities and women; and
- Minorities and women who were self-employed reported significantly lower earnings than non-minority males in all business categories.

Overall combined findings from MGT's private sector analysis also lead to the following conclusions[29]:

- Differences in capacity alone are an insufficient explanation for the very low M/WBE subcontractor utilization in private commercial construction.
- Disparities associated with race and gender in business formation rates and earnings persist after controlling for financial capacity, education level, and business experience.
- Race and gender variables explain a large percentage of the differences in market outcomes across all industry categories as indicated by business earnings.

To the extent that M/WBE subcontractor utilization is all but absent in the private sector, credence may be given to the proposition established in *Croson* that the City of Charlotte would become a passive participant in private sector discrimination if it did not require contractors who apply for public sector construction projects to solicit and negotiate with M/WBE subcontractors in good faith.[30]

Overall 'Strong Basis' in Evidence

Charlotte can demonstrate that its governmental interest is compelling only if it satisfies two conditions. First, it must identify the past or present discrimination "with some specificity." Second, it must also demonstrate that a "strong basis in evidence" supports its conclusion that remedial action is necessary. *Shaw v. Hunt*, 517 U.S. 899, 909-10 (1996); *see also Concrete Works v. City and County of Denver*, 321 F.3d 950, 958 (10th Cir. 2003). Considering the totality of the quantitative and qualitative evidence presented in MGT's Study Update, the City of Charlotte has identified past and present discrimination with specificity, and has also established that it has a "strong basis in evidence" that supports consideration of the use of narrowly tailored race / gender-conscious remedial policies to more fully remedy the ongoing effects of marketplace discrimination upon its contracting.

[28] Study Update at pp. 5-28 to 5-40.
[29] Study Update at p. 5-40 to 5-41.
[30] Id. at p. 5-41.

C. Race- and Gender-Neutral Policies Recommended by MGT Are Appropriately Narrowly Tailored to Address Identified Discrimination

Assuming the "compelling governmental interest" prong of the strict scrutiny standard has been met by the City of Charlotte, the second prong of strict scrutiny analysis then requires the City to demonstrate that its proposed remedy is narrowly tailored to address the ongoing effects of that identified discrimination. One aspect of 'narrow tailoring' is that the City must have considered in good faith the efficacy of race- and gender-neutral remedies and determined that race- and gender-neutral remedies, in and of themselves, are not likely to fully remedy the ongoing effects of such discrimination. In this context, the Study Update has confirmed that for the past 8 years, the City of Charlotte has aggressively implemented a mandatory Small Business Opportunity (SBO) Program. The SBO Program is race- and gender-neutral, and indeed, the entire 5-year study period upon which the Study Update was conducted occurred within the tenure of the City's SBO Program. In evaluating the degree to which the City's SBO Program and other race- and gender-neutral policies and practices have been fully successful in remedying the effects of identified discrimination, MGT has made the following findings and proposed adoption of the following additional race- and gender-neutral policies:

1. Following eight years of the aggressive implementation of the SBO Program in City contracts, despite significant increases since 2003 in the absolute dollar level of utilization of M/WBE firms in prime contracts and subcontracts, relative to the increased levels of availability of such firms in the relevant marketplace, there remain substantial and statistically significant disparities in the utilization of M/WBE firms in City prime contracts and subcontracts. Such disparities have continued to occur among certain segments of the M/WBE population for each and every industry category.[31]

2. In addition to the continuation of the SBO Program, MGT has recommended several additional race- and gender-neutral policy options for the purpose of improving M/WBE utilization at the prime contract level. These policy recommendations include:

    a. Raising the dollar threshold for informal construction contracts from $200,000 to $500,000 to enable more flexibility in applying the SBO Program to prime contract opportunities;[32]

[31] Study Update at pp. 7-2 to 7-4, and p. 4-20. (MGT found statistically significant underutilization of African American, Hispanic American, and Native American firms in the category of construction subcontracts; statistically significant underutilization of African American firms in the category of Architectural & Engineering subcontracts; substantial underutilization of African American, Hispanic American, Native American, and Nonminority Women firms in the category of construction prime contracts; substantial underutilization of African American, Hispanic American, Native American and Nonminority Women firms in the category of Architectural & Engineering prime contracts; substantial underutilization of Asian American and Nonminority Women firms in the category of Professional Services prime contracts; substantial underutilization of Hispanic American, Asian American, and Nonminority Women firms in the category of Other Services prime contracts; and substantial underutilization of African American, Asian American, and Nonminority Women firms in the category of Goods & Supplies prime contracts.)

[32] Id. at p. 7-18.

b. Vendor rotation for certain kinds of repetitively purchased goods and services;[33] and
c. Expansion of Charlotte's SBE directory to include firms that are more likely to be vendors for P-card transactions and highlighting these additional firms to Charlotte staff that are authorized P-card users.[34]

MGT has also recommended that the City adopt a Mandatory Joint Venture policy with SBEs, citing the success of an Atlanta version of this policy in which joint ventures between prime contractors that are of different ethnic/gender backgrounds is required on projects in excess of $10 million.[35] However, in our view, such policies are race- and gender-conscious and invoke strict scrutiny because they rely upon racial and gender-classifications in determining which joint ventures are eligible to compete. Such a policy recommendation by MGT is therefore inconsistent with MGT's own conclusion that it lacks a sufficiently strong basis in evidence to warrant consideration of race- and gender-conscious policies.[36]

D. Additional Race- and Gender-Neutral Policies That Are Appropriately Narrowly Tailored to Address Identified Discrimination

Mandatory Centralized Bidder Registration

The above race- and gender-neutral policy recommendations of MGT are all appropriately narrowly tailored remedies in keeping with controlling legal precedent, and pose minimal legal risks. In addition to the above neutral recommendations, we also strongly recommend that the City of Charlotte also adopt and implement an automated Mandatory Centralized Bidder Registration System ("CBR"). The CBR should require all prospective prime contractors, subcontractors, consultants, sub-consultants, and vendors that are interested in performing City contracts or subcontracts to register basic contact and business profile information (i.e., identify appropriate commodity codes that represent the types of goods and services that the prospective bidder seeks to sell) through the City website. Such registration should be a prerequisite for all firms, regardless of ethnicity or gender of ownership, to receive bid solicitation, contract award, and payment as either a prime contractor or a subcontractor on City contracts. The CBR would automatically issue a unique CBR I.D. number to each registrant, and that number would be required for bid solicitation, contract award, and invoice / payment procedures.[37] Benefits of the CBR system would include the following:

[33] Id. at p. 7-19. By requiring SBE firms to be included within the rotation of vendors that are routinely selected for repetitive tasks or purchases, the City will indirectly enhance the opportunity for M/WBE vendors to perform on smaller prime contracts and purchases.
[34] Id. at p. 7-19.
[35] Id. at p. 7-19. Under Atlanta's Mandatory Joint Venture policy, joint venture partners of the same ethnic or gender background are not eligible to compete.
[36] Moreover, MGT's insertion of this proposed policy recommendation might also be viewed as tacit acknowledgement by MGT that race- and gender-neutral remedies have not been fully successful in remedying the substantial disparities in the utilization of M/WBE firms in prime contracts that its Study Update has revealed.
[37] There are a number of jurisdictions that have already designed and installed such bidder registration systems that could serve as useful models to the City, including the State of North Carolina, the Washington Suburban Sanitary Commission, the U.S. Small Business Administration (ccr.gov), the City of Columbia, SC, and the Metropolitan District in Hartford, CT.

- Enables enhanced targeted outreach to prospective bidders through free email alerts based upon registered commodity / industry code profiles;

- Greatly reduces the administrative burden for the following:

  - Ensuring compliance with good faith efforts requirements;

  - Contract-specific goal setting;

  - Accurate and timely reporting of M/WBE, non-M/WBE, and SBE prime and subcontract utilization based upon actual payments; and

  - Providing transparency of payments issued by the City to primes through email notifications to all subcontractors performing on a contract to permit better enforcement of prompt payment provisions.

E. Additional Race- and Gender-Conscious Policies That Are Appropriately Narrowly Tailored to More Fully Remedy Identified Discrimination

Particularly in the context of the inability of an aggressive small business enterprise program (implemented over the span of eight years) to fully eliminate significant and substantial disparities in the utilization of ready, willing, and able M/WBE firms, we conclude that based upon the totality of the evidence presented in MGT's Study Update, the City of Charlotte has a strong basis for considering the use of narrowly tailored race- and gender-conscious remedial policies to more fully remedy the ongoing effects identified discrimination upon its contracting.

MGT has reached a different conclusion on this core issue based upon its review of the same body of evidence. As reasonable minds may well disagree about this legal conclusion, a fuller discussion about the merits of MGT's stated reasons for reaching a conclusion that there is not a sufficiently strong basis in evidence to warrant consideration of race-conscious remedies is appropriate. These reasons are identified and addressed below.

MGT Rationale

MGT concluded that there is no 'strong basis in evidence' to support the City of Charlotte's consideration of race- and gender-conscious remedies for the following reasons[38]:

1. Existing statistically significant disparities are in part due to larger M/WBE availability in recent years; if current M/WBE utilization as reflected in the Study Update is compared to 2003 measures of M/WBE availability, there is no disparity.

2. Increased utilization of M/WBE subcontractors in absolute dollars and percentage participation since the inception of the SBO Program in 2003 indicates that race-neutral remedies work, and that race-conscious remedies are not necessary.

3. The percentage of total contract dollars going to M/WBE construction subcontractors has tripled since 2003.

[38] Study Update at pp. 7-1, 7-7 to 7-8, 7-12 to 7-13, and 7-20 to 7-21.

4. The SBO Program has been a more effective remedy than Charlotte's former M/WBE Program.

5. The Charlotte SBO Program is apparently as effective as other M/WBE Programs in the Charlotte area.

6. The anecdotal evidence in the Study Update is weak.

Alternative Arguments and Views of the Same Evidence

Upon closer examination, MGT's stated rationales for its conclusion are not supportable for the following reasons:

1. While it is true that a comparison of current M/WBE utilization to 2003 Disparity Study measures of availability would not yield any disparities, MGT readily admits that all three of its measures of M/WBE availability used in the 2011 Study Update resulted in higher percentages of M/WBE availability estimates than in the 2003 Study.[39] The "Custom Census" approach that MGT has used most recently in estimating availability of M/WBE firms has been upheld repeatedly in the most recent court cases, and it more accurately reflects the full universe of available firms.[40] MGT was correct in relying upon these larger M/WBE availability measures in the Study Update, and therefore, the resulting disparities using this methodology are legally defensible.

2. MGT's juxtaposition of the M/WBE utilization numerators in disparity ratios from two different time frames (i.e., 2003 vs. 2011) absent the appropriate context of M/WBE availability denominators is not a valid comparison, and is misleading. The appropriate comparison is between the disparity *ratios* from 2003 and 2011, and *not* between the utilization levels alone from those time periods. The erroneous mathematical basis of MGT's argument is apparent. For example, if in hypothetical time frame A there were a disparity ratio of ½ (i.e., one dollar of utilization for 2 available M/WBEs), and then in time frame B both M/WBE availability and utilization increased dramatically such that there was now $5 dollars of utilization for 10 available M/WBEs (i.e., a disparity ratio of 5/10), by focusing solely upon the numerators in comparing market outcomes from these two time periods, one might erroneously conclude that M/WBEs were doing much better in time frame B because their cumulative dollar utilization had increased five-fold from $1 to $5 over this span of time. Yet, when one considers the entire disparity ratio and compares the ½ disparity ratio from time frame A to the 5/10 disparity ratio in time frame B, it is quite apparent the disparity ratios are identical and there has been no relative improvement in M/WBE utilization over time in this hypothetical example. The comparison of actual disparity ratio results from the 2003 and 2011 studies are admittedly considerably more varied and nuanced (by ethnic group and by industry) than this

[39] Id. at p. 7-8. Moreover, it is undisputed that the entire Charlotte CSA has grown dramatically over the past decade, and Charlotte is now the 18th largest city in the United States. So it is hardly surprising that the business population would expand significantly as well.
[40] These cases include the recent 4th Circuit decision in *H.B. Rowe v. Tippett*, *Northern Contracting v. Illinois DOT*, and *Concrete Works v. City and County of Denver*.

hypothetical example. However, it is undisputed from the Study Update that while the SBO Program did have a generally positive effect in reducing the size of the disparities found in 2003, statistically significant and substantial disparities remain in 2011 across all industries for certain segments of the M/WBE population. By ignoring the differences in availability measures that were used in these two time frames, MGT obliterates the proper context for evaluating the significance of the increase in absolute M/WBE utilization dollars and greatly exaggerates the degree to which the SBO Program successfully remedied the ongoing effects of identified discrimination.[41]

In addressing the Disparity Study Advisory Committee, MGT's lead researcher, Dr. Vince Eagan, acknowledged this point when he stated the following: "If someone came up to me and said you have done this study, you have shown these disparities, have you shown the SBO Program didn't work? I could say "Yes", it didn't work because there are still some disparities... In terms of the application in this case if they said the SBO Program failed to address the disparities you could kind of say that."[42]

Moreover, while the SBO Program has been of some benefit to M/WBE firms, it is also undisputed by MGT that non-minority male contracting firms are disproportionately benefiting from this program as they represent only 25% of all SBE firms but are receiving approximately 52% of all contracting dollars received by SBE firms.[43]

3. MGT's presumption of the superiority of the SBO Program over an M/WBE program for reducing disparities based upon the lower relative utilization of M/WBEs under the City's prior M/WBE program and present-day M/WBE programs in neighboring jurisdictions is not necessarily valid, as all M/WBE programs are not created equal. Due to vastly different program features, staff resources, and administration, some M/WBE programs are far more effective than others. MGT has not examined whether those past and present M/WBE Programs that it is comparing to the SBO Program are in keeping with today's M/WBE program "best practices" such as:

    - Effective and narrowly-tailored outreach;
    - Strong monitoring of compliance with policy;
    - Contract-specific goal setting;
    - Narrow tailoring of program eligibility for M/WBEs by ethnic/gender group and by industry based upon industry-specific disparity ratios;
    - Enforcement of sanctions for violations of policy;

[41] The fact that the disparity ratios from 2003 and 2011 are based upon entirely different methodologies for measuring availability makes such juxtapositions and comparisons all the more inappropriate.
[42] October 11, 2011, Disparity Study Advisory Committee Minutes, at p. 1.
[43] October 11, 2011, Disparity Study Advisory Committee Minutes at p. 4. Dr. Vince Eagan stated, "Yes, I would say they [nonminority male contractors] are getting more benefits from the program. Nonminority women and nonminority males... they are getting the bulk of the benefits of the [SBO] Program." This phenomenon, in and of itself, may be further evidence that differences in size and capacity do not fully explain the disparities and underutilization of M/WBE firms as racial and gender-based disparities persist even within the context of the SBO program.

- Clear standards for good faith efforts documentation requirements and waiver requests;
- Adequate staffing and resources; and
- Automated bidder registration and automation in the tracking of availability and actual prime contract and subcontracting payment data.

With the inclusion of the improved features of modern-day M/WBE programs, there is every reason to believe that the next generation of Charlotte's M/WBE program would be far more effective than its previous one.

Similarly, MGT has made no qualitative assessment regarding other M/WBE programs in the area and their adherence to such "best practices" in program design and administration.[44]

4. When considering that marketplace discrimination often occurs outside the presence of those affected, there is a low probability for victims to have direct knowledge of specific instances of discrimination. Accordingly, it would not be at all surprising if the majority of M/WBE business owners did not perceive such discrimination on a routine basis. For example, fraudulent reporting of M/WBE subcontracting, bid shopping, price discrimination by suppliers, double standards in performance, and exclusion from opportunities to bid, are all forms of discrimination where unless a third party informs the M/WBE firm of the disparate treatment on the basis of race or gender, the victim will not be in a position to even know that the discrimination has occurred. Moreover, even when an M/WBE owner suspects that they are not being treated fairly, it is far easier for them to view the occurrence as being unique and isolated rather than part of a systemic pattern of racial or gender discrimination. To conclude otherwise could lead them to an uncomfortable and depressing assessment that their decision to be self-employed in business was an irrational one given the highly competitive nature of the marketplace.[45] Yet, despite these factors, the anecdotal evidence compiled in the Study Update is quite robust with over 100 particularized accounts and affirmations of various forms of discrimination gathered through four different methodologies (e.g., surveys, personal interviews, focus groups, and public hearing testimony).[46] The quantity and quality of this anecdotal evidence compares favorably with other disparity studies,[47] and when

[44] MGT readily admits that "the relative effectiveness of the Charlotte SBO Program is, in all likelihood, due to the more rigorous good faith efforts requirements of the SBO Program (as compared to the State of North Carolina's M/WBE statute), and the fact that Charlotte can, and has been, more aggressive in enforcing project goals under the SBO Program due to the reduced risk of litigation on constitutional grounds. Charlotte rejected the bids of twelve low bidders during the current study period for noncompliance with the SBO Program as compared to rejecting two low bidders for noncompliance with the previous M/WBE program during the study period of the 2003 Disparity Study." Study Update at p. 7-21.

[45] Successful entrepreneurs are typically optimistic, in nature even in the face of substantial obstacles to success.

[46] See Section III. B. of this memorandum for an extensive summary of this anecdotal evidence.

[47] In *Concrete Works IV,* the 10th Circuit Court of Appeals found a strong basis in evidence with disparity study interviews of just 38 M/WBE firms in construction and professional design services(*Concrete Works I*, 823 F.Supp 821 at 834), and where only 8 M/WBE firms testified at trial that general contractors only used them on City construction projects and not private projects, and where only 18 prime contractors (versus 42 prime contractors in Charlotte) were identified as having performed City contracts while also excluding M/WBE subcontractors on their private sector projects. *Concrete Works* at 976

combined with strong statistical disparities in government contracting and private sector data reflecting near total exclusion of M/WBE firms from subcontracting opportunities in private commercial projects, and regression analyses showing stark disparities in business formation rates and business earnings based on race and gender, establishes a strong basis for concluding that marketplace discrimination occurs in much more than a few isolated instances. Therefore, consideration of narrowly tailored class-based race- and gender-conscious remedies is warranted.

F. Other Considerations and Constraints in Drafting Remedial Policies for the City

Although it is not the primary purpose of this memorandum to provide detailed policy guidance on the specific features of a Charlotte M/WBE program, in the event the City of Charlotte follows the recommendation of this memorandum to consider the adoption of narrowly tailored race- and gender-conscious remedies, there are additional constraints on the City's adoption of such policies that need to be taken into consideration:

1. It is important that the M/WBE policy be harmonized with the State of North Carolina's statute that authorizes local governments to establish good faith efforts minority business participation goals programs. As Charlotte is not a "home rule" municipality, Charlotte can only establish M/WBE programs to the extent authorized by State law.[48] However, Charlotte must also be careful to comply with the legal precedents of *H.B. Rowe* and other relevant legal precedents in narrowly tailoring the program definitions of M/WBE firms that are eligible to participate in the remedial relief based upon the findings of the Study Update.

2. Mandatory good faith efforts documentation requirements should be strengthened to the maximum extent permitted under N.C.G.S. § 143-128.2. This has been a key to the success of the SBO Program. For example, submission of documentation of good faith efforts negotiations with subcontractors should be mandatory.

3. The features of the SBO Program should be saved and merged into a single "hybrid" SBO / M/WBE Program that includes contract-specific determinations for the application of either race- / gender-neutral SBO program features or race- and gender-conscious M/WBE program features based upon established criteria that clearly define under what conditions it is appropriate to consider application of the race- / gender-conscious remedial program features.[49]

[48] Specific issues that will need to be addressed will include the extent to which the City may establish definitions of M/WBE firms that are subsets of the categories of firms certified by the State. Some firms that are certified by the State are located out of state and may not be within the relevant geographic market as established by the City's factual predicate. Moreover, depending upon the industry, the City may need to define "M/WBE" more narrowly in terms of program-eligible race and gender classifications than the State has defined them for purposes of satisfying the "narrow tailoring" prong of strict scrutiny under the Equal Protection Clause of the 14th Amendment of the U.S. Constitution.

[49] While such hybrid programs are more challenging to implement from an administrative standpoint, because they provide for a contract-by-contract determination of whether to apply race-neutral program features or race-conscious program features, they are far more narrowly tailored than more traditional M/WBE programs. As such, they are less susceptible to facial legal challenges under the 14th Amendment Equal Protection Clause.

4. Whenever M/WBE subcontracting goals are applied, they should be set on a contract-specific basis based upon relative availability for that specific project. The City's former M/WBE program approach of applying uniform industry-based goals to each and every contract is no longer considered as a best practice.[50]

IV. Conclusions and Recommendations

Through the combination of multiple methodologies, including disparity analysis, anecdotal evidence, private sector commercial construction permitting data ("passive participant" analysis), and regression analysis of PUMS data, MGT has provided the City with a "strong basis" in evidence for considering the use of race- and gender-conscious remedies in its public contracting. Consistent with this finding, we recommend the consideration of the following policies:

1. A hybrid SBO / M/WBE Program with features including contract-specific goal setting and clear standards and criteria for contract-specific determinations as to when it is appropriate to apply race- and gender-neutral program features and when it is appropriate to apply race- and gender-conscious program features;
2. Vendor rotation policy for certain kinds of repetitively purchased goods and services;
3. Increase the formal bid threshold for construction contracts from $200,000 to $500,000;
4. Expand Charlotte's SBE directory to include firms that are more likely to be vendors for P-card transactions and highlighting these additional firms to Charlotte staff that are authorized P-card users; and
5. Establish an automated mandatory centralized bidder registration system that enhances targeted outreach capabilities and greatly reduces the administrative burdens for satisfying good faith efforts requirements, undertaking contract-specific goal-setting, tracking and reporting of SBE and M/WBE utilization as reflected in prime contract and subcontract payments, and providing transparency in payments for better enforcement of prompt payment provisions.

[50] Narrow tailoring of the goal setting process through a contract-specific goal setting mechanism has the additional benefit of reducing the scope of exposure from legal challenges to the individual contracts for which the application of the M/WBE program is being challenged. Assuming the facial legal challenges to the M/WBE Program are initially rebuffed, the potential liability from all subsequent challenges will be limited to damages from the particular contracts at issue and attorneys fees. In such "as applied" challenges, the worst possible outcome should likely be that the program is held to be unconstitutional, but only as it has been applied to a specific contract, and the remainder of the program should remain intact.