

Department of Legislative Services
Maryland General Assembly
2019 Session

FISCAL AND POLICY NOTE
First Reader

Senate Bill 433 (Senator Zucker, *et al.*)
Education, Health, and Environmental Affairs

Responsible Workforce Development Percentage Price Preference Act

This bill establishes a procurement price preference of at least 4% for a responsive bid for which either (1) the responsible bidder and each subcontractor certify that their total payments for employee health care expenses have been at least 10% of the aggregate wages paid by the bidder or subcontractor or (2) the responsible bidder is a certified minority business enterprise (MBE). **The bill takes effect July 1, 2019.**

Fiscal Summary

State Effect: Procurement expenditures (all funds) likely increase by more than 4% on affected contracts, which may total tens of millions of dollars. State agencies can implement the bill with existing resources. No material effect on revenues from penalty provisions.

Local Effect: Local government finances and operations are not materially affected.

Small Business Effect: Meaningful.

Analysis

Bill Summary:

Health Care Expenses Defined

The Board of Public Works (BPW) must adopt regulations that require each State agency to establish the percentage price preference of at least 4%.

“Employee health care expenses” are any costs for health care services, as defined by the bill, paid by a responsible bidder or subcontractor to an employee, including:

- contributions made on behalf of an employee to a health savings account, as defined under the federal Internal Revenue Code, or any other similar account;
- reimbursements to an employee for health care expenses;
- payments to a third party to provide health care services to an employee;
- payments under a collective bargaining agreement to provide health care services to an employee; and
- costs incurred in the direct delivery of health care services to an employee.

Certification Requirements

If the price preference is provided on the basis of health care payments by the employer, the certification provided by a responsible bidder or subcontractor must indicate that aggregate employee health care expenses paid by the employer were at least 10% of aggregate Social Security wages paid during (1) the 12-month period immediately before the submission of the bid or (2) if the bidder or subcontractor did not have any employees in the State during that entire time, for the period of time between 3 months and 12 months immediately before submission of the bid in which the bidder or subcontractor had an employee in the State. A procurement officer may require a bidder or subcontractor to provide documentation in support of its certification. The Department of General Services and the Department of Labor, Licensing, and Regulation must collaborate on the development of a certification form.

The price preference may not be applied on the basis of health care payments by an employer if a bidder or subcontractor (1) fails to submit the records requested by a procurement officer or (2) has not employed an individual in the State for at least three months immediately prior to the submission of the bid.

Enforcement

A bidder or subcontractor who is awarded a contract to which the price preference was applied on the basis of health care payments by the employer must continue to pay at least 10% of wages for health care expenses for at least one year after contract award. A procurement officer may request documentation of continued compliance.

If a contract awardee fails to provide the required documentation in a reasonable period of time, the procurement officer may void the contract. An awardee who otherwise fails to comply with the bill’s requirements must pay the agency that awarded the contract an amount equal to twice what the awardee would have paid for employee health expenses.

A person who provides false information under the bill is subject to a civil penalty of between \$2,500 and \$25,000 for each violation. An action for the civil penalty may be brought by the agency that awarded the contract, the Attorney General, or the State's Attorney.

Current Law/Background: For a complete description of the State's MBE program, please see the **Appendix 1 – Minority Business Enterprise Program**.

Competitive sealed bidding is one of several procurement methods authorized by statute. It is most often used for the procurement of commodities and construction. Historically, it has been the most common procurement method used by the State, in large measure because of a statutory preference for its use. However, that preference was repealed by Chapters 588 and 589 of 2017. Nevertheless, competitive sealed bidding is likely to remain a commonly used procurement method.

Under competitive sealed bidding, a contract is awarded to the responsible bidder who submits the responsive bid that (1) is the lowest bid price; (2) if the invitation for bids so provides, the lowest evaluated bid price; or (3) if the procurement generates revenue for the State, the bid that is most favorable to the State. A "responsible bidder" is defined as a person who has the capability in all respects to perform fully the requirements of the contract, and who possesses the integrity and reliability that will ensure good faith performance. A responsive bid is one that conforms in all material respects to the invitation for bids.

The State currently awards a price preference of no more than 5% for products that are mercury free or that contain the least amount of mercury (if the product may contain mercury). The State also requires schools and State facilities to give a price preference of no more than 5% for locally grown food. Finally, the Small Business Preference Program, which applies to a limited number of agencies and procurements, provides a 5% price preference for small businesses, a 7% price preference for veteran-owned small businesses, and an 8% price preference for disabled veteran-owned small businesses.

Mandated Study on Health Care Coverage

Chapter 468 of 2018 required BPW to collect the information listed below for all construction-related contracts awarded by competitive sealed bids in the three months following the enactment of the bill, and submit a report on its findings to specified committees of the General Assembly by November 1, 2018:

- whether the bidder and any subcontractor provide employee health care coverage on projects that require payment of prevailing wages;

- for the year preceding the bid, what the percentage of total Social Security wages was as well as the total amount spent on employee health care;
- the percentage of total health insurance coverage costs paid by an insurance company compared with the percentage paid by an employee;
- the type and scope of coverage as well as the average percentage of monthly premiums paid by the bidder or subcontractor; and
- the average percentage of monthly premium paid by the bidder's or subcontractor's employees and the average deductible in each health care plan offered.

The report included information from more than 300 contractors and subcontractors involved with 48 different procurements. It found that 75% of respondents provided employee health insurance coverage on prevailing wage projects. Coverage levels among those that provided health insurance varied tremendously, but most employers paid at least 50% of plan premiums, and most deductibles were at or below \$2,500.

State Expenditures: The bill authorizes the State to award contracts to a bidder whose bid is at least 4% higher than the lowest bid if the bidder meets either of the bill's two criteria. Thus, to the extent that bidders meet those criteria, State procurement expenditures (all funds) likely increase by at least 4% on affected contracts.

In addition, bidders that do not currently pay for their employees' health care expenses and elect to do so in order to remain competitive in State procurements likely pass along those costs to the State in the form of higher bids. A reliable estimate of the extent to which bids increase is not possible because the proportion of personnel costs varies by contract size and type, but they will clearly add to the contract costs paid by the State beyond the 4% paid for the price preference.

As an illustration of the potential fiscal effect of the bill, in fiscal 2017, the State paid MBEs \$1.3 billion under procurement contracts. Applying the minimum 4% price preference just to that amount results in an estimate of State procurement payments increasing by \$52.0 million, even before the price preference is applied on the basis of health care payments by employers. The effect is smaller to the extent that some of those MBE payments were for contracts awarded on the basis of procurement methods other than competitive sealed bidding (*e.g.*, competitive sealed proposals).

Small Business Effect: Small businesses are less likely than larger businesses to provide health insurance coverage to their employees, so non-MBEs will be at a distinct disadvantage in competing for State contracts. Although small businesses that elect to provide health insurance can pass those costs along to the State, they will only be reimbursed for the portion of time during which employees are doing work for the State. Moreover, they must demonstrate that they have provided insurance for at least a year

before a bid is submitted, so a decision to provide health insurance likely results in a large amount of uncompensated costs for small businesses.

Certified MBEs receive the price preference regardless of their expenditures for health care for their employees.

Additional Information

Prior Introductions: SB 492 of 2018, a similar bill as introduced, was amended to only require submission of the study by BPW discussed above. It passed both houses as amended and was signed by the Governor as Chapter 468. Its cross file, HB 776 of 2018, was also amended to require a study by BPW. It passed the House and was assigned to the Senate Rules Committee, but no further action was taken.

Cross File: HB 680 (Delegate Cullison, *et al.*) - Health and Government Operations.

Information Source(s): State Board of Contract Appeals; Judiciary (Administrative Office of the Courts); Maryland State's Attorneys' Association; Department of General Services; Department of Labor, Licensing, and Regulation; Board of Public Works; Department of Legislative Services

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sb/ljm

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Appendix 1 – 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 (GOMA), 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, GOMA 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 2019. GOMA issued subgoal guidelines in July 2011, summarized in **Exhibit 1**, which are also still in effect. 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 MBE Participation

	<u>Construction</u>	<u>Architectural/ Engineering</u>	<u>Maintenance</u>	<u>Information Technology</u>	<u>Services</u>	<u>Supplies/ Equipment</u>
African						
American	7%	6%	8%	7%	7%	6%
Hispanic	-	2%	3%	2%	-	-
Asian	4%	-	3%	-	4%	5%
Women	-	9%	-	8%	12%	10%
Total	11%	17%	14%	17%	23%	21%
Total +2	13%	19%	16%	19%	25%	23%

MBE: Minority Business Enterprise

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 2017, the most recent year for which data is available.

Exhibit 2
Minority Business Enterprise Participation Rates, by Agency
Fiscal 2017

<u>Cabinet Agency</u>	<u>% Participation</u>
Aging	0.4%
Agriculture	7.6%
Budget and Management	6.0%
Commerce	3.1%
Education	23.0%
Environment	57.4%
Executive Department	4.6%
General Services	19.5%
Health	11.5%
Higher Education Commission	16.1%
Housing and Community Development	32.0%
Human Services	8.3%
Information Technology	4.1%
Juvenile Services	7.1%
Labor, Licensing, and Regulation	13.1%
Military	30.2%
Natural Resources	3.9%
Planning	7.5%
State Police	11.9%
Public Safety and Correctional Services	53.9%
Transportation – Aviation Administration	23.1%
Transportation – Motor Vehicle Administration	11.3%
Transportation – Office of the Secretary	27.9%
Transportation – Port Administration	24.9%
Transportation – State Highway Administration	21.2%
Transportation – Transit Administration	16.5%
Transportation – Transportation Authority	22.2%
Statewide Total¹	21.0%

¹Includes 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 2019 is \$1,749,347.