



# Richmond City Council

The Voice of the People

Richmond, Virginia

## Office of the Inspector General

May 24, 2021

Mr. Lincoln Saunders  
Acting Chief Administrative Officer  
City of Richmond

The Office of the Inspector General (OIG) completed an investigation within the Office of Minority Business Development (OMBD), Procurement Services, Department of Public Utilities, a City of Richmond contracted vendor, and its subcontractors as it relates to a complaint about minority business participation on specific city contracts. This report presents the results of the investigation.

### Allegations

The Office of the Inspector General received multiple complaints from an individual who alleged fraud and abuse of the City of Richmond's Minority Business Enterprise (MBE) program. Of these complaints, three were substantiated.

The substantiated allegations are as follows:

- 1) The Contractor is using MBE Subcontractor (B) to meet its goal for Minority Business Enterprise compliance for contract #1, when in fact the MBE Subcontractor (B) is used as a pass-through to circumvent the MBE participation goal by providing an employee to Subcontractor (A) which is a subsidiary of the Contractor's company. In violation of the Office of Minority Business Development Policy 1.4 Purpose.
- 2) MBE Subcontractor (B)'s Small, Women-Owned, and Minority-Owned Business (SWaM) certification with the Virginia Department of Small Business and Supplier Diversity expired on April 8, 2016, and that this information was provided by the complainant during a pre-construction meeting for contract #3. In violation of Office of Minority Business Development Policy 2.3.1 Registration.
- 3) The Contractor used MBE Subcontractor (C), a printing company, to order supplies on a sewer contract. In violation of Office of Minority Business Development Policy 1.4 Purpose.

## Legal and City Policy Requirements

- 1) In accordance with the Code of Virginia §15.2-2511.2, the Inspector General is required to investigate all allegations of fraud, waste, and abuse. Also, City Code Section 2-214 requires the Office of the Inspector General to conduct investigations of alleged wrongdoing. In addition, during this investigation, the investigator referred to the following regulations:
- 2) The City of Richmond Code of Ordinances, Chapter 21, Article VII *Utilization of Minority Business and Emerging Small Businesses* establishes the city's MBE program. Section 21-221 authorizes the Office of Minority Business Development (OMBD) to promulgate rules and regulations to implement the article. In addition to the rules and regulations of OMBD, Section 21-251 allows for the Chief Administrative Officer to debar a contractor for two years if the contractor is found to have engaged in substantial and intentional misrepresentation concerning either good faith minority business enterprise and emerging small business participation efforts or minority owner status. The determination is to be made by the Chief Administrative Officer.
- 3) Section 1.4 of the Office of Minority Business Development policy states in part: "It is the overall purpose of the Office of Minority Business Development to increase the number of minority business enterprises and emerging small businesses that participate in a commercially useful function in all contracts." The definitions section of OMBD policy gives the following definition for commercially useful function:

***"Commercially Useful Function*** – Minority Business Enterprise/Emerging Small Business Enterprise (MBE/ESB) participation, the MBE/ESB must be performing a "commercially useful function" in order for MBE/ESB participation credit to apply. MBE/ESB entity must be more than a pass-through entity and cannot exist in name only.

While the specific requirements may vary slightly, the "commercially useful function" requirement usually focuses on whether the MBE/ESB is acting like a non-MBE/ESB contractor or non-MBE/ESB supplier would under similar circumstances. Examples of the criteria include:

- Whether it is actually managing its own labor and performing work;
- Whether an MBE/ESB contractor is providing its own materials;
- Whether an MBE/ESB supplier is transporting, storing, or delivering the materials;
- Whether it is paying for its own labor; and
- Whether there are consequences if the MBE/ESB fails to perform.

**In other words, the prime will get credit for the work that is actually being performed by the MBE/ESB firm."**

4) Section 2.3.1 of the Office of Minority Business Development policy states:

**Registration**

It is the policy of the Office of Minority Business Development to register all firms who are seeking to work with the City of Richmond as a sub-contractor/vendor. These firms must meet the criteria of a minority business. The firm must be certified as a minority business by a certifying agency. The agencies that are recognized by:

- a. Small Business Administration (SBA) 8(a) Program
- b. Virginia Department of Small Business and Supplier Diversity (VDSBSD): Small, Women and Minority (SWaM, MS)
- c. Virginia Department of Small Business and Supplier Diversity: Disadvantaged Business Enterprise (DBE)
- d. Washington Metropolitan Airport Authority (MWAA)

5) Section 2.3.10 of the Office of Minority Business Development policy states:

**Payments**

The Office of Minority and Business Development (OMBD) shall monitor all payments made to Minority Business Enterprise and Emerging Small Businesses (MBE/ESB) prime, sub-contractors and vendors. The OMBD shall work closely with Finance and Procurement Departments as it relates to payments MBE/ESBs contractors and vendors. The OMBD must verify all payments to MBE/ESBs firms to ensure that they are not a "pass-through".

- 6) The Virginia State Code §18.2-498.3 defines actions that violate the Virginia Governmental Frauds Act. Virginia State Code §18.2-498.5 requires action brought in violation of §18.2-498.3 to be initiated by the Attorney General of a state agency and the local Commonwealth's Attorney if involving a local governmental agency.
- 7) Federal regulation 49 CFR §26.55 How is Disadvantaged Business Enterprise (DBE) participation counted towards goals?

**Introduction**

The City of Richmond engages outside contractors to perform services for the city. Through ordinance, the City of Richmond endeavors to include minority businesses to participate in city contracts through contracted Minority Business Enterprise participation goals either as a prime contractor or subcontractor. Any contracts exceeding \$5,000.00 are to go through a bidding process with Procurement Services. Once a contract is awarded, the services provided are administered by the requesting department. By ordinance, the Office of Minority Business Development is charged with verification of Minority Business Enterprises and compliance with Minority Business Enterprises participation goals as sub-contractors.

In this complaint, one Minority Business Enterprise is acting as a sub-contractor and the other as a supplier. One of the key elements in monitoring minority business participation is ensuring that work and services are actually being performed by the minority businesses and that they are not acting as merely a pass-through business to meet compliance goals.

## Findings

### Allegation #1

During the investigation, the Investigator obtained and analyzed documents that showed the Contractor was using MBE Subcontractor (B) to provide an employee to the Contractor in order to meet its goal for Minority Business Enterprise compliance for contract #1, when in fact the MBE Subcontractor (B) is being used as a pass-through to circumvent the MBE participation goal. The employee was working with Subcontractor (A), which is a subsidiary of the Contractor. The Contractor sent a timesheet for the MBE Subcontractor (B) employee to MBE Subcontractor (B) who in turn would invoice the Contractor for payment. The MBE Subcontractor (B) employee worked for MBE Subcontractor (B) on paper only. The employee actually works for Subcontractor (A). The employee reported and was supervised by Subcontractor (A) for daily work, and clocked in and out at Subcontractor (A) facility. The employee wore a Subcontractor (A) uniform and drove Subcontractor (A)'s vehicle and used Subcontractor (A)'s equipment. Any leave requests and vacation time were handled by Subcontractor (A). The MBE Subcontractor (B) did not appear on the job site, supervise their employee, manage their own labor, perform any work, or provide their own materials for the project. The MBE Subcontractor (B) only provided an employee to the Contractor to meet the MBE participation goal.

The investigator conferred with the Deputy Director of OMBD who explained that the Contractor had a participation goal of 20% for this contract (#1) and was on track to meet that goal. The Deputy Director was aware of the method the Contractor was used to meet its goal and did not believe it to be a pass-through. The Deputy Director stated that the owner of MBE Subcontractor (B) was confirmed to be a 51% owner of MBE Subcontractor (B) and was providing an employee. The reporting method for compliance is OMBD form MBE-3. The Contractor submits MBE-3 forms monthly on contracts with an MBE participation goal, even if there was no MBE work performed that month. Invoices for the MBE work are to be attached to obtain credit.

The investigator requested copies of the MBE-3 report from OMBD for contract #1. The investigator was instead sent the Contractor's MBE-3 reports contract #2. These reports had 100% of the employee's time as credit for the Contractor's MBE participation goal. The investigator requested and received the corresponding MBE-3 reports for contract #1 and found overlapping submissions. The Contractor had submitted the same invoices for credit on two separate contracts. The Contractor was also claiming MBE Subcontractor (C) as an MBE supplier for both of these contracts. The same MBE Subcontractor (C) invoices were on both contracts. MBE Subcontractor

(C) will be addressed in Allegation #3. The investigator requested complete copies of both contract files from OMBD and a copy of the OMBD Policy Manual.

The investigator conducted a complete analysis of the two files and policy. The investigator concluded numerous MBE-3 reports were missing from contract #1 making it impossible to reconcile what OMBD had credited the Contractor, what the Contractor claimed as a credit, and what the OMBD file had documented. The contract #2 file contained a memo from the Deputy Director of OMBD in October 2019 indicating that the Vice President from the Contractor's Company had submitted invoices for contract #2 because the person responsible for reporting within the company was no longer employed and had not submitted them. These were the overlapping invoices from the two MBEs. The invoices submitted to the OMBD Deputy Director were from July 2017 to September 2019. The former employee, an accounting manager, had already submitted MBE-3 reports during this period. The accounting manager submitted zeros for MBE participation each month from July 2017 to July 2019 when the accounting manager left the Company. When the Vice President of the Contractor's company was interviewed, he was asked about the memo from the Deputy Director of OMBD. He stated that he is new to the leadership role at the company, and he said that since the accounting manager left, he has been covering their work and he submitted what he thought were different invoices, he did not realize they were the same.

The OMBD file for Contract #1 contained three MBE payment verification forms sent to the owner of MBE Subcontractor (B). There was no indication of the forms being returned. The owner (MBE Subcontractor B) was asked about the forms and said that he had not seen one in a few years and was not sure if he had sent them back.

The file for contract #1 from OMBD contained the Contractor's submission for the bid packet and OMBD's evaluation of the bid packet. Both the Contractor's submission, on the MBE-2 (subcontractor list & participation) form, and OMBD's evaluation of the bid list that MBE Subcontractor (B) will be used as a subcontractor on this contract.

The investigator confirmed with the DPU Program Manager's assigned to administer the two contracts that the Contractor and the Subcontractor (A) were using the MBE Subcontractor (B) for an employee and the MBE Subcontractor (C) to purchase plumbing supplies.

The investigator interviewed the owner of MBE Subcontractor (B) and his partner, the vice-president of the Contractor Company, and the detailed employee of the MBE Subcontractor (B). There was no dispute from any of the four individuals as to the relationship between the employee and the two companies as alleged by the complainant. It is the Contractor's position that this relationship would not be a pass-through as MBE Subcontractor (B) is minority owned and is making a profit and that both OMBD and DPU were aware of the arrangement. All four acknowledge that there are no written contracts between the Contractor and MBE Subcontractors (B) and (C). The vice president of the Contractor's Company said it was structured in this manner because their work is very specialized and there are not many other companies to do

what they do, this is evidenced by the fact that they are usually the only bidder or one of a few.

The investigator requested a written response from the Director, OMBD, asking if OMBD considered the Contractor, MBE Subcontractor (B), and MBE Subcontractor (C) to be in MBE compliance. The Deputy Director, OMBD requested a meeting with the investigator and stated with the information learned, OMBD would not consider the contractors to be in compliance. The Director, OMBD subsequently followed up with a written response indicating that the Contractor was not in compliance, no credit for MBE participation will be given to the Contractor for MBE Subcontractor (B) and MBE Subcontractor (C). The Director also stated that the Contractor's MBE participation goal had been adjusted and the contractor would now be using MBE Subcontractor (D) for MBE participation compliance.

Federal regulations and practices, namely 49 CFR 26.55, as well several state agency rules and guidelines were reviewed for standard industry practices related to minority business enterprise participation. This along with the authority cited for OMBD to establish rules and regulations and applying the cited definition for providing a *commercially useful function*, the relationship between the Contractor and MBE Subcontractor (B) fails this test and appears that MBE Subcontractor (B) is acting as a pass-through for MBE compliance. Since the relationship between the Contractor and MBE Subcontractor (B) is a pass-through and no credit should be given for MBE participation goals, the amount of time the employee spent on which type of job is a moot issue at this time.

#### Allegation #2

The investigator interviewed MBE Subcontractor (B) and inquired about MBE Subcontractor (B)'s SWAM certification and was advised that the Deputy Director OMBD contacted MBE Subcontractor (B) about the expiration and MBE Subcontractor (B) told the investigator MBE Subcontractor (B) did not recertify their SWAM certification. The investigator inquired if MBE Subcontractor (B) was an MBE contractor on Subcontractor (A)'s recently awarded a contract in 2020 and MBE Subcontractor (B) said they were going to be an MBE subcontractor for that contract as well (this is the replacement contract for #1, which expired in February 2020). The investigator asked how it was approved for MBE Subcontractor (B) to be an MBE on this contract with an expired certification and the MBE Subcontractor (B) replied with, "no one asked."

The investigator brought this up in a meeting with the Deputy Director of OMBD and the Economic Development Analyst. The Economic Development Analyst said MBE Subcontractor (B) was approved because when he checked the Small Business and Supplier Diversity registry, it showed MBE Subcontractor (B)'s recertification was pending. The investigator told the Economic and Development Analyst the registry said the same thing when checked in January and again in July. In July the investigator called the state office and found that MBE Subcontractor (B) was no longer on the registry, but was still in the contractor portal. The investigator was told the system is still holding it open because someone had gone on the portal at some point and clicked

the recertify tab which opened the process, but there was never anything filled out or submitted. The Economic Development Analyst and the Deputy Director of OMBD said they would address this development.

### Allegation #3

As noted in Allegation #1, the investigator spoke with the program managers for the contracts and confirmed the supplies purchased and submitted by the Contractor from MBE Subcontractor (C) were items used on the City of Richmond contracts and they both confirmed the purchases.

The investigator went to the office of MBE Subcontractor (C) a printing company and spoke with the owner. The investigator requested several invoices submitted by the Contractor and asked to see the paperwork associated with these purchases. The Invoices showed the items were purchased from a national plumbing supply company with a local office. The invoices from the plumbing supply company showed no state tax charged to MBE Subcontractor (C). The owner (MBE Subcontractor C) explained that in addition to his printing business, he brokers items for sale. The items are purchased from the plumbing supply company. The plumbing supply company invoices MBE Subcontractor (C), MBE Subcontractor (C) marks up the items, adds the sales tax, and bills the Contractor. The plumbing supply company delivers the supplies to Subcontractor (A).

The investigator spoke with an employee of the plumbing supply company. The investigator found that the plumbing supply company is a commercial distributor for plumbing and industrial supplies. The Contractor/Subcontractor (A) has an account with the plumbing supply company. Subcontractor (A) will sometimes order supplies directly or be invoice through MBE Subcontractor (C). When invoiced to MBE Subcontractor (C), the bill is sent to MBE Subcontractor (C) and the plumbing supply company delivers the product to Subcontractor (A). The investigator asked if MBE Subcontractor (C) gets a lower price for the product, the supply company employee said no.

Federal regulations and practices, namely 49 CFR 26.55, as well several state agency rules and guidelines were reviewed for standard industry practices related to minority business enterprise participation. This along with the authority cited for OMBD to establish rules and regulations and applying the cited definition for providing a *commercially useful function*, the relationship between the Contractor and MBE Subcontractor (A) fail this test and appears that MBE Subcontractor (C) is acting as a pass-through for MBE compliance.

**Conclusion**

Based on the findings, the OIG concludes that these allegations are substantiated. The Inspector General recommends the Office of Minority Business Development update policy and procedures to include monitoring compliance for Minority Participation. Monitor MBE-3 Reports for accuracy and completeness. Verify MBE subcontractors are properly registered with the appropriate agency. Ensure the MBE is providing the contracted work and not acting as a pass-through entity.

If you have any questions, please contact me at extension 1840.

Sincerely,



James Osuna  
Inspector General

Cc: Sharon Ebert, DCAO Economic Development  
Honorable Members of City Council  
Patricia Foster, Director of Office of Minority Business Development  
Betty Burrell, Director of Procurement Services  
Alfred Scott, Interim Director of Public Utilities