

Memorandum

To: WIPP PROCUREMENT COMMITTEE

From: PAT MEAGHER
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Date: 11/18/2008

Re: ROTHE DEVELOPMENT CORPORATION V. DEPARTMENT OF
DEFENSE, CAFC No. 2008-1017 (November 4, 2008)

Under the National Defense Authorization Act, 10 U.S.C. Sec. 2323, Congress has set a goal of awarding 5% of the total dollar amount of federal defense contracts to small businesses owned and controlled by “socially and economically” disadvantaged individuals. Under the Act, blacks, Hispanics, Native Americans, and Asian-Pacific Americans are presumed to be socially and economically disadvantaged. In addition, Congress mandated that the Department of Defense give specified forms of assistance to the listed entities including, when practicable and necessary to achieve the 5% goal, contract awards at prices up to 10% above fair market cost.

In 1998, Rothe Development Corporation, a non-minority women owned business, submitted a bid for a defense contract for computer related services and was the lowest bidder. However, after Rothe’s bid was adjusted upward by DOD by 10%

as permitted in the Act, a firm owned by an Asian-American that qualified for the preference became the lowest bidder, and was awarded the contract.

Rothe Development Corporation filed a lawsuit alleging that the preference afforded to socially and economic disadvantaged firms violates the Equal Protection Clause. Under current law, for such a racial preference to be valid, it must survive the legal *strict scrutiny* test: Congress must be deemed to have made sufficient findings of general societal discrimination against racial minorities to justify giving them a preference. The Court of Appeals for the Federal Circuit found that Congress did not have a strong basis in evidence upon which to conclude that the Department of Defense was a passive participant in pervasive, nationwide racial discrimination requiring race-conscious remedial measures. As a result, the Court held that the statute was unconstitutional and enjoined its application.

The statistical and anecdotal evidence included *six* disparity studies of state or local contracting conducted by private research and consulting firms between 2002 and 2005 at the behest of the cities of Dallas, Cincinnati and New York, Cuyahoga County Ohio and Alameda County California, and the Commonwealth of Virginia. It also included a study by the U.S. Commission on Civil Rights, letters from individual business owners, various anecdotes recounted by members of Congress, testimony before Congress, and SBA reports. The court found, however, scrutinized the methodology of the disparity studies and, after finding significant problems, concluded that the disparity studies “do not provide a substantially probative and broad-based statistical foundation necessary for the ‘strong basis in evidence’ that

must be the predicate for nationwide, race-conscious [contracting preference program].” The remaining statistical and anecdotal evidence was no more persuasive to the court.

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The bid preference declared unconstitutional in the *Rothe Development Corporation* case has been suspended for several years because DOD has been meeting the 5% goal. The Court nevertheless decided to hear the case because of the possibility that the preference may take effect again in the future. The Court’s decision declaring the preference unconstitutional is the most recent case attacking Government programs designed to assist minority contractors. A separate case questioning the constitutionality of the Small Business Administration’s 8(a) program called *Dynalantic vs. Defense Department* is pending before the U.S. District Court for the District of Columbia and may be decided next year.

Gender-based preferences such as the Women-owned Small Business Contracting Program must satisfy what the U.S. Supreme Court has called "intermediate" or "heightened" scrutiny. This standard which is more demanding than the “rational-basis standard” that is applied to programs such as the veteran’s preference program but is not as severe as the “strict scrutiny” standard which is applied to race-based preference programs.

The *Rothe* decision makes clear that courts will invalidate contracting preference programs unless there is proof that there was sufficient statistical evidence

of discrimination before Congress when the statute is enacted. The Government must identify the discrimination to be remedied, public or private, with some specificity and must have a strong basis in evidence upon which to conclude that remedial action is necessary. If a court determines that the evidence was lacking, or that there were material flaws in the methodology used in the disparity studies relied upon by Congress, the statute establishing the contracting preference program will not survive a constitutional challenge.