

Date of Hearing: April 21, 2015

ASSEMBLY COMMITTEE ON JOBS, ECONOMIC DEVELOPMENT, AND THE ECONOMY

Eduardo Garcia, Chair

AB 1218 Weber – As Amended April 14, 2015

SUBJECT: Public contracts: disabled veteran business enterprise

SUMMARY: Makes changes to the goal and implementation actions associated with the disabled veteran business enterprise (DVBE) targeted procurement program, administered through the Department of General Services (DGS). Specifically, **this bill:**

- 1) Expands the 3% DVBE procurement participation goal to include the amount actually awarded, as well as the existing requirement to report on the value of the DVBE participation at the time the contract was let.
- 2) Modifies the existing DVBE incentive program by requiring a higher incentive for a bid package that includes a DVBE:
 - a) Serving as the prime contractor.
 - b) Prime whose workforce is comprised of more than 50% veterans or proposes to use a DVBE subcontractor who has a workforce that is comprised of more than 50% veterans.
- 3) Deletes a requirement for a periodic survey of newly certified DVBEs to determine how they learned about the program and why they became certified and, instead, requires California Department of Veteran Affairs and state contracting agencies to identify who attends state procurement promotional events and compare that list to who becomes a certified DVBE and/or participates in a state contract, as specified.
- 4) Requires awarding departments to retain DVBE payment records for five-years. The bill also requires the awarding department to establish a process to confirm that these records are submitted, accurate, and reflect the agreement set forth in the state contract. These records are already mandated to be submitted by prime contractors who have committed to using DVBE subcontractors, however, the State Auditor found that many agencies were not retaining or checking records for compliance with state law.
- 5) Refines the information DGS is already required to report in the State Consolidated Report to include:
 - a) Separate listing of the aggregate level of DVBE participation in state contracts as a prime contractor and as a subcontractor.
 - b) The aggregate amount of funds actually paid to the DVBE. Current law allows reporting of what was intended to be the DVBE participation rate at the time the contract was let.
- 6) Requires DGS to establish procedures for reporting multi-year contracts.

EXISTING LAW:

- 1) Establishes the California Disabled Veteran Business Enterprise Program, administered by DGS, for the purpose of addressing the special needs of disabled veterans seeking rehabilitation and training through entrepreneurship, and to recognize the sacrifices California's disabled veterans made during

their military service. Contracts for professional bond services are administered through the State Treasurer's Office.

- 2) Applies the 3% DVBE participation goal on each awarding state agency, department, and officer that enters into a contract for materials, supplies, equipment, alteration, repair, or improvement. This requirement can be waived on a specific contract with the approval of the department director or another designated person. Contracts with a DVBE for equipment rentals do not count toward the goal.
- 3) Defines the following terms:
 - a) A DVBE contractor, subcontractor, or supplier is any person or entity that has been certified by the administering agency and that performs a commercially useful function, as defined.
 - b) A disabled veteran is a veteran of the military, naval, or air service of the U.S. who has a service-connected disability of at least 10% and who is domiciled in the state.
 - c) A DVBE is a business certified by the administering agency as meeting all of the following requirements:
 - i) The legal structure of the business is a:
 - (1) Sole proprietorship with at least 51% owned by one or more disabled veterans;
 - (2) Publicly owned business with at least 51% of its stock unconditionally owned by one or more disabled veterans;
 - (3) Subsidiary that is wholly owned by a parent corporation, but only if at least 51% of the voting stock of the parent corporation is unconditionally owned by one or more disabled veterans; or
 - (4) Joint venture in which at least 51% of the joint venture's management, control, and earnings are held by one or more disabled veterans.
 - ii) The management and control of the daily business operations are by one or more disabled veterans. The disabled veterans who exercise management and control are not required to be the same disabled veterans as the owners of the business.
 - iii) It has a home office located in the United States, which is not a branch or subsidiary of a foreign corporation, foreign firm, or other foreign-based business.
- 4) Requires DGS to collect information from awarding departments on the level of DVBE procurement participation. The current report lists total contract values awarded and amount expected to be paid to DVBE contractors.
- 5) Requires an awarding state department to require a prime contractor who has committed to using a DVBE subcontractor to certify upon completion of the contract:
 - a) The total amount the prime contractor received under the contract.
 - b) The name and address of the DVBE that participated in the performance of the contract.
 - c) The amount each DVBE subcontractor received from the prime contractor.
 - d) That all required payments under the state contract have been made to the DVBE subcontractor.

- 6) Provides that a person or entity that knowingly provides false information on the DVBE subcontractor certification shall be subject to a civil penalty for each violation in the minimum amount of \$2,500 and the maximum amount of \$25,000.

FISCAL EFFECT: Unknown

POLICY ISSUE FRAME:

This bill implements changes to the DVBE Program in response to a 2014 State Auditor Report which found, among other things, that DVBE participation was limited to a fairly small segment of the certified DVBE contractors, compliance data was potentially misleading, and awarding departments failed to maintain sufficient records on contracts involving DVBEs.

The Comment section of the analysis includes background on the Small Business Procurement and Contract Act, current DVBE Program activity, previous legislative efforts to improve program accountability, recommendations from the 2014 State Audit, and related legislation. The author will be proposing an amendment, which is discussed in Comment 6.

COMMENTS:

- 1) **Author's Purpose:** According to the author's statement, "As California works to address the employment needs of the latest cohort of veterans from recent conflicts, it is time to revisit the Disabled Veteran Business Enterprise (DVBE) program to ensure that it works as intended and provides greater access to new entrepreneurial ventures.

A recent review of the program by the California State Auditor, found departments were using the less than accurate measure of the contract amount awarded to a DVBE, rather than actual amount paid, as a measure of performance toward the required goal of 3 percent goal. Additionally, investigators discovered that only about 2 percent of firms out of 1,400 received 83 percent of the total spent on DVBE contracts, and only 19 percent of DVBE firms are acting as prime contractors.

AB 1218 would make a number of changes to improve access to the program and to improve program accountability including, preferences for both new DVBEs and those seeking to become prime contractors; more accuracy in measuring performance toward 3 percent goals; and outcome-based measurements of DVBE recruitment efforts."

- 2) **Small Business Procurement and Contract Act:** The Small Business Procurement and Contract Act, administered through DGS, was implemented more than 30 years ago to establish a small business preference within the state's procurement process that would increase the number of contracts between the state and small businesses. A DVBE component was added in 1989.

The Small Business Procurement and Contract Act states that it is the policy of the State of California to aid the interests of small businesses in order to preserve free competitive enterprise and to ensure that a fair portion of the total purchases and contracts of the state be placed with these enterprises. The statute further states that DVBE participation is strongly encouraged to address the special needs of disabled veterans seeking rehabilitation and training through entrepreneurship, and to recognize the sacrifices of California's disabled military veterans. Statute sets an annual 3% DVBE participation goal and a 25% participation goal for small businesses and microbusinesses was set in 2006 through executive order.

- 4) **The DVBE Program:** The 3% DVBE procurement participation goal is applied to the state agency or department's overall contracting activities in the given fiscal year and may be achieved by awarding state contracts to DVBEs as prime contractors or when DVBEs are used as a subcontractor.

Awarding departments have an option of including DVBE participation in every contract or making alternative arrangements, as long as the 3% objective is met at the end of the year. Each agency and department is required to designate a small business and DVBE contracting liaison to facilitate it in meeting the 3% DVBE goal and the 25% small business goal.

Departments also have the option of offering a 1% to 5% DVBE contracting preference to assist bidders in helping to meet the state DVBE goal. Although not currently being utilized, bidders that are unable or unwilling to include a DVBE in a contract also have the option of submitting a DGS approved utilization plan that commits the businesses to using DVBEs in the future. DGS is authorized to audit businesses that submit utilization plans to ensure compliance.

State departments that fail to meet the annual 3% goal can have their delegated contracting authority removed, although DGS has never removed program authority solely based on an agency or department's failure to meet its DVBE contracting goal.

DGS has a range of responsibilities relating to the implementation of the DVBE Program including:

- Certification of DVBEs (1,537 DVBEs certified in 2013-14);
- Certification of small businesses and microbusinesses, with approximately 90% of DVBEs also holding a small business or microbusiness certifications (1,289 small businesses and microbusinesses certified in 2013-14);
- Outreach to the potential bidders and the veteran community (150 events in FY 2013-14);
- Marketing of the DVBE program to state agencies;
- Consulting with the California Procurement Contracting Academy on the DVBE training of state contracting staff;
- Preparation of an annual consolidated report on DVBE, small business, and microbusiness participation within state contracting activities; and
- Program oversight to identify abuses by bidders and failures to preform by state agencies.

Below are charts displaying three years of DVBE participation rates. The charts include information on mandatory reporting entities and all reporting entities. Under both reporting metrics, it appears that the state is consistently meeting its DVBE procurement participation goals.

DVBE Three-Year Contracting Activity – Mandated Agencies				
Fiscal Year	Total Contract Dollars	Total DVBE Dollars	Total DVBE Percent	Total DVBE Contracts
2013-14	\$6,566,406,979	\$241,002,566	3.67%	12,777
2012-13	\$7,151,257,013	\$216,903,765	3.03%	14,907
2011-12	\$7,173,594,329	\$340,156,464	4.74%	16,246
Average	\$6,963,752,774	\$266,020,932	3.82%	14,643

DVBE Three-Year Contracting Activity – All Reporting Agencies				
Fiscal Year	Total Contract Dollars	Total DVBE Dollars	Total DVBE Percent	Total DVBE Contracts
2013-14	\$8,233,113,660	\$299,683,794	3.64%	14,305
2012-13	\$8,573,498,623	\$267,285,324	3.12%	16,776
2011-12	\$8,508,477,596	\$373,936,941	4.39%	17,835
Average	\$8,438,363,293	\$313,635,353	3.7%	16,305

2013-14 DGS Consolidated Report

While the year-to-year percentages are useful to review, it is also important to note that consistency among which agencies report varies. As an example, in 2011-12, 86% of the mandatory reporting entities reported their contracting activity to DGS. In 2012-13, 79% reported their contracting activity and in 2013-14, 80% reported.

- 5) **Concerns with DVBE Program:** While DVBE participation rates are generally up, programmatic challenges continue to plague the program. Among other things, significant issues have been raised relative to the accuracy of the reporting data and on fraudulent bidder practices. In the past several years, the Committee has repeatedly heard testimony from veteran groups about bidders that fail to follow-through on the DVBE commitments made in bid proposals, bidders that use DVBEs that haven't renewed their certification, and of DVBEs being included within bid proposals, but never actually performing a commercially useful function.

Some of these program concerns have been addressed in legislation which increased penalties, defined commercially useful function, and strengthened bidder reporting requirements, including AB 177 (Ruskin and V. Manuel Pérez) Chapter 342, Statutes of 2010 and SB 1510 (Wright), Chapter 421, Statutes of 2012, respectively. A more comprehensive list of compliance enhancements is included under the related bills section of the analysis.

Other concerns, such as poor reporting of data, lack of enforcement tools, and challenges to increasing the number of certified DVBEs that participate in state contracting activities have not been comprehensively addressed in more than a decade. Responding to these and other issues, Senator Hueso, then Chair of the Senate Committee on Veterans Affairs, and former Senator Ron Calderon, requested in March 2013 that the Joint Legislative Audit Committee approve a comprehensive review of the DVBE program by the California State Auditor. The audit was released in February 2014 and among other findings, the State Auditor found the following:

- a) The objective of the program "to increase DVBE participation in state procurement," is not appropriately being measured through the current reporting system. The system measures the award value and not the actual amount DVBEs' receive.
- b) Only a small percentage of certified DVBEs serve as prime contractors. As an example, only 19% of certified DVBEs served as primes and, of those, 30 firms received 83% funding.
- c) There is inadequate documentation by state contracting agencies on DVBE participation.
- d) Reporting methodologies differ by state agencies on DVBE participation.
- e) DGS has inadequate control over the state's procurement vendor, Bidsync.
- f) CalVet needs to take a more active role in working with state agencies and tracking outreach activities.

Based on these findings, the Auditor recommended key actions for the Legislature, DGS, and CalVet. These recommendations focused on better and more consistent reporting including: verification of DVBE status before finalizing the contract, increasing the number of DVBEs that participate in state contracting, better management by the state vendor, and a heightened role and accountability for CalVet. Bills were amended in the Assembly and the Senate to address these concerns, however, both measures were unable to pass their respective appropriations committees, SB 839 (Correa) and AB 1735 (Jones-Sawyer) from 2014.

In January 2015, the State Auditor again highlighted the deficiencies in the program and encouraged the Legislature to take action. AB 1218 addresses the concerns raised in the 2014 audit, improves program accountability, and requires DGS and state awarding agencies to take actions to meet the mission of the DVBE program.

- 6) **Proposed Amendments:** Staff understands the author will present an amendment to add a third bidding preferences for bids that include a DVBE that have not formerly contracted with the state. With the committee's favorable consideration, the actual amendment will be made in the following committee.
- 7) **Related Legislation:** Below is a list of related measures including those from the current session and prior sessions.
 - a) Bills introduced in the 2015-16 Legislative Session:
 - i) **AB 351 (Jones-Sawyer) Small Business Goal:** This bill requires each state agency to establish and achieve a 25% small business participation goal. Status: scheduled to be heard on April 21, 2015, in the Assembly Committee on Jobs, Economic Development and the Economy.
 - ii) **AB 1125 (Weber) Small Business Procurement Incentives:** Increases the maximum financial value of an individual small business bid preference and the aggregate value that may be applied to a bid package that includes more than one preference. The bill also modifies the base of that calculation from being the lowest responsible bidder to the lowest responsible non-small business bidder. Status: Scheduled to be heard in the Assembly Committee on Jobs, Economic Development, and the Economy on April 21, 2015.
 - iii) **AB 1445 (Brown) Small Business Procurement Incentive:** This bill increased the maximum contract threshold amount for awards to small business, including microbusiness, and DVBEs under the state's streamlined procurement process, from \$250,000 to \$500,000, as specified. Status: Pending in the Assembly Committee on Accountability and Administrative Review.
 - iv) **SB 159 (Nielsen) DVBE Clarification:** This bill provides that the 3% DVBE procurement goal is to be measured based on the overall dollar amount expended each year by the awarding department. The bill states that this is declaratory of existing law. Status: Scheduled to be heard on April 28, 2015, in the Senate Governmental Organization Committee.
 - b) Bills introduced in a prior legislative sessions:
 - i) **AB 31 (Price) Public Contracts: Small Business Procurement and Contract Act:** This bill increased the maximum contract threshold amount for awards to small business (SME), including microbusiness, and DVBEs under the state's streamlined procurement process, from \$100,000 to \$250,000, as specified. This bill requires contractors to report the contract amount allocated to SMEs and DVBE 's with which they made contract commitments. Status: The bill was signed by the Governor, Chapter 212, Statutes of 2009.

- ii) **AB 177 (Ruskin and V. Manuel Pérez) Enforcement of Small Business Act:** This bill increases and conforms penalties for persons who falsely engage in activities relating to the Small Business Procurement and Contract Act, including small businesses, microbusinesses, and disabled veteran-owned business enterprises. Status: The bill was signed by the Governor, Chapter 342, Statutes of 2010.
- iii) **AB 309 (Price) Public Contracts: Small Business Participation:** This bill would have required the establishment of a 25% small business participation goal for all state entities and directs DGS to monitor each agency's progress in meeting this goal. The bill would have required that the Office of the Small Business Advocate receive the same progress report information as state entities and directs DGS and the Office of the Small Business Advocate to work collaboratively to assist state entities in meeting their goal. This goal is currently provided for in Executive Order (EO) D-37-01 and EO S-02-06. Status: Held in the Assembly Committee on Appropriations in May 2010.
- iv) **AB 550 (Brown) State Procurement Procedures for Small Businesses:** This bill would have required the establishment of a 25% small business participation goal for all state entities and directs DGS to monitor each agency's progress in meeting this goal. The bill would have required that the Office of the Small Business Advocate receive the same progress report information as state entities and directs DGS and the Office of the Small Business Advocate to work collaboratively to assist state entities in meeting their goal. This goal is currently provided for in Executive Order (EO) D-37-01 and EO S-02-06. Status: Held on the Suspense File of the Assembly Committee on Appropriations, 2013.
- v) **AB 1568 (Grove) Quotes for Public Contracts:** This bill would have required state agencies that opt to acquire goods, services, or information technology through a specified small business and disabled veteran business enterprise contracting option to solicit at least three price quotes, and obtain at least two quotes before awarding the contract. Status: Held on the Suspense File in the Senate Committee on Appropriations, 2014.
- vi) **AB 1734 (Jones-Sawyer) Public contracts: Small Business Participation: Disabled Veterans:** This bill would have required each state agency to establish and achieve a 25% small business participation goal and increased the annual procurement participation goal for disabled veteran business enterprise from 3% to 5% of the value of state contracts. In addition the bill required greater reporting and accountability of DVBE program information. Status: Held on the Suspense File in the Assembly Committee on Appropriations, 2014.
- vii) **AB 2249 (Ruskin) DVBE Documentation:** This bill requires applicants for small business or DVBE certification to submit a written declaration, under penalty of perjury, that the information submitted to DGS is true and correct. The bill also authorizes DGS, if it determines that just cause exists, to require the owner of a DVBE or small business to submit the Internal Revenue Service Form 4506-T which would allow DGS to obtain a copy of their tax return. Finally, the bill requires that at least 51% of the stock or voting stock of a disabled veteran business enterprise be unconditionally owned by disabled veterans. Status: Signed by the Governor, Chapter 383, Statutes of 2010.
- viii) **AB 2682 (Wagner) Responsible Small Business and DVBE Contractors:** This bill would have required a state agency that solicits offers, awards a contract, or consents to subcontracts, under the Small Business Procurement and Contract Act, to do so only with responsible and reliable parties. Prohibits a state agency from allowing a party to participate in any procurement activity if the party has been suspended, debarred, or otherwise excluded from

participation in a state contract. Status: Died in the Assembly Committee on Accountability and Administrative Review, 2014.

- ix) ***SB 67 (Price) Small Business Participation in Public Contracts***: This bill would have authorized DGS to direct all state entities to establish an annual goal of achieving no less than 25% small business participation in state procurement contracts, as specified. This goal is currently provided for in Executive Order (EO) D-37-01 and EO S-02-06. Status: Held in the Assembly Committee on Appropriations in 2011.
- x) ***SB 733 (Block) Disabled Veteran Business Enterprise Participation Goals***: This bill deletes provisions of law allowing an awarding department to accept submission of a disabled veteran business enterprise utilization plan to meet the 3% statewide participation goal for awarded contracts. The bill authorizes, instead, a new review process for demonstrating a business's long-term commitment to using veteran-owned businesses. Status: Died in the Assembly Committee on Jobs, Economic Development, and the Economy, 2014.
- xi) ***SB 839 (Correa) Contracting with Veterans***: This bill would have modified reporting requirements for state departments with respect to DVBEs including contracts where the DVBE acted as the prime and as a subcontractor. Status: Held on the Suspense File in the Senate Committee on Appropriations, 2014.
- xii) ***SB 941 (Flores) DVBE Advocates***: This bill requires the Department of Veteran's Affairs and awarding departments to appoint DVBE advocates to assist in meeting DVBE procurement participation goals. Status: Signed by the Governor, Chapter 666, Statutes of 2002.
- xiii) ***SB 1510 (Wright) Commercial Useful Purpose***: This bill tightens the bidder requirements for demonstrating that a small business, microbusiness, or DVBE will serve a commercially useful function (CUF) in carrying out a state contract. The purpose of the CUF requirement is to prevent a bidder from using a business as a "pass through" or "front" for another business that would otherwise not qualify for the small business, microbusiness or DVBE bid preference. By meeting the CUF requirements, a bidder may claim a bid preference on competitive state contracts for goods, services, informational technology, and public works. Status: The bill was signed by the Governor, Chapter 421, Statutes of 2012.

- 8) **Double Referral**: The Assembly Rules Committee has referred this to measure the Assembly Committee on Jobs, Economic Development and the Economy and to the Assembly Committee on Accountability and Administrative Review (AAR). Should this measure pass the committee, it will be referred to AAR for further policy consideration.

REGISTERED SUPPORT / OPPOSITION:

Support

None received

Opposition

None received