CITY OF BALTIMORE
STEPHANIE RAWLINGS-BLAKE, Mayor

DEPARTMENT OF LAW
GEORGE A. NILSON, City Solicitor
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Baltimore, Maryland 21202

April 29, 2016

The Honorable President and Members
of the Baltimore City Council
Attn: Natawna Austin, Executive Secretary
Room 409, City Hall
100 N. Holliday Street
Baltimore, Maryland 21202

Re: City Council Bill 16-0619 -- Minority and Women's Business Enterprises - Small Local Business Enterprise Procurement Preferences

Dear President and City Council Members:

City Council Bill 16-0619 establishes and implements a small, local business enterprise procurement preference to be administered by the Minority and Women's Business Opportunity Office which creates goal setting committees, defines eligibility, establishes graduation and suspension criteria for qualifying businesses, implements "affirmative procurement initiatives" requires certain reports, reviews, hearings and appeal procedures and imposes penalties for violation of the program. Chapter 3 of the proposed ordinance establishes small local business procurement requirements. The bill calls for the creation of a Goal Setting Committees for specific industry categories that would establish participation goals for small local businesses in city contracts and select the appropriate affirmative procurement initiative to be applied to each contract. These initiatives include bonding and insurance waivers, bid incentive, price preferences, sheltered markets contracts, mandatory subcontracting, competitive business development demonstration projects and evaluation preference points in the scoring of proposals.

The program goes significantly further than the current MWBE program and raises constitutional and charter issues.

Local Preference Requirements

To be eligible for the program, a business must be individually owned, not controlled or influenced by another business and maintain an office in the City and obtain 50% of its overall sales through that office, have no more than 50 employees in the last year, meet certain annual gross revenue limits and not received more than a certain amount in payments under City contracts. Giving benefits to "local" businesses as defined by the bill raises several constitutional issues.

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Although a business would not have standing to bring a Privileges and Immunities claim, an individual who is denied these benefits because his business does not qualify could have standing. As we have advised many times in the past, discriminating against nonresidents would only survive a Privileges and Immunities claim if the City obtained statistical proof that nonresidents contributed to the "evil" at which the program is aimed (underutilization of local businesses). No such proof is referenced in the bill. Although this program technically gives benefits to businesses rather than individuals, the distinction is without a difference. The practical effect would discriminate against nonresident workers and their businesses. Although there are some cases which have upheld local bidding preferences, including a Fourth circuit case *Setzer* 20 F.3d 1311 (1994) (P&I claim dismissed on standing), those cases do not involve P&I claims and usually involve Equal Protection claims which are easier to defeat by satisfying the rational basis standard. Furthermore, there are just as many cases where local bidding preferences are *not* upheld on constitutional grounds as there are cases upholding them. In sum, the bill would be vulnerable to a challenge under the Privileges and Immunities Clause.

If there are local business preference laws that currently remain intact, it is because of the complexity of obtaining standing to bring a case based upon a violation of the privileges and immunities clause. Many Privileges and Immunities challenges are dismissed for failure to obtain standing to sue. The Privileges and Immunities Clause "is inapplicable to corporations." This allows judges to dismiss P&I claims brought by corporate plaintiffs. Out-of-state residents who are not corporations consistently succeed against resident preferences.

The bill could also be challenged on Equal Protection grounds. Although this is an easier legal hurdle for the City, absent any data to support the program, there would be no defense. In other words, protectionism is not a legitimate goal and courts have struck down programs which attempt to base preferences on protectionist grounds absent data to support the idea that local businesses are suffering due to their nonresident counterparts. *See, e.g., Merrifield v. Lockyer,* 547 F.3d 978, 991 n.15 (9th Cir.2008) ("mere economic protectionism for the sake of economic protectionism is irrational with respect to determining if a classification survives rational basis review"); *Craigmiles v. Giles,* 312 F.3d 220, 229 (6th Cir.2002). In order to protect the law from challenge on these grounds, a disparity study should be done to support the claim that resident-businesses are suffering due to non-resident businesses and not some other factor. This would also aid in the defense of the bill should it be challenged.

Absent a legitimate goal supported by statistical evidence, the bill could also be challenged on Commerce Clause grounds. The Supreme Court has developed two tests for determining whether the Commerce Clause is violated. When a plaintiff establishes that a statute, either on its face or in its practical effect, clearly discriminates against interstate commerce, then the statute is subject to heightened scrutiny. A state must show that it has a legitimate purpose for this discrimination and that it cannot achieve its ends through less discriminatory means. *See Philadelphia v. New Jersey*, 437 U.S. 617, 624 (1986)).

If, on the other hand, the statute serves a legitimate state interest and burdens interstate commerce only incidentally, then challenges to it must establish that the burden on interstate commerce clearly outweighs the benefits sought by the government. *Id.*

In applying these rules to Council Bill 16-0619, the bill appears to be clearly discriminatory in regards to interstate commerce, if not on its face then in its practical effects. The bill is aimed at protecting local economic interests and its actual impact will accomplish these ends. "It is clear, however, that when a government acts to favor local economic interests over non-local interests such a regulation is often struck down as violating the Commerce Clause because economic protectionism is not a legitimate local purpose. *See, e.g., Fort Gratiot Sanitary Landfill, Inc. v. Michigan Dept. of Natural Resources,* 504 U.S. 353 (1992)(Impermissible to prohibit private landfill owners from taking in solid waste generated outside of the county); *Dean Milk Co. v. Madison,* 340 U.S. 349 (1951) (local political subdivision may not prohibit the sale of milk as pasteurized by requiring pasteurization within five miles of the city's square); *City of Philadelphia v. New Jersey,* 437 U.S. 617 (1978) (Impermissible to prohibit private landfill owners from taking solid waste generated outside of the state).

Furthermore, a local business preference would not withstand a Commerce Clause challenge if the City did not have a "proprietary interest" sufficient to make it a "market participant" under the law. In essence, when the government enters the market as a participant rather than as a regulator, its actions are exempt under the Commerce Clause. *South-Central Timber Development, Inc. v. Wunnicke*, 467 U.S. 82, 93 (U.S.,1984) ("Our cases make clear that if a State is acting as a market participant, rather than as a market regulator, the dormant Commerce Clause places no limitation on its activities."). The City must bear substantial economic risk on a project to fall within the scope of the exception. More to the point, Bill 16-0619 makes the City a regulator and not a market participant.

Local preferences also raise the possibility for retaliatory laws in adjacent jurisdictions.

The bill contains language that requires the law to be applied on a "contract-by-contract basis to the maximum practicable extent permissible under federal and state law and the City Charter." See City Council Bill 16-0619, §§ 28-97(B), 29-102(A)(1)(II), 28-113, 28-114, and 28-115. This language could be used to prevent implementation of those portions of the bill providing for local preferences that violate the Privileges and Immunities Clause and the Equal Protection Clause.

Small Business Preference

The Law Department further notes that the preference given to small businesses would need a rational basis to survive an Equal Protection claim. Although this would seem an easier, more defensible classification than a local one, data would need to support the theory that small businesses need extra support and would in fact be utilized more as a result of the program.

For example, the preferences given under the MWBE program is supported by disparity studies. There also exist unique circumstances and legal authority which further support programs designed to remedy past gender and racial discrimination which would not support a local or small business preference.

Charter Concerns

Generally speaking, the Charter requires that the Board of Estimates determine the fiscal policy of the City. The current MWBE law contains a statement that it does not abrogate that authority. This bill contains language that requires the law to be applied on a "contract-by-contract basis to the maximum practicable extent permissible under federal and state law and the City Charter." See City Council Bill 16-0619, §§ 28-97(B), 29-102(A)(1)(II), 28-113, 28-114, and 28-115. However, a mere statement that the program does not threaten that authority does not work to save the bill from any infirmity under federal and state law and the City Charter.

The SLBE program goes significantly further than current law and dramatically increases the discretion and authority of the MWBE office at the expense of the Board of Estimates and in violation of the charter. The most dramatic example of this is the "sheltered market program" where a city contract is taken completely out of the bidding process at the discretion of the MWBE chief and the contracting agency and offered for bidding exclusively among certified firms. The competitive business development demonstration project raises the same issue – here the chief may reserve certain contracts within an industry category for an RFP process open exclusively to joint ventures involving a certified SLBE. The program also involves "evaluation preferences" where the "City" can reserve up to 20% of total points available for an RFP evaluation for certified firms. The bill also allows for a 10% bidding preference for certified firms.

All of these "affirmative procurement initiatives" not only undermine the Board of Estimates Charter authority, but also interfere and violate the charter's lowest responsible bidder requirement.

Clearly, the bill, if enacted, would result in a law that is extremely vulnerable to challenge on any of the grounds enumerated above. The Law Department is committed to working with the Council to attempt to shape the kind of disparity study and supporting data that could make the legislation defensible.

The City could incur significant expense defending the law and there is a high probability of success by the plaintiff. Because of these significant legal issues, the Law Department cannot, without reservation, approve the bill for form and legal sufficiency as it cannot say with complete certainty that the bill would stand up to a constitutional challenge.

Sincerely,

Victor Tervala
Chief Solicitor

cc: George Nilson, City Solicitor
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