Considering Local Business Preference Policies in Bids and Purchases

By Semoon Chang

Finance officers need to consider the approximate economic benefit the community receives from local preference policies.

Many state and local governments give preference to local businesses in bidding and purchasing, but jurisdictions don't always analyze the concept. Finance officials need to know approximately, if not exactly, how much economic benefit the community receives from purchasing goods from local suppliers, rather than from outside suppliers. This article reviews the issues involved with local preference policies, allowing finance officers to take a closer look at the practice.

The term "local preference" encompasses several ways in which local governments favor local businesses. What is meant by a "local business" varies and can refer to a business that is owned by local residents, or to the local branch of a multi-state business that has a local business license, pays all local taxes, and hires all local residents as its employees. There is also more than one type of local preference. One jurisdiction might issue requests for proposals specifying that qualifying businesses have a local presence; another might allow extra points or higher bid prices for local contractors; a higher bid price for locally produced goods or local suppliers in construction and public works projects; and still others might require vendors to employ local residents.

PRACTICES IN CITIES AND COUNTIES

Issues relating to local preference policies at the municipal level vary widely; there are no national surveys of preference policies at the local level. Exhibit 1 summarizes policies in selected cities for local preferences in terms of percentage benefits, types of contracts subject to local preference, any limitation in dollar amounts, and reciprocal laws. The appropriate cells are left blank whenever information was not clearly stated.

Cities that maintain local preference policies usually limit their preference to businesses with city business licenses and locations within the city limits, although some expand their location requirement to include the county in which the city is located. Some cities require the local business to have been in their jurisdiction for at least a year. Most cities, however, do not have an explicit statement of such requirement.

The percentage preference given to local businesses ranges from 1 to 5 percent, with the 5 percent being most popular. Also, some cities set a maximum amount of contracts that their preference will apply to, and others set a minimum amount. Many cities exclude public works and construction contracts from their preference policies, while others include public

Exhibit 1: Local Preference Policies in Selected Cities

City	State	Preference	Public Works/Reciprocity? Construction Included?	Note
Albuquerque	NM	5% local +5% local small	No	Small = SBA standards
Baltimore	MD	3% women-owned 20% minority-own	No	Applies to purchases over $25,000
Berkeley	CA	5% (up to $25,000)		Vendor pays full price once selected
Chicago	IL	2%	No	
Columbus	OH	1%: $10,000+ 5%: $10,000-	No	
Dallas	TX		Yes	Texas law provides reciprocity
Detroit	MI	2%: $500000.01+ 3%: $100,000.01+ 4%: $10,000.01+ 5% up to $10,000	No	
D of Columbia		5%		Administrative practice
Fremont	CA	5% on $25,000+ 2.5% on bids	No	Benefit limited to $10,000 purchases
Grover Beach	CA	5%	Yes	Public works 5% or $5,000, whichever is lower
Houston	TX		Yes	Texas law provides reciprocity
Los Angeles	CA	10% small & local	No	Small business with gross receipts up to $3 million; applies to contracts up to $100,000 PLA applies in hiring
Memphis	TN	5% on $10,000	No	Preference not to exceed purchases $100,000 5% on RFPs
Milwaukee	WI	5%	No	Applies to bids and purchases
New York	NY			5% local preference repealed in 1999
Oakland	CA	1% for every 10% of contract dollars up to 5% total	Yes	Applies to bids and 75% of construction under $100,000 awarded to local business; construction over $100,000 should have 20%+ local participation
Palmetto	FL			"The city reserves the right to select any applicant…"
Pearland	TX	3% $3,000-50,000 5% $50000-100000		
Phoenix	AZ	5% to $250,000 2.5% to $500,000		Called bid incentives
Pismo Beach	CA	2%		
Redding	FL	5%		
Richmond	CA		Yes	Local hiring requirements: 20%+ for construction, 30%+ for other contracts
San Francisco	CA	10% bid price	Yes	To qualify, average sales should not exceed $14M for construction; $2.5 to $7M for other contracts
San Jose	CA	2.5% on purchase 5% on RFPs local +5% local and small		Small business with 35 employees
Seattle	WA	2%; local business 5%; women-owned 5%; minority-owned		
Sunnyvale	CA	1% on all bids		

Source: Summarized from numerous Web sources.

works projects. Reciprocal requirement is not popular among cities unless it is required by state law. Cities with blank space in the Reciprocity Required column of Exhibit 1 do not have a reciprocity requirement in their ordinances.

Counties that maintain local preference policies limit their preference to businesses that have business licenses with the county and are located within their county limits. One of the main differences between city and county preference policies is that a greater number of counties have reciprocal arrangements with other counties. Another difference is that the percentage preference counties give to local businesses is higher, at 5 to 10 percent, than it is for cities. Local preference policies in selected counties are summarized in Exhibit 2.

POLICY CONSIDERATIONS

To make the playing field equal for all businesses, while still pursuing savings in costs, cities and counties that do not currently have local preference policies might consider pursuing reciprocal arrangements with other jurisdictions. They could do so by inserting a clause in competitive bidding and purchasing contracts that requires reciprocity in local business preference policies. A reciprocity clause in contracts might have the following properties:

- If the bids submitted are identical, the local business with the lowest bid will be selected. This is because local businesses spend a greater amount in the local economy than businesses from other areas.
- If an outside business submits the lowest bid and the jurisdiction in which the outside business is located does not have local business preference policies, the contract will be awarded to the outside business with the lowest bid.
- If an outside business submits the lowest bid and the jurisdiction in which the outside business is located has local business preference policies, the bid amount by the outside business will be increased by the same percentage preference that jurisdiction gives to local businesses. If the outside business's bid amount remains lower than any bid submitted by a local business, the contract will still go to the outside business.

Exhibit 2: Local Preference Practices in Selected Counties

City	State	Preference	Public Works/Construction Included? Reciprocity?	Note
Alameda	CA	5% for local +5% for small	No	Small by SBA standards
Charlotte	FL	5% for local	Yes	Reciprocity among selected nearby counties
Collier	FL	10% for local	Yes	Reciprocity to Lee County
Lee	FL	Yes	Yes	Reciprocity to Collier County
Los Angeles	CA			Small business certified by the State of California
Manatee	FL	Selection of local if bids are identical	Yes	Reciprocity among Manatee, Desoto, Hardee, Hillsboro, Pinellas and Sarasota counties
Miami-Dade	FL	5% for local		Policy for the Miami-Dade Expressway Authority (MDX). Policy not applicable for emergency or sole procurements
Monroe	FL	2.5% for local +2.5% for 50%+ Local subcontract		
Multnomah	OR		Yes	Oregon requires reciprocal preference
Sacramento	CA	2% for small 3% for local 5% for local & small	Yes	Reciprocity applies to regional market area that reciprocates preference. Applies to $250,000 contract
Sarasota	FL	10% for local	Yes	Reciprocity among Sarasota, Manatee, Desoto or Charlotte counties
Suffolk	NY	10% for local	Yes	

Source: Summarized from numerous Web sources.

- If an outside business submits the lowest bid and the jurisdiction in which the outside business is located has local business preference policies, the bid amount by the outside business will be increased by the same percentage preference the other jurisdiction gives to local businesses. If the bid amount by the outside business becomes higher than one submitted by a local business, the local business will be given an opportunity to match the lowest bid made by the outside business. This matching opportunity process helps ensure the efficiency of the local business and cost savings for the local jurisdiction. If the local business can match the lowest bid made by the outside business, the contract will be awarded to the local business at the matched lowest bid. If the local business cannot match the lowest bid, the contract will be awarded to the outside business at the original, lowest bid.

Reciprocity requirements should apply only to those projects in which both local and outside businesses are equally qualified to do the work or local and outside products are of equal quality. The only difference between local and outside businesses should be the quoted cost or price. Further, the reciprocity requirement in contracts would apply to all future bids, contracts, and purchases made by public and private organizations and also to all future contracts and subcontracts of projects that are attracted with state and local incentive packages.

If contracts are awarded and purchases are made without a competitive process, city and county decision makers might also consider using local businesses or businesses that hire local workers, although this should not be required, as such a requirement goes beyond leveling the playing field level between local and outside businesses and might prompt retaliation against local businesses by outside jurisdictions.

CONCLUSIONS

Hiring outside businesses instead of equally qualified local businesses does create disadvantages. For instance, outside businesses may not pay business licenses on contracts that do not require permits, if the business license fee is based on gross revenues (as it is common among southern cities and counties). Also, the principals of outside businesses may not file non-resident state income tax returns, where non-resident income tax returns are required. Outside rental businesses may also have a cost advantage if the jurisdictions where they are located do not require tax on inventories of rental properties. In addition, local businesses have been shown to contribute more to local taxes and to local charities.[1] Local governments might decide that these considerations are more important than a simple comparison of costs.

Note

1. Semoon Chang, "RIMS II-Based Model of Estimating Economic Impacts: An Illustration Based on the Mobile, Alabama, Area Study," *Applied Research in Economic Development*, Vol. 3, No. 2, 2006.

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