

Date of Hearing: April 21, 2015

ASSEMBLY COMMITTEE ON JOBS, ECONOMIC DEVELOPMENT, AND THE ECONOMY

Eduardo Garcia, Chair

AB 351 (Jones-Sawyer) – As Introduced February 17, 2015

SUBJECT: Public contracts: small business participation

SUMMARY: Requires each state agency to establish and achieve a 25% small business participation goal. Specifically, **this bill:**

- 1) Establishes a 25% small business participation goal for contracting activities by state agencies, boards, departments, and commissions.
- 2) Assigns the responsibility for achieving this goal to the heads of the contracting departments and requires them to annually report his or her agency's progress in meeting the goal.
- 3) Requires agencies that fail to meet their annual small business procurement participation goal to submit a corrective plan to the Department of General Services (DGS) within 45 days of the close of any fiscal year.
- 4) Requires DGS to regularly monitor the progress agencies are making in meeting the 25% goal and to regularly share related information with the Office of the Small Business Advocate (OSBA) including providing a copy of the corrective action plans. DGS and the OSBA are directed to assist agencies, to the extent feasible, in implementing their corrective action plans.
- 5) Requires all state agencies to use the streamlined small business procurement process for contracts under \$100,000 and construction contracts under \$120,000.
- 6) Requires DGS to actively outreach and promote the small business preference programs and in doing so collaborate with the OSBA.
- 7) Specifies that the small business provisions of this act apply to the University of California, the California State University, and the California Community Colleges when contracting with state funds.

EXISTING LAW:

- 1) Designates the DGS as the administer of the state Small Business Procurement and Contract Act (Small Business Procurement Act), which includes certifying and implementing targeted preference programs for certified small businesses, microbusinesses, and disabled veteran owned business enterprises (DVBE).
- 2) Authorizes a 5% preference for state contract bidders that are either a certified small or microbusiness or commit to using a certified small or microbusiness in effecting the contract.
- 3) Authorizes a streamlined small business procurement process for state contracts over \$50,000 and under \$250,000. Under this process, the contract is not put out to public bid, instead the contracting agency is allowed to award the contract to a certified small business or DVBE after obtaining a two price quotes from two certified small businesses and/or DVBEs.

- 4) Defines a small business as independently owned, not dominant in its field of operation, domiciled in California, employing 100 or fewer employees, and earning \$10 million or less in average annual gross revenues for the three previous years.
- 5) Defines a microbusiness as a small business (refer to definition above) that has an average annual gross receipt of \$3.5 million or less during the previous three years or is a manufacturer with 25 or fewer employees.

FISCAL EFFECT: Unknown

POLICY ISSUE FRAME:

Small businesses play an essential role within the California economy, contributing the most net new jobs, offering an alternative to un- and underemployment, and helping to disburse the financial advantages of the state's globally connected economy. State procurement opportunities represent an important economic tool to support small business development. In the last 15 report periods, the state has met the 25% small business procurement participation goal only five times including 2013-14.

This bill proposes to codify the 25% small business procurement participation goal, assign specific responsibility for meeting the goal, mandate corrective action plans, and provide support for state agencies in taking remedial actions to meet the goal. The Comment section of the analysis includes additional information on the state's Small Business Act, historic compliance issues, and current and prior legislation.

COMMENTS:

- 1) **Author's Purpose:** According to the author, "Codifying this executive order, not only places the policy in statute, only to be removed by the Legislature, but also sends a strong message to potential investors that the State of California supports small businesses".
- 2) **The Role of Small Businesses within the California Economy:** California's dominance in many economic areas is based, in part, on the significant role small businesses play in the state's \$2.2 trillion economy. Two separate studies, one by the U.S. Census Bureau and another by the Kaufman Foundation, found that net job growth was strongest among businesses with less than 20 employees. Among other advantages, small businesses are crucial in the state's international competitiveness and are an important means for dispersing the positive economic impacts of trade within the California economy.

Nonemployer firms make up the single largest component of businesses in California, 2.9 million out of an estimated 3.6 million firms in 2012, representing over \$149 billion in revenues with highest number of businesses in the professional, scientific, and technical services industry sector. As these non-employer businesses grow, they continue to serve as an important component of California's dynamic economy. Excluding nonemployer firms, businesses with less than 20 employees comprise nearly 90% of all businesses and employ approximately 18% of all workers. These non-employer and small employer firms create jobs, generate taxes, and revitalize communities.

In hard economic times, smaller size businesses often function as economic engines. In this most recent recession the trend continued, with the number of nonemployer firms increasing from 2.6 million firms (\$137 billion in revenues) for 2008 to 2.8 million firms (\$138 billion in revenues) for

2010. In the post-recession economy, small businesses are expected to become increasingly important due to their ability to be more flexible and better suited to meet niche market needs. Their small size, however, results in certain challenges in meeting regulatory requirements, accessing capital, and marketing their goods and services. California's network of technical assistance providers assist businesses with a range of services, including access to quality education, one-on-one counseling, mentoring, marketing data, and other business development resources.

- 3) **Small Business Procurement Act:** The Small Business Procurement 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 DBVE component was added in 1989. Today, approximately 90% of DVBEs have dual certification as a small business or microbusiness.

The Small Business Procurement Act states that it is the policy of the State of California that the state 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 2010 executive order sets a 25% goal for small businesses and microbusinesses.

The charts below show small business and microbusiness aggregate procurement participation rates for fiscal years 2011-12, 2012-13, and 2013-14 for mandatory reporting agencies and total reporting agencies.

Small Business and Microbusiness Contracting Activity – Mandated Reporters				
Fiscal year	Total Contract Dollars	Total Small Business and Micobusiness Contract Dollars	Total Percent	Total Number of Contracts
2013-14	\$7,101,433,433	\$2,013,377,792	28.35%	90,784
2012-13	\$7,616,142,071	\$1,801,695,547	23.66%	105,617
2011-12	\$7,399,022,425	\$1,796,451,722	24.28%	165,523
Average	\$7,372,199,310	\$1,870,508,354	25.43%	120,641

2013-14 DGS Statewide Consolidated Annual Report

Small Business and Microbusiness Contracting Activity – Total Reporting				
Fiscal year	Total Contract Dollars	Total Small Business and Micobusiness Contract Dollars	Total Percent	Total Number of Contracts
2013-14	\$8,768,140,114	\$2,262,238,822	25.8%	102,480
2012-13	\$9,038,383,681	\$2,011,723,130	22.26%	123,668
2011-12	\$8,733,905,692	\$2,021,984,956	23.15%	179,471
Average	\$8,846,809,829	\$2,098,648,969	23.74%	135,206

2013-14 DGS Statewide Consolidated Annual Report

Unfortunately, participation rates have not been as high as desired, with state agencies meeting the 25% small business goal in only five out of the last 15 report years. Further, in comparing year to year numbers, it is important to note that not all of the mandatory reporting agencies provide annual data to DGS for inclusion in the report. As an example, only 80% of the mandatory reporters provided data for 2013-14.

- 4) **Increasing Small Business and DVBE Procurement Participation:** Every year, Members of the Legislature introduce a range of bills to improve outreach and increase targeted preferences to increase small business participation in state contracting. Over the years, direct and innovative approaches have been added including mandating small business and DVBE liaisons at every agency, establishing official state-level Small Business and DVBE Advocates, and requiring the state join a national on-line contracting platform (BidSync), which is soon to be transferred back to a state-only web platform (F\$SCAL).

Among other challenges, is the high concentration of contracting within a few departments including several which bid contracts for specialized services. According to the 2013-14 Statewide Consolidated Annual Report by DGS, the top 10 contracting agencies awarded more than 83% of contract dollars in 2013-14. The data suggests that having department specific strategies to increase small business participation will be required to consistently meet the 25% goal.

In 2013-14, 61% of all state contracts were awarded by the Department of Corrections (SDCR), the Department of Transportation, and the Department of Health Care Services (DHCS). This means that regardless of the efforts of the California School Finance Authority (88.04% of the \$99.677 contracts awarded) and California Transportation Commission (89.44% of the \$14,291 in contracts awarded), the state's largest contracting entities must do a better job in contracting with small businesses and microbusiness if the state is going to consistently meet its mission of offering small businesses meaningful procurement opportunities. The chart below shows information on the contracting activities of the top 10 contracting departments for 2013-14.

Top 10 Contracting Agencies in 2013-14				
Departments	Total Contact Dollars	Percentage of Statewide Spending	Small Business and Microbusiness Participation Percentage	DVBE Participation Percentage
All Mandatory Reporters	\$7,372,199,310	100%	28.35%	3.67%
Corrections and Rehabilitation	\$2,196,722,703	30.93%	36.03%	3.60%
Transportation	\$1,0174,833,768	15.14%	28.24%	3.70%
Health Care Services (DHCS)	\$1,069,021,018	15.05%	2.36%	0.45%
State Hospitals	\$553,519,167	7.79%	49.17%	2.12%
Water Resources	\$351,102,439	4.94%	19.79%	2.62%
Highway Patrol	\$234,348,394	3.30	12.28	1.72
General Services	135,233,255	1.90%	42.23%	10.49%
Parks and Recreation	123,503,810	1.74%	31.49%	6.76%
Motor Vehicles	111,305,071	1.57%	25.09%	6.55%
Public Utilities Commission	\$99,350,011	1.40	12.34	3.34
Top 10 Total	\$5,975,205,480	83.77%	27.35%	3.02%

Source: 2013-14 Statewide Consolidated Annual Report prepared by DGS

According to DGS, the state's inability to reach its small business procurement goal in 2011-12 was directly attributable to DHCS' poor performance. In 2011, DHCS issued a multiyear contract for Medi-Cal Dental Services worth \$300 million per year without any small business or DVBE participation. Had DHCS met their small business goals on this one contract, DHCS would have had

a 21% small business participation rate, instead of the reported 5%. DGS suggested that DHCS focus on certifying the individual dentists that will be subcontracting under the master Delta Dental contract, otherwise this single contract will continue to hold down the state's overall participation rates for years to come.

In 2013-14, as shown above, DHCS contracted with small business for only 2.36% of its contracting activities. In fact, the Health and Human Services Agency had the lowest overall small business and microbusiness participation rates (20.285) among all other agencies in the state.

5) **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 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.
- ii) ***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 states streamlined procurement process, from \$250,000 to \$500,000, as specified. Status: Pending in the Assembly Committee on Accountability and Administrative Review.

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 states 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 172 (Weber) State Agency Contracts and Microbusiness Preference:*** This bill would have created the microbusiness procurement preference from 5% to 7% for state contracts to purchase goods, services, information technology, and construction of state facilities. The preference may be awarded to either a microbusiness bidder or a non-microbusiness bidder that uses a microbusiness subcontractor. Status: Held on the Suspense File of the Assembly Committee on Appropriations, 2013.
- iii) ***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.
- iv) ***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.

- i) **AB 550 (Brown) Office of Small Business and Disabled Veteran Business Enterprise Services:** This bill would have codified the 25% small business participation goal in state procurement, which was initially set through Executive Order (EO) D-37-01 and EO S-02-06. The bill also would have made key changes to state procurement procedures for the purpose of increasing small business, including microbusiness, and disabled veteran-owned business enterprise participation rates. Status: Held on the Suspense File of the Assembly Committee on Appropriations, 2013.
- ii) **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.
- iii) **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. Status: Held on the Suspense File in the Assembly Committee on Appropriations, 2014.
- iv) **AB 2278 (Weber) Small Business Procurement Incentive:** This bill would have increased 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: Held on the Suspense File of the Assembly Committee on Appropriations, 2014.
- v) **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.
- vi) **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. Status: Held in the Assembly Committee on Appropriations in 2011.
- vii) **SB 733 (Price) High Speed Rail:** This bill would have required the California High-Speed Rail Authority (HSRA) to include in its January 1, 2012 business plan a strategy for ensuring California-certified small business participation in contracts awarded with state and federal funds during all phases of the high-speed rail project. It also would have required the HSRA to have a strategy for working with the Employment Development Department to ensure that at least 25% of the project workforce at each worksite is from the local workforce. Status: Held in Senate Committee on Appropriations in 2011.

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

REGISTERED SUPPORT / OPPOSITION:

Support

California Asian Pacific Chamber of Commerce

Opposition

None received

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