

OFFICE OF INSPECTOR GENERAL
CITY OF NEW ORLEANS



ED QUATREVAUX
INSPECTOR GENERAL

August 10, 2010

Honorable Mitchell J. Landrieu, Mayor
City Hall, Room 2E04
1300 Perdido Street
New Orleans, Louisiana 70112

Dear Mayor Landrieu:

I am writing to present my staff's observations, based on a preliminary review, of the City's Disadvantaged Business Enterprise (DBE) program. My Office initiated a review of the DBE program earlier this year and had planned to complete a comprehensive evaluation with findings and recommendations of best practices. After the City announced its intention to redesign the program, I decided to defer this evaluation until the changes have been implemented. Although our program evaluation has been postponed, I am writing to share our observations regarding the program, which may be helpful as the City implements changes.

Our observations are: (1) that the personnel responsible for implementing this program did not have a clear understanding of the applicable legal standards; (2) that the certification procedure implemented did not have written rules or comply with open meeting laws; and, (3) that the responsible office lacks sufficient staff and funding to carry out its intended functions.

Between April and June of 2010, my staff conducted interviews with relevant persons, such as the Director of the City's Office of Supplier Diversity, the Director of the New Orleans Aviation Board's Disadvantaged Business Enterprise Office, and attorneys with the City's Law Department; collected and reviewed relevant documents, such as DBE-related legislation, approved DBE vendor lists, and a Cooperative Endeavor Agreement among the City, New Orleans Aviation Board (NOAB), Sewerage & Water Board (SWB), and Harrah's Casino to create a joint DBE Certification Panel (Panel). They also observed a monthly meeting of the Panel, attended by program directors, staff, and legal counsel for the City, NOAB, SWB, and Harrah's, during which applications for DBE certification were considered. Finally, they surveyed the relevant law including federal and state case law, state statutes, City ordinances, executive

orders, and policy memoranda. This letter summarizes significant issues identified in course of this review.

History of the City's DBE Program

The objective of the DBE program is to provide opportunities for businesses owned by socially and economically disadvantaged persons to participate in contracts with the City of New Orleans. The program has evolved over the years through the enactment of ordinances, executive orders, and other policy instruments, partly in response to litigation. This complex history has led to conflicting rules and standards for certifying eligible businesses.

During the 1980's, the City enacted an ordinance establishing a DBE program, codified in Chapter 70 of the Code for the City of New Orleans. This program was authorized by a state statute, La. R.S. 38:2233 *et seq.*, which empowered municipalities to enact ordinances setting aside a percentage of public contracts for award to minority-owned or women-owned businesses. The statute defined "minority" as a person who is American Indian or Alaskan Native, Black, Female, or Hispanic. The City's first DBE program used gender or membership in an ethnic or race-based group as a criterion for qualifying as a socially and economically disadvantaged person.

In 1989, the United States Supreme Court ruled that a similar race-based set aside program in the City of Richmond, Virginia, violated the equal protection clause of the United States Constitution. The Court in *City of Richmond v. Croson*, 488 U.S. 469 (1989) held that in order to withstand strict scrutiny, a program that uses race as a criterion for preferential treatment must be narrowly tailored to remedy the effects of past discrimination.

In response to the *City of Richmond* decision, the City of New Orleans in 1989 adopted the "Interim Disadvantaged Small Business Development" ordinance in Chapter 46 of the City Code ("Interim Ordinance"). The Interim Ordinance initiated a new DBE program that prohibited the use of gender or race as a criterion and required an individual to demonstrate personal social and economic disadvantage in order for the business he or she owned to be certified as a DBE. The Interim Ordinance suspended provisions of the first DBE ordinance in Chapter 70 of the City Code as well as all other ordinances, executive orders, and policies that required or authorized the use of gender or race-based goals, set asides, or preferences for city contracts.

The S&WB and the NOAB did not immediately follow the City's lead in adopting gender and race-neutral criteria for certifying DBEs, and each of these entities subsequently faced a lawsuit challenging the constitutionality its program. The State of Louisiana was also sued over its minority set aside program. This litigation, described below, had an impact on the development of the City's DBE program.

Litigation

In 1996, the Louisiana Supreme Court struck down a state statute setting aside a percentage of state contracts for award to minority or women-owned business enterprises because it violated Article I, Section 3 of the Louisiana Constitution, which prohibits any law that discriminates on the basis of race. In *Louisiana Associated General Contractors v. State of Louisiana*, 669 So. 2d 1185 (1996), the Court found that the Louisiana Constitution was intended to give greater equal protection rights than are provided under the Fourteenth Amendment to the United States Constitution and forbids all discrimination based on race, including laws intended to remedy the effects of past discrimination. Under this ruling, the use of racial classifications in any set aside or preference program is prohibited in Louisiana.

During the same time period, a group of contractors filed suit in federal court against the S&WB, alleging that its minority set aside program was unconstitutional. That case resulted in a 1996 settlement agreement requiring the S&WB to operate its DBE program on a race and gender neutral basis. Under the settlement agreement, the S&WB was also required to make the DBE participation goals voluntary, based on good faith efforts, rather than mandatory quotas.

In 1999, the Louisiana Supreme Court considered a challenge to the DBE program established by the NOAB for its state and/or locally funded construction contracts.¹ In *Louisiana Associated General Contractors, Inc. v. New Orleans Aviation Board*, 764 So. 2d 31 (1999), the Court did not rule on the constitutionality of NOAB's program because it found that the NOAB is a City agency and therefore bound by City ordinances. The NOAB program used both race and gender to qualify individuals as socially and economically disadvantaged, but the City's Interim Ordinance prohibited use of these classifications. In its decision, the Court invalidated the NOAB's program because it violated the City's Interim Ordinance.

As a result of these lawsuits, the S&WB and NOAB modified the criteria and procedures used to certify DBEs. Under these criteria, there were no presumptions of disadvantaged status for any racial or ethnic group or gender. The S&WB enacted a resolution in 1997 creating a Certification Committee, to be appointed by the Board, made up of at least three experts in economics, sociology, history, or related fields. The Certification Committee was solely responsible for determining whether business owners qualified as socially and economically disadvantaged persons. The NOAB entered into an agreement with the S&WB, which provided for cross certification of DBEs by the two entities for some contracts.

¹The NOAB uses federal DBE standards, under the Louisiana Unified Certification Program, for federally funded contracts and maintains a separate list of certified DBEs for those contracts.

The Cooperative Endeavor Agreement

In 2004, Mayor C. Ray Nagin signed a Cooperative Endeavor Agreement (CEA) with the S&WB and the NOAB establishing a Joint Certification Program.² The three entities agreed to designate the expert committee established by the S&WB as a Certification Panel (Panel) to review applications and produce a list of eligible businesses for all three DBE programs. The CEA called for the three entities to share expenses for the Panel and to use their DBE personnel to assist in processing applications.

The CEA did not establish criteria for certifying DBEs, but Policy Memorandum No. 46(R), issued by the Chief Administrative Officer on April 26, 2004, set forth policies and goals for the City's DBE program. Policy Memorandum 46(R) adopted by reference the S&WB's certification standards and procedures. These procedures give the Panel complete discretion to set its own rules for the conduct of its meetings and sole authority for approving or denying applications for certification.

Recent Legislative Actions

The City Code has two separate sets of ordinances establishing standards and procedures for the City's DBE program, the original ordinance codified in Chapter 70 and the Interim Ordinance in Chapter 46. The Interim Ordinance states that the program established in Chapter 70, along with all other ordinances, orders, or policies creating gender or race-based set asides or preferences, are suspended for so long as the Chapter 46 provisions are in effect. Recent actions, however, have created confusion as to which of these conflicting legislative programs the City deems to govern its DBE policies.

In 2006, Mayor C. Ray Nagin issued Executive Order CRN 06-15, increasing the City's goals for contracting with local businesses and with socially and economically disadvantaged businesses. This executive order incorporated a definition of "disadvantaged business enterprise" from the Louisiana Unified Certification Program (UCP). The UCP, based on federal DBE participation requirements for contracts funded by the U.S. Department of Transportation, uses gender and racial classifications to qualify individuals as disadvantaged. To the extent that this Executive Order imports gender and race-based criteria for DBEs, it is in direct conflict with the City's Interim Ordinance in Chapter 46 of the City Code and the Louisiana Constitution.

In 2009, the City Council adopted an ordinance amending the City's original DBE program in Chapter 70 of the City Code. The 2009 amendment was intended, like the Mayor's 2006 Executive Order, to increase the City's goals for contracting with local businesses and with socially and economically disadvantaged businesses. However, the DBE program set forth in Chapter 70 had previously been suspended by the Interim Ordinance. By amending Article IV of Chapter 70 without repealing Chapter 46, City officials created confusion as to whether they

² In 2009, the CEA was amended to add Harrah's Casino as a fourth participant in the Joint Certification Program.

consider that program or the gender and race-neutral program established by Chapter 46 to govern the City's DBE standards and procedures.

Observations

The following observations relate to the program's operation prior to the recent Executive Order MJL 10-02, establishing a Provisional Certification program pending the completion of a study. They do not reflect any changes that may have been implemented subsequent to that order.

Observation 1: Legislative Confusion. Our preliminary review found that the personnel responsible for implementing the City's DBE program did not have a clear understanding of the legal authority for program standards and procedures.

We asked the Director of the City's Office of Supplier Diversity, who is responsible for overseeing the DBE program, what legal rules govern the program. He told us that he follows CAO Policy Memorandum 46(R), but referred us to the City Attorney's office to answer our questions about City ordinances. None of the four attorneys we interviewed from the City Attorney's office could say whether the program operated under Chapter 46 or Chapter 70. The attorneys were familiar only with Executive Orders that set percentage goals for DBE participation, but not with the policies and procedures set forth in the City Code.

As previously discussed, the City has been operating under a certification procedure put in place through a CEA between the City, the S&WB, and the NOAB, which is referenced in Policy Memorandum 46(R). However, the use of this joint certification panel conflicts with both Chapter 70 and Chapter 46 of the City Code. Chapter 70 calls for eligibility to be determined by a three-person panel appointed by the Mayor, made up of representatives from the CAO's office, the Department of Finance, and the City Attorney's office. Decisions of this panel can be appealed to the City Council. Under the program created by Chapter 46, the CAO is required to designate an administrator who has sole responsibility for eligibility determinations. An applicant aggrieved by the administrator's decision is entitled to a hearing before the CAO or an independent hearing officer appointed by the CAO. Neither of these two ordinances authorizes the procedures the City has implemented.

Observation 2: Lack of Accountability. The certification procedure the City has implemented does not follow clear, written rules or adhere to open meeting laws.

The only written description of the certification procedure is the 1997 S&WB resolution calling for the Board to appoint a certification panel. The resolution states that the panel has sole power to determine eligibility. The only appeal right afforded disappointed applicants is an opportunity to present arguments to the Panel at an informal hearing, with no appeal to any other person or entity. The panel is also empowered to set its own rules for the conduct of meetings.

The current panel consists of four individuals; two economics professors and two sociology professors. A fifth member retired from the panel for personal reasons. The panel members were appointed for indefinite terms and are paid \$150 to \$200 per hour for their work relating to the DBE program. The panel meets about once a month, but the meetings are not advertised and are not open to the public. There are no minutes or other records of the panel's discussions.

We attended a meeting of the panel in which applications were discussed and certification determinations made. We found that the factors considered in deciding whether an individual is socially and economically disadvantaged were often subjective and that the standards applied from one applicant to the next were sometimes inconsistent. The only objective standards were Small Business Administration maximums for net worth and gross revenue, but the panel regarded these only as guidelines that can be waived at their discretion. Overall, the process lacked clear and objective standards needed to assure that decisions were uniform and fair. The panel's accountability was also undermined by the lack of open meetings, records of discussions, or a meaningful appeal process.

Observation 3: Lack of Resources. The City's Office of Supplier Diversity is not adequately staffed or funded to carry out its intended functions. The Director is the department's only employee. He spends much of his time assembling documentation for applications and responding to complaints. Although CAO Policy Memorandum 46(R) sets out extensive requirements for monitoring and enforcing compliance with DBE participation goals, the lack of resources has made it impossible to implement these requirements. According to the Director, adequate oversight of the program would require additional funding and staff.

Conclusion

The limited observations described in this letter indicate that you are well-advised to redesign the City's DBE program. The pervasive questions as to the source of legislative authority and the appropriate standards and procedures for the program should be faced and resolved. This will require careful attention to constitutional issues and to concerns of basic fairness. I hope these observations will assist you in this endeavor. Should you have any questions or wish to provide comments regarding this letter, please contact Janet Werkman, Assistant Inspector General for Inspections and Evaluations, at 504-681-3202 or jwerkman@nolaoig.org.

Sincerely,



Edouard Quatrevaux,
Inspector General