

SUMMARY OF FINDINGS

BLACK

Black business owners interviewed in the course of our study reported evidence of virtually every identified form of industry discrimination discussed in this report. The particularized evidence of discrimination in the telecommunications marketplace against black-owned firms encompasses examples including denials of opportunity, discrimination in technical training, customer/end user discrimination, exclusion from the "good old boy" network in subcontracting, bid shopping, bid manipulation, price discrimination by suppliers, discrimination in financing, bonding, including double standards in performance and qualifications, limited access to technology transfer, slow payment and non-payment, and stereotypical attitudes on the part of buyers and contracts managers.

HISPANIC

Hispanic business owners interviewed during the course of our study also reported evidence of racial discrimination in the telecommunications industry. Although the forms of identified discrimination adversely affecting Hispanic firms were not as numerous as that reported by blacks, there were significant similarities in several areas.

Hispanic MWBEs suffer discrimination in denials of opportunity to bid, bonding, customer/end user discrimination, exclusion from the "good old boy" subcontracting network, price discrimination by suppliers, financing, limited access to private sector

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markets, slow payments, and stereotypical attitudes towards citizenship and technical capability on the part of buyers and contract managers.⁸

ASIAN

Several Asian-American business owners were interviewed during our study. Asian MWBEs reported similar forms of discrimination as blacks and Hispanics, with the exception of "Asian- or Japan-bashing," and stereotypical attitudes towards citizenship were a key form of racial discrimination in their experiences in the telecommunications industry.

NATIVE AMERICANS

Native American MWBEs suffer a very high level of denial to contracting opportunities. Several interviewees presented evidence that their companies have been repeatedly ignored and refused the opportunity to do work for large telecommunications companies. Native Americans in the telecommunications industry reported discrimination similar to blacks, Hispanics, and Asians.⁹

PRICE DISCRIMINATION

There is considerable anecdotal evidence from MWBEs that telecommunications products and equipment suppliers frequently quote them higher prices and give them inferior credit terms to those offered to white-owned competitors. The complaints seem to follow along racial lines. Interviewees presented numerous examples of these anti-competitive practices.

⁸ Interviewees nos. 2, 4, 5, 6, 7-10, 13, 15, 16, 18, 19, 20, 22, 24, 31,

⁹ Interviewees nos. 4, 20, 22, 31, 34.

FALSE REPORTING

Interviewees provided examples of false reporting by prime telecommunications contractors. Project owners and government agencies require prime contractors to submit contracting plans for small and small disadvantaged businesses on federal projects of \$1 million or more for construction contracts and \$500,000 or more for all other contracts.

Interviewees reported that telecommunications companies often make false reports to government agencies under subcontracting plans. MWBE firms are told that their company has been selected as a small disadvantaged subcontractor under the contract, should the company be the successful bidder. When the MWBE inquires later with the successful bidder, the MWBE is given a vague reason as to why their company was not used as a subcontractor. One interviewee was told by a major telecommunications company that they could not get in touch with them, so they used another subcontractor - a white firm.¹⁰

On another project, a female interviewee related a similar experience in which a prime contractor made a false report to a government agency regarding the use of her company as a subcontractor on a large government project. The government agency later contacted the minority company to verify that he company had performed the subcontract work. The minority company informed the government agency that at no time during the project did the prime contractor inform her that her company would be listed as a subcontractor on that or any other project. The minority company never heard back from the government agency or the prime contractor again.¹¹

¹⁰ Interviewees nos. 8, 11, 16, 31, 34.

¹¹ Interviewees nos. 8, 11, 16, 31, 34.

SLOW PAYMENT AND NON-PAYMENT

Slow payment and non-payment by large white-owned firms (whether discriminatory or not) adversely affects the continued availability and capacity of minority-owned firms.

Slow payment of invoices was a consistent problem for 46.1% of all MWBE respondents (see Telecommunications Survey Results, page 10).

Financially weak and undercapitalized firms can ill afford interruptions to their cash flow. Their inability to replace working capital, due to slow or non-payment by vendors, makes these minority firms unable to fund existing work in process, and often leads to loss of profit.

A Native American woman business owner responding to the telecommunications survey wrote "the problem is they simply do not pay in a timely manner. We have had to wait for four to five months for payment from two telecommunications companies. It is very difficult for our company to survive like this. Our invoices indicate that there is a 1½% charge on all invoices over 30 days and they simply say "we do not pay late charges."¹²

A black-owned collection agency has filed a suit against a telecommunications company for alleged racial and gender discrimination, and telecommunications company's alleged non-payment for services allegedly requested by the telecommunications company.¹³

¹² Interviewees nos. 2, 5, 18, 22, 31.

¹³ U.S. District Court, Eastern District of New York. Civil Action No. CV 90-3689 (ADS).

DOUBLE STANDARDS IN PERFORMANCE AND QUALIFICATIONS

There is considerable evidence regarding discrimination against MWBEs in the form of the application of double standards. MWBEs have cited instances where they are held to higher standards than their white competitors and counterparts in terms of contract performance and required qualifications. These double standards sometimes result in MWBEs suffering termination from contracts, loss of income, denial of contract awards, or even harassment and frustration to the point of voluntary withdrawal from the market.

A Native American interviewee in the telecommunications service business stated that his Native American project managers experience more problems from other contractors, contracts managers, and employees on telecommunications jobs than do his white project managers. This interviewee asserts that his white employees get far better results from purchasing and contracts managers than do his Native American employees.¹⁴

Another Native American in the injection molding business filed a complaint with MBELDEF of constantly having his company's marketing efforts ignored by telecommunications companies -- so much so that he made an unusual request of a purchasing manager that his company's name be removed from their data base since they refused to acknowledge any of his marketing efforts, including a refusal to return numerous phone calls to the company.

¹⁴ Interviewees nos. 9, 10, 24.

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Two black American telemarketing companies have filed suits against a telecommunications company for alleged discrimination and alleged failure to do business in good faith when the telecommunications company allegedly awarded large telemarketing contracts to the companies, and allegedly terminated the companies' contracts with ten days notice, which allegedly resulted in the closure of the companies and the loss of several hundred jobs held by minority employees.

A Hispanic long distance calling company reports that it has marketed its services to numerous long-distance carriers with no success. The company states that discriminatory practices have limited the company's market to small- to medium-sized Hispanic-owned companies.¹⁵

TECHNOLOGY TRANSFER

When it comes to high technology, stereotypical attitudes about the kind of work minority businesses in the telecommunications industry are capable of performing continue to hinder the development and advancement of minority companies.

¹⁵ There are no minority-owned companies in the telecommunications industry that own a national switched telephone network. Most minority companies are being restricted to agent or switchless reseller agreements with major telecommunications carriers. A few minority companies own and operate a single switch site serving a limited market and are able to offer national calling by purchasing terminating agreements with white-owned firms with switch sites in locations where the minority companies have none.

There is a general perception that minority firms are inferior and are only capable of performing construction, landscaping, and janitorial services. Repeatedly, MWBE interviewees attempting to obtain contracts for high-technology network services or products stated they met strong resistance from major telecommunications companies and experienced very limited success.

One black telecommunications company has filed suit against a telecommunications company for its alleged failure to live up to its agreement to provide technology transfer for the company to manufacture a special high-technology switching equipment cabinet. The telecommunications company's claim alleges that the dispute between the companies has nothing to do with minority issues, but with a failure on the part of the minority company to make payments to it under their distributor agreement.¹⁶

Another black female manufacturer attributed the difficulty her firm had encountered in attempting to market a new voice response product to several telecommunications companies as "the major telephone companies have not established a special program by which small minority companies can introduce, demonstrate, and test their equipment; it is impossible for minority companies to introduce their new products and equipment under a system that is monopolized by a few large companies."¹⁷

In order to facilitate technology transfer, major telecommunications companies must be willing to make available technical specifications and product requirements to MWBEs.

¹⁶ U.S. District Court, Northern District of California. Civil Action No. C-91-4485.

¹⁷ Interviewee no. 8.

Established white-owned companies have an advantage over minority-owned companies in that they have enjoyed long-term relationships with major telecommunications companies. Minority-owned companies, for the most part, have been limited to selling the technology, products, and equipment of white-owned companies and offered little opportunity to develop, manufacture, and market their own technology, products, and equipment.

During our study, we were unable to identify any minority-owned companies that were authorized dealers for A major manufacturer of central office equipment. And, in another, we were able to find very few value-added resellers (VARs) of its high-technology products. Minority firms are, for the most part, limited to smaller, lower-end PABX and business key system products.¹⁸

Minority companies complained that they are rarely involved in the installation of advanced telecommunications systems for telecommunications companies. The typical involvement for MWBEs is where the equipment manufacturer, or the purchasing company, decides to authorize a minority company to purchase and resell a large piece of equipment to its customer for installation, often by the manufacturer. The minority company does not participate in the installation, but receives a small profit for facilitating, in many cases, a paper transaction only. The sale of a piece of network switching equipment may generate several million dollars in MWBE participation credit, but offers no technology transfer or technical training to the minority company.

¹⁸ Interviewees nos. 14, 15, 19, 20.

Perhaps no form of discrimination is more devastating to the growth and development of minority-owned businesses than the preconceived notions about their limitations and capabilities. These entrenched stereotypical attitudes are based solely upon the race or gender of the business owner and are not easily overcome. Unfortunately, the telecommunications industry is perpetuating these outmoded notions of MWBE inferiority.

USING MINORITY COMPANIES AS "FRONTS"

In July, 1977, a moratorium was imposed by the SBA on the 8(a) program for a period of three months, temporarily halting any new applications into the program. This action was taken in order to correct abuses which, according to the SBA, stemmed from non-minority businesses, which for the most part used black and Hispanic "fronts" to receive Federal non-competitive contracts under the 8(a) program.

An investigation of the program by the Senate Governmental Affairs Spending Committee uncovered instances of business firms being admitted into the program which were not minority-owned and controlled. It found that white entrepreneurs were setting up captive firms and installing blacks and Hispanics in fake executive positions in order to obtain Federal contracts. The Subcommittee determined that as a result of such illicit activities, these firms were able to reap millions of dollars in noncompetitive Federal contracts that were intended to help only minority businesses.¹⁹

¹⁹ U.S. Congress. House Committee on Small Business. Subcommittee on Minority Enterprise and General Oversight. 8(a) Program Moratorium and Small Business Administration Personnel Practices. Hearings, 95th Cong., 1st Sess., October 19, 1977. Washington, U.S. Govt. Print. Off., 1977.

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A close investigation by the Minority Business Enterprise Legal Defense and Education Fund has uncovered "fronting" activity in the telecommunications industry.

Resistance to the use of legitimate minority companies is due in part to the perception by many white firms that participation by bonafide minority companies will only serve to reduce their market share and profits.

By establishing fronting relationships, white firms are able to increase their business, often with the same customer, by introducing a minority company to satisfy the customer's minority business participation goals, at the same time controlling the growth of the minority company.

During the mid-seventies and through the early eighties, it was pretty easy to identify front companies. Today, the task has become more difficult due to the sophistication of these charades.

KEY INDICATORS THAT COMMONLY IDENTIFY MINORITY FRONTS

- (1) **Front companies are often headed by a minority executive, while the company's management, staff, and work force are predominantly white;**
- (2) **Front companies rarely create much net equity, as the lion's share of the company profits are usually siphoned off;**
- (3) **Frequent subcontracts between the front company and the white firm, with the majority of the work going to the white firm;**
- (4) **Equipment rental agreements between the front company and the white firm at rates that exceed the norm;**
- (5) **Management and consulting agreements for technical and managerial services at rates that exceed reasonable compensation for the services performed;**
- (6) **Excessive bond indemnification fees paid to the white firm for guaranteeing payment and performance bonds.**

Our examination of minority contracting in the telecommunications industry revealed that the number one vehicle being used for fronting is **distributorships**. However, distributorships are by no means the only area of the industry where fronting is occurring.

DISTRIBUTORSHIPS

While distributorships do represent a legitimate form of business, they have become the vehicle of choice for telecommunications companies, and other major suppliers who are using minority companies as conduits primarily for the purpose of generating sales volume, which is then reported as credit towards achievement of their minority business participation goals. Several of the minority companies interviewed stated that becoming a distributor was the only way they could gain access to the industry.

Due to their limited access to capital, minority distributors are often established and kept in business through inventory consignment agreements with major distributors and manufacturers of telecommunications products and equipment. Minority companies attempting to access the telecommunications product and equipment markets find that manufacturers continue to dominate standard supply relationships with the industry's largest customers.

On the other hand, the telecommunications product and equipment manufacturers face another dilemma. The product or equipment's end users are seeking minority participation under existing contracts or new contracts they wish to capture. In order to satisfy the end users' MWBE goals, the manufacturers will negotiate agreements with minority distributors to sell their products to the end users, which usually generate very low profit margins to the minority company, and no technical training or technology transfer.

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For example, in 1989, a black-owned distributor generated approximately \$16 million in gross sales of a telecommunications company's products and equipment to a purchasing company. Sales to the purchasing company represented 90% of the company's sales for that year. The minority distributor's net earnings for that year totaled less than 1% of gross sales.

In 1990, the same minority distributor's gross sales increased to approximately \$45 million with 98% of its products and equipment purchased from a telecommunications company and sold to a purchasing company. The minority distributor's net earnings for that year totaled less than $\frac{1}{2}$ of 1% of gross sales.

While the minority distributor's net sales increased by \$29 million, or over 280%, between the years 1989 and 1990, its net earnings only increased by \$30,000, or 20%. It should be noted that our analysis of the minority distributor's audited 1989 and 1990 financial statements show the distributor's gross profit margins to be less than 4% in both years.²⁰

During 1989, in its annual MWBE report to the State Public Utilities Commission, the purchasing company reported \$53.8 million in procurement with black-owned business. The minority distributor accounted for approximately 27% of the purchasing company's total procurement with black-owned businesses.

²⁰ Interviewee no. 8 sworn statement and 1989 & 1990 audited corporate financial statements.

In 1990, in its annual MWBE report to the State Public Utilities Commission, the purchasing company reported \$65.4 million in procurement with black-owned businesses. The same minority distributor accounted for approximately 67% of the purchasing company's total procurement with black-owned businesses.²¹

In November of 1991, the telecommunications company terminated the minority company's distributor agreement and all credit and shipments to the company for non-payment. The telecommunications company also filed a suit against the company for monies alleged to be due it. The minority company has filed a counter suit against the telecommunications company alleging numerous counts of fraud and misrepresentation, and failure to provide developmental assistance and technology transfer as allegedly agreed.²²

Without exception, every minority distributor interviewed stated there was "no future in being a distributor." The rate of return on investment is low and the customer's view of the service is that it is marginally value-added.

Large telecommunications companies continue to outsource much of their inventory distribution and management to other companies because it is simply not a profit center. If these companies find it too costly to carry and manage inventory, how can minority companies with far fewer financial resources afford to finance inventory at rates of interest often equal to or greater than the gross profit margin realized from the distribution business?²³

²¹ See Appendix I, Table V, Black Procurement.

²² U.S. District Court, Northern District of California. Civil Action No. C-91-4485.

²³ Interviewees nos. 1, 4, 5, 9. Reviewed various interviewees' distributor agreements.

COLLUSION

Many of the minority interviewees reported collusion as a developing trend in the telecommunications industry. Interviewees cited instances of white employees, usually decision makers in the purchasing, contracts and materials management departments acting collusively to award large contracts to minority companies that they later join as shareholders, highly paid consultants, or employees.

A black female-owned telecommunications company filed a complaint with MBELDEF alleging discrimination involving a \$30 million contract opportunity with a telecommunications company in which her company was the low bidder. The contract however, was awarded to a newly formed white female-owned company alleged to have no expertise in the field. One of the principals in the new company is a former employee of the telecommunications company, who is alleged to have been directly involved in the award of the \$30 million contract to the white female-owned company. The telecommunications company employee is alleged to have retired shortly after the award to join the company receiving the contract.

Another black interviewee cited a similarly large contract award by a former employee of another telecommunications company to a minority-owned company. The former telecommunications company employee is alleged to have joined the minority-owned company shortly after the contract award.²⁴

²⁴ Interviewees nos. 15, 19.

DISCRIMINATION IN FEMALE PROCUREMENT

The particularized evidence of discrimination in the telecommunications marketplace against women-owned firms in general revealed examples including denials of opportunity to bid, discrimination in technical training, customer/end user discrimination, exclusion from the "good old boy" network in subcontracting, bid shopping, bid manipulation, price discrimination by suppliers, discrimination in financing, bonding, including double standards in performance and qualifications, limited access to technology transfer, slow payment and non-payment, and stereotypical attitudes on the part of buyers and contracts managers.

Evidence of discrimination against women-owned firms in general is significant, however, the evidence of discrimination against white female-owned firms in the telecommunications industry is not as severe as against other minority female-owned firms.

The single most prominent complaint among interviewees was the disparity between contracts awarded to white female-owned firms compared to other minorities.

Interviewees provided evidence that white female-owned businesses are being established as "fronts" for outsourcing contracts that otherwise would go to other minority companies.

A key finding of our examination of the industry is a developing trend, whereby contracts to blacks, Hispanics, and other minority groups are decreasing, while contracts to white females are increasing. (See Appendix I, Tables VII-XII.)

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The California Public Utilities Code §283 established goals of not less than 15% for minority enterprises and 5% for women enterprises. Discriminatory practices on the part of telecommunications companies are producing results that do not comply with the intent of the law. (See female procurement, Fig. I; see also Appendix I, Tables I, VI, and VII.)

Interviewees verified this disparity trend throughout the telecommunications industry. White female-owned companies are being selected preferentially over other minorities by purchasing and contracts managers. Numerous white female-owned firms that started their businesses in the industry with no prior experience were cited by interviewees as having already received millions of dollars in contract awards while other minority firms with industry background and experience have received only nominal contracts.

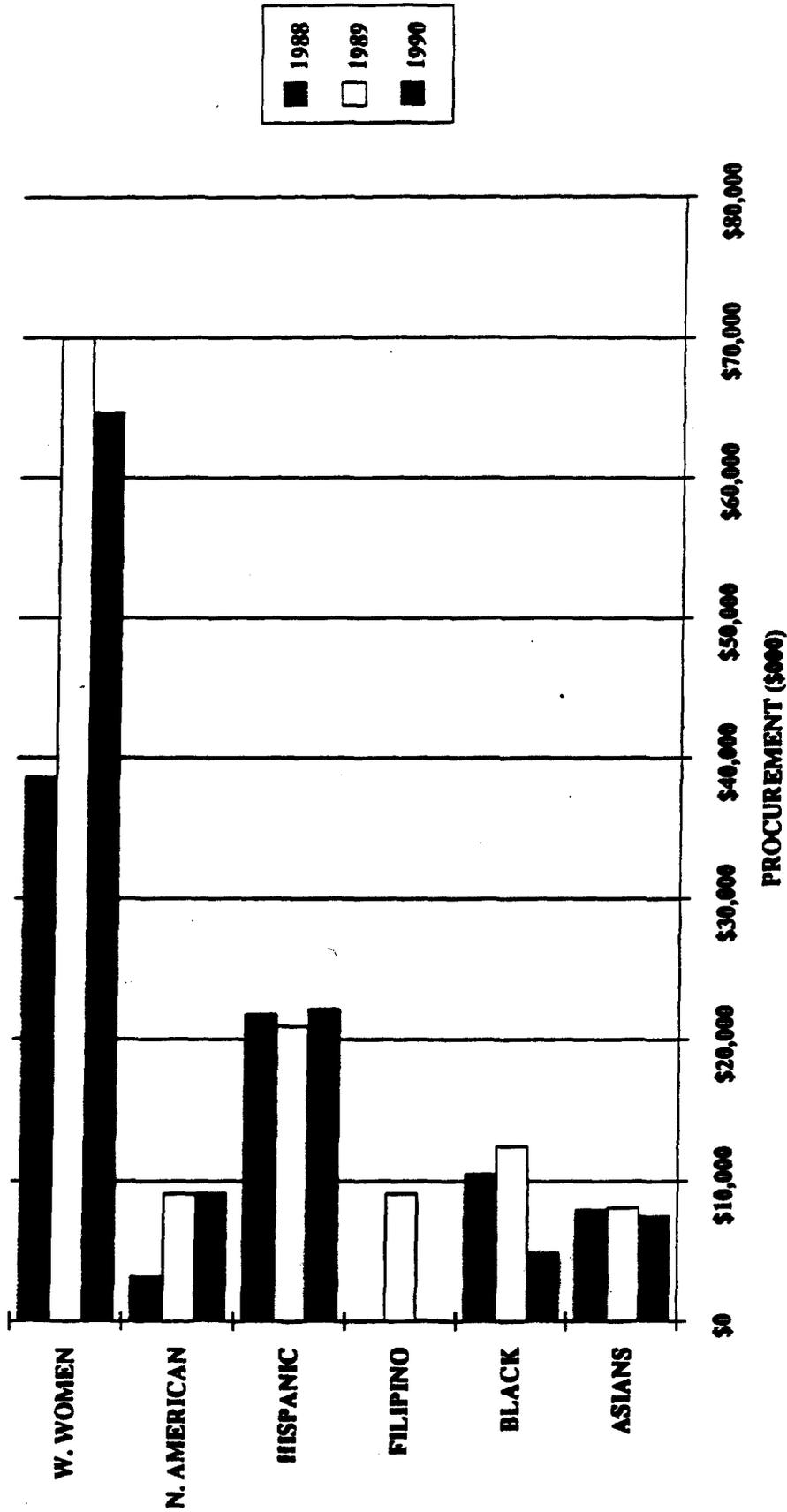
There is an enormous disparity between white female and minority female procurement in the industry. For example, from 1988 - 1990 in California, while white females received 6.7% of all procurement from large utilities, minority women received only 1.8% of all procurement.

Among white females and all other minorities combined, between 1988 - 1990, white females received the overwhelming percentage of total minority procurement at 47.5%. (See Fig. III.)

For example, total female procurement for Pacific Bell increased dramatically to \$200 million. White females received the largest dollar value of total procurement overall and Pacific Bell reported the largest total female procurement with a single company in 1990, at \$160 million. GTE was the next highest. (See Fig. II and IV; see also Appendix I, Table VIII.)

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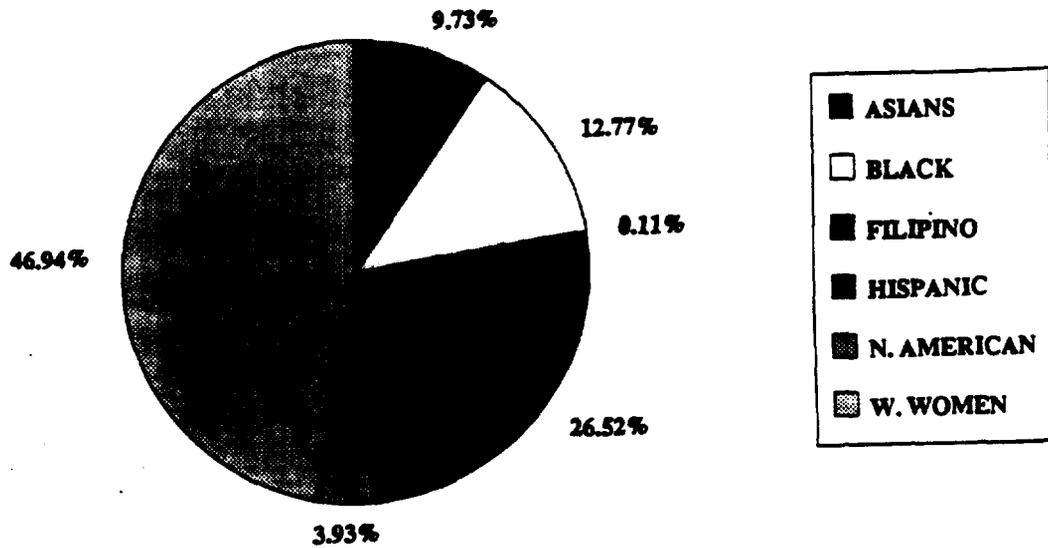
FIG. 1 - CTE Procurement by Detail Minority and Gender Status and Year



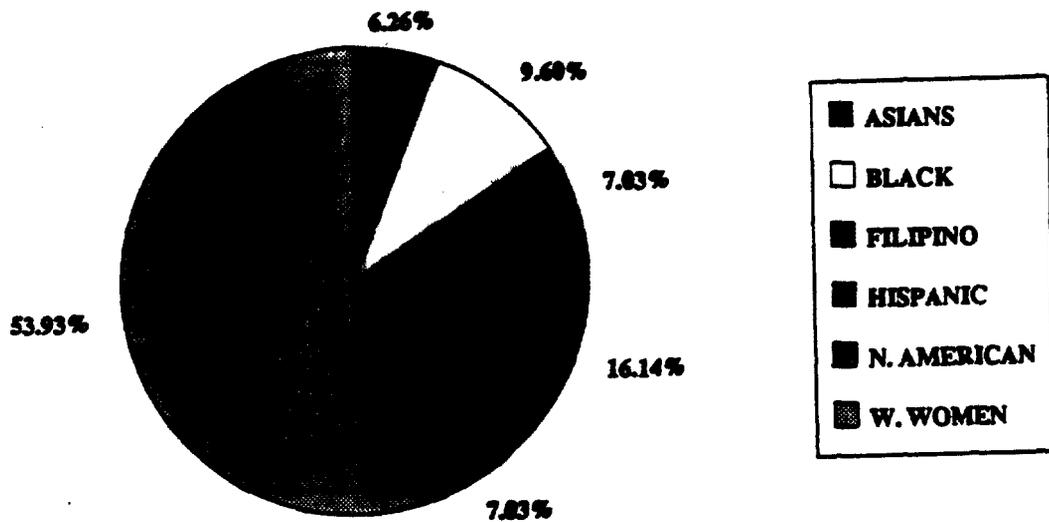
Source: CALIFORNIA PUBLIC UTILITIES COMMISSION

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FIG. II -
GTE PROCUREMENT BY MINORITY GROUP AND GENDER, 1988



GTE PROCUREMENT BY MINORITY GROUP AND GENDER, 1989



GTE PROCUREMENT BY MINORITY GROUP AND GENDER, 1990

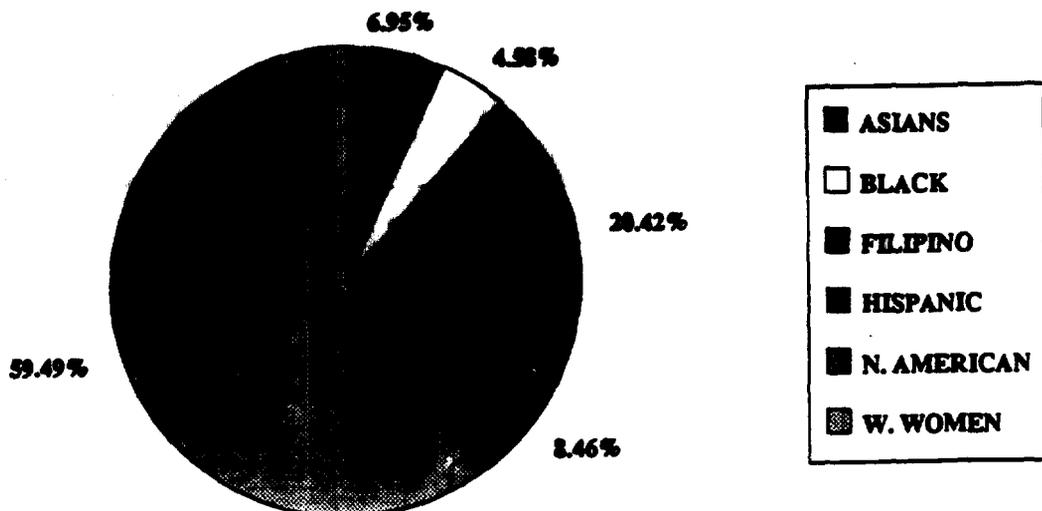
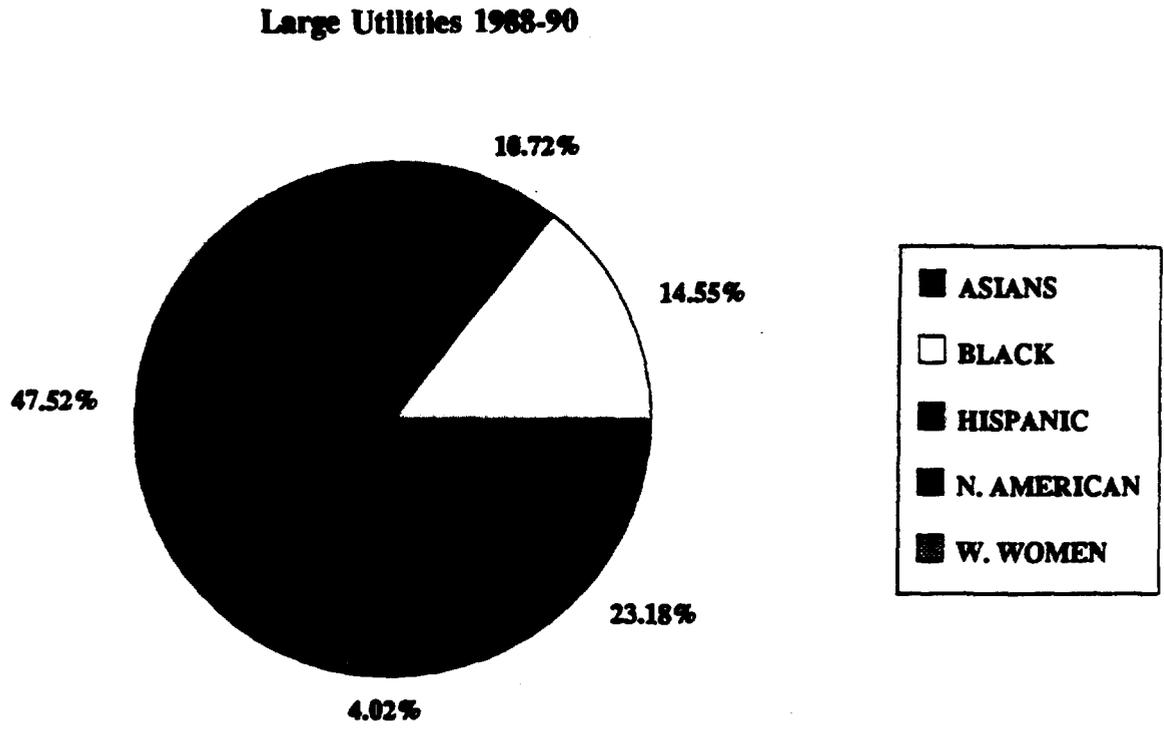
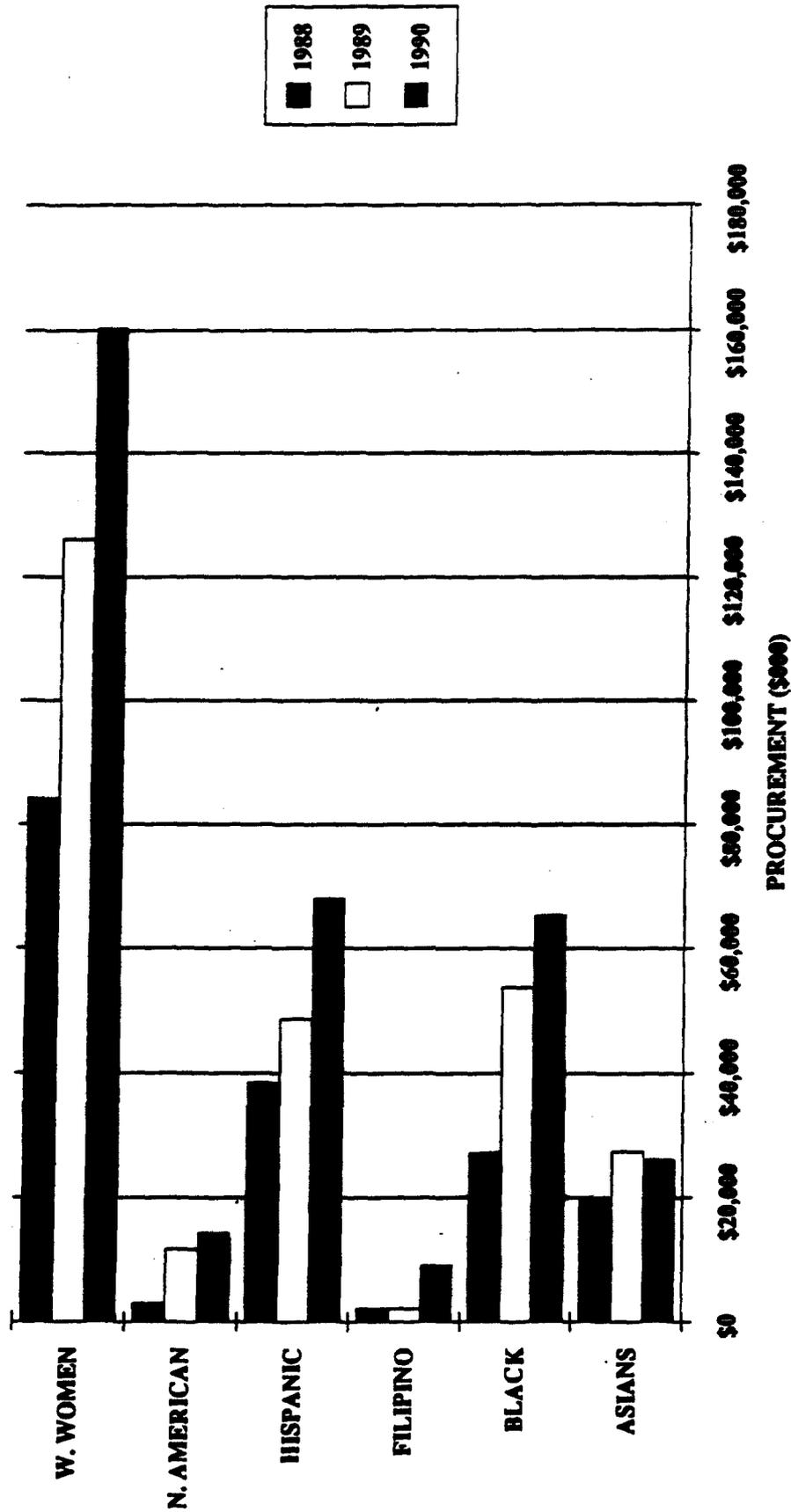


FIG. III - % Of All Minority Procurement



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FIG. IV - Pacific Bell Procurement by Detail Minority and Gender Status and Year



Source: CALIFORNIA PUBLIC UTILITIES COMMISSION

SUMMARY AND RECOMMENDATIONS

SUMMARY

The central issue supporting the case for meaningful development of minority-owned business in the telecommunications industry is that minority rate payers continue to pay a substantial portion of the costs for the public telephone network, its equipment, research and development, depreciation and maintenance. These same minority groups are being denied access to the very equipment and technology they have substantially financed.

It is especially important that the American public understand and believe that minority business development programs are in the public interest and are fair. Supreme Court Justice Powell noted in his concurrence in Fullilove, which upheld the Federal minority set-aside program, "respect for the law, especially in an area as sensitive as this, depends in large measure on the public's perception of fairness. It, therefore, is important that the legislative record supporting race-conscious remedies contain evidence that satisfies fair minded people that governmental action is just."²⁵

²⁵ Fullilove, 448 U.S. 507, n. 8.

The following is a list of typical program activities touted by major telecommunications companies as evidence of their commitment to minority business. In light of all these activities the question still remains -- why are there so few competitive and financially viable minority-owned telecommunications companies? We maintain that it is the lack of meaningful long-term development assistance.

INTERNAL PROGRAM ACTIVITIES

- Small Business Outreach Coordinators
- Employee Awareness Programs
- MWBE Subcontractor Training Seminars
- Employee MWBE Recognition Programs
- MWBE (800) Newslines

OUTREACH ACTIVITIES

- Minority-Owned Publications
- Minority Business Consultant Contracts
- MWBE Newsletters
- (800) Number for MWBEs
- MWBE Conferences and Trade Fairs
- Participation in Regional Minority Purchasing Councils
- Participation in National Minority Supplier Development Council
- White House Conference on Small Business
- U.S. Small Business Administration (MED Week)
- Hispanic Chamber of Commerce Conference
- Asian Community Leadership Forum
- Various Supplier Outreach Meetings
- Various Small Business Luncheons
- Company-Sponsored Minority Procurement Conferences