



Denial of M/WBE Certification is Not Necessarily the End of the Line

LEGAL LOG

BY HENRY L. GOLDBERG, MANAGING PARTNER, GOLDBERG AND CONNOLLY AND STA LEGAL COUNSEL

Obtaining certification as an MBE or WBE from a public agency can be a daunting task. I have personally witnessed a talented and qualified woman virtually reduced to tears after being grilled by the reviewer of her company's application for WBE certification. Historically, it has been generally perceived that there was not much recourse available for a wrong decision in this context. However, a recent NYS court case demonstrates that despite the discretion afforded public agencies in this regard, the "edict" of the reviewing agency denying certification may actually not be the end of the line.

In a decision that may have far-reaching ramifications for situations where contractors and minority or women-owned enterprises increasingly seek to "team up" in a business arrangement, a New York trial court has overruled the NYC Dept. of Small Business Services ("SBS") denial of a contractor's application for certification as a Minority-Owned Business Enterprise ("MBE").

The contractor's application for MBE certification, which the SBS Certification Unit actually recommended for approval, was ultimately denied by the Associate Director of the Division of Economic and Financial Opportunity ("Associate Director"). The Associate Director found, in material part, that the minority owner-shareholder lacked the ability to fire his non-minority owner-shareholder and that each shareholder shared unlimited access to the company's assets and, therefore, found that "[t]he minority owner failed to establish his ability to control independently the company as defined in the NYC Charter and MBE Rules."

Under NYC law and regulations, to be eligible for M/WBE certification, the applying entity must demonstrate that the minority or woman owner has ultimate control over

the business, which means that the minority or woman owner has the authority to, and actually makes, decisions pertaining to the operations of the business and has experience and technical competence in the business enterprise and the working knowledge and ability needed to operate the business. In addition, the corporate or partnership documents and/or agreements must permit the minority or woman owner to make decisions pertaining to the operations of the business without restrictions.

In reversing the SBS's denial for certification, the Court recognized that the M/WBE program is intended to only benefit minority- or women-owned businesses, in which the minority owner exercises "operational control and



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managerial control over the enterprise which is real, substantial and continuing, beyond pro forma ownership, including the power and ability to make basic 'day-to-day decisions ... on matters of management, policy and operation.'" The Court noted, however, that it is equally as important that a denial of certification be based on a genuine and rational basis.

In reviewing a decision of an administrative body, courts are generally constrained to determining only whether the decision of SBS was "arbitrary and capricious" and "without rational basis."

SBS's denial of MBE certification was based upon an administrative rule which provides, in part, that "[w] here the actual management of the business enterprise is contracted out to individuals other than minority group members or women, minority group members and women must demonstrate that they have the ultimate power to hire and fire these managers, that they exercise this power and make other substantial decisions which reflect control of the business enterprise." (Emphasis added).

The Court noted that the M/WBE rules did not define the term "contracted out." However, the use of the phrase in other cases suggested that it required a real and substantial transfer of activities and authority. After examining the record, the Court concluded that the minority owner did not "contract out" management of the company to the non-minority owner. As such, there was no rational basis for the SBS's determination that the minority owner did not have independent control of the Company because it did not have the authority to "fire" his non-minority group business partner and did not have sole authority to enter contracts and sign payroll. According to the Court, it was enough that the minority owner demonstrated that he, in fact, signed contracts and payroll and had the authority to make other financial and operations decisions, which authority was not restricted in any way by the entity's corporate by-laws.

G&C Commentary

As we have said before, the current trend in public contracting is not only more rigorous enforcement of M/WBE and DBE participation goals by prime contractors, but also strict scrutiny and investigation of subcontractors

and/or suppliers applying for certification as M/WBEs or DBEs. As demonstrated by the above-discussed case, one of the more scrutinized areas by certifying agencies is the independence and control of the minority or woman owner. This heightened scrutiny is the result of certain contractors "utilizing" M/WBEs that were simply "pass throughs" or owned by minority or women "figure heads" who did not actually control or perform the work in recent years.

This case is particularly timely. We have recently received many inquiries from non-M/WBE firms that are looking to either encourage the launching of a new M/WBE in conjunction with one of their minority or women employees of long standing, or team-up with an established M/WBE firm. While public agencies encourage such teaming arrangements among M/WBEs and non-M/WBEs, when entering such relationships, non-M/WBE firms must be careful that they do not take too much control of the operations and that the minority or woman not only has the expertise and knowledge in the construction discipline in which the firm will operate, but also that the minority or woman has actual control over such things as negotiations of contracts, purchasing of supplies and equipment, and signing payroll, leases, insurance bonds, etc., without restriction. If such minority control is present and actually exercised, you will ensure that the firm is truly eligible to be certified and that the M/WBE actually performs a commercially useful function. What this case also shows, is that the courts may, occasionally at least, apply common sense to real world business circumstances regarding the application of the M/W/DBE rules and regulations.

Brian P. Craig, an associate with the firm, assisted with preparation of this article.