

Department of Legislative Services
Maryland General Assembly
2022 Session

FISCAL AND POLICY NOTE
Third Reader - Revised

House Bill 542
Appropriations

(Delegate J. Lewis)

Budget and Taxation

State Retirement and Pension System - Use of Minority and Women-Owned
Business Enterprises (Diversity Among Asset Managers Act of 2022)

This bill requires the Maryland Department of Transportation (MDOT) and the Governor’s Office of Small, Minority, and Women Business Affairs (GOSBA), in consultation with specified entities, to conduct a study regarding brokerage and investment management services used by the State Retirement and Pension System (SRPS) to evaluate whether remedial measures to assist minority- and women-owned businesses in those sectors are consistent with specified federal or constitutional requirements. Beginning in fiscal 2023 and annually thereafter, the SRPS board must assess the use of minority business enterprises (MBEs) as required by the bill. **The bill takes effect June 1, 2022; provisions related to studies and reports by MDOT and GOSBA terminate June 30, 2023.**

Fiscal Summary

State Effect: Transportation Trust Fund (TTF) expenditures increase in FY 2023 by between \$30,000 and \$90,000 for a disparity study. Otherwise, MDOT and GOSBA can implement the bill’s provisions with existing resources. Any effect on SRPS assets and pension liabilities is contingent on the findings of the mandated study and any remedial measures implemented as a result and, therefore, cannot be reliably estimated.

Local Effect: Any effect on local pension assets and pension liabilities is contingent on the findings of the mandated study and any remedial measures implemented as a result and, therefore, cannot be reliably estimated.

Small Business Effect: Potential meaningful.

Analysis

Bill Summary: SRPS must provide MDOT any information deemed necessary to assess the need for remedial measures to assist minority- and women-owned businesses in the brokerage and investment management industry and market. By July 1, 2023, MDOT and GOSBA must submit their findings to the Legislative Policy Committee (LPC).

GOSBA, in consultation with specified entities, must develop race- and gender-neutral approaches to address the needs of minority- and women-owned businesses in the brokerage and investment management services industry and market. It must submit its report to LPC by December 1, 2022.

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

Consistent with minority business purchasing standards in State law and consistent with its fiduciary duties, the board must direct the Investment Committee to *attempt to use, to the greatest extent feasible*, MBEs to provide brokerage and investment management services. To achieve this goal, the Investment Committee must take measures to remove barriers to the full participation of MBEs in brokerage and investment management services. Current law does not establish a specific numeric goal for MBE participation in brokerage or investment management services.

Fiduciary Duties

Members of the SRPS board, as fiduciaries, must discharge their duties solely in the interest of participants and:

- for the exclusive purpose of providing benefits to members and for reasonable expenses of operating the system;
- with the care, skill, prudence, and diligence under the circumstance then prevailing, that a prudent person acting in like capacity and familiar with such matters would use;
- by diversifying the investments to minimize the risk of large losses; and
- in accordance with the laws, documents, and instruments governing the system.

State Expenditures: MDOT advises that TTF expenditures increase for a separate disparity analysis of the brokerage and investment management industry; that study is expected to cost between \$30,000 and \$90,000 in fiscal 2023. MDOT notes, however, that completion of the required disparity analysis may divert agency and contractor resources from the ongoing statewide disparity study for the reauthorization of the MBE program

and, therefore, may delay its completion. MDOT further advises that the schedule and quality of the required report is dependent on the data provided by SRPS for the disparity analysis.

Small Business Effect: Small, minority- and women-owned businesses that provide asset management and brokerage services may benefit from any remedial measures and race- and gender-neutral approaches implemented as a result of the disparity study findings and the bill.

Additional Information

Prior Introductions: None.

Designated Cross File: SB 954 (Senator Benson) - Budget and Taxation.

Information Source(s): Maryland State Treasurer's Office; Department of General Services; Maryland Department of Transportation; State Retirement Agency; Department of Legislative Services

Fiscal Note History: First Reader - February 16, 2022
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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. The Maryland Department of Transportation (MDOT) 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 2022. 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. 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 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, 2022; Chapter 340 of 2017, which reauthorized the program for the eighth time since its inception, required a new disparity study to be completed by September 2021 to inform the subsequent reauthorization process. However, MDOT has requested an extension to September 2023 due to delays in procuring a consultant to conduct the study. The program may be reauthorized in its current form pending the completion of the study. **Exhibit 2** provides MBE participation rates for major Executive Branch agencies based on contract awards made during fiscal 2020, the most recent year for which data is available.

Exhibit 2
Minority Business Enterprise Participation Rates, by Agency
Fiscal 2020

<u>Cabinet Agency</u>	<u>% Participation</u>
Aging	0.6%
Agriculture	7.2%
Budget and Management	0.8%
Commerce	9.1%
Education	3.7%
Environment	9.0%
Executive Department	1.4%
General Services	16.5%
Health	10.5%
Higher Education Commission	1.1%
Housing and Community Development	20.9%
Human Services	7.2%
Information Technology	3.7%
Juvenile Services	5.6%
Labor	6.0%
Military	3.3%
Natural Resources	2.5%
Planning	6.6%
State Police	24.0%
Public Safety and Correctional Services	11.3%
Transportation – Aviation Administration	25.0%
Transportation – Motor Vehicle Administration	38.6%
Transportation – Office of the Secretary	22.0%
Transportation – Port Administration	14.3%
Transportation – State Highway Administration	18.4%
Transportation – Transit Administration	17.0%
Transportation – Transportation Authority	20.3%
Statewide Total¹	14.1%

¹ 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.

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 2022 is \$1,847,024.