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Legislative Counsel Committee

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To: Representative John Lively

From: Alan S. Dale, Senior Deputy Legislative Counsel

Subject: HB 2266-1 and the Equal Protection Clause of the Fourteenth Amendment

The -1 amendments to House Bill 2266 require the Oregon Business Development Department to develop and implement a program to make loans exclusively to a defined category of eligible businesses. Eligible businesses include those that are majority owned and controlled by minority individuals, defined to include African Americans, Hispanics, Asian Americans, Portuguese and American Indian or Alaska Natives.[1] A state's race-conscious policy may be challenged under the Equal Protection Clause of the Fourteenth Amendment to the U.S. Constitution, which mandates that state governments treat similarly situated persons equally under the law.[2] (Please note that the U.S. Supreme Court subjects state policy based on race and ethnicity to the same analysis.[3])

We believe, under the following analysis, that a court would likely conclude that this preference for loans to minority-owned businesses is a race-conscious policy: If a small business concern owned by an African American man and an otherwise similarly situated small business concern owned by a white man are not eligible for loans under any other category, e.g., a business that a service-disabled veteran owns, the former small business concern will still be eligible for a loan while the latter will not, and the different outcome is based solely on the race of the owner. Please note that, under the affirmative action jurisprudence of the United States Supreme Court, the fact that not all categories in a state law are race-conscious does not affect the standard of review applied to those that are.[4]

The United States Supreme Court has concluded that all race-conscious state laws are so inherently suspect that they are unconstitutional under Equal Protection analysis unless they

[1] Section 13 (1) of HB 2266-1, cross-referencing ORS 200.005 (6).
[2] *See Engquist v. Or. Dept. of Agriculture*, 553 U.S. 591, 601-602 (2008).
[3] *See Grutter v. Bollinger*, 539 U.S. 306, 323 (2003) ("[W]hen governmental decisions 'touch upon an individual's race or ethnic background, he is entitled to a judicial determination that the burden he is asked to bear on that basis is precisely tailored to serve a compelling governmental interest.'") (*citing Regents of Univ. of Cal. v. Bakke*, 438 U.S. 265, 299 (1978)).
[4] *See Adarand Constructors v. Pena*, 515 U.S. 200, 223 (1995) ("Any preference based on racial or ethnic criteria must necessarily receive a most searching examination") (internal quotations and citations omitted).

pass strict scrutiny,[5] which is a two-step test: (1) Whether the law serves a compelling government interest; and (2) Whether the law is narrowly tailored to achieve that interest.[6]

Under step one, remedying the present effects of past discrimination has long been recognized as a compelling government interest in affirmative action cases.[7] However, a state must demonstrate that, under the facts and circumstances particular to the relevant market or industry in the geographic area subject to the policy,[8] the identification of present effects of past discrimination is supported by a "strong basis in evidence."[9] Where a significant statistical disparity can be demonstrated, e.g., between the availability of qualified minority businesses in an industry and geographic area and the utilization of those minority businesses, that disparity may be sufficient to raise an inference of discrimination.[10] However, the use of racial balancing, *i.e.*, the assumption that minorities will participate in a particular industry or trade in numeric proportion to their representation in a particular population, is constitutionally invalid.[11]

The evidence must also separately justify the inclusion of every racial or ethnic category benefited by the law,[12] e.g., each group listed in the definition of "minority individual" as used in HB 2266-1. Anecdotal evidence may effectively complement statistical evidence but is not generally sufficient by itself.[13] "[M]ere speculation, or legislative pronouncements, of past discrimination" or generalized societal discrimination are insufficient.[14] The strong basis in evidence justifying the race-conscious policy must be presented to the legislature before passage of the bill.[15] And, finally, the initial burden is on the state to justify the use of racial or ethnic preferences.[16]

I have attached a copy of *Associated General Contractors of America v. California Department of Transportation* to show what the Ninth Circuit considered a sufficient basis in evidence to support race-conscious legislation in California. The discussion begins on page 4 of

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[5] *Hunt v. Cromartie*, 526 U.S. 541, 546 (1999). Gender-based discrimination is also suspect, but courts apply a less searching standard of review, intermediate scrutiny. *U.S. v. Virginia*, 518 U.S. 515, 533 (1996). In this memorandum we discuss only race-conscious policy and the strict scrutiny standard because it is the more difficult standard to satisfy.
[6] *Grutter v. Bollinger*, 539 U.S. at 326; *Local 28 of Sheet Metal Workers' Int'l Ass'n v. EEOC*, 478 U.S. 421, 484-485 (1986) (Powell, J., concurring).
[7] *See, e.g., Fullilove v. Klutznick*, 448 U.S. 448, 480 (1980); *Richmond v. J.A. Croson Co.*, 488 U.S. 469, 476-477 (1989).
[8] *See, e.g., J.A. Croson Co.*, 488 U.S. at 506, 510; *U.S. v. Paradise*, 480 U.S. 149, 171 (1987); *Local 28 of Sheet Metal Workers' Int'l Ass'n v. EEOC*, 478 U.S. at 486-487 (Powell, J., concurring); *Assoc'd Gen. Contrs. of Amer. v. Cal. DOT*, 713 F.3d 1187, 1196 (9th Cir. 2013); *Adarand Constructors, Inc. v. Slater*, 228 F.3d 1147, 1163 (10th Cir. 2000).
[9] *Adarand Constructors, Inc*, 228 F.3d at 1166. *See also Western States Paving Co. v. Wash. State DOT*, 407 F.3d 983, 991 (9th Cir. 2005).
[10] *See J.A. Croson Co.*, 488 U.S. at 509.
[11] *Id.* at 507-508 ("[Racial balancing] rests upon the completely unrealistic assumption that minorities will choose a particular trade in lockstep proportion to their representation in the local population.") (internal quotations omitted); *Adarand Constructors, Inc.*, 228 F.3d at 1164; *Assoc'd Gen. Contrs. of Ohio, Inc. v. Drabik*, 214 F.3d 730, 736 (6th Cir. 2000).
[12] *J. A. Croson Co.*, 488 U.S. at 506. The state law challenged in *J.A. Croson* defined "minority business enterprises" in a manner similar to the definition of "minority-owned business" in HB 2266-1, requiring 51 percent ownership and control by United States citizens who were Blacks, Spanish-speaking, Orientals, Indians, Eskimos or Aleuts, with no geographic limit. *Id.* at 478. In that case, the inclusion of racial and ethnic groups without a strong basis in evidence of past discrimination against them in the market and geographical area at issue led the court to question the remedial nature of the legislation. *Id.* at 506.
[13] *Assoc'd Gen. Contrs. of Amer.*, 713 F.3d at 1196 (*citing Int'l Bhd. of Teamsters v. U.S.*, 431 U.S. 324, 339 (1977)).
[14] *Assoc'd Gen. Contrs. of Ohio, Inc.*, 214 F.3d at 735 (internal quotations and citations omitted); *Western States Paving Co.*, 407 F.3d at 991 ("Congress may not merely intone the mantra of discrimination to satisfy the searching examination mandated by equal protection.") (internal quotations and citations omitted); *J.A. Croson Co.*, 488 U.S. at 505-506.
[15] *Shaw v. Hunt*, 517 U.S. 899, 909-910 (1996).
[16] *Western States Paving Co.*, 407 F.3d at 990.

the copy, under the highlighted heading "1. Evidence Gathering and the 2007 Disparity Study." Also highlighted is a paragraph on page 9 in which the court comments approvingly on the state's disparity study. In addition, please be aware that the "whereas" clauses in the preamble to HB 2266-1 make plain the race-conscious intention of the bill, but are the kind of legislative pronouncements that courts do not consider sufficient as evidence of the present effects of past discrimination.

In determining, under step two, whether a race-conscious public policy is narrowly tailored to remedy the present effects of past discrimination that has first been substantiated under step one, courts consider a series of factors, including: (1) the necessity for the relief; (2) the efficacy of race-neutral alternative remedies; (3) the flexibility of the relief, including the availability of waiver provisions; (4) the duration of the relief; (5) the relationship of the numeric goals to the relevant labor market, including over- and under-inclusion of minority groups; and (6) the impact of the relief on the rights of third parties.[17]

While narrow tailoring "does not require exhaustion of every conceivable race-neutral alternative," it does require "serious, good faith consideration" of workable, less restrictive, race-neutral alternatives that do not unduly burden members of unfavored racial groups.[18] An overinclusive remedial public policy—one that provides preferential treatment to a minority group that, according to the evidentiary record, does not face the present effects of past discrimination in the relevant marketplace and geographical area or to the extent for which the state law provides a remedy—is not narrowly tailored and will fail step two of strict scrutiny.[19] Put simply, the precise fit between the ends sought (remedying the present effects of the identified past discrimination) and the means chosen (the race-conscious policy) must be demonstrably and logically justified by the evidentiary record established under step one.[20] Finally, a race-conscious public policy that, to the greatest extent possible, makes an individualized determination as to eligibility, as opposed to relying on racial status alone, is more likely to survive strict scrutiny.[21]

We cannot say whether the requested racial and ethnic preferences for loan eligibility in HB 2266-1 would be challenged under the Equal Protection Clause, or whether, if they were challenged, they would be upheld. We can say, however, that a court would analyze facial state-law preferences based on race and ethnicity under the strict scrutiny standard, and that the law is more likely to be upheld if those preferences are justified by a strong basis in evidence, meeting the Supreme Court's requirements, that is presented to the legislature before enactment of the law.[22]

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[17] *Paradise*, 480 U.S. at 171. *See also Adarand Constructors, Inc.*, 228 F.3d at 1178. The program embodied in ORS 200.005 to 200.075 for which the definitions used in HB 2266-1 were enacted includes a waiver provision under ORS 200.045 (2) that is absent from the loan program in HB 2266-1.

[18] *Grutter v. Bollinger*, 539 U.S. at 339-341; *J.A. Croson Co.*, 488 U.S. at 507.

[19] *Mt. West Holding Co. v. Montana*, 691 Fed. Appx. 326, 329-330 (9th Cir. 2017); *J.A. Croson Co.*, 488 U.S. at 506.

[20] *Grutter*, 539 U.S. at 333; *Western States Paving Co.*, 407 F.3d at 994-995 ("To be narrowly tailored, a minority preference program must establish utilization goals that bear a close relationship to minority firms' availability in a particular market."); *J.A. Croson Co.*, 488 U.S. at 493.

[21] *J.A. Croson Co.*, 488 U.S. at 508 ("[S]uch programs are less problematic from an equal protection standpoint because they treat all candidates individually, rather than making the color of an applicant's skin the sole relevant consideration."); *Adarand Constructors, Inc.*, 228 F.3d at 1184-1185 ("In short, by inquiring into economic disadvantage on an individual basis, the program could avoid improperly increasing the contracting opportunities of those minority entrepreneurs whose access to credit, suppliers, and industry networks is already sufficient to obviate the effects of discrimination, past and present.").

[22] Please note that the preference for loans to minority-owned businesses under HB 2266-1 could also be challenged under Article I, section 20, of the Oregon Constitution, which prohibits the state from providing to a class of citizens privileges or immunities that do not apply on the same terms to all citizens. The test under the Privileges or Immunities Clause has been established by case law, but we are not aware of any cases applying it to an affirmative action

Finally, a related issue is currently being litigated as *Cocina Cultura, LLC v. State of Oregon* in the federal District Court of Oregon, which may provide updated guidance.

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program. While we believe a favorable decision is possible, it would likely require some evidentiary showing of actual discrimination, as is required under strict scrutiny. Without relevant case law, however, we cannot predict the type and strength of evidence an Oregon court would require, though we think it likely that evidence that satisfies the requirements of the Equal Protection Clause would also satisfy the requirements of the Privileges and Immunities Clause.