F I S C A L I M P A C T R E P O R T

SPONSOR Tripp **ORIGINAL DATE** 02/27/11 **LAST UPDATED** 03/11/11 **HB** 598/a HLC

SHORT TITLE Procurement Preference for Veterans **SB**

ANALYST Graeser

ESTIMATED ADDITIONAL OPERATING BUDGET IMPACT (dollars in thousands)

	FY11	FY12	FY13	3 Year Total Cost	Recurring or Non-Rec	Fund Affected
		$700.0	$1,400.0	$2,100.0	Recurring	General Fund
		$800.0	$1,600.0	$2,400.0	Recurring	OSF
		$2,000.0	$4,000.0	$6,000.0	Recurring	STBs and GOBs
		$500.0	$1,000.0	$1,500.0	Recurring	Local funds
		$2,000.0	$4,000.0	$6,000.0	Recurring	Local CIP and School Construction bonds

(Parenthesis ( ) Indicate Expenditure Decreases)

SOURCES OF INFORMATION
LFC Files

Responses Received From
Veteran's Services Department (VSD)

SUMMARY

Synopsis of HLC amendment

The House Labor and Human Resources Committee Amendment to House Bill 598 accomplishes three modifications to the original bill:

1) reinstates the 5% recycled goods preference as in the current procurement code;
2) removes the requirement that a veteran business employ at least five resident New Mexicans;
3) redefines a veteran business to mean a company solely owned by honorably discharged veterans.

These amendments taken together do not materially alter the fiscal impact of the bill as previously reported:

1) reinstating the recycled goods preference increases the cost to state and local

government entities by as much as 5% of the contracts where the quality of recycled goods is equal to that of virgin content goods.

2) Removing the requirement that a veteran business employ at least five resident New Mexicans means that more businesses can qualify for the resident veterans procurement preference. This increased competition may reduce agency costs.
3) The redefinition of a “veteran business” to mean one solely owned by a New Mexico resident veteran somewhat counters the effect of item #2 above. However, the resident business may subcontract the services offered to an out-of-state provider. The affiliate relationship test (page 2, subsection c) would not be invoked.

Overall, this bill will increase the number of veteran “brokers” – resident veteran businesses that partner or sub-contract with an out-of-state provider to jointly bid on contract offerings or procurements. The out-of-state providers do the work and the resident veteran broker qualifies the bid for a 10% resident veteran preference. Currently, many brokering arrangements exist, but the fiscal impact is limited to non-federally funded contract procurements under $5 million in value. This bill as amended retains those restrictions, but doubles the value of the resident preference for veteran owned businesses.

Synopsis of Original Bill

House Bill 598 proposes changes to the State’s Procurement Code to establish a resident veteran’s business preference of 5% in addition to the current 5% resident business preference. The bill also establishes a 5% resident veteran’s contractor preference. The New York state preference sections are amended or repealed to eliminate this archaic equivalence. The bill also eliminates the 5% recycled goods preference and the 5% resident manufacturer’s preference.

The bill retains the federal fund exclusion and $5,000,000 contract limit for preference. Further, the resident veteran’s business preference is restricted in Section 13-1-22 NMSA 1978 to state level procurement of materials and services only. However, Section 13-4-22 NMSA 1978 provides that the 10% resident veteran contractor preference applies to both state and local level contracts as long as the bidder is certified by the State Purchasing Agent.

The duty of certifying a resident veteran business or a resident veteran contractor is assigned to the State Purchasing Agent.

The effective date of the provisions of the bill is July 1, 2011.

FISCAL IMPLICATIONS

Last year, this type of bill would have carried an “indeterminate” operating budget, revenue and appropriations fiscal impacts. This year, LFC is making a considerable effort to quantify revenue, appropriation and operating budget impacts. This quantification may require adopting new, somewhat untested methods. Quantifying the fiscal impact of this bill is a clear example of this approach. Since this bill amends the state procurement code as does SB 19, SB 539 and HB 309, a similar methodology for the op bud impact will be adopted.

Total procurement (excepting procurement funded with federal money) by state agencies exceeds $1.7 billion – roughly $1.1 billion in personal services, $500 million in GO and STB capital outlay (average) and $200 million in supplies, materials, furniture and fixtures. Over $300 million in federal highway funding and over $1 billion in federal Medicaid funding would be exempt from the resident bid preference provisions. A careful detailing of the 2010 General Appropriations Act and the Feed Bill shows the following:

			Excluding sole source contracts and contracts over $5 million	
	General Fund	OSF/IFT	General Fund	OSF/IFT
Contracts Line	$251,968.2	$850,147.3	$78,228.4	$85,882.7

Approximately $120 million general fund is the competitive base of this bill -- $78 million in personal services contracts and $40 million in procurement of supplies, materials, furniture and fixtures. This estimate excludes roughly $4 million in sole source contracts (general fund and OSF/IAT). Industry sources estimate that approximately 40% of state contracts and procurement is awarded to true resident contractors and businesses. Most of the remaining 60% is currently awarded to out-of-state businesses and contractors who can easily qualify for technical residency pursuant to current statute by using a broker.

Potentially, the cost of this bill to the general fund could be as much as $7.2 million, assuming that the bid cost of all contracts and procurement would increase by the full 10% of the resident veteran's business and contractor preferences. ($125 x 60% x 10%). However, the bill eliminates the 5% resident manufacturer's preference, ~~the 5% recycled goods preference~~ and the New York state equivalence. Pursuant to other provisions of the bill, it will be somewhat more difficult than at present for an out-of-state business to qualify and certify as a resident business or contractor. "Brokering" will be about as easy as under current law, but will only benefit a fraction of the current 15,000+ veteran owned businesses in the state, a majority of which only employ one or two persons, including the owner. [By HLC amendment, all of the 15,000+ veteran owned businesses can qualify for the resident veteran owned business preference, making "brokering" significantly easier and more pervasive than at present.] ~~A resident veteran's business or contractor must employ five state residents (no requirement for full-time equivalent employees).~~ This may mean that a number of veteran's businesses will transition to become the resident partner/broker of a multi-state partnership. The bill will not greatly change the relative ratio of contracts that will go to genuine New Mexico residents, but will double the returns to brokering by doubling the resident preference to 10% from the current 5%. This additional cost will persist through time. There will be little increased competition from genuine resident businesses to move prices back down to traditional levels. Veteran businesses and contractors acting as brokers will continue to receive windfall profits, but no more New Mexican workers will obtain permanent jobs.

Limiting this full amount of additional agency cost is a budget constraint. In general, if bidders submit proposals in excess of the amount appropriated for the project or procurement, then the winning bidder can negotiate quantities or other issues in order to bring the final bid under the amount appropriated. Although this feature will have no effect on whether the contract is awarded to a true in-state firm or to a resident veteran broker with an out-of-state partner, agency bid price increases will be moderated. We estimate that the budget-constrained price increase will be 20% of the full 10% in-state preference (less than HB 539 because this bill eliminates two ~~three~~ other preferences). This puts the initial increase in general fund costs at $1.4 million for the full year and $700.0 million for the initial half year. Other state funds would experience cost increases of $800.0 first year and $1.6 million subsequently. Local government operating costs would also increase commensurately. Capital outlay costs would also increase significantly, since construction contracts less than $5 million would become eligible for both state and local resident contract preference.

Somewhat offsetting the increase in agency costs, there would be an increase in revenues, particularly Gross Receipts tax, and, to a lesser extent, Corporate Income Tax, Personal Income Tax and Motor Vehicle Excise Tax. The general fund increase would be on the order of 5% of increased costs and other state funds and local funds increase would be on the order of 4%. On a $12.2 million base ($1.4 million general fund, $1.6 million OSF and $1.2 million local governments and $8 million capital construction), this would be $610.0 general fund and $500.0 OSF and local funds. There is unlikely to be a significant employment effect, since the new veterans business and contract brokers will simply displace the current crop of resident brokers.

GSD/SPD indicates additional personnel and systems will be required to fill the needs and intent of this bill. Veteran information is not captured today and a process will be required to determine vendor applicability to the preference requirements, development of the application and review/acceptance requirements, issuance of certification, and tracking capability. GSD/SPD did not quantify this impact.

OTHER SIGNIFICANT ISSUES

Deleting the New York State equivalence provisions in the procurement code – placed there in 1997 to allow NovaBus, a Roswell bus manufacturer to sell buses manufactured in New Mexico to New York City – may be timely, but may have unintended consequences.

Wikipedia has an interesting article on the various bus companies with a connection to Roswell:

Transportation Manufacturing Corporation (TMC) was a bus manufacturer based in Roswell, New Mexico. The company was formed in 1974 by Greyhound Bus Lines to manufacture Motor Coach Industries vehicles. In 1987, General Motors decided to close its bus division and sold the manufacturing rights of the Rapid Transit Series (RTS) bus and the **Classic** to Greyhound subsidiary, Motor Coach Industries. RTS production would move to the TMC plant in Roswell, New Mexico, while the Classic bus production would remain in the former GM bus plant in Saint-Eustache, Quebec. Motor Coach Industries sold its Classic and RTS bus license to Nova Bus in 1993. In 1990, TMC began development of an enclosed automobile-transport semitrailer. This trailer used small-diameter wheels to maximize interior space, and robotic arms to lift the automobiles and position them closely together in the trailer body. The trailer lacked the traditional ramps and racks: automobiles were fitted with pins strapped to the tires, which slotted into holders inside the trailer. These features maximized the capacity of the trailer. In 1994, MCI sold the TMC plant to NovaBus, which closed it in 2003. The Roswell, New Mexico plant was reopened later under the name Millennium Transit Services LLC.
Deleting the New York State equivalence provisions might result in a disadvantage for some New Mexico businesses. New York State's procurement code prohibits non-resident bidders if the base state of the non-resident bidders discriminate against New York State businesses bidding in the other state.

ADMINISTRATIVE IMPLICATIONS

The ability of the State Purchasing Agent to receive validation from Veteran Affairs in a timely fashion is uncertain and will (1) increase the workload/tracking by State Purchasing and (2) delay certification of veteran's businesses and veteran's contractors. Additional steps and validations will increase the responsibilities of the State Purchasing personnel by increasing the tracking required for the added steps. Today tracking is accommodated by Excel spreadsheets and should be migrated to a database allowing more users to safely add/change data. Use of Excel places the data at risk of corruption and deletion. Delays may cause contractors to not receive applicable preference pending determination.

CONFLICT, DUPLICATION, COMPANIONSHIP, RELATIONSHIP

A number of bills modify provisions of the procurement code. While some of these could be construed together, most modify 13-1-21 NMSA 1978 and would be in conflict:

- HB 128 revises the rules for emergency and sole source contracts;
- HB 309 provides a 15% veteran preference, doubles the resident preference to 10%, cancels all leases and contracts as of 7/1/11;
- HB 539 provides a 5% additional resident small business preference, a 5% additional disadvantaged small business preference and retains the 5% recycled content preference;
- SB 19 substantially revises the rules to qualify as a resident business or resident contractor. The purpose of SB 19 is to restrict "brokering" and implement a true resident preference. However, SB 19 eliminates the $5 million cap on contracts;
- SB 63 provides a New Mexico-grown food content goal;
- SB 149 provides an additional 3% veteran's preference, retains the 5% resident preference and retains the New York equivalence;

OTHER SUBSTANTIVE ISSUES

This bill does not reform "brokering," whereby a small brokering firm, which qualifies for a resident preference, affiliates with a large out-of-state firm that does the actual work required in the contract. This affiliation could be through a sub-contract. All the in-state broker must do is maintain a principal headquarters and hire at least five New Mexico residents. The large out-of-state firm can establish a solely or partially owned subsidiary in a small "headquarters" office and qualify for the 5% resident preference or 10% resident veteran's preference on all contracts less than $5 million in value.

According to a recent SBA business survey, New Mexico has 15,212 veteran owned businesses. Many of these companies have only 1 or 2 employees. The additional preference would possibly allow these businesses to expand and create more jobs at the local level.

ALTERNATIVES/POSSIBLE AMENDMENTS

It would seem reasonable to prohibit brokering and focus on developing a true resident preference.

WHAT WILL BE THE CONSEQUENCES OF NOT ENACTING THIS BILL

Not to put too much emphasis on the downside, but this bill might simply replace one set of brokers with another set of brokers, with the new set of brokers allowed a 10% procurement preference, rather than the current 5% preference. No additional resident employment would result from this exchange. Not enacting the bill would ensure that this unintended consequence would not happen.

POSSIBLE QUESTIONS

Can GSD/SPD show how this veteran preference is restricted to state level contracts and procurement? 13-1-22 NMSA 1978 (and Section 2 of the bill) provides that no resident business or resident veteran business may be granted a preference for state-level procurement of materials or services unless the resident business is certified by the State Purchasing Agent. However, Section 13-4-2 NMSA 1978 does not mention state-level contracts and simply defines a resident veteran contractor as a contractor owned more than 51% by an honorably discharged veteran. A similar provision for contractors applies the resident contractor and resident veteran's contractor preferences to state and local level contracts. A "contractor" is defined in the Procurement Code as any entity that has a contract with a state or local agency.

LG/svb:mew