

Department of Legislative Services
Maryland General Assembly
2013 Session

FISCAL AND POLICY NOTE

House Bill 26 (Delegate B. Robinson)
Health and Government Operations

Minority Business Enterprise Program - Former Subcontractors Transitioning to Prime Contractors

This bill requires the Board of Public Works (BPW) to develop procurement regulations under the Minority Business Enterprise (MBE) program that recognize and give credit to former subcontractors who submit bids as prime contractors if the former subcontractor has performed satisfactory work for prime contractors under State procurements over the previous 10 years.

Fiscal Summary

State Effect: Potential negative effect on the quality and timeliness of State contracts to the extent that firms with experience only as subcontractors are not otherwise qualified to become prime contractors. To the extent that the bill increases bid protests, administrative costs increase for State procurement units to adjudicate the protests. Administrative costs may also increase for the State to track and confirm subcontractors' prior experience. No effect on revenues.

Local Effect: None.

Small Business Effect: Meaningful.

Analysis

Current Law/Background: For a complete description of the MBE program, please see the **Appendix – Minority Business Enterprise Program**.

In the case of competitive sealed bids, which is the most common procurement method used in the State, State law and regulations generally require that procurement units award contracts to the responsible bidder who submits a responsive bid that is for the lowest bid price. If the invitation for bids includes additional requirements or criteria that are to be evaluated in making the award, the award is to be made to the lowest evaluated bid price. Invitations for bids, especially for large projects, typically include a requirement that bidders as prime contractors exhibit evidence of past experience as prime contractors on projects of similar size and scope. Prior experience as subcontractors typically does not count in the determination of whether bidders as prime contractors are responsible.

State Fiscal Effect: The State has a direct interest in ensuring that prime contractors, especially for large construction or other contracts, have a proven track record in managing large projects and multiple subcontractors. Subcontractors typically have specialized skills in a specific area, but they may lack expertise in managing large projects. To the extent that the bill facilitates the promotion of subcontractors who lack the preparation or experience to become prime contractors, the quality and timeliness of State contracts may deteriorate. The bill may also lead to more challenges to procurement awards from non-MBE prime contractors, which may increase administrative costs. Administrative costs may also increase for the State to track and confirm subcontractors' past experience; whether subcontractors performed adequately is not currently assessed by procurement units.

Small Business Effect: The bill facilitates the transition from subcontractor to prime contractor for small MBEs that have long participated as subcontractors in State procurement projects.

Additional Information

Prior Introductions: None.

Cross File: None.

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

Fiscal Note History: First Reader - February 4, 2013
ncs/rhh

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Appendix – Minority Business Enterprise Program

The State’s Minority Business Enterprise (MBE) program, which is scheduled to terminate July 1, 2016, 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 Minority 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.

Prior to the enactment of Chapters 252 and 253 of 2011 (HB 456/SB 120) and Chapter 154 of 2012 (HB 1370), State law established a goal that at least 25% of the total dollar value of each agency’s procurement contracts be awarded to MBEs, including subgoals of 7% for African American-owned businesses and 10% for woman-owned businesses. As of January 2013, a new statewide goal had not been issued by GOMA, so the 25% statewide goal remains in effect. GOMA issued subgoal guidelines in July 2011, summarized in **Exhibit 1**, which are 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 percentage points.

Exhibit 1 Subgoal Guidelines Issued July 2011

	<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%

Source: Governor’s Office of Minority 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 February 2011 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) 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 marketplace 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.

Another disparity study is due by December 31, 2015, prior to the July 1, 2016 termination date for the MBE program. (The program has been reauthorized six times since 1990, most recently by Chapter 154 of 2012.) **Exhibit 2** provides MBE participation rates for major Executive Branch agencies for fiscal 2011, the most recent year for which data is available.

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.

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. 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 2013 is \$1,615,663.

Exhibit 2
MBE Participation Rates, by Agency
Fiscal 2011

<u>Agency</u>	<u>% MBE Participation</u>
Aging	30.7%
Agriculture	6.9%
Budget and Management	10.5%
Business and Economic Development	43.9%
Education	20.3%
Environment	25.2%
Executive Department	14.0%
General Services	33.9%
Health and Mental Hygiene	46.1%
Higher Education Commission	14.0%
Housing and Community Development	21.9%
Human Resources	8.4%
Information Technology	13.7%
Juvenile Services	8.9%
Labor, Licensing, and Regulation	36.1%
Morgan State University	22.3%
Natural Resources	10.9%
Planning	8.3%
State Police	8.8%
Public Safety and Correctional Services	33.0%
Transportation – Aviation Administration	26.2%
Transportation – Motor Vehicle	46.7%
Transportation – Office of the Secretary	29.5%
Transportation – Port Administration	7.8%
Transportation – State Highway	26.1%
Transportation – Transit Administration	16.8%
Transportation – Transportation Authority	25.4%
University System of Maryland	19.7%
Veterans Affairs	18.2%
Statewide Total¹	23.8%

¹Includes additional non-Cabinet agencies.
Source: Governor’s Office of Minority Affairs
