ALASKA LEGISLATURE COMMITTEE FILES 1981-1982 8672

1516 SHESS SB 399 - SB 415

1516

CS SB 399

1) change current procedure for providing original birth certificate

2) keep section 2 of SB399

3) provide for the collection and distribution of medical information

age? → parents (~~child~~) → child adoptive

by:
1) H&SS
2) adoption agencies
3) lawyers
4) doctors

? definition section ?

Rocky 5-15-81

5/15/81

PROPOSED COMMITTEE SUBSTITUTE FOR SENATE BILL 399 - AN ACT RELATING TO ADOPTION

*Section 1. AS 20.15.060(a) is amended to read:

(a) The required consent to adoption shall be executed at any time after the birth of the child in the presence of the court or in the presence of a person authorized to take acknowledgements. The consent is not valid unless

(1) the consent form states that the person required to consent to adoption under AS 20.15.040 has the right to withdraw consent as provided in AS 20.15.070(b); and

(2) the person signing the consent is provided with a copy of the consent.

*Section 2. AS 18.50.220(b)(1) is amended to read:

(b) When a new certificate of birth is established, the actual place and date of birth shall be shown. The new certificate shall be substituted for the original certificate of birth, and

(1) thereafter, the original certificate and the evidence of adoption or legitimation are not subject to inspection except upon order of the superior court;[OR AS PROVIDED BY REGULATION] however, [THE] regulation shall allow inspection by an agent of the state or federal government acting in the performance of his official duties;

*Section 3. AS 18.50 is amended by adding new sections to read:

Sec. 18.50.500. RELEASE OF INFORMATION. On request to the state registrar a person adopted after January 1, 1982, and the adoptive parents of a person adopted after January 1, 1982, are entitled to the following information, if the information is available:

(1) general physical characteristics of the biological parents of the adoptive person in terms of height, weight, color of hair, eyes, and skin, and other information of a similar nature;

(2) the health history of the biological parents and of blood relatives of the biological parents provided on a standardized form prepared by the commissioner;

(3) the race of the biological parents.

Sec. 18.50.550. MAINTENANCE OF RECORDS. The commissioner, child adoption agencies, and all persons empowered by law or regulation to place minors for adoption shall assist the state registrar to maintain the information required under AS 18.50.500 for all adoptions which occur after January 1, 1982. If the information required under AS 18.50.500 is requested but is not available for adoptions that occurred before January 1, 1982, the state registrar shall request the commissioner to attempt to obtain the required information, to the extent that it is available, from child adoption agencies, records of the commissioner, court adoption records, or any other persons empowered by law or regulation to place minors for adoption.

Sec. 18.50.570. RECORDS. Child adoption agencies licensed under AS 47.35.100 and other persons empowered by law or regulation to place minors for adoption shall maintain records required under AS 18.50.550. and by the regulations of the commissioner. If a child adoption agency ceases to act as a child adoption agency, it shall transfer its records to the commissioner.

Sec. 18.50.600. DEFINITIONS. In AS 18.50.500 - 18.50.600

(1) "adoptive parent" means a parent who adopted a person ~~but who is not the biological parent of the person;~~

(2) "biological parent" means a birth parent who is named on the original certificate of birth of an adopted person;

(3) "child adoption agency" means a child adoption agency licensed under AS 47.35.100;

(4) "commissioner" means the commissioner of health and social services;

(5) "state registrar" means the state registrar appointed under AS 18.50.030.

*Section 4. This Act takes effect January 1, 1982.

Adoptive son may get help

Associated Press

Kansas City, Mo. — In a move that could save a Florida man's life, a mother who gave up her son for adoption years ago and a half sister have agreed to be tested anonymously to see if they could donate bone marrow to ease his cancer suffering.

James Grant George, a computer system consultant from Miami found out 11 months ago he is dying from a bone marrow cancer that could be fought with a transplant from his natural mother or half sister.

But efforts by the 33-year-old man to find out the identities of the mother and half-sister were stymied because adoption records are secret. He was given up for adoption here as an infant.

Finally, a lawyer representing the relatives agreed Wednesday to anonymous testing for compatible bone marrow. George could find out if his bone marrow matches that of his relatives without learning who they are or where they live. The agreement was reached after a four-hour Jackson County Court hearing to open his adoption records.

SB
414

BACKGROUND PAPER

SENATE BILL 414 AND SURETY BONDING OPTIONS

by Ira Winograd
March 1, 1982

Senate Bill 414, an Act Establishing a State Operated Small Contractor Surety Bonding Corporation

The rationale for S.B. 414 is contained in the Legislative finding that many competent small contractors, whether minority or otherwise, experience difficulty or are totally unable to obtain at a reasonable cost the surety bonds necessary to bid on both public and private construction projects.[1] This finding contains a minor factual error and it rests on an undefined concept of 'competency'. The error occurs in the implication that bonds are necessary to bid on private construction projects. Private obligees, parties requesting bids, may request bonding but they often forego bonding, especially on smaller projects. They are less likely than public obligees to solicit bids from unfamiliar contractors and they are not bound to accept the lowest bid. The private sector has less need for the prequalification services provided by sureties and surety bonding. On occasion, even a large private sector obligee will forego surety bonding. For example, the TAPS oil pipeline obligees did not require surety bonding. Surety bonds are primarily a requirement of public sector obligees. S.B. 414 would not necessarily improve the prospects of emerging contractors competing for private sector projects.

SB 414 is designed to assist contractors who are denied bonds for reasons other than lack of competence. Testimony presented to the State Affairs Committee in support of S.B. 414 asserts that many competent contractors cannot obtain bonds.[2] The surety industry denies this assertion. This difference of opinion might be explained, at least in part, by the working definition of 'competency' used by sureties.

The low bid method of choosing contractors demands a very stringent definition of competency. A surety bond is a guarantee to the obligee that the contractor is competent to perform according to contract specifications. A surety bond is not issued as an insurance policy to be drawn upon in the event of incompetency. The obligee wants to be certain that all bonded contractors, especially the low bidder, will perform according to contract. From the obligees perspective, execution of the contract is more desirable than collecting financial compensation for failure to perform. The insurance aspect of surety bonding is only used as a last resort. It is used so infrequently that surety rates are not high enough to generate a loss paying insurance fund.

Under normal market conditions, sureties provide bonds only when they conclude that there is a very minimal chance that their own assets will be called upon as a result of a combination of two factors: contractor incompetency and insufficient 'net quick'. If there is the slightest doubt about competency, the contractor must demonstrate a satisfactory cash position, 'net quick'. Net quick cash is a sureties term for the ratio of net working capital to the current and expected work load of the contractor. Net working capital is the value of current assets less liabilities. Traditionally, sureties have looked for a net quick ratio of at least 10% of the total work load on bid upon work.[3]

An emerging contractor has to show an unusally strong balance sheet in order to obtain a surety bond. The sureter wants to be certain that,

in the event of breach of contract, the contractor has adequate assets to cover liability. The sureter demands competency in ability to perform and ability to provide financial compensation for nonperformance. The working definition of competency within the surety industry is far more stringent than the common definition of competency.

Senate Bill 414 is proposed as a means of providing bonds to competent contractors who have been denied bonding. It is not evident from the hearings held before the Senate State Affairs Committee that sureties are denying bonds to contractors on the basis of criteria which are irrelevant to their definition of competency. Federal experience with the Surety Bond Guarantee Program of the Small Business Administration indicates that recipients of public sector financed bonds tend to be less competent than recipients of private sector bonds. Insurance reports filed with the State of Alaska show a surety loss to premium ratio of 32.3% between 1975 and 1978.[4] Premiums average about 1% of the bond amount, so the loss to bond amount was approximately .32%.[5] Over the life of the S.B.A. Surety Bonding program in the Pacific Northwest, the average loss has been 1.25% of the bond and current losses are 1.37%.[6] This rough comparison shows that the S.B.A. bonding program produces losses at a rate which is four times greater than that incurred by the private sector surety market. The Federal experience indicates that S.B. 414 might increase bonding of fully competent contractors although it would tend to increase bonding of less competent contractors. Some competent contractors might benefit from S.B. 414, while the majority of competent contractors might be harmed by increased competition from less competent competitors.

The Administration of the S.B.A. evaluated their own Surety Bond Guarantee Program and concluded that it results in a net savings to government.[7] Net savings is defined as the difference between obligee accepted low bids presented by S.B.A. bonded contractors and the next highest bid, less program expenses and losses. For every one million dollars in S.B.A. backed bonds accepted by public sectorobligees the government saves $23,000. The S.B.A. estimates that the average difference between S.B.A. backed low bids which are accepted by government agencies and the next highest bid is almost 10% of the low bid.

The income statement of the Surety Bond Guarantee program shows a net loss.[8] Since the 1971 inception of the National program losses plus expenses exceed income by 455%. Using the conservative estimate that 1.25% of each S.B.A. backed bond in Alaska is defaulted, then losses (excluding operating expenses) exceed income by between 200% and 235%.[9]

Due to the similarities of S.B. 414 and the S.B.A. Surety Guarantee Program it is reasonable to expect that S.B. 414 would require a government subsidy. A subsidized Surety Guarantee Program might produce an overall government savings and it might aid some emerging contractors. It would also tend to lower competency standards. In order to evaluate the desirability of S.B. 414, it should be compared to other programs designed to alleviate problems facing emerging contractors. The remainder of this paper reviews the range of problems

which may be encountered by emerging contractors and specific programs designed to alleviate them.

Problems for Emerging Contractors

Small contractors have trouble obtaining bonds, but a wide variety of reasons can contribute to denials. An overriding problem results from the required qualification aspect of surety bonding. In addition, surety bonds might be denied because a contractor is not fully competent, is being discriminated against, or is hindered by market distortions. A detailed discussion of S.B. 414 is contained under the subheading of Competency problems.

Required Qualification

In Alaska, a contractor is not qualified to submit a bid above $50,000, to a State Government obligee, unless a surety bond is obtained.[10] A surety bond is a required qualification and there is no alternative way to provide the necessary pre-bid qualification. The surety has life and death control over contractors seeking State contracts. There are two classes of remedies to alleviate the importance of required qualification via surety bonding: 1) raise the contract size below which no bonding is required, 2) create an optional bonding category.

The $50,000 upper limit for non-bonded contractors was established in 1976. Since establishment of this limit the Anchorage consumer price index has increased 51%.[11] The current $50,000 limit can be raised 50% to $75,000, and the original real dollar value of the original exemption would be maintained. If the 1976 limit were raised by 1/3 in real dollars, the current limit would be $100,000 in todays dollars.

It appears that a $100,000 limit may meet the average bond requests of emerging contractors. The average contract size of S.B.A. guaranteed contracts is between $90,000 and $100,000.[12] Furthermore, a $100,000 limit is not apt to cause extensive State liabilities. This limit is low enough to limit State liability on any one project and it is reasonable to assume that public agencies would be very cautious before hiring a non-bonded emerging contractor who had failed on previous contracts.

An optional bonding category could provide another alternative to existing surety requirements. Within a fixed dollar category, non-bonded contractors might be allowed to compete with bonded contractors. In order to avoid penalizing bonded contractors and to preserve an incentive to obtain bonding, non-bonded contractors could receive a penalty equal to a fixed percentage of their bid. For example, if a bonded and a non-bonded contractor submit identical bids, the bonded contractor would receive the contract because the non-bonded contractor would have his bid raised by a penalty, equal to x%, for the purpose of bid evaluation. Although a non-bonded contractor would be at a severe disadvantage over the long-run, an optional bonding category provides an opportunity for an emerging contractor to demonstrate competancy so that

bonding might be obtained in the future.

The category might extend from the upper limit of the 'no bond' category to an amount which is high enough to allow an emerging contractor to demonstrate competency on mid-sized projects. The upper limit could be set low enough for the State to avoid excessive liabilities. The upper limit might be set equal to the new limit for the S.B.A. surety bonding program, $250,000, or the traditional S.B.A. limit of $1,000,000.

The penalty might relate to the provisions of SB 415 which provide that minorities and women shall be awarded contracts if, "the bid is not more than 15% higher than the bid of the lowest bidder; and the bidder agrees to lower his bid by 5%"[13] The following chart illustrates the effect of various penalties in conjunction with the provisions of SB 415, and without SB 415. Each contractor is assumed to submit an identical $1 bid, and figures are rounded for ease of comparison.

S.B. 415, 15% Advantage to Minorities and Women

Penalty	non-bonded Non-minority	non-bonded Minority	bonded Non-minority	bonded Minority
5%	1.05	.90	1.00	.85
10%	1.10	.95	1.00	.85
15%	1.15	1.00	1.00	.85
20%	1.20	1.05	1.00	.85
Without SB 415				
5%	1.05	1.05	1.00	1.00
10%	1.10	1.10	1.00	1.00
15%	1.15	1.15	1.00	1.00
20%	1.20	1.20	1.00	1.00

If SB 415 is in effect, any penalty below 15% would give an advantage to a non-bonded minority compared to a bonded non-minority. Any penalty above 15% would give an advantage to a bonded non-minority over a non-bonded minority. In both cases, the maximum advantage accrues to bonded minorities or women. This arrangement provides maximum growth incentive for bonded minority/woman contractors. Additional minority members could be employed by expanding minority firms and additional minority members might thereby obtain the necessary experience for successful development of new minority firms.

If S.B. 415 is not passed, all non-bonded contractors would be treated equally. As the penalty increases they become less competitive with bonded contractors.

Competency

A non-profit surety could bond contractors who do not meet general surety competency standards. The non-profit S.B.A. Surety Guarantee program has approved 94.7% of all applications received since inception of the program in 1971. In December 1981, the S.B.A. approved 88.7% of all applications and in fiscal year 1981 the S.B.A. approved 93% of all applications in the Pacific Northwest.[14] The high approval rate, and high loss ratio, which is four times greater than the private sector, indicate that the S.B.A. program has liberal competency standards.

The rate structure of the S.B.A. Program encourages relatively higher competency standards to obtain bonds over $250,000 than for bonds under $250,000. The S.B.A. program operates in conjunction with private specialty sureties. Most sureties are general sureties who do not participate in the S.B.A. program.[15] The S.B.A. retains 10% of the premium (20% on bonds over $250,000), and the specialty surety retains 90% of the premium (80% for bonds over $250,000). In return, the S.B.A assumes 80% of the risk of default (90% if the bond is less than $250,000) and the speciaty sureter assumes 20% of the risk of default (10% if the bond is less than $250,000). Specialty sureters have less incentive to underwrite bonds over $250,000 and this could explain why some contractors have had trouble obtaining bonds over $250,000. (The S.B.A. has issued notification that a $250,000 upper limit shall be in effect on individual bonds as of January 18, 1982.)

S.B. 414 would transfer 100% of the risk and premium to a State Small Contractor Surety Bonding Corporation. The Corporation could underwrite bonds without being constrained to match private sector competency standards. The benefit of increased bond availability to the emerging contractor should be weighed against net direct losses to the program, operations cost, indirect cost of contract failures, and any harm which might accrue to bonded contractors.

Net direct losses are dependent on the contract failure rate and the premium collected. If the State maintains a premium structure and competency standards similar to S.B.A. standards it would incur a loss to premium ratio of 75% to 100% on bonds between $250,000 and $1,000,000.[16] This estimate assumes a conservative loss rate of 1.25% of guaranteed bonds. This same 1.25% default rate would yield a loss to premium ratio of 200% to 235% for the S.B.A. Surety Guarantee Program because 80% to 90% of the premium is transferred to specialty sureties and 80% to 90% of losses are absorbed by the S.B.A. The State program would not share losses and premiums with private sureties. If the State decreased rates below S.B.A. rates, to match private sector surety rates, the loss to premium ratio would increase.[17]

S.B. 414 operations costs are apt to exceed S.B.A. costs. In return for giving a large percentage of premiums, 80% to 90%, to specialty sureties the S.B.A. program relies on the specialty sureties to perform administrative tasks associated with the program including preparation of application forms. The S.B.A. Surety Bond Guarantee Program requires

only 16 people to issue 1.5 billion dollars worth of surety bonds per year.[18] The S.B.A. administrative overhead is only 20% of income or .1% of guaranteed bonds.[19] Private sector surety expenses average about 55% of earnings.[20] If a 55% operations cost is assumed for a State Surety Guarantee Program, and added to net direct losses, of 75% to 100%, the combined expected cost is between 130% and 155% of premiums.[21] This analysis indicates that a State operated Surety Guarantee Program would incur a net loss.

The net annual loss could be between $50,000 and $150,000, assuming that the State Contractor Surety Bonding Corporation underwrites the same value of bonds, at the same rate structure, as the S.B.A. currently underwrites in Alaska. This estimate assumes that the State would incur a loss rate of 1.25%. The 1981 S.B.A. loss ratio was 1.34% of the total bonded amount in Alaska. In fiscal year 1981 the S.B.A. sponsored 145 active bonds in Alaska for $20,224,281. Since the S.B.A. absorbs between 80% and 90% of loss, the total loss on these bonds was between $301,117 and $338,757, [.0134($20,224,281)/.8=$338,757, .0134(20,$224,281)/.9=$301,117.]. A maximum premium of $260,582 is derived by assuming a low loss/premium ratio of 130% applied to the maximum total loss ($338,757/1.3=$260,582), and a minimum premium of $194,269 is derived by assuming a high loss/premium ratio of 155% applied to the minimum total loss ($301,117/1.55=$194,269). The minimum net loss of $40,535 is derived by subtracting the maximum premium from the minimum total loss ($301,117-260,582=$40,535) and the maximum net loss of $144,488 is derived by subtracting the minimum premium from the maximum total loss ($338,757-194,269=$144,488.) These costs might underestimate actual costs because they assume that all costs are variable, when in fact, surety bonding might require large fixed costs in relation to the size of the Alaska emerging contractor surety market. Fixed costs are the minimum costs needed to initiate and operate the program. Losses would increase in proportion to the total value of issued bonds.

The remaining factors to be considered are too subjective to be evaluated in dollar amounts. These factors include benefits to emerging contractors in need of an opportunity to demonstrate competency, indirect costs of contract failures which are borne by the obligee, and any harm which might accrue to bonded contractors who might be forced to compete with less qualified contractors. In addition, an excessively lenient system could harm the viability of the low bid system of contractor evaluation. These factors have a direct bearing on an evaluation of public surety bonding but they do not lend themselves to monetary evaluation.

Only one State has passed legislation to provide surety bonding. The State of Connecticut has passed legislation enabling the Commissioner of Economic Development to issue surety bonds.[22] Regulations have not been promulgated at this time. There is a great deal of concern about establishing regulations to prevent large contractors from establishing subsidiaries to take advantage of the program. The proposed regulations establish a $25,000 limit and this gives the program an extremely limited scope.

An alternative approach to the problem of stringent competency standards is to raise the competency of emerging contractors. Competancy is in large part determined by a review of past performance. Programs which provide experience for emerging contractors allow them to improve their competency. S.B. 415, which provides an advantage to minority and woman contractors, would tend to improve the competency of these contractors. A raise in the rate below which bonding is not required, and creation of an optional bonding category, would also tend to provide work experience and increase the competency of small contractors.

Discrimination

The State might provide an alternative bonding system, as proposed by SB 414, which would offer an alternative for competent contractors who were denied contracts because of private sector discrimination. The State could avoid excessive losses by maintaining competency standards comparable to private sector standards. An alternative public system might be justified if there is discrimination in the private sector and legal remedies are inappropriate.

Discrimination is difficult to prove in the current surety market. A surety is not required to inform the contractor of the reasons for denial. Legislation might be passed requiring, as a condition of doing business with contractors operating in Alaska, that each sureter furnish, in writing upon request by a bond applicant, a detailed statement of the reasons which led the surety to refuse bonding to the applicant on a particular contract. Any statutes and regulations governing this requirement should be sufficiently flexible so as to avoid the danger that sureties will develop the practice of responding to bond applicants with a set of routine, meaningless formulations of the reasons for refusal.

Provision might be made to protect sureties from lawsuits arising out of a candid statement of the underwriting decision. Alternative legislation might require rejection reasons to be filed with the Department of Commerce and Economic Development, Division of Insurance. Sureties are already required to file financial statements with the Division. This option would be less burdensome to sureties than public disclosure requirements and it would still provide anti-discrimination benefits.

If one must give reasons for a decision, it is a discipline of the decision making process itself. This will tend to remove subjective predujices from underwriting. The simple process of having to explain forestalls too much subjectivity by well meaning people. An additional benefit of written reasons is that the emerging contractor can gain a better understanding of bond requirements.

A surety under this proposal could decide on one ground, and give entirely different written reasons. However, this kind of dishonesty is even more difficult to police in the absence of written reasons. In

their presence patterns emerge and can be monitored. A particular pattern with respect to particular sureties and contractors should arise, and this information could prove useful in determining if discrimination has occurred. A consistent pattern of written reasons might provide investigative evidence of suspected discrimination.

The surety business is almost exclusively conducted by insurance companies operating through specialized independent surety agents. These agents are located in centralized market areas. There are a limited number of active agents in Alaska and most Alaskan business is underwritten by Seattle sureties. An Alaska disclosure requirement would have to be constructed in conformance with the Federal Interstate Commerce Clause so as to avoid an illegal restraint of trade.

Market Distortions

An emerging contractor can be hindered by a shortage of bonds created by inadequate competition among sureties. In monopolistic, or limited competition markets, the supplier can reduce output, in this case bonds, while maintaining profit by charging more per bond. However, bond rates are based on the Rating Manual of the Surety Association of America, and there is little room for sureties to manipulate rates. Inadequate competition might be manifested in a tendency to only accept overqualified contractors and this might produce excessive profits.

Prior to enactment of the S.B.A. Surety Guarantee Program, the Department of Housing and Urban Development commissioned a study of surety bond adequacy and availability which included an analysis of surety profitability.[23] The study reviewed the period between 1958 and 1967, and concluded that, "Ownership of the surety enterprise, overall, received probably a 10-15% return on ownership equity for acting as construction bond sureties during the ten year period."[24] It is possible that the Alaska experience is quite different. The Legislature might conduct a study, or direct the Department of Commerce and Economic Development, Division of Insurance, to study the return on ownership within the surety industry. The study could indicate the degree of competitiveness among sureties involved in Alaska and the kinds of data which might be monitored for an ongoing evaluation of surety bonding.

An emerging contractor might also be hindered by a market structure which is fully competitive but which is not scaled to the needs of small contractors. It is possible that emerging contractors are hindered because the size of available contracts is too large for their capacity. The Department of Transportation and Public Facilities does not maintain a record of contracts by size classification. However, this data could be tabulated, and if the percentage devoted to small contracts appears to be too small, larger contracts might be broken down into smaller contracts. Successful completion of a number of smaller contracts would also help emerging contractors to establish the kind of track record for successful performance that could ultimately enable them to obtain bonds on successively larger projects.

The factoring of larger projects runs counter to the desire for greater efficiency by letting contracts in large aggregate amounts. This should be balanced against the benefit to emerging contractors.

Summary

The following chart summarizes four problem areas facing emerging contractors and programs designed to alleviate these problems.*

Problem	Program	Precedent	Expense
Required Qualification	No-bonding category	AS 36.25.010.	moderate
	Optional bonding.	none.	moderate
Competency	S.B. 414.	S.B.A.	maximum
	No-bonding category.	AS 36.25.010.	moderate
	Optional bonding.	none.	moderate
	S.B. 415.	State bidder preference, AS 37.05.230.	maximum
Discrimination	S.B. 414.	S.B.A.	maximum
	Reporting requirements.	none.	minimum
Market Distortions	Market study.	H.U.D.	minimum
	Factoring of larger projects.	none.	moderate

* There is overlap between problem areas which is not shown in the chart.

The expense estimates are divided into three general categories: maximum, moderate and minimum. The maximum category contains programs which require operating costs or for which costs are not limited to contracts having a specified monetary size. The moderate cost programs are limited to contracts having a specified monetary size. The minimum category applies to programs which do not require continuing government subsidies.

In all problem areas facing the emerging contractor, except one, there is a moderate or minimum cost alternative. The one exception is the problem of stringent competency requirements. The only viable short-run solution is a lowering of qualifications and this would require a State financed surety bond guarantee program. The competency problem can be avoided, within selected contract classifications, by enacting programs to alleviate the required qualification burden of surety bonding. From the obligee's point of view, stringent competency standards are not a problem. Stringent competency standards are the key to the surety

system that enables the owner to have confidence that the lowest bidder can successfully perform on contract on time.

FOOTNOTES

1. (SB 414, Section 1, Legislative Findings, [1]).
2. (State Affairs Committee, April 16, 1981)
3. ("Construction Surety Bonds: Their Adequacy and Availability, by David Dykhouse, p.58.)
4. (Insurance Reports for 1977-1979, issued by the Department of Commerce and Economic Development, Division of Insurance)
5. (Availability of Contract Bonding, Anne DeVries, House Research Agency, p.12.)
6. (Ibid. A. DeVries, p.15, and telephone conversation with Tom Sault, Director of S.B.A. Regional Office, Seattle)
7. (See appendix A)
8. (Ibid, Appendix A)
9. (Op. cit. A. DeVries, Table 3.)
10. (AS 36.25.010.)
11. (Wage & Clerical C.P.I. increased from 164.9 in July 1976 to 249.3 in Nov. 1981.)
12. (Op. Cit. Appendix A., Average size in Dec. 1981 is $91,8[illegible]0, National S.B.A. average).
13. (Sec 10. 37.05.230.iii,iv as proposed by SB 415)
14. (Op. Cit. A. DeVries, p.16.)
15. (Op. Cit. Appendix A and conversation with Tom Sault, Region X Director of S.B.A. Surety Guarantee Program)
16. (see Appendix B table 3 DeVries, S.B.A. premium schedule is 1.5% of first $250,000 or less, (until recently, 1% on amounts over $250,000 up to $1 million), plus a .2% service fee on the entire bond.)
17. (Standard surety premiums equal 1.2% for the first $500,000 and .725% on the next $2,000,000 in bonds.
18. (conversation with H. Huegel, Chief, Surety Bond Guarantee Branch, S.B.A.)
19. (Appendix A.)
20. (Op. Cit. Dykhouse, p. 74.)
21. (Operations cost could equal more than 55% of SB 414 premiums because State premium rates could be less than private surety rates.)
22. (Connecticut Public Act 79-611)
23. (Op. Cit, Dykhouse)
24. (Op. Cit Dykhouse p. 77.).

AGENCY-WIDE SURETY BOND GUARANTEE PROGRAM STATISTICS
Inception (January 1971) through December 1981

	December 1981	1/71 - 1/1/82
Net Profit/Savings to Government (Federal, State, Local)		
Public Sector Savings due to SBG Contracts (see attached Analysis*)		382,667,040
Net SBG Program Loss to Date		136,888,443
Net Profit/Savings to Government to Date		245,778,597
Surety Bond Guaranty Activity		
Applications for Guarantee Received	2,224	288,360
Applications Approved	1,973	273,016
Actual Contracts Awarded (low bids, etc.)	725	141,088
Contract Totals (actually obtained)	$66,591,586	$10,689,770,335
Average Contract Size	$91,850	$75,764
Number of Contractors Assisted	169	24,672
Minority Contractors Assisted	25	3,492
Defaults Recorded	77	8,225
Percentage of Defaults	6.9	5.8
Income		
Application Fees		$2,097,552
Contractor Fees		$21,695,464
Surety Premiums/Fees		$25,467,354
		$49,260,370
Expenses		
Administrative (SBA Overhead)		$3,832,491
Interest to Treasury		$5,791,248
		$9,623,739
SBG Claims Losses		
Claims Incurred		$238,869,586
Recoveries, Refunds, etc.		$24,181,440
Net Claims Incurred		$214,688,146
Bulk Reserve (Established by P.F.M.)		$38,163,072
Net Claims Paid		$176,525,074
Expenses (SBA Administrative Overhead)		$9,623,739
Total Loss and Expenses		$186,148,813
Less Income (Premiums, Fees)		$49,260,370
Net SBG Program Loss - Paid Claims To Date		$136,888,443

ATTACHMENT TO SBG PROGRAM STATISTICS

*<u>Analysis of Public Sector Savings due to SBG Contracts</u>

The estimate of public sector savings from program inception in 1971 through December 31, 1981, was calculated as follows:

Total Awards through the SBG Program	10,689,770,335
Percent from Public Sector	x 38.7
Awards from Public Sector through SBA Program	4,136,940,990
Bid Spread Factor (bid spread - 9.25 percent)**	x 1.0925
Projected Public Sector Awards - if no SBG Program	4,519,608,030
Less Awards through SBG Program	4,136,940,990
Savings to the Public Sector	382,667,040

**These factors were developed from the 11/77 Study of the SBG program by PPED/OPRD. It is estimated that both are significantly higher at this time, but have been held at the 1977 levels in this exhibit for conservative analysis.

TABLE 3

COMPARISON OF LOSS/PREMIUM RATIOS FOR THE SPECIALTY SURETY AND THE SBA

	BOND AMOUNTS				
	$249,999	$250,000	$500,000	$750,000	$1,000,000
SPECIALTY SURETY					
-Loss	312	625	1,250	1,875	2,500
-Premium	3,000	3,000	5,000	7,000	9,000
-Loss/Premium	10.4%	20.8%	25.0%	26.8%	27.8%
SBA					
-Loss	2,812	2,500	5,000	7,500	10,000
-Premium	750	750	1,250	1,750	2,250
-Service Charge	500	500	1,000	1,500	2,000
-Premium + Service Charge	1,250	1,250	2,250	3,250	4,250
-Loss/Premium + Service Charge	225.0%	200.0%	222.2%	230.8%	235.3%
OVERALL					
-Loss/Premium + Service Charge	73.5%	73.5%	86.2%	91.5%	94.3%

House Research Agency

July 1, 1980

Alaska State Legislature

Senate Committee on State Affairs

Vic Fischer, Chairman • Pouch V • Juneau, Alaska 99811 • (907) 465-4954

Official Business

HIGHLIGHTS OF CS FOR SENATE BILL NO 414 (State Affairs)

An Act establishing a Small Contractor Surety Bonding Corporation

* Section 1. Establishes a Small Contractor Surety Bonding Corporation

Sec. 45.71.070. CONDITIONS FOR ISSUANCE OF GUARANTEE. The corporation may guarantee and enter into commitments to guarantee a surety against loss from the breach of a bid bond, payment bond, or performance bond by a principal on a contract up to $1,000,000 for work on public construction...

The bond principal cannot exceed $1,000,000 and bonds will only be issued for public projects. The S.B.A. Surety Bond Guarantee Assistance Program has had a $1,000,000 limit. In February, 1982, the limit was reduced to $250,000. In 1981, DOTPF issued 362 contracts in the $1,000,000 or less category. Of those, 66 percent (231) were less than $250,000 and 33 percent (131) were between $250,000 and $1,000,000.

(1) The person who would be the principal on the bond is a contractor or subcontractor whose gross revenue for the most recently completed fiscal year was not in excess of $1,000,000.

This section limits eligibility to small contractors whose annual gross revenues are less than $1,000,000.

Sec. 45.71.080 EXTENT OF LIABILITY (a) A guarantee under this section shall obligate the corporation to pay to the surety for a breach of contract a sum not to exceed 90 percent of the loss incurred and paid by the surety as a result of the breach.

A private surety would have to agree to accept 10 percent of the liability before the surety bonding corporation issues a bond. This is modeled after the S.B.A. Surety Bond Guarantee Assistance Program. In return for the 10 percent private surety liability, the private surety receives 90 percent of the fees and the S.B.A. receives the remaining 10 percent plus a service charge.

*Section 4. This Act takes effect upon elimination of the United States Small Business Administration surety bond guarantee assistance program.

C.S. for S.B. 414 creates a back-up program to avoid costly delays for small contractors in the event that the S.B.A. program is eliminated.

SB 414
Testimony by the Alaska Division of Insurance
Before the Senate State Affairs Committee

We are not in favor of SB 414. The bill places the State directly in the business of insurance and does so in a way to deny the public the protection of the insurance code (AS 21).

In Section 1 of the bill, an assumption appears to be made which is the basis for establishing the corporation and which is not the principal reason for any bond availability problem. The section suggests that competence is the prime consideration in providing a bond, but it is only a part of the consideration.

First it should be understood that the bond is not a risk-shifting device for its purchaser. It has another purpose Its purpose is to secure the interests of the party with whom the contractor wishes to deal. This interest is secured in two ways. First, the surety assumes the owner's financial risks of nonperformance by the contractor; and, second, the suretyship mechanism prescreens or prequalifies contractors and only issues bonds to those who, in the surety's judgment, will be able successfully to perform a given contract.

The surety is concered with a number of factors when considering the issuance of a bond to a contractor including:

- -What is the financial condition of the contractor?
- -Has he done jobs of this magnitude before?
- -Were they successfully completed according to contract specs?
- -Are there factors to make this contract more difficult to perform then his past contracts?
- -What's his travel record on past contracts?
- -Is he capable of doing the work?
- -Is he capable of accurately identifying his costs?

When the bond is issued, the surety is in effect contracting with the owner for completion of the contract. If the contractor gets in trouble, the surety has three choices. First, he can contract with the same contractor to complete the contract; second, he can contract with someone else to complete the contract; or third, he can let it default and pay on the court's decision of what the surety penalty should be.

The surety binds itself to the contractor for performance of a contract. If you were so bound, what would you want to know about the contractor?

The surety "premium" does not contemplate loss. It has some loss paying capacity but it is not the chief source out of which losses are intended to be paid.

Competence is a factor, but the phrase is not confined to work skills. Other skills would include managing and controlling costs, skill in competitive bidding, and skill in collecting receivables. These are major causes of contractor failures.

It appears that the real problem falls into other areas such as availability of work and thin financial resources of the contractor.

The response for availability of work is to strengthen the contractor. This can be done by raising the size of contracts requiring bonds and making jobs available in reasonably small jobs.

The response for thin financial resources is to develop a program of facultative reinsurance or indemnity to help availability. Here, care should be exercised to permit the surety to administer the bond and adjust the loss with the State's role limited to finance and setting the conditions of reinsurance or indemnity. This could be accomplished with direction similar to that on page 3, lines 20-23.

APPARENT CAUSES OF CONTRACTOR FAILURES

Cause	Percentage
Heavy operating expenses (lack of skill in managing and and controlling costs)	26.4%
Inadequate sales (lack of skill in competitive bidding)	25.2%
Competitive weakness	23.8%
Receivables difficulties	14.6%

UNDERLYING CAUSES OF CONTRACTORS FAILURES

Cause	Percentage
Incompetence	45.4%
Unbalanced experience	18.6%
Lack of managerial experience	18.5%

SOURCE: Dunn & Bradstreet, Inc. - 1968

THE LEGISLATURE OF THE STATE OF ALASKA

TWELFTH LEGISLATURE

FISCAL NOTE

I. REQUEST

Bill/Resolution No. SB 414

Title "An Act establishing a state-operated Small Contractor Surety Bonding Corp. and providing for an effective date."

Requested by Fischer Date 4-21-81

II. FISCAL DETAIL

Agency Affected Department of Commerce & Economic Development

Program Category Affected Public Protection

BRU, Program, or Subprogram(s) Affected Regulation & licensing of professions - admin.

(Note: If more than one budget component is affected, separate line-item amounts and funding for each component in the analysis section.)

EXPENDITURES (Thousands of Dollars)

		FY 81	FY 82	FY 83	FY 84	FY 85	FY 86
100	PERSONAL SERVICES		147.4	157.7	168.7	180.5	193.1
200	TRAVEL		8.0	8.9	9.8	10.9	12.2
300	CONTRACTUAL		182.3	195.1	208.8	223.[illegible]	239.0
400	COMMODITIES		6.2	6.2	6.2	6[illegible]	6.2
500	EQUIPMENT		7.3	.0	.0	.0	.0
600	LAND & STRUCTURES		8.1	8.1	8.1	8.1	8.[illegible]
700	GRANTS, CLAIMS, ETC.						
	TOTAL		359.3	376.0	401.6	429.1	458.6

FUNDING (Thousands of Dollars)

	FY 81	FY 82	FY 83	FY 84	FY 85	FY 86
GENERAL FUND		359.3	376.0	401.6	429.1	458.6
FEDERAL FUNDS						
OTHER (Specify Fund Source)						

POSITIONS

	FY 81	FY 82	FY 83	FY 84	FY 85	FY 86
FULL TIME		3	3	3	3	3
PART TIME		1	1	1	1	1
TEMPORARY						

III. ANALYSIS (See Fiscal Note Preparation Instructions, Section III)

PERSONAL SERVICES - FY'82 salary schedule; exempt. 7% inflation factor projected.

1 Executive Director, range 22, 12 mos	$ 50,791.00
1 Secretary I, range 10, 12 mos.	22,735.00
1 Accountant III, range 16, 12 mos.	33,303.00
1 Assistant Attorney General, ½ time	20,620.00
Additional support staff (full or part-time)	20,000.00
	$ 147,449.00

TRAVEL - 12% inflation factor projected.

Minimum of 3 meetings per year, 3 days ea., 5 members	5,000.00
Executive Director	1,000.00
Assistant Attorney General	1,000.00
Additional staff as necessary	1,000.00
	$ 8,000.00

IV. DATE 4-21-81 PREPARED BY [signature]

AGENCY Division of Occupational Licensing

PHONE 465-2535

Original: Legislative Finance

cc: Budget and Management

Prime Sponsor (First Legislator Named)

33-001 (Rev. 12/80)

SS 414 Fiscal note continued. . . .

CONTRACTUAL - 7% inflation factor projected.

Consultants: Financial, Investment, Bond Underwriting and Investigative	$ 160,000.00
Word Processing lease	8,500.00
Phone hook-up	1,800.00
Long Distance Telephone	6,000.00
Copier rental	1,000.00
Postage meter	1,000.00
Printing and duplication	3,000.00
Publications (various)	1,000.00
	$ 182,300.00

COMMODITIES

Postage	4,000.00
Paper stock	2,000.00
Tapes for lanier recorder	180.00
	$ 6,180.00

EQUIPMENT - one time expense in FY'82.

2 desks, double pedestal, 60x30"	704.64
1 desk, single pedestal with typing extension	432.83
2 credenzas, 19x62"	706.36
2 tables, 72x36"	395.70
4 file cabinets, 4 drawer legal with lock	863.96
1 bookcase, 3 shelves	102.64
1 storage cabinet	184.71
1 chair, exec. swivel with arms	176.83
2 chairs, posture without arms	232.54
3 side chairs	224.70
1 typewriter mat	35.46
1 typewriter, correcting selectric, IBM	1,028.83
3 calculators, desk, printing 10 digit	534.78
1 Lanier	1,000.00
2 brief cases	180.00
2 file tubs	363.00
mail baskets	30.00
waste baskets	40.00
form racks	50.00
	$ 7,286.98

LAND & STRUCTURES

150 sq.ft. X 1.50 X 3 X 12 mos. = 8,100.00

MINORITY
BUSINESS ASSISTANCE CENTER

BUSINESS OFFICE:
836 E. 15th Ave., Suites 3 & 4
Anchorage, Alaska 99501
Phone: 907-274-3689/3680

MAILING ADDRESS:
P.O. Box 3315
Anchorage, Alaska 99510

April 17, 1981

Senator Vic Fischer
Chairman
Senate State Affairs
Alaska State Legislature
Pouch V
Juneau, AK 99811

RE: Senate Bills 45,414 and 415

Dear Senator Fischer

Herein capsulated are the comments we provided at this past Thursday's Teleconference.

Senate Bill 45

Two brief points: It is recommended that the act waiver limits reflect an appreciation for the yearly increases in the Construction Cost Index. This can be accomplished by either attaching an automatic yearly or periodic muiltiplier to the limit.

The waiver provision should clearly state it applies to both general contracts and bids submitted by subcontractors to prime contractors on larger jobs.

Senate Bill 414

General Overview:

The introduction of this bill is very timely and you are to be commended for your efforts.

Under existing state statute companies writing bonds are not required to give the applicant a reason (verbal or written) why their request was denied. This practice effectively denies a contractor an opportunity to correct any deficiencies in future applications. However a more likely situation is the local bonding agent is not brothering to "work" the applicant's package. The proposed bill would certainly correct this situation. Alternately, informal reasons given for not writing bonds in the range being suggested is the profit margin is not substantial enough and the only way they would consider writing bonds in this range was if the contractor was placing his more profitable insurance coverage needs with the company.

Sponsored by: Minority Resource and Services, Inc.
A Private Non-Profit Corporation
"IN SERVICE TO THE COMMUNITY"

Briefly discussed below are specific points on SP 414:

Section 45.71.020, (Board of Directors), pge. 2. Consideration should be given to having the dire tor of insurance serve on the board in place of the Commissioner of Commerce. He or she should have more working knowledge of the problems.

Section 45.71.070, (Eligible Contractors), pge 4. Mechanics of how a contractor could be pre-qualified should be addressed. This would miminize the possibility of the contractors being caught in a time squeeze by going through the process of being turned down (which can be a drawn out process) by a private insurer and then applying to the state at the same time he must be satisfying other conditions of contract award i.e. mobilizing.

Section 45.71.110, (Contractor Surety Funds), pge 5. It would be helpful if a determination could be made as to whether the proposed capitalization is of a sufficent magnitude to meet possible demand.

Concluding discussion should be included on how lonc a contractor is eligible to participate in the program and what are the penalities for a contractor who does not perform?

Senate Bill 415

Section 1 AS 19.10.190 (Advertisement, etc), pge 1. The ending sentence should be more specific in terms of how informal bids will be solicited.

Section 10 AS 37.05.230(1), (no title), pge 5. point(II) How is data for this section to be developed and verified?

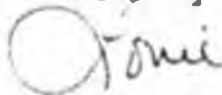
Section 16 AS 37.05.230 (Amended), pge 7. point (10) It may be that DOTPF or Commerce are more capable of providing this function. Alternately if the thinking was the office of EEO could assume the duties, it should be clearly understood that these functions are not necessarily campatible for administrative purposes.

Concluding discussion on SB415, Section 17 is very strong and good and we were pleased to see the University of Alaska brought under the guidelines of this act.

Hopefully these bills will be enacted to the ultimate benefit of all Alaskans.

Finally we requested support of the center from Mr. Putman of your staff by placing in the state budget an amount that will allow us to continue operating the center in FY82, your support of this request will be sincerely appreciated.

Yours truly



E. Louis Overstreet

KDT

THE LEGISLATURE OF THE STATE OF ALASKA
TWELFTH LEGISLATURE

FISCAL NOTE

I. REQUEST
Bill/Resolution No. SB 414
Title An Act establishing a state-operated Small Contractor Surety Bonding Corporation.
Requested by ______ Date April 14, 1981

II. FISCAL DETAIL
Agency Affected Department of Community and Regional Affairs
Program Category Affected Development
BRU, Program, or Subprogram(s) Affected Local Government Assistance
(Note: If more than one budget component is affected, separate line-item amounts and funding for each component in the analysis section.)

EXPENDITURES (Thousands of Dollars)

	FY 81	FY 82	FY 83	FY 84	FY 85	FY 86
100 PERSONAL SERVICES		-0-				
200 TRAVEL		-0-				
300 CONTRACTUAL		-0-				
400 COMMODITIES		-0-				
500 EQUIPMENT		-0-				
600 LAND & STRUCTURES		-0-				
700 GRANTS, CLAIMS, ETC.		-0-				
TOTAL		-0-				

FUNDING (Thousands of Dollars)

	FY 81	FY 82	FY 83	FY 84	FY 85	FY 86
GENERAL FUND		-0-				
FEDERAL FUNDS		-0-				
OTHER (Specify Fund Source)		-0-				

POSITIONS

	FY 81	FY 82	FY 83	FY 84	FY 85	FY 86
FULL TIME		-0-				
PART TIME						
TEMPORARY						

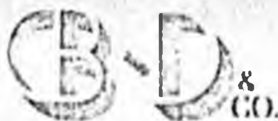
III. ANALYSIS (See Fiscal Note Preparation Instructions, Section III)

No fiscal impact on this agency.

IV. DATE [illegible] 14, 1981 PREPARED BY Terry L. Earley
AGENCY Department of Community & Regional Affairs
PHONE 465-4730

Original: Legislative Finance
cc: Budget and Management
Prime Sponsor (First Legislator Named)

33-001 (Rev. 12/80)



CORROON & BLACK/DAWSON & CO., INC.

4220 "B" Street
Anchorage, Alaska 99503
907-279-3471 Telex: 25-109

April 21, 1981

Senator Vic Fischer, Chairman
Senate State Affairs
Alaska State Legislature
Pouch V
Juneau, Alaska 99811

RE: Senate Bills No's. 45, 414 and 415

Dear Senator Fischer:

Thank you very much for allowing me to pa icipate in the Teleconference Hearing on the above referenced bills held on Thursday, April 16th throughout the State. At that point in time you had asked for written in-put either pro or con concerning the referenced Senate Bills. I realize that my in-put may not be very welcome as you are one of the sponsors of the bills, but I must submit my comments both as a businessman and as a concerned citizen relating to my opposition to all three of these bills.

First of all, I feel it is only proper that I identify myself as being the manager in charge of surety operations for the State of Alaska for Corroon and Black/Dawson & Co., which position I have held in excess of thirteen years. This means that I devote my full working hours to assisting contractors in obtaining bonding. In addition to this I am also a member of the National Legislative Committee of the National Association of Surety Bond Producers. I am using this method of identifying myself to show that I have had experience in the bonding industry and can therefore speak from a position of some authority.

I should, at this time, clear up a common misconception. That is that bonding and insurance are the same. As you are quite aware, they are not. Simply stated, surety is an extension of unsecured credit on the part of one party to guarantee the acts and/or omissions of another party. Insurance, on the other hand, is where, for a fee, a company will allow an individual into a pool of risk and agree to indemnify him against loss due to his or others' negligence. Most people feel that surety and insurance are one and the same because most surety companies are also insurance companies. This is not true. The only reason that insurance companies write surety is because they have the necessary financial reserves to enable them to do so.

I'm sure that one of the reasons for the introduction of this bill is because you and other State representatives have received information

from constituants stating that they were unable to obtain the necessary bonding to bid on State, Federal and private projects. The major reason for this is probably because of the lack of people qualified to assist contractors in obtaining surety in this state. Most insurance brokerage firms in Alaska have no thorough knowledge of how to obtain surety credit for their clients. I can liken this to shopping at a drug store in order to obtain a commercial loan. For the lack of skilled personnel in the surety field in this state, I do apologize, however the few of us that are available are doing our best.

I should now like to list my overall and more specific objections to Senate Bills No's. 414, 415 and 45.

First, I feel that Senate Bill No. 414 would be a duplication of existing bond facilities. At the present time there is, under the State Little Miller Act, a provision for Personal Surety under Section 36.25.010 and Section 36.25.025. I feel that all that is needed is to draft adequate regulations to control personal surety and there would be absolutely no need for Senate Bill No. 414. In addition to this, there is the United States Small Business Administration Surety Guarantee Program, which has been in effect for nearly ten years. You will also find that there are a number of corporate sureties active in Alaska and actively seeking new bonding business. I also feel that Senate Bill 414 would result in increased costs to the State by granting projects to unqualified contractors. Which would result in defaults, rebids, late completion of projects, etc.

Another major objection would be in considering the acceptability of the State as a surety on other than State funded projects. For instance, the Federal Government requires that any surety on Federal projects or Federally funded projects appear on the U. S. Treasury list showing the name, address, assets and single bond capability of the company. This is especially true in light of the fact that in Senate Bill No. 414, under Section 8, Page 7, the State would prorate payments if there were inadequate funds in the bonding fund to pay full claims. I'm sure that the Federal Government would object quite strongly to that type of surety.

Another objection is that the primary purpose of bonding is "prequalification" of a contractor for performance of a particular contract according to the terms and conditions and timing as laid out in the contract. This means that an independent organization has reviewed the contractor with people who have years of experience in doing just

that and have then decided to provide a bond.

As a voter and tax payer in Alaska, I take exception to Senate Bill 45, which increases the contract amount that is to be required to bond from $50,000 to $100,000. I feel that in this the State is assuming too much of the risk and also putting too much of a burden on the contracting officer in attempting to qualify contractors prior to award. It has been proven by the U. S. General Accounting Office that no other system outside of Corporate Suretyship has been found to appropriately and adequately qualify contractors, to provide an open competitive market place and to bring jobs in on time, while protecting the public. The GAO statement was: "factors that are arguing against the Government becoming a self insured (surety) are the Federal Construction Agency's lack of legal means, administrative machinery and in-house expertise for handling claims submitted by contractors, suppliers, and labor and for providing financial aid to contractors."

Even Dun and Bradstreet recognizes the fact that the contracting business has the distinction of being the industry with the highest failure rate. Their 1980 records indicated contractor failure nationwide at a 15 year high. This failure ratio compared to 1979 showed a 50% increase. Interms of dollars, the liabilities of the failed firms amounted to $465,000,000. Sub contractor casualties were the highest since 1966.

Dun and Bradstreet study blamed the majority of failures on:

1. Incompetence

2. Financial inadequacies

3. Managerial experience

4. Inflation

Is it the responsibility of the State of Alaska to encourage the under-financed and under-experienced individuals in to competition in an already over populated construction industry? Furthermore it seems unconscionable to expect that the contracting officer underwrite decisions without the benefit of those resources available to a surety. The point is, the taxpayer is going to be asked to pick up the expenses and losses.

The increase in the size of projects requiring bonds would negate the one main area of expertise that the surety brings to protecting the public. This area is prequalification of the contractor which at the same time provides protection for injured parties. This promotes the reason why a system of proven surety is crucial to the people of Alaska.

Returning to Senate Bill No. 414, I might compare that to the record of the U. S. Small Business Administration which has been in the guarantee business for over nine years. In reviewing the statistics on SBA guarantees you will find that in the past nine years the SBA issued 125,371 guarantees totalling $13 billion dollars in construction work. These guarantees were issued for 21,393 contractors of which 3,060 were minority contractors. Of this total of 21,393 contractors there were 7,007 defaults resulting in net losses to the program of $203.5 million dollars. This does not count outstanding bonds upon which claims have been reserved and for which amounts have not yet been established. These are only dollars that have been paid out by the Small Business Administration.

You must recall that these dollars represent 80 to 90 percent of the actual losses as the surety is required to accept 10 to 20 percent of the loss. The surety also cannot receive any payment from the SBA until they can prove a loss has occured. In any event, these losses have totalled over $20,000,000 per year for the life of the program. No corporate surety could stand that type of loss.

I'm enclosing for your review several documents among which is a book entitled "The Unseen Services of a Surety." This shows how the corporate surety deals with losses or anticipated losses, not merely by paying out unpaid bills but by also providing engineering, accounting, and financial assistance to contractors who have gotten into trouble, in order that the project may be completed on time to the benefit of the owner. All that is contemplated under Senate Bill No. 414 is that payment be made to either the owner or to unpaid suppliers, sub contractors, material men etc., this does not insure that the project will be completed.

This letter is becoming quite lengthy and I do have several objections to Senate Bill No. 415, however I must reserve those to a later date.

I would like to make a flat, unqualified statement that an individual or company actively engaged in a construction business, who is qualified from an educational and experience standpoint, who has adequate assets

to meet job expenses and who has established him/her/itself as a responsible member of society, can obtain corporate surety without State assistance. On the other hand, if a contractor is not qualified, I do not believe the State should assume the responsibility for underwriting this type of contractor. In the age of growing consumer awareness this removal of a proven safeguard could very well prove disastrous to the ongoing building and construction industry and strike a severe blow to the over-all economy of Alaska.

I would be very happy to appear at any hearing or to provide further written testimony concerning these bills upon request.

Thank you very much for your interest.

Sincerely,

R. L. Richmond
Vice-President/Bond Manager

RLR:da

Appropriation (supplemental) (trans. for handicapped & elderly)

SENATE BILL NO. 413, by Senators Stimson, Fischer, Sturgulewski and Rodey. Makes a supplemental appropriation of $144,500 from the general fund for payment as a grant to the Municipality of Anchorage for the expenses of local transportation for the elderly and handicapped for the fiscal year ending June 30, 1981. Act provides for an immediate effective date.

Introduced April 10 and referred to Community and Regional Affairs, then to Finance.

Small Contractor Surety Bonding Corporation (estab. state operated)

SENATE BILL NO. 414, by Senators Fischer and Stimson. States that the legislature finds that many small contractors are unable to obtain at reasonable costs surety bonds necessary to bid on both private and public construction projects. This inability can in effect reduce competition and contribute to increased costs for such projects. Also finds that establishing a state program to provide bonding to small contractors at reasonable costs would promote increased competition and reduced costs for public and private construction projects while maintaining acceptable risk levels for the contracting agency or company.

Adds a new chapter to AS 45 (Trade and Commerce). Chapter 71-Small Contractor Surety Bonding Corporation. Establishes the corporation in the Department of Commerce and Economic Development, but having a legal existance independent of and separate from the state. Establishes a board of directors consisting of the commissioner of Commerce and Economic Development and four members appointed by the Governor who serve for a term of four years. Two of the appointed members to be small contractors who are licensed in the state and actively engaged in a contracting enterprise for the preceding five years. Two members shall be public members who may not be contractors and may not have a direct financial interest in or be associated by legal contract with a licensed contractor except as a consumer of services provided by a contractor. Board shall meet not less than once each four months. Board shall employ an executive director who may, with approval of the board, hire staff as necessary. Employees of the board are in the exempt service category. The corporation may contract for outside services as necessary. The attorney general is the legal counsel for the corporation.

Act provides for general powers of the corporation and states that it has the power to, "issue or participate in the issuance of surety bonds, including bid bonds, performance bonds and payment bonds, to elegible small contractors, whether as prime contractors or subcontractors, if the corporation determines that these bonds are not otherwise available, wholly or in part, from a corporate surety upon reasonably equivalent terms and conditions." Also allows the corporation to, "guarantee or enter into commitments to guarantee corporate sureties against loss as the result of a breach of the terms of a bid bond, performance bond, or payment bond issued to a contractor as the principal of the bond."

Program requires contractors to have been doing business in the state for at least one year and to have maintained his principal place of business in the state for at least one year before the date of application. Also requires that the person's gross revenue for the most recently completed fiscal year was not in excess of $1,000,000.

SB 414. (cont'd)

The corporation may not issue to a single contractor a bond in excess of $500,000. If more than one bond is issued to a contractor, the aggregate total of bonds outstanding at one time may not exceed $500,000.

Act provides for fees and payments by contractors, payment by corporate sureties, and a contractor surety fund which may not exceed $5,000,000. Outlines claims for payment, consideration of application, findings and payment, order of claim payment and right to subrogation.

The board shall prepare for the Governor and the legislature an annual report of its activities under this chapter including a summary of the amount and type of bonds issued and the disposition of claims filed with the corporation.

Adds the Small Contractor Surety Bonding Corporation to the list of state boards and commissions. Act provides an immediate effective date.

Introduced April 10 and referred to State Affairs, Labor and Commerce, then to Judiciary.

Competitive Bidding Procedures

SENATE BILL NO. 415, by Senators Fischer and Stimson. Rewrites competitive bidding procedures contained in AS 37.05.230 & 240 and requires the following contracts to be awarded in accordance with new provisions:

--Highway construction contracts for $50,000 or more (currently only those for $100,000 or more must solicit competitive bids) and highway maintenance contracts for $25,000 or more (new provision). (Secs. 1-3 of bill. Amends AS 19.10.190 & 210.)

--Contracts for Local Service Roads & Trails entered into by a local government if the amount of state money is $50,000 or more and Local Services Roads & Trails maintenance contracts for $25,000 or more. (Secs. 4-5 of bill. Amends AS 19.30.191)b) and 211(a).)

--State public works construction contracts for $50,000 or more (currently $100,000) and maintenance contracts for $25,000 or more (new provision). (Secs. 6-8 of bill. Amends AS 35.15.030 & 050.)

--Contracts entered into by a municipality or REAA for construction of a public works project if state portion is $50,000 or more (Sec. 9 of bill. Adds new subsection (g) to AS 35.15.080, "Local Control of State Public Works Projects".)

--Contracts awarded by the University of Alaska if state money is $50,000 or more. (Sec. 18 of bill.)

--Contracts awarded by a nonprofit corporation if state money is $50,000 or more. (Sec. 19 of bill.)

--State grants to municipalities and other recipients who propose to award a contract of which $50,000 or more is financed with the grant or other state money. (Secs. 20-22 of bill. Amends AS 37.05-.315.)

SB 415 (cont'd)

Makes the following amendments to AS 37.05.230 (Competitive Bidding):

--Sec. 10 of bill amends (1) to require that competitive bid be awarded to a bidder on the "certified minority bidders list" (created in bill) if the value of contracts awarded during the fiscal year to bidders on the list is less than 20% of the total value of contracts, the bid is not more than 15% higher than the lowest bid, and the bidder agrees to lower the bid by 5%. Subject to the foregoing provision, bids shall be awarded to Alaskan bidders if bidder is on the "certified Alaska bidders list" and bid is not more than 10% higher (currently 5% higher) than the bid of the lowest nonresident bidder. States that competitive bids are not required "(i) for contractual services when no known competition exists; (ii) when rates are fixed by law or ordinance; (iii) for items traded in on like items; or (iv) for professional services." (Existing law also exempts sales involving fair trade items and cases where, in the judgment of a purchasing agent, food, clothing, or medical supplies, or material for use in laboratory and experimental studies may be purchased otherwise to the best advantage of the state.)

--Sec. 11 of bill requires notices to be sent to those on Alaska bidders list and adds provision to (2) which allows state to "limit solicitation of bids" if it finds that it is in the best interests of the state.

--Sec. 12 of bill amends definition of "Alaska bidder" in (5) to add that person must not be delinquent in payment of state taxes and must maintain inventories or facilities in support of business activities in the state.

--Sec. 14 of bill amends (7) to state that the minority and resident bidding preference does not apply to highways & public works contracts of the Dept. of Transportation & Public Fac. estimated to be less than $50,000 (currently resident preference does apply to contracts estimated to exceed $5,000).

--Sec. 15 of bill amends (8) to bring contracts for $50,000 or more for the purchase of products or services manufactured or provided by a sheltered workship under the competitive bidding requirements.

--Sec. 16 of bill adds new paragraphs (9), (10), & (11) to AS 37.05.230: (9) directs the Dept. of Admin. to compile and update a certified Alaska bidders list; (10) directs the Dept. to compile and update a certified minority bidders list; (11) states that the minority and resident bidding preferences do not apply to purchases and contracts involving federal money received by the state if the application of a bidding preference would violate federal law or program guidelines.

Section 17 of the bill amends AS 37.05.240 relating to bid requirements and award of contracts and purchases. Adds new subsections which require a prime contractor, when submitting a bid, to name the principal subcontractors he intends to use. After bid awarded contractor may change subcontractors only "for cause." Also requires at least 20% of the money from a contract awarded under competitive bidding which is paid to subcontractors to be paid to subcontractors

SB 415 (cont'd)

on the certified minority bidders list, unless no subcontractors on the list are available.

Section 23 of bill adds definition of "department" (Dept. of Admin.) to definitions section of AS 37.05.

Section 24 of bill deletes current exceptions granted by AS 44.33.300 to competitive bidding requirements for state public works and highway construction contracts in areas hit by economic disaster.

Does not provide for effective date.

Introduced April 10 and referred to State Affairs, Transportation and Finance.

Appropriation (special) (Seward Hwy. Paving)

SENATE BILL NO. 416, by Senator Fischer. Appropriates $65,140 from the general fund to the Dept. of Transportation & Public Fac. for payment to the Boysen Investment Corp. for an unanticipated increase in costs of petroleum products used in paving the Seward Highway (O'Malley interchange-Potter job). Effective immediately.

Introduced April 10 and referred to Transportation and Finance.

State Health Insurance Program

SENATE BILL NO. 417, by Senators Kerttula, Dankworth, Fischer and Stimson. Directs the Commissioner of Administration to establish a state health insurance program for Alaskan residents. Minimum benefits shall be established by Commissioner by regulation and shall include hospital and medical expense benefits. Program shall not include dental care or eye glasses or hearing aids or their prescription or fitting. Premiums shall be paid by state for any resident enrolled in the program who is not enrolled in a group health insurance plan. Sets limit for annual deductibles under the program at $100 for each enrolled resident or $300 for each enrolled family. Copayment amount for each enrolled resident may not exceed 20% of expenses covered. Sets maximum cost to enrolled resident at $2,500 per year. Directs Commissioner of Administration, on the enactment of bill, to immediately undertake the adoption of regulations and the preparation of contracts so that coverage and benefits may begin on July 1, 1982. (New provisions added to AS 18 under Chapter 23, State Health Insurance Program.) Provides for immediate effective date.

Introduced April 10 and referred to Health, Education & Social Services and Finance.

Agricultural Development Projects

SENATE BILL NO. 418, by Senator Kerttula. Expands the powers of the Commissioner of Natural Resources (in AS 38.05.020), the Director of the Div. of Lands (in AS 38.05.035), and the Alaska Agricultural Action Council (in AS 44.33.670) by adding that those officials & that agency may "require prequalification, including the submission of conservation plans, development plans, or other plans, schedules, or programs, of persons who apply to participate in an agricultural development project." Retroactive to January 1, 1980 and effective immediately.

Introduced April 10 and referred to Resources and Finance.

SB
415

National Federation of Independent Business

March 25, 1982

Senator Vic Fischer
Alaska Senate
Pouch V
Juneau, Alaska 99811

RE: CSSB 415 (State Affairs)
Proposed Revision to Section 15

Dear Senator Fischer:

In response to your request of March 23, I have considered several alternatives regarding an appropriate definition of "Alaska bidder" for purposes of the preference provided in the law. The following language is proposed for your review:

*Sec. 15. AS 37.05.230(5) is amended to read:
(5) an "Alaska bidder," for the purpose [OF BID AWARDS UNDER (1)(F)] of this section, is a person who
(A) holds a current Alaska business license; [,]
(B) submits a bid for goods or services under the name as appearing on his current Alaska business license; [,]
(C) has, if an individual, derived at least 50% of his earned income, or, if a corporation or partnership, the officer or partner submitting the bid has derived at least 50% of his earned income from the operation of the business [MAINTAINED A PLACE OF BUSINESS] within the state for a period of six months immediately preceding the date of his bid;
(D) provides sufficient information to clearly establish that for the immediately preceeding six month period, he has been actively engaged, in the state, in the business of providing the goods and/or services for which the bid is being submitted; and
(E) is not delinquent in the payment of state taxes;

In addition to the above language, you could consider adding one additional requirement to a bid submitted by anyone claiming the Alaska bidder preference. That requirement would be for him to state, if for goods, the percentage which will be provided from an inventory maintained by the bidder in the state, and, if for services, the percentage which will be performed in Alaska. The obvious question then is, what good is this information? Possibly, you could add another stipulation to the above statutory language whereby a bidder for goods would be required

Director, Governmental Relations/Alaska
P.O. Box 194, Auke Bay, Alaska 99821, Tel. 907/586-4100

to deliver a certain percentage from an inventory in Alaska or a bidder for services would be required to perform a certain percentage of the services in Alaska. Unfortunately, a requirement of this nature could possibly produce a worse quagmire than anything else because there will be some bids where all of the goods should be drop shipped from the lower states regardless of who the bidder was and others where 100% could be delivered from inventories in Alaska. The same thing would also be true on some of the services contracts.

It appears that if the Legislature wants to maintain the "Alaska bidder" preference, you can only go so far without creating more administrative problems than anything else. If you decide to go with some of the more stringent requirements suggested above, a penalty should be added to the law for a bidder submitting false information when seeking the "Alaska bidder" preference. I would suggest that the individual submitting the false information be barred and any company for which he was a majority stockholder or an officer be barred from being able to apply for "Alaska bidder" preference for a period of 10 years. Ten years may seem a little stiff, however, if the penalty is not sufficiently severe, the bidder may decide it's worth the gamble to falsify an application.

I hope that these suggestions are of some assistance as you consider this very difficult issue. If I can be of assistance in the future, feel free to contact me.

Very truly yours,

Gary L. Jenkins
Director, Governmental Relations
Alaska

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March 19, 1982

The Honorable Vic Fischer
Chairman, Senate State Affairs
Committee
Alaska State Legislature
Pouch V
Juneau, Alaska 99811

Re: Surety Bonding Bills

Dear Senator Fischer:

We understand that your committee will take up SB 45, and a possible committee substitute for SB 414, as well as a new SB 869, next week. Unfortunately, I will have to be out-of-town because of federal court settings, but I wanted to give the Committee some expression with regard to the three bills on behalf of the American Insurance Association.

SB 869 would serve the useful purpose of allowing an applicant for a surety bond to know the reasons for a denial, and presumably work to overcome them, when he or she is not granted a bond. However, candid and full disclosure of all such adverse information could result in embarrassment to the applicant and possible assertions of liability against the company. The problems with regard to the handling of such adverse information have been the subject of lengthy consideration by the industry and by the National Association of Insurance Commissioners. The NAIC has adopted a model privacy act, making clear that adverse underwriting information must be made available, but stipulating how the information is to be kept and the circumstances under which it is divulged, and protecting the persons and companies involved from liability for meeting the requirements of the statute. The American Insurance Association supports the model bill. Obviously, what this comment is leading to, is that the bill before you requires divulgence of adverse information in one very limited line of the insurance business, and does not contain any of the well thought out provisions that have been included in

the model act. We would urge that the Committee consider the model act if it wants to require the kind of disclosure that SB 869 would entail.

An alternative, and much less desirable (because piecemeal) approach, would be to require that the information be retained by the insurer, and to allow the Director of Insurance on investigation to review the information and make such use of it as is appropriate under the circumstances.

Turning to SB 414 as rewritten in the work draft paper, we understand the motivations behind the draft, but we would urge the Committee to be careful that it is obtaining adequate information concerning the cost of such undertaking, and also that the Committee consider the degree to which it wishes a government agency to determine the extent of its involvement in the private market. Speaking to the latter point first, proposed Section 45.71.070(3), makes one of the conditions for issuance of a guarantee of a surety bond, that "the person is not able to obtain the bond on reasonable terms and conditions from a corporate surety ...". What that means in practical effect is that the executive director of the new agency will determine what is reasonable as a price or condition on the issuance of a corporate surety, and will therefore determine the extent to which the agency competes by penetrating the market. This assumes, then, that there is a competitive private market. The alternative would be to make subparagraph (3) read, "the person is not able to obtain the bond from a corporate surety ...". This would make the State the sureter of last resort, but not the sureter of any and all who may be dissatisfied with the private market's rates and can convince a government employee to issue a bond on better terms.

The concern about the cost of the new enterprise is generated in part because the available figures concerning the cost of the SBA program come from the SBA itself. As we are all aware, the SBA budget is under review and the agency has an incentive to make the net cost of their program look small. We are unaware of any statistics which corroborate the agency's assertion that government bids are 10% lower because of the program, and when looking at their cost data, it seems incredible that they have had as many employees over as many years as they report, at no greater cost than they report. One suspects that much of the very substantial indirect cost of the program is not being allocated in this study. Since we do not have independent numbers to challenge the SBA's internal study with, it is perhaps enough to note that one could have had more confidence in the numbers if they had been found in a GAO report.

A further concern with SB 414, as written, is that it will tend not only to cost the State substantially in failed contracts and delays on government construction, but that it will also adversely affect small contractors who have achieved a proven track record and have bonding capacity. Those contractors will not be able to compete effectively with contractors who will qualify for this program, largely for the very reasons which qualify them for bonding: they will be better capitalized, have a proven work force, own their equipment, and generally have, and need to pay for, the things which convince a bonding company that they are not going to fail in a proposed contract. Because the State is responsible for so much of the construction activity in Alaska, depending upon how the program is administered, it could have a very adverse impact on our good contractors. Specifically, we draw the Committee's attention to the fact that proposed Section 45.71.070 promises bid bonds, payment bonds, and performance bonds on contract up to One Million Dollars, but only to contractors whose gross revenue for the most recently completed fiscal year was not in excess of that same figure. It seems likely that, in an effort to allow contractors to gain experience on larger projects, the State will guarantee the performance of contractors who are extended well beyond their capacity.

We also note that the claim processing provisions of proposed AS 45.71 are inappropriate in a surety bond setting.

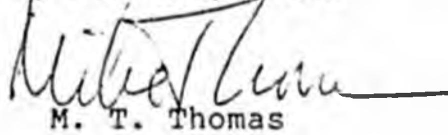
Turning to SB 45, we acknowledge that any statute which sets a dollar cutoff needs to be reviewed periodically as inflation devalues the dollar. However, in reviewing this statute, the Legislature should require objective evidence that competent contractors are being denied work that they could do because of the bonding requirement, and that the benefits to the State outweigh the adverse consequences. These would include depriving bondable contractors of the work, and increasing the odds that the State will have a major contract held up, and its costs greatly expanded, because of the failure of a subcontractor. It may be that the objective evidence exists, but we are not aware of it. We are in fact aware that small specialty bonding companies have been trying in the last few years to write more and more business in the State.

We would like to commend Mr. Winograd for his thoughtful staff paper. He has identified many of the competing considerations which the Committee must address. We would also like to thank you for the opportunity to comment on these bills. I have sent them for further comment to AIA offices on both coasts, and I will certainly make available further information as it is

received. Unfortunately, that is unlikely to be before the time scheduled for your hearings on the 23rd. If, however, the Committee would be able to use further information that the insurance industry might have available, please contact my office and we will do the best we can to obtain it for you.

Sincerely,

ROBERTSON, MONAGLE, EASTAUGH & BRADLEY



M. T. Thomas

MTT:sd

Alaska State Legislature

Senate Committee on State Affairs

Vic Fischer, Chairman • Pouch V • Juneau, Alaska 99811 • (907) 465-4954

Official Business

MEMORANDUM

DATE: March 25, 1982

TO: All Legislators

FROM: Senator Vic. Fischer

RE: CS for S.B. 415, EXECUTIVE SUMMARY

An Act Relating to Bidders Preferences for Alaska Businesses and Businesses Owned by Minorities and Women and Veterans, and Contracting and Procurement Procedures

The CS for S.B. 415 provides a system to insure that public contracting procedures will favor Alaska bidders. Existing statutes are full of loopholes which result in State subsidization of out-of-state interests. The major features of CS for S.B. 415 are:

1) Closes loopholes which allow State funded contracts to avoid State bidding requirements.
2) The Alaska bidders preference is raised to 10%, from the existing 5%.
3) To qualify for an Alaska bidders preference a business must have 50% of its employees residing in Alaska <u>or</u> employ at least 10 resident employees, and no more than 50% of the contract can be subcontracted to businesses whose primary place of operation is outside of Alaska.
4) If during the prior fiscal year a proportionally smaller dollar amount of contracts are awarded to minority bidders compared to target levels, then businesses owned by economic minorities, including women, Alaska Indians, Eskimos, Aleuts, Blacks and Viet Nam veterans, receive a 10% bidders preference on contracts less than $1,000,000 for the next fiscal year.
5) The Department of Administration is required to prepare an annual report on contracts awarded in accordance with bidders preference lists by all State agencies, municipalities, and other entities for contracts using State monies. The report shall be submitted to the House and Senate State Affairs Committees.

This legislation would provide a means to help accomplish our long-standing goals of redistributing State wealth to Alaskans, strengthening domestic businesses, and increasing economic participation by minority groups. Therefore, I respectfully request your consideration and support.

STATE OF ALASKA
THE LEGISLATURE

POUCH Y · STATE CAPITOL
JUNEAU, ALASKA 99811
907 465-3800

LEGISLATIVE AFFAIRS AGENCY

M E M O R A N D U M

March 23, 1982

SUBJECT: Public contracts -- CSSB 415
(Work Order No. 12-2755)

TO: Senator Vic Fischer
Chairman, Senate State
Affairs Committee

FROM: Tamara Brandt Cook
Legislative Counsel TBC

Here is the section-by-section analysis you requested of the draft of CSSB 415 (State Affairs).

Sec. 1. The Department of Transportation and Public Facilities is required to award a highway construction contract in accordance with bidding requirements if the contract is $50,000 or more. Existing law requires the department to award a contract in accordance with bid requirements only if it exceeds $100,000. The reference to AS 44.33.300 is deleted, since that section allows a waiver only if the contract is less than $50,000 and by its terms it would not apply to contracts awarded for $50,000 or more.

Sec. 2. The Department of Transportation and Public Facilities is required to award a contract for maintenance of a highway in accordance with bidding requirements if the contract is $25,000 or more. It is discretionary with the department whether to award smaller contracts in accordance with bidding requirements. The department may not award contracts in smaller increments to avoid the bidding requirements. These are new provisions.

Sec. 3. The Department of Transportation and Public Facilities is required to comply with the bidding requirements and preferences of AS 37.05.230(1) in awarding a contract that is subject to bid requirements. Existing law only requires the department to award a contract to the lowest responsible bidder.

Sec. 4. A local government is required to comply with the bidding requirements and preferences of AS 37.05.230(1) in awarding contracts for a local service road or trail that the local government has assumed from the Department of Transportation and Public Facilities if the amount of state money to be used on the project is $50,000 or more. Existing law only requires that contracts be awarded on the basis of the lowest responsible bid.

Sec. 5. A contract for maintenance of local service roads and trails that is for $25,000 or more entered into by the state and a contract for maintenance of local service roads and trails that is for $25,000 or more for which state money is to be used entered into by a local government is required to be awarded in accordance with the bidding requirements and preferences of AS 37.05.230(1).

Sec. 6. The Department of Transportation and Public Facilities is required to award a public works construction contract in accordance with bidding requirements if the contract is $50,000 or more. Existing law requires the department to award a contract in accordance with bid requirements only if it exceeds $100,000. The reference to AS 44.33.300 is deleted, since that section allows a waiver only if the contract is less than $50,000 and by its terms it would not apply to contracts awarded for $50,000 or more.

Sec. 7. The Department of Transportation and Public Facilities is required to award a contract for maintenance of a public works project in accordance with bidding requirements if the contract is $25,000 or more. It is discretionary with the department whether to award smaller contracts in accordance with bidding requirements. The department may not award contracts in smaller increments to avoid the bidding requirements. These are new provisions.

Sec. 8. The Department of Transportation and Public Facilities is required to comply with the bidding requirements and preferences of AS 37.05.230(1) in awarding a contract for a public works project that is subject to bid requirements. Existing law only requires the department to award a contract to the lowest responsible bidder.

Sec. 9. A municipality or regional educational attendance area is required to comply with the bidding requirements and

preferences of AS 37.05.230(1) in awarding a contract for a public works project assumed from the Department of Transportation and Public Facilities if the amount of state money to be used on the project is $50,000 or more.

Sec. 10. Subject to certain bidding preferences added by this bill, a bid shall be awarded by the Department of Administration to an Alaska bidder if his bid is not more than 10 percent higher than the bid of the lowest nonresident and he is on the certified Alaska bidders list. Existing law requires a bid to be awarded to an Alaska bidder if his bid is not more than five percent higher and makes no provision for a bidders list.

Sec. 11. Existing law provides that competitive bids are not required for sales involving fair trade items or when materials for use in laboratory and experimental studies may be purchased otherwise to the best advantage of the state. These two exceptions to the bid requirements have been deleted.

Sec. 12. A contract shall be awarded to a bidder on the certified minority bidders list under certain conditions, including a requirement that during the prior fiscal year a proportionally smaller dollar amount of contracts were awarded to minority bidders compared to the population of minority people in the state, that the bid not be more than 15 percent higher than the lowest bid, that the minority bidder agrees to lower his bid by five percent or match the lowest bid. This preference applies only to contracts of $1,000,000 or less. A contract shall be awarded to a bidder on the certified women bidders list under similar conditions as those applied to the minority bidders preference, except that during the prior fiscal year women bidders must have received less than 10 percent of the value of contracts of $1,000,000 or less awarded for the preference to apply. A contract shall be awarded to a bidder on the certified Viet Nam veterans bidders list under similar conditions as those applied to minority bidders preference, except that during the prior fiscal year Viet Nam veterans must have received less than five percent of the value of contracts of $1,000,000 or less awarded for the preference to apply. If two or more bidders qualify for a minority bidders, women bidders, or Viet Nam veterans bidders preference a contract shall be awarded to the lowest of the bidders. These are new provisions.

Sec. 13. The Department of Administration is required to solicit bids by sending notices to all bidders on the certified Alaska bidders list and the department may limit solicitation of bids. Under existing law the department is required to send notices to known active prospective bidders and the department is not authorized to limit solicitation of bids.

Sec. 14. A contract for $50,000 or more for the operation of a transportation system for students is subject to competitive bid requirements. Under existing law this type of contract is exempt from the bid requirements.

Sec. 15. Besides the requirements of existing law, to qualify as an Alaska bidder a person may not be delinquent in the payment of state taxes and must maintain inventories or facilities in support of business activities in the state.

Sec. 16. The bidding preferences do not apply to contracts that are less than $50,000 of the Department of Transportation and Public Facilities. Under existing law the Alaska bidders preference does not apply to contracts that exceed $5,000.

Sec. 17. A contract for $50,000 or more for products or services of a sheltered workshop operating in the state is subject to competitive bid requirements. Under existing law this type of contract is exempt from the bid requirements.

Sec. 18. The Department of Administration is required to compile and update a certified Alaska bidders list, a certified minority bidders list, a certified women bidders list, and a certified Viet Nam veterans bidders list. To qualify for a certified list, other than the Alaska bidders list, a person must be on the certified Alaska bidders list and have a business with at least 85 percent of its interest beneficially owned or 85 percent of its voting interest owned by the type of person for which the preference is granted. In addition, the daily operations of the business must be controlled by the type of person for which the preference is granted. The bidders preferences do not apply to contracts involving federal money if the application of a bidding preference would violate federal law or program guidelines. These are new provisions.

Sec. 19. Except for the bidding preferences of AS 37.05.-230, a contract for which competitive bids are required shall be awarded by the Department of Administration to the lowest responsible bidder. Under existing law there is a preference for Alaska bidders only.

Sec. 20. A prime contractor must name the principal subcontractors he intends to use when submitting a bid. After a bid is awarded the subscontractors may be changed only for cause. "Principal subcontractor" is defined. This is a new provision.

Sec. 21. At least 20 percent of the money under a contract awarded through the competitve bid process shall be paid to subcontractors on the certified minority bidders list, certified women bidders list, or certified Viet Nam veterans bidders list unless no subcontractor on those lists is available. A prime contractor must identify subcontractors on the lists that he intends to use when submitting his bid. These are new provisions.

Sec. 22. If a bid is awarded under the competitive bid requirements, a proposed substitution for a subcontractor named in the bid shall be submitted to the Department of Administration for approval. This is a new provision.

Sec. 23. The Department of Administration is required to prepare a report on contracts awarded in accordance with a bidders preference for minority bidders, women bidders, or Viet Nam veterans bidders by state agencies, the University of Alaska, municipalities, and other entities. The report shall be submitted to the Senate State Affairs Committee and the House State Affairs Committee. This is a new provision.

Sec. 24. If the amount of state money used to finance a contract of the University of Alaska is $50,000 or more the competitive bidding and preference provisions of AS 37.05.-230(1) apply. This is new.

Sec. 25. If the amount of state money used to finance a contract of a non-profit corporation is $50,000 or more, the bidding and preference provisions of AS 37.05.230(1) apply. This is new.

Sec. 26. To qualify for receipt of a grant, a municipality must comply with the bidding and preference provisions of AS 37.05.230(1) in the award of a contract if $50,000 or more of the contract is financed with the grant or other state money. This is a new requirement.

Sec. 27. To qualify for receipt of a grant, a named recipient must comply with the bidding and preference provisions of AS 37.05.230(1) in the award of a contract if $50,000 or more of the contract is financed with the grant or other state money. This is a new requirement.

Sec. 28. In the awarding of a contract to an entity in an unincorporated community the Department of Community and Regional Affairs must determine if there is an incorporated entity that will agree, along with other things required by existing law, to award any contract of $50,000 or more financed by the grant in accordance with the bidding and preference provisions of AS 37.05.230(1).

Sec. 29. Technical amendments are made to the section providing for a waiver of provisions regarding public contracts in an area impacted by an economic disaster so that citations are to sections dealing with contracts of under $50,000.

Sec. 30. The bill is effective July 1, 1982.

TBC:ljb

Official Business

Alaska State Legislature

Senate Committee on State Affairs

Vic Fischer, Chairman • Pouch V • Juneau, Alaska 99811 • (907) 465-4954

3/18/82

REVISED

SENATE STATE AFFAIRS COMMITTEE SCHEDULE

TUESDAY
March 23
1:30 pm

Bill	Subject
✓ SB 45	Surety bonding exemptions
✓ SB 414	Small Contractor Surety Bonding Corp.
✓ SB 415	Contracting, procurement and competitive bidding
✓ SR 23 —	[Study of contracting for state services]
✓ SCR 50 —	[Delivery of state services]
✓ SB 865	Award of state contracts to minority groups
✓ SB 866 —	[Appropriation for study of state contracting]
SB 821 (handwritten)	
✓ SB 867	Incentive to hire older Alaskans
✓ { SB 868	Committee on Employment and Productivity
SB 869	Recordkeeping requirements for surety insurers

THURSDAY
March 25
1:30 pm Further consideration of bills listed above

Committee meetings will be conducted in the Senate State Affairs Committee Room, 423 Capitol.

COMPLETE COVERAGES FOR YOUR COMMERCIAL AND PERSONAL NEEDS

Pate Insurance Agency, Inc.

P.O. BOX 257 • HOMER, ALASKA 99603
PHONE [illegible]
TELEX [illegible]

April 23, 1981

The Honorable Senators
Fischer and Stimson
The State Senate
Juneau, Alaska

Re: Senate Bills 414, 415

Dear Senators Fischer and Stimson:

It was with great interest that I read the above captioned bills. Unfortunately, I was out of the state during the teleconference which was recently held to discuss the presentations; however, after reviewing the conference with some of those who were in attendence, there are a couple of points I would like to bring to your attention.

I don't think that anyone invoved in the bonding markets in this state can deny the fact that there is a real problem currently for the contractor attempting to operate in the $0 to $500,000 range of bidding. In most instances contractors operating on jobs that require bonds in excess of $500,000 already have standard bonding [illegible] secured; however, even in these areas there is sometimes [illegible]ity. The current SBA market is simply not responsive to the needs of our local contractors. Their current restrictions are not realistic. The service which is generally provided is neither prompt nor professional. And, their general approach seems geared to contractors operating in the southern 48 states, but, allows little regard for the seasonal type of contracting that is done in Alaska.

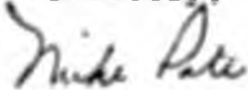
I am extremely hesitant to recommend that the State become involved in any insurance practices. Certainly bonding is an area of insurance that requires a great deal of care and expertise. However, if it were possible for the State to establish a specific fund to secure performance bonds for contractors operating in the $0 to $500,000 range, and then utilize the existing insurance expertise available through local agents licensed to do business in this state, I believe that a realistic program could be developed that would not only solve the needs of our contractors, but also, avoid the State's intrusion on an area traditionally controlled by private enterprise. After all, the SBA is now guaranteeing 80% of most existing bonding. Why can't the State assume this position and guarantee 100% of the bonding?

It would naturally be extremely important that this program be monitored very closely, and that there be definite guidelines that would have to be followed.

I believe that you are in a position to tailor a specific program to meet a very obvious need. After all, it is the small contractors of this state that provide the backbone of our construction industry, and they certainly deserve our consideration. I would appreciate hearing from you further on this matter, and will most anxiously watch both of these bills as they work their way through committees.

Thank you for your time and consideration.

Sincerely,



J. Michael Pate

JMP/bam

THE LEGISLATURE OF THE STATE OF ALASKA
TWELFTH LEGISLATURE

FISCAL NOTE

REVISED

I. REQUEST

Bill/Resolution No. SB 415

Title An Act Relating to Contracting and Procurement Procedure...

Requested by Fischer & Stimson Date April 23, 1981

II. FISCAL DETAIL

Agency Affected Department of Administration

Program Category Affected General Government

BRU, Program, or Subprogram(s) Affected General Services - Administrative Services

(Note If more than one budget component is affected, separate line-item amounts and funding for each component in the analysis section.)

EXPENDITURES (Thousands of Dollars)

	FY 81	FY 82	FY 83	FY 84	FY 85	FY 86
100 PERSONAL SERVICES		45.6	49.2	53.2	57.5	62.1
200 TRAVEL						
300 CONTRACTUAL		168.0	73.4	79.3	85.7	92.5
400 COMMODITIES		1.5	1.6	1.7	1.9	2.0
500 EQUIPMENT		3.6	3.9	4.2	4.5	4.9
600 LAND & STRUCTURES						
700 GRANTS, CLAIMS, ETC						
TOTAL		218.7	128.1	138.4	149.6	161.5

FUNDING (Thousands of Dollars)

	FY 81	FY 82	FY 83	FY 84	FY 85	FY 86
GENERAL FUND		218.7	128.1	138.4	149.6	161.5
FEDERAL FUNDS						
OTHER (Specify Fund Source)						

POSITIONS

	FY 81	FY 82	FY 83	FY 84	FY 85	FY 86
FULL TIME		2	2	2	2	2
PART TIME						
TEMPORARY						

III. ANALYSIS (See Fiscal Note Preparation Instructions, Section III)

The contractu services expenditures includ computerization and implementation of the required certified lists. It also includes funds to revise and reprint existing pamphlets and brochures to reflect statuary changes and to conduct advertising to inform minority businesses of the new regulations.

IV. DATE April 23, 1981 PREPARED BY George Elgee

AGENCY Department of Administration

PHONE 465-2250

Original Legislative Finance

cc Budget and Management

Prime Sponsor (Full Legislator Named) Fischer

33-001 (Rev. 12/80)

	POSITION TITLE				RANGE/STEP	BARG. UNIT.	LOCATION	GOV.	APPROV.	DISAPP.
1	Administrative Support Technician II				8B	G	Juneau			
2	TYPE OF POSITION: PFT	STAFF MONTHS: 12	RP No.	PCN No.	PRIORITY		FORM 12 PAGE/LINE	LEG.		

	TYPE OF EXPENDITURE		AMOUNT
3	1	2	3
4	PERSONAL SERVICES: SALARY 1,433/mo.	17,196	
5	BENEFITS .1579	2,715	
6	FICA .0613	1,054	
7	HEALTH INS. 150 x 12	1,800	
8	TOTAL PERSONAL SERVICES	01	22.8
9	TRAVEL	02	
10	CONTRACTUAL	03	3.0
11	COMMODITIES	04	.5
12	EQUIPMENT	05	1.8
13	OTHER		
14	TOTAL COST		28.1

	CODE	FUNDING SOURCE	
15		FED RCPTS. 1002	
16		GF MATCH. 1003	
17		GEN FUND 1004	
18	902	I-A RCPTS 1007	28.1
19		PGM RCPTS 1008	
20		OTHER	
21	CONTINUATION		
22	ADDITION		

FOR B&M USE ONLY

4A KEY NUMBER ______ ______ COLUMN NO. ______

JUSTIFICATION:

The purchasing section is presently backlogged. There is no flexibility to assume further requirements.

This position will evaluate applications for the two lists, update listing, review requirements for preferences, and maintain minority purchase records. In addition they will provide copies and updates of the certified lists to other groups covered by the legislation. They will also complete the additional standard clerical tasks necessitated by adding new groups on interested parties to the system and involving more complex and time consuming bid awards.

AGENCY ______ PROGRAM ______

BRU ______

COMPONENT ______

13 REQUEST FOR NEW POSITION

Page ____ of ____

REVISED DATE ______

FY 82

	POSITION TITLE				RANGE/STEP	BARG. UNIT.	LOCATION		APPROV.	DISAP.
1	Clerk Typist III				8B	G	Anchorage	GOV.		
2	TYPE OF POSITION: PFT	STAFF MONTHS: 12	RP No.	PCN No.	PRIORITY		FORM 12 PAGE/LINE	LEG.		

	TYPE OF EXPENDITURE		AMOUNT
3	1	2	3
	PERSONAL SERVICES:		
4	SALARY 1,433/mo.	17,196	
5	BENEFITS .1579	2,715	
6	FICA .0613	1,054	
7	HEALTH INS. 150 x 12	1,800	
8	TOTAL PERSONAL SERVICES 01		22.8
9	TRAVEL 02		
10	CONTRACTUAL 03		4.0
11	COMMODITIES 04		1.0
12	EQUIPMENT 05		1.8
13	OTHER		
14	TOTAL COST		29.6

	CODE	FUNDING SOURCE	
15		FED RCPTS. 1002	
16		GF MATCH. 1003	
17	100	GEN. FUND 1004	29.6
18		I-A RCPTS. 1006	
19		PGM RCPTS 1029	
20		OTHER	
21	CONTINUATION		
22	ADDITION		

FOR B&M USE ONLY

4A KEY NUMBER ______ COLUMN NO. ______

JUSTIFICATION:

The purchasing section is presently backlogged. There is no flexibility to assume further requirements.

This position will evaluate applications for the two lists, update listing, review requirements for preferences, and maintain minority purchase records. In addition they will provide copies and updates of the certified lists to other groups covered by the legislation. They will also complete the additional standard clerical tasks necessitated by adding new groups on interested parties to the system and involving more complex and time consuming bid awards.

AGENCY Administration

PROGRAM Centralized Administrative Services

BRU General Services

COMPONENT Purchasing

13 REQUEST FOR NEW POSITION.

Page ____ of ____

REVISED DATE ______

FY 82

THE LEGISLATURE OF THE STATE OF ALASKA
TWELFTH LEGISLATURE

FISCAL NOTE

REVISED

I. REQUEST
Bill/Resolution No. SB 415
Title A Act Relating to Contracting and Procurement Procedure...
Requested by Fischer & Stimson Date April 23, 1981

II. FISCAL DETAIL
Agency Affected All
Program Category Affected All
BRU, Program, or Subprogram(s) Affected All
(Note: If more than one budget component is affected, separate line-item amounts and funding for each component in the analysis section.)

EXPENDITURES (Thousands of Dollars)

	FY 81	FY 82	FY 83	FY 84	FY 85	FY 86
100 PERSONAL SERVICES						
200 TRAVEL						
300 CONTRACTUAL						
400 COMMODITIES						
500 EQUIPMENT						
600 LAND & STRUCTURES						
700 GRANTS, CLAIMS, ETC.						
*** Additional Costs of Goods & Services		5,500.0	5,940.0	6,415.2	6,298.4	7,482.7
TOTAL						

FUNDING (Thousands of Dollars)

	FY 81	FY 82	FY 83	FY 84	FY 85	FY 86
GENERAL FUND		5,500.0	5,940.6	6,415.2	6,298.4	7,482.7
FEDERAL FUNDS						
OTHER (Specify Fund Source)						

POSITIONS

	FY 81	FY 82	FY 83	FY 84	FY 85	FY 86
FULL TIME						
PART TIME						
TEMPORARY						

III. ANALYSIS (See Fiscal Note Preparation Instructions, Section III)

The exact fiscal impact of this bill is difficult to analyze due to lack of sufficient data to evaluate vendor response to changes in purchasing preferences. Some out of state vendors will drop out of bidding thereby reducing competition and providing increased prices. We project increased costs of goods and service to be approximately 10%* for FY 82 and we assume state expenditures will increase 8% a year. We feel both are conservative estimates.

The increased costs which we have identified will have to be absorbed by each individual agency. This fiscal note is not a request for an additional appropriation to the Department of Administration or any other Department but reflects what we estimate the costs that this bill could be to all state agencies. This will be reflected in their reduced purchasing capabilities. Agencies will either find additional funding within their existing budgets or procure less goods and services or in some cases not procure those goods at this time and submit larger budget requests in future years.

IV. DATE April 23, 1981 PREPARED BY George Elgee
AGENCY Department of Administration
PHONE 465-2250

Original: Legislative Finance
cc: Budget and Management
Prime Sponsor (First Legislator Named) Fischer

33-001 (Rev. 12/80)

*** (The National Association of State Purchasing Officials, who oppose any local preference statutes, estimate that a bidder's preference raises the cost of doing business proportionate with the preference.)

From a purely professional purchasing standpoint vendor preferences are not condusive to good purchasing practice nor in the purchaser's best interest. We are sympathetic to the idea of stimulating various sectors of business, however we do not believe this is the correct vehicle. A vendor preference is a weak and easy approach to the problem which will not solve it. The preference is little more than a token gesture of appeasement to an interest group. Open competition is the backbone of our free market system. To reduce or eliminate it adversely affects everyone.

PURCHASING PREFERENCES

PRO's

- New jobs are created.
- Businesses are encouraged to locate within the State.

CON's

- Arguably unconstitutional as a barrier to interstate commerce.
- In direct conflict with the principles of competition and precludes the purchaser from obtaining the best competitive price.
- Many bidders who otherwise would be interested are discouraged from competing and potential sources of supply are reduced.
- Preferred bidders feel more secure and have less incentive to submit their best prices when a free competitive market is absent.
- Results in higher costs to taxpayers, prices usually are increased by the amount of the preference.

Sec. 44.33.285. Action by governor. The governor may, upon recommendation of the commissioner of commerce and economic development, designate by proclamation an area as an area impacted by an economic disaster. When an area is so designated, assistance grants shall be made by the Department of Commerce and Economic Development as provided in AS 37.11.100 and the governor may recommend in his budget submission that capital projects planned for the area be accelerated and that new projects be funded for the area. The proclamation may provide that waivers of capital projects requirements, as authorized in AS 44.33.300, become effective only to the extent set out in the proclamation. (§ 1 ch 277 SLA 1976)

Sec. 44.33.290. Employment preference. (a) In the performance of contracts awarded by the state in an area impacted by an economic disaster, residents of the area shall be employed where they are available and qualified so that the economic effects of alleviating the disaster will be maximized. If resident labor is not available, the contractor shall inform the Department of Labor of the number of additional workers needed, the positions to be filled, and the efforts made at recruitment in the area. If the Department of Labor is satisfied that a good faith effort has been made by the contractor to hire residents of the area, it may issue a certificate allowing other hire for designated positions. A clause requiring these provisions shall be part of each state contract awarded.

(b) Wages paid for employment under this section shall be in conformance with the minimum rates of pay schedule published by the Department of Labor in accordance with AS 36.05.030. (§ 1 ch 277 SLA 1976)

Sec. 44.33.295. Contractors' preference. If the department determines that there are contractors in an area designated as an area impacted by an economic disaster and who are qualified to perform a contract, preference to the extent feasible shall be given to those contractors under regulations adopted by the department. (§ 1 ch 277 SLA 1976)

Sec. 44.33.300. Waiver of certain provisions. When the governor has by proclamation declared an area impacted by an economic disaster, the following provisions regarding public contracts may be waived to the extent specified in the proclamation:

(1) the requirement of a contractor's bond as prescribed in AS 36.25.010 may be waived if the contract amount does not exceed $100,000;

(2) the public bid requirements as contained in AS 19.10.170, 19.10.190, 19.30.191(b), and AS 35.15.010 — 35.15.030 may be waived if the contract is to be performed by a contractor whose principal office is in the designated area and the contract amount does not exceed $50,000;

(3) the general policy to require all construction to be under bid contract as contained in AS 35.15.010 may be waived if the contract is to be performed by the state, another governmental entity, or a nonprofit entity. (§ 1 ch 277 SLA 1976)

Sec. 44.33.305. Regulations. The department, after consultation with the Department of Labor, may adopt regulations to implement AS 44.33.285 — 44.33.310. (§ 1 ch 277 SLA 1976)

Sec. 44.33.310. Definitions. In AS 44.33.285 — 44.33.310,

(1) "base period" means any 10 years after 1950, not necessarily continuous, and if the economic disaster is caused by a fisheries failure the period shall consist of years during which a fishery produced at economically representative levels as determined by the Department of Fish and Game;

(2) "department" means the Department of Commerce and Economic Development;

(3) "economic disaster" means that the annual income to workers in the designated area dropped below the average annual income for the base period for workers in the designated area and the drop in income is of such magnitude that the average family income of all residents of the designated area as determined by the department is below the Federal Social Security Administration Poverty Guideline, adjusted by the department to reflect subsistence economic patterns and appropriate cost-of-living differentials; the availability of alternate employment shall be considered in determining whether an economic disaster has occurred under this paragraph. (§ 1 ch 277 SLA 1976)

Article 8. Residential Care Facility Revolving Loan Fund.

Section
320. Residential care facility revolving loan fund
330. Powers and duties of the department in administering the fund
340. Purpose of loans

Section
350. Loan terms
360. Eligibility for loans
370. Sale or transfer of mortgages and notes
380. Definitions

Sec. 44.33.320. Residential care facility revolving loan fund. There is established in the Department of Commerce and Economic Development a residential care facility revolving loan fund to carry out the purposes of AS 44.33.320 — 44.33.380. The fund may be used for no other purpose. (§ 6 ch 153 SLA 1978)

Sec. 44.33.330. Powers and duties of the department in administering the fund. (a) The department may

(1) make loans for the construction, renovation, and equipping of residential care facilities;

(2) promulgate regulations necessary to carry out the provisions of AS 44.33.320 — 44.33.380.

THE LEGISLATURE OF THE STATE OF ALASKA
TWELFTH LEGISLATURE

FISCAL NOTE

I. REQUEST
Bill/Resolution No. SB 415
Title An Act relating to contracting and procurement procedures
Requested by ______ Date April 14, 1981

II. FISCAL DETAIL
Agency Affected Department of Community and Regional Aff[illegible]

(Note: If more than one budget component is affected, separate line-item amounts and funding for each component in the analysis section.)

EXPENDITURES (Thousands of Dollars)

	FY 81	FY 82	FY 83	FY 84	FY 85	FY 86
100 PERSONAL SERVICES		-0-				
200 TRAVEL		-0-				
300 CONTRACTUAL		-0-				
400 COMMODITIES		-0-				
500 EQUIPMENT		-0-				
600 LAND & STRUCTURES		-0-				
700 GRANTS, CLAIMS, ETC.		-0-				
TOTAL		-0-				

FUNDING (Thousands of Dollars)

	FY 81	FY 82	FY 83	FY 84	FY 85	FY 86
GENERAL FUND		-0-				
FEDERAL FUNDS		-0-				
OTHER (Specify Fund Source)		-0-				

POSITIONS

	FY 81	FY 82	FY 83	FY 84	FY 85	FY 86
FULL TIME		-0-				
PART TIME						
TEMPORARY						

III. ANALYSIS (See Fiscal Note Preparation Instructions, Section III)

No fiscal impact on this agency.

IV. DATE April 14, 1981 PREPARED BY Terry L. Earley
AGENCY Department of Community & Regional Affairs
PHONE 465-4730

Original: Legislative Finance
cc: Budget and Management
Prime Sponsor (First Legislator Named)

DOTPF

1976-1978 Prime Contracts

[vi]sion	Total $ Awarded	Total $ Awarded to MBE's	M.B.E. % Participation
[hig]hways	229,573,793	7,278,265	3.2%
[...]l Design & Construction	69,367,851	2,008,027	2.9%
[...]tion	64,406,589	2,377,990	3.7%
[Har]bors & Waterways	10,917,443	4,231,711	38.8%
[Tot]al	374,265,676	15,895,993	4.2%

M.B.E. participation figure for the 3 main contracting divisions, excluding Harbors & Waterways, is 3.2%.

THE LEGISLATURE OF THE STATE OF ALASKA
TWELFTH LEGISLATURE

FISCAL NOTE

I. REQUEST
Bill/Resolution No. * SB 415
Title An Act Relating to Contracting and Procurement Procedure...
Requested by Fischer & Stimson Date April 10, 1981

II. FISCAL DETAIL
Agency Affected All
Program Category Affected All
BRU, Program, or Subprogram(s) Affected All
(Note: If more than one budget component is affected, separate line-item amounts and funding for each component in the analysis section.)

EXPENDITURES (Thousands of Dollars)

	FY 81	FY 82	FY 83	FY 84	FY 85	FY 86
100 PERSONAL SERVICES		45.6	49.2	53.2	57.5	62.1
200 TRAVEL						
300 CONTRACTUAL		168.0	73.4	79.3	85.7	92.5
400 COMMODITIES		1.5	1.6	1.7	1.9	2.0
500 EQUIPMENT		3.6	3.9	4.2	4.5	4.9
600 LAND & STRUCTURES						
700 GRANTS, CLAIMS, ETC.						
* Additional Costs for Goods & Services		5,500,000	5,940,000	6,415,200	6,928,416	7,482,689
TOTAL						

FUNDING (Thousands of Dollars)

	FY 81	FY 82	FY 83	FY 84	FY 85	FY 86
GENERAL FUND		5,500,000	5,940,000	6,415,200	6,928,416	7,482,689
FEDERAL FUNDS*						
OTHER (Specify Fund Source)						

POSITIONS

	FY 81	FY 82	FY 83	FY 84	FY 85	FY 86
FULL TIME		2	2	2	2	2
PART TIME						
TEMPORARY						

III. ANALYSIS (See Fiscal Note Preparation Instructions, Section III)

The exact fiscal impact of this bill is difficult to analyze due to lack of sufficient data to evaluate vendor response to changes in purchasing preferences. Some out of state vendors will drop out of bidding thereby reducing competition and providing increased prices. We project increased costs of goods and service to be approximately 10%* for FY 82 and we assume state expenditures will increase 8% a year. We feel both are conservative estimates.

The contractual services expenditures include computerization and implementation of the required certified lists. It also includes funds to revise and reprint existing pamphlets and brochures to reflect statuary changes and to conduct advertising to inform minority businesses of the new regulations.

IV. DATE April 20, 1981 PREPARED BY George Elgee
AGENCY Department of Administration
PHONE 465-2250

Original: Legislative Finance
cc: Budget and Management
Prime Sponsor (First Legislator Named)

001 (Rev. 12/80)

* (The National Association of State Purchasing Officials, who oppose any local preference statutes, estimate that a bidder's preference raises the cost of doing business proportionate with the preference.)

From a purely professional purchasing standpoint vendor preferences are not condusive to good purchasing practice nor in the purchaser's best interest. We are sympathetic to the idea of stimulating various sectors of business, however we do not believe this is the correct vehicle. A vendor preference is a weak and easy approach to the problem which will not solve it. The preference is little more than a token gesture of appeasement to an interest group. Open competition is the backbone of our free market system. To reduce or eliminate it adversely affects everyone.

PURCHASING PREFERENCES

PRO's

- New jobs are created.
- Businesses are encouraged to locate within the State.

CON's

- Arguably unconstitutional as a barrier to interstate commerce.
- In direct conflict with the principles of competition and precludes the purchaser from obtaining the best competitive price.
- Many bidders who otherwise would be interested are discouraged from competing and potential sources of supply are reduced.
- Preffered bidders feel more secure and have less incentive to submit their best prices when a free competitive market is absent.
- Results in higher costs to taxpayers, prices usually are increased by the amount of the preference.

	POSITION TITLE				RANGE/STEP	BARG. UNIT.	LOCATION	GOV	APPROV	DISAPP.
1	Clerk Typist III				8B	G	Anchorage			
2	TYPE OF POSITION PFT	STAFF MONTHS 12	RP No.	PCN No.	PRIORITY		FORM 12 PAGE/LINE	LEG.		

	TYPE OF EXPENDITURE		AMOUNT
3	1	2	3
	PERSONAL SERVICES:		
4	SALARY 1,433/mo.	17,196	
5	BENEFITS .1579	2,715	
6	FICA .0613	1,054	
7	HEALTH INS. 150 x 12	1,800	
8	TOTAL PERSONAL SERVICES 01		22.8
9	TRAVEL 02		
10	CONTRACTUAL 03		4.0
11	COMMODITIES 04		1.0
12	EQUIPMENT 05		1.8
13	OTHER		
14	TOTAL COST		29.6

	CODE	FUNDING SOURCE	
15		FED RCPTS. 1002	
16		GF MATCH. 1003	
17	100	GEN. FUND 1004	29.6
18		I-A RCPTS. 1007	
19		PGM RCPTS 1008	
20		OTHER	
21	CONTINUATION		
22	ADDITION		

FOR B&M USE ONLY

4A KEY NUMBER ________ COLUMN NO. ____

JUSTIFICATION:

The purchasing section is presently backlogged. There is no flexibility to assume further requirements.

This position will evaluate applications for the two lists, update listing, review requirements for preferences, and maintain minority purchase records. In addition they will provide copies and updates of the certified lists to other groups covered by the legislation. They will also complete the additional standard clerical tasks necessitated by adding new groups on interested parties to the system and involving more complex and time consuming bid awards.

AGENCY Administration

PROGRAM Centralized Administrative Services

BRU General Services

COMPONENT Purchasing

13 REQUEST FOR NEW POSITION.

Page____of____

REVISED DATE ______

FY 82

	POSITION TITLE			RANGE/STEP	BARG. UNIT.	LOCATION	GOV.	APPROV.	DISAPP.
1	Administrative Support Technician II			8B	G	Juneau			
2	TYPE OF POSITION: PFT	STAFF MONTHS: 12	RP No.	PCN No.	PRIORITY	FORM 12 PAGE/LINE	LEG.		

3	TYPE OF EXPENDITURE		AMOUNT
	1	2	3
4	PERSONAL SERVICES: SALARY 1,433/mo.	17,196	
5	BENEFITS .1579	2,715	
6	FICA .0613	1,054	
7	HEALTH INS. 150 x 12	1,800	
8	TOTAL PERSONAL SERVICES	01	22.8
9	TRAVEL	02	
10	CONTRACTUAL	03	3.0
11	COMMODITIES	04	.5
12	EQUIPMENT	05	1.8
13	OTHER		
14	TOTAL COST		28.1

	CODE	FUNDING SOURCE	
15		FED RCPTS. 1002	
16		MATCH. 1003	
17		GEN. FUND 1004	
18	902	I-A RCPTS. 1007	28.1
19		PGM RCPTS 1005	
20		OTHER	
21	CONTINUATION		
22	ADDITION		

FOR B&M USE ONLY

KEY NUMBER ______ COLUMN NO. ______

JUSTIFICATION:

The purchasing section is presently backlogged. There is no flexibility to assume further requirements.

This position will evaluate applications for the two lists, update listing, review requirements for preferences, and maintain minority purchase records. In addition they will provide copies and updates of the certified lists to other groups covered by the legislation. They will also complete the additional standard clerical tasks necessitated by adding new groups on interested parties to the system and involving more complex and time consuming bid awards.

AGENCY Administration

PROGRAM Centralized Administrative Services

BRU General Services

COMPONENT Purchasing

Page ____ of ____

REVISED DATE ______

13 REQUEST FOR NEW POSITION

FY 82

PLEASE NOTE: THE FOLLOWING PAGES WERE TREATED AS A UNIT IN THE ORIGINAL DOCUMENT

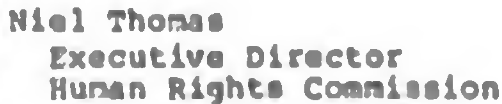
MEMORANDUM State of Alaska

TO: Senator Vic Fischer

DATE: April 20, 1981

FILE NO:

TELEPHONE NO:



FROM: Niel Thomas
Executive Director
Human Rights Commission

SUBJECT: Minority/Female Business Enterprise Legislation
SB415

Here is a package of materials prepared in anticipation of your State Affairs Committee session on April 21. These are the materials we promised you during the committee hearing on April 16 to implement several recommendations we discussed in our testimony.

<u>Preamble and Findings</u>

We suggested that remedial legislation of this type can be insulated from legal challenges based on a reverse discrimination theory by having the legislative body make clear the problem for which it is providing a remedy. One way to do this is with a preamble in the bill in which the legislature makes specific findings. Attachment A is draft language, largely taken from a bill we saw in an earlier legislative session, which you might like to use for ideas. You will have to fill in specific details, and, as will be seen below, include findings with respect to female business enterprises also. If you wish to compare with census data you can refer to the preliminary 1980 data showing that approximately 25% of the Alaska population is now composed of minority people.

The Committee could also consider releasing a report with findings upon which Alaska's courts can review and rely on for legislative intent. I know that certain kinds of reports are used by courts this way in Alaska and certain other kinds of reports are not. You should consult with the legislature's advisors about the form such a report must take in order to be respected by courts as legislative intent.

Attachment B is a copy of the <u>Fullilove</u> decision in which the Supreme Court analyzed similar federal legislation. We have highlighted both the standards which the Supreme Court used in reviewing the legislation and the specific findings which the Congress made. I am calling these to your attention to acquaint your staff with the principles which courts apply in looking at this type of legislation, and to give some further examples of the types of substan-

tive findings which a legislative body can make as a justification for adopting legislation of this type.

One comment in the Fullilove decision noted that the legislation was acceptable because it was limited in scope and duration. You could provide for this by including a sunset provision in the bill. We suggest a sunset review after five years, but not less.

Female Business Enterprises (FBE's)

We suggested, with the apparent concurrence of Senator Stinson, that businesses owned and operated by females should also be included in this bill on the theory that these businesses have experienced many of the types of problem of discrimination which minority business enterprises face. We suggested that to the extent that FBE's are included, however, the goals for them must be set separately from the goals for minority business enterprises. Otherwise, as the federal experience has indicated, there is a substantial risk that goals for a combined FBE/MBE group will be consumed nearly exclusively by the FBE's to the disadvantage of the minority firms. Attachment C is paste-up of the existing bill with our suggested revisions. As you can see, we have suggested a 10% goal for the FBE's which operates independently of the existing 20% goal for MBE's.

Here is a hypothetical which demonstrates how this system would work. Suppose the low bidder was a white male owned firm which bids a job at $100. The FBE bid is $114 and the MBE $115. If the 10% goal for that fiscal year for FBE's has not been achieved, the FBE gets the job because it falls within the 15% bidders preference and is lower than MBE bid. If the FBE goal has been reached by that time, the MBE would get the job. (The FBE would have had to bid it at $99 to get it if the FBE goal had been met at that time.) In other words, the FBE and MBE's compete with each other until the goal for either has been reached. At that point, each of these groups competes on an equal footing with no bid preference as against other firms.

Definition of MBE's/FBE's

We suggested that the existing definition of MBE's be amended to add to the qualification standard the requirement that the firm be managed by minority people (or, in the case of FBE's, by females) or

. be on its way toward that objective through an acceptable affirmative action plan. We have suggested language in the paste up draft of Attachment C.

You will notice that we have not tried to go to great length in the legislation to define the details of how this should work, beyond articulating the principle. These details strike us as something which should be left to the Administration to provide for by regulation. We have also inserted the suggestion made by others that the qualification program be administered by the principal department which lets the contracts, the Department of Transportation, instead of Administration.

If you or any of your staff have any questions of us during your session on April 21 we will be available in Anchorage at 276-7474.

SUGGESTED PREAMBULARY LANGUAGE FOR MINORITY
and
FEMALE BID PREFERENCE PROVISIONS OF SB 415.

LEGISLATIVE FINDINGS. Reliable testimony indicates and the legislature finds that

(1) the Alaska minority and female business communities suffer economic distress because they receive a disproportionately low percentage of contracts awarded by the state;

(2) while minorities comprise 25% of Alaska's population according to current 1980 census figures, the most recent data from the Executive Branch indicates that less than _____% of State contract dollars was realized by minority business concerns. Despite the increasing interest among women in owning and operating their own businesses, less than _____% of State contract dollars was realized by female-owned and operated business concerns;

(3) these inequities contribute to the high rate of unemployment in the minority community, and to underemployment among women;

(4) these inequities limit the aspirations of minority and female children to become leaders in business, government, and service to all people;

(5) the disproportinately high unemployment among minority and female workers can be reduced through the awarding of state contracts to minority and female businesses; and

(6) it is in the public interest that the principles relating to the encouragement of minority enterprise embodied in the Public Works Employment Act of 1977, P. L. 95-28, be extended to all procurement by the State in order to place minority and female businesses on a more equitable footing with respect to State contracting opportunities.

The United States

LAW WEEK

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OPINIONS ANNOUNCED JULY 2, 1980

The Supreme Court decided:

LABOR—Occupational Health

Decision by U.S. Court of Appeals for Fifth Circuit that Labor Secretary exceeded his standard-setting authority under Occupational Safety and Health Act by promulgating standard which limited permissible employee exposure to airborne concentrations of benzene to one part per million and which prohibited dermal contact with solutions containing benzene is affirmed. (Industrial Union Department, AFL-CIO v. American Petroleum Institute, Nos. 78-911 & 78-1036) page 5022

MEDIA LAW—Fair Trial Free Press

Press and public have right of access under First Amendment to attend criminal trials and may not be excluded from such trials merely upon agreement of trial judge and parties in absence of any findings sufficient to overcome presumption of open trials. (Richmond Newspapers, Inc., v. Virginia, No. 79-243) page 5008

PUBLIC WORKS—Federal Funding

"Minority business enterprise" provision of 1977 Public Works Employment Act, which provides that, absent administrative waiver, at least ten percent of any grant thereunder for local public works projects "shall be expended for minority business enterprises," does not violate equal protection guarantees of Constitution. (Fullilove v. Klutznick, No. 78-1007) page 4979

[illegible]

Full Text of Opinions

No. 78-1007

H. Earl Fullilove et al., Petitioners, *v.* Philip M. Klutznick, Secretary of Commerce of the United States, et al.	On Writ of Certiorari to the United States Court of Appeals for the Second Circuit.

[July 2, 1980]

Syllabus

The "minority business enterprise" (MBE) provision of the Public Works Employment Act of 1977 (1977 Act) requires that, absent an administrative waiver, at least 10% of federal funds granted for local public works projects must be used by the state or local grantee to procure services or supplies from businesses owned by minority group members, defined as United States citizens "who are Negroes, Spanish-speaking, Orientals, Indians, Eskimos, and Aleuts." Under implementing regulations and guidelines, grantees and their private prime contractors are required, to the extent feasible, in fulfilling the 10% MBE requirement, to seek out all available, qualified, bona fide MBE's, to provide technical assistance as needed, to lower or waive bonding requirements where feasible, to solicit the aid of the Office of Minority Business Enterprise, the Small Business Administration, or other sources for assisting MBE's in obtaining required working capital, and to give guidance through the intricacies of the bidding process. The administrative program, which recognizes that contracts will be awarded to bona fide MBE's even though they are not the lowest bidders if their bids reflect merely attempts to cover costs inflated by the present effects of prior disadvantage and discrimination, provides for handling grantee applications for administrative waiver of the 10% MBE requirement on a case-by-case basis if infeasibility is demonstrated by a showing that, despite affirmative efforts, such level of participation cannot be achieved without departing from the program's objectives. The program also provides an administrative mechanism to ensure that only bona fide MBE's are encompassed by the program, and to prevent unjust participation by minority firms whose access to public contracting opportunities is not impaired by the effects of prior discrimination.

Petitioners, several associations of construction contractors and subcontractors and a firm engaged in heating, ventilation, and air conditioning work, filed suit for declaratory and injunctive relief in Federal District Court, alleging that they had sustained economic injury due to enforcement of the MBE requirement and that the MBE provision on its face violated, *inter alia*, the Equal Protection Clause of the Fourteenth Amendment and the equal protection component of the Due Process Clause of the Fifth Amendment. The District Court upheld the validity of the MBE program, and the Court of Appeals affirmed.

Held: The judgment is affirmed.

584 F. 2d 600, affirmed.

Mr. Chief Justice Burger, joined by Mr. Justice White and Mr. Justice Powell, concluded that the MBE provision of the 1977 Act, on its face, does not violate the Constitution.

[illegible]

[illegible]

(1) Viewed against the legislative and administrative background of the 1977 Act, the legislative objectives of the MBE provision, and the administrative program thereunder, were to ensure—without mandating the allocation of federal funds according to inflexible percentages solely based on race or ethnicity—that, to the extent federal funds were granted under the 1977 Act, grantees who elected to participate would not employ procurement practices that Congress had decided might result in perpetuation of the effects of prior discrimination which had impaired or foreclosed access by minority businesses to public contracting opportunities.

(2) In considering the constitutionality of the MBE provision, it first must be determined whether the *objectives* of the legislation are within Congress' power.

(a) The 1977 Act, as primarily an exercise of Congress' spending power under Art. I, § 8, cl. 1, "to provide for the . . . general Welfare," conditions receipt of federal moneys upon the recipient's compliance with federal statutory and administrative directives. Since the reach of the spending power is at least as broad as Congress' regulatory powers, if Congress, pursuant to its regulatory powers, could have achieved the objectives of the MBE program, then it may do so under the spending power.

(b) Insofar as the MBE program pertains to the actions of private prime contractors, including those not responsible for any violation of antidiscrimination laws, Congress could have achieved its objectives under the Commerce Clause. The legislative history shows that there was a rational basis for Congress to conclude that the subcontracting practices of prime contractors could perpetuate the prevailing impaired access by minority businesses to public contracting opportunities, and that this inequity has an effect on interstate commerce.

(c) Insofar as the MBE program pertains to the actions of state and local grantees, Congress could have achieved its objectives by use of its power under § 5 of the Fourteenth Amendment "to enforce by appropriate legislation" the equal protection guarantee of that Amendment. Congress had abundant historical basis from which it could conclude that traditional procurement practices, when applied to minority businesses, could perpetuate the effects of prior discrimination, and that the prospective elimination of such barriers to minority-firm access to public contracting opportunities was appropriate to ensure that those businesses were not denied equal opportunity to participate in federal grants to state and local governments, which is one aspect of the equal protection of the laws. Cf., *e. g., Katzenbach* v. *Morgan*, 384 U. S. 641; *Oregon* v. *Mitchell*, 400 U. S. 112.

(d) Thus, the objectives of the MBE provision are within the scope of Congress' spending power. Cf. *Lau* v. *Nichols*, 414 U. S. 563.

(3) Congress' use here of racial and ethnic criteria as a condition attached to a federal grant is a valid means to accomplish its constitutional objectives, and the MBE provision on its face does not violate the equal protection component of the Due Process Clause of the Fifth Amendment.

(a) In the MBE program's remedial context, there is no requirement that Congress act in a wholly "color-blind" fashion. Cf., *e. g., Swann* v. *Charlotte-Mecklenburg Board of Education*, 402 U. S. 1; *McDaniel* v. *Barresi*, 402 U. S. 39; *North Carolina Board of Education* v. *Swann*, 402 U. S. 43.

(b) The MBE program is not constitutionally defective because it may disappoint the expectations of access to a portion of government contracting opportunities of nonminority firms who may themselves be innocent of any prior discriminatory actions. When effectuating a limited and properly tailored remedy to cure the effects of prior discrimination, such "a sharing of the burden" by innocent parties is not impermissible. *Franks* v. *Bowman Transportation Co.*, 424 U. S. 747, 777.

(c) Nor is the MBE program invalid as being underinclusive in that it limits its benefit to specified minority groups rather than extending its remedial objectives to all businesses whose access to government contracting is impaired by the effects of disadvantage or discrimination. Congress has not sought to give select minority groups a preferred standing in the construction industry, but has embarked on a remedial program to place them on a more equitable footing with respect to public contracting opportunities, and there has been no showing that Congress inadvertently effected an invidious discrimination by excluding from coverage an identifiable minority group that has been the victim of a degree of disadvantage and discrimination equal to or greater than that suffered by the groups encompassed by the MBE program.

(d) The contention that the MBE program, on its face, is overinclusive in that it bestows a benefit on businesses identified by racial or ethnic criteria which cannot be justified on the basis of competitive criteria or as a remedy for the present effects of identified prior discrimination, is also without merit. The MBE provision, with due account for its administrative program, provides a reasonable assurance that application of racial or ethnic criteria will be narrowly limited to accomplishing Congress' remedial objectives and that misapplications of the program will be promptly and adequately remedied administratively. In particular, the administrative program provides waiver and exemption procedures to identify and eliminate from participation MBE's who are not "bona fide," or who attempt to exploit the remedial aspects of the program by charging an unreasonable price not attributable to the present effects of past discrimination. Moreover, grantees may obtain a waiver if they demonstrate that their best efforts will not achieve or have not achieved the 10% target for minority firm participation within the limitations of the program's remedial objectives. The MBE provision may be viewed as a pilot project, appropriately limited in extent and duration and subject to reassessment and re-evaluation by the Congress prior to any extension or re-enactment.

(4) In the continuing effort to achieve the goal of equality of economic opportunity, Congress has latitude to try new techniques such as the limited use of racial and ethnic criteria to accomplish remedial objectives, especially in programs where voluntary cooperation is induced by placing conditions on federal expenditures. When a program narrowly tailored by Congress to achieve its objectives comes under judicial review, it should be upheld if the courts are satisfied that the legislative objectives and projected administration of the program give reasonable assurance that the program will function within constitutional limitations.

MR. JUSTICE MARSHALL, joined by MR. JUSTICE BRENNAN and MR. JUSTICE BLACKMUN, concurring in the judgment, concluded that the proper inquiry for determining the constitutionality of racial classifications that provide benefits to minorities for the purpose of remedying the present effects of past racial discrimination is whether the classifications serve important governmental objectives and are substantially related to achievement of those objectives, *University of California Regents* v. *Bakke*, 438 U. S. 265, 359 (opinion of BRENNAN, WHITE, MARSHALL, and BLACKMUN, JJ., concurring in judgment in part and dissenting in part), and that, judged under this standard, the 10% minority set-aside provision of the 1977 Act is plainly constitutional, the racial classifications being substantially related to the achievement of the important and congressionally articulated goal of remedying the present effects of past racial discrimination.

BURGER, C. J., announced the judgment of the Court and delivered an opinion, in which WHITE and POWELL, JJ., joined. POWELL, J., filed a concurring opinion. MARSHALL, J., filed an opinion concurring in the judgment, in which BRENNAN and BLACKMUN, JJ., joined. STEWART, J., filed a dissenting opinion, in which REHNQUIST, J., joined. STEVENS, J., filed a dissenting opinion.

MR. CHIEF JUSTICE BURGER announced the judgment of the Court and delivered an opinion in which MR. JUSTICE WHITE and MR. JUSTICE POWELL joined.

We granted certiorari to consider a facial constitutional challenge to a requirement in a congressional spending program that, absent an administrative waiver, 10% of the federal funds granted for local public works projects must be used by the state or local grantee to procure services or supplies from businesses owned and controlled by members of statutorily identified minority groups. 441 U. S. 960.

I

In May 1977, Congress enacted the Public Works Employment Act of 1977, Pub. L. 95-28, 91 Stat. 116, which amended the Local Public Works Capital Development and Investment Act of 1976, Pub. L. 94-369, 90 Stat. 999. The 1977 amendments authorized an additional $4 billion appropriation for

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federal grants to be made by the Secretary of Commerce, acting through the Economic Development Administration (EDA), to state and local governmental entities for use in local public works projects. Among the changes made was the addition of the provision that has become the focus of this litigation. Section 103 (f)(2) of the 1977 Act, referred to as the "minority business enterprise" or "MBE" provision, requires that: [2]

> "Except to the extent that the Secretary determines otherwise, no grant shall be made under this Act for any local public works project unless the applicant gives satisfactory assurance to the Secretary that at least 10 per centum of the amount of each grant shall be expended for minority business enterprises. For purposes of this paragraph, the term "minority business enterprise" means a business at least 50 per centum of which is owned by minority group members or, in case of a publicly owned business, at least 51 per centum of the stock of which is owned by minority group members. For the purposes of the preceding sentence, minority group members are citizens of the United States who are Negroes, Spanish-speaking, Orientals, Indians, Eskimos, and Aleuts."

In late May 1977, the Secretary promulgated regulations governing administration of the grant program which were amended two months later.[3] In August 1977, the EDA issued guidelines supplementing the statute and regulations with respect to minority business participation in local public works grants,[4] and in October 1977, the EDA issued a technical bulletin promulgating detailed instructions and information to assist grantees and their contractors in meeting the 10% MBE requirement.[5]

On November 30, 1977, petitioners filed a complaint in the United States District Court for the Southern District of New York seeking declaratory and injunctive relief to enjoin enforcement of the MBE provision. Named as defendants were the Secretary of Commerce, as the program administrator, and the State and City of New York, as actual and potential project grantees. Petitioners are several associations of construction contractors and subcontractors, and a firm engaged in heating, ventilation and air conditioning work. Their complaint alleged that they had sustained economic injury due to enforcement of the 10% MBE requirement and that the MBE provision on its face violated the Equal Protection Clause of the Fourteenth Amendment, the equal protection component of the Due Process Clause of the Fifth Amendment, and various statutory antidiscrimination provisions.[6]

After a hearing held the day the complaint was filed, the District Court denied a requested temporary restraining order and scheduled the matter for an expedited hearing on the merits. On December 19, 1977, the District Court issued a memorandum opinion upholding the validity of the MBE program and denying the injunctive relief sought. *Fullilove* v. *Kreps*, 443 F. Supp. 253 (SDNY 1977).

The United States Court of Appeals for the Second Circuit affirmed, 584 F. 2d 600 (CA2 1978), holding that "even under the most exacting standard of review the MBE provision passes constitutional muster." *Id.*, at 603. Considered in the context of many years of governmental efforts to remedy past racial and ethnic discrimination, the court found it "difficult to imagine" any purpose for the program other than to remedy such discrimination. *Id.*, at 605. In its view, a number of factors contributed to the legitimacy of the MBE provision, most significant of which was the narrowed focus and limited extent of the statutory and administrative program, in size, impact and duration, *id.*, at 607–608; the court looked also to the holdings of other courts of appeals and district courts that the MBE program was constitutional, *id.*, at 608–609.[7] It expressly rejected petitioners' contention that the 10% MBE requirement violated the equal protection guarantees of the Constitution.[8] 584 F. 2d, at 609.

II

A

The MBE provision was enacted as part of the Public Works Employment Act of 1977, which made various amendments to Title I of the Local Public Works Capital Development and Investment Act of 1976. The 1976 Act was intended as a short-term measure to alleviate the problem of national unemployment and to stimulate the national economy by assisting state and local governments to build needed public facilities.[9] To accomplish these objectives, the Congress authorized the Secretary of Commerce, acting through the Economic Development Administration, to make grants to state and local governments for construction, renovation, repair or other improvement of local public works projects.[10] The 1976 Act placed a number of restrictions on project eligibility designed to assure that federal monies were targeted to accomplish the legislative purposes.[11] It established criteria to determine grant priorities and to apportion federal funds among political jurisdictions.[12] Those criteria directed grant funds toward areas of high unemployment.[13] The statute authorized the appropriation of up to

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[2] 91 Stat. 116, 42 U. S. C. [illegible]

[3] 13 CFR part 317 [illegible]

[4] U. S. Department of Commerce, Economic Development Administration, [illegible] Public Works Program [illegible] Business Participation in LPW Grants [illegible] App. [illegible]

[5] U. S. Department of Commerce, Economic Development Administration, EDA Minority Business Enterprise (MBE) Technical Bulletin [illegible] Information Available to Grantees and Their Contractors In Meeting The 10% MBE Requirement [illegible], App. [illegible]

[6] [illegible] Stat. [illegible] 42 U. S. C. [illegible] Rights Act of 1964, 78 Stat. 252, 42 U. S. C. [illegible] of the Civil Rights Act of 1964, 78 Stat. [illegible] as amended, 42 U. S. C. § 2000e et seq.

[7] *Ohio Contractors Association* v. *Economic Development Administration*, 580 F. 2d 213 (CA6 1978); *Constructors Association* v. *Kreps*, 573 F. 2d 811 (CA3 1978); *Rhode Island Chapter, Associated General Contractors* v. *Kreps*, 450 F. Supp. 338 (RI 1978); *Associated General Contractors* v. *Secretary of Commerce*, No. 77-4218 (Kan. Dec. 19, 1977); *Carolinas Branch, Associated General Contractors* v. *Kreps*, 442 F. Supp. 392 (SC 1977); *Ohio Contractors Assoc.* v. *Economic Development Administration*, 452 F. Supp. 1013 (SD Ohio 1977); *Montana Contractors' Association* v. *Secretary of Commerce*, 439 F. Supp. 1331 (Mont. 1977); *Florida East Coast Chapter* v. *Secretary of Commerce*, No. 77-8351 (SD Fla. Nov. 3, 1977); but see *Associated General Contractors* v. *Secretary of Commerce*, 441 F. Supp. 955 (CD Cal. 1977), vacated and remanded for consideration of mootness, 438 U. S. 909 (1978), on remand 459 F. Supp. [illegible] (CD Cal.), appeal docketed sub nom. *Armistead* v. *Associated General Contractors of California*, No. 78-1107.

[8] Both the Court of Appeals and the District Court rejected petitioners' [illegible] arguments without extended discussion. 584 F. 2d, at 609, n. 15; 443 F. Supp., at 262.

[9] H. R. Rep. No. 94-1077, p. 2 (1976). The bill discussed in this report was accepted by the Conference Committee in preference to the Senate version. S. Conf. Rep. No. 94-939, p. 1 (1976); H. R. Conf. Rep. No. 94-1260, p. 1 (1976).

[10] 90 Stat. 999, 42 U. S. C. § 6702.

[11] 90 Stat. 1000, 42 U. S. C. § 6705.

[12] 90 Stat. 1001, 42 U. S. C. § 6707.

[13] 90 Stat. 1001, 42 U. S. C. § 6707 (e).

$2 billion for a period ending in September 1977;[13] this appropriation was soon consumed by grants made under the program.

Early in 1977, Congress began consideration of expanded appropriations and amendments to the grant program. Under administration of the 1976 appropriation, referred to as "Round I" of the local public works program, applicants seeking some $25 billion in grants had competed for the $2 billion in available funds; of nearly 25,000 applications, only some 2,000 were granted.[14] The results provoked widespread concern for the fairness of the allocation process.[15] Because the 1977 Act would authorize the appropriation of an additional $4 billion to fund "Round II" of the grant program,[16] the congressional hearings and debates concerning the amendments focused primarily on the politically sensitive problems of priority and geographic distribution of grants under the supplemental appropriation.[17] The result of this attention was inclusion in the 1977 Act of provisions revising the allocation criteria of the 1976 legislation. Those provisions, however, retained the underlying objective to direct funds into areas of high unemployment.[18] The 1977 Act also added new restrictions on applicants seeking to qualify for federal grants;[19] among these was the MBE provision.

The origin of the provision was an amendment to the House version of the 1977 Act, H. R. 11, offered on the floor of the House on Feb. 23, 1977 by Representative Mitchell of Maryland.[20] As offered, the amendment provided:[21]

> "Notwithstanding any other provision of law, no grant shall be made under this Act for any local public works project unless at least 10 per centum of the articles, materials, and supplies which will be used in such project are procured from minority business enterprises. For purposes of this paragraph, the term 'minority business enterprise' means a business at least 50 percent of which is owned by minority group members or, in case of publicly owned businesses, at least 51 percent of the stock of which is owned by minority group members. For the purposes of the preceding sentence, minority group members are citizens of the United States who are Negroes, Spanish-speaking, Orientals, Indians, Eskimos, and Aleuts."

The sponsor stated that the objective of the amendment was to direct funds into the minority business community, a sector of the economy sorely in need of economic stimulus but which, on the basis of past experience with government procurement programs, could not be expected to benefit significantly from the public works program as then formulated.[22] He cited the marked statistical disparity that in fiscal year 1976 less than 1% of all federal procurement was concluded with minority business enterprises, although minorities comprised 15–18% of the population.[23] When the amendment was put forward during debate on H. R. 11,[24] Rep. Mitchell reiterated the need to ensure that minority firms would obtain a fair opportunity to share in the benefits of this government program.[25]

The amendment was put forward not as a new concept, but rather one building upon prior administrative practice. In his introductory remarks, the sponsor rested his proposal squarely on the ongoing program under § 8 (a) of the Small Business Act of 1958, Pub. L. 85–536, § 2 (8), 72 Stat. 389, which, as will become evident, served as a model for the administrative program developed to enforce the MBE provision:[26]

> "The first point in opposition will be that you cannot have a set-aside. Well, Madam Chairman, we have been doing this for the last 10 years in Government. The 8–A set-aside under SBA has been tested in the courts more than 30 times and has been found to be legitimate and bona fide. We are doing it in this bill."

Although the proposed MBE provision on its face appeared mandatory, requiring compliance with the 10% minority participation requirement "[n]otwithstanding any other provision of law," its sponsor gave assurances that existing administrative practice would ensure flexibility in administration if, with respect to a particular project, compliance with the 10% requirement proved infeasible.[27]

Representative Roe of New Jersey then suggested a change of language expressing the twin intentions (1) that the federal administrator would have discretion to waive the 10% requirement where its application was not feasible, and (2) that the grantee would be mandated to achieve at least 10% participation by minority businesses unless infeasibility was demonstrated.[28] He proposed as a substitute for the first sentence of the amendment the language that eventually was enacted:[29]

> "Except to the extent that the Secretary determines otherwise, no grant shall be made under this Act for any local public works project unless the applicant gives satisfactory assurance to the Secretary that at least 10 percent of the amount of each grant shall be expended for minority business enterprises."

The sponsor fully accepted the suggested clarification because it retained the directive that the initial burden of compliance would fall on the grantee. That allocation of burden was necessary because, as he put it, "every agency of the Government has tried to figure out a way to avoid doing this very thing. Believe me, these bureaucracies can come up with 10,000 ways to avoid doing it."[30]

Other supporters of the MBE amendment echoed the sponsor's concern that a number of factors, difficult to isolate or

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[13] 90 Stat. [illegible], 42 U. S. C. § 6710. The actual appropriation of the [illegible] was made several weeks later [illegible] 1977.

[14] 123 Cong. Rec. 5339 (Feb. 23, 1977) (remarks of Sen. Randolph).

[15] See, e. g., Hearings on H. R. 11 and related bills before the Subcommittee on Economic Development of the House Committee on Public Works and Transportation, 95th Cong., 1st Sess. (1977); H. R. Rep. No. 95-20 (1977); S. Rep. No. 95-38 (1977).

[16] [illegible]

[17] [illegible]

[18] [illegible]

[19] [illegible]

[20] 123 Cong. Rec. H1436 (Feb. 23, 1977) (remarks of Rep. Mitchell).

[21] Id., at H1436.

[22] Id., at H1436–H1440.

[23] Id., at H1440.

[24] Id., at H1437 (Feb. 24, 1977). As reintroduced, the first sentence of the amendment was modified to provide: "Notwithstanding any other provision of law, no grant shall be made under this Act for any local public works project unless at least 10 per centum of the dollar volume of each contract shall be set aside for minority business enterprise and, or, unless at least 10 per centum of the articles, materials, and supplies which will be used in such project are procured from minority business enterprises."

[25] Id., at H1436–H1437.

[26] Id., at H1437.

[27] Id., at H1437–H1438.

[28] Id., at H1438 (remarks of Rep. Roe).

[29] Ibid.

[30] Id. (remarks of Rep. Mitchell).

quantify, seemed to impair access by minority businesses to public contracting opportunities. Representative Conyers of Michigan spoke of the frustration of the existing situation, in which, due to the intricacies of the bidding process and through no fault of their own, minority contractors and businessmen were unable to gain access to government contracting opportunities.

Representative Biaggi of New York then spoke to the need for the amendment to "promote a sense of economic equality in the Nation." He expressed the view that without the amendment, "this legislation may be potentially inequitable to minority businesses and workers" in that it would perpetuate the historic practices that have precluded minority businesses from effective participation in public contracting opportunities. The amendment was accepted by the House.

Two weeks later, the Senate considered S. 427, its package of amendments to the Local Public Works Capital Development and Investment Act of 1976. At that time Senator Brooke of Massachusetts introduced an MBE amendment, worded somewhat differently than the House version, but aimed at achieving the same objectives. His statement in support of the 10% requirement reiterated and summarized the various expressions on the House side that the amendment was necessary to ensure that minority businesses were not deprived of access to the government contracting opportunities generated by the public works program.

The Senate adopted the amendment without debate. The Conference Committee, called to resolve differences between the House and Senate versions of the Public Works Employment Act of 1977, adopted the language approved by the House for the MBE provision. The Conference Reports added only the comment, "This provision shall be dependent on the availability of minority business enterprises located in the project area."

The device of a 10% MBE participation requirement, subject to administrative waiver, was thought to be required to assure minority business participation; otherwise it was thought that repetition of the prior experience could be expected, with participation by minority business accounting for an inordinately small percentage of government contracting. The causes of this disparity were perceived as involving the longstanding existence and maintenance of barriers impairing access by minority enterprises to public contracting opportunities, or sometimes as involving more direct discrimination, but not as relating to lack—as Senator Brooke put it—"of capable and qualified minority enterprises who are ready and willing to work." In the words of its sponsor, the MBE provision was "designed to begin to redress this grievance that has been extant for so long."

B

The legislative objectives of the MBE provision must be considered against the background of ongoing efforts directed toward deliverance of the century-old promise of equality of economic opportunity. The sponsors of the MBE provision in the House and the Senate expressly linked the provision to the existing administrative programs promoting minority opportunity in government procurement, particularly those related to § 8 (a) of the Small Business Act of 1958. Section 8 (a) delegates to the SBA an authority and an obligation "whenever it determines such action is necessary" to enter into contracts with any procurement agency of the Federal Government to furnish required goods or services, and, in turn, to enter into subcontracts with small businesses for the performance of such contracts. This authority lay dormant for a decade. Commencing in 1968, however, the SBA was directed by the President to develop a program pursuant to its § 8 (a) authority to assist small business concerns owned and controlled by "socially or economically disadvantaged" persons to achieve a competitive position in the economy.

At the time the MBE provision was enacted, the regulations governing the § 8 (a) program defined "social or economic disadvantage" as follows:

> "An applicant concern must be owned and controlled by one or more persons who have been deprived of the opportunity to develop and maintain a competitive position in the economy because of social or economic disadvantage. Such disadvantage may arise from cultural, social, chronic economic circumstances or background, or other similar cause. Such persons include, but are not limited to, black Americans, American Indians, Spanish-Americans, oriental Americans, Eskimos, and Aleuts . . . ."

The guidelines accompanying these regulations provided that a minority business could not be maintained in the program, even when owned and controlled by members of the identified minority groups, if it appeared that the business had not been deprived of the opportunity to develop and maintain a competitive position in the economy because of social or economic disadvantage.

As the Congress began consideration of the Public Works Employment Act of 1977, the House Committee on Small

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Id., at H1440 (remarks of Rep. Conyers).

Id., at H1440–H1441 (remarks of Rep. Biaggi).

Id., at H1441.

Id., at S3910 (Mar. 10, 1977) (remarks of Sen. Brooke). [illegible]

[illegible]

[illegible]

123 Cong. Rec. S3910 (Mar. 10, 1977) (remarks of Sen. Brooke).

Id., at H1440 (Feb. 24, 1977) (remarks of Rep. Mitchell).

Id., at H1437; id., at S3910 (Mar. 10, 1977) (remarks of Sen. Brooke).

Exec. Order No. [illegible], 3 CFR [illegible] (1966–1970 Comp.), Exec. Order No. [illegible], 3 CFR [illegible] (1966–1970 Comp.).

13 CFR § 124.8-1 [illegible] (1977).

U. S. Small Business Administration, Office of Business Development, Section 8 (a) Program, Small Business Administration Standard Operating Procedure [illegible]

Business issued a lengthy report summarizing its activities, including its evaluation of the ongoing § 8 (a) program. One chapter of the report, entitled "Minority Enterprise and Allied Problems of Small Business," summarized a 1975 committee report of the same title dealing with this subject matter. The original report, prepared by the House Subcommittee on SBA Oversight and Minority Enterprise, observed:

> "The subcommittee is acutely aware that the economic policies of this Nation must function within and be guided by our constitutional system which guarantees 'equal protection of the laws.' *The effects of past inequities stemming from racial prejudice have not remained in the past. The Congress has recognized the reality that past discriminatory practices have, to some degree, adversely affected our present economic system.*
>
> "While minority persons comprise about 16 percent of the Nation's population, of the 13 million businesses in the United States, only 382,000, or approximately 3.0 percent, are owned by minority individuals. The most recent data from the Department of Commerce also indicates that the gross receipts of all businesses in this country totals about $2,540.8 billion, and of this amount only $16.6 billion, or about 0.65 percent was realized by minority business concerns.
>
> "These statistics are not the result of random chance. The presumption must be made that past discriminatory systems have resulted in present economic inequities. In order to right this situation, the Congress has formulated certain remedial programs designed to uplift those socially or economically disadvantaged persons to a level where they may effectively participate in the business mainstream of our economy.*
>
> "*For the purposes of this report the term 'minority' shall include only such minority individuals as are considered to be economically or socially disadvantaged." (Emphasis added.)

The 1975 report gave particular attention to the § 8 (a) program, expressing disappointment with its limited effectiveness. With specific reference to government construction contracting, the report concluded, "there are substantial § 8 (a) opportunities in the area of Federal construction, but . . . the practices of some agencies preclude the realization of that potential." The subcommittee took "full notice . . . as evidence for its consideration" of reports submitted to the Congress by the General Accounting Office and by the U. S. Commission on Civil Rights, which reflected a similar dissatisfaction with the effectiveness of the § 8 (a) program. The Civil Rights Commission report discussed at some length the barriers encountered by minority businesses in gaining access to government contracting opportunities at the federal, state and local levels. Among the major difficulties confronting minority businesses were deficiencies in working capital, inability to meet bonding requirements, disabilities caused by an inadequate "track record," lack of awareness of bidding opportunities, unfamiliarity with bidding procedures, preselection before the formal advertising process, and the exercise of discretion by government procurement officers to disfavor minority businesses.

The subcommittee report also gave consideration to the operations of the Office of Minority Business Enterprise (OMBE), an agency of the Department of Commerce organized pursuant to Executive Orders to formulate and coordinate federal efforts to assist the development of minority businesses. The report concluded that OMBE efforts were "totally inadequate" to achieve its policy of increasing opportunities for subcontracting by minority businesses on public contracts. OMBE efforts were hampered by a "glaring lack of specific objectives which each prime contractor should be required to achieve," by a "lack of enforcement provisions," and by a "lack of any meaningful monitoring system."

Against this backdrop of legislative and administrative programs, it is inconceivable that Members of both Houses were not fully aware of the objectives of the MBE provision and of the reasons prompting its enactment.

C

Although the statutory MBE provision itself outlines only the bare bones of the federal program, it makes a number of critical determinations: the decision to initiate a limited racial and ethnic preference; the specification of a minimum level for minority business participation; the identification of the minority groups that are to be encompassed by the program; and the provision for an administrative waiver where application of the program is not feasible. Congress relied on the administrative agency to flesh out this skeleton, pursuant to delegated rulemaking authority, and to develop an administrative operation consistent with legislative intentions and objectives.

As required by the Public Works Employment Act of 1977, the Secretary of Commerce promulgated regulations to set into motion "Round II" of the federal grant program. The regulations require that construction projects funded under the legislation must be performed under contracts awarded by competitive bidding, unless the federal administrator has made a determination that in the circumstances relating to a particular project some other method is in the public interest. Where competitive bidding is employed, the regulations echo the statute's requirement that contracts are to be awarded on the basis of the "lowest responsive bid submitted by a bidder meeting established criteria of responsibility," and they

H. R. Rep. No. 94-1791 (1977).

Id., at 124-149.

H. R. Rep. No. 94-468, pp. 1-3 (1975).

Another chapter of the 1977 Report of the House Committee on Small Business summarized a review of the SBA's Surety Bond Guarantee Program, making specific reference to minority business participation in the construction industry. [illegible]

[illegible] H. R. Rep. No. 94-1791, p. 182 [illegible] H. R. Rep. No. [illegible] (1975).

[illegible] (1975).

Id., at 29.

Id., at [illegible]; U. S. General Accounting Office, "Questionable Effectiveness of the 8 (a) Procurement Program" (1975); U. S. Commission on Civil Rights, "Minorities and Women as Government Contractors" (1975).

U. S. Commission on Civil Rights, "Minorities and Women as Government Contractors" 19-28, 86-89 (1975).

Id.

Exec. Order No. 11458, 3 CFR 779 (1966-1970 Comp.); Exec. Order No. 11625, 3 CFR 616 (1971-1975 Comp.).

H. R. Rep. No. 94-468, p. 32 (1975). For other congressional observations with respect to the effect of past discrimination on current business opportunities for minorities, see, e. g., H. R. Rep. No. [illegible], p. 3 (1972); H. R. Rep. No. 92-[illegible], p. 8 (1971); S. Rep. No. 92-[illegible], pp. 16-[illegible] (1971); S. Rep. No. 94-[illegible], pp. [illegible] (1976); see also, e. g., H. R. Doc. No. 92-[illegible], p. [illegible] (1971); H. R. Doc. No. 92-194, p. 1 (1972).

[illegible] Stat. 117, 42 U. S. C. § 6705 (supp. [illegible]); 13 CFR part 317 (1978).

also restate the MBE requirement.

EDA also has published guidelines devoted entirely to the administration of the MBE provision. The guidelines outline the obligations of the grantee to seek out all available, qualified, bona fide MBE's, to provide technical assistance as needed, to lower or waive bonding requirements where feasible, to solicit the aid of the Office of Minority Business Enterprise, the Small Business Administration or other sources for assisting MBE's in obtaining required working capital and to give guidance through the intricacies of the bidding process.

EDA regulations contemplate that, as anticipated by Congress, most local public works projects will entail the award of a predominant prime contract, with the prime contractor assuming the above grantee obligations for fulfilling the 10% MBE requirement. The EDA guidelines specify that when prime contractors are selected through competitive bidding, bids for the prime contract "shall be considered by the Grantee to be responsive only if at least 10 percent of the contract funds are to be expended for MBE's." The administrative program envisions that competitive incentive will motivate aspirant prime contractors to perform their obligations under the MBE provision so as to qualify as "responsive" bidders. And, since the contract is to be awarded to the lowest responsive bidder, the same incentive is expected to motivate prime contractors to seek out the most competitive of the available, qualified, bona fide minority firms. This too is consistent with the legislative intention.

The EDA guidelines also outline the projected administration of applications for waiver of the 10% MBE requirement, which may be sought by the grantee either before or during the bidding process. The technical bulletin issued by EDA discusses in greater detail the processing of waiver requests, clarifying certain issues left open by the guidelines. It specifies that waivers may be total or partial, depending on the circumstances, and it illustrates the projected operation of the waiver procedure by posing hypothetical questions with projected administrative responses. One such hypothetical is of particular interest, for it indicates the limitations on the scope of the racial or ethnic preference contemplated by the federal program when a grantee or its prime contractor is confronted with an available, qualified, bona fide minority business enterprise who is not the lowest competitive bidder. The hypothetical provides:

> "*Question:* Should a request for waiver of the 10% requirement based on an unreasonable price asked by an MBE ever be granted?
>
> "*Answer:* It is possible to imagine situations where an MBE might ask a price for its product or services that is unreasonable and where, therefore, a waiver is justified. However, before a waiver request will be honored, the following determinations will be made:
>
> "a) The MBE's quote is unreasonably priced. This determination should be based on the nature of the product or service of the subcontractor, the geographic location of the site and of the subcontractor, prices of similar products or services in the relevant market area, and general business conditions in the market area. Furthermore, a subcontractor's price should not be considered unreasonable if he is merely trying to cover his costs because the price results from disadvantage which affects the MBE's cost of doing business or results from discrimination.
>
> "b) The contractor has contacted other MBE's and has no meaningful choice but to accept an unreasonably high price."

This announced policy makes clear the administrative understanding that a waiver or partial waiver is justified (and will be granted) to avoid subcontracting with a minority business enterprise at an "unreasonable" price, *i. e.*, a price above competitive levels which cannot be attributed to the minority firm's attempt to cover costs inflated by the present effects of disadvantage or discrimination.

This administrative approach is consistent with the legislative intention. It will be recalled that in the report of the House Subcommittee on SBA Oversight and Minority Enterprise the subcommittee took special care to note that when using the term "minority" it intended to include "only such minority individuals as are considered to be economically or socially disadvantaged." The subcommittee also was cognizant of existing administrative regulations designed to ensure that firms maintained on the lists of bona fide minority business enterprises be those whose competitive position is impaired by the effects of disadvantage and discrimination. In its report, the subcommittee expressed its intention that these criteria continue to govern administration of the SBA's § 8 (a) program. The sponsors of the MBE provision, in their reliance on prior administrative practice, intended that the term "minority business enterprise" would be given that same limited application; this even found expression in the legislative debates, where Representative Roe made the point:

> ". . . when we are talking about companies held by minority groups . . . [c]ertainly people of a variety of backgrounds are included in that. That is not really a measurement. They are talking about people in the minority and deprived."

The EDA technical bulletin provides other elaboration of the MBE provision. It clarifies the definition of "minority group members." It also indicates EDA's intention "to allow credit for utilization of MBE's only for those contracts in which involvement constitutes a basis for strengthening the long-term and continuing participation of the MBE in the construction and related industries." Finally, the bulletin outlines a procedure for the processing of complaints of "unjust participation by an enterprise or individuals in the MBE program," or of improper administration of the MBE requirement.

III

When we are required to pass on the constitutionality

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91 Stat. 117, 42 U. S. C. (1976 ed., Supp. II) § 6705 (e)(1); 13 CFR § 317.19 (1978).

Guidelines, n. 2, supra, at 2-7, App. 157a-159a. The relevant portions of the guidelines are set out in the Appendix to this opinion, ¶ 1.

Id., at 2, App. 157a; see 123 Cong. Rec. H1437-H1438 (Feb. 24, 1977) (remarks of Rep. Mitchell and Rep. Roe).

Guidelines, n. 2, supra, at 8, App. 161a.

See 123 Cong. Rec. H1437-H1438 (Feb. 24, 1977) (remarks of Rep. Mitchell and Rep. Roe).

Guidelines, n. 2, supra, at 11-12, App. 165a-167a. The relevant portions of the guidelines are set out in the Appendix to this opinion, ¶ 2.

Technical Bulletin, n. 4, supra, at 3, App. 170a.

Id., at 9-10, App. 163a.

Text accompanying n. 46, supra.

H. R. Rep. No. 94-468, p. 30 (1975).

123 Cong. Rec. H1439 (Feb. 24, 1977) (remarks of Rep. Roe).

Technical Bulletin, n. 4, supra, at 1, App. 171a-172a. These definitions are set out in the Appendix to this opinion, ¶ 3.

Id., at 3, App. 175a.

Id., at 10, App. 183a. The relevant portions of the technical bulletin are set out in the Appendix to this opinion, ¶ 4.

of an Act of Congress, we assume "the gravest and most delicate duty that this Court is called on to perform." *Blodgett* v. *Holden*, 275 U. S. 142, 148 (1927) (opinion of Holmes, J.). A program that employs racial or ethnic criteria, even in a remedial context, calls for close examination; yet we are bound to approach our task with appropriate deference to the Congress, a co-equal branch charged by the Constitution with the power to "provide for the . . . general Welfare of the United States" and "to enforce by appropriate legislation" the equal protection guarantees of the Fourteenth Amendment. Art. I, § 8, cl. 1; Amdt. 14, § 5. In *Columbia Broadcasting System, Inc.* v. *Democratic National Committee*, 412 U. S. 94, 102 (1973), we accorded "great weight to the decisions of Congress" even though the legislation implicated fundamental constitutional rights guaranteed by the First Amendment. The rule is not different when a congressional program raises equal protection concerns. See, *e. g.*, *Cleland* v. *National College of Business*, 435 U. S. 213 (1978); *Mathews* v. *De Castro*, 429 U. S. 181 (1976).

Here we pass, not on a choice made by a single judge or a school board but on a considered decision of the Congress and the President. However, in no sense does that render it immune from judicial scrutiny and it "is not to say we 'defer' to the judgment of the Congress . . . on a constitutional question," or that we would hesitate to invoke the Constitution should we determine that Congress has overstepped the bounds of its constitutional power. *Columbia Broadcasting*, *supra*, 412 U. S., at 103.

The clear objective of the MBE provision is disclosed by our necessarily extended review of its legislative and administrative background. The program was designed to ensure that, to the extent federal funds were granted under the Public Works Employment Act of 1977, grantees who elect to participate would not employ procurement practices that Congress had decided might result in perpetuation of the effects of prior discrimination which had impaired or foreclosed access by minority businesses to public contracting opportunities. The MBE program does not mandate the allocation of federal funds according to inflexible percentages solely based on race or ethnicity.

Our analysis proceeds in two steps. At the outset, we must inquire whether the *objectives* of this legislation are within the power of Congress. If so, we must go on to decide whether the limited use of racial and ethnic criteria, in the context presented, is a constitutionally permissible *means* for achieving the congressional objectives and does not violate the equal protection component of the Due Process Clause of the Fifth Amendment.

A

(1)

In enacting the MBE provision, it is clear that Congress employed an amalgam of its specifically delegated powers. The Public Works Employment Act of 1977, by its very nature, is primarily an exercise of the Spending Power. U. S. Const., Art. I, § 8, cl. 1. This Court has recognized that the power to "provide for the . . . general Welfare" is an independent grant of legislative authority, distinct from other broad congressional powers. *Buckley* v. *Valeo*, 424 U. S. 1, 90-91 (1976); *United States* v. *Butler*, 297 U. S. 1, 65-66 (1936). Congress has frequently employed the Spending Power to further broad policy objectives by conditioning receipt of federal moneys upon compliance by the recipient with federal statutory and administrative directives. This Court has repeatedly upheld against constitutional challenge the use of this technique to induce governments and private parties to cooperate voluntarily with federal policy. *E. g.*, *California Bankers Assn.* v. *Shultz*, 416 U. S. 21 (1974); *Lau* v. *Nichols*, 414 U. S. 563 (1974); *Oklahoma* v. *United States Civil Service Comm'n*, 330 U. S. 127 (1947); *Helvering* v. *Davis*, 301 U. S. 619 (1937); *Steward Machine Co.* v. *Davis*, 301 U. S. 548 (1937).

The MBE program is structured within this familiar legislative pattern. The program conditions receipt of public works grants upon agreement by the state or local governmental grantee that at least 10% of the federal funds will be devoted to contracts with minority businesses, to the extent this can be accomplished by overcoming barriers to access and by awarding contracts to bona fide MBE's. It is further conditioned to require that MBE bids on these contracts are competitively priced, or might have been competitively priced but for the present effects of prior discrimination. Admittedly, the problems of administering this program with respect to these conditions may be formidable. Although the primary responsibility for ensuring minority participation falls upon the grantee, when the procurement practices of the grantee involve the award of a prime contract to a general or prime contractor, the obligations to assure minority participation devolve upon the private contracting party; this is a contractual condition of eligibility for award of the prime contract.

Here we need not explore the outermost limitations on the objectives attainable through such an application of the Spending Power. The reach of the Spending Power, within its sphere, is at least as broad as the regulatory powers of Congress. If, pursuant to its regulatory powers, Congress could have achieved the objectives of the MBE program, then it may do so under the Spending Power. And we have no difficulty perceiving a basis for accomplishing the objectives of the MBE program through the Commerce Power insofar as the program objectives pertain to the action of private contracting parties, and through the power to enforce the equal protection guarantees of the Fourteenth Amendment insofar as the program objectives pertain to the action of state and local grantees.

(2)

We turn first to the Commerce Power. U. S. Const., Art. I, § 8, cl. 3. Had Congress chosen to do so, it could have drawn on the Commerce Clause to regulate the practices of prime contractors on federally funded public works projects. *Katzenbach* v. *McClung*, 379 U. S. 294 (1964); *Heart of Atlanta Motel, Inc.* v. *United States*, 379 U. S. 241 (1964). The legislative history of the MBE provision shows that there was a rational basis for Congress to conclude that the subcontracting practices of prime contractors could perpetuate the prevailing impaired access by minority businesses to public contracting opportunities, and that this inequity has an effect on interstate commerce. Thus Congress could take necessary and proper action to remedy the situation. *Ibid.*

It is not necessary that these prime contractors be shown responsible for any violation of antidiscrimination laws. Our cases dealing with application of Title VII of the Civil Rights Act of 1964, 78 Stat. 253, as amended, express no doubt of the congressional authority to prohibit practices "challenged as perpetuating the effects of [not unlawful] discrimination occurring prior to the effective date of the Act." *Franks* v. *Bowman Transportation Co.*, 424 U. S. 747, 761 (1976); see *California Brewers Assn.* v. *Bryant*, — U. S. —, No. 78-1548, Feb. 20, 1980; *International Brotherhood of Teamsters*

v. *United States*, 431 U. S. 324 (1977); *Albemarle Paper Co.* v. *Moody*, 422 U. S. 405 (1975); *Griggs* v. *Duke Power Co.*, 401 U. S. 424 (1971). Insofar as the MBE program pertains to the actions of private prime contractors, the Congress could have achieved its objectives under the Commerce Clause. We conclude that in this respect the objectives of the MBE provision are within the scope of the Spending Power.

(3)

In certain contexts, there are limitations on the reach of the Commerce Power to regulate the actions of state and local governments. *National League of Cities* v. *Usery*, 426 U. S. 833 (1976). To avoid such complications, we look to § 5 of the Fourteenth Amendment for the power to regulate the procurement practices of state and local grantees of federal funds. *Fitzpatrick* v. *Bitzer*, 427 U. S. 445 (1976). A review of our cases persuades us that the objectives of the MBE program are within the power of Congress under § 5 "to enforce by appropriate legislation" the equal protection guarantees of the Fourteenth Amendment.

In *Katzenbach* v. *Morgan*, 384 U. S. 641 (1966), we equated the scope of this authority with the broad powers expressed in the Necessary and Proper Clause, U. S. Const., Art. I, § 8, cl. 18. "Correctly viewed, § 5 is a positive grant of legislative power authorizing Congress to exercise its discretion in determining whether and what legislation is needed to secure the guarantees of the Fourteenth Amendment." 384 U. S., at 651. In *Katzenbach*, the Court upheld § 4 (e) of the Voting Rights Act of 1965, 79 Stat. 439, which prohibited application of state English-language literacy requirements to otherwise qualified voters who had completed the sixth grade in an accredited American school in which a language other than English was the predominant medium of instruction. To uphold this exercise of congressional authority, the Court found no prerequisite that application of a literacy requirement violate the Equal Protection Clause. 384 U. S., at 648–649. It was enough that the Court could perceive a basis upon which Congress could reasonably predicate a judgment that application of literacy qualifications within the compass of § 4 (e) would discriminate in terms of access to the ballot and consequently in terms of access to the provision or administration of governmental programs. *Id.*, at 652–653.

Four years later, in *Oregon* v. *Mitchell*, 400 U. S. 112 (1970), we upheld § 201 of the Voting Rights Act Amendments of 1970, 84 Stat. 315, which imposed a five-year nationwide prohibition on the use of various voter-qualification tests and devices in federal, state and local elections. The Court was unanimous, albeit in separate opinions, in concluding that Congress was within its authority to prohibit the use of such voter qualifications; Congress could reasonably determine that its legislation was an appropriate method of attacking the perpetuation of prior purposeful discrimination, even though the use of these tests or devices might have discriminatory effects only. See *City of Rome* v. *United States*, — U. S. —, No. 78-1840, slip op., at 16–19 (Apr. 22, 1980). Our cases reviewing the parallel power of Congress to enforce the provisions of the Fifteenth Amendment, U. S. Const., Amdt. 15, § 2, confirm that congressional authority extends beyond the prohibition of purposeful discrimination to encompass state action that has discriminatory impact perpetuating the effects of past discrimination. *South Carolina* v. *Katzenbach*, 383 U. S. 301 (1966); cf. *City of Rome*, *supra*.

With respect to the MBE provision, Congress had abundant evidence from which it could conclude that minority businesses have been denied effective participation in public contracting opportunities by procurement practices that perpetuated the effects of prior discrimination. Congress, of course, may legislate without compiling the kind of "record" appropriate with respect to judicial or administrative proceedings. Congress had before it, among other data, evidence of a long history of marked disparity in the percentage of public contracts awarded to minority business enterprises. This disparity was considered to result not from any lack of capable and qualified minority businesses, but from the existence and maintenance of barriers to competitive access which had their roots in racial and ethnic discrimination, and which continue today, even absent any intentional discrimination or other unlawful conduct. Although much of this history related to the experience of minority businesses in the area of federal procurement, there was direct evidence before the Congress that this pattern of disadvantage and discrimination existed with respect to state and local construction contracting as well. In relation to the MBE provision, Congress acted within its competence to determine that the problem was national in scope.

Although the Act recites no preambulary "findings" on the subject, we are satisfied that Congress had abundant historical basis from which it could conclude that traditional procurement practices, when applied to minority businesses, could perpetuate the effects of prior discrimination. Accordingly, Congress reasonably determined that the prospective elimination of these barriers to minority firm access to public contracting opportunities generated by the 1977 Act was appropriate to ensure that those businesses were not denied equal opportunity to participate in federal grants to state and local governments, which is one aspect of the equal protection of the laws. Insofar as the MBE program pertains to the actions of state and local grantees, Congress could have achieved its objectives by use of its power under § 5 of the Fourteenth Amendment. We conclude that in this respect the objectives of the MBE provision are within the scope of the Spending Power.

(4)

There are revelant similarities between the MBE program and the federal spending program reviewed in *Lau* v. *Nichols*, 414 U. S. 563 (1974). In *Lau*, a language barrier "effectively foreclosed" non-English-speaking Chinese pupils from access to the educational opportunities offered by the San Francisco public school system. *Id.*, at 564–566. It had not been shown that this had resulted from any discrimination, purposeful or otherwise, or from other unlawful acts. Nevertheless, we upheld the constitutionality of a federal regulation applicable to public school systems receiving federal funds that prohibited the utilization of "criteria or methods of administration *which have the effect* . . . of defeating or substantially impairing accomplishment of the objectives of the [educational] program as respect individuals of a particular race, color, or national origin." *Id.*, at 568 (emphasis added). Moreover, we upheld application to the San Francisco school system, as a recipient of federal funds, of a requirement that "[w]here inability to speak and understand the English language excludes national origin-minority group children from effective participation in the educational program offered by a school district, the district must take affirmative steps to rectify the language deficiency in order to open its instructional program to these students." *Ibid.*

It is true that the MBE provision differs from the program approved in *Lau* in that the MBE program directly employs racial and ethnic criteria as a means to accomplish congressional objectives; however, these objectives are essentially the same as those approved in *Lau*. Our holding in *Lau* is

instructive on the exercise of congressional authority by way of the MBE provision. The MBE program, like the federal regulations reviewed in *Lau*, primarily regulates state action in the use of federal funds voluntarily sought and accepted by the grantees subject to statutory and administrative conditions. The MBE participation requirement is directed at the utilization of criteria, methods or practices thought by Congress to have the effect of defeating, or substantially impairing, access by the minority business community to public funds made available by congressional appropriations.

B

We now turn to the question whether, as a *means* to accomplish these plainly constitutional objectives, Congress may use racial and ethnic criteria, in this limited way, as a condition attached to a federal grant. We are mindful that "[i]n no matter should we pay more deference to the opinion of Congress than in its choice of instrumentalities to perform a function that is within its power," *National Mutual Insurance Co.* v. *Tidewater Transfer Co.*, 337 U. S. 582, 603 (1949) (opinion of Jackson, J.). However, Congress may employ racial or ethnic classifications in exercising its Spending or other legislative Powers only if those classifications do not violate the equal protection component of the Due Process Clause of the Fifth Amendment. We recognize the need for careful judicial evaluation to assure that any congressional program that employs racial or ethnic criteria to accomplish the objective of remedying the present effects of past discrimination is narrowly tailored to the achievement of that goal.

Again, we stress the limited scope of our inquiry. Here we are not dealing with a remedial decree of a court but with the legislative authority of Congress. Furthermore, petitioners have challenged the constitutionality of the MBE provision on its face; they have not sought damages or other specific relief for injury allegedly flowing from specific applications of the program; nor have they attempted to show that as applied in identified situations the MBE provision violated the constitutional or statutory rights of any party to this case.[72] In these circumstances, given a reasonable construction and in light of its projected administration, if we find the MBE program on its face to be free of constitutional defects, it must be upheld as within congressional power. *Parker* v. *Levy*, 417 U. S. 733, 760 (1974); *Fortson* v. *Secretary of State of Georgia*, 379 U. S. 433, 438–439 (1965); *Aptheker* v. *Secretary of State*, 378 U. S. 500, 515 (1964); see *United States* v. *Raines*, 362 U. S. 17, 20-24 (1960).

Our review of the regulations and guidelines governing administration of the MBE provision reveals that Congress enacted the program as a strictly remedial measure; moreover, it is a remedy that functions prospectively, in the manner of an injunctive decree. Pursuant to the administrative program, grantees and their prime contractors are required to seek out all available, qualified, bona fide MBE's; they are required to provide technical assistance as needed, to lower or waive bonding requirements where feasible, to solicit the aid of the Office of Minority Business Enterprise, the Small Business Administration or other sources for assisting MBE's to obtain required working capital, and to give guidance through the intricacies of the bidding process. *Supra*, at 17. The program assumes that grantees who undertake these efforts in good faith will obtain at least 10% participation by minority business enterprises. It is recognized that, to achieve this target, contracts will be awarded to available, qualified, bona fide MBE's even though they are not the lowest competitive bidders, so long as their higher bids, when challenged, are found to reflect merely attempts to cover costs inflated by the present effects of prior disadvantage and discrimination. *Supra*, at 18–19. There is available to the grantee a provision authorized by Congress for administrative waiver on a case-by-case basis should there be a demonstration that, despite affirmative efforts, this level of participation cannot be achieved without departing from the objectives of the program. *Supra*, at 17–18. There is also an administrative mechanism, including a complaint procedure, to ensure that only bona fide MBE's are encompassed by the remedial program, and to prevent unjust participation in the program by those minority firms whose access to public contracting opportunities is not impaired by the effects of prior discrimination. *Supra*, at 19–20.

(1)

As a threshold matter, we reject the contention that in the remedial context the Congress must act in a wholly "color-blind" fashion. In *Swann* v. *Charlotte-Mecklenberg Board of Education*, 402 U. S. 1, 18–21 (1971), we rejected this argument in considering a court-formulated school desegration remedy on the basis that examination of the racial composition of student bodies was an unavoidable starting point and that racially based attendance assignments were permissible so long as no absolute racial balance of each school was required. In *McDaniel* v. *Barresi*, 402 U. S. 39, 41 (1971), citing *Swann*, we observed that "[i]n this remedial process, steps will almost invariably require that students be assigned 'differently because of their race.' . . . Any other approach would freeze the status quo that is the very target of all desegregation processes." (Citations omitted.) And in *North Carolina Board of Education* v. *Swann*, 402 U. S. 43 (1971), we invalidated a state law that absolutely forbade assignment of any student on account of race because it foreclosed implementation of desegregation plans that were designed to remedy constitutional violations. We held that "[j]ust as the race of students must be considered in determining whether a constitutional violation has occurred, so also must race be considered in formulating a remedy." 402 U. S., at 46.

In these school desegregation cases we dealt with the authority of a federal court to formulate a remedy for unconstitutional racial discrimination. However, the authority of a court to incorporate racial criteria into a remedial decree also extends to statutory violations. Where federal anti-discrimination laws have been violated, an equitable remedy may in the appropriate case include a racial or ethnic factor. *Franks* v. *Bowman Transportation Co.*, 424 U. S. 747 (1976); see *International Brotherhood of Teamsters* v. *United States*, 431 U. S. 324 (1977); *Albemarle Paper Co.* v. *Moody*, 422 U. S. 405 (1975). In another setting, we have held that a state may employ racial criteria that are reasonably necessary to assure compliance with federal voting rights legislation, even though the state action does not entail the remedy of a constitutional violation. *United Jewish Organizations of Williamsburgh, Inc.* v. *Carey*, 430 U. S. 144, 147–165 (1977)

[72] In their complaint, in order to establish standing to challenge the validity of the program, petitioners alleged as "[s]pecific examples" of economic injury three instances where one of their member associations would have been awarded a public works contract but for enforcement of the MBE provision. Petitioners requested only declaratory and injunctive relief against continued enforcement of the MBE provision; they did not seek any remedy for these specific instances of assertedly unlawful discrimination. App. 12a–13a, 17a–18a.

opinion of WHITE, J. joined by BRENNAN, BLACKMUN, and STEVENS, JJ.); *id.*, at 180-187 (BURGER, C. J., dissenting on other grounds).

When we have discussed the remedial powers of a federal court, we have been alert to the limitation that "[t]he power of the federal courts to restructure the operation of local and state governmental entities is not plenary. . . . [A] federal court is required to tailor the scope of the remedy to fit the nature and extent of the . . . violation." *Dayton Board of Education* v. *Brinkman*, 433 U. S. 406, 419-420 (1977) (quoting *Milliken* v. *Bradley*, 418 U. S. 717, 738 (1974), and *Swann* v. *Charlotte-Mecklenburg Board of Education*, *supra*, 402 U. S., at 16).

Here we deal, as we noted earlier, not with the limited remedial powers of a federal court, for example, but with the broad remedial powers of Congress. It is fundamental that in no organ of government, state or federal, does there repose a more comprehensive remedial power than in the Congress, expressly charged by the Constitution with competence and authority to enforce equal protection guarantees. Congress not only may induce voluntary action to assure compliance with existing federal statutory or constitutional antidiscrimination provisions, but also, where Congress has authority to declare certain conduct unlawful, it may, as here, authorize and induce state action to avoid such conduct. *Supra*, at 22-28.

(2)

A more specific challenge to the MBE program is the charge that it impermissibly deprives nonminority businesses of access to at least some portion of the government contracting opportunities generated by the Act. It must be conceded that by its objective of remedying the historical impairment of access, the MBE provision can have the effect of awarding some contracts to MBE's which otherwise might be awarded to other businesses, who may themselves be innocent of any prior discriminatory actions. Failure of nonminority firms to receive certain contracts is, of course, an incidental consequence of the program, not part of its objective; similarly, past impairment of minority-firm access to public contracting opportunities may have been an incidental consequence of "business-as-usual" by public contracting agencies and among prime contractors.

It is not a constitutional defect in this program that it may disappoint the expectations of nonminority firms. When effectuating a limited and properly tailored remedy to cure the effects of prior discrimination, such "a sharing of the burden" by innocent parties is not impermissible. *Franks*, *supra*, at 777; see *Albemarle Paper Co.*, *supra*; *United Jewish Organization*, *supra*. The actual "burden" shouldered by nonminority firms is relatively light in this connection when we consider the scope of this public works program as compared with overall construction contracting opportunities.[72] Moreover, although we may assume that the complaining parties are innocent of any discriminatory conduct, it was within congressional power to act on the assumption that in the past some nonminority businesses may have reaped competitive benefit over the years from the virtual exclusion of minority firms from these contracting opportunities.

[72] The Court of Appeals relied upon Department of Commerce statistics to calculate that the $4.2 billion in federal grants conditioned upon compliance with the MBE provision amounted to about 2.5% of the total of nearly $170 billion spent on construction in the United States during 1977. Thus the 10% minimum minority business participation contemplated by this program would account for only 0.25% of the annual expenditure for construction work in the United States. *Fullilove* v. *Kreps*, 584 F. 2d 600, 607 (CA2 1978).

(3)

Another challenge to the validity of the MBE program is the assertion that it is underinclusive—that it limits its benefit to specified minority groups rather than extending its remedial objectives to all businesses whose access to government contracting is impaired by the effects of disadvantage or discrimination. Such an extention would, of course, be appropriate for Congress to provide; it is not a function for the courts.

Even in this context, the well-established concept that a legislature may take one step at a time to remedy only part of a broader problem is not without relevance. See *Dandridge* v. *Williams*, 397 U. S. 471 (1970); *Williamson* v. *Lee Optical Co.*, 348 U. S. 483 (1955). We are not reviewing a federal program that seeks to confer a preferred status upon a nondisadvantaged minority or to give special assistance to only one of several groups established to be similarly disadvantaged minorities. Even in such a setting, the Congress is not without a certain authority. See, *e. g.*, *Personnel Administrator of Massachusetts* v. *Feeney*, 442 U. S. 256 (1979); *Califano* v. *Webster*, 430 U. S. 313 (1977); *Morton* v. *Mancari*, 417 U. S. 535 (1974).

The Congress has not sought to give select minority groups a preferred standing in the construction industry, but has embarked on a remedial program to place them on a more equitable footing with respect to public contracting opportunities. There has been no showing in this case that Congress has inadvertently effected an invidious discrimination by excluding from coverage an identifiable minority group that has been the victim of a degree of disadvantage and discrimination equal to or greater than that suffered by the groups encompassed by the MBE program. It is not inconceivable that on very special facts a case might be made to challenge the congressional decision to limit MBE eligibility to the particular minority groups identified in the Act. See *Vance* v. *Bradley*, 440 U. S. 93, 109-112 (1979); *Oregon* v. *Mitchell*, 400 U. S. 112, 240 (1970) (opinion of BRENNAN, WHITE, and MARSHALL, JJ.). But on this record we find no basis to hold that Congress is without authority to undertake the kind of limited remedial effort represented by the MBE program. Congress, not the courts, has the heavy burden of dealing with a host of intractable economic and social problems.

(4)

It is also contended that the MBE program is overinclusive—that it bestows a benefit on businesses identified by racial or ethnic criteria which cannot be justified on the basis of competitive criteria or as a remedy for the present effects of identified prior discrimination. It is conceivable that a particular application of the program may have this effect; however, the peculiarities of specific applications are not before us in this case. We are not presented here with a challenge involving a specific award of a construction contract or the denial of a waiver request; such questions of specific application must await future cases.

This does not mean that the claim of overinclusiveness is entitled to no consideration in the present case. The history of governmental tolerance of practices using racial or ethnic criteria for the purpose or with the effect of imposing an invidious discrimination must alert us to the deleterious effects of even benign racial or ethnic classifications when they stray from narrow remedial justifications. Even in the context of a facial challenge such as is presented in this case, the MBE provision cannot pass muster unless, with due account for its administrative program, it provides a reasonable assurance that application of racial or ethnic criteria will be

limited to accomplishing the remedial objectives of Congress and that misapplications of the program will be promptly and adequately remedied administratively.

It is significant that the administrative scheme provides for waiver and exemption. Two fundamental congressional assumptions underlie the MBE program: (1) that the present effects of past discrimination have impaired the competitive position of businesses owned and controlled by members of minority groups; and (2) that affirmative efforts to eliminate barriers to minority-firm access, and to evaluate bids with adjustment for the present effects of past discrimination, would assure that at least 10% of the federal funds granted under the Public Works Employment Act of 1977 would be accounted for by contracts with available, qualified, bona fide minority business enterprises. Each of these assumptions may be rebutted in the administrative process.

The administrative program contains measures to effectuate the congressional objective of assuring legitimate participation by disadvantaged MBE's. Administrative definition has tightened some less definite aspects of the statutory identification of the minority groups encompassed by the program.[73] There is administrative scrutiny to identify and eliminate from participation in the program MBE's who are not "bona-fide" within the regulations and guidelines; for example, spurious minority-front entities can be exposed. A significant aspect of this surveillance is the complaint procedure available for reporting "unjust participation by an enterprise or individuals in the MBE program." *Supra*, at 20. And even as to specific contract awards, waiver is available to avoid dealing with an MBE who is attempting to exploit the remedial aspects of the program by charging an unreasonable price, *i. e.*, a price not attributable to the present effects of past discrimination. *Supra*, at 17-19. We must assume that Congress intended close scrutiny of false claims and prompt action on them.

Grantees are given the opportunity to demonstrate that their best efforts will not succeed or have not succeeded in achieving the statutory 10% target for minority firm participation within the limitations of the program's remedial objectives. In these circumstances a waiver or partial waiver is available once compliance has been demonstrated. A waiver may be sought and granted at any time during the contracting process, or even prior to letting contracts if the facts warrant.

Nor is the program defective because a waiver may be sought only by the grantee and not by prime contractors who may experience difficulty in fulfilling contract obligations to assure minority participation. It may be administratively cumbersome, but the wisdom of concentrating responsibility at the grantee level is not for us to evaluate; the purpose is to allow the Economic Development Administration to maintain close supervision of the operation of the MBE provision. The administrative complaint mechanism allows for grievances of prime contractors who assert that a grantee has failed to seek a waiver in an appropriate case. Finally, we note that where private parties, as opposed to governmental entities, transgress the limitations inherent in the MBE program, the possibility of constitutional violation is more removed. See *United Steelworkers of America* v. *Weber*, 443 U. S. 193, 200 (1979).

That the use of racial and ethnic criteria is premised on assumptions rebuttable in the administrative process gives reasonable assurance that application of the MBE program will be limited to accomplishing the remedial objectives contemplated by Congress and that misapplications of the racial and ethnic criteria can be remedied. In dealing with this facial challenge to the statute, doubts must be resolved in support of the congressional judgment that this limited program is a necessary step to effectuate the constitutional mandate for equality of economic opportunity. The MBE provision may be viewed as a pilot project, appropriately limited in extent and duration, and subject to reassessment and reevaluation by the Congress prior to any extension or re-enactment.[74] Miscarriages of administration could have only a transitory economic impact on businesses not encompassed by the program, and would not be irremediable.

IV

Congress, after due consideration, perceived a pressing need to move forward with new approaches in the continuing effort to achieve the goal of equality of economic opportunity. In this effort, Congress has necessary latitude to try new techniques such as the limited use of racial and ethnic criteria to accomplish remedial objectives; this especially so in programs where voluntary cooperation with remedial measures is induced by placing conditions on federal expenditures. That the program may press the outer limits of congressional authority affords no basis for striking it down.

Petitioners have mounted a facial challenge to a program developed by the politically responsive branches of Government. For its part, the Congress must proceed only with programs narrowly tailored to achieve its objectives, subject to continuing evaluation and reassessment; administration of the programs must be vigilant and flexible; and, when such a program comes under judicial review, courts must be satisfied that the legislative objectives and projected administration give reasonable assurance that the program will function within constitutional limitations. But as Justice Jackson admonished in a different context in 1941:[75]

> "The Supreme Court can maintain itself and succeed in its tasks only if the counsels of self-restraint urged most earnestly by members of the Court itself are humbly and faithfully heeded. After the forces of conservatism and liberalism, of radicalism and reaction, of emotion and of self-interest are all caught up in the legislative process

[73] The MBE provision, 42 U. S. C. § 6705(f)(2) (1976 ed., Supp. II), classifies as a minority business enterprise any "business at least 50 per centum of which is owned by minority group members or, in the case of a publicly owned business, at least 51 per centum of the stock of which is owned by minority group members." Minority group members are defined as "citizens of the United States who are Negroes, Spanish-speaking, Orientals, Indians, Eskimos, and Aleuts." [illegible] Appendix to this opinion [illegible] requirements of the [illegible] Revitalization and Regulatory Reform Act of 1976, 45 U. S. C. § [illegible] 42 Fed. Reg. [illegible] (1977), on which Congress relied [illegible] for the MBE provision. See 123 Cong. Rec. [illegible] The House Subcommittee on SBA [illegible] Minority Enterprise, whose activities played a significant part [illegible] of the MBE provision, also [illegible] that these categories were included within the Federal Government's definition of minority business enterprise." H. R. Rep. No. [illegible] The specific inclusion of these groups in the MBE provision demonstrates that Congress concluded they were victims of discrimination. [illegible] Court of Appeals, there is no reason for the Court to pass upon the issue at this time.

[74] Cf. GAO Report to the Congress, Minority Firms on Local Public Works Projects—Mixed Results, CED-79-9 (Jan. 16, 1979); U. S. Dept. of Commerce, Economic Development Administration, Local Public Works Program, Interim Report on 10 Percent Minority Business Enterprise Requirement (Sept. 1978).

[75] R. H. Jackson, The Struggle for Judicial Supremacy 321 (1941).