HB 422

Department of Legislative Services

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FISCAL AND POLICY NOTE
Third Reader

House Bill 422 (Delegate D. Barnes)
Economic Matters Education, Health, and Environmental Affairs

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Minority Participation in the Alcoholic Beverages Industry - Study

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This bill requires the Governor's Office of Small, Minority, and Women Business Affairs (GOSBA), in consultation with specified entities, to conduct a study of the participation of minority-owned businesses in the alcoholic beverages industry in the State. The Office of the Attorney General (OAG) and the Maryland Department of Transportation (MDOT) provide staff for the study. GOSBA must report its findings and recommendations to the Governor and the General Assembly by January 1, 2021. **The bill takes effect June 1, 2021, and terminates June 30, 2022.**

Fiscal Summary

State Effect: General and/or special fund expenditures increase, potentially significantly, in FY 2022 to conduct the required disparity study, as discussed below. GOSBA and/or MDOT can otherwise conduct the study with existing resources. Apart from any costs associated with the disparity study, OAG and MDOT can provide staff support for the study with existing resources. No effect on revenues.

Local Effect: None.

Small Business Effect: Minimal.

Analysis

Bill Summary: The study must include:

- historical and current levels of participation by minority-owned businesses in the alcoholic beverages industry in the State;

- historical and current levels of market activity in retail sales of alcoholic beverages in the State, especially in areas with high concentrations of minority population;
- a demonstration of historical and current disparities in the levels of participation of minorities in the alcoholic beverages industry *through a commissioned and completed disparity study (*emphasis added); and
- consideration and development of legally supportable mechanisms to increase the participation of minorities in each tier of the alcoholic beverages industry.

Current Law: For a complete description of the State's Minority Business Enterprise (MBE) program, please see the **Appendix – Minority Business Enterprise Program**.

The distinctive component of Maryland's approach to regulating alcohol sales is the three-tier distribution system. Designed to thwart an arrangement called "vertical integration" in which all steps in the supply chain are controlled by the same company, the system separates ownership and operations among (1) manufacturers; (2) wholesalers; and (3) retailers. In its purest form, the system authorizes manufacturers (tier one) to sell only to wholesalers (tier two); wholesalers only to retailers (tier three); and retailers only to consumers. Generally in Maryland, the Alcohol and Tobacco Commission issues statewide licenses to manufacturers and wholesalers (an authority that transferred from the Comptroller's Office by statute, beginning in 2021), while each licensing jurisdiction issues licenses to retailers to operate within its boundaries.

State Expenditures: As noted in the appendix, implementation of race-based procurement preferences or set-aside programs must be justified by the results of a study that shows disparity in the participation of minority-owned businesses in particular industries. The bill requires GOSBA to conduct such a study, but it also requires MDOT to provide staff for the study. The appendix notes that MDOT is the State's MBE certification agency; in that capacity, MDOT conducts the statewide MBE disparity studies roughly every five years. The last one was completed in February 2017. Therefore, GOSBA has no experience conducting a disparity study.

A complete statewide disparity study typically costs between $3 million and $5 million. Industry-specific disparity studies cost less, but the price varies depending on whether the statewide study examined the specific industry (alcohol manufacturing, distribution, and sales) in question, and whether data from the statewide study can, therefore, be used and/or reanalyzed for the industry-specific study. Chapter 598 of 2018 required a disparity study for the medical cannabis industry, and MDOT was able to do a reanalysis of the statewide data because it included the necessary North American Industrial Classification System (NAICS) industry codes for the medical cannabis industry. That reanalysis was done for approximately $75,000. However, MDOT advises that if an original study for the alcohol industry is necessary, it may cost as much as $500,000.

A review of the 2017 statewide study does not offer a definitive answer regarding whether NAICS codes for the alcohol industry were included in the analysis. The "commodities, supplies, and equipment" industry category included some industry groups that may include components of the alcohol industry, including "special food services," "beverage manufacturing," and "specialty food stores," but these findings do not yield a definitive conclusion regarding the inclusion of the alcohol industry. A more in-depth analysis of the NAICS codes used in the analysis is required and that is beyond the scope of this fiscal and policy note.

Thus, the cost of the disparity study required by the bill likely ranges between $75,000 and $500,000, depending on the availability of data from the statewide study. As the bill requires GOSBA to conduct the study with staff support from MDOT, which has extensive experience managing similar studies and also has access to the data from the statewide study, either general or special funds (or both) may be used for the study. GOSBA otherwise advises that, if MDOT takes the lead on the disparity study, it can provide support with existing resources. It is assumed that OAG and MDOT can provide staff support to the study with existing resources.

Additional Information

Prior Introductions: HB 1333 of 2020 passed the House as amended and was referred to the Senate Education, Health, and Environmental Affairs Committee, but no further action was taken.

Designated Cross File: SB 285 (Senator Patterson) - Education, Health, and Environmental Affairs.

Information Source(s): Department of Commerce; Maryland Department of Transportation; Governor's Office of Small, Minority, and Women Business Affairs; Montgomery and Prince George's counties; Comptroller's Office; Department of Legislative Services

Fiscal Note History: First Reader - February 18, 2021
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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 (GOSBA), 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, GOSBA 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 2021. GOSBA issued subgoal guidelines in July 2011 and then updated them effective August 2020, as summarized in **Exhibit 1.** 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 Minority Business Enterprise Participation

	Construction	Architectural/ Engineering	Maintenance	Information Technology	Services	Supplies/ Equipment
African American	8%	7%	9%	10%	-	6%
Hispanic	-	-	3%	-	2%	2%
Asian	-	-	2%	-	3%	-
Women	11%	10%	-	10%	10%	8%
Total	**19%**	**17%**	**14%**	**20%**	**15%**	**16%**
Total +2	**21%**	**19%**	**16%**	**22%**	**17%**	**18%**

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 Minority Business Enterprise 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 2019, the most recent year for which data is available.

Exhibit 2
Minority Business Enterprise Participation Rates, by Agency
Fiscal 2019

Cabinet Agency	% Participation
Aging	1.4%
Agriculture	4.9%
Budget and Management	7.4%
Commerce	1.2%
Education	6.0%
Environment	28.6%
Executive Department	1.8%
General Services	15.0%
Health	14.6%
Higher Education Commission	3.0%
Housing and Community Development	38.4%
Human Services	14.7%
Information Technology	15.4%
Juvenile Services	19.5%
Labor	26.1
Military	7.0%
Natural Resources	NA[1]
Planning	4.6%
State Police	15.0%
Public Safety and Correctional Services	17.5%
Transportation – Aviation Administration	27.2%
Transportation – Motor Vehicle Administration	16.0%
Transportation – Office of the Secretary	18.5%
Transportation – Port Administration	18.5%
Transportation – State Highway Administration	20.3%
Transportation – Transit Administration	15.1%
Transportation – Transportation Authority	11.6%
Statewide Total[2]	**17.9%**

[1] Data not provided.
[2] Includes the University System of Maryland, Morgan State University, St. Mary's College of Maryland, and non-Cabinet agencies.

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

Requirements for Minority Business Enterprise 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 may be certified as being owned by both a woman and by a member of a racial or ethnic minority, but for the purpose of participating on a contract as an MBE, it can only be counted as one or the other. 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 2021 is $1,788,677.