

NEWS & INSIGHTS

Partnering to bid on government contracts for diverse and non-diverse business entities

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In February, I wrote about the process and benefits of becoming certified as a diverse business entity (DBE). This month, I want to talk about how DBEs can partner with non-DBEs—legally. It is no secret that public projects, and increasingly some private projects, require a certain quota or percentage of DBE participation. Although DBEs are increasing in number, the process has been slow and finding a qualified DBE can be difficult.

For years, many companies have tried to use creative loopholes, but in doing so, they likely violate the law. Two common examples of this are when a non-diverse entity contracts with either a “front” or “pass-through” DBE when bidding on a project. A “front” company is when a non-diverse entity creates a DBE to bid on projects; however, in reality, the non-diverse entity maintains full control over the DBE and uses its own labor to staff the project. A “pass-through” company, on the other hand, is an independent DBE that bids on a project, but through an agreement, passes on the majority of the work to a non-diverse contractor to actually perform the work.

While these bidding structures have allowed for some DBE participation, it is contrary to the stated goals of the DBE initiative, which is to increase opportunities for entities owned and run by women or minorities in the construction industry. Teaming agreements are a great way to increase DBE participation without running afoul of the DBE initiative. Teaming agreements allow two or more independent companies to join for a specific business purpose, such as bidding on a project. A well-drafted teaming agreement is critical. The agreement should clearly state the parties’ intentions, expectations, responsibilities, and address confidentiality. Also, certain projects may prohibit teaming agreements, so it is important to review the specific requirements for the project you intend to bid on.

Teaming agreements also help prevent you from violating the law. The use of front and pass-through companies is often times considered fraud. And, over the last few years, the government is taking notice. In late 2019, a Baltimore based painting and construction company was convicted of conspiracy, wire fraud, and false statements in the Eastern District of Pennsylvania. The company was required to use DBEs to furnish supplies for a public project. The company used a DBE pass-through for its supplies and falsified invoices to make it appear the supplies were coming from the DBE pass-through when in reality the supplies were being provided by non-diverse entities. The company was sentenced to five years’ probation, a \$500,000 fine, and forfeiture of \$10.9 million. The project manager was also charged and sentenced to 70 months’ imprisonment, three years’ of supervised release, and a \$17,500 fine for his role in the fraud.

Prosecution of DBE violations is also increasing at the state level. Most recently, the New York State Inspector General announced findings of alleged DBE fraud in the Tioga Downs Racino project. To meet New York state mandated DBE percentages, contractors on the Racino project used pass-through DBEs; however, all the work and materials were supplied by non-diverse entities. Emails revealed the parties were aware of the purpose of the arrangement — to meet the NY State mandates for DBE participation. Charges have not been filed, but many expect they will be.

In response to the disconnect between federal and state DBE mandates and the limited number of qualified DBE contractors, trade organizations are stepping up. Rather than continuing to find shortcuts, mentoring programs for DBEs have become increasingly popular. These programs connect prospective and existing DBE entrepreneurs with successful business leaders in the industry. The mentors provide mentoring on best business practices, risk allocation, safety, personnel management, etc.

If you are considering leveraging DBE partnerships to win more government or private contracts, retaining legal counsel to provide you with proper advice is critical. The lawyers of Saxton & Stump’s Construction Law Group can assist in advising on proper DBE participation and drafting teaming agreements.

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