

DISPARITY STUDY: Phase 1

Key Points

PURPOSE

Public Act 12-1, Section 110 stated that the Disparity Study conducted by the Connecticut Academy of Science and Engineering, “shall provide an analysis of existing statistical data concerning the state's current set-aside program, established under section 4a-60g of the general statutes, to determine whether its current form achieves the goal of facilitating the participation in state contracts of small contractors and minority business enterprises.”

WHAT IS A DISPARITY STUDY

- Analysis of whether a statistical disparity, or a difference, exists between the number of companies available to participate in contracts, and those that are actually utilized on those contracts in a particular market area.
- A disparity study helps to determine whether the contracting market is fair and equitable to all parties involved.

WHY STUDY PHASING IS RECOMMENDED AND HAS BEEN AUTHORIZED

Study Findings show that:

- Subcontractor data is not uniformly collected by the state agencies.
- Collection and analysis of subcontractor data is a critical component of a valid disparity study in order to create a legally defensible MBE program.

Recommended study phases are as follows:

- ✓ Phase 1: Connecticut’s State Set-Aside Program Review and Analysis, Legal Issues, and Stakeholder Anecdotal Information/Analysis (Completed)
- ✓ Phase 2: Diversity Data Management System Specification and Review of Agency Procedures and Practices Related to System Implementation, Best Practices Review and Analysis, and Establishing MBE/Women’s Business Enterprise (WBE) Program Requirements (under contract for FY14, with completion scheduled by June 2014)
- ✓ Phase 3: Diversity Data Management System Testing, Econometric Model Acquisition and Testing, Legal Issues Update, Agency Progress and Race-Neutral Measures Implementation Review, and MBE/WBE Company Survey. (Tentatively Scheduled for FY15)
- ✓ Phase 4: Data Analysis and Goal Setting, Anecdotal Information/Analysis, and Final Project Report (Tentatively Scheduled for FY16, FY17, FY18)

PHASE 1 BRIEF STATEMENT OF PRIMARY CONCLUSION

The purpose of a minority business enterprise program should be to eliminate discrimination in state contracting in the market area. Although Connecticut’s current program was intended to achieve this objective, it was not designed as a *narrowly tailored* program, and thus does not meet the *strict scrutiny* judicial standard for justifying a race-based program.

PHASE 1 METHODOLOGY

- Legal review discussing *City of Richmond v. J.A. Croson Co.; 1989* and subsequent case law and legal standards
- Legislation review regarding Connecticut’s Small and Minority Business Enterprise Set-Aside Program
- Assessment of Connecticut’s program as related to case law and legal standards
- Review of policies and procedures through state agency interviews and meetings
- Analysis of state’s certification requirements
- Discussions with data management system vendors and states that utilize them
- Qualitative evidence from DAS-certified and non-certified companies — state agency survey; survey of business chambers; survey of DAS-certified companies; focus groups: prime contractors, small- and minority-owned businesses; small and minority business forums

FINDINGS: LEGAL REVIEW

- Based on case law, Connecticut’s Set-Aside Program statute, C.G.S. §4a-60g, will not be upheld in the Second Circuit Court or any court of law, if challenged.
- Connecticut’s Set-Aside Program is limited to MBEs located in Connecticut, yet the market for contracting services often extends beyond state borders.
- The set-aside appears to have been set arbitrarily without a statistical determination of whether there is a disparity in the state contracting market, and hence discrimination.

- Connecticut’s Set-Aside Program is structured as a *rigid* quota system. Race-based programs that have been deemed constitutional by courts use a “goals” method instead of a quota system.
- Program leadership must continually evaluate whether race-conscious measures on state contracts are contributing to eliminating discrimination in the market.

Additionally, to be *narrowly tailored a race-based program*:

- Must not penalize recipients of contract dollars for not meeting MBE goals, if *good faith efforts* were used by a prime contractor to identify eligible MBEs.
- Must limit the types of companies that are eligible for the preference.
- A *narrowly tailored* program cannot give preference to companies that have significant economic advantages, regardless of race.
- The SBE program is not based on race; therefore it is not held to *strict scrutiny* review. Thus, the two programs cannot be intertwined.

RECOMMENDATIONS: LEGAL ISSUES

Connecticut’s statute must be changed in the following manner:

- Until completion of the disparity study, adopt legislation to separate the state’s SBE Set-Aside Program from the current MBE Program. The SBE Program is not based on race or gender, and thus, not held to *strict scrutiny* or *intermediate scrutiny* review.
- Assess what geographies fall under Connecticut’s state agency contracting market. Once the geography is identified, identify all *ready, willing, and able* firms in this market (i.e. allow MBEs from beyond state borders to apply for certification and participate in the program.)
- Until completion of the disparity study’s econometric analysis, set the current statutory goal, 25% of the 25% of the SBE program contracting dollars (6.25% of total eligible contracting dollars), as the MBE program interim goal.
- Institute a goal-based MBE program, rather than a quota system, that allows for flexibility by encouraging, rather than requiring, contractors to use MBEs, and providing waivers to contractors who are unable to meet the goals but can substantiate their *good faith efforts*.

The following recommendations set additional standards for a *narrowly tailored* race-based program that do not have to be revised in statute:

- If a dispute arises about whether a *good faith effort* was made by a party, the party should have the option of appealing to a committee that can hear the dispute and decide a reasonable outcome.
- Establish business size limits that are representative of industry trends, so that the program applies to MBEs that also have some aspect of disadvantage (such as being small), while having distinct limits for different sub-industries.
- Based on the disparity study’s econometric analysis, an overall MBE annual goal will be determined. If a particular minority group is found to experience discrimination in the contracting market, but is still underutilized despite the establishment of an overall MBE goal, then additional methods should be explored and employed to mitigate discrimination.
- State agencies should consider reaching as many of their established goals as possible through race-neutral means.
- The MBE/WBE Opportunities Program (recommended new name of program) must be subject to periodic evaluation to determine if there is a continuing need.

FINDINGS: DATA COLLECTION

- Quality data collection and appropriate analytical techniques are crucial aspects of designing a legally defensible disparity study and providing evidence justifying that any goals that are established are in fact necessary.
 - Collecting full and complete and timely prime contract and associated subcontract awards and actual payments is also critical to effective program implementation and monitoring.
- Connecticut’s current recordkeeping system presents a significant challenge to assessing the SBE and MBE programs.
 - The application and approval of budget exclusions plays a significant role in whether an agency is successful in meeting their SBE and MBE goals.
- The following data elements must be systematically collected and available in order to conduct a valid disparity study:

- Subcontractors and payment data to subcontractors; P-card purchases; consistent accounting methods (cash versus accrual) across branches of state government.

RECOMMENDATIONS: DATA COLLECTION

- Collect data regarding actual payments to subcontractors for all contracts.
- Acquire access to and implement the use of a statewide diversity data management system.
 - Include subcontractor information, bidders and award winners, and P-card purchases
- The system should have the functionality to:
 - track pass-through funding to municipalities
 - generate annual reports at various levels of state government
- Anecdotal evidence should be gathered not only from minority groups, but all stakeholders in the contracting process.
- Calculate availability of small- and minority-owned businesses for each distinct industry sector.
- Rather than having the agencies utilize a process of budget exclusions to determine goals, consider setting goals according to the number of certified firms and industry sector availability.
- Examine the *capacity* of firms by
 1. finding a measure of *capacity* that is appropriate, if any; and
 2. conducting a separate analysis of what variables affect the *capacity* of a firm. If researchers find that discrimination impacts *capacity*, then it should not be controlled for in the econometric model.

FINDINGS: CERTIFICATION PROCESSES

- There is some confusion among a variety of stakeholders about what it means to be SBE/MBE “certified” with the state, including the expectation of results.
- The level of paperwork to become certified is perceived as cumbersome by some contractors.
- Bid documentation that is required by the state far exceeds what is required for any private sector bid.
- The quality of the state’s contractor certification list is frequently questioned, which makes it difficult for prime contractors and agencies to find legitimate SBE/MBEs with whom to partner and build relationships.
- The revenue size standard for SBE/MBE certification eligibility can have the impact of limiting these businesses from growing in order to remain eligible for the program.

RECOMMENDATIONS: CERTIFICATION PROCESSES

- Adopt either
 1. A uniform certification process using the federal DBE requirements.
 2. Have a portal where companies can apply for certifications that interest them.
- Develop a single online database of companies with all certifications listed (including SBE, MBE, WBE, DisBE, DBE, prequalified, municipal, etc.) so that agencies do not have to search multiple lists to check for the appropriate qualifications.
- Educate certified companies about the next steps that are involved in obtaining state contracts, which will help to manage expectations about the results of the SBE and MBE/WBE programs.
- Remove the Connecticut location requirement for MBE program certification. Additionally, Connecticut should consider developing reciprocity agreements with other states for MBE program certification.
- Consider revising the definition of “small” for certifications programs based on industry analysis of geographic market area and research the application of multiple levels of business size. If a revenue standard is used, it should be linked to inflation.
- Consider developing alternatives that would enable companies that exceed the revenue limit of the program under certain conditions to maintain their MBE/WBE certification eligibility.
- Increase the number of unannounced on-site visits conducted by DAS to companies to ensure compliance with state certification requirements.
- Match company certification categories with the online database of companies with certifications (i.e. describe what minority group is represented rather than just noting it as MBE-certified).

FINDINGS: AGENCY PROCESSES

- All state agencies are required to establish small- and minority-owned business enterprise goals in their budgets; however, not every agency reports their goals to DAS and CHRO. There are no penalties for an agency not reporting its annual goals, quarterly status updates, or for failing to meet its goals.

- Although there is an established process for determining agency or political subdivision goals, the specific contracts that are to have a set-aside component are decided by the individual procurement managers, rendering the goal-setting process arbitrary.
- There is sometimes confusion among contractors regarding what constitutes a *good faith effort*.
- Funding that is passed through to municipalities is statutorily exempt from the Set-Aside Program; only three cities (Bridgeport, New Haven, and Hartford) voluntarily participate.
- Monitoring is on a “paper” basis only, with little or no field work that would help to assess penalties to agencies or to contractors for noncompliance.

RECOMMENDATIONS: AGENCY PROCESSES

- Create a working group of key agency leaders, co-chaired by the DAS commissioner and CHRO’s executive director, with program implementers, representing all branches of government and financial systems.
- Conduct joint (DAS and CHRO) workshops for agencies about the goal setting procedures, and conduct workshops for companies about what is needed to effectively work on state contracts.
- Utilize the diversity data management system to:
 - maintain agency goal-setting
 - analyze agency performance in meeting goals
 - identify minority firms by various sub-categorizations that bid on or were awarded contracts, etc.
 - develop annual agency and statewide MBE/WBE program performance reports that would be issued jointly by DAS and CHRO via the proposed working group
- Monitor agency budget exclusions to make sure that they are reasonable and consistent.
- More actively review MBE/WBE utilization plans to make sure that *good faith efforts* are being utilized and conduct an analysis of the results of such efforts.
- Utilize the statutory authority that awarding agencies have to fine or deny companies that misrepresent information provided on SBE and MBE certification applications (in some instances legal action may also be necessary).
- If a certified MBE/WBE receives a contract, but subcontracts a portion of that contract to a non-certified business, then the only portion of that contract that can be counted toward the MBE/WBE contract goal is the portion performed by the MBE/WBE.

FINDINGS: BARRIERS FOR SMALL AND MINORITY BUSINESS ENTERPRISES

- Access to capital and bonding, recordkeeping, strategic planning, and marketing are consistently seen as challenges to small businesses.
- The state’s inconsistency with managing and enforcing its Set-Aside Program compliance rules and requirements was another often mentioned barrier to growth.
- The \$15 million threshold for SBE/MBE certification was generally considered too high by stakeholders, which some focus group participants indicated puts the smaller SBE/MBEs at a disadvantage competitively.
- Paperwork, bonding, and insurance requirements for state jobs were generally seen as barriers to growth.
- The difficulty of small businesses “getting their foot in the door” for state contracts was mentioned by both small companies and prime contractors in focus groups.
- There was a general sentiment among companies that processes and resources could be better streamlined so that companies that need support services can efficiently receive them.
- Many companies do not know about or understand how to obtain state certification so that they can bid on state projects.

RECOMMENDATIONS: SUPPORT FOR SMALL AND MINORITY COMPANIES

- Implement race-neutral measures to assist all small businesses with issues that have been identified as obstacles for participation in state contracting.
- Educate businesses about the resources and support services that are already available as part of a company’s registration.
- Reduce paperwork needed to fulfill state contracting requirements.
- Reduce the complexity of the contracting process by providing boilerplate common terms and conditions for bids, RFPs and contracts online.
- Articulate the importance of the goal in the RFP criteria and add a level of transparency to the bid and contract awarding process.

ACTIONS TO BE TAKEN AS SOON AS POSSIBLE

- Establish a Working Group with representation from all state agencies/branches of government, co-chaired by the commissioner of the Department of Administrative Services and the executive director of the Commission on Human Rights and Opportunities to oversee and coordinate the MBE/WBE and SBE programs.
- Separate the SBE Set-Aside Program from the MBE/WBE Opportunities Program by amending the applicable state statute(s).
- Consider the current MBE/WBE business goals to be interim goals until the statistical analysis of the disparity study is completed.
- Remove the Connecticut location requirement for MBE/WBE businesses and allow for reciprocity among other states by amending applicable state statute(s) and/or regulations.

SHORT-TERM ACTIONS

- Collect comprehensive data for all state agencies and across multiple financial systems through a statewide diversity data management system.
- Conduct an initial statistical analysis, after collection of one year of comprehensive data with a statistically significant sample size, to determine new interim goals based on the results of the analysis, including separating MBE and WBE goals, and sub-goals by race and ethnicity, where needed, based on the data.
- Coordinate existing race-neutral and capacity-building programs for small businesses and add additional programming support to fill in the gaps in need. These programs help all small companies, and furthermore, a legally defensible program must demonstrate it has achieved as much parity as possible using race-neutral measures.
- Streamline certification processes; and improve and simplify the state's contracting processes.
- Strengthen the certification process by increasing unannounced site visits to certified companies and monitoring and compliance enforcement of utilization plans to create more trust among subcontractors and prime contractors.
- Standardize the agency budget exclusion and exemption process.
- Eliminate the statutory municipal exclusion legislation for all state-funded projects and procurement, and require municipalities to use the state's diversity data management system for tracking and reporting on all state-funded municipal projects and procurement.

FUTURE ACTIONS

Complete the econometric analysis of the Disparity Study, based on three years of comprehensive data, to determine if there is a persistence of discrimination in state contracting, and if so, to establish specific goals for individual racial groups and gender, and for industry types of contracting and procurement. Additionally, to support the statistical analysis and the *compelling interest*, continue to gather anecdotal information so as to customize race-neutral and race-conscious measures and initiatives to better address identified disparities.