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**HOUSE OF REPRESENTATIVES
AS REVISED BY THE COMMITTEE ON
GENERAL GOVERNMENT APPROPRIATIONS
ANALYSIS**

BILL #: HB 1323
RELATING TO: Fla. Minority Business Loan Program
SPONSOR(S): Representative(s) Kallinger, Holloway and others
TIED BILL(S):

ORIGINATING COMMITTEE(S)/COUNCIL(S)/COMMITTEE(S) OF REFERENCE:

- (1) STATE ADMINISTRATION YEAS 3 NAYS 0
 - (2) GENERAL GOVERNMENT APPROPRIATIONS YEAS 12 NAYS 0
 - (3) COUNCIL FOR SMARTER GOVERNMENT
 - (4)
 - (5)
-

I. SUMMARY:

Current law provides for certification of Minority Business Enterprises (MBE) to participate in bidding on contracts of state agencies for goods and services. The Department of Management Services reports that there are no programs that provide assistance to MBEs to obtain working capital financing so that these vendors can purchase the materials or hire the personnel necessary to complete a contract. This bill creates the Florida Minority Business Loan Mobilization Program to provide a mechanism to advance a portion of the base contract award amount to a MBE vendor to be used as collateral in obtaining working capital financing.

Fiscal Impact: The bill does not appear to have a fiscal impact on the state government, as the monies to be advanced in this program are part of the base contract amount awarded to the vendor. Section 215.422(14), F.S., authorizes the Comptroller to adopt rules to authorize advance payments for goods and services. Such rules are to provide objective criteria for determining when it is in the best interest of the state to make payments in advance and must also provide adequate protection to ensure that such goods or services will be provided.

The bill may conflict with certain other provisions of law relating to procurement of personal property and services. Chapter 287.057(14), F.S., requires services to be rendered in accordance to contract terms prior to invoice payment. Please see section V., "Comments" of this analysis.

The bill takes effect October 1, 2002.

On February 21, 2002, the Committee on State Administration adopted a strike-all amendment that makes editorial changes so that MBE vendors and elements of the program are referred to consistently in the bill and provides a specific grant of rulemaking authority to the Department of Management Services to approve lending institutions participating in the program. The amendment is traveling with the bill.

On February 27, 2002, the Committee on General Government Appropriations adopted a substitute amendment to the strike-all amendment. (See section VI on this analysis for an explanation.) This substitute amendment is traveling with the bill.

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II. SUBSTANTIVE ANALYSIS:

A. DOES THE BILL SUPPORT THE FOLLOWING PRINCIPLES:

- | | | | |
|-----------------------------------|---|--|---|
| 1. <u>Less Government</u> | Yes <input type="checkbox"/> | No <input checked="" type="checkbox"/> | N/A <input type="checkbox"/> |
| 2. <u>Lower Taxes</u> | Yes <input type="checkbox"/> | No <input type="checkbox"/> | N/A <input checked="" type="checkbox"/> |
| 3. <u>Individual Freedom</u> | Yes <input checked="" type="checkbox"/> | No <input type="checkbox"/> | N/A <input type="checkbox"/> |
| 4. <u>Personal Responsibility</u> | Yes <input type="checkbox"/> | No <input checked="" type="checkbox"/> | N/A <input type="checkbox"/> |
| 5. <u>Family Empowerment</u> | Yes <input type="checkbox"/> | No <input type="checkbox"/> | N/A <input checked="" type="checkbox"/> |

1. This bill creates an optional activity within the state procurement process to advance payment to minority business enterprise vendors for collateral to back capital financing agreements.

4. The bill provides state government assistance to entities in order to secure a business loan.

B. PRESENT SITUATION:

Part IV, ch. 288, F.S., provides definitions, applicable to all government agencies in the state, concerning small and minority business enterprises in the state. These definitions are used in determining whether to certify a minority business enterprise as vendors for purposes of bidding on state contracts for goods and services. This certification process is found in s. 287.0943, F.S. The Department of Management Services reports in its analysis of this bill that there is no mechanism available to assist MBEs towards obtaining working capital financing towards fulfilling state contracts.

C. EFFECT OF PROPOSED CHANGES:

The bill creates s. 288.706, F.S., the Florida Loan Mobilization Program (Program), to assist minority business enterprises in competing for a state contract for goods and services by providing a mechanism to obtain working capital financing.

Legislative Intent

The stated intent is:

“to promote diversity in state contracting by eliminating barriers that prevent minority business enterprises from providing goods and services to the state. It is also the intent to encourage prime contractors to participate in agency contracts by providing a mechanism to minimize any risk to which the contractor might be exposed as a result of a reduction in the amount of allowable subcontract retainage¹ withheld by the prime contractor for vendors participating in the [Florida Loan Mobilization] program.”

Program Creation

¹ “Retainage is a common construction contracting practice whereby a certain percentage of compensation is withheld by the project owner from the general contractor and, in turn, by the general contractor from subcontractors until the project is completed satisfactorily. Retainage is also used as leverage to assure timely completion.” See OPPAGA Special Review, Inflexibility in Contracting and Retainage Practices Could Hurt Construction Industry, Report No. 00-26 (December 2000).

The Florida Loan Mobilization Program would assist minority business enterprises in fulfilling a state contract for goods and services. A minority business enterprise vendor may only apply to participate in the Program after it has been awarded a state agency contract. Minority Business Enterprises (MBE) are defined in s. 288.703(2), F.S., as:

“any small business concern as defined in subsection (1) [a small business] which is organized to engage in commercial transactions, which is domiciled in Florida, and which is at least 51-percent-owned by minority persons who are members of an insular group that is of a particular racial, ethnic, or gender makeup or national origin, which has been subjected historically to disparate treatment due to identification in and with that group resulting in an under representation of commercial enterprises under the group's control, and whose management and daily operations are controlled by such persons. A minority business enterprise may primarily involve the practice of a profession. Ownership by a minority person does not include ownership which is the result of a transfer from a nonminority person to a minority person within a related immediate family group if the combined total net asset value of all members of such family group exceeds \$1 million. For purposes of this subsection, the term “related immediate family group” means one or more children under 16 years of age and a parent of such children or the spouse of such parent residing in the same house or living unit.”

Program Operation

The Program provides that the contracting state agency can disburse a portion of the base contract award amount to a MBE vendor (prime or subcontract) to be used as collateral towards obtaining working capital financing. This designated loan mobilization payment would be made by the agency directly to the lending institution on behalf of the vendor and would be pledged as collateral by the vendor. Upon disbursement, the agency would retain no interest the designated loan mobilization payment.

Alternatively, the contracting agency could advance directly a portion of the contract amount to a MBE vendor for use as a retainer to fund the basic service portion of a contract.

Advance payment of retainer for basic services portion of a contract.

A contacting agency that has awarded a contract to a MBE vendor for construction, professional services, or the provision of goods and services is authorized to advance up to 10 percent of the base contract award amount to that vendor as a retainer to fund the basic services portion of a contract. The basic services portion of a contract is that portion which goes towards preliminary work that underlies the project, for example, surveying a site, preparing working agreements, and design activities.

The contracting agency may advance to a MBE vendor providing professional services up to 5 percent of the base contract amount as a direct retainer. Alternatively, if the MBE vendor is a participant in the Program, the contracting agency may advance up to 10 percent of the base contract award amount as a direct retainer. The bill does not provide any limitation on the use of this retainer. Ideally, the vendor would be limited to obtaining the material and personnel necessary to fulfill the contract.

Disbursement of designated loan mobilization payment as collateral for working capital agreement.

The contacting agency may disburse to a MBE vendor a portion of the base contract award amount, termed the “designated loan mobilization payment” (DLMP), for use as collateral to obtain working capital financing.

Once a MBE vendor is awarded a contract, that vendor may apply to an participating lending institution to obtain working capital financing. The lending institution must be one approved by the Department of Management Services. However, as the bill is written, the department does not have the authority to

approve the lending institutions for participation in the program. The line of credit obtained under the working capital agreement is based on the amount in the DLMP and can be between 125 and 200 percent of that amount. The actual amount of the DLMP disbursed by the contracting agency can be between \$5,000 and \$250,000.

The DLMP is an amount between 5 and 10 percent of the base contract amount of the contract between the prime vendor and the contracting agency. The DLMP can be between 5 and 10 percent of the subcontract amount of a contract between a subcontract vendor and a prime contract vendor. The DLMP is to be disbursed by the contracting agency to the lending institution. Upon disbursement, the bill provides that the contracting agency no longer maintains an interest in the DLMP payment. Under both instances, it is needs to be made clear who the MBE vendor is in the relationship.

The bill provides for the timing of the release of the DLMP. A prime contractor may request the disbursement of the DLMP in the first application for payment, or for contractors on nonconstruction contracts, by letter delivered to the agency after award of the contract but before the commencement of the contract. In both cases, the request must be accompanied by the working capital agreement. In the case of construction contracts, the DLMP is released following the issuance of the notice to proceed (on the contract) and within 10 days of the agency's approval of the initial application for payment. For nonconstruction contracts, the release of the DLMP occurs 10 days after the agency's approval of the letter of request from the vendor. The bill provides authority to a contracting agency to include as an element of the contract that the release of the DLMP will start the time clock that determines timely completion of the contract.

MBEs that are a subcontractor or vendor to a prime contractor which has been awarded a state contract may participate in this program. The subcontractor must submit a letter to the contracting agency requesting the DLMP which indicates that the prime contractor has been notified of the request and that there is a valid working capital agreement with an approved lending institution. The bill provides a limitation on these working agreements but the limitation is not clearly written. The release of the DLMP appears predicated on the receipt by the lending institution of documentation indicating the subcontractor's contract amount or "other documentation acceptable to the agency evidencing the subcontract amount." The authority provided the agency in this sub-subparagraph does not describe to the agency the types of information or documentation that can be considered in determining the subcontractor's contract amount for determining the DLMP. Prime contractors can retain no more than 5 percent of the amount earned by the participating subcontractor.

Prime contractors are required to incorporate the Program into subcontract agreements or purchase orders when the subcontractors and vendors are participants in the Program.

Contracting agency rights and responsibilities.

The bill provides contracting agencies with additional responsibilities under the program. The contracting agency is directed to encourage prime contactors to make weekly or bi-weekly payments to participating subcontractors. It is not clear how this encouragement would apply to contractual timeliness requirements.

The contracting agency must "monitor compliance with and effectiveness of the procedures set forth in this section." This is interpreted to mean that the contacting agency must monitor contractor compliance with the program and determine the effectiveness of the program in ensuring MBE participation in state contracts.

The bill provides that the program does not supersede the contracting agency's right to "insist upon strict compliance with the requirements of the contract document."

The bill makes clear that the agency cannot be a party to any working capital agreements entered into by a participating MBE vendor and a lending institution. The bill reiterates that the contracting agency is

to disburse the DLMP to the lending institution. The lending institution is to notify the agency (although it is not clear that it is the contracting vendor that is to be notified) of the receipt of an application for a working capital agreement by a participating vendor.

The bill allows for other methods to disburse contract awards to MBE vendors when the MBE has agreed to an assignment of the contract proceeds in order to obtain a line of credit. The bill provides that participation in the Program (and it appears to be assumed) that the payment of a DLMP is exclusive to any other agreements that a participating MBE vendor might be party to.

Finally, the bill provides authority to the Department of Management Services to adopt rules to implement the "provisions of the section". This general grant of rulemaking authority should be tied to specific activities found in the bill, such as the approval of lending institutions to extend working capital financing where the collateral is a portion of the base contract award amount.

The bill takes effect October 1, 2002.

D. SECTION-BY-SECTION ANALYSIS:

Section 1. Creates s. 288.706, F.S., creating the Florida Minority Business Loan Mobilization Program. (1) Provides legislative findings and intent; (2) Creates the Florida Minority Business Loan Mobilization Program; (3) Authorizes state agencies to disburse payment as retainer; (4) Authorizes a direct retainer from the agency or participation in the Florida Minority Business Loan Program; (5) Provides application and award procedures, including disbursement of loan by state agencies to lending institutions; (6) Requires all prime contractors to incorporate the designated loan mobilization payment procedures in subcontract agreements or purchase orders with vendors participating in the program; (7) Requires agency to encourage prime contractors to make weekly or biweekly payment to participating subcontract vendors; (8) Requires agency to monitor compliance with and effectiveness of the procedures set forth in this section; (9) Prohibits the agency from being a party to the working capital agreement between the participating lending institution and the vendor; Requires agency to disburse the loan payment directly to the lending institution; (10) Provides that the loan program is exclusive to any line of credit or other credit facility based upon a prime contract or subcontract for an agency project; and (11) Authorizes the Department of Management Services to adopt rules to implement the provision of the section [288.706, F.S.].

Section 2. Provides an effective date of October 1, 2002.

III. FISCAL ANALYSIS & ECONOMIC IMPACT STATEMENT:

A. FISCAL IMPACT ON STATE GOVERNMENT:

1. Revenues:

None.

2. Expenditures:

None.

B. FISCAL IMPACT ON LOCAL GOVERNMENTS:

1. Revenues:

None.

2. Expenditures:

None.

C. DIRECT ECONOMIC IMPACT ON PRIVATE SECTOR:

Minority contractors will be able to obtain working capital using an advance from the contract awarded as collateral for a working capital agreement from a participating lending institution.

D. FISCAL COMMENTS:

There appears to be no fiscal impact on the state. The monies provided to a contractor are part of the total contract award. It is money already encumbered by the agency for the contract's purpose. The contracting agency would be required to provide a retainer directly to the vendor or to disburse a loan payment to an approved lending institution on behalf of the vendor. The agency would retain no interest in the designated loan payment.

Section 215.422(14), F.S., states "the Comptroller may adopt rules to authorize advance payments for goods and services, including, but not limited to, maintenance agreements and subscriptions. Such rules shall provide objective criteria for determining when it is in the best interest of the state to make payments in advance and shall also provide for adequate protection to ensure that such goods or services will be provided."

The bill providing payment of funds prior to delivery of contracted services. This conflicts with Chapter 287.057(14), F.S., which requires services to be rendered in accordance to contract terms prior to invoice payment. (See section V.C. Other Comments below).

The Department of Management Services may incur some insignificant costs in association with its responsibilities for the program.

IV. CONSEQUENCES OF ARTICLE VII, SECTION 18 OF THE FLORIDA CONSTITUTION:

A. APPLICABILITY OF THE MANDATES PROVISION:

The bill does not require counties or municipalities to spend funds or to take action requiring the expenditure of funds.

B. REDUCTION OF REVENUE RAISING AUTHORITY:

The bill does not reduce the authority that counties or municipalities have to raise revenues in the aggregate.

C. REDUCTION OF STATE TAX SHARED WITH COUNTIES AND MUNICIPALITIES:

The bill does not reduce the percentage of a state tax shared with counties or municipalities.

V. COMMENTS:

A. CONSTITUTIONAL ISSUES:

This bill does not appear to create a "set-aside" program for minority businesses, although it does treat minority business vendors differently than non-minority business vendors. The United States Supreme Court has addressed this issue extensively and recent case law indicates that it has become skeptical of government programs that make use of race-based classifications. See *City of Richmond v. J.A. Croson Co.*, 488U.S. 469 (1989) (city program which set aside a percentage of construction projects for minority

contractors must be subjected to strict scrutiny) and *Adarand Constructors, Inc. v. Pena*, 515 U.S. 200 (1995) (federal set-aside programs for minority contractors would be subjected to strict scrutiny).

B. RULE-MAKING AUTHORITY:

The department is authorized to adopt rules but needs specific authority to approve participating lending institutions and to promulgate the list of those approved lenders. This general grant of rulemaking authority should be tied to specific activities found in the bill, such as the approval of lending institutions to extend working capital financing when the collateral is a portion of the base contract award amount. The strike-everything amendment adopted by the Committee on State Administration provides specific rulemaking authority to the department to adopt rules to approve lending institutions for participation in the Program.

C. OTHER COMMENTS:

The bill appears to conflict with certain provisions of chapter 287, F.S., relating to procurement of personal property and services. The bill appears to conflict with sections that address contingent fee contracts for professional services. Section 287.057(14) F.S., provides that: “[t]he agency shall establish procedures to ensure that contractual services have been rendered in accordance with the contract terms prior to processing the invoice for payment.” The provisions of this bill appear to conflict with this requirement.

Black’s Law Dictionary (6th Ed.) defines collateral as “property which is pledged as security for the satisfaction of a debt.”

VI. AMENDMENTS OR COMMITTEE SUBSTITUTE CHANGES:

At its February 21, 2002, meeting, the Committee on State Administration adopted a strike-all amendment that makes editorial changes so that MBE vendors and elements of the program are referred to consistently in the bill. The amendment also provides specific rulemaking authority to the department to approve lending institutions for participation in the Program. The amendment is traveling with the bill.

On February 27, 2002, the Committee on General Government Appropriations adopted a substitute amendment to the strike-everything amendment adopted on by the Committee on State Administration. The substitute amendment makes editorial changes so that MBE vendors and elements of the program are referred to consistently in the bill. The substitute amendment includes language notwithstanding sections 215.422(14) and 216.181(16), F. S., to allow certain advanced payments for goods and services purchased by the State. It also provides that the vendor and the financial institution are cosignatories. In addition, the substitute amendment eliminates specific rulemaking authority to the department to approve lending institutions; rather, it requires the department to maintain a listing of financial institutions willing to participate in the program.

VII. SIGNATURES:

COMMITTEE ON STATE ADMINISTRATION:

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