

11-1-1972

Public Contracts -- Small Business Act of 1958 -- Constitutional Law -- Denial of Due Process of Law and Equal Protection in Placement of Government Contracts with Firms Owned by "Disadvantaged Persons" Pursuant to Section 8(a) of the Small Business Act of 1958 -- Ray Baillie Trash Hauling, Inc. v. Kleppe

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Recommended Citation

Charles S. Johnson III, *Public Contracts -- Small Business Act of 1958 -- Constitutional Law -- Denial of Due Process of Law and Equal Protection in Placement of Government Contracts with Firms Owned by "Disadvantaged Persons" Pursuant to Section 8(a) of the Small Business Act of 1958 -- Ray Baillie Trash Hauling, Inc. v. Kleppe*, 14 B.C.L. Rev. 148 (1972), <http://lawdigitalcommons.bc.edu/bclr/vol14/iss1/7>

CASE NOTES

Public Contracts—Small Business Act of 1958—Constitutional Law—Denial of Due Process of Law and Equal Protection in Placement of Government Contracts with Firms Owned by “Disadvantaged Persons” Pursuant to Section 8(a) of the Small Business Act of 1958—*Ray Baillie Trash Hauling, Inc. v. Kleppe*.¹—At the request of the Small Business Administration (SBA), prime contracts for the hauling and disposal of refuse from Homestead Air Force Base, Florida, were set aside by the Air Force in 1968 and 1969² in order that the work be placed with small business concerns.³ These contracts were subsequently awarded by the Air Force after formal advertising and competitive bidding restricted to small businesses. The SBA and the Air Force then arranged for the placement of the 1970 Homestead refuse-disposal contract by a different method. Pursuant to regulations ostensibly promulgated under the authority of Section 8(a) of the Small Business Act,⁴ the prime contract for 1970 was placed directly

¹ 334 F. Supp. 194 (S.D. Fla. 1971).

² Small business “set-aside” contracts are authorized by § 2(8)(b)(11) of the Small Business Act of 1958, which gives the SBA the power

to make studies and recommendations to the appropriate Federal agencies to insure that a fair proportion of the total purchases and contracts for property and services for the Government be placed with small-business enterprises, to insure that a fair proportion of Government contracts for research and development be placed with small-business concerns, to insure that a fair proportion of the total sales of Government property be made to small-business concerns, and to insure a fair and equitable share of materials, supplies, and equipment to small-business concerns. . . .

15 U.S.C. § 637(b)(11) (1970). In 1968 the successful bidder on the Homestead set-aside contract for refuse hauling and disposal was the South Florida Sanitation Co. of Dade County, which received the contract at a price of \$42,245. In 1969 the successful bidder was the L&J Waste Service, which received the contract at a price of \$49,116. 334 F. Supp. at 197.

³ Section 2 of the Small Business Act contains the following definition of a “small-business” concern:

For the purposes of this chapter, a small-business concern shall be deemed to be one which is independently owned and operated and which is not dominant in its field of operation. In addition to the foregoing criteria the Administrator, in making a detailed definition, may use these criteria, among others: number of employees and dollar volume of business. Where the number of employees is used as one of the criteria in making such definition for any of the purposes of this chapter, the maximum number of employees which a small-business concern may have under the definition shall vary from industry to industry to the extent necessary to reflect differing characteristics of such industries and to take proper account of other relevant factors.

15 U.S.C. § 632 (1970).

⁴ 15 U.S.C. § 637(a) (1970) provides as follows:

It shall be the duty of the Small Business Administration, and it is empowered, whenever it determines such action is necessary—

- (1) to enter into contracts with the United States Government and any department, agency, or officer thereof having procurement powers obligating the Administration to furnish articles, equipment, supplies, or materials to the Government. In any case in which the Administration certifies to any

with the SBA. The SBA in turn subcontracted the work, without advertising or competitive bidding, to All American Waste, Inc., a black-owned firm which had been organized with financial and managerial assistance from the SBA.⁵ The 1971 Homestead refuse disposal contract was again placed with the SBA pursuant to this new procedure. When three small non-minority refuse-disposal firms were informed that the SBA was again planning to award the subcontract to All American, they demanded an opportunity to compete for the job.⁶ This demand was rejected by the SBA, and the 1971 Homestead subcontract was awarded to All American.

Shortly thereafter, the non-minority disposal firms brought suit in the United States District Court for the Southern District of Florida, alleging that the SBA's new contracting procedure was without statutory authority and that the plaintiffs' constitutional rights of due process and equal protection had been violated. By order of the district court, performance of the 1971 subcontract was held in abeyance, and the prior subcontract was extended to October 25, 1971. Subsequently, on a motion for summary judgment, the district court HELD: the program administered by the SBA under which subcontracts are awarded on a non-competitive basis to firms owned by socially or economically disadvantaged persons is without congressional authorization. Further, finding that the program utilizes race, color, and ethnic origin as its primary criteria for eligibility, the court concluded

officer of the Government having procurement powers that the Administration is competent to perform any specific Government procurement contract to be let by any such officer, such officer shall be authorized in his discretion to let such procurement contract to the Administration upon such terms and conditions as may be agreed upon between the Administration and the procurement officer; and

(2) to arrange for the performance of such contracts by negotiating or otherwise letting subcontracts to small-business concerns or others for the manufacture, supply, or assembly of such articles, equipment, supplies, or materials, or parts thereof, or servicing or processing in connection therewith, or such management services as may be necessary to enable the Administration to perform such contracts.

The subcontracting program authorized under § 2(8)(a) of the Small Business Act of 1958 will hereinafter be referred to as the 8(a) program inasmuch as the SBA regulations and the court utilize this nomenclature.

⁵ The subcontract was awarded to All American for a price of \$65,000, which was arrived at by a computation of estimated cost plus allowance for a reasonable profit. Shortly after its receipt of the Homestead subcontract, All American was able to underbid a "non-minority" refuse-disposal firm on several of the latter firm's largest commercial accounts, causing it to lose an estimated 40% of its gross revenues. 334 F. Supp. at 197.

⁶ The complaining firms included South Florida Sanitation Co. and L&J Waste Service, which had previously been successful in competing for the Homestead contract under the "set-aside" procedure. They alleged that denial of the opportunity to bid deprived them of between 45% and 85% of their gross annual revenues. Joining these two firms was Ray Baillie Trash Hauling, Inc., the firm which claimed to have lost its major private contracts as a result of the action of the Air Force and the SBA. Named as defendants in the suit were the Administrator of the SBA, the Secretary of the Air Force, All American Waste and the contracting officer at Homestead Air Force Base.

that non-minority-owned firms are deprived of property without due process and denied equal protection of the laws. Finding that the language of section 8(a) does not release the SBA from the statutory requirement that government contracts be competitively offered, the court ordered that the Homestead subcontract be awarded on the basis of the maximum competitive bidding practicable among small business concerns.⁷

The *Ray Baillie* decision is significant in that it represents the most successful challenge thus far made to the SBA's utilization of its small-business subcontracting power—a power derived from Section 8(a) of the Small Business Act⁸—as part of the recently announced effort by the federal government to encourage the development of minority business enterprises. This note will examine the *Ray Baillie* court's treatment of the SBA's small-business subcontracting power and suggest possible additional sources of statutory authority for that subcontracting program which were overlooked by the court. The note will also examine the *Ray Baillie* decision in the light of present notions of due process and equal protection.

Section 8(a) of the Small Business Act authorizes the SBA to enter into procurement contracts with other government agencies and to arrange for the performance of such contracts by placing subcontracts with small business concerns.⁹ The first regulations implementing section 8(a) were promulgated in 1958.¹⁰ In 1970, a new set of implementing regulations was published,¹¹ differing from the original regulations in two major respects. First, unlike the original regulations, the 1970 regulations¹² provided that subcontracts be awarded to small business concerns on a regular basis without regard to the general policy of Congress—expressed on more than one occasion—favoring formal advertising with competitive bidding as the preferred method to be employed by federal agencies in awarding contracts.¹³ The 1970 regulations also differed from the original regulations in that they

⁷ 334 F. Supp. at 202-03.

⁸ See Section 8(a) of the Small Business Act, note 4 supra. In this casenote, the terms "subcontracting power" and "small-business subcontracting power" will be used interchangeably to refer to the power reposed in Section 8(a).

⁹ See note 4 supra.

¹⁰ 13 C.F.R. §§ 124.8-1 et seq. (1958).

¹¹ 13 C.F.R. §§ 124.8-1 et seq. (1972).

¹² 13 C.F.R. §§ 124.8-1, 124.8-2 (1972).

¹³ Procurement of goods and services by military and civilian agencies of the federal government is carried on by two methods: formal advertising and negotiation. When the former method is used, the Government publishes general invitations for bids, and bids are received according to a procedure prescribed in the Federal Property and Administrative Services Act of 1949, 41 U.S.C. § 252 (1970). Contracts are awarded to the bidder whose bid conforms to all of the requirements contained in the invitation to bid and is considered the most advantageous to the Government in terms of price, delivery and other factors. Negotiation refers to methods of procurement other than by formal advertising, including sole-source negotiation as well as informal competition among several firms specifically invited to bid. Of the two methods, formal advertising is the one preferred by Congress. 10 U.S.C. §§ 2302, 2304; 41 U.S.C. § 252 (1970).

authorized the use of the 8(a) subcontracting authority exclusively for the purpose of assisting small businesses owned by "disadvantaged persons."¹⁴ The court in *Ray Baillie* concluded that these 1970 innovations in the 8(a) program had been promulgated by the SBA without any congressional authorization.¹⁵ Further, the court noted that there was nothing in the history of the small-business subcontracting power or in the language of Section 8(a) of the Small Business Act which revealed any intention on the part of Congress either to create an exception to the general requirement that government contracts be competitively offered or to create a program for the benefit of firms owned by disadvantaged persons.¹⁶

In examining the court's conclusion that the 1970 innovations in the 8(a) regulations were without statutory authorization, it will be helpful to review briefly the history of the small-business subcontracting power. Under the Defense Production Act Amendments of 1951,¹⁷ Congress entrusted the prototype of the small-business subcontracting power to the Small Defense Plants Administration (SDPA). The SDPA was authorized, under the Defense Production Act Amendments of 1951, to enter into contracts with other government agencies and to subcontract to small business concerns "without regard to any other provision of law," such as the ordinary requirements of formal advertising and competitive bidding, whenever such action would facilitate the prosecution of the war in Korea.¹⁸ This procurement-assistance power was originally created as an emergency measure to assure that small businesses would not be bypassed in the rush to meet wartime procurement needs; it was to be used only as a last resort, when other efforts to include small businesses in wartime production had failed. After the war, the power was to be retained for use in emergencies so that, when necessary, competitive procedures could be bypassed to insure small business participation in the Government's emergency

¹⁴ 13 C.F.R. § 124.8-1 (1972).

¹⁵ 334 F. Supp. at 202.

¹⁶ *Id.*

¹⁷ Act of July 31, 1951, ch. 275, 65 Stat. 131.

¹⁸ Under the 1951 Defense Production Act amendments, the SDPA was expressly authorized to contract with other federal agencies and subcontract to small businesses "without regard to any provision of law except the regulations prescribed under Section 201 of the First War Powers Act, 1941, as amended." Act of July 31, 1951, ch. 275, § 110, 65 Stat. 140-41. Section 201 of the War Powers Act authorized contracting "without regard to the provisions of law relating to the making, performance, amendment or modification of contracts," whenever such action would facilitate the prosecution of the war. Act of December 18, 1941, ch. 593, 55 Stat. 839. On February 2, 1951, President Truman issued Exec. Order No. 10210, 16 Fed. Reg. 1049 (1951), by which he authorized certain specified agencies, including the Department of Defense, to exercise the contracting power granted by section 201, specifically providing that "[a]dvertising, competitive bidding, and bid, payment, performance or other bonds or other forms of security need not be required." *Id.* This order, like the Defense Production Act of 1950 and its amendments, came as a response to the critical situation of the Korean War and authorized only temporary action.

efforts.¹⁹ Then, in 1953, Congress passed the first Small Business Act,²⁰ establishing the SBA as a peacetime successor to the SDPA. The 1953 Act transferred to the SBA many of the powers of the SDPA, including the small-business subcontracting power. However, the Small Business Act of 1953 contained no authorization, such as that contained in the 1951 Defense Production Act Amendments, to exercise the subcontracting power "without regard to any other provision of law."²¹

In 1958, Congress enacted the second Small Business Act²² and included therein the present section 8(a), explicitly authorizing subcontracting. The SBA then promulgated the first regulations governing the 8(a) program. These regulations stated that the subcontracting power was being reserved for activation only during periods of emergency, and that any subcontracting undertaken under that power would utilize publicized competition and standard procurement procedures.²³ The 1958 8(a) regulations remained in force until they were superseded by the 1970 regulations.²⁴ The 1970 regulations, as noted

¹⁹ 334 F. Supp. at 199. See also Boskoff, *The Small Business Administration and Its Minority Subcontracting Program*, ABA Section of Public Contract Law, 7 *Public Contract Newsletter: Federal, State and Local Government Contracts* No. 2 at 11-12 (1972).

²⁰ Act of July 30, 1953, ch. 282, 67 Stat. 235.

²¹ The *Ray Baillie* court considered the absence of this phrase from the 1953 Act to be a fact of major significance, although it saw no similar significance in the Act's direction to arrange for the performance of 8(a) contracts "by negotiating or otherwise letting subcontracts." 334 F. Supp. at 202. See note 46 *infra*.

²² Prior to the passage of the 1958 Act, the SBA stated in its 1958 Report to Congress that the subcontracting power had not been used and that there was no intention to use the power in the future. The report concluded with the recommendation that the power be continued on a standby basis for use in emergencies only. 334 F. Supp. at 199. However, the House Committee on Small Business did not accept this approach. See text at note 33 *infra*.

²³ 13 C.F.R. § 124.8-1 (1958) began by paraphrasing paragraph (1) of Section 8(a) of the Small Business Act (see note 4 *supra*), but it made no mention of the provisions of paragraph (2). It went on to state that "this prime contracting authority has been placed on a standby basis and will be activated as required to protect the interests of small business." It then continued as follows:

(b) Standard Government procurement contracts, forms and procedures applicable to civilian agencies in effect at the time of such contracting will be utilized by SBA in making prime contracts and subcontracts.

13 C.F.R. § 124.8-2 (1958) provided as follows:

(a) During periods of emergency determined by the Administrator to warrant exercise by SBA of its prime contract authority, SBA will review procurement plans and programs of other Government departments and agencies to determine the contracts for property, equipment, supplies, or materials which SBA should undertake to furnish to the Government through the exercise of its prime contracting authority. Upon making such determination, SBA will make the certification provided for in section 8(a)(1) of the Small Business Act and will enter into a formal contract with the procuring agency. Thereafter, SBA will widely publicize its requirements and fully utilize its facilities listing in soliciting bids or proposals. Awards will then be made to the best qualified supplier, price and other factors considered.

²⁴ 13 C.F.R. § 124.8-2 (1972) provides as follows:

(a) Concerns may submit applications for consideration under this program to SBA regional or district offices. Applications will include complete information regarding the concern's qualifications and capabilities to perform a contract.

above, differ from the original regulations in that they do not restrict the use of subcontracting power to emergency use, and they do not prescribe formal advertising as the sole method to be employed in awarding subcontracts.

Furthermore, the 1970 regulations announce a new policy of the SBA to employ the subcontracting authority "to assist small concerns owned by disadvantaged persons to become self-sufficient, viable businesses capable of competing effectively in the marketplace."²⁵ Pursuant to this new policy, the regulations provide that to be eligible for an 8(a) subcontract, a firm must be "owned or destined to be owned by socially or economically disadvantaged persons."²⁶ The new regulations further define the standards of eligibility by stating that "this category [of disadvantaged persons] often includes, but is not restricted to, Black Americans, American Indians, Spanish Americans, Oriental Americans, Eskimos and Aleuts."²⁷

After tracing this statutory and regulatory development of the SBA's small-business subcontracting power, the court in *Ray Baillie* determined that Congress intended the power to be exercised in the manner prescribed by the 1958 8(a) regulations, i.e., on a competitive basis during emergencies for the benefit of small businesses as a class. This finding was inescapable, the court concluded, for several reasons. First, the court noted that Congress, "in reposing the 8(a) power in the SBA restricted the power by removing from it the right to exercise . . . [the subcontracting power] without regard to any other provision of law."²⁸ Further, the court reasoned, Congress did not intend the 8(a) subcontracting power to be utilized for the benefit of "socially or economically disadvantaged persons."²⁹ Since the 1970 regulations differed significantly from the original regulations, which were thought by the court to express the intent of Congress, the court concluded that the 1970 innovations were unauthorized and therefore illegal.³⁰

It is submitted that the failure of the court to find any legal authority for the 8(a) program as administered under the 1970 regu-

(b) SBA will review procurement programs of other Government departments and agencies and identify proposed procurements suitable for performance by potential subcontractors.

(c) SBA will determine if a potential subcontractor is competent to perform a specific contract and will conduct appropriate negotiations with the other agency or department for the proposed procurement contract. Upon the request of the other agency or department, SBA will certify that the Administration is competent to perform the contract. Upon agreement as to terms, including price, SBA and the agency will enter into a prime contract using forms and provisions prescribed by statute and regulations applicable to the other Government agency. Thereafter, SBA will enter into appropriate subcontracts with the subcontractors for the performance of the prime contract.

²⁵ 13 C.F.R. § 124.8-1(b) (1972).

²⁶ 13 C.F.R. § 124.8-1(c) (1972).

²⁷ *Id.*

²⁸ 334 F. Supp. at 200.

²⁹ *Id.* at 202.

³⁰ *Id.* at 200-01.

lations is due primarily to the fact that the court's search for authority was incomplete in several respects. Because the 1958 subcontracting regulations were promulgated in virtual contemporaneity with the passage of Section 8(a) as part of the 1958 Small Business Act, the court too readily assumed that those original regulations accurately reflected the intent of Congress. Furthermore, the court mistakenly assumed that the Small Business Act is the sole source of the SBA's authority, and that inquiry into the nature of the subcontracting power as authorized by law should therefore end with the passage of the 1958 Act and its implementing regulations. The court also failed to consider the details of the government's general contracting policy as they relate to the facts of this particular case. That this incomplete treatment of the issue of statutory authorization led the court into much unnecessary difficulty and, ultimately, to an erroneous decision should be evident from the following analysis.

On the basis of the contemporaneity of the 1958 subcontracting regulations with the enactment of Section 8(a), and the similarity of the subcontracting program outlined in those regulations to the program authorized by the first Small Business Act, the court determined that the "emergency-use-only" approach of those original regulations accurately reflected the intent of Congress.⁸¹ However, the court neglected to consider factors which could lead to the conclusion that Congress *did not* intend to restrict the subcontracting power to use only in emergencies. First of all, there is no such limitation in the statute itself, which provides that the SBA can exercise its 8(a) powers "whenever it determines such action is necessary."⁸² Furthermore, the "emergency-use-only" approach contained in the 1958 SBA regulations appears to have been expressly rejected by Congress. The House Select Committee on Small Business made the following statement in 1960 regarding employment of the 8(a) power:

It is the conclusion of the committee that the interpretation of this Section of the act by SBA is too narrow and limited; that it was the intention of Congress that it would be used whenever necessary to assure that small business receives its fair share of Governmental procurement and not just in "national emergency." The committee believes that small business is not getting its fair share, and that there could very well be instances wherein the assuming of prime contracts by SBA for the purpose of letting subcontracts would be feasible.⁸³

Hence the original 8(a) regulations, at least insofar as those regulations provided that the small-business subcontracting power was avail-

⁸¹ *Id.* at 200.

⁸² 15 U.S.C. § 637(a) (1970).

⁸³ H.R. Rep. No. 2235, 86th Cong., 2d Sess. 81 (1960). A 1958 report that shows the SBA's "narrow and limited" interpretation is mentioned in note 22 *supra*.

able for use only in emergencies, do not appear to have reflected accurately congressional intent regarding that power. Rather, it would appear that the restriction of the 8(a) power to use in emergencies, originally contained in the 1951 Defense Production Act Amendments, was incorporated into the 1958 subcontracting regulations contrary to the express will of Congress.

The court in *Ray Baillie* also failed to realize that the Small Business Act, read in isolation, does not adequately reflect the full congressional and executive design regarding the 8(a) subcontracting authority. After tracing the legislative history of that power up to the passage of the Small Business Act of 1958, the court made no further inquiry as to other possible sources of authority for the subcontracting program as it is presently administered. As a result, the *Ray Baillie* court failed to discern that much of the SBA's authority to utilize the 8(a) subcontracting power on behalf of "socially" and "economically" disadvantaged persons is conferred by other statutes and by executive orders promulgated since 1958.

One major post-1958 source of SBA authority is Title IV of the Economic Opportunity Act,⁸⁴ which has as one of its purposes "to assist in the . . . strengthening of small business concerns and improve the managerial skills employed in such enterprises, with special attention to small business concerns . . . owned by low income individuals . . ."⁸⁵ Pursuant to this purpose, Title IV directs the SBA to provide technical and financial assistance to eligible firms and specifically requires that:

The Administrator of the Small Business Administration shall take such steps as may be necessary and appropriate, in coordination and cooperation with the heads of other Federal departments and agencies, so that contracts, subcontracts, and deposits made by the Federal Government or in connection with programs aided with Federal funds are placed in such a way as to further the purposes of this [title]. . . .⁸⁶

This section, it is submitted, clearly provides express authorization for the SBA to conduct a program, such as 8(a), which places government

⁸⁴ 42 U.S.C. §§ 2901-07 (1970).

⁸⁵ 42 U.S.C. § 2901 (1970).

⁸⁶ 42 U.S.C. § 2906c (1970). The court in *Ray Baillie* attached great significance to the definition of "financial assistance" contained in Section 609 of the Economic Opportunity Act, which includes within the meaning of that term "assistance advanced by grant, agreement, or contract, but . . . not . . . the procurement of plant or equipment, or goods or services. . . ." 42 U.S.C. § 2949 (1970). This section was interpreted by the court as prohibiting the award of procurement contracts as part of the SBA's program of financial assistance. 334 F. Supp. at 201. However, in light of the express provision of 42 U.S.C. § 2906c, it appears that section 609 was intended not to prohibit the award of procurement contracts, but merely to prohibit administrators from giving away Government *property* as part of any program of financial assistance.

contracts with those firms that Title IV is designed to benefit, e.g., small business concerns owned by "low-income individuals." Congress appears to have been concerned that the term "low-income individuals" would be inadequate to describe the owners of firms eligible for contract assistance under Title IV, for they authorized the Administrator of the SBA "to define the meaning of low income as it applies to owners of small business concerns eligible to be assisted under this [title]. . . ."⁸⁷

The SBA was not without guidance as to the factors it was to consider in creating a definition of "low-income" pursuant to Title IV. There were some indications that at least part of the Title IV program should be directed toward members of disadvantaged racial minorities. The Senate Committee on Labor and Public Welfare, in its Report on the 1967 Amendments to the Economic Opportunity Act, urged adoption of the present Title IV in the following words: "The Committee feels that an important priority of the anti-poverty effort must be to expand the opportunities for a stake in community economic life for low-income persons *and minority group members*, especially in the urban ghettos."⁸⁸ The SBA was given further guidance and direction in its efforts to define low-income as it relates to eligibility for Title IV benefits by two executive orders which were issued between the enactment of the present Title IV and the promulgation of the present 8(a) regulations.⁸⁹ On March 5, 1969, President Nixon issued Executive Order 11458, calling for the appropriate departments and agencies of the federal government to develop and coordinate a national program for *minority* business enterprise.⁴⁰ Thereafter, on March 2, 1970, the President issued Executive Order 11518, which provided for the increased representation of the interests of small business within the federal government and ordered the SBA "to particularly consider the needs and interests of minority-owned small business concerns and of members of minority groups seeking entry into the business community."⁴¹

Clearly, then, an important part of the SBA's subcontracting authority is derived from sources—Title IV and the subsequent executive orders—which came into being after the enactment of Section 8(a). The SBA has apparently chosen to utilize the 8(a) subcontracting program as a mechanism for implementing the mandates from these sources. This choice is particularly appropriate in light of the goal of

⁸⁷ 42 U.S.C. § 2906 (1970).

⁸⁸ S. Rep. No. 563, 90th Cong., 1st Sess. 65 (1967) (emphasis supplied).

⁸⁹ Executive Orders have the force and effect of law. *Farmer v. Philadelphia Electric Co.*, 329 F.2d 3, 7 (3d Cir. 1964); *Contractors Ass'n. v. Schultz*, 311 F. Supp. 1002, 1009 (E.D. Pa. 1970), *aff'd*, 442 F.2d 159 (3d Cir.), cert. denied, 404 U.S. 854 (1971).

⁴⁰ 34 Fed. Reg. 4937 (1969). The President's power to establish equal opportunity programs was established in *Farkas v. Texas Instrument Corp.*, 375 F.2d 629 (5th Cir.), cert. denied, 389 U.S. 977 (1967). Cf. *Farmer v. Philadelphia Electric Corp.*, 329 F.2d 3, 7-8 (3d Cir. 1964).

⁴¹ 35 Fed. Reg. 4939 (1970).

Title IV to arrange for the placement of government contracts with firms owned by low-income individuals. The use in the 1970 8(a) regulations of social or economic disadvantage as the standard of eligibility under the program appears to be pursuant to the authorization in Title IV to further "define the meaning of low income."⁴² Finally, as will be demonstrated below, utilization of ethnic terms as part of the auxiliary standards of eligibility is an attempt to implement the mandate of Executive Orders 11458 and 11518 to encourage the development of minority business enterprises.⁴³ Thus it appears that the new policy announced in the 1970 8(a) regulations, by which the benefits of the small-business subcontracting program are directed toward firms owned by disadvantaged persons, is authorized by Congress and the Executive, contrary to the finding of the *Ray Baillie* court.

In finding that the SBA, by promulgating its 1970 8(a) regulations, had created an unauthorized exception to the congressional policy favoring the use of formal advertising and competitive bidding in the placement of government contracts,⁴⁴ the court in *Ray Baillie* appears to have assumed that this policy represents a strict statutory requirement. However, the legislative preference for publicized competition is far from absolute. There is some authority to the effect that this policy governs only prime contracts awarded directly to private concerns, and does not apply to situations in which the SBA holds a prime contract and does its own subcontracting to small business concerns under section 8(a).⁴⁵ Moreover, section 8(a) on its face pro-

⁴² Approval by the Chief Executive of the standards of eligibility contained in the 1970 8(a) regulations is evidenced by a subsequent Executive Order. On October 14, 1971, Executive Order 11458 was superseded by Executive Order 11625, 36 Fed. Reg. 19967 (1971), which directed each federal department or agency to continue all current efforts to foster and promote minority business enterprises. That order contained the following definition of the class which its provisions were intended to benefit:

(a) "Minority business enterprise" means a business enterprise that is owned or controlled by one or more socially or economically disadvantaged persons. Such disadvantage may arise from cultural, racial, chronic economic circumstances or background or other similar cause. Such persons include, but are not limited to, Negroes, Puerto Ricans, Spanish-speaking Americans, American Indians, Eskimos, and Aleuts.

Id. at 19970.

⁴³ The further definition created by the SBA in the 1970 regulations appears to be well within the scope of authority traditionally committed to administrative agencies. It has long been recognized that, in the establishment of a governmental program, "Congress may declare its will and after fixing a primary standard, devolve upon administrative officers the 'power to fill up the details' by prescribing administrative rules and regulations." *United States v. Shreveport Grain & Elevator Co.*, 287 U.S. 77 (1932).

⁴⁴ 334 F. Supp. at 202.

⁴⁵ Judge Wyzanski of the District of Massachusetts has stated, in a case similar to the *Ray Baillie* case in terms of the facts and issues presented, that the procurement statutes "are wholly inapplicable to a contract made by the Department of Defense with the SBA which has specific statutory authority to enter into this type of contract." *Kleen-Rite Janitorial Services, Inc. v. Laird*, No. 71-1968-W (D. Mass. Sept. 21, 1971). The challenge to 8(a) subcontracting in *Kleen-Rite* was made on constitutional grounds, however, and the legal authority for the 1970 8(a) regulation was not directly questioned.

claims an exception to the general requirement of formal advertising.⁴⁶ Not only does the section permit negotiation in the placement of subcontracts, but—by use of the words “or otherwise letting”—it gives the SBA discretion in choosing the manner in which its subcontracts are let.

From the above investigation it appears that the court in *Ray Baillie* was led into error through its failure to inquire thoroughly into the legal authority underlying the 1970 subcontracting regulations. The court's willingness to accept automatically the “emergency-use-only” approach of the first subcontracting regulations as expressive of the intent of Congress prevented consideration of persuasive indications that the SBA is authorized to let subcontracts whenever it determines that such action is necessary. By limiting inquiry into the legislative and administrative history of the subcontracting power, the court failed to discover a portion of that history which was of particular relevance to the case it was considering. By assuming that the congressional preference for publicized competition in awarding contracts is absolute, the *Ray Baillie* court permitted itself to remain ignorant of a relevant exception to this preference. A thorough inquiry into the derivation of the innovation in the 1970 8(a) subcontracting regulations must yield the conclusion that the new regulations are fully authorized by law.

The *Ray Baillie* court found the placement of subcontracts under the 1970 8(a) regulations invalid not only on the ground of a lack of authority, but on constitutional grounds as well. The court determined that the complaining “non-minority” firms had been denied their Fifth and Fourteenth Amendment rights to equal protection of the laws by the placement of the Homestead subcontracts with All American pursuant to the 1970 8(a) regulations.⁴⁷ The court further found that the utilization of government lending and contracting powers to enhance All American's competitive advantage in the private commercial field “violates plaintiffs' rights under the Fifth Amendment . . . in that it serves to deprive them of their property without due process of law.”⁴⁸ These conclusions were stated summarily by the court without

⁴⁶ The Small Business Act authorizes procurement by negotiation in Section 8(a)(2), which provides that the SBA has the power and the duty “to arrange for the performance [of its contracts with other government agencies] by negotiation or otherwise letting subcontracts to small business concerns.” 15 U.S.C. § 637(a)(2) (1970) (emphasis supplied). See note 4 supra. The *Ray Baillie* court, which considered only section 8(a)(1), failed to notice this provision. Each of the statutes cited by the *Ray Baillie* court as expressive of the congressional preference for competition and formal advertising contains a long list of exceptions. Among the exceptions listed in the Armed Services Procurement Act of 1947, 10 U.S.C. § 2304 (1970), as well as in the Federal Property and Administrative Services Act of 1949, 41 U.S.C. § 252(c)(15) (1970), is one to the effect that publicized competition is not required where negotiation is “otherwise authorized by law.” Several examples of negotiation “otherwise authorized by law” are listed in the regulations promulgated pursuant to the Federal Property and Administrative Services Act. Among the examples listed in that regulation is “negotiation permitted by the Small Business Act.” 41 C.F.R. § 18-3.217-3 (1972).

⁴⁷ 334 F. Supp. at 202.

⁴⁸ *Id.*

citation of any judicial authority, and, it is submitted, resulted from a misapplication of the doctrines of equal protection and due process.

In reaching the conclusion that the plaintiffs' right to equal protection had been denied, the court considered the text of the 1970 8(a) regulations as well as the affidavits of the Chiefs of the Procurement and Management Assistance Division for SBA's regional offices in Atlanta and Boston.⁴⁹ The statements of both of these officials indicated that 8(a) benefits had not been restricted to members of ethnic minorities and that, while most of the 8(a) subcontracts had been awarded to non-whites, a small number of Caucasians had in fact received subcontracts under the new program.⁵⁰ On the basis of this evidence the court found that "whites" were not eligible for 8(a) subcontracts except on a token basis, and that the primary criteria for eligibility under the 8(a) program as presently administered are race, color, or ethnic origin. Finding "no evidence that the members of 'minority' groups identified in the substitute 8(a) regulations have been discriminated against in the formation and operation of small business concerns by reason of race, color, or ethnic origin,"⁵¹ the court determined that the exclusion of whites from 8(a) benefits "represents invidious discrimination against them."⁵²

This charge of "reverse discrimination" levelled by the court against the SBA is one which is being raised with increasing frequency now that affirmative action⁵³ is being taken in the public and private sectors to remedy the effects of past racial oppression.⁵⁴ So far as *Ray*

⁴⁹ In addition to the affidavit of John T. Scruggs, Atlanta Regional Director of Procurement and Management Assistance, the court considered the affidavit of Boston official David C. Buell. Buell's affidavit had originally been filed in the similar case of *Kleen-Rite Janitorial Services, Inc. v. Laird*, No. 71-1968-W (D. Mass. Sept. 21, 1971).

⁵⁰ The affidavit of John T. Scruggs contained the following statement:

In determining whether one is socially or economically disadvantaged, reliance is not placed on a single factor but rather on a composite of all the factors. In addition, the Regulations promulgated with respect to 8(a) contracts apply equally to members of all races. Thus, a Caucasian may be found to be socially or economically disadvantaged and thereby eligible for participation in this program. Moreover, within my jurisdiction the Agency has awarded approximately 225 8(a) contracts. Of this number, 212 were awarded to Black Americans, eight to Spanish-Americans, two to American Indians, and three were awarded to Caucasians.

334 F. Supp. at 198.

⁵¹ *Id.* at 202.

⁵² *Id.*

⁵³ "Affirmative action," in the employment context, is the policy of developing programs which shall provide in detail for specific steps to guarantee equal employment opportunity keyed to the problems and needs of members of minority groups, including when there are deficiencies, the development of specific goals and timetables for the prompt achievement of full and equal employment opportunity.

Contractors Ass'n of Eastern Pa. v. Schultz, 311 F. Supp. 1002, 1009 (E.D. Pa. 1970), *aff'd*, 442 F.2d 159 (3d Cir.), cert. denied, 404 U.S. 854 (1971). See also *Nash, Affirmative Action Under Executive Order 11,246*, 46 N.Y.U.L. Rev. 225, 226 (1971).

⁵⁴ See *Contractors Ass'n of Eastern Pa. v. Schultz*, 311 F. Supp. 1002 (E.D. Pa. 1970), *aff'd*, 442 F.2d 159 (3d Cir.), cert. denied, 404 U.S. 854 (1971), where the court

Baillie is concerned, however, it is difficult to reconcile a finding of unconstitutional "reverse discrimination" with the facts of the case or with present notions of equal protection.

The court found that the racial neutrality of the term "socially or economically disadvantaged persons" in the description of persons eligible for 8(a) subcontracts under the 1970 regulations was of little significance. According to the court, the primary criterion for eligibility under the new 8(a) regulations is racial, and therefore unconstitutionally discriminatory against white firms. In several respects, the facts of the case could lead to a contrary conclusion. A careful reading of the new regulations reveals that the "racial" or "ethnic" terms used represent auxiliary guidelines to aid in determining the identity of those persons who satisfy the primary, racially neutral criterion of being "socially or economically disadvantaged." As Judge Wyzanski of the District of Massachusetts has said in commenting upon the new 8(a) program, "social and economic classifications are common in welfare and other legislation, and have . . . not been regarded as unconstitutional on that ground."⁵⁵ That the primary criteria for eligibility under the new regulations are social and economic rather than "racial" is indicated by the statements, in the new regulations as well as in the affidavits before the court,⁵⁶ that eligibility is not limited to the "racial" groups described. The suggestion of SBA "tokenism" toward white firms⁵⁷ is largely dispelled when the proportion of contracts awarded through the 8(a) program is compared with the overall volume of contracts placed with SBA assistance. In this larger view of SBA con-

was faced with the constitutionality of the Philadelphia Plan. The Philadelphia Plan required bidders on federal or federally assisted construction contracts that exceeded \$500,000 to "take affirmative action to insure that applicants are employed . . . without regard to their race, color, religion, sex or national origin." 311 F. Supp. at 1005 (quoting Exec. Order No. 11,246, § 202(1), 3 C.F.R. 418, 419 (1972)). Plaintiffs argued that the Plan violated Title VII of the Civil Rights Act of 1964, 42 U.S.C. §§ 2000e et seq. (1970), in that the contractors would be required to "hire and employ on the basis of and with regard to race, color and national origin" because the Plan "imposes racial 'quotas'; . . . requires 'preferential' treatment for minority persons and so creates reverse discrimination or in the ordinary context, the contractors, in order to meet his goals would necessarily have to discriminate against white persons in order to hire minority applicants." 311 F. Supp. at 1008. The court, however, rejected these contentions, and concluded the Plan was not in conflict with Title VII. In reaching this conclusion, the court noted that the Plan did not require that a certain percentage of minority individuals be hired, but only that a contractor make a good faith effort to meet the required goals of the Plan. Moreover, the court reasoned that the Plan would be one of "inclusion rather than exclusion" and that the "strength of any society is determined by its ability to open doors and make its economic opportunities available to all who can qualify." *Id.* at 1010. See Comment, Annual Survey of Labor Relations Law, 13 B.C. Ind. & Com. L. Rev. 1347, 1368 (1972). See also Significant Developments, Legal Education—Preferential Admissions: A Constitutional Challenge, 52 B.U. L. Rev. 304 (1972).

⁵⁵ *Kleen-Rite Janitorial Services, Inc. v. Laird*, No. 71-1968-W (D. Mass. Sept. 21, 1971).

⁵⁶ See note 50 and accompanying text *supra*.

⁵⁷ 334 F. Supp. at 202.

tract assistance, aid to firms owned by "disadvantaged persons" is proportionately insignificant; by far the greater portion of SBA-assisted contracts goes to firms owned by non-disadvantaged persons.⁵⁸

Implicit in the court's finding that the 8(a) eligibility guidelines were unconstitutionally discriminatory is the assumption that all racial classifications are unconstitutional per se. However, this assumption is not consistent with present notions of equal protection. This is not to say that racial classifications are not constitutionally suspect, and not subject to strict scrutiny.⁵⁹ Any agency which erects a classification on the basis of race has the burden of establishing its validity by showing that the classification is not "invidious," that the classification is related to a compelling governmental interest, and that the classification is a rational means of implementing that interest.⁶⁰

It is submitted that such a burden is met by the SBA in justifying the use of racial terms in its 1970 8(a) regulations. The distinctive feature of section 8(a) is the fact that it dispenses with the requirement of competition and thus provides the most appropriate medium for extending contracts to firms which might otherwise be unable to compete. Unquestionably, there are groups of disadvantaged persons within the larger class of small-business owners with an especially acute need to participate in government contracts.⁶¹ These groups, because of the effects of past discrimination, racial or otherwise, have been excluded from the mainstream of economic life.⁶² In all likelihood,

⁵⁸ Of the total military and civilian contracts made available through the SBA in the two and a half years preceding the *Ray Baillie* decision, the amount for which the 8(a) program was responsible was only .28 percent of that total. The total dollar volume of all government contracts placed through SBA programs during that period was \$23,480,707,000, while the 8(a) program took up only \$65,171,560 of that total amount. From Statistics of the Department of Defense and the General Services Administration cited in the Government's Brief at 5, *Kleen-Rite Janitorial Services, Inc. v. Laird*, No. 71-1968-W (D. Mass. Sept. 21, 1971).

⁵⁹ O'Neil, *Preferential Admissions: Equalizing the Access of Minority Groups to Higher Education*, 80 *Yale L.J.* 699, 711 (1971); *Developments in the Law—Equal Protection*, 82 *Harv. L. Rev.* 1065, 1091-1101 (1969). See also *McLaughlin v. Florida*, 379 U.S. 184, 193-94 (1964), and *Skinner v. Oklahoma ex rel. Williamson*, 316 U.S. 535 (1941).

⁶⁰ *Bolling v. Sharpe*, 347 U.S. 497, 499 (1954); *Loving v. Virginia*, 388 U.S. 1, 9 (1967).

⁶¹ While the minorities mentioned in the substitute 8(a) regulations make up about 16% of the population of the United States, they account for only 3% of the 5,500,000 businesses in the United States. Stans, Report to the President on Minority Business Enterprise (Washington, D.C., 1970).

⁶² The example of America's black minority is particularly illustrative. The City of Newark, New Jersey, has approximately 400,000 people, of whom more than half are black. Of the 12,172 licensed businesses in the city, a little more than 10% are black-owned. In Los Angeles there are 600,000 black people. Of its 121,039 licensed businesses, an "almost invisible fraction" is owned by black people, and these few black-owned businesses are located principally in ghetto areas. Of the 800,000 residents of Washington, D.C., 63% are black, but only 1,500 of the 11,755 businesses—or less than 13%—are owned by black people. 1968 Annual Report of the Interracial Council for Business Opportunity, cited in T. Cross, *Black Capitalism: Strategy for Business in the Ghetto* 60 (1969). Only seven of the 17,500 authorized automobile dealers in the United States are

members of these groups would remain excluded absent affirmative corrective measures such as the 8(a) program. Thus, far from being "invidious," the racial classifications in the new 8(a) regulations are remedial.⁶³ Having as their purpose "to assist small concerns owned by disadvantaged persons to become self-sufficient, viable businesses capable of competing effectively in the marketplace,"⁶⁴ the classifications pursue the same governmental interests as those proclaimed in Title IV of the Economic Opportunity Act and in Executive Orders 11458 and 11518. Given the nexus which exists between socio-economic disadvantage and membership in the enumerated minority groups,⁶⁵ the use of racial terminology as an aid in determining the identity of "disadvantaged persons" is a rational means of implementing these governmental interests. Therefore it appears that the auxiliary guide-

black. Although 108 of this country's more than 6,000 radio stations direct their programs to black listeners, only eight radio stations in this country are black owned. Id.

⁶³ Statutes and regulations create many classifications which do not deny equal protection. It is only "invidious discrimination" which offends the Constitution. *Ferguson v. Skrupa*, 372 U.S. 726, 732 (1963). The Supreme Court has recognized that there are situations in which race may be considered in forming a remedy for past inequities. *North Carolina State Board of Education v. Swann*, 402 U.S. 43, 46 (1971); *McDaniel v. Barresi*, 402 U.S. 39, 41 (1971). In *Youngblood v. Board of Public Instruction*, 430 F.2d 625 (5th Cir. 1970), the court noted that "at this point, and perhaps for a long time, true nondiscrimination may be attained, paradoxically, only by taking color into consideration . . ." Id. at 630.

In support of its conclusion, the court in *Youngblood* cited the following passage from *United States v. Jefferson County Board of Education*, 372 F.2d 836 (5th Cir. 1966):

The Constitution is both color blind and color conscious. To avoid conflict with the equal protection clause, a classification that denies a benefit, causes harm, or imposes a burden must not be based on race. In that sense, the Constitution is color blind. But the Constitution is color conscious to prevent discrimination being perpetrated and to undo the effects of past discrimination. The criterion is the relevancy of color to a legitimate governmental purpose.

Id. at 876.

This proposition was elaborated upon in *Norwalk CORE v. Norwalk Redevelopment Agency*, 395 F.2d 920 (2d Cir. 1968), in which the court made the following observation:

What we have said may require classification by race. That is something which the Constitution usually forbids, not because it is inevitably an impermissible classification, but because it is one which usually, to our national shame, has been drawn for the purpose of maintaining racial inequality. Where it is drawn for the purpose of achieving equality it will be allowed, and to the extent that it is necessary to avoid unequal treatment by race, it will be required.

Id. at 931-32.

⁶⁴ 13 C.F.R. § 214.8-1 (1972). See note 25 and accompanying text *supra*.

⁶⁵ [T]he incidence of poverty is much higher among non-whites than among whites. In 1967, 41 percent of the non-white population was poor, compared with 12 percent of the white population. Non-whites thus constitute a far larger share of the poverty population (31 percent) than of the American population as a whole (12 percent). Moreover, the non-white proportion of the poverty population has been increasing, slowly but steadily, since the first racial count was made in 1959; it was 28 percent then, and 32 percent by 1967.

Building the American City: Report of the National Commission on Urban Problems to the Congress and the President of the United States, H.R. Doc. No. 91-34, 91st Cong., 1st Sess. 45 (1969).

lines for determining eligibility under the 1970 8(a) regulations represent a permissible classification on the basis of race, rather than an example of "invidious discrimination," and that the plaintiffs in *Ray Baillie* were not deprived of equal protection of the laws.

The final claim raised by the plaintiffs in *Ray Baillie*, and sustained by the court, involved a question of due process. One of the plaintiffs maintained that the loss of its right to bid for the Homestead contract under the 1970 regulations, coupled with the non-competitive placement of the Homestead subcontract with All American at a premium price, unfairly enhanced the competitive position of the black firm. In support of its claim of a shift in competitive advantage, this firm further alleged that the receipt of the subcontract enabled All American to submit low bids for the performance of private commercial contracts causing the complaining firm to lose several of its regular customers to All American.⁶⁶ Accepting these allegations as true, the court concluded that the SBA had deprived this plaintiff of property without due process of law by utilization of government contracting powers pursuant to the new 8(a) regulations.⁶⁷

This conclusion is difficult to reconcile with generally accepted notions of due process. It has been recognized that the federal government, when contracting for goods or services or otherwise disbursing its moneys, acts with all the prerogatives of a similarly situated private party, subject to the limitations of the Constitution.⁶⁸ The government has often utilized these broad prerogatives, which include the power to set "the terms and conditions upon which its money allotments . . . shall be disbursed"⁶⁹ and "to determine those with whom it will deal"⁷⁰ in furtherance of social or economic goals which go beyond the immediate needs of the specific procurement or allotment transaction.⁷¹ Beyond a reference to "competitive advantage," the court did not indicate the exact manner in which the SBA deprived the plaintiff of its property by awarding the Homestead subcontract pursuant to the new 8(a) regulations. However, a concern's competitive advantage is not a sufficient interest to be protected as "property" under the due process clause,⁷² as courts have been unwilling to afford a general

⁶⁶ For a discussion of a similar claim of "displacement," see Significant Developments, Legal Education—Preferential Admissions: A Constitutional Challenge, 52 B.U. L. Rev. 304 (1972).

⁶⁷ 334 F. Supp. at 201.

⁶⁸ *Perkins v. Lukens Steel Co.*, 310 U.S. 113, 127 (1940).

⁶⁹ *King v. Smith*, 392 U.S. 309, 333 n.34. (1968).

⁷⁰ 310 U.S. at 127.

⁷¹ Use of this general power is illustrated by the adoption by the Department of Labor of the Philadelphia Plan, a program designed to increase overall minority group employment in certain construction industry trades. The validity of this program was sustained in *Contractors Ass'n v. Schultz*, 311 F. Supp. 1002 (E.D. Pa. 1970), aff'd, 442 F.2d 159 (3d Cir.), cert. denied, 404 U.S. 854 (1971). See note 54 supra.

⁷² *Tennessee Electric Power Co. v. TVA*, 306 U.S. 118, 139 (1939). In this case several power companies complained that the sale of electricity by the TVA was not authorized by the constitutional mandate to improve navigation and control floods in

right within our economic system to be free from competition.⁷³ Thus, if the only injury suffered by the complaining firm was a diminution of its competitive advantage, such a claim was *damnum absque injuria*.⁷⁴ It is submitted that the non-minority plaintiff in *Ray Baillie* had no valid claim under the due process clause.

Conclusion

The foregoing analysis reveals several difficulties in the district court's treatment of the issues before it in *Ray Baillie*. These difficulties fall roughly into two categories. The first comprises problems arising from an incomplete inquiry into the sources of authority for the 8(a) program as it has been administered since 1970. The court's conclusion that Congress intended the 8(a) power to be used only in emergencies resulted from its erroneous assumption that the intent of Congress was accurately expressed in the 1958 8(a) regulations. The failure to discover the extensive legislative and executive authorization for employment of the subcontracting power as an aid to low-income individuals and members of minority groups resulted from the court's failure to investigate sources of authority other than the 1958 regulations. By failing to inquire into the details of government procurement policy or into the full text of Section 8(a) of the Small Business Act, the court left itself unadvised of the fact that Section 8(a) itself contains an exception to the general requirement of formal advertising.

The second category of difficulty relates to the court's application of the constitutional doctrines of equal protection and due process to the facts of this case. Contrary to the court's finding, the primary criteria for eligibility under the 1970 8(a) regulations are social and

the navigable waters of the nation, and that such continued sale in competition with them deprived them of property without due process of law. In the course of deciding that plaintiffs had asserted no interest sufficient to give them standing in the federal courts, the Supreme Court indicated by way of dicta that the competitive position alleged to have been injured was not a sufficient interest to merit protection as "property" under the due process clause. *Id.*

Insofar as it held that one's competitive advantage is not a sufficient interest to confer standing, the Supreme Court has modified its position since the *Tennessee Electric Power* decision. In *Investment Company Institute v. Camp*, 397 U.S. 150 (1971), plaintiffs sought a declaratory judgment invalidating a regulation of the Comptroller of the Currency which permitted national banks to compete with them in the mutual fund industry. The Supreme Court held in that case that plaintiffs had standing as competitors if (1) they suffered injury in fact from the competition, (2) the challenged regulation permitted competition which was arguably unauthorized by law, and (3) Congress had not intended to proscribe judicial review of the challenged agency action.

In the *Investment Company Institute* case, the plaintiffs' claim was based solely upon federal statutes regulating banks and securities. There was no reliance upon the Constitution and no attempt to equate "life, liberty or property" with "injury in fact." Thus, insofar as it held that one's competitive advantage is not "property" within the meaning of the due process clause, the authority of the *Tennessee Electric Power* case is not affected by the decision in *Investment Company Institute*.

⁷³ See Note, 37 Mich. L. Rev. 1134 (1939).

⁷⁴ 306 U.S. at 137.

economic, not ethnic or racial. It is submitted that the rule of "per se" unconstitutionality is not applicable to the racially-cast eligibility guidelines, inasmuch as these ethnic qualifications are merely auxiliary, and constitute a reasonable means of pursuing a remedial purpose proclaimed in executive orders of the President. Furthermore, since the operation of the 8(a) program infringes upon no right claimed in this case which the law is prepared to recognize, the contention that one of the plaintiffs had been deprived of property without due process is without merit. In using its procurement powers to further the purposes proclaimed in the 1970 8(a) regulations, and to promote economic integrations at the entrepreneurial level, the government has chosen a valid and appropriate means of remedying the economic inequities which for too long have been characteristic of American life.

CHARLES S. JOHNSON, III

Income Tax—Reallocation of Gross Income—Controlled Corporations—*Commissioner v. First Security Bank of Utah, N.A.*¹—Respondent taxpayers, First Security Bank of Utah, N.A., and First Security Bank of Idaho, N.A. (the Banks), are national banks which were wholly owned subsidiaries of First Security Corporation, a publicly owned bank holding company. First Security Corporation (the Holding Company) also controlled Ed. D. Smith & Sons (the Management Company), Smith (the Insurance Agency) and, starting in 1954, an insurance company, First Security Life Insurance Company of Texas (Security Life).

In 1948, the Banks made arrangements to offer credit life insurance to their borrowers.² Until 1954, the Banks referred all borrowers deciding to purchase this insurance to two independent insurance carriers.³ Federal banking laws prohibited the Banks from receiving sales commissions or other income from the credit insurance generated by

¹ 405 U.S. 394 (1972).

² The Tax Court lists the reasons for the Banks providing this service:

. . . (1) to offer a service increasingly supplied by competing financial institutions, (2) to obtain the benefits of the additional collateral which credit insurance provides by repaying loans upon the death, injury, or illness of the borrower, and (3) to provide an additional source of income—part of the premiums from the insurance—to Holding Company or its subsidiaries.

First Security Bank of Utah, N.A. v. Commissioner, 26 CCH Tax Ct. Mem. 1321, 1322 (1967).

³ The Banks followed a certain routine in making this insurance available to their customers. The lending officer would describe the purpose and availability of credit life insurance. If the borrower wanted the coverage, the Banks would fill out the required form, deliver a certificate to the customer, and collect the premium or add it to his loan. The completed forms were then forwarded to the Management Company which maintained the insurance records, forwarded customer premiums to the independent insurer, and processed claims filed under the policies. The Banks' costs in providing these services were estimated at \$2000. 405 U.S. at 396-97.