

HOUSE BILL REPORT

HB 1770

As Passed House:
March 5, 2011

Title: An act relating to enhancing small business participation in state purchasing.

Brief Description: Enhancing small business participation in state purchasing.

Sponsors: Representatives Hasegawa, Kenney, Orcutt, Frockt and Stanford.

Brief History:

Committee Activity:

State Government & Tribal Affairs: 2/17/11 [DP];
Ways & Means: 2/24/11, 2/25/11 [DP].

Floor Activity:

Passed House: 3/5/11, 74-23.

Brief Summary of Bill

- Creates the in-state Small Business Vendor Bidding Preference Program (Program).
- Authorizes state purchasing agencies to provide specified bidding preferences to in-state small businesses bidding on state procurement contracts.
- Authorizes sanctions against businesses who provide false information, or withhold information, in order to obtain the benefits of the Program.
- Prohibits the application of the bidding preference in instances when it conflicts with international trade agreements, would preclude federal funding, or conflicts with federal law.
- Requires the Department of General Administration to annually report to the Governor and the Legislature regarding implementation of the Program.

HOUSE COMMITTEE ON STATE GOVERNMENT & TRIBAL AFFAIRS

Majority Report: Do pass. Signed by 6 members: Representatives Hunt, Chair; Darneille, Dunshee, Hurst, McCoy and Miloscia.

This analysis was prepared by non-partisan legislative staff for the use of legislative members in their deliberations. This analysis is not a part of the legislation nor does it constitute a statement of legislative intent.

Minority Report: Do not pass. Signed by 4 members: Representatives Taylor, Ranking Minority Member; Overstreet, Assistant Ranking Minority Member; Alexander and Condotta.

Staff: Thamas Osborn (786-7129).

HOUSE COMMITTEE ON WAYS & MEANS

Majority Report: Do pass. Signed by 18 members: Representatives Hunter, Chair; Darneille, Vice Chair; Hasegawa, Vice Chair; Dammeier, Assistant Ranking Minority Member; Orcutt, Assistant Ranking Minority Member; Carlyle, Cody, Dickerson, Haigh, Hudgins, Hunt, Kagi, Kenney, Ormsby, Pettigrew, Seaquist, Springer and Sullivan.

Minority Report: Do not pass. Signed by 9 members: Representatives Alexander, Ranking Minority Member; Bailey, Assistant Ranking Minority Member; Chandler, Haler, Hinkle, Parker, Ross, Schmick and Wilcox.

Staff: Andy Toulon (786-7178).

Background:

State Procurement.

The Department of General Administration (GA) establishes overall state policy for state purchasing, and contracts with individuals and companies outside of state government to provide goods and services to the state. Under delegated authority, other state agencies and the institutions of higher education also contract for goods and services. The state's purchasing authority is generally organized into categories based on the type of service. Among these categories are:

- *Purchased goods and services.* These goods and services are those provided by a vendor to accomplish routine, continuing, and necessary functions.
- *Personal services.* This term refers to professional or technical expertise provided by a consultant to accomplish a specific study or project.
- *Information services.* These services include data processing, telecommunications, office automation, and computerized information systems.
- *Printing services.* This term refers to the production of the state's printed materials.

Except in specific circumstances, Washington law does not provide preferences to bidders who are in-state. The statutory exceptions include:

- *Ferries.* In Washington, the Department of Transportation's bid documents for jumbo ferries must include a requirement that the vessels be constructed within Washington, with exceptions for certain equipment and systems.
- *Washington-grown food for schools.* School districts are authorized to implement policies to maximize the purchases of Washington-grown food. Such policies may include permitting a percentage price preference for Washington-grown food.
- *In-state printing.* Printing for state agencies must be done within Washington, unless the work cannot be executed in state or the lowest in-state bid exceeds the customary charges in the private sector.

In addition to these in-state preferences, the GA is required to identify other states that provide in-state preferences to their own bidders. If a bidder from one of those states submits a bid for a state contract in Washington, the GA may add a percentage increase to that bidder's proposal. This increase is used only to evaluate the bid and is not paid to any supplier whose bid is accepted.

Legal Challenges to In-State Preference Laws.

State procurement laws that give preference to domestic goods or prohibit purchasing foreign goods have been challenged on one or more grounds. These include arguments that such laws are: (1) invalid exercises of state power under the federal Commerce Clause; (2) preempted by federal statute or in violation of international agreements on government procurement; or (3) in violation of Equal Protection/Privileges and Immunities clauses in the United States Constitution (Constitution).

Commerce Clause.

The Constitution reserves to Congress the power to regulate commerce. The United States Supreme Court (Court) has struck down state laws that regulate commerce in a manner that promotes businesses in the state at the expense of businesses in other states or foreign countries. However, the Court has also recognized that, when a state acts as a market participant, rather than a market regulator, it is not subject to the restraints of the Commerce Clause.

Federal Preemption.

The Court has found that state laws in conflict with valid federal laws, including statutes, treaties, or foreign policies and diplomatic objectives of the President and the Congress are preempted. For example, states may receive federal funding with conditions that include prohibitions on local bidding preferences.

Trade agreements may also raise a barrier to local preferences. The Agreement on Government Procurement (GPA) is one of many World Trade Organization agreements to which the United States is a party, and is one of several agreements that apply to Washington and certain other states. In Washington, state agencies subject to the GPA include certain executive branch agencies such as the GA and the Department of Transportation, as well as the state institutions of higher education. For the calendar years of 2010-2011, state contracts subject to the GPA currently include contracts of \$554,000 or more for goods and services, and contracts of \$7,804,000 or more for construction services. Article III of the GPA, dealing with national treatment and non-discrimination, provides that:

- Parties to the agreement must treat the products, services, and suppliers of other parties no less favorably than domestic products, services, and suppliers.
- Parties must not treat locally-established suppliers less favorably than other suppliers on the basis of foreign affiliation or ownership.
- Parties must not discriminate against locally-established suppliers on the basis of the country of production of the good or service being supplied.

Equal Protection/Privileges and Immunities.

In general, courts may require states to justify a local preference law as rationally related to a legitimate state interest. At least one court has found that the state has a legitimate interest in ensuring that tax monies are recycled through the local economy through the purchase of locally produced products or purchases from local vendors.

Other States' In-State Preference Laws.

Several other states, including Alaska, Hawaii, Louisiana, Montana, New Mexico, New York, South Carolina, and Wyoming, have government procurement bidding preferences for in-state bidders or products. Arizona and California have a bidding preference for in-state small businesses.

Summary of Bill:

Subject to specified terms and conditions, all state purchasing agencies must apply a bidding preference in the purchase of goods and services from in-state small businesses. The application of the bidding preference requires the contracting agency to provide:

- a 5 percent bidding preference to the bids of in-state small businesses;
- a bidding preference of up to 5 percent to the bids of in-state businesses which are not small businesses, but which provide for small business subcontractor participation in the contract; and
- assistance to small businesses by providing vendor information about bid solicitation requirements either prior to the bid due date, or after the contract award, in order to assist the vendor.

A purchasing agency that, in good faith, applies the bidding preference is exempt from any legal action for damages arising out of the contract award.

If state bidding preference provisions conflict with international trade agreements, federal agreements regarding the allocation of funding to the state, or with federal law, then the purchasing agency cannot apply the conflicting bid preference.

A business that receives the bidding preference is subject to a variety of sanctions if it provides or withholds information that is material to the award of the contract. These sanctions may include:

- payment of an assessment related to the value of the contract;
- a civil penalty; and
- ineligibility for future contracts for a period of six months to three years.

"In-state business" means a business that has its principal office located in Washington and its officers domiciled in Washington.

"Small business" means a business that is owned and operated independently from all other businesses and:

- has either 50 or fewer employees; or

- has a gross revenue of less than \$7 million averaged over the previous three years;
or
- is certified by the Office of Minority and Women's Business Enterprises.

Beginning on December 1, 2011, and each December 1 thereafter, the GA must provide a comprehensive report to the Governor and the Legislature regarding its implementation of the Small Business Vendor Bidding Preference Program (Program).

The Small Business Bidding Preference Account (Account) is created in the office of the State Treasurer. The Account is the repository of the receipts of any civil penalties collected under the act.

The Director of the GA must establish overall state policy regarding the development of procurement procedures necessary to implement the Program, including model bidding application documents.

Appropriation: None.

Fiscal Note: Preliminary fiscal note available.

Effective Date: The bill takes effect 90 days after adjournment of the session in which the bill is passed.

Staff Summary of Public Testimony (State Government & Tribal Affairs):

(In support) This is a good bill that would assist local, small businesses in obtaining state contracts. This bill passed the House of Representatives last year, but did not get out of the Senate.

(With concerns) Providing in-state small businesses with preferential treatment in the bidding process presents problems with respect to implementation and unintended negative effects. It will burden state agencies with considerable costs, including the costs of revamping the bidding system and creating an administrative apparatus. The onerous penalty provisions of the bill may have the effect of impairing the ability of state agencies to recruit small businesses for contracts. Such preferential treatment will create problems for Washington vendors when they bid on contracts in other states that impose reciprocal preferential treatment. Also, the GA does not have the accounting systems necessary to meet the bill's reporting requirements.

(Opposed) None.

Staff Summary of Public Testimony (Ways & Means):

(In support) Other states currently apply bidding preferences but the Department of General Administration has consistently said they do not have the resources to apply retaliation to these states, so in effect our small businesses are suffering. California is the main one applying a 5 percent preference. This bill is important to the small business community. This bill was passed last year on an 84-10 vote and was vetoed by the Governor as a result of

the changes made in the Senate. The fiscal note has changed considerably from last year and where that comes from I do not know. This will be self-policing, relying on small businesses looking for opportunities to catch people who are cheating.

(Opposed) None.

Persons Testifying (State Government & Tribal Affairs): (In support) Representative Hasegawa, prime sponsor.

(With concerns) Servando Patlan, Washington State Department of General Administration.

Persons Testifying (Ways & Means): Representative Hasegawa, prime sponsor.

Persons Signed In To Testify But Not Testifying (State Government & Tribal Affairs): None.

Persons Signed In To Testify But Not Testifying (Ways & Means): None.