

Department of Legislative Services
 Maryland General Assembly
 2010 Session

FISCAL AND POLICY NOTE
Revised

House Bill 250 (Delegate Morhaim, *et al.*)
 Health and Government Operations Education, Health, and Environmental Affairs

Procurement - Minority Business Enterprises - Certification Process

This bill requires that regulations governing the State’s Minority Business Enterprise (MBE) program include provisions that promote and facilitate certification of MBEs certified by the U.S. Small Business Administration (SBA) or a county that uses a certification process that is substantially similar to the process used by the Maryland Department of Transportation (MDOT). The Board of Public Works (BPW) must report annually on the number and identity of MBEs certified through that process.

Fiscal Summary

State Effect: Transportation Trust Fund (TTF) expenditures may increase by \$50,640 in FY 2012 to hire one contractual employee to assist in processing a potential surge in applications for MDOT certification, if MDOT institutes an expedited certification process. The need for a contractual position likely ends in FY 2013 due to an anticipated drop off in the number of new certification applications. BPW can meet the reporting requirements with existing resources. Revenues are not affected.

(in dollars)	FY 2011	FY 2012	FY 2013	FY 2014	FY 2015
Revenues	\$0	\$0	\$0	\$0	\$0
SF Expenditure	0	50,600	0	0	0
Net Effect	\$0	(\$50,600)	\$0	\$0	\$0

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

Local Effect: None.

Small Business Effect: Meaningful.

Analysis

Current Law: 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 woman-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. 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.

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 fiscal 2010 is \$1,504,585.

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

Background:

MBE Certification

Only businesses that have been certified by MDOT as MBEs may participate in the State's MBE program. MBE certification requires submission of extensive documentation that the firm qualifies for MBE certification in accordance with the program's governing laws, regulations, and guidelines.

Businesses may complete a certification application online, but the application cannot be submitted electronically. Instead, applicants must print out a copy of the completed form and mail it together with the documentation requested. Among the documents that must be submitted by a corporation, partnership, or limited liability company seeking certification are:

- a current financial statement;
- complete federal tax returns for the most recent three years;
- proof of minority status (birth certificate, driver's license, passport or naturalization papers);
- general business insurance information;
- resumes of key personnel;
- a statement of net worth; and
- a statement of disadvantage (notarized affidavit).

MBE certification must be renewed annually. Recertification requires the submission of the most recent financial statement and tax returns, a personal net worth form, and a list of State contracts and subcontracts awarded to the firm.

SBA Certification

SBA certifies two types of businesses: Section 8(a) minority small businesses and HUBZone (historically underutilized business zone) small businesses. Section 8(a) of the Small Business Act is a minority-owned small business set-aside program for federal contracting. Businesses certified under the 8(a) program must be small businesses that are unconditionally owned and controlled by one or more socially and economically disadvantaged individuals who are of good character and citizens of the United States, and that demonstrate potential for success. HUBZone businesses must be small, U.S.-owned, located in a HUBZone, and have at least 35% of their employees reside in a HUBZone. Nationally, there are more than 2,000 designated HUBZones characterized by low income, high poverty, and/or high unemployment. As of 2008, there were 298

HUBZone businesses in Maryland. Although certified HUBZone businesses do not need to be minority-owned, only those that are owned by minorities would be eligible for certification as MBEs under this bill.

The small business standards that govern both 8(a) and HUBZone certification are very different from those used by Maryland. The standards vary by individual industry; however, the maximum gross annual receipts for a construction firm to qualify as a small business under federal guidelines is \$31 million, compared with Maryland's cap of \$7 million. Similarly, under the federal guidelines, small wholesalers can employ up to 100 employees, but Maryland's limit is 50 employees.

The federal guidelines for the personal net worth of a socially and economically disadvantaged individual are stricter than Maryland's guidelines. For initial 8(a) certification, the net worth of an individual claiming disadvantage must be less than \$250,000; for recertification it must be less than \$750,000, or roughly half of Maryland's net worth cap. Both the federal and State net worth caps exclude the individual's ownership interest in a primary residence and in the small business, but Maryland's net worth cap also excludes up to \$500,000 in qualified retirement savings.

State Fiscal Effect: According to MDOT, SBA reports there are approximately 1,000 8(a) certified firms in Maryland, and Baltimore City reports it has certified 1,280 minority-owned firms. Other local jurisdictions also have minority-owned business preference programs, but most require MDOT certification as a precondition to local certification (Baltimore City does not). However, MDOT does not have any information on the overlap between MBEs certified by the State and those certified by SBA or Baltimore City.

To the extent that some minority-owned firms have obtained 8(a) or Baltimore City certification but not pursued MDOT certification because they viewed the process as overly cumbersome, this bill may prompt an initial increase in the number of such firms seeking MDOT certification due to the process encouraged by this bill. The Department of Legislative Services (DLS) cannot reliably estimate how many firms may be in that position. On the one hand, the certification process is not dissimilar for the three jurisdictions, so some firms may have sought certification simultaneously to minimize the effort necessary to collect and submit the necessary documentation. Yet, the process can be cumbersome, and some firms that initially obtained certification from only SBA or Baltimore City may have decided not to pursue MDOT certification because of the effort involved.

MDOT indicates that, under the flexibility provided by the bill, it will not automatically grant certification to firms that provide evidence of certification from SBA or a local government. MDOT notes that 8(a) firms do not have to demonstrate competence in a

given field, whereas MDOT certifies firms to perform only certain functions based on the North American Industrial Classification System. Therefore, while SBA or locally certified firms may encounter an expedited certification process, they will not be granted full waivers from MDOT's process.

Therefore, DLS estimates that, to the extent MDOT institutes an expedited certification process, the bill has the potential to generate an initial surge in applications for MDOT certification from firms that have been certified by SBA or Baltimore City, but have previously opted not to pursue MDOT certification. Although a precise estimate is not possible, the number of new requests could be as high as 500. Given the bill's October 1, 2010 effective date and the time needed to promulgate regulations to establish the new process encouraged by the bill, DLS estimates that TTF expenditures may increase by \$50,640 in fiscal 2012.

MDOT has determined that one regular full-time position is needed to implement this bill. However, DLS advises that the added responsibilities incurred by this legislation are not permanent and thus may be performed by a contractual employee. This estimate reflects the cost of hiring one MBE officer to assist in processing the potential initial surge in MBE certification applicants from firms with 8(a) or local MBE certification. It includes a salary and one-time start-up costs. DLS anticipates that, after the initial surge in applications during the first year, the number of firms seeking certification will drop off, and that, beginning in fiscal 2013, MDOT will no longer require the contractual position to handle subsequent new certifications and renewals.

Salaries	\$45,922
Operating Expenses	<u>4,718</u>
Total FY 2012 State Expenditures	\$50,640

Small Business Effect: This bill will facilitate MDOT certification for participation in the State's MBE program for firms that have already been certified under the federal 8(a) program or by Baltimore City.

Additional Information

Prior Introductions: None.

Cross File: SB 130 (Senator Pugh, *et al.*) - Education, Health, and Environmental Affairs.

Information Source(s): Board of Public Works, Department of Budget and Management, Department of General Services, Maryland Department of Transportation,

University System of Maryland, U.S. Small Business Administration, Department of
Legislative Services

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