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

**ORIGINAL DATE** 02/25/11
**SPONSOR** Trujillo **LAST UPDATED** ______ **HB** 539

**SHORT TITLE** Protect New Mexico Small Businesses **SB** ______

**ANALYST** Graeser

## REVENUE (dollars in thousands)

| Estimated Revenue | | | Recurring or Non-Rec | Fund Affected |
|---|---|---|---|---|
| FY11 | FY12 | FY13 | | |
| | NFI | NFI | NA | NA |

(Parenthesis ( ) Indicate Revenue Decreases)

Duplicates, Relates to, Conflicts with, Companion to SB 19

## ESTIMATED ADDITIONAL OPERATING BUDGET IMPACT (dollars in thousands)

| | FY11 | FY12 | FY13 | FY14 | 4 Year Total Cost | Recurring or Non-Rec | Fund Affected |
|---|---|---|---|---|---|---|---|
| **Total** | | ≈$1,500.0* | ≈$2,900.0* | ≈$2,900.0* | ≈$7,300.0* | Recurring | State General Fund |
| | | ≈$2,800.0* | ≈$5,700.0* | ≈$5,700.0* | ≈$14,200.0* | Recurring | All other state and local funds (Except State Road Fund and Medicaid) |

(Parenthesis ( ) Indicate Expenditure Decreases)

See Fiscal Implications for discussion of the methodology leading to these estimates.

**SOURCES OF INFORMATION**
LFC Files

Responses Received From

Reponses Received from the following concerning related bills
Office of State Auditor (OSA)
New Mexico Environment Department (NMED)
General Services Department (GSD)
Attorney General's Office (AGO)
New Mexico Corrections Department (NMCD)

## SUMMARY

Synopsis of Bill

House Bill 539 proposes changes to the State's Procurement Code to enhance the resident preference provisions. The New York state preference sections are amended or repealed to eliminate this archaic equivalence.

The bill substantially revises the details of the resident procurement preference:

- Retains the 5% bid preference for resident businesses and resident manufacturers;
- Adds an additional 5% bid preference for resident small business procurement;
- Adds a third additional 5% bid preference for disadvantaged small business;
- Retains the 5% preference for recycled goods;
- Slightly redefines the definition of resident business to require five full-time equivalent employees who are residents of the state.
- Excludes construction and construction materials from the preferences;
- Retains the $5 million per contract limit and the exclusion for procurement using federal funds from the preference procedures.

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, 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.
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 in-state disadvantaged small business preference. ($125 x 60% x 10%). 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 somewhat more difficult since the resident business entity must have five full-time equivalent employees. However, the five full-time equivalent employees requirement will be waived for a disadvantaged small business. This may mean that a number of disadvantaged small business entities will form and will become the resident partner/broker of a multi-state partnership. Since the bill may enhance brokering, the cost of the bill to state entities will tend toward the maximum cost increase. 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. Disadvantaged small businesses 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 disadvantaged small business broker with an out-of-state partner, agency bid prices will be moderated. We estimate that the budget-constrained price increase will be 40% of the full 10% in-state preference. This puts the initial increase in general fund costs at $2.9 million for the full year and $1.5 million for the initial half year. Other state funds would experience cost increases of $1.6 first year and $3.2 million subsequently. Local government operating costs would also increase commensurately. Capital outlay costs would not increase significantly, since construction and construction materials are excluded from the resident procurement 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 $8.6 million base ($2.9 million general fund, $3.2 million OSF and $2.5 million local governments), this would be $430.0 general fund and $340.0 OSF and local funds. There is unlikely to be a significant employment effect, since the new disadvantaged small business brokers will simply displace the current crop of resident brokers.

**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 State Purchasing Agent is assigned the duty and responsibility to certify resident businesses, resident manufacturers, resident small businesses and resident disadvantages small businesses.

**CONFLICT, DUPLICATION, COMPANIONSHIP, RELATIONSHIP**

SB 19 amends the procurement code to change resident preference qualifications. The purpose of SB 19 is to restrict "brokering" and implement a true resident preference.

HB 309 eliminates any possibility of "pay-to-play" in current contracts and leases and to extend that promise to future contracts and leases. In addition, it establishes a 15% "resident veteran ontractor" preference, doubles the resident business procurement preference to 10%, eliminates the 5% preference for resident manufacturer and eliminates the 5% preference for recycled goods.

HB 128 proposes new procedures for making sole source procurements. Unlike HB 309, however, HB 128 does not require the Governor's approval of sole source procurements.

HB 598 adds a resident veteran's preference and mimics some of the other features of HB 309.

**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. 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 or partially owned subsidiary in a small "headquarters" office and qualify for the 5% resident preference on all contracts less than $5 million in value.

## ALTERNATIVES/POSSIBLE AMENDMENTS

It would seem reasonable to prohibit brokering and focus of 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 15% 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.

LG/bym