

Department of Legislative Services
 Maryland General Assembly
 2021 Session

FISCAL AND POLICY NOTE
 Third Reader - Revised

Senate Bill 909

(Senator Smith, *et al.*)

Budget and Taxation

Appropriations

Capital Projects - Minority Business Enterprise Goals

This bill requires the Governor’s Office of Small, Minority, and Women Business Affairs (GOSBA) – prior to the release of funds to a recipient of a State capital grant of \$3.0 million or more from a miscellaneous grant program, a House of Delegates initiative, or a Senate initiative – to review the project for subcontracting opportunities under the State’s Minority Business Enterprise (MBE) program and, if practicable, establish MBE subgoals for the project. The bill establishes oversight and reporting requirements for GOSBA and the Department of General Services (DGS). **The bill takes effect July 1, 2021, but the application of MBE subgoals to grant recipients takes effect July 1, 2022.**

Fiscal Summary

State Effect: General fund expenditures increase by \$26,900 in FY 2022 to implement the bill; out-year expenditures reflect annualization and ongoing operating expenses. Costs may increase further, potentially significantly, if a determination is made that a new disparity study must be completed, as discussed below. No effect on State revenues.

(in dollars)	FY 2022	FY 2023	FY 2024	FY 2025	FY 2026
Revenues	\$0	\$0	\$0	\$0	\$0
GF Expenditure	26,900	42,000	43,100	44,700	46,400
Net Effect	(\$26,900)	(\$42,000)	(\$43,100)	(\$44,700)	(\$46,400)

Note: () = decrease; GF = general funds; FF = federal funds; SF = special funds; - = indeterminate increase; (-) = indeterminate decrease

Local Effect: Any local government projects that receive miscellaneous State capital grants of at least \$3.0 million are subject to the bill’s requirements. They can comply with the requirements, or request a waiver, with existing resources. No effect on local revenues.

Small Business Effect: Potential meaningful.

Analysis

Bill Summary: In setting subgoals for a project, GOSBA must consider the availability and capacity of MBEs in Maryland and in the county where the project is located to fulfill the subgoal. If GOSBA establishes MBE subgoals for a capital project, the recipient must (1) certify to DGS that the recipient expects to achieve the subgoals or (2) request a waiver of all or part of the subgoals from GOSBA. GOSBA must review each request for a waiver and report the revised subgoals to DGS.

By July 31 of each year, DGS must submit a report to the Governor and the General Assembly on the number of waivers granted for the prior fiscal year. The report must include (1) a description of the capital project; (2) whether the waiver was a partial or full waiver; and (3) the justification for the waiver.

By June 30, 2022, the Special Secretary for GOSBA, in consultation with the Secretary of Transportation and the Attorney General, must establish policies and guidelines to implement the bill's provisions. By December 1, 2022, GOSBA must report to the General Assembly on the establishment of MBE subgoals in accordance with the bill, including (1) whether the establishment of subgoals was practicable based on the type of capital project and (2) whether any changes should be made to the capital MBE subgoal framework established by the bill.

The bill may not be construed to prevent a capital project that meets the threshold requirements, and for which a waiver has been requested, from receiving funds appropriated for the project in the capital budget.

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

The General Assembly may authorize the Board of Public Works (BPW) to borrow money for any public purpose and issue State bonds to evidence the debt.

With the support of a legislative sponsor, any applicant may request funding from the General Assembly for a capital project. Projects that request funding must (1) be capital in nature; (2) have a useful life of at least 15 years; (3) serve a public purpose; and (4) not be for a religious purpose. For the 2021 session, project sponsors do not need to provide matching funds (which have been required in the past).

State Expenditures:

Department of General Services

The Capital Grants and Loan Division within DGS oversees and monitors approximately 1,400 active recipients of capital grants from the State. Each project is required to undergo a compliance review process to ensure its compliance with the program's current requirements as established by BPW. Between 200 and 300 new projects are typically authorized each year; in recent years, between 10 and 12 projects have received grants of at least \$3.0 million each year.

The bill assigns two new duties to DGS, which can be absorbed with existing resources. The first is to receive certifications from affected grantees that they expect to achieve the MBE subgoals established by GOSBA. The bill does not assign any enforcement duties to DGS related to monitoring achievement of the goals, nor does it make achievement of the goals a condition of the grant, so negligible additional effort by DGS is required. DGS may elect to incorporate MBE compliance in its compliance review process, but, in the absence of an active enforcement role, that can be done with existing resources. Second, the bill requires DGS to report annually on the number and nature of waivers awarded to grantees. Given the limited number of affected grantees each year, DGS can prepare the required report with existing resources.

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

The bill requires GOSBA to (1) establish policies and guidelines to implement the bill; (2) review each project for subcontracting opportunities; (3) if practicable, establish MBE subgoals for the project; (4) review and process requests for waivers of the subgoals from grantees; and (5) report by December 2022 on the implementation of the program. These tasks, though related to GOSBA's mission, are beyond GOSBA's current duties and expertise and require additional staff. The limited number of affected projects, however, requires only a half-time staff person.

Therefore, general fund expenditures increase by \$26,886 in fiscal 2022, which accounts for new staff beginning on January 1, 2022, due to MBE requirements not applying to grant recipients until fiscal 2023. The estimate reflects a 0.5 full-time-equivalent MBE compliance officer to perform the functions assigned to GOSBA, as described above, and allows sufficient time to establish guidelines and begin reviewing new grantees when the fiscal 2023 capital budget is passed in April 2022. It includes a salary, fringe benefits, one-time start-up costs, and ongoing operating expenses.

Position	0.5
Salary and Fringe Benefits	\$21,632
Operating Expenses	<u>5,254</u>
Total FY 2022 GOSBA Expenditures	\$26,886

Future year expenditures reflect a full salary with annual increases and employee turnover and ongoing operating expenses.

Disparity Study

As noted in the appendix, the *Croson* decision by the Supreme Court requires that a race-based preference program be based on demonstrated economic disparities based on race, which has typically been demonstrated by the completion of a disparity study. GOSBA advises that the State’s disparity study examines disparities in State procurement spending and that a new disparity study must be conducted prior to the implementation of the bill to examine disparities outside of State procurement spending. A full disparity study costs between \$3 million and \$5 million; reanalysis of data collected by existing studies cost much less, typically between \$75,000 and \$500,000.

However, the Department of Legislative Services advises it is not certain that a new study or reanalysis is required for two reasons: (1) the current study, although focused on State spending, also demonstrates economic disparities in Maryland’s commercial region; and (2) State funds are being used, at least in part, to fund the capital projects affected by the bill. However, to the extent that a new disparity study, or reanalysis, is needed, costs increase, potentially significantly, to conduct the study. Further, implementation of the bill is likely delayed by at least one year until the study is completed.

Small Business Effect: The bill may expand contracting opportunities for MBEs in the construction industry to participate in capital construction projects that receive State grants.

Additional Information

Prior Introductions: None.

Designated Cross File: None.

Information Source(s): Governor’s Office of Small, Minority, and Women Business Affairs; Department of General Services; Board of Public Works; Maryland Department of Transportation; Department of Legislative Services

Fiscal Note History:
rh/ljm

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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

	<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. 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

<u>Cabinet Agency</u>	<u>% Participation</u>
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 Total²	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.