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During the late 1970s and early 1980s, federal, state and local government agencies established minority business programs to address decades of unfair treatment experienced by minority entrepreneurs. Today, the worse of the unfair practices have ceased, but some issues still remain.

The mandates of those programs were a watershed for minority businesses because they opened market opportunities that did not exist otherwise. The opportunities transformed the character of minority enterprises.

Federal law prohibits discrimination in the award and execution of contracts that are financed wholly or in part by public funds. Nevertheless, before minority business programs, the contracting record of most public agencies indicated wide disparities in awards to minority and nonminority contractors. Even controlling for differences in capacity, studies have shown that minority entrepreneurs were not nearly as successful as were similarly situated nonminority entrepreneurs in securing prime contracts, subcontracts or in providing commodities and supplies to public agencies.

In many locations, the historical record revealed racial barriers operated beneath the surface of what appeared to be open and fair contracting practices. While most of these practices adversely affected minority business owners, some also put nonminority small businesses at a significant disadvantage. Based on the consulting experience of EuQuant (which powers the Gazelle Index) we list some lingering problematic areas for minority business programs. Below are problems that still need to be resolved. Some of them are old problems, but some are relatively new:

1. Many programs have subcontracting goals, which mandate prime contractors use minority subcontractors up to a given percentage. In such cases, it is too often true that minority firms are crowded into low value added subcontracting activities, e.g. clearing and hauling, rather than paving and heavy construction.

2. Sometimes minority firms reinforce their own victimization by failing to diversify their revenue stream beyond the low value added opportunities made available by non-minority primes.

3. No matter how well a minority subcontractor performs, many non-minority primes will not use the minority contractor on private work outside of a program mandate. For example, there is usually a large difference in the use of minority firms by prime contractors on state highway projects that have mandates (because they receive federal funds) and state projects that do not have mandates (because they involve only state funds).

4. A personal net worth ceiling exists in most state and federal minority business programs. This threshold cannot be exceeded by persons who participate in the program. The rationale is to target the program to disadvantaged individuals. However, the ceiling makes it difficult for participants to grow their business because bonding and loans are tied to personal wealth. Furthermore, the ability to bid competitively for prime contracts depends on bonding capacity.

5. A particularly distressing outcome is that some minority business owners keep their business small intentionally. They do so to qualify for minority business programs. One reason for this is minorities have problems winning private sector contracts. However, the problem is magnified by the conscious decision of some minority business owners to keep their business small.

6. Competitively bid prime contracts often contain language that is written specifically to give a certain prime contractor a unique advantage. Under such circumstances, the lowest and most responsible bid can be predetermined.

7. Some prime contracts are unnecessarily bundled into large amounts that are beyond the capacity of small and minority businesses to perform – even when they can be broken down efficiently into smaller lots.

8. Bonding requirements often prevent small and minority contractors from bidding on larger projects because (as many minorities complain repeatedly) unregulated bonding practices are often characterized by unfair and discriminatory treatment of minorities.

9. Authoritative studies have documented that blacks, and Hispanics are less likely to receive a bank loan and more likely to pay a higher interest rate than do similarly situated non-minorities.

10. Non-minority women are increasingly receiving a larger share of benefits from minority business programs. This is causing some unspoken polarization between minority entrepreneurs and white women. The irony is that in many locations, white women are still underutilized relative to their capacity, even if they receive a larger percentage than minorities.

These are major problems. In a future post, we will outline our view of how these problems can be corrected.