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FISCAL IMPACT REPORT

ORIGINAL DATE 02/09/11
 LAST UPDATED 02/18/11 **HB** _____

SPONSOR SCORC

SHORT TITLE In-State Business Procurement Advantage **SB** CS/19/aSCORC/aSJC

ANALYST Graeser

REVENUE (dollars in thousands)

Appropriation		Recurring or Non-Rec	Fund Affected
FY11	FY12		
\$0.0	\$400.0*	Recurring	General Fund (TRD application fees)
\$0.0	\$0.0	Recurring	General Fund (Civil fines)
\$0.0	\$0.0	Recurring	OSF and local funds

(Parenthesis () Indicate Expenditure Decreases)

* See narrative

May conflict with SB31, Contractor Registration

May increase agency costs relating to appropriations in the General Appropriation Act

ESTIMATED ADDITIONAL OPERATING BUDGET IMPACT (dollars in thousands)

	FY11	FY12	FY13	FY14	4 Year Total Cost	Recurring or Non-Rec	Fund Affected
Total		≈\$1,200.0*	≈\$1,600.0*	≈\$800.0*	≈\$3,600.0*	Nonrecurring	State General Fund
		≈\$2,400.0*	≈\$3,200.0*	≈\$1,600.0*	≈\$7,200.0*	Nonrecurring	All other state and local funds (Except State Road Fund and Medicaid)
		\$400.0	\$200.0	\$200.0	\$0.0	Recurring	Taxation and Revenue Dept. (General Fund) – certification function
		\$0.0	\$0.0	\$0.0	\$0.0	Recurring	State Purchasing Agent – investigation/hearing/civil penalty admin.

(Parenthesis () Indicate Expenditure Decreases)

*See Fiscal Impact narrative for discussion of this impact

SOURCES OF INFORMATION

LFC Files

Responses Received From

New Mexico Economic Development Department (EDD)

Department of Transportation (DOT)

New Mexico Finance Authority (NMFA)

Attorney General (AGO)

Department of Workforce Solutions (DWS)

New Mexico Environment Department (NMED)

SUMMARY

Synopsis of SJC Amendment

The SJC amendment to CS/SB 19 as amended reassigns various administrative duties with respect to the resident procurement preference. TRD retains the duty to approve the certificate of resident preference based, in part, on payment of TRD-administered taxes. The application prepared and attested by a CPA will contain the information regarding ownership or lease of real property.

Disbarment or suspension from future bidding based on providing false information in order to obtain a certificate or failing to perform the percentage of the contract specified in the bid or proposal would be assigned to the State Purchasing Agent. Implicitly, these grounds for disbarment would also be grounds for a bid protest – also assigned to the State Purchasing Agent in the State Procurement Code (13-1-172 NMSA 1978).

The amendment also clearly reassigns to the State Purchasing Agent the administration of the up-to-\$50,000 civil penalty per violation imposed for violation of the grounds listed above. The State Auditor is authorized to audit or review the issuance or validity of certificates and can work with the State Purchasing Agent to impose and collect the civil penalty in cases of egregious violation of the preference rules.

Because of the existence of the penalties (suspension or disbarment from future bidding and a civil penalty of up to \$50,000 per violation), bidders will be very careful to understate the percentage of resident participation in a joint project. It is unlikely that there will be any significant increase of workload for the State Purchasing Agent/Office attributable to protests over preference certificates. There might be one, or perhaps, two protests a year.

Synopsis of SCORC Amendment

The SCORC amendment to CS/SB 19 shortens the qualification period for a resident business certificate from five years of paying taxes in the state to three years. The qualification period for a resident contractor's license remains at five years of paying taxes in the state.

Synopsis of Original Bill

SCORC substitute for Senate Bill 19 modifies the state's procurement code's preference for resident businesses and resident contractors by making it somewhat more difficult to qualify as a resident business or resident contractor. The new multi-step process follows: (a) a prospective resident contractor or business obtains an affidavit from a certified public accountant that the contractor or business is licensed to conduct business in the state, has paid property taxes or rent on real property located in the state, and has paid at least one other tax administered by TRD in each of the five years immediately preceding the submission of the affidavit (or equivalent quali-

fications in the case of an entrepreneur, a legacy business or a relocated business); (b) based on the affidavit from a CPA, the bill requires the Taxation and Revenue Department to issue a contractor or business certificate for the prospective contractor to include with bid documents; and (c) based on the certification as a resident contractor or resident business, the state agency or local government entity is then required to implement a 5% price preference for the resident contractor or business. If a resident business or contractor is in partnership or other joint arrangement with a non-resident business or contractor, then the 5% preference is ratioed by the anticipated participation of the dollar value of the goods or services to be provided by resident business and non-resident business. This feature will restrict “brokering,” where the non-resident business or contractor provides the vast majority of the goods and services, but the relationship with the resident broker invokes the full 5% preference in current law.

The Taxation and Revenue Department has 30 days in which to act on the application for certification. The certificate is valid for three years. Aggrieved or denied applicants may schedule a hearing with TRD and present evidence. If TRD finds that a business or contractor applicant has presented false information, or if TRD determines that an applicant has misused a certificate in various ways, then the business or contractor’s certificate may be revoked for a period of five years and TRD may assess an administrative penalty of \$50,000. TRD may cover its costs of administration of the certificate system with a fee, but the fee is not appropriated to the Department.

The bill defines a “legacy contractor,” an “entrepreneur” and a “relocated business” and defines the specific requirements for certification – approximately equivalent to the main requirements. A “relocated business” for example, would qualify for preference if 80% of the employees of the business the year before the submission of the affidavit were residents of New Mexico and that the business had leased property in the state for ten years or purchased property in the state greater than \$100,000 in value.

The bill strikes language which previously allowed New York businesses to be considered “resident businesses” and modifies the procedures for evaluating a proposal or bid. The bill, however, retains the 5% preference for the purchase of recycled goods, although provides that only one 5% preference applies.

The bill retains the provision of current law and declares that the preference does not apply if the procurement or project is funded at least partially with federal funds.

The effective date of the bill is July 1, 2011, however section 5 provides that a GSD certification as a resident business or resident manufacturer that is in effect on June 30, 2011 would be valid until January 1, 2012.

FISCAL IMPLICATIONS

Last year, this same bill carried an “indeterminate” operating budget fiscal impact. 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.

Total procurement, excepting procurement funded with federal money, by state agencies exceeds \$2 billion -- approximately \$400 million from the general fund for contracts less than \$5 million in value. 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. Note that over \$250 million in federal highway funding and over \$1 billion in Medicaid funding would be exempt from the resident bid preference provisions. LFC is currently attempting to refine this somewhat rough estimate of general fund contracts of less than \$5 million in value.

Potentially, the cost of this bill to the state could be as much as \$12 million, assuming that the bid cost of all contracts and procurement would increase by the full 5% of the in-state preference. ($\$400 \times 60\% \times 5\%$). Under the terms of the bill, it will be relatively easy for an out-of-state business to qualify and certify as a resident business or contractor, but the resulting firm must employ residents, at least 80% of the total crew. The biggest change from this bill will be in restricting brokering and ensuring that New Mexico workers benefit from the resident preference. Although there may be a very short term increase in costs to state and local agencies, within, at most, three years, increased competition will move prices back down to traditional levels, brokers will not receive windfall profits and more New Mexican workers will have permanent jobs. 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. Because of this strong limit, the major effect of this bill will be to direct contracts to true in state businesses or contractors. In the short run, we estimate that the price increase will be 1/5th of the full 5% in-state preference. This puts the initial increase in general fund costs at \$2.4 million for the full year and \$1.2 million for the initial half year. Second full year costs to general fund agencies would be about \$1.6 million and third full year costs less than \$1 million. Local government operating costs and capital outlay costs would also increase commensurately in the short term.

Initially, and for several years in the future, true resident contractors and businesses would have an advantage, and this advantage would slightly increase costs to the agencies. Eventually, economics would prevail and more efficient producers would qualify as resident businesses and the state and local governments would then receive competitive prices. This is shown in the table as a declining cost to the agencies.

Offsetting this temporary 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 \$2.5 million base, this would be \$120.0 general fund and \$100.0 OSF and local funds. There might also be slight decrease in unemployment costs as more New Mexicans were hired for public works projects.

For the purpose of this estimate, it is assumed that 8,000 contractors would apply to TRD initially for certification and that TRD would set the application fee at \$5. After the initial rush, the steady state workload would average 4,000 certifications a year. These fees are not appropriated to TRD, so the fee collections would be transferred to the general fund as miscellaneous revenue.

The following comment has largely been addressed by the SJC amendment.

~~The Taxation and Revenue Department's office would probably be able to certify resident businesses and contractors with existing staff and data. However, conducting investigations pursuant to complaints from aggrieved businesses and contractors, conducting hearings and imposing civil~~

~~finer exceeds TRD's expertise. Either the State Auditor or TRD would probably have to establish a dedicated bureau or section to approve business and contractor certificates, investigate complaints, conduct hearings and impose and collect civil fines. The \$250.0 cost shown in the table represents a minimum estimate of additional costs within TRD or the State Auditor's Office, whether the investigation, civil penalty and hearing function were assigned to TRD or the State Auditor.~~

OTHER SIGNIFICANT ISSUES

The primary purpose of this bill is to prevent abuse of the current resident preference provisions. Apparently, one of the abuses noted in the current procedure is "brokering." A true resident business or contractor – with a principal place of business in the state, five resident employees and a history of paying tax in the state – makes an arrangement with an out-of-state contractor to take advantage of the "affiliate" provision of current law. The broker may not actually participate in the project awarded, but does qualify the joint proposal for resident treatment.

The substance of the DOT review of this bill follows:

SB 19 would also clarify that if a joint bid is submitted by both resident and nonresident businesses, the preference is reduced in proportion to the percentage of the contract that will be performed by the nonresident business.

SB 19 further recognizes that, because the federal government will not permit in-state preference on public-sector projects that are at least partially funded by the federal government, the preference shall not apply when the expenditure of federal funds is involved. This provision is of particular relevance to DOT contracts, since the bulk of road construction funding comes from the Federal Government. SB 19 also clarifies that disputes arising under the statute should be handled by agencies as bidding disputes under the Procurement Code.

SB 19 would also eliminate the preference for resident manufacturers, New York State businesses and recycled content goods. It should be noted that because New York State's Procurement Code reciprocally bans doing business from any state with an "discriminatory" in-state preference, NMSA 1978, § 13-1-21.2, continues to prohibit differential treatment of any kind between New York state business enterprises and New Mexico businesses in New Mexico procurement.

EDD provides two examples of New Mexico companies that might benefit from a genuine resident preference:

- 1) P&M Signs is a sign manufacturing company located in Mountainair. This business would be able to compete and potentially secure contracts through the Department of Transportation and the State Forestry Department;
- 2) Simtable is a Santa Fe business that has created software for 3-D simulations. The company will also attempt to secure contracts through the State Forestry Department.

ADMINISTRATIVE IMPLICATIONS

The administrative difficulties discussed here have largely been solved by the SJC amendment.

~~This bill will somewhat increase the complexity of the procurement and contracting processes and may increase costs for both the contractors and agencies. Some agency, either the Taxation and Revenue Department or the State Auditor, would probably have to establish a dedicated office or bureau to administer certification and verification, investigate complaints, conduct hearings and impose and collect civil fines. All of this is new territory for TRD.~~

CONFLICT, DUPLICATION, COMPANIONSHIP, RELATIONSHIP

SB19 may conflict with SB31, although the bills may be construed together. SB19 affects the resident preference under the procurement code, while SB31 is an ethics bill that requires contractor registration and prohibits political contributions from some contractors and prospective contractors.

OTHER SIGNIFICANT ISSUES

The following issues have been addressed in the SJC amendment.

~~Section 2F will be administratively awkward and difficult. TRD will be able to deal with grievances concerning a denial of a certification, but will not be able to deal with information or allegations that the resident business or contractor that promised a percentage division between a resident business or contractor and a non-resident business or contractor and failed to deliver the promised percentages.~~

~~The bill provides that the protest and disbarment provisions of the procurement code (Sections 13-1-172 through 13-1-183) apply to a protest to a public body concerning the awarding of a contract in violation of the certification provisions. This means that if a bidder has evidence that a certification was fraudulently obtained, or that other provisions of the bill are violated, the aggrieved bidder can request a hearing before the state purchasing agent. The state purchasing agent may have the staff to investigate these complaints and might be the appropriate agency to administer all of the provisions of this bill, except the certification which will be administered by TRD.~~

WHAT WILL BE THE CONSEQUENCES OF NOT ENACTING THIS BILL

Procurement and contracting between private businesses and the state and local governments will be subject to the same rules and procedures as at present.

POSSIBLE QUESTIONS

Are non-resident businesses and contractors more efficient than resident businesses and contractors? If so, what can resident businesses do to improve efficiency and reduce costs and qualify for state contracts and procurement on an equal basis with out-of-state contractors?

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