

Date of Hearing: March 28, 2017

ASSEMBLY COMMITTEE ON JOBS, ECONOMIC DEVELOPMENT, AND THE ECONOMY

Sharon Quirk-Silva, Chair

AB 632 (Acosta) – As Introduced March 21, 2017

SUBJECT: Small Business Procurement and Contract Act: disabled veteran business enterprise

SUMMARY: Increases the maximum contract amount for direct source contracting with a disabled veteran owned business enterprise (DVBE) under the Streamline Procurement Option from \$250,000 to \$500,000. Prior to making the award, existing law, not modified in this bill, requires the agency to obtain price quotations from two or more DVBEs.

EXISTING LAW:

- 1) Establishes the California Disabled Veteran Business Enterprise Program, administered by Department of General Services (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) Authorizes a state agency to utilize the Streamline Procurement Option when awarding a contract for the acquisition of goods, services, or information technology to a certified small business, including a microbusiness, or to a DVBE, if the estimated value is greater than \$5,000, but less than \$250,000. Prior to making the award, the agency is required to obtain price quotations from two or more certified small business, including a microbusiness, or DVBEs.
- 4) 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.

FISCAL EFFECT: Unknown

POLICY FRAMEWORK:

Each year, California state government enters into billions of dollars in contracts. In 2015-16, \$8.1 billion in contracts were awarded through 159 different department and agencies. These moneys present an important revenue stream for businesses, including the 21,739 contracts which were awarded to DVBEs.

The state has developed a number of programs to encourage contract participation by DVBEs and small businesses. Among those incentives is a Streamlined Procurement Option, which allows a state entity to bypass the more timely and complex bidding process and, instead, directly contact with a DVBE or small business. Costs are contained by limiting the size of the contracts to only those between \$5,000 and \$250,000 and requiring comparable price quotations from two or more small businesses or DVBEs.

This bill would increase the maximum dollar amount for contracts with DVBEs to as high as \$500,000, while leaving the current \$250,000 limit for contracts with small businesses. While this is intended to be beneficial to DVBEs, the two tier approach of small businesses having certain limits and DVBEs having another could inadvertently remove some of the advantages of the Streamlined Procurement Option.

The Coalition of Small and Disabled Veteran Businesses, opposed to this bill, raised concerns over the state's overall use of the Streamlined Procurement Option and does not support expanding its use. Opposition arguments are discussed in Comment 7. The analysis also includes background on the DVBE Program, the Streamlined Procurement Option, and an extended list of related legislation.

COMMENTS:

- 1) **Small Business Procurement and Contract Act:** The Small Business Procurement and Contract Act (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 DVBE component was added in 1989.

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 25% goal is set through executive order for small businesses and microbusinesses.

In 2015-16 there were 25,834 certified small businesses and microbusinesses and 1,736 certified DVBEs. A majority of DVBEs are smaller size firms with 75.4% of holding a dual certification as a DVBE and microbusiness and 9.6% having a dual DVBE and small business certification. The remaining 15% of DVBEs operate with only a single DVBE certification.

- 4) **Streamlined Procurement Option:** To assist the state in reaching the small business and DVBE procurement goals, contracting entities have the option of using a streamlined procurement method. This method allows the awarding entity to bypass the general advertising, bidding, and protest provisions in the State Contract Act and use special provisions to directly contract with a certified small business or DVBE. Prior to entering into the contract, the state entity is required to assess the appropriateness of the proposed contract price by checking the rate with two or more small businesses or DVBEs.

Contracts offered under the Streamlined Procurement Option are currently limited to contracts between \$5,000 and \$250,000. AB 632 would increase the amount to \$500,000 for DVBE contracts issued for goods, services, and information technology. In 2015-16, 15,207 contracts were initiated using this Streamlined Procurement Option, which accounts for over \$426 million in contracting. The California State University System reported using this process for 560 contracts totaling \$31 million in contracts.

DGS is currently not able to provide data on the number of contracts that were awarded to small business vs. DVBE using the Streamlined Procurement Option. In the future, beginning with contracting activity on or after January 2016, FISCAL will be able to track and report each of the targeted procurement categories separately.

While prior bills have proposed increasing the contracting cap on both small business and DVBEs, this bill creates a two tier system. Given that less than 7% of DVBEs are not dually certified as a small or microbusiness, the overall impact on contracting activity may be small. According to the author, this disparity is necessary in order to limit the bills projected fiscal impact on the General Fund and is appropriate given DVBE's sacrifices and service to the county.

- 5) **Impact of Increasing Contracting Limit:** According to data from the State Contract & Procurement Registration System, in FY 2015-16, there were a total of 160,143 contracts valued between \$1 and \$499,999, including those that were awarded using the Streamlined Procurement Option and those awarded under all other bidding procedures. Of these contracts, only 718 (0.45%) were valued between \$250,000 and \$499,999.
- 6) **The DVBE Program:** The 3% DVBE procurement participation goal applies 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% contracting incentive to strengthen the competitiveness of DVBE primes and non-DVBE primes that subcontract with DVBEs. Although not currently being utilized, statute includes authority for bidders that are unable or unwilling to include a

DVBE in a contract to submit a utilization plan to DGS 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 (2,043 DVBEs certified in 2015-16);
- Certification of small businesses and microbusinesses (25,824 small businesses and microbusinesses certified in 2015-16);
- Outreach to the potential bidders and the veteran community (191 events in FY 2015-16);
- Marketing of the DVBE program to state agencies;
- Partnering with CalVet on meetings with departments that are not meeting participation goals.
- 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 microbusinesses participation within state contracting activities; and
- Program oversight to identify abuses by bidders and failures to preform by state agencies.

In a further effort to increase oversight and enhance small business and DVBE contracting activities DGS and the California Department of Veterans Affairs, met with 13 departments during 2015-16 that did not achieve one or both of their goals, including:

- High spend state entities with over \$20 million in annual contracting: California High Speed Rail Authority; California Public Utilities Commission, and the Office of Systems Integration.
- Small and medium-spend state entities with under \$20 million in annual contracts: Agricultural Labor Relations Board; California Housing Finance Agency; California Arts Council; California Human Resources/State Personnel Board; California Science Center; Delta Stewardship Council; Department of Managed Health Care; Governor's Office of Business and Economic Development; Office of Environmental Health Hazard Assessment; and the California Coastal Conservancy.

Below are charts displaying five 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 Five-Year Contracting Activity – Mandated Agencies (dollars in millions)				
Fiscal Year	Total Contract Dollars	Total DVBE Dollars	Total DVBE Percent	Total DVBE Contracts
2015-16	\$5,855	\$274	4.67%	18,638
2014-15	\$8,105	\$314	3.87%	16,192
2013-14	\$6,566	\$241	3.67%	12,777
2012-13	\$7,151	\$216	3.03%	14,907
2011-12	\$7,173	\$340	4.74%	16,246
Average	\$6,970	\$277	4.00%	15,752

DGS Consolidated Reports for specified contracting periods

DVBE Five-Year Contracting Activity – All Reporting Agencies (dollars in in millions)				
Fiscal Year	Total Contract Dollars	Total DVBE Dollars	Total DVBE Percent	Total DVBE Contracts
2015-16	\$8,090	\$349	4.41%	21,739
2014-15	\$10,073	\$407	4.04%	18,228
2013-14	\$8,233	\$299	3.64%	14,305
2012-13	\$8,573	\$267	3.12%	16,776
2011-12	\$8,508	\$373	4.39%	17,835
Average	\$8,695	\$339	3.92%	17776

DGS Consolidated Reports for specified contracting periods

While the year-to-year percentages are useful to review, it is also important to note that consistency among which agencies report or even which agencies believe that they are mandated to report varies. As an example, in 2011-12 86% of the mandatory reporting entities reported their contracting activity to DGS. For 2013-14, 2014-15, and 2015-16 only 80% of mandatory reporters provided the required data to DGS.

- 7) **Opposition:** The Coalition of Small and Disabled Veteran Businesses, opposed to this bill, has raised concerns over the state's overall use of the Streamlined Procurement Option and does not support expanding its use. Based on previous enforcement actions against small businesses who have allegedly colluded to set artificially high contract prices and the findings from the 2014 State Audit, they state that "this proposed measure is extremely dangerous and virtually guaranteed [not] to provide the proposed benefits the sponsors claim."

The Coalition of Small and Disabled Veteran Businesses further states that the previous increase in the contract cap did not actually result in increased DVBE and small business contracting. In 2016, the Coalition of Small and Disabled Veteran Businesses hired a consultant to examine the number of state contracts valued at less than \$250,000 which were awarded to small businesses and DVBE's following the implementation of 2010 increase in contract size, AB 31 (Price), Chapter 212, Statutes of 2009. According to the assessment, the number of small businesses and DVBEs being awarded contracts below \$250,000 decreased significantly from prior periods.

Another area of concern raised by the Coalition of Small and Disabled Veteran Businesses relates the small number of prime contractors that are DVBEs. According to a 2014 state audit, "The top 30 DVBE firms from fiscal year 2012–13 made up 83 percent of the total amount the State awarded to DVBE businesses directly—and these top 30 DVBE firms also accounted for 76 percent of the total number of DVBE contracts awarded. Although SCPRS may not include all lower value DVBE contracts, the data in SCPRS nevertheless provide a strong indicator that only a relatively small subset of DVBE firms enjoy the major part of the State's business."

DGS acknowledges that the 2014 audit identified a number areas where program delivery could be strengthened and have made changes. Among other activities, DGS negotiated more small business and DVBE contracting "off-ramps" to the state large strategically sourced contracts, as well as modifying guidance documents and staff training curriculum. DGS also increased engagement with low performing state agencies (as discussed above) and publically committed to more closely monitoring the use of the Streamlined Procurement Option. Beginning in 2016, DGS transferred to the state's multiagency computer platform, FISCAL. This new online platform should provide DGS with new tools to track contracting activities.

At the writing of this analysis, the author had requested, but had not yet met with the opposition. Mr. Acosta provided this statement: "I fully support DGS' efforts and commitment to address any issues with bad actors who are utilizing the streamlined contracting process for small businesses and DVBEs. DGS has recognized there is an issue and has the authority to pursue enforcement actions against these bad actors within the program. I have reached out to the opposition to discuss their issues and explore options to possibly resolve those issues."

8) **Related Legislation:** Below is a list of related measures.

- a) *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.
- b) *AB 1445 (Brown) Streamlined Contracting Authority:* This bill would have increased the maximum amount a state agency is authorized to directly contract with a certified small business or disabled veteran business enterprise, from \$250,000 to \$500,000. Status: Held on the Suspense File of the Assembly Committee on Appropriations, 2015.
- c) *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.
- d) *AB 2358 (Bigelow and Wood) Streamlined Contracting Authority:* This bill, as passed by the Assembly, would have increased the maximum amount for which a state agency can directly contract with a certified small business or a disabled veteran business enterprise from \$250,000 to \$300,000. Status: The contracting related language was removed in the Senate and the bill became a vehicle for an unrelated issue. Signed by the Governor, Chapter 298, Statutes of 2016.
- e) *SB 276 (Roth) Streamlined Contracting Authority:* This bill would have increased the maximum amount a state agency is authorized to directly contract with a certified small business or disabled veteran business enterprise, from \$250,000 to \$500,000. Status: Held on the Suspense File of the Senate Committee on Appropriations, 2013.

REGISTERED SUPPORT / OPPOSITION:

Support

2020 VET
CMG Alliance
CommTech
Global Blue
Global Environmental Network, Inc.
Granite Data Solutions
KKO Labs
Sandberg Group

Opposition

Coalition of Small and Disabled Veteran Businesses

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