

Department of Legislative Services
 Maryland General Assembly
 2012 Session

FISCAL AND POLICY NOTE
Revised

House Bill 1370 (Chair, Health and Government Operations Committee, *et al.*) (By Request - Departmental - Transportation)

Health and Government Operations Education, Health, and Environmental Affairs

Procurement - Minority Business Participation

This departmental bill extends the termination date of the State’s Minority Business Enterprise (MBE) program for four years, until July 1, 2016, and requires the completion of a new disparity study by September 30, 2015. It also repeals the existing statewide goal of having at least 25% of the total dollar value of each agency’s procurement contracts be awarded to MBEs and instead requires that a statewide goal be established biennially through the regulatory process under the Administrative Procedure Act. It reaffirms the need for the MBE program based on the findings of the most recent disparity study and makes other changes related to the program’s operation.

The bill takes effect July 1, 2012.

Fiscal Summary

State Effect: Transportation Trust Fund (TTF) expenditures by the Maryland Department of Transportation (MDOT) increase by \$1.0 million in FY 2015 and \$349,100 in FY 2016 to contract with a consultant to conduct the mandated disparity study. Although the extension of the State’s MBE program could result in higher procurement costs than if the program were allowed to terminate, the program is well-established, having existed in its current form for more than 20 years and been extended five different times. Therefore, its extension has no practical fiscal effect. MDOT, the Governor’s Office of Minority Affairs (GOMA), and State procurement units can implement the bill’s additional provisions with existing resources. No effect on revenues.

(in dollars)	FY 2013	FY 2014	FY 2015	FY 2016	FY 2017
Revenues	\$0	\$0	\$0	\$0	\$0
SF Expenditure	0	0	1,047,400	349,100	0
Net Effect	\$0	\$0	(\$1,047,400)	(\$349,100)	\$0

Note:() = decrease; GF = general funds; FF = federal funds; SF = special funds; - = indeterminate effect

Local Effect: None.

Small Business Effect: MDOT has determined that this bill has a meaningful impact on small business (attached). Legislative Services concurs with this assessment. (The attached assessment does not reflect amendments to the bill.)

Analysis

Bill Summary: The biennial statewide MBE goal is established by the Special Secretary for GOMA, in consultation with the Secretary of Transportation and the Attorney General. Notwithstanding the Board of Public Works' (BPW) role in controlling State procurement, the Special Secretary must publish the biennial overall MBE goal in regulations. In a year in which there is a delay in establishing the overall goal, the previous year's goal applies. The Special Secretary is also required to establish biennial guidelines for State procurement units to consider in deciding whether to establish subgoals for different minority groups recognized in statute. In a year in which there is a delay in issuing the guidelines, the previous year's guidelines apply.

The overall goal and subgoal guidelines must be established, to the maximum extent feasible, so that they approximate the level of MBE participation that would be expected in the absence of discrimination. However, the bill does include a statement that race-conscious measures will be used only where necessary to eliminate discrimination that is not alleviated by race-neutral measures. Factors that must be considered in establishing overall goals include:

- the relative availability of minority- and women-owned businesses to participate in State procurement, based on the findings of the most recent disparity study;
- past participation of MBEs in State procurement, except participation related to leases of real property; and
- other factors that contribute to goal setting that conforms to constitutional requirements.

GOMA must allow public participation in its process for establishing overall goals and subgoal guidelines, including consulting with minority, women's, and general contractor groups, community organizations, and other stakeholder groups that could have information about (1) the availability of minority- and women-owned businesses; (2) the effects of discrimination on MBEs and women-owned businesses; and (3) the State's operation of the MBE program.

The bill gives State procurement units greater flexibility in establishing MBE participation goals for individual procurements, including the authority not to establish

goals for some contracts. In establishing goals for individual contracts, procurement units may rely on additional factors other than those already in statute that contribute to constitutional goal setting. Regulations issued by BPW must require a contract with MBE participation goals to contain a liquidated damages provision that applies in the event that the contractor fails to comply in good faith with program requirements or applicable terms in the contract.

The bill clarifies and expands several statutory provisions affecting the MBE program. Procurement units must monitor and collect data about prime contractors' compliance with contract goals and institute corrective action when prime contractors do not make good faith efforts to comply with contract goals. Units may not use quotas or any goal-setting process that solely relies on the State's or any other jurisdiction's overall MBE goal or that fails to incorporate existing requirements to analyze the availability and feasibility of MBE participation in a contract. The bill further reaffirms that MBE prime contractors must meet contract-specific MBE subcontracting goals and requires the Special Secretary, in consultation with the Secretary of Transportation and the Attorney General, to establish procedures for counting MBE prime contractors' participation in a contract against a contract's MBE goals. Individuals with physical or mental disabilities are still considered socially and economically disadvantaged, notwithstanding the findings of the most recent disparity study.

Provisions regarding changes to MBE participation schedules, which are already required by statute and regulation, are also clarified or modified. Prior to contract execution, an MBE participation schedule may not be amended unless the bidder or offeror provides a satisfactory explanation of why an unavailable or ineligible MBE was originally included on the schedule. After contract execution, the participation schedule must be attached to the contract. The prime contractor on an executed contract may not cancel the contract of an MBE subcontractor listed on the schedule without showing good cause and obtaining the prior written consent of the procurement unit's head and MBE liaison; the written consent must be sent to GOMA.

The bill's provisions are severable, and any court ruling that a provision is invalid does not affect the bill's other provisions.

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; long-standing subgoals of 7% for African American-owned businesses and 10% for woman-owned businesses were repealed by Chapters 252 and 253 of 2011. Instead, Chapters 252 and 253 authorize

GOMA, in consultation with MDOT and the Office of the Attorney General, to establish guidelines for each unit to consider while determining whether to set subgoals for individual procurements based on existing categories for minority groups. There are no penalties for agencies that fail to reach the 25% target. 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. There are no restrictions on the size or management structure of not-for-profit entities that can be considered MBEs.

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. An MBE owned by a woman who is also a member of an ethnic or racial minority group is certified as either owned by a woman or owned by a racial or ethnic minority, but not both. MDOT is the State's MBE certification agency and is responsible for conducting the mandated disparity study.

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, adjusted annually for inflation, is not considered economically disadvantaged. The inflation-adjusted limit for calendar 2012 is \$1,577,377.

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

MBE Participation Schedules and Waivers

BPW must issue regulations consistent with State procurement law to carry out the purposes of the MBE program. Procurement regulations issued under this authority

require bidders and offerors to submit with each bid or proposal an MBE participation schedule that includes the name of each certified MBE that will participate in the project, the work that each MBE will perform, and the price or contract percentage to be paid to each MBE. Failure to include the participation schedule can result in a bid or proposal being deemed not responsive. The regulations also require that procurement units verify that MBEs listed on the participation schedule actually perform the work and receive compensation consistent with the schedule.

Chapter 254 of 2011 requires a bidder or offeror on a State procurement contract that has not yet been executed to notify the procurement unit within 72 hours if an MBE listed on the MBE participation schedule has become or will become unavailable or ineligible to perform the work. In that circumstance, the bidder or offeror may submit a written request for approval to amend the MBE participation schedule submitted with the bid or offer. The request must indicate the bidder's or offeror's efforts to substitute another certified MBE to perform the same work, and it must be approved by the unit's procurement officer in consultation with the unit's MBE liaison. Chapter 254 also prohibited an MBE participation schedule from being amended after contract execution unless the request is approved by the head of the unit and the contract is amended.

A bidder or offeror may request a waiver from an MBE contract or subcontract goal. A waiver may be granted only if the bidder or offeror reasonably demonstrates that certified MBE participation could not be obtained, or could not be obtained at a reasonable price, and if the agency head determines that the public interest is served by a waiver. Failure to comply with MBE contract provisions, or to secure a waiver, can result in contract termination, referral to the Office of the Attorney General for appropriate action, or initiation of any other specific remedy identified in the contract.

Background: In 1989, the U.S. Supreme Court held in the *City of Richmond v. J.A. Croson Co.*, that state or local MBE programs using race-based classifications are subject to strict scrutiny under the equal protection clause of the Fourteenth Amendment to the U.S. Constitution. In addition, the ruling held that an MBE program must demonstrate clear evidence that the program is narrowly tailored to address actual disparities in the marketplace for the jurisdiction that operates the program. As a result, prior to each reauthorization of the State's MBE program, the State conducts a disparity study to determine whether there is continued evidence that MBEs are underutilized in State contracting. Since the program was established in its current form in 1990 in response to the *Croson* decision, it has been reauthorized five times, in 1995, 2000, 2001, 2006, and 2011, the latter for just one year. A disparity study was completed in 2006, just prior to a five-year reauthorization of the program that included a requirement for another study to be completed by September 30, 2010. Completion of that study was delayed until February 2011.

The 2011 disparity study found continued and ongoing disparities in the overall annual wages, business earnings, and rates of business formation between nonminority males and minorities and women in Maryland. For instance, average annual wages for African Americans (both men and women) and nonminority women were 33% lower than for comparable nonminority males. It also found continued disparities in the use of MBEs compared to their availability in the market place to perform work in designated categories of work. For instance, African American-owned businesses were paid 4.5% of State construction contract dollars, but they make up 9.7% of the construction sector in the State. Woman-owned businesses were paid 8.5% of maintenance contract dollars, despite making up 18.0% of the maintenance contract sector. Similar disparities were found in other contracting sectors and for other MBE categories. **Exhibit 1** shows the level of MBE participation by agency for fiscal 2010, the most recent data available.

State Fiscal Effect: MDOT's Office of Minority Business Enterprise advises that the most recent disparity study, which was completed by a consultant in February 2011, had a total cost of \$1.33 million. The study required to be completed by September 30, 2015, is assumed to have a similar cost, adjusted for inflation, of \$1,396,500. Based on the due date for the study, it is assumed that the bulk of the work by the consultant hired to do the work will occur in fiscal 2015, with a small portion of the work done in fiscal 2016 to finalize the study for publication and dissemination. Therefore, TTF expenditures by MDOT increase by \$1,047,375 in fiscal 2015 and by \$349,125 in fiscal 2016 to complete the study.

MDOT, GOMA, and State procurement units can implement the bill's remaining provisions with existing budgeted resources. The liquidated damages provisions required to be included in many State procurement contracts are not expected to have a meaningful effect on State revenues due to their limited application.

Exhibit 1
MBE Participation Rates, by Agency
Fiscal 2010

<u>Cabinet Agency</u>	<u>% MBE Participation</u>
Aging	24.2%
Agriculture	7.0%
Budget and Management	21.4%
Business and Economic Development	42.6%
Education	33.2%
Environment	25.6%
Executive Department	14.4%
General Services	30.0%
Health and Mental Hygiene	46.9%
Higher Education Commission	64.6%
Housing and Community Development	19.4%
Human Resources	14.1%
Information Technology	20.1%
Juvenile Services	14.0%
Labor, Licensing, and Regulation	24.1%
Natural Resources	11.8%
Planning	10.4%
State Police	16.3%
Public Safety and Correctional Services	20.0%
Transportation – Aviation Administration	20.6%
Transportation – Motor Vehicle Administration	25.2%
Transportation – Office of the Secretary	34.2%
Transportation – Port Administration	11.1%
Transportation – State Highway Administration	25.2%
Transportation – Transit Administration	11.4%
Transportation – Transportation Authority	26.2%
Veterans Affairs	8.6%
Cabinet Agency Total	24.5%
Public School Construction Program	19.6%
Statewide Total	23.2%

Note: Statewide total also includes public universities, Lottery, and other noncabinet State agencies.
Source: Governor's Office of Minority Affairs

Additional Information

Prior Introductions: None.

Cross File: None.

Information Source(s): Department of Budget and Management, Governor's Office of Minority Affairs, Department of General Services, Maryland Department of Transportation, University System of Maryland, Department of Legislative Services

Fiscal Note History: First Reader - March 15, 2012
ncs/rhh Revised - House Third Reader - April 1, 2012

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ANALYSIS OF ECONOMIC IMPACT ON SMALL BUSINESSES

TITLE OF BILL: Procurement – Minority Business Participation

BILL NUMBER: HB 1370

PREPARED BY: Maryland Department of Transportation

PART A. ECONOMIC IMPACT RATING

This agency estimates that the proposed bill:

 WILL HAVE MINIMAL OR NO ECONOMIC IMPACT ON MARYLAND
SMALL BUSINESS

OR

 X WILL HAVE MEANINGFUL ECONOMIC IMPACT ON MARYLAND
SMALL BUSINESSES

PART B. ECONOMIC IMPACT ANALYSIS

The impact of the legislation on small business is hard to quantify. But there should be a positive overall impact for Maryland businesses because of a reduction in discriminatory practices and increased access to opportunities for MBEs.