NORTH CAROLINA GENERAL ASSEMBLY

LEGISLATIVE FISCAL NOTE

BILL NUMBER: House Bill 1447

SHORT TITLE: Small Business Procurement Act

SPONSOR(S): Representative Shaw

FISCAL IMPACT: **Expenditures:** **Increase ()** **Decrease ()**
Revenues: **Increase ()** **Decrease ()**
No Impact ()
No Estimate Available (X**)**

FUND AFFECTED: **General Fund (**X**)** **Highway Fund (**X**)** **Local Govt. ()**
Other Funds (X**)**

BILL SUMMARY: SMALL BUSINESS PROCUREMENT ACT. TO REQUIRE THE SECRETARY OF ADMINISTRATION TO SET BUSINESS SIZE STANDARDS AND APPLY THEM TO THE PROCUREMENT PROCEDURES TO PROMOTE INCREASED PROCUREMENTS FROM SMALL AND MEDIUM-SIZED BUSINESSES. G.S. 143-52, =53, and -54 as title indicates. Requires report by Department of Administration to the General Assembly prior to the 1997 Session on measures to encourage the use of small and medium sized businesses to provide supplies, materials, equipment, and contractual services to state government.

EFFECTIVE DATE: Upon ratification.

PRINCIPAL DEPARTMENT(S)/PROGRAM(S) AFFECTED: Potential administrative costs could affect the Department of Administration. Potential increases in the costs of goods and services purchased by the State could affect all agencies and programs.

FISCAL IMPACT

	FY 1996-97	FY 1997-98	FY 1998-99	FY 1999-00	FY 2000-01
EXPENDITURES:	**No estimate available**				

ASSUMPTIONS AND METHODOLOGY:

Preferences based on size
The bill could affect competitive bidding procedures for the awarding of term (indefinite quantity) contracts. Currently, the Secretary of Administration consolidates estimates of the State's needs for certain products, and awards contracts for these products to the suppliers who submit the "lowest responsive and responsible bid." The goal of the current system is to minimize the price the State pays for goods and

services by obtaining volume discounts and by fostering competition among bidders.

The bill would modify this emphasis on low purchase price by requiring DOA to establish procedures for dividing estimates of the State's needs among businesses based on firm size. In practice, this bill could result in the State awarding some of its contracts to firms based on their size rather than on the competitiveness of their price. The frequency with which this could occur cannot be determined, nor can its affect on bid prices. However, reduction in price competition could increase the prices the State pays for goods and services purchased under term contracts.

Public procurement officials believe that preferences based on business size reduce competition and increase the costs of goods and services. A resolution by the National Institute of Governmental Purchasing states that it is "opposed to all types of preference law and practice and views it as an impediment to cost effective procurement of goods, services and construction in a free enterprise system."

Preferences based on firm size could also affect prices indirectly. Dividing purchases on term contracts among more firms would reduce the volume of business awarded to a single vendor. Purchasing experts believe that reducing the volume of business awarded to any one supplier would reduce the volume discounts the State receives on items it purchases. According to procurement consultant Willis Brown, because prices per unit typically increase as volume decreases, this legislation could result in higher unit prices.

Consolidation of bids from small and medium firms

Current State law requires that firms submit separate, competitive bids. The requirement is based on the widely accepted theory that separate, competitive bids foster competition between firms, and that this competition leads to lower prices. The Small Business Procurement Act could reduce competition by allowing firms to consolidate their bids. In other words, firms would be permitted to submit a consolidated bid rather than separate, competitive bids. This practice could reduce competition and could have an inflationary effect on the prices the State pays for goods and services. All seven of the procurement professionals we met with or interviewed over the telephone believed that allowing firms to consolidate bids would decrease price competition and raise prices.

Administrative Costs

Procurement professionals contacted in connection with this fiscal note believe that preference programs - in this case based on firm size - increase the administrative costs of purchasing goods and services. A reference from State and Local Government Purchasing, published by the National Association of State Purchasing Officials states:

> "The past decade has seen substantial growth in _procurement preferences for the goods and services of small business, minority or women-owned business, veterans or labor area legislation. These preferences_are political products. Unfortunately, there

has been little substantive demonstration of program cost or quality effectiveness. Rather, there has been strong indications of increased administrative costs and unnecessary limitations on competition." (emphasis added)

The opinion that preferences increase administrative costs is based on arguments that preference programs require more preparation time for bid requests and require more time to work with larger numbers of suppliers. Also, because business size introduces an additional element of complexity into award decisions, these award decisions would probably require more time and effort. Finally, House Bill 1447 would also require the Secretary of Administration to establish standards for the size of small and medium size businesses and establish procedures for dividing State purchases among these firms.

Fiscal Impact

We cannot estimate what this bill would cost the State for a number of reasons discussed below:

1)The rules and regulations that would implement this legislation have not yet been established. These rules will determine the administrative costs. The Department has not provided information on what rules and regulations would be adopted.

2)A workload analysis of the impact of these rules and regulations is required before we can estimate the fiscal impact of these rules. The Department's estimate of the administrative costs associated with this bill is based not on an analysis of the Purchase and Contract workload, but on speculation.

3)We cannot estimate the economic effects of preferences and consolidated bids on the prices of goods and services purchased by the State. For perspective, the value of goods and services purchased annually from statewide term contracts is $500 million.

In summary, we believe that establishing preferences based on company size, and allowing small and medium firms to consolidate bids would likely increase prices and administrative costs, but we cannot estimate the amount of these increases.

SOURCES OF DATA: Willis Holding, Jr., public procurement specialist and consultant; Don Buffum, Mississippi Office of Purchasing and Travel; Paula Moskowitz, New York Department of General Services, Standards and Purchasing Group; Hal D'Ambrogia, procurement consultant, Peat Marwick; Jerry Elefante, Associate Director for Purchasing, UNC-CH; Mary Saunders, Assistant Director of Purchasing, NCSU; John Leaston, North Carolina Director of Purchase and Contract; Glen Peterson, General Counsel, DOA; State and Local Government Purchasing, National Association of Purchasing Officials; National Institute of Governmental Purchasing.

TECHNICAL CONSIDERATIONS: In a memorandum to fiscal staff, General Counsel for the Department of Administration stated its opinion that the provision allowing consolidation of bids from small and medium firms may violate federal antitrust laws.

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DATE: June 17, 1996

Official
Fiscal Research Division
Publication

Signed Copy Located in the NCGA Principal Clerk's Offices