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FISCAL AND POLICY NOTE
First Reader

House Bill 1616 (Prince George's County Delegation and Montgomery
County Delegation)

Health and Government Operations

Washington Suburban Sanitary Commission – Minority Business Enterprises –
Subcontracting
PG/MC 115-18

This bill authorizes a prime contractor and higher-tier subcontractors to include lower-tier subcontractors in the calculation of the expected degree of minority business enterprise (MBE) participation under the Washington Suburban Sanitary Commission's (WSSC) MBE utilization program. It also requires the program to include specified provisions related to the participation of MBEs as both first-tier and lower-tier subcontractors. **The bill takes effect July 1, 2018.**

Fiscal Summary

State Effect: None. The bill pertains only to WSSC.

Local Effect: Expenditures by WSSC increase by \$233,500 in FY 2019 for enforcement. Out-year expenditures grow based on annualization and salary increases. No effect on revenues.

Small Business Effect: Meaningful for small businesses that contract with WSSC.

Analysis

Bill Summary: The bill applies to all WSSC contracts for design/build services, construction, and other goods and services. Regulations governing the MBE utilization program must, for contracts that have an expected level of MBE participation:

- require proof of a certified MBE commitment for both first-tier and lower-tier subcontracts;
- require each general contractor to submit monthly reports of the number of MBEs employed by each subcontractor, including lower-tier subcontractors;
- require each general contractor to provide prompt notification if a subcontract with an MBE is terminated; and
- provide for MBE participation through subcontracting in all tiers of the contract.

To assist WSSC in enforcing the MBE utilization requirements, monthly reports submitted by a certified MBE subcontractor must identify any relevant subcontracts and list payments received from any higher-tier subcontractor as well as invoices sent to higher-tier subcontractors that have not been paid.

The bill specifies that contractor compliance with MBE program requirements includes payments being made (or withheld) either by the contractor or through a higher-tier subcontractor.

Current Law: By resolution and adopting regulations, WSSC must establish a mandatory MBE utilization program to facilitate the participation of responsible certified MBEs in contracts for design/build services, construction, and goods and services. WSSC's Office of Supplier Diversity and Inclusion administers the program.

Regulations governing the program must recognize the certification of MBEs by the State and any other certification program that WSSC determines substantially duplicates the State requirements. For an overview of the State's MBE certification program, please see the **Appendix – Minority Business Enterprise Program**. Statute generally requires the regulations to address, and WSSC to enforce, MBE participation by subcontractors, but it does not address the role of lower-tier subcontractors. It also does not explicitly authorize that lower-tier subcontractors can be included in the calculation of expected MBE participation on a contract.

Local Expenditures: WSSC advises that that the bill's provisions require additional enforcement personnel to determine whether contractors comply with the expanded MBE provisions. It anticipates hiring two new compliance officers at an annual cost of \$297,960 in fiscal 2019; after reflecting a 90-day start-up delay from the bill's July 1, 2018 effective date, personnel costs by WSSC increase by \$223,470 in fiscal 2019. WSSC also anticipates making upgrades to its procurement software to accommodate enhanced enforcement, with a one-time cost of \$10,000 in fiscal 2019. Therefore, total expenditures by WSSC increase by \$233,470 in fiscal 2019; out-year costs continue to increase based on annualization and salary increases.

Small Business Effect: Small businesses that contract with WSSC must comply with the enhanced MBE participation requirements. It may be easier for them to meet MBE contract requirements if they can include the participation of lower-tier subcontractors in their calculation of MBE participation. MBEs may experience increased demand for their participation in WSSC contracts.

Additional Information

Prior Introductions: None.

Cross File: SB 948 (Senator Rosapepe) - Finance.

Information Source(s): Washington Suburban Sanitary Commission; Montgomery and Prince George's counties; Department of Legislative Services

Fiscal Note History: First Reader - March 6, 2018
nb/ljm

Analysis by: Michael C. Rubenstein

Direct Inquiries to:
(410) 946-5510
(301) 970-5510

Appendix – Minority Business Enterprise Program

The State’s Minority Business Enterprise (MBE) program requires that a statewide goal for MBE contract participation be established biennially through the regulatory process under the Administrative Procedure Act. The biennial statewide MBE goal is established by the Special Secretary for the Governor’s Office of Small, Minority, and Women Business Affairs (GOMA), in consultation with the Secretary of Transportation and the Attorney General. 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.

In August 2013, GOMA announced a new statewide goal of 29% MBE participation that applied to fiscal 2014 and 2015; as no new goal has been established, the 29% goal remains in effect for fiscal 2018. GOMA issued subgoal guidelines in July 2011, summarized in **Exhibit 1**, which are also still in effect. The guidelines state that subgoals may be used only when the overall MBE goal for a contract is greater than or equal to the sum of all recommended subgoals for the appropriate industry, plus two. In June 2014, new regulations took effect allowing MBE prime contractors to count their own work for up to 50% of a contract’s MBE goal and up to 100% of any contract subgoal. Previously, certified MBE prime contractors could not count their own participation toward any goal or subgoal on an individual contract, but their participation was counted toward the State’s MBE goal.

Exhibit 1 Subgoal Guidelines for MBE Participation

	<u>Construction</u>	<u>Architectural/ Engineering</u>	<u>Maintenance</u>	<u>Information Technology</u>	<u>Services</u>	<u>Supplies/ Equipment</u>
African American	7%	6%	8%	7%	7%	6%
Hispanic	-	2%	3%	2%	-	-
Asian	4%	-	3%	-	4%	5%
Women	-	9%	-	8%	12%	10%
Total	11%	17%	14%	17%	23%	21%
Total +2	13%	19%	16%	19%	25%	23%

MBE: Minority Business Enterprise

Source: Governor’s Office of Small, Minority, and Women Business Affairs

There are no penalties for agencies that fail to reach the statewide target. Instead, agencies are required to use race-neutral strategies to encourage greater MBE participation in State procurements.

History and Rationale of the MBE Program

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.

The most recent disparity study was completed in 2017 and serves as the basis for the most recent reauthorization of the MBE program. It 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) were 37% lower than for comparable nonminority males; average annual wages for nonminority women were 33% lower than for comparable nonminority males. It also found continued disparities in the use of MBEs by the State compared to their availability in the marketplace to perform work in designated categories of work. For instance, African American-owned construction businesses were paid 5.1% of State construction contract dollars, but they made up 10.3% of the construction sector in the relevant State marketplace. Nonminority women-owned construction businesses were paid 7.5% of State construction contract dollars but made up 13.7% of the construction sector. According to the analysis, these differences were large and statistically significant.

The MBE program is scheduled to terminate July 1, 2022; it has been reauthorized eight times since 1990, the latest by Chapter 340 of 2017. **Exhibit 2** provides MBE participation rates for major Executive Branch agencies based on contract awards made during fiscal 2016, the most recent year for which data is available.

Exhibit 2
MBE Participation Rates, by Agency
Fiscal 2016

<u>Cabinet Agency</u>	<u>% MBE Participation</u>
Aging	0.4%
Agriculture	4.7%
Budget and Management	23.8%
Commerce	5.0%
Education	15.2%
Executive Department	13.2%
General Services	21.0%
Health and Mental Hygiene*	11.2%
Higher Education Commission	4.0%
Housing and Community Development	20.1%
Human Resources*	19.8%
Information Technology	2.5%
Juvenile Services	6.8%
Labor, Licensing, and Regulation	20.8%
Military	11.3%
Natural Resources	7.2%
Planning	12.1%
State Police	10.1%
Public Safety and Correctional Services	48.8%
Transportation – Aviation Administration	20.7%
Transportation – Motor Vehicle Administration	54.3%
Transportation – Office of the Secretary	22.0%
Transportation – Port Administration	19.4%
Transportation – State Highway Administration	19.3%
Transportation – Transit Administration	20.3%
Transportation – Transportation Authority	21.1%
Statewide Total¹	20.2%

MBE: Minority Business Enterprise

¹Includes University System of Maryland, Maryland Department of the Environment, and non-Cabinet agencies.

*Former names of the Maryland Department of Health and the Department of Human Services

Source: Governor’s Office of Small, Minority, and Women Business Affairs

Requirements for MBE Certification

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.

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. 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 his or her 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 2018 is \$1,713,333.