

Department of Legislative Services
Maryland General Assembly
2023 Session

FISCAL AND POLICY NOTE
First Reader

House Bill 646 (Delegate Charles, *et al.*)
Health and Government Operations and
Appropriations

State Procurement - Minority Business Enterprises and Small Business
Enterprises - Procurement Forecast, Employee Performance, and Outreach
(Small Business Protection Act of Maryland)

This bill bars procurement officers and other procurement-related employees from receiving merit increases or promotions in any fiscal year in which their agency does not meet the State’s minority business enterprise (MBE) goal and does not show improvement over the prior year’s performance. If there is no improvement in meeting the goal over three consecutive fiscal years, the agency must either terminate the employees’ employment or reassign them to a position that does not involve procurement. The bill also requires State agencies to publish, by May 1 each year, a forecast of anticipated procurements in the coming year and the anticipated MBE participation goal for each procurement. The Governor’s Office of Small, Minority, and Business Affairs (GOSBA) must conduct specified outreach and develop a program to (1) identify and increase awareness of procurement opportunities for small businesses and (2) assist small businesses in participating in State procurement.

Fiscal Summary

State Effect: Likely short-term reductions in expenditures (all funds) for employee compensation, but expenditures likely increase significantly over time for employee recruitment and training due to increased employee turnover, as discussed below. GOSBA can implement the bill with existing resources. No effect on revenues.

Local Effect: None.

Small Business Effect: Potential meaningful.

Analysis

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

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

GOSBA is established in statute and is led by a Special Secretary appointed by the Governor. Statute assigns numerous responsibilities to GOSBA, among them:

- promoting activities and the use of resources of the State, local governments, and private entities for the growth of MBEs;
- providing training and educational opportunities for nonminority prime contractors regarding the duties and responsibilities of a prime contractor with respect to MBEs; and
- providing technical assistance and managerial assistance to MBEs.

In addition to overseeing the MBE program, GOSBA also oversees the Small Business Reserve Program and the Veteran-Owned Small Business Enterprise program.

State Fiscal Effect: As the appendix shows, in fiscal 2021, only three agencies met the State's 29% goal for MBE contracting, and the State as a whole fell well short of the goal. Moreover, the State has not met its MBE goal since it was set at that level in 2012. Thus, the bill likely results in a significant number of State employees not qualifying for annual merit increases or promotions. Although this has the potential to reduce State expenditures (all funds) for employee compensation in the near term, it also has the potential to lead to significant staff turnover, resulting in significant recruitment and training costs and loss of efficient State operations over the long term. Multiple agencies advise that they have a high volume of vacancies in their procurement divisions and that filling more vacancies would be problematic, especially in the context of the bill's punitive provisions.

These effects may be offset to the extent that the bill provides incentives for agencies (particularly, procurement staff in those agencies) to improve MBE performance, but it is not clear that it does so. The 29% MBE goal currently set in regulation is a statewide aspirational goal and is not intended to serve as a goal for each contract or for each agency. The role of procurement staff within agencies is to set MBE goals for each contract that maximize MBE contracting opportunities based on the goods or services being purchased and the availability of certified MBEs in the marketplace for those specific goods or services. Many contracts have goals that are well below 29% because the marketplace does not have the capacity to reach that level for a specific good or service. Thus, depending on the mix of goods and services that a particular agency purchases, procurement staff in an

agency can implement the MBE program as it is designed and intended to be implemented and still not achieve the goal. Moreover, responsibility for enforcing contract goals rests with an agency's contract managers, not procurement staff. Thus, under the bill, procurement staff may be held accountable for something they cannot control.

The bill's other provisions have no material operational or fiscal effect. Agencies already provide procurement forecasts to GOSBA under current law. GOSBA already conducts outreach and training for MBEs and, therefore, advises that it can carry out those requirements with existing resources.

Small Business Effect: To the extent that the bill results in agencies improving their performance relative to the State's MBE participation goal, small businesses experience an increase in opportunities to do business with the State.

Additional Information

Prior Introductions: Similar legislation has not been introduced within the last three years; however, legislation with similar provisions has been proposed. For example, see SB 207 of 2021.

Designated Cross File: SB 578 (Senator Hayes) - Budget and Taxation.

Information Source(s): Governor's Office of Small, Minority, and Women Business Affairs; Maryland Department of Aging; Department of Commerce; Maryland State Treasurer's Office; Maryland Higher Education Commission; Maryland State Library Agency; Maryland State Department of Education; University System of Maryland; Morgan State University; Public School Construction Program; Maryland Department of Agriculture; Department of Budget and Management; Maryland Department of the Environment; Department of General Services; Department of Human Services; Maryland Department of Health; Department of Juvenile Services; Department of Natural Resources; Maryland Department of Planning; Department of Public Safety and Correctional Services; Board of Public Works; Department of State Police; Maryland Department of Transportation; Department of Veterans Affairs; State Department of Assessments and Taxation; Maryland Energy Administration; Maryland Insurance Administration; Maryland State Lottery and Gaming Control Agency; State Retirement Agency; 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 Office of the Attorney General (OAG). 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. The Maryland Department of Transportation is the State’s MBE certification agency.

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 2023. 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. MBE prime contractors may count their own work for up to 50% of a contract’s MBE goal and up to 100% of any contract subgoal. Their full participation counts toward the State’s 29% goal.

Exhibit 1 Subgoal Guidelines for Minority Business Enterprise Participation

	<u>Construction</u>	<u>Architectural/ Engineering</u>	<u>Maintenance</u>	<u>Information Technology</u>	<u>Services</u>	<u>Supplies/ Equipment</u>
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. However, Chapters 155 and 156 of 2022 require GOSBA to refer prime contractors that persistently fail to meet MBE participation goals on their contracts to OAG for debarment for up to three years.

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 disparity study completed in 2017 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, 2024; Chapter 117 of 2022, which reauthorized the program for the ninth time since its inception, required a new disparity study to be completed by September 2023 to inform the subsequent reauthorization process. **Exhibit 2** provides MBE participation rates for major Executive Branch agencies based on contract awards made during fiscal 2021, the most recent year for which data is available.

Exhibit 2
Minority Business Enterprise Participation Rates, by Agency
Fiscal 2021

<u>Cabinet Agency</u>	<u>% Participation</u>
Aging	0.1%
Agriculture	5.0%
Budget and Management	1.0%
Commerce	2.2%
Education	4.4%
Environment	33.4%
Executive Department	2.2%
General Services	15.3%
Health	3.6%
Higher Education Commission	0.7%
Housing and Community Development	22.6%
Human Services	NA
Information Technology	6.0%
Juvenile Services	12.6%
Labor	3.3%
Military	1.4%
Natural Resources	1.2%
Planning	1.2%
State Police	8.2%
Public Safety and Correctional Services	33.3%
Transportation – Aviation Administration	21.5%
Transportation – Motor Vehicle Administration	32.8%
Transportation – Office of the Secretary	28.20%
Transportation – Port Administration	17.8%
Transportation – State Highway Administration	24.5%
Transportation – Transit Administration	23.9%
Transportation – Transportation Authority	19.3%
Statewide Total¹	17.2%

¹ Includes the University System of Maryland, Morgan State University, St. Mary’s College of Maryland, and non-Cabinet agencies.

NA: Not Available/Did Not Report

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.

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 2023 is \$1,995,008.