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Federal District Court Enjoins U.S. Small Business Administration from Using Race-Based Rebuttable Presumption Under 8(a) Program

*By Robert K. Tompkins, Leila S. George-Wheeler, Kelsey M. Hayes and Hillary J. Freund**

In this article, the authors review a federal district court decision striking down the federal government's use of a "rebuttable presumption" of social disadvantage for certain minority groups to qualify for inclusion in the Small Business Administration's 8(a) program.

The U.S. District Court for the Eastern District of Tennessee ruled in *Ultima Servs. Corp. v. U.S. Dept of Agric.* that the U.S. Small Business Administration's (SBA) and U.S. Department of Agriculture's (USDA) use of a "rebuttable presumption" of social disadvantage for certain minority groups to qualify for inclusion in the SBA's 8(a) Business Development Program (the 8(a) Program) violates the Fifth Amendment's Due Process Clause.

The decision comes on the heels of the U.S. Supreme Court's ruling in *Students for Fair Admissions, Inc. v. President & Fellows of Harvard College*, in which the Supreme Court struck down race-based affirmative action in the college admissions process.

As part of the district court's ruling in *Ultima*, it has enjoined the federal government from using the presumption of social disadvantage in administering the 8(a) Program. The ruling could have significant and far-reaching impacts on the 8(a) Program.

THE PROGRAM

The 8(a) Program, established under Section 8(a) of the Small Business Act, is a business development program that offers small disadvantaged businesses (SDBs) training, technical assistance and federal contracting opportunities in the form of set-aside and sole-source awards. The 8(a) Program is generally limited to small businesses "unconditionally owned and controlled by one or more socially and economically disadvantaged individuals."¹ Under the 8(a)

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¹ 15 U.S.C. § 637(a)(4)(A).

Program, there is a rebuttable presumption that members of certain racial and ethnic groups are “socially disadvantaged,” whereas individuals who do not belong to these groups must prove they are socially disadvantaged.²

ULTIMA’S CHALLENGE

The plaintiff, Ultima Services Corp. (Ultima) is a small business that provides administrative and technical support services. Ultima is owned and operated by a white woman. Since 2004, Ultima had competed for and won multiple federal services contracts with the Natural Resources Conservation Service (NRCS), a unit within the USDA. Beginning around 2018, the USDA began awarding sole-source contracts for the services Ultima had been providing to 8(a) Program participants. Because Ultima was not an 8(a) participant, it was ineligible for consideration. On March 4, 2020, Ultima filed its lawsuit alleging the defendants (i.e., the federal government) engaged in race discrimination in violation of the Fifth Amendment of the U.S. Constitution. Specifically, Ultima alleged that the use of the rebuttable presumption of social disadvantage for certain minority groups in the 8(a) Program discriminated on the basis of race.

THE DISTRICT COURT’S FINDINGS

First, the district court rejected Ultima’s argument that the SBA lacked statutory authority to impose a rebuttable presumption of social disadvantage pursuant to the Small Business Act. Under the Act, Congress provided SBA with the authority to carry out its goal of awarding government contracts to SDBs and contemplated that “SBA would identify group characteristics and accompanying forms of bias that would be considered when evaluating claims of social disadvantage.” Thus, the district court noted that insofar as “SBA is using the rebuttable presumption to ‘arrange for the performance of procurement contracts . . . [by] socially and disadvantaged small business concerns,’ that exercise falls within the statutory framework Congress set out.”

Having found SBA has the statutory authority to create a rebuttable presumption, the district court proceeded to evaluate Ultima’s claim under the Fifth Amendment’s Due Process Clause. That clause provides that no person may be “deprived of life, liberty, or property, without due process of law” and which courts have held “incorporates, as against the federal government, the Equal Protection Clause of the Fourteenth Amendment.”³ The district court analyzed Ultima’s equal protection claim under the Fifth Amendment (as

² See 13 C.F.R. § 124.103.

³ The Fourteenth Amendment provides that no state shall “deny to any person . . . the equal protection of the laws.”

against the federal government) just as the Supreme Court analyzed the petitioner's equal protection claim in *Students for Fair Admissions* under the Fourteenth Amendment (as against state and local governments). In both cases, the courts were asked to consider the government's racial classifications using a two-step examination known as "strict scrutiny," which asks (1) whether the racial classification is used to "further compelling governmental interests," and (2) whether the government's use of race is "narrowly tailored" (meaning "necessary" to achieve that interest).

Here, as with the Supreme Court in *Students for Fair Admissions*, the district court found that the rebuttable presumption did not survive strict scrutiny. The district court found (1) the defendants failed to show a compelling interest for their use of the rebuttable presumption as applied to Ultima, and (2) even if the defendants could establish a compelling interest, the rebuttable presumption was not narrowly tailored to serve the asserted interest. Each of these findings is addressed below.

COMPELLING GOVERNMENTAL INTEREST

The defendants argued that they had a compelling interest in remedying the effects of past racial discrimination in federal contracting. However, the district court noted that the USDA admitted they did not maintain goals for the 8(a) Program, and the SBA did not require agencies to have goals for the 8(a) Program. Thus, the district court concluded, "If the rebuttable presumption were a tool to remediate specific instances of past discrimination, Defendants should be able to tie the use of that presumption to a goal within the 8(a) program" and the "lack of any stated goals for Defendants' continued use of the rebuttable presumption does not support Defendants' stated interest in 'remediating specific, identified instances of past discrimination[.]'"

Next, the district court concluded that even if there was a compelling interest, the defendants failed to demonstrate a "strong basis in evidence" to support the use of the race-based rebuttable presumption. The district court found that the studies submitted by the defendants, including expert reports and agency studies regarding disparities that SDBs face nationally, failed to identify a "specific instance of discrimination" and failed to show the disparities are "tied to specific actions, decisions, or programs that would support an inference of intentional discrimination that the use of the rebuttable presumption allegedly addresses." The district court further found that the defendants' evidence did not show that the government was a "passive participant in such discrimination in the relevant industries in which Ultima operates."

NARROWLY TAILORED

The district court also found that, even if the defendants could establish a compelling interest, the rebuttable presumption was not narrowly tailored. In

doing so, the district court examined several factors, including the necessity for the race-based relief, the efficacy of alternative remedies, the flexibility and duration of the relief and the impact of the relief on the rights of third parties. The district court found that the 8(a) Program was not flexible because there is no formal process for submitting evidence that could overcome the rebuttable presumption, and “individuals who do not receive the presumption must put forth double the effort to qualify for the 8(a) program.” The district court also found the 8(a) Program was not limited in duration because although participants can only remain in the 8(a) Program for nine years, “Defendants conceivably could use the rebuttable presumption for as long as the 8(a) program itself is in place[.]”

The district court went on to note that the lack of specific remedial objectives “shows that the Defendants are not using the rebuttable presumption in a narrow or precise manner.” The district court also found that the rebuttable presumption was overinclusive because “the rebuttable presumption sweeps broadly by including anyone from the specified minority groups, regardless of the industry in which they operate” and underinclusive because “certain groups that could qualify will be left out of the presumption.” Because SBA had not “revisited the use of the rebuttable presumption since 1986,” the district court found there was no basis to conclude that no workable race-neutral alternative existed to achieve the asserted compelling interest. Finally, the district court concluded that the rebuttable presumption impacted Ultima because it presented an “obstacle to fulfilling” the contracts at issue and hampered Ultima’s “ability to compete for the other contracts” that the government set aside for the 8(a) Program.

CONCLUSION

In its opinion and order, the district court enjoined the SBA from using the rebuttable presumption of social disadvantage in administering the 8(a) Program. There are open questions concerning the implications of the decision, including how SBA will comply with the order and whether it applies nationwide. At the time of publication, the court had not yet reached a final decision on the scope of the remedy to be applied.