



February 9, 2007

Ms. Velma Laws  
Director, Affirmative Action and Contract Compliance  
City of Houston  
611 Walker, 7th Floor  
Houston, TX 77002

Subject: City of Houston Disparity Study - Private Sector Analysis

Dear Ms. Laws:

Enclosed please find the Private Sector Analysis Chapter.

Please feel free to contact me if you have any questions or concerns about this report.

Sincerely,

*Eleanor Ramsey*

Eleanor Mason Ramsey, Ph.D.  
President

cc: Lynn Reddrick, Senior Project Manager

# THE CITY OF HOUSTON DISPARITY STUDY

## Private Sector Analysis

Houston, Texas February 2007



SUBMITTED BY  
MASON TILLMAN  
ASSOCIATES, LTD.

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# 1

## ***PRIVATE SECTOR ANALYSIS***

### ***I. BACKGROUND***

In 2006, the City of Houston (City) engaged Mason Tillman Associates, Ltd. (Mason Tillman) to conduct a Disparity Study. The Disparity Study had two components. The first component was the Disparity Study itself, an analysis to determine if a statistically significant disparity existed in the award of City contracts to available market area businesses. The second component, the Private Sector Analysis, was an assessment of the practices of the City's prime contractors in the private sector when their contracts were not subject to minority and woman-owned business enterprise (M/WBE) requirements. This chapter contains the findings from the private sector analysis.

The City requested a private sector analysis as an alternative means of assessing whether discrimination existed in its market area. The private sector, where contracting was not subject to government-imposed M/WBE contracting requirements, was identified by the City as a relevant context for assessing actual market conditions affecting M/WBE utilization. The City postulated that the factual predicate for it to institute a race-based remedy was a finding that its prime contractors discriminated in the private sector.

A review of the case law on the subject of private sector findings as a predicate for a government-sponsored, race-based program is critical in order to understand the prevailing legal standards. Private sector findings as a legal precedent for a governmental remedy are discussed in the following section.

## **II. LEGAL STANDARDS**

*City of Richmond v. J.A. Croson Co.*<sup>1</sup> (*Croson*) allowed race-conscious contracting when it is a narrowly tailored remedy for identified discrimination in which the government is an active or passive participant. For purposes of equal protection analysis pursuant to the Fourteenth Amendment of the U.S. Constitution, it is a given that the governmental entity is an “active participant” in the prime contracts that it awards, and is a “passive participant” in the subcontracts awarded by its prime contractors. The governmental entity is seen as an active participant, because it actually awards the contract to the prime contractor. It is held to be a passive participant in the case of subcontracts because the entity acquiesces in the award of the subcontract, allowing the prime contractor to award the subcontract to the subcontractor of its choice.

In January 2003, the Tenth Circuit decided *Concrete Works of Colorado v. City and County of Denver*<sup>2</sup> (*Concrete Works*) where it explicitly held that business activities conducted in the private sector if within the government’s marketplace are also appropriate areas to explore the issue of passive participation. However, the court was not asked in that case to review the appropriateness of the city’s remedy but only to examine the facts to determine if the private sector business practices under consideration constituted discrimination. For technical legal reasons<sup>3</sup> the court did not examine whether a consequent public sector remedy, i.e., one involving a goal requirement on the city of Denver’s contracts was “narrowly tailored” or otherwise supported by the city’s findings of discrimination.

That question whether a particular public sector remedy is narrowly tailored when it is based solely on business practices within the private sector was in issue in *Builders Association of Greater Chicago v. City of Chicago*<sup>4</sup> (*City of Chicago*). *City of Chicago* was decided ten months after *Concrete Works*, and the District Court found that certain business practices constituted discrimination against minorities in the Chicago market area. However, it did not find the city of Chicago’s M/WBE subcontracting goal to be a remedy that is “narrowly tailored” to address the documented private discriminatory business practices that had been discovered within the city’s market area. The court explicitly stated that certain documented discriminatory business practices, namely access to credit, constituted private sector discrimination. It is notable that the documented discriminatory business practices were similar to those reviewed in *Concrete Works*. Notwithstanding the fact that discrimination in market access was documented, the Court determined that the evidence was insufficient

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<sup>1</sup> *City of Richmond v. J.A. Croson Co.*, 488 U.S. 469 (1989)

<sup>2</sup> *Concrete Works of Colorado v. City and County of Denver*, 321 F.3d 950 (Tenth Circuit, 2003)

<sup>3</sup> Plaintiff had not preserved the issue on appeal. Therefore, it was no longer part of the case.

<sup>4</sup> *Builders Association of Greater Chicago v. City of Chicago*, 298 F.Supp.2d 725 (N.D. Ill. 2003)

to support race-based subcontracting goals. The Court ordered an injunction designed to invalidate the city of Chicago's goal-based program.

Given the current case law's challenging requirement that a private sector analysis must show a nexus between the government remedy and private sector discrimination, a private sector analysis would be most productive in those instances when the statistical analysis of a jurisdiction's prime contractors and subcontractors yields a finding of no disparity. Such a private sector analysis would be best advised where a jurisdiction has operated an aggressive race-based program. Under such a program, one may anticipate that the goals may have corrected any statistical disparity that previously existed, even though the fundamental market practices had not changed.

When the Disparity Study was commissioned in 2006, the City had been operating a minority, woman, disadvantaged, and small business enterprise (M/W/DBE/SBE) program since 1984. Therefore, the City anticipated that the adopted goals would have corrected the disparity upon which their programs were based. Given the fact that there had been long-standing M/W/DBE/SBE programs, Mason Tillman was directed to conduct a narrowly tailored inquiry into the private sector business practices of the City's prime contractors. This inquiry was undertaken to determine if discrimination existed in the private sector.

The methodology employed and the findings from the research are set forth below.

### **III. METHODOLOGY**

The four objectives in the private sector analysis are:

1. To determine if minority and woman-owned prime contractors hire M/WBE subcontractors at a different rate from non-minority contractors
2. To determine if there are differences in a prime contractor's acceptance of M/WBE subcontracting bids in the public sector compared to the private sector
3. To determine if prime contractors who have worked for public agencies in the past and were subject to M/WBE requirements demonstrate a different M/WBE utilization pattern from the contractors without previous public sector contracts
4. To determine the level of M/WBE subcontractor utilization when goals are not required on exempt procurements

The research techniques that were used to address these objectives were telephone surveys of prime contractors with a known private project and their subcontractors, one-on-one interviews with contractors with a known private project and no city contracts, statistical

analysis of the City's contract records, and a review of the City's M/WBE procurement policies.

Construction permit records were pulled to identify private sector jobs that were performed between July 1, 2003 and June 30, 2006, the period of the Disparity Study. A series of questions were formulated to inquire about the history of utilizing M/WBE subcontractors and the percentage of their contracts that were subcontracted to M/WBE subcontractors.

## **IV. DATA ANALYSIS**

### **A. Utilization of M/WBE Subcontractors in the Public Sector**

The purpose of this component of the private sector analysis is to determine if minority and woman-owned prime contractors hire M/WBE subcontractors at a different rate than non-M/WBE prime contractors. The City's prime contract and subcontract records were used in this analysis.

As illustrated by Table 1.01 below, M/WBE prime contractors have a generally higher rate of utilizing M/WBE subcontractors in their contracts. In the architecture and engineering industry, non-M/WBE and M/WBE prime contractors utilized M/WBE subcontractors at nearly the same rate, with M/WBE prime contractors using M/WBE subcontractors slightly more. A similar rate of M/WBE subcontractor utilization is found in the construction industry.

However, in the professional services and goods and other services industries, M/WBE prime contractors demonstrated a significantly larger level of M/WBE subcontractor utilization. In the professional services industry, M/WBE prime contractors utilized M/WBE subcontractors for 23.3 percent of their contract dollars, while non-M/WBE prime contractors showed a utilization of 17.61 percent, which is the greatest difference in utilization levels. M/WBE prime contractors awarded M/WBE subcontractors 13.9 percent of their contracts while non-M/WBE prime contractors utilized M/WBE subcontractors at 8.79 percent.

While the percentage of awards that M/WBE subcontractors received from non-M/WBE prime contractors was not significantly lower than what was received from M/WBE prime contractors, the overall utilization comparison shows a significant difference. Additionally, while the percentage of awards that M/WBE subcontractors received from both categories of prime contractors was quite close, the dollar amounts differed greatly. For each industry, M/WBE prime contractors received substantially less contract dollar amounts than did non-M/WBE prime contractors. This difference transferred to M/WBE subcontractors as well.

Thus, in the public sector, M/WBE prime and subcontractors received less contract dollars than did their non-M/WBE counterparts.

**Table 1.01 M/WBE Subcontractor Use in Public Sector**

<b>Prime Status</b>	<b>Prime Contract Amount</b>	<b>Amount M/WBE Subcontractor Received</b>	<b>Percentage of Award M/WBE Subcontractor Received</b>
<b>Construction</b>			
Non-M/WBE	\$1,394,276,922	\$253,412,387	18.18%
M/WBE	\$169,144,031	\$31,855,214	18.83%
<b>Architecture and Engineering</b>			
Non-M/WBE	\$147,240,099	\$36,172,361	24.57%
M/WBE	\$58,699,815	\$16,323,688	27.81%
<b>Professional Services</b>			
Non-M/WBE	\$60,907,851	\$10,723,935	17.61%
M/WBE	\$11,544,586	\$2,690,144	23.30%
<b>Goods and Other Services</b>			
Non-M/WBE	\$528,058,591	\$46,420,805	8.79%
M/WBE	\$78,891,056	\$10,967,181	13.90%
<b>Totals</b>			
Non-M/WBE	\$2,130,483,463	\$346,729,488	16.27%
M/WBE	\$318,279,488	\$61,836,253	19.43%

***B. Effects of Governmental M/WBE Contracting Rules on Market Behavior***

The purpose of this component of the analysis is to determine if there are differences in prime contractors' acceptance of M/WBE subcontracting bids in the public sector compared to the private sector. A survey of subcontractors that had worked in both the public and

private sectors was conducted in order to analyze the experiences of M/WBE subcontractors. Table 1.02 provides data on the number of subcontractors and their level of response to Mason Tillman's survey.

**Table 1.02 Subcontractor Data Collection**

<b>Total Subcontractors Contacted</b>	<b>Number of Subcontractor Responses</b>	<b>Percentage of Subcontractors Responding to Survey</b>
56	21	37.50%

The number of subcontractors that Mason Tillman initially contacted, 56, stems from information from prime contractors that Mason Tillman surveyed. Mason Tillman contacted 29 prime contractors that in turn provided information on the subcontractors that they had used in projects in both the public and the private sector.

Table 1.03 depicts the number of subcontractors that had been invited to perform work on a project in the private sector. As illustrated below, over half of the M/WBE subcontractors surveyed reported having the opportunity to work in the private sector or having been invited to bid on a private sector project. This information is reinforced in Table 1.04, which provides information on whether or not the surveyed subcontractors performed more work in the private than in the public sector.

**Table 1.03 M/WBE Subcontractor Invitations to Work in Private Sector**

<b>Invited to Bid</b>	<b>Number of Firms</b>	<b>Percentage of Firms</b>
Yes	12	57.14%
No	8	38.10%
Unsure	1	4.76%
<b>Total</b>	<b>21</b>	<b>100.00%</b>

As Table 1.04 below shows, more than half (52.38 percent) of the surveyed subcontractors performed more work in the private sector than in the public sector.

**Table 1.04 Level of Subcontractor Work in Private Sector  
Versus Public Sector**

<b>Worked More in the Private Sector</b>	<b>Number of Firms</b>	<b>Percentage of Firms</b>
Yes	11	52.38%
No	8	38.10%
Unsure	2	9.52%
<b>Total</b>	<b>21</b>	<b>100.00%</b>

**C. Effects of Public Contracting Requirements on M/WBE Subcontractor Use**

The purpose of this component of the private sector analysis is to determine if prime contractors that have worked on projects in the public sector in the past and were subject to M/WBE requirements demonstrate a different M/WBE utilization pattern than do contractors without prior experience in the public sector. A survey of prime contractors that had worked in both the public and private sectors was conducted in order to analyze the utilization of M/WBE subcontractors. Tables 1.05 and 1.06 report the results for prime contractors that have only worked in the private sector.

As Table 1.05 shows, nearly 73 percent of prime contractors that have only worked in the private sector reported using M/WBE subcontractors. Those prime contractors that reported using M/WBE subcontractors in their private sector jobs were then surveyed regarding the level of M/WBE subcontractor participation. Those results are depicted in Table 1.06.

**Table 1.05 Level of M/WBE Subcontractor Use by Prime Contractors with Only Private Sector Experience**

<b>M/WBE Subcontractor Use</b>	<b>Number of Firms</b>	<b>Percentage of Firms</b>
Yes	85	72.65%
No	32	27.35%
<b>Total</b>	<b>117</b>	<b>100.00%</b>

As shown below in Table 1.06, the majority of prime contractors that used M/WBE subcontractors (79.69 percent) subcontracted less than half of their awards to M/WBEs.

**Table 1.06 Percentage of Work Subcontracted to M/WBEs by Prime Contractors with Only Private Sector Experience**

<b>Percentage of M/WBE Subcontracted Private Sector Work</b>	<b>Number of Firms</b>	<b>Percentage of Firms</b>
1% to 10%	13	20.31%
11% to 25%	19	29.69%
26% to 50%	19	29.69%
More than 50%	13	20.31%
<b>Total</b>	<b>64</b>	<b>100.00%</b>

The results for prime contractors that have worked in both the private and public sectors are presented in Tables 1.07 and 1.08.

As shown below in Table 1.07, most prime contractors with work experience in both the private and public sectors utilized M/WBE subcontractors on their projects in the private sector.

**Table 1.07 Level of M/WBE Subcontractor Use by Prime Contractors with Private and Public Sector Experience**

<b>M/WBE Subcontractor Use</b>	<b>Number of Firms</b>	<b>Percentage of Firms</b>
Yes	10	83.33%
No	2	16.67%
<b>Total</b>	<b>12</b>	<b>100.00%</b>

As with prime contractors with only private sector contracting experience, the majority of prime contractors with private and public sector experience reported using M/WBE subcontractors on their private sector projects.

**Table 1.08 Percentage of Work Subcontracted to M/WBEs by Prime Contractors with Private and Public Sector Experience**

<b>Percentage of M/WBE Subcontracted Private Sector Work</b>	<b>Number of Firms</b>	<b>Percentage of Firms</b>
1% to 10%	0	0.00%
11% to 25%	8	88.89%
26% to 50%	1	11.11%
More than 50%	0	0.00%
<b>Total</b>	<b>9</b>	<b>100.00%</b>

***D. Contracts with Goals Versus Contracts without Goal Requirements***

The level of M/WBE subcontracting reported by prime contractors on City contracts with M/WBE subcontracting goals and those without M/WBE goals were compared with the purpose of determining whether or not the presence of M/WBE subcontracting goals influences M/WBE subcontractor utilization. The construction and goods and other services industries offered contracts with and without goals while the professional and architecture and engineering industries only offered contracts without goals. The results of the analysis of City contracts with and without goals are presented below in Tables 1.09 and 1.10.

As Table 1.09 below illustrates, in the construction industry prime contractors subcontracted with M/WBEs slightly more often on contracts with goals than on contracts without goals. However, while the percentage of M/WBE utilization on contracts with and without goals is quite close, the dollar amount that prime and M/WBE subcontractors received was substantially less on contracts without goals than on contracts with goals.

It should be noted that in the goods and other services category, prime contractors reported that their payments to M/WBE subcontractors exceeded the prime contractor's award. This accounts for the percentage of awards that M/WBE subcontractors received on contracts without goals in the goods and other services industry being 173.44 percent. On contracts with goals in the goods and other services category, M/WBE subcontractors received 9.4 percent of the prime contractors' contract award.

**Table 1.09 M/WBE Subcontractor Utilization on Contracts with and without Goals**

<b>Contract</b>	<b>Prime Contract Amount</b>	<b>Amount M/WBE Subcontractor Received</b>	<b>Percentage of Award M/WBE Subcontractor Received</b>
<b>Construction</b>			
Contracts with Goals	\$1,556,035,169	\$283,968,635	18.25%
Contracts without Goals	\$7,385,784	\$1,298,966	17.59%
<b>Goods and Other Services</b>			
Contracts with Goals	\$606,737,414	\$57,019,895	9.40%
Contracts without Goals	\$212,233	\$368,091	173.44%

As shown below in Table 1.10, in the architecture and engineering and professional services industries, where there are no contract goals M/WBE subcontractors received 25.49 percent and 18.51 percent of the prime contractors' awards, respectively.

**Table 1.10 M/WBE Subcontractor Utilization in Contracts without Goals**

<b>Prime Contract Amount</b>	<b>Amount M/WBE Subcontractor Received</b>	<b>Percentage of Award M/WBE Subcontractor Received</b>
<b>Architecture and Engineering</b>		
\$205,939,914	\$52,496,049	25.49%
<b>Professional Services</b>		
\$72,452,437	\$13,414,079	18.51%

## **V. CONCLUSION**

In gathering prime contractor data for the private sector analysis, Mason Tillman relied upon information drawn from the City's permit information, which was the only source from which information about private jobs performed within the study period could be obtained. This data was not drawn from United States Census records, the preferred data source. Thus, the amount of contracts and prime contractors available for analysis was significantly smaller than the amount of data that would allow for the most comprehensive analysis.

As shown in Table 1.01, M/WBE prime contractors utilize M/WBE subcontractors to a greater extent than do non-M/WBE prime contractors. For professional services and goods and other services contracts, the difference between M/WBE and non-M/WBE utilization of M/WBE subcontractor utilization is approximately five percent in each industry.

More than half of the M/WBE subcontractors surveyed had been invited to perform work on a job in the private sector. Similarly, more than half of the M/WBE subcontractors performed more work in the private sector than in the public sector. Assuming the presence of market area discrimination, it would be expected that M/WBE subcontractors would work more in the public sector due to the presence of M/WBE subcontracting goals on the City's contracts.

In conducting the telephone survey of prime contractors, Mason Tillman received some input that may explain why M/WBE subcontractors received similar levels of contract awards in the private and public sector. Some M/WBE prime contractors included themselves when reporting the percentage of a contract award that went to M/WBEs. Also, some prime contractors considered the workforce of the subcontractors they used instead of counting the ownership of the subcontractor firms. Thus, a non-M/WBE subcontractor may have erroneously been counted as an M/WBE based on the ethnic or racial make-up of its employees.

The results of the private sector analysis show that the City's prime contractors possessed extensive experience working on public sector contracts with M/WBE requirements. Presumably, these prime contractors would draw on their public sector experience with M/WBE goal requirements to attain M/WBE participation on their private sector contracts, and on their public sector contracts without M/WBE goal requirements. However, as shown in Tables 1.06 and 1.08, contractors with experience in both the private and public sectors utilized M/WBE subcontractors to a lesser extent than did prime contractors with experience only in the private sector. For example, 50 percent of prime contractors with only private sector experience reported awarding 25 percent or more of their contract dollars to M/WBE subcontractors, compared to 11 percent of prime contractors with private and public sector experience.

Using the data available, Mason Tillman's private sector analysis has determined that there is discrimination in the use of M/WBEs. However, the extent of the discrimination cannot be precisely determined due to the small number of prime and subcontractors that were available for this analysis. Thus, a more thorough examination may be necessary.