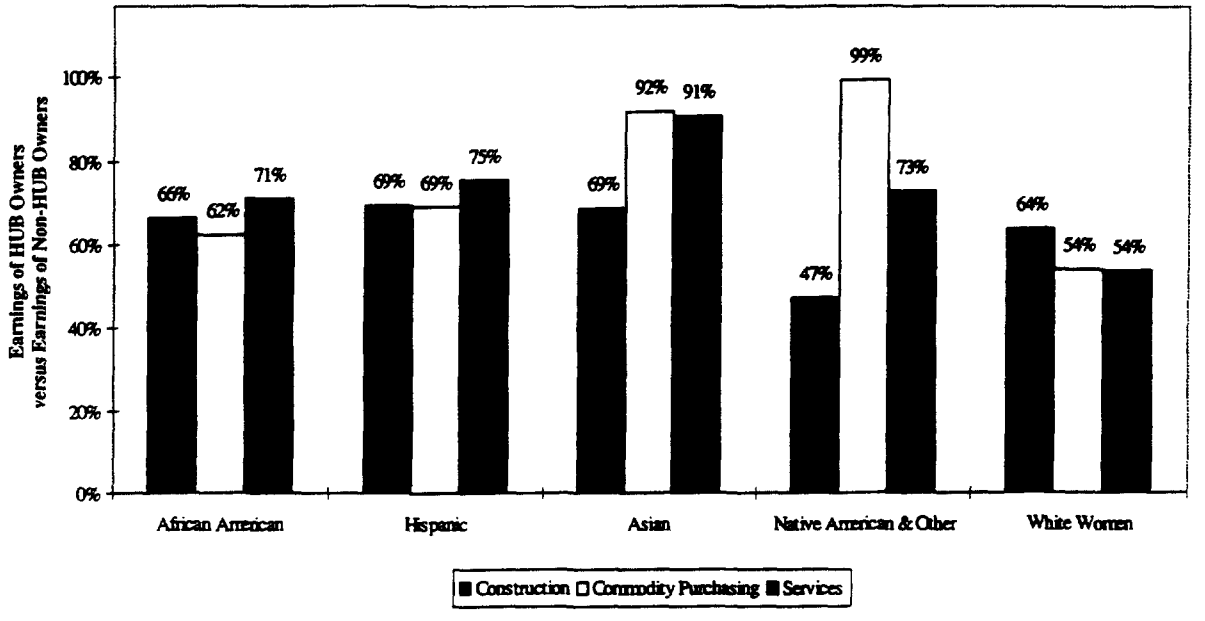
African American, Hispanic and white woman-owned firms are all roughly 10 percent higher (indicating less disparity) in the program period relative to the pre-program period. The disparity ratio for Asian-owned firms in subcontracting was about 37 in the pre-program period, and 121 in the program period, indicating that Asian-owned firms were used as subcontractors more than we would expect during the program period.

The study also conducted several analyses of the success of small businesses owned by minorities and women in the private sector of the State's economy. These analyses were designed, in part, to see whether firm qualifications can explain the underutilization of HUBs reported above.

The first analysis focused on small businesses in Texas. It asked whether HUBs get a smaller share of business revenue than non-HUBs given their availability. It found results strikingly similar to those described above. HUB utilization was less than 80 percent of HUB availability for each procurement category and race/sex group.

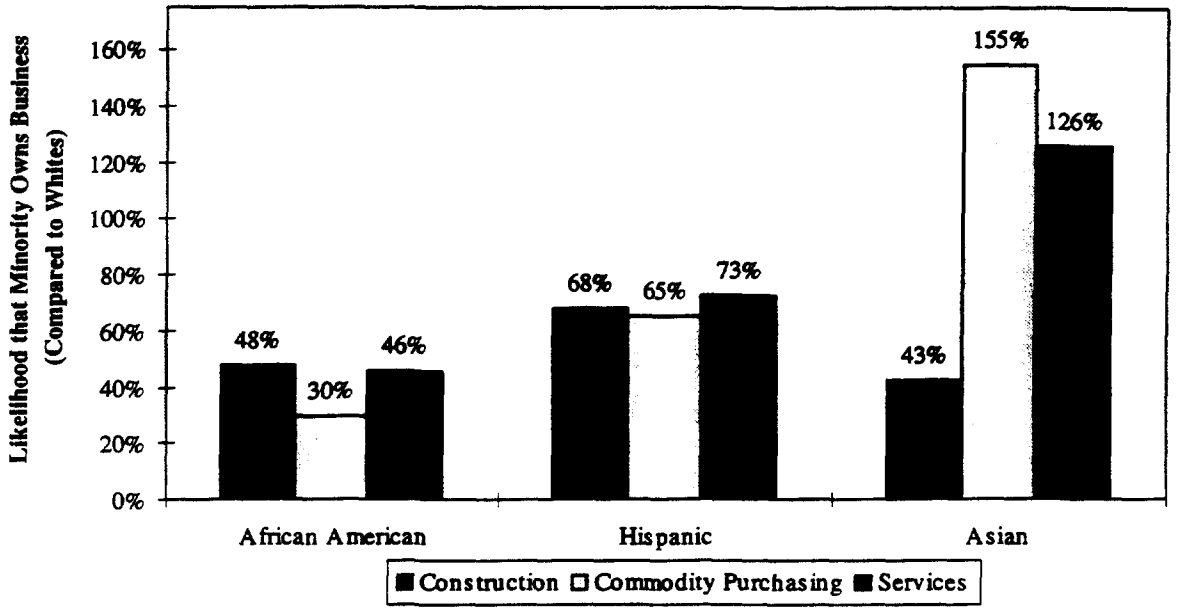
The second analysis focused on the personal earnings of small business owners in Texas. It compared the earnings of HUB owners and non-HUB owners in the same industry and with the same education, age, marital status, assets and other characteristics. It found that minorities and women, with few exceptions, earn substantially less than white men. These disparities are shown in Figure 3.

FIGURE 3
HUB Owners in Every Industry Earn Less from Their Businesses than Non-HUB Owners with Similar Characteristics



The third analysis focused on the formation of small businesses by minorities. It compared the percent of businesses owned by minorities to the percent of businesses owned by non-minorities with similar personal characteristics, such as age, education or wealth. It found that, with the exception of Asians in commodities and services, minorities were substantially less likely to operate a business than non-minorities with similar characteristics. Figure 4 summarizes the findings of this analysis. (A similar analysis could not be conducted for women because it is difficult, statistically, to separate changes in female labor force participation from changes in business ownership patterns over time.)

FIGURE 4
Minorities in Most Industries Are Less Likely to Operate Businesses than Whites with Similar Characteristics



Is the Underutilization of HUBs the Result of Discrimination?

In each of the study's analyses, HUBs are found to be doing less well than non-HUBs. There are fewer businesses owned by minorities in Texas than one would expect based on the number and qualifications of minorities in Texas. Businesses that are owned by minorities and women do not earn as much money for their owners as do businesses that are owned by white men with similar socioeconomic characteristics. Of the revenues earned by small businesses in Texas, HUBs get a smaller share than one would expect given HUBs' presence in the marketplace. And, finally, HUBs get a smaller share of State spending than one would expect based, again, on HUBs' presence in the marketplace. But are these conditions the result of discrimination or of other obstacles we have not identified? To help answer this question, the study looked for direct evidence of discrimination from several sources.

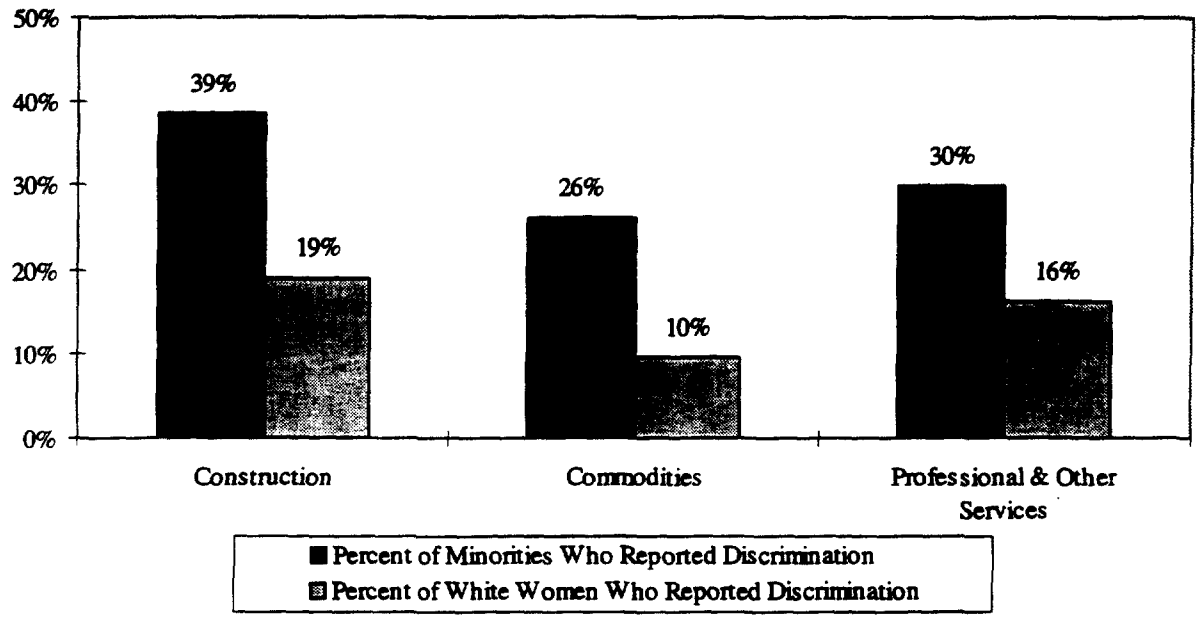
General Discrimination in Texas

Before there were strong legal and social sanctions against discrimination, people could discriminate overtly. There was a time when individuals could openly refuse to deal with members of race or sex groups they disliked and suffer no legal penalties or social reproach. Strong discrimination laws and changes in social mores have reduced discrimination. But they have also made discrimination more covert. The study reviewed court decisions and reports that documented evidence of discrimination in employment, housing, lending and public accommodations in Texas. For example, several recent studies have found discrimination in insurance and mortgage lending, and a number of companies in Texas were found guilty of employment discrimination in the 1980s.

Survey of HUBs

The study obtained survey responses from 4,763 HUBs. These HUBs were asked whether and in what circumstances they had experienced discrimination. Overall, 22.8 percent indicated that they had personally experienced at least one instance of discrimination in business dealings in the last five years. That percent varied from 48.4 percent for African American-owned construction firms to 9.7 percent for white female-owned commodity firms. In general, HUBs most commonly reported problems in the area of obtaining commercial credit and bonds. The industry in which HUBs reported the greatest incidence of discrimination was construction. Figure 5 summarizes these findings for minorities and white women.

FIGURE 5
Minorities and White Women Both Reported Experiencing Discrimination in the Last Five Years
(Based on Respondents to NERA's Mail Survey)

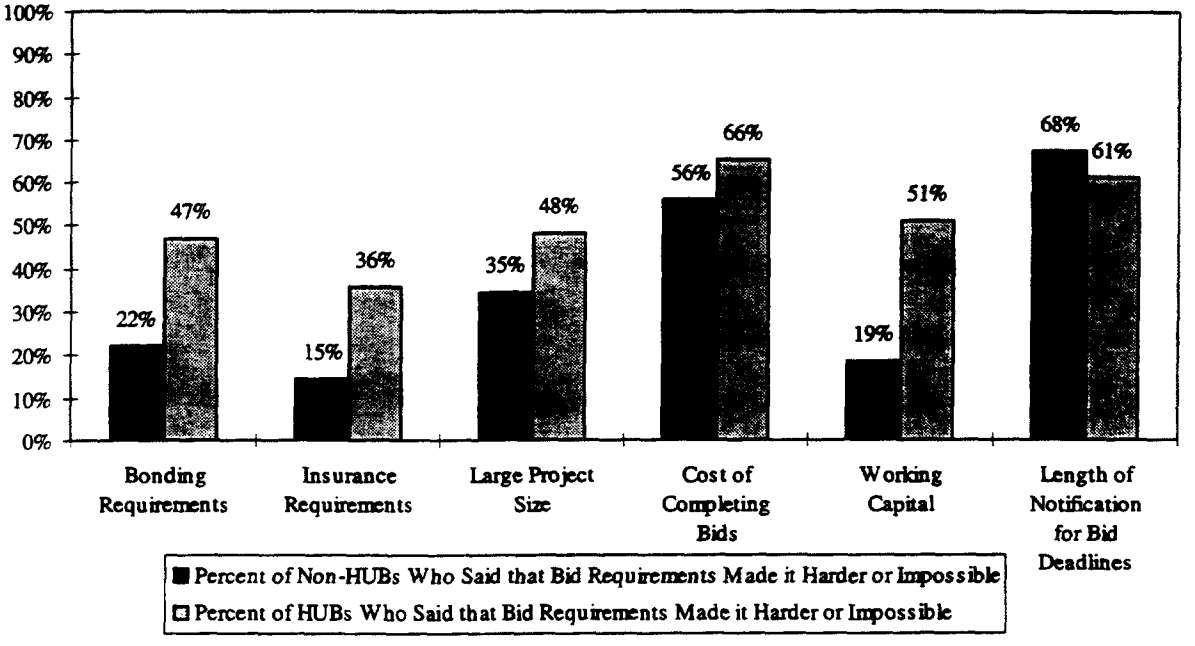


Comparison of HUBs and Non-HUBs

The study also obtained survey responses from 804 non-HUBs. The non-HUBs and HUBs were asked similar questions concerning whether certain bid requirements made it harder or impossible to obtain a contract from the State. In almost all cases, HUBs were more likely to report that a requirement made it harder or impossible to obtain an award. Figure 6 reports a sample of the results of these surveys for HUB and non-HUB construction firms.

To consider the possibility that it is harder for HUBs to obtain State contracts because these firms are newer or smaller than non-HUBs, the study compared responses for HUBs and non-HUBs that were similar in terms of age, revenue and employment. The study found that even after controlling for these differences between HUBs and non-HUBs, HUBs reported significantly more difficulty.

FIGURE 6
In Most Cases, More HUB than Non-HUB Construction Firms Report that Bid Requirements Make It Harder or Impossible to Obtain An Award



Personal Interviews

As part of the study, 300 interviews were conducted with HUB owners and 27 interviews were conducted with non-HUB owners. Many of the HUB owners reported that they were treated adversely in business dealings for reasons based on race or sex. Many of those interviewed said that they were treated more adversely than similar white-male owned firms. For example, several minority business owners reported that they had been turned down for financing or bonding when non-HUBs in less favorable financial positions were approved. Similarly, female business owners reported that they could get financing only if they asked a man to present their case. Finally, both minority and female businesses owners reported receiving higher prices from suppliers than those received by white men.

Of the complaints of discriminatory treatment in business, the largest number we heard during interviews concerned general unwillingness to work with HUBs, followed by complaints relating to sham good faith efforts, financing and problems related to the bidding process. Other areas in which HUB

representatives complained of discriminatory treatment included dealings with suppliers, obtaining bonds and insurance, late payments and certification.

While those interviewed signed written statements confirming their oral interviews, the study did not independently verify any of their claims.

III. How Can the State Assist HUBs?

The study addressed two types of measures for helping the State improve its utilization of businesses owned by minorities or women.

(1) *Race/Sex-Neutral Measures* are measures that (a) help all small businesses and thereby indirectly help HUBs most of which tend to be small. or that (b) directly help HUBs by providing direct financial or technical assistance or by modifying bid requirements that have a disparate impact on HUBs. These measures stop short of actually giving a preference to HUBs that bid on State contracts as prime or subcontractors.

(2) *Race/Sex-Conscious Measures* are measures that directly increase HUB participation on State procurements by giving HUBs some form of preference as either prime contractors or subcontractors.

The appropriate mix of these measures for any State or agency to adopt depends on a variety of economic, policy and legal judgements that were outside the scope of this study. The Legislature, General Services Commission and other select State agencies will need to decide what strategy to pursue.

The effectiveness of race/sex-neutral and race/sex-conscious remedies varies according to the particular problem they are designed to remedy. Race/sex-neutral remedies are more effective at addressing problems that affect all small businesses and that have a disparate impact on HUBs primarily because HUBs are small. Race/sex-conscious remedies are more effective at addressing problems that result directly from race or sex discrimination.

The direct and indirect cost of administering remedies also varies. The direct costs of a remedy includes the cost of administering the remedy including hiring staff and possibly making direct payments to participating businesses. The indirect costs of a remedy include inefficiencies introduced into the

bidding process and indirect payments to participating businesses as a result of, for example, not awarding contracts to the lowest qualified bidder.

What Non-Preference Measures Could the State Consider?

Bonding, information access, financing, training deficiencies and competition from large firms all serve as obstacles to HUB participation in State contracts. Some solutions to these obstacles that would help all small businesses win more State contracts include the following:

> ***Bonding***—All small businesses, HUBs and non-HUBs, would be helped by reduced bonding requirements on bids for smaller contracts and waivers on performance bonds for smaller contracts. Alternatively, small businesses would benefit from referral to bonding assistance programs that might help them obtain bonds. The State could also consider imposing a specific prohibition against race or sex discrimination by surety companies.
>
> ***Information***—Small businesses can be provided with increased information about procurement opportunities in a variety of ways including focus sessions and pre-bid conferences, procurement newsletters or a procurement hotline. The conferences and focus sessions have the added feature of nurturing networking and contacts among vendors.
>
> *Capital*—Small businesses are often hampered by difficulties managing their flow of capital. Loans would be one way of smoothing these difficulties, as would the adoption of mandatory prompt payment procedures for prime contractors and subcontractors.
>
> ***Competition from Large Firms***—Different programs can assist all small businesses in competing with large firms. Such programs can be as direct as a small business preference program, or more indirect, such as programs to enhance procurement officers' awareness of available small businesses, or referrals to small business assistance programs such as those operated by the U.S. Department of Commerce.

What Preference Measures Could the State Consider?

Since the 1989 Supreme Court decision—*City of Richmond v. J. A. Croson & Co.*—that struck down Richmond's program to set aside 30 percent of the City's construction spending for minority firms, the courts have carefully scrutinized race-based preferences granted by state and local governments. Under *Croson*, a state or local government may adopt race-based classifications if it demonstrates that the use of the classification is justified by a compelling governmental interest and that the race-conscious measures are *narrowly tailored* to remedy that discrimination. Race-conscious remedies that are not based on a detailed record of discrimination against minority businesses, that include groups for which there is no

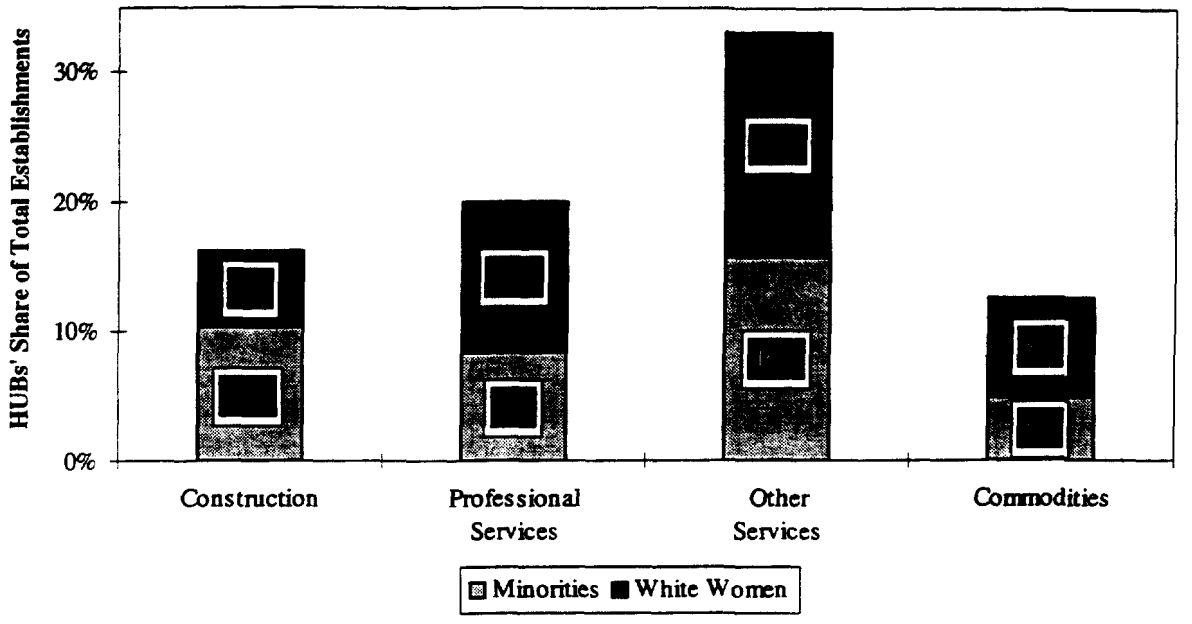
evidence of discrimination, or that are especially onerous on non-minority businesses are likely to be struck down by the courts. Sex-conscious remedies are held to a less strict standard by the courts.

Where there is evidence that the state or local governmental entity would become a passive participant in marketplace discrimination, however, it is permissible for the government to use narrowly tailored race and sex-based preferences. If the Texas Legislature, General Services Commission or another agency chooses to implement some sort of preference program, it would have to be careful to include certain attributes that an appropriate preference program should possess.

> ***Flexibility***—The preference mechanism should be flexible. For example, a program that asks prime contractors to subcontract a certain portion of the work to HUBs should provide waivers in those instances where the prime can show that HUBs are not available or that their use would be uneconomic.
>
> ***Program Length***—The program should have a sunset provision after which the program could be reinstated only after a further review of discrimination and its effects.
>
> ***Geographic Scope***—Some courts have indicated that the program should only benefit firms that have actively tried to do business in the government's jurisdiction. Therefore, out-of-state firms should probably be included only if they can make this showing.
>
> ***Identity of Disadvantaged Groups***—Only groups for which there is *specific* evidence of discrimination should be able to obtain the preferences.
>
> ***Setting Goals***—Goals, such as those in the State's HUB Program, should be based on an objective measure of HUB availability. Figure 7 reports availability based on the percent of all establishments with at least one paid employee that are owned by minorities or women. Some courts suggest that it may be permissible to set goals higher than actual availability in some circumstances. Unrealistically high goals, however, often lead to fraud and abuse.
>
> ***Enforcing Goals***—Without vigorous enforcement of the goals and vigilant attention to potential abuses, goal programs can fail to provide meaningful assistance to HUBs. Officials need to ensure that HUBs are actually paid for the work they are doing, that HUBs are providing a commercially useful function and that HUBs are legitimate minority or woman-owned businesses.

Without vigorous enforcement and vigilant attention to potential abuses, goal programs easily can fail to provide much meaningful assistance to HUBs. For example, some studies have found that the absence of fraud penalties tends to encourage the development of front firms; in contrast, strong

FIGURE 7
The Actual Availability of HUBs in Texas



certification programs, along with financial and technical assistance, tends to encourage minority business development. When problems arise, they tend to occur in the following areas:

> ***Certification Fraud***—Businesses that are not owned and controlled by members of the protected classes covered by the program may try to get certified as HUBs. This problem can be widespread. For example, one study reports that after an investigation of the certified minority or woman-owned firms that had received contracts from the City of Indianapolis, the City revoked the certification of 30 percent of these vendors. Frequently, these situations arise when a husband and wife or father and daughter put the ownership of the business in the name of the woman and falsely attempt to persuade certifying authorities that the woman has active control over the business. Another common problem is where majority firms establish a HUB primarily for the purpose of evading the program. For example, a Baltimore County Grand Jury found that "a great number of certified minority businesses have traded the opportunity to gain a foothold in the construction industry for the quick profit available from selling the use of their MBE name to nonminority firms." One approach to these problems is prevention: conducting more careful certifications of HUBs and reviewing these certifications periodically. Unfortunately, this solution often creates its own problems: excess bureaucracy, delays in certifying firms, and the possibility that legitimate HUBs will not get certified. A second approach is discouragement: firms may be less likely to undertake fraud if they face regular investigations and stiff penalties if found guilty of system abuses.
>
> ***Follow-Through***—Majority primes do not meet the HUB participation levels specified in their contracts. This can arise in several ways. First, HUB subcontractors are replaced

with non-HUB contractors. Second, HUB subcontractors are not used to the extent originally agreed upon in the contract. Third, HUB subcontractors are not paid in full for the work they perform. Fourth, as a result of change orders the dollar value of the contract increases but HUBs are not used for the additional work. Careful verification can combat these problems: an agency could require the majority prime contractor, possibly as a condition of receiving payments, to provide documentation, such as cancelled checks from the HUBs, that they have met their goals.

Nominal Use—Majority primes meet the goals on their contracts in ways that do not create meaningful business opportunities for HUBs. For example, as mentioned above, primes may try to meet the goals by having HUB subcontractors pay for goods and services that the primes would ordinarily purchase. To take another example, majority firms may simply pay the HUB a fee for having the HUB on the project but not have the HUB actually perform useful business functions. While the HUB may find this satisfactory, it obviously defeats the purpose of the program. To correct these sorts of problems, agencies need to make sure that only firms that perform commercially useful functions get certified. Moreover, during the course of the project, agency officials need to check that the HUBs named on the project are performing commercially useful work.

The State of Maryland is one example of a jurisdiction that has effectively combined race/sex-neutral and race/sex-conscious remedies. The State has several financial assistance programs, such as a surety bond program, that are targeted to small businesses. It also has financial assistance programs, such as one to assist providing working capital for government contracts, to businesses owned socially or economically disadvantaged persons. Finally, it has a goals-based program, with waiver provisions for contractors that cannot legitimately meet the goals. The State also aggressively investigates and prosecutes fraudulent abuses of the program. Many other jurisdictions have adopted unyielding quotas (e.g., the City of Detroit) and have had their programs enjoined by the courts.

Unfortunately, there is little evidence on whether and to what extent race/sex-neutral or race/sex-conscious measures have achieved their objectives or have done so in a cost–effective manner. The State of Texas will certainly want to review programs developed in other jurisdictions and proceed carefully in developing its responses to the findings of this study.

IV. Concluding Remarks

This executive summary has presented the major findings of the State of Texas Disparity Study and has highlighted some of the key pieces of evidence upon which those findings are based. The study has

found that marketplace discrimination makes it harder for HUBs to compete for business from the State as prime or subcontractors. The State's HUB Program has had only a modest effect offsetting these competitive disadvantages. To the extent that any of these disadvantages arise because more HUBs than non-HUBs tend to be small and new, the State could consider expanding or instituting programs targeted to assist all small businesses, rather than focusing only on race or sex-specific remedies.

The Legislature or certain State agencies may decide that more direct and specific remedies could be useful to offset the effects of marketplace discrimination. To this end, the State may wish to consider improving the effectiveness of its HUB Program through greater enforcement and supervision, through adopting other measures to help offset the consequences of marketplace discrimination, and through implementing programs for assisting small businesses in general. It is now up to the Texas Legislature and certain State agencies to consider appropriate courses of action.

CHAPTER 1
INTRODUCTION

This report was authorized pursuant to House Bill 2626 of the 73rd Legislature of the State of Texas, with overwhelming bi-partisan support, to examine the performance of the State's Historically Underutilized Business (HUB) Program and to assess the program's compliance with the requirements of *City of Richmond v. J.A. Croson Co.*[1] The HUB Program, established in 1991, encourages State agencies to procure goods and services from minority and woman-owned businesses. To pursue this inquiry, the report examines:

[1] 488 U.S. 469 (1989).

- whether, and to what extent, HUBs have experienced discrimination in the State of Texas; and

- possible remedies for eradicating or offsetting the effects of discrimination, where found, on the ability of HUBs to participate in State procurement opportunities.

Consistent with State law, we refer to businesses owned by minorities and women as "Historically Underutilized Businesses" (HUBs).[2]

This report is divided into eight chapters. This introductory chapter presents some basic economic and demographic information on the State of Texas. The rest of the report documents the experience of HUBs in doing business *with* the State of Texas and *in* State of Texas. The remaining chapters address the following questions:

Chapter 2: How does the State procure goods and services?

Chapter 3: How are HUBs utilized by the State and how does that utilization compare to the availability of HUBs in the marketplace?

Chapter 4: How are HUBs utilized in the private sector and how does their utilization compare to their availability in Texas?

Chapter 5: Are minorities less likely than whites to start businesses and, if so, is this due to discrimination? Does discrimination reduce the earnings women and minorities obtain from businesses they establish?

Chapter 6: Do HUB owners believe they are discriminated against and, if so, what are the areas of business dealing in which they feel the pressure of discrimination?

Chapter 7: What is the current state of the law concerning affirmative-action plans developed for nonfederal entities such as the State?

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[2] Art. 601b, Tex. Civ. Stat. (Vernons 1994) §§ 102(3), 1.03. The State Purchasing and General Services Act contains specific provisions regarding HUBs. Effective September 1, 1991, the statute identifies a HUB as a businesses owned by one or more persons who "are socially disadvantaged because of their identification as members of certain groups, including black Americans, Hispanic Americans, women, Asian Pacific Americans, and Native Americans, and have suffered the effects of discriminatory practices or similar insidious circumstances over which they have no control..." These persons must own at least 51 percent of the business and must demonstrate active participation in the control, operation, and management of the firm.

Chapter 8: What does the evidence collected in this study show concerning the extent of discrimination against businesses owned by particular race, ethnic and sex groups?

In assessing these questions, we undertake statistical analyses that compare utilization to availability, and we look at direct evidence from surveys, public hearings and interviews, as well as evidence found in academic, journalistic, and legal literature. Finally, we look closely at the constitutional limits defined by the U.S. Supreme Court in *City of Richmond v. J.A. Croson Co.*, which struck down Richmond's minority business set-aside program.[3] According to *Croson* and related decisions, a non-federal entity may adopt a preference program based on race if it demonstrates that the use of such preference is justified by a compelling governmental interest and that the race-conscious remedies enforced by the program are narrowly tailored to address racial discrimination. We also discuss a variety of methods to remedy problems that hinder HUBs in competing for public-sector procurement awards.

Before proceeding, it will prove useful to say a few words about Texas and the makeup of its population and economy. Texas is the second largest state in the nation with a population of over 17 million in 1990.[4] Its major cities include Houston, Dallas, San Antonio, El Paso, Austin and Fort Worth and three of its Metropolitan Statistical Areas (MSAs)—Houston, Dallas/Ft. Worth and San Antonio—rank in the top ten most populated metropolitan areas in the country. In 1990, roughly 83 percent of all Texans lived in metropolitan areas.[5]

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[3] 488 U.S. 469 (1989).

[4] U.S. Bureau of the Census, *Statistical Abstract of the United States: 1993* (113th edition) Washington, D.C., 1993, p. 43.

[5] *Id.*, p. 36.

Today, the Texas economy enjoys a diversity unique in the State's history. Texas leads all states in oil production, natural gas production, and oil refining capacity. In addition, other industries, such as agriculture (e.g., cotton and cattle), high technology (e.g., computers and telecommunications equipment) and services (e.g., medical services and research) also prove important in the current economy. Agricultural production, which dominated state revenues before oil and gas took over as the main industry in the 1900's, remains important as Texas ranks among the top five states in annual crop value. In addition, as the price of crude oil fell to below 10 dollars per barrel on March 16, 1986, the Texas economy took an historic turn. In 1980, the oil and gas industry accounted for 23.2 percent of state revenues. This year, the Comptroller's Office estimates that the industry will make up only 11.8 percent of the gross state product.

Texas led the country in job creation from 1990 through 1993. In the nation as a whole and in Texas specifically, job growth in the service sector outpaced all other sector growth. In addition, during a time period in which the number of manufacturing jobs in the nation fell, Texas gained manufacturing jobs.

The State of Texas possesses a diverse work force. In 1990, minorities accounted for approximately 34 percent of the State's work force as shown in Table 1.1. Hispanics were the largest minority group, accounting for over 20 percent of the State's work force.[6] Most Hispanics in Texas are of Mexican descent. African Americans are the next largest minority group, accounting for just over 10 percent of the work force. Asians, consisting of Asian Pacific (1.8 percent) and Asian Indian (0.3 percent), are the third largest group. Native Americans account for 0.4 percent of the State's work force. Finally, white women comprise about 27 percent of the work force.

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[6] Individuals of Hispanic ethnicity can belong to several race groups. To eliminate double counting, we count Caucasian Hispanics as Hispanics and Hispanics of other race groups (e.g., African American) in those respective groups.

TABLE 1.1

RACE AND SEX COMPOSITION OF TEXAS WORK FORCE AND BUSINESS OWNERS

Race/Sex Group	Percent of Work Force[1]	Percent of Business Owners[2]
African American	10.41%	3.95%
Hispanic		
Mexican	18.70	12.74
Other[3]	1.94	1.77
Asian & Other[4]		
Asian Pacific	1.78	2.18
Asian Indian	0.34	0.52
Native American	0.43	0.35
Other	0.01	0.00
Total Minorities	33.61	21.51
White Women	27.21	19.80

Note [1]Restricted to the employed civilian labor force, non-farm workers, over age 18 that were employed full-time in 1989.
[2]Individuals who work primarily for their own incorporated and unincorporated business.
[3]Other includes Central Americans, South Americans, Puerto Ricans, Dominicans, and other Hispanics.
[4]Other is defined by Census as non-white, but without specific race group.

Source *1990 United States Census of Population and Housing*: Public Use Microdata Samples, U.S.

We see a similar diversity in the ownership of small businesses in Texas.[7] In 1990, there were 110,476 small business owners in Texas of which 45,656 were minorities and women. Minorities accounted for approximately 21.5 percent and white women 19.8 percent of all small business owners. Of the minority business owners, Hispanics accounted for the largest percent, followed by African Americans and then Asians. The race, ethnic and sex composition of the small

[7] These are individuals who work primarily for their own incorporated or unincorporated business.

business population mirrors, but only to a degree, that of the work force. The percentage of business owners for each minority group, except Asian Pacific and Asian Indian, is lower than their percentage of the work force.

CHAPTER 2
STATE PROCUREMENT PROGRAMS

Assessing the State of Texas's HUB utilization requires an understanding of the way the State procures goods and services, State laws governing procurement, and HUB programs. This chapter answers the following questions:

- What are the State laws governing the HUB program?
- How does the State and its agencies procure different types of goods and services?
- How do State procurement laws affect HUBs?
- What race and gender neutral efforts does the State make to assist small businesses seeking State contracts?

Obtaining work in the public sector is invariably a more difficult, time-consuming, and complex process than in the private sector. Bids involve more paperwork, and successful public sector bidders often face stiffer requirements, such as insurance and bonding, than private sector bidders. Yet it is also a process that, at least ostensibly, is more open than the private sector, where long-standing relationships between businesses are hard to make and hard to break. For example, construction contracts in the public sector almost always are awarded to the lowest bidder, even one unfamiliar to the public agency that has solicited the bid. Therefore, public-sector procurement presents a significant opportunity for newer firms that have not yet developed the reputation and contacts that are invaluable in the private sector.

The opportunities and difficulties associated with public-sector procurement are magnified for HUBs that may be victims of discrimination. For example, it may appear less likely that discrimination would preclude HUBs in construction from obtaining public-sector work than from obtaining private-sector work because awards to the lowest bidder are ostensibly color blind. But discrimination may raise certain costs to HUBs and thereby make it more difficult for them to submit low bids. For example, public-sector requirements such as bonding may be difficult for HUBs to meet if either a history of social discrimination has impeded the accumulation of wealth by minorities or contemporary private-sector discrimination continues to make it difficult for HUBs to obtain bonding and financing. We will discuss the evidence of this difficulty in Chapter 6.

The extent to which public-sector procurement presents opportunities or obstacles for HUBs depends in large part on state and local procurement laws. These laws dictate the rules for soliciting and evaluating bids and present the requirements successful bidders must satisfy. Agency procurement practices regarding the size and scope of projects put out for bid, notification of bid opportunities, and the time available for preparing a bid can also have a significant impact on

potential bidders. HUB opportunities can be affected by various affirmative-action efforts that public-sector agencies may use.

The State of Texas spends billions of dollars each year in procuring a wide variety of goods and services. From FY89 through FY93, the State spent approximately $9 billion dollars on construction, $0.6 billion on professional services, $1.6 billion on other services, and $3.3 billion procuring supplies and equipment.[8] This expenditure level not only provides tremendous business opportunities, but also presents substantial obstacles for HUBs and non-HUBs alike. This chapter reviews the relevant state procurement laws and regulations; the procurement practices followed by the State agencies and institutions included in this report; and the affirmative efforts those public entities employ to increase HUB participation.

I. State of Texas Procurement Laws and Regulations

A. Historically Underutilized Businesses

The State Purchasing and General Services Act contains specific provisions regarding HUBs. Effective September 1, 1991, the statute identifies a historically underutilized business using certain criteria. First, owners of such businesses must be persons who:

> are socially disadvantaged because of their identification as members of certain groups, including black Americans, Hispanic Americans, women, Asian Pacific Americans, and Native Americans, and have suffered the effects of discriminatory practices or similar insidious circumstances over which they have no control; . . . and [who] have a proportionate interest and demonstrate active participation in the control operation, and management of the [business] affairs.[9]

Second, these persons must meet minimum ownership thresholds. Specifically, if the legal form of the business is a corporation or a partnership, the socially disadvantaged person or persons must own

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[8] Chapter 3 presents specific detail about state expenditures during the study period.

[9] Art. 601b, Tex. Civ. Stat. §§ 1.02(3), 1.03 (Vernon's 1994).

at least 51 percent of the corporation's stock (or other equitable securities) or partnership's assets and interest. If the business is a sole proprietorship, the socially disadvantaged person(s) must have 100 percent ownership, operation, and control of the business.[10]

The statute mandates that the General Services Commission (GSC) certify HUBs and provide them training and assistance with State procurement procedures. The GSC must compile a directory of HUBs on a semiannual basis and provide the directory to each State agency. The GSC and the other State agencies must use this directory in soliciting bids for State purchasing and public works contracts. Also, the GSC must prepare a semiannual report which details the total number and dollar amount of contracts awarded and actually paid to HUBs. The statute also requires the GSC to encourage the use of HUBs, assist State agencies in seeking HUBs capable of meeting their needs, and help State agencies to increase the volume of business awarded to HUBs.

B. Purchasing System

1. Construction

Under the State Purchasing and General Services Act,[11] the GSC is authorized to acquire real and personal property, modernize, remodel, build, and equip buildings for State purposes.[12] The GSC is responsible for administering construction projects for all State agencies except those statutorily excluded.[13] In some circumstances, the GSC can delegate administration of a construction project to

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[10] *Id.* The statute also recognizes joint ventures where each entity is a HUB, or a supplier contract where a HUB is one of the parties in a prime contractor-supplier relationship under certain limited circumstances.

[11] Art. 601b, Tex. Civ. Stat. § 1.01 *et seq* (Vernon's 1994).

[12] *Id.*, § 5.01.

[13] Of those State entities surveyed for purposes of this study, the institutions of higher education (University of Texas at Austin, University of Texas System, Texas A&M University at College Station and Texas A&M University System) and the Departments of Transportation, Criminal Justice and Parks and Wildlife are among those statutorily excluded. Art. 601b Tex. Civ. Stat. § 5.13 (Vernon's 1994). Construction for the Department of Mental Health and Mental Retardation also is exempted from the GSC's control. Tex. Health & Safety

the individual State agency. According to the GSC, such delegation is done on a case-by-case basis with no pre-set monetary threshold.

All new construction contracts for the State are solicited on a competitive bid basis according to rules and procedures spelled out by statute.[14,15] In general, public notice of a construction opportunity must be placed in two or more newspapers of general circulation at least thirty days prior to the bid opening date. Only those bidders who are qualified to bid can obtain the bidding documents. A contractor can become qualified to bid for a particular project by filling out the GSC's Contractor Qualification Form. This form solicits information regarding a contractor's previous experience, financial condition, and bonding capacity, and requests financial and construction-related references.[16] All qualified bidders must include a 5 percent bid bond with their completed bidding documents.[17]

After all bids are received, the GSC or the administering State agency must award the project to the "lowest and best" bidder.[18] Any State agency entering into a contract for a construction project

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Code § 551.007.

[14] 1 Tex. Admin. Code § 115.9.

[15] *Id.* § 123.

[16] The determination of qualifications based on information from these forms is specific only to the individual project for which the contractor is currently bidding. A determination that a contractor is qualified to bid on a particular construction project does not apply automatically to other projects for which the GSC or another State entity has construction procurement responsibilities. The contractor must repeat the process for each project he or she wishes to bid on.

[17] Normally, the bidder receives notice of whether the GSC has found the bidder to be qualified, but the bidder need not provide proof of insurance or a payment or performance bond prior to award of the contract. *Id.* § 123.19(e).

[18] Art. 601b, Tex. Civ. Stat. § 5.20(c) (Vernon's 1994); 1 Texas Admin. Code § 123.19(a).

must also make a good faith effort to assure that HUBs receive not less than 30 percent of the total value of each construction contract.[19]

2. Commodity Purchasing

In addition to its general authority to administer construction projects, the GSC is required to purchase all supplies, materials, services, and equipment for all State agencies.[20] However, the GSC may delegate these purchasing functions to a State agency or institution of higher education. Certain procurement rules, including the threshold below which delegation is allowed, changed beginning with FY93. Prior to that time, the individual State agencies had independent authority to purchase supplies, materials, and equipment so long as the purchase did not exceed $5,000. By rule, the GSC could delegate purchasing authority to the agencies when the purchase exceeded $5,000. Beginning in FY93, individual agencies have the authority to handle purchases of goods for $10,000 or less; the GSC has jurisdiction over purchases only if the contract price exceeds $10,000.[21]

Regardless of whether the GSC or the individual agencies purchase supplies, materials, services, or equipment, certain statutory and regulatory procurement procedures must be followed. For FY89 through FY92, the majority of the study period, individual agencies could make purchases of commodities only up to $5,000. Purchases up to $1,000 required no bid. Purchases from $1,000.01 to $2,500 required at least three informal bids and purchases from $2,500.01 to $5,000 required a minimum of three formal bids. For purchases in excess of $5,000, the GSC handled the

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[19] Art. 601b, Tex. Civ. Stat. § 5.36 (Vernon's 1994).

[20] Art. 601b, Tex. Civ. Stat. § 3.01 *et seq* (Vernon's 1994). The regulations we describe in this section for purchases of services apply to all services except for professional and consulting services, which are described in later sections.

[21] 1 Tex. Admin. Code § 113.11.

bid process by sending invitations to bid to all firms on its bidders list. Agencies had authority to procure services up to $100,000, but were required to secure GSC approval of all bid specifications.

TABLE 2.1

GSC'S 1993 PURCHASING REQUIREMENTS FOR COMMODITIES

Dollar Amount	Requirements
Up to $1,000	Purchase delegated to individual agency; no bid required.
$1,000.01 to $5,000	Purchase delegated to individual agency; at least three informal bids required; at least one bid must be from minority-owned business and at least one must be from woman-owned business.
$5,000.01 to $10,000	Purchase delegated to individual agency; at least three formal (written) bids required; at least one bid must be from minority-owned business and at least one must be from woman-owned business.
$10,000.01 and more	Purchase handled by GSC.

Source: GSC Rule 113.11.

Beginning in FY93, procedures changed somewhat. The GSC's 1993 purchasing requirements for commodities are described in Table 2.1. Generally, competitive bidding is required unless the purchase is for $1,000 or less. In those instances where competitive bidding is required, purchasers must obtain at least three competitive bids from sources that normally offer for sale the merchandise being purchased. Under current GSC regulations, at least one of these bids must come from a minority-owned business and at least one must come from a woman-owned business.[22]

The GSC's 1993 purchasing requirements for services, generally, are described in Table 2.2. These requirements differ from the GSC's commodity purchasing requirements primarily in the dollar

[22] 1 Tex. Admin. Code § 113.11(e)(l)(A). The GSC did not require agencies to solicit bids from HUBs until FY93, which began on September 1, 1992.