Department of Legislative Services

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2021 Session

FISCAL AND POLICY NOTE
First Reader

Senate Bill 33 (Senator Ellis)
Education, Health, and Environmental Affairs

State and County Procurement - Minority Business Enterprise Program Participation Goals

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This bill establishes a procurement preference program for African American-owned businesses that mirrors the State's current minority business enterprise (MBE) preference program. It also requires specified county governments to establish a procurement participation goal for African American-owned businesses and to structure their procurement procedures to try to achieve that goal. **The bill is contingent on the completion of the next scheduled disparity study and on a finding in the study that the new program meets federal or constitutional requirements.**

Fiscal Summary

State Effect: The bill likely has substantial operational effects on various State agencies, but it likely has limited or no effect on governmental finances, as discussed below.

Local Effect: The bill likely has no material effect on local governmental finances, as discussed below.

Small Business Effect: Potential meaningful.

Analysis

Bill Summary:

State Preference Program

The bill removes African Americans from the current definition of "socially and economically disadvantaged individual[s]" and instead alters the existing definition of an MBE to include any business organized to engage in commercial transactions that is:

- at least 51% owned and controlled by one or more individuals who have origins in any of the black racial groups of Africa;
- managed by, and the daily business operations of which are controlled by, one or more of the individuals who have such origins; and
- is not owned, controlled, or managed by an individual whose personal net worth exceeds $1.5 million, as adjusted annually for inflation according to the Consumer Price Index.

The bill requires the Special Secretary for the Office of Small, Minority, and Women Business Affairs to establish two separate contract participation goals, one for MBEs (as in current law but not including African American-owned firms) and one for African American-owned firms. In setting the goals, the Governor's Office of Small, Minority, and Women Business Affairs (GOSBA) must consider the percentage of the State's population who have origins in any of the black racial groups of Africa (in addition to factors in current law). State agencies must then structure their procurement procedures to meet both goals.

County Preference Programs

Any county that has a procurement program that seeks to encourage and assist the participation of MBEs in county procurement must establish an overall percentage participation goal for African American-owned businesses. In establishing the goal, the counties must consider the percentage of the county's population who have origins in any of the black racial groups of Africa. Each affected county must then structure its procurement procedures to try to achieve their respective participation goals.

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

The next disparity study is scheduled to be completed and delivered to the Legislative Policy Committee by September 30, 2021.

State Expenditures: This analysis assumes that the bill's provisions are found to be consistent with constitutional requirements. The Department of Legislative Services (DLS) notes, however, that there is a possibility that such a finding may not occur. Race-based preference programs are subject to strict scrutiny and guidelines, as described in the appendix, including that any participation goal be based on the prevalence of minority-owned firms in the marketplace. The requirement that the proportion of African Americans in the larger population be considered may be found to not be consistent with those strict requirements.

GOSBA and the Maryland Department of Transportation (MDOT) both advise that they require additional staff to administer and enforce the bill's requirements, but DLS disagrees. GOSBA's estimate is largely based on an interpretation that it will have to oversee implementation of county preference programs for African American-owned businesses, but the bill assigns that responsibility to the counties themselves. Moreover, the goal-setting process managed by GOSBA is generally not a labor-intensive process; the statewide goal has not changed since 2013, and it is generally dictated by the findings of the periodic disparity study. Moreover, as GOSBA recently updated its subgoals (including the subgoal for African American-owned businesses), establishing a new goal for that subgroup should not require additional staff. Although incorporating the overall proportion of the African American population into the calculation may affect the goal, it does not substantially complicate the goal-setting process.

With regard to MDOT, which certifies MBEs, the bill does not substantially alter the certification requirements or process. The current process already distinguishes firms according to the race/ethnicity of its owners (for the purpose of tracking subgoals). However, because the bill rebases the net worth for African American-owned MBEs at $1.5 million (whereas for other MBEs it has escalated to almost $1.8 million due to inflation), more African American-owned firms will qualify as MBEs under the bill than under current law. Nevertheless, MDOT likely does not require additional staff.

Agencies most certainly experience operational challenges associated with complying with two separate preference programs. Only a subset of contracts currently apply the MBE subgoals; the bill requires that every contract apply two different goals (MBE and African American) to each contract. However, agencies should be able to adapt to the new requirements with existing staff, as the changes required are largely procedural in nature.

Local Expenditures: The bill affects only counties that already have an MBE program in place. As is the case with State agencies, carving out a separate goal for African American-owned businesses can likely be carried out with existing staff, as reported by both Montgomery and Prince George's counties. Nevertheless, counties also likely experience operational challenges in establishing a parallel preference program.

Small Business Effect: The bill's effect on minority-owned businesses is unclear, as it depends on the goal established for African American-owned businesses and the resulting effect on companies owned by other racial minorities.

Additional Information

Prior Introductions: None.

Designated Cross File: None.

Information Source(s): Governor's Office of Small, Minority, and Women Business Affairs; Garrett, Montgomery, and Prince George's counties; Department of General Services; Board of Public Works; Maryland Department of Transportation; Department of Legislative Services

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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 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 2021 is $1,788,677.