

Department of Legislative Services
Maryland General Assembly
2008 Session

FISCAL AND POLICY NOTE

House Bill 1206 (Delegate Taylor, *et al.*)
Health and Government Operations

State Procurement - Structuring and Bundling of Procurements

This bill bars a unit of State government that is subject to State procurement law from structuring or bundling a procurement for the purpose of: • precluding the participation of minority business enterprises (MBEs); • limiting the number of competitive bidders or offerors; or • limiting participation to a predetermined group of bidders or offerors.

Fiscal Summary

State Effect: No direct effect on State procurement expenditures, but the bill would likely result in the termination or substantial redesign of the Small Business Reserve Program. The program's termination or redesign could, in turn, eliminate certain inefficiencies in the State's procurement processes and alleviate administrative burdens on State procurement officers. However, the bill's prohibition against bundling of procurements could increase inefficiencies. The net effect is likely to be negligible.

Local Effect: None.

Small Business Effect: Meaningful.

Analysis

Current Law:

Minority Business Enterprise Program. The State's MBE program establishes a goal that at least 25% of the total dollar value of each agency's procurement contracts be awarded to MBEs, including 7% to African American-owned businesses and 10% to women-owned businesses. There are no penalties for agencies that fail to reach these

targets. Instead, agencies are required to use race-neutral strategies to encourage greater MBE participation in State procurements.

An MBE is a legal entity, other than a joint venture, that is:

- organized to engage in commercial transactions;
- at least 51% owned and controlled by one or more individuals who are socially and economically disadvantaged; and
- managed by, and the daily business operations of which are controlled by, one or more of the socially and economically disadvantaged individuals who own it.

MBEs include not-for-profit entities organized to promote the interests of physically or mentally disabled individuals.

A socially and economically disadvantaged individual is defined as a citizen or legal U.S. resident who is African American, Native American, Asian, Hispanic, physically or mentally disabled, a woman, or otherwise found by the State's MBE certification agency to be socially and economically disadvantaged. The Maryland Department of Transportation is the State's MBE certification agency.

A socially disadvantaged individual is someone who has been subject to racial or ethnic prejudice or cultural bias within American society because of their membership in a group and without regard to individual qualities. An economically disadvantaged individual is someone who is socially disadvantaged whose ability to compete in the free enterprise system has been impaired due to diminished capital and credit opportunities compared with those who are not socially disadvantaged. An individual with a personal net worth in excess of \$1.5 million is not considered economically disadvantaged.

The MBE program is scheduled to terminate July 1, 2012.

Small Business Reserve Program. Chapter 75 of 2004 established the Small Business Reserve Program and defined a small business as either a minority-owned business that meets the criteria specified below, or a business other than a broker that is independently owned and operated; not a subsidiary of another firm; and not dominant in its field of operation.

In addition, a business must meet the following criteria to qualify for small business certification by the State:

- average gross sales over the last three years did not exceed \$2.0 million in retail operations, wholesale operations, manufacturing operations, or service operations;

- average gross sales over the last three years did not exceed \$7.0 million in construction operations; and
- the firm does not employ more than 25 people in its retail operations, 50 people in either its wholesale or construction operations, or 100 people in either its service or manufacturing operations.

The Small Business Reserve Program requires most State procurement units to structure their procurements so that at least 10% of the total dollar value of their procurements is made directly to small businesses. Under regulations adopted by the Department of General Services, each agency must prepare an annual forecast of its total procurement spending. The agency must then develop a plan to allocate at least 10% of its forecasted spending to contracts for small businesses serving as prime contractors.

The Small Business Reserve Program sunsets September 30, 2010.

Exemptions from State Procurement Law. The University System of Maryland, Morgan State University, and St. Mary's College of Maryland are exempt from most provisions of State procurement law. However, they are subject to the goals and procedures of the State's MBE program and the University System of Maryland and Morgan State University participate in the Small Business Reserve Program. State law also exempts other agencies, in whole or in part, from State procurement law, including:

- Blind Industries and Services of Maryland;
- Maryland State Arts Council;
- Maryland Health and Higher Educational Facilities Authority;
- Department of Business and Economic Development;
- Maryland Food Center Authority;
- Maryland Public Broadcasting Commission;
- Maryland State Planning Council on Developmental Disabilities;
- Maryland Automobile Insurance Fund;
- Maryland Historical Trust;
- Rural Maryland Council;
- Maryland State Lottery Agency;
- Maryland Health Insurance Plan;
- Maryland Energy Administration;
- Maryland Developmental Disabilities Administration;
- Maryland Stadium Authority; and

- State Retirement and Pension System.

Background:

MBE Program: The 2006 MBE report issued by the Governor's Office on Minority Affairs, the most recent data available, found that 22% of the value of State procurement contracts had been awarded to MBEs. This represented a slight increase over the 21% of contract awards made to MBEs in fiscal 2005 but still short of the State's 25% target. African American-owned firms received 4.3% of contract awards and women-owned firms received 5.7%, which were also below the targets for those subgroups. Legislative Services notes that these figures represent contract awards rather than actual payments to MBEs, which experience has shown are often lower than promised participation levels at the time of contract awards. The 2006 MBE disparity study mandated by law and conducted by NERA Economic Consulting found continuing disparities between the availability and use of MBE firms for State contracts across all contracting categories and demographic groups.

Small Business Reserve Program. **Exhibit 1** lists the 22 agencies currently subject to the Small Business Reserve Program, and provides preliminary results for each one from fiscal 2006, the most recent data available. Based on these figures, the exhibit shows that only 8 of the 22 agencies achieved the program's target of 10% of procurement dollars being awarded to certified small businesses. However, all three of the State's procurement control agencies (Treasurer, Department of Budget and Management, and Department of General Services) achieved the 10% target.

Exhibit 1
Percentage of Procurement Dollars Going to Certified Small Businesses
Fiscal 2006

<u>Agency</u>	<u>% of Procurement Dollars</u>
Environment	18.9%
Maryland Stadium Authority	18.0%
State Retirement Agency	12.8%
Treasurer	11.9%
Business and Economic Development	11.6%
Budget and Management	10.7%
General Services	10.0%
Housing and Community Development	10.0%
Maryland Insurance Administration	8.8%
State Police	8.6%
Public Safety and Correctional Services	7.8%
Transportation	7.5%
Natural Resources	7.5%
University System of Maryland	5.4%
Juvenile Services	5.2%
Human Resources	3.8%
Morgan State University	3.7%
Health and Mental Hygiene	3.3%
Maryland Port Administration	3.3%
Education	2.5%
Labor, Licensing, and Regulation	1.7%
State Lottery Agency	1.0%

Source: Board of Public Works

State Fiscal Effect: The bill would not directly affect the value of State procurement expenditures, but would require the termination or substantial redesign of the Small Business Reserve Program. The program is in direct contradiction to the bill's prohibition against bundling procurements in a way that limits participation to a predetermined group of bidders or offerors.

Termination of the SBR program could have an indirect effect on State procurement spending by potentially eliminating inefficiencies in the State's procurement process. Setting aside procurements for small businesses may preclude certain economies of scale that could be provided by larger contractors. In certain cases, limiting a procurement to

small businesses could mean that a contract is not awarded to the lowest available bidder or offeror if a large company could provide the product or service for a lower price. Termination of the SBR program would also alleviate administrative responsibilities for State procurement officers who have to comply with its requirements but would not result in any direct savings or reductions in staffing.

Any potential gains in efficiency created by the elimination of the SBR program could be offset by the bill's prohibition against bundling of procurements. Procurement bundling is done to increase efficiency by having one contractor perform tasks or projects that are closely linked and would benefit from economies of scale. By prohibiting the bundling of procurements to increase MBE participation in State contracts, the bill could eliminate those efficiencies.

Small Business Effect: The termination or substantial redesign of the Small Business Reserve Program could reduce the participation of small businesses in State procurement by eliminating small business set-asides. However, small businesses that are also MBEs could still benefit from the State's MBE program.

Additional Information

Prior Introductions: None.

Cross File: SB 772 (Senators Pugh and McFadden) – Education, Health, and Environmental Affairs.

Information Source(s): Maryland Department of Transportation, Board of Public Works, Department of General Services, University System of Maryland, Department of Legislative Services

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