

REPORT OF: City Comptroller's Office Purchasing Staff

TITLE: Information Requested by the Common Council Regarding a Local Preference Purchasing Policy for the City of Madison.

AUTHORS: Dean C. Brassler, City Comptroller
Patricia A. Brill, Accounting Services Manager
Randy A. Whitehead, Purchasing Supervisor

DATED: September 27, 2006

TO THE COMMON COUNCIL:

On August 1, 2006, the Common Council adopted Resolution 06-00701 (file No.03234) entitled "A study to determine the ability and efficacy of a local preference purchasing policy for the City of Madison." Specifically, the resolution requested Comptroller's staff to report on the following:

1. A suggested appropriate level of preference given in the bidding or Request for Proposal (RFP) process.
2. Possible policies to encourage local purchasing through Limited Purchase Orders (LPO's), Purchasing Cards or other purchase orders and any other method of purchasing items that do not require a RFP or bidding process.
3. Additional costs or cost savings that may be a result of a local purchasing policy.
4. Economic benefits to the City of Madison of a local purchasing policy.
5. Administrative challenges of a local purchasing policy.

The following report serves to respond to this request on behalf of the Comptroller's purchasing staff.

Current City Purchasing Methods and Administration

There are three primary methods by which city agency staff purchase commodities and services: 1) Purchase Order; 2) Limited Purchase Order; and 3) Purchasing Card. The method used for any given purchase is determined by the cost of the items or services to be purchased, the availability of established vendor contracts, and administrative efficiency. These current purchasing procedures and practices were designed to maximize competition to obtain the best price and value for high cost purchases and to allow for efficient procurement of low cost items with a minimum of administrative expense. None of these established purchasing methods currently include provisions for a local vendor purchasing preference.

Purchase Order

A Purchase Order is a contract for the purchase of goods or services, generally over \$5,000, which must be reviewed, approved and administered by designated Comptroller's Office purchasing staff. The Purchasing Supervisor has the authority to authorize and approve the purchase of commodities for any dollar amount and service contracts for up to \$25,000 and 1 year in duration. Pursuant to Madison General Ordinances Section 3.61(5) service contracts for an amount greater than \$25,000 or a term of more than 1 year must be authorized by a resolution of the Common Council and signed by the Mayor and City Clerk.

Reliance on open competition is a fundamental component of the City's procurement processes. It is common practice that City purchasing staff members, with participation by personnel from other agencies, form committees to establish product specifications and requirements for solicitations that exceed \$25,000. These specifications will include price along with other factors intended to ensure that the products and services purchased are the most cost effective available.

Formulated specifications and requirements are then distributed in the form of a Request for Quotation, Request for Bid, or Request for Proposal. These solicitation requests include the Purchasing Services Standard Terms and Conditions that contain the City’s legal requirements for contracting. The requirements include Living Wage, Prevailing Wage Rates, the Affirmative Action plan and other requirements. Responses are evaluated and scored based on the pre-established criteria, and a purchase order is awarded to the qualified bidder that obtains the highest score.

It is also common for the City of Madison to purchase products using established State of Wisconsin contracts when a product specification can be met and it is cost effective to do so. The State, in its own competitive procurement program, routinely awards bids that allow any municipality in the state to obtain the same pricing as state agencies. This service saves municipalities throughout the state, including Madison, valuable staff time, while taking advantage of the favorable pricing which results from the vast buying power of the State of Wisconsin. When State contract pricing is available for a product or commodity to be purchased by a City agency, the City can avoid the expense of a separate process and receive better pricing than would otherwise be available. In such cases, a purchase order is issued directly to the State contract supplier. State contract pricing has commonly been used to purchase computers, fuel products, furniture, office supplies and standardized vehicles such as police cars.

Many of the vendors under State contract are not located in the City of Madison. Implementing a local purchasing preference may limit the City’s ability to utilize these contracts, which will increase product costs and require substantial additional purchasing staff time for bidding.

Limited Purchase Order

The Limited Purchase Order (LPO) is another method by which city agency staff may purchase commodities and services for limited amounts, generally up to \$5,000, that were not previously contracted nor solicited. The LPO may also be used when a supplier will not accept the City’s purchasing card. It also serves as a release of payment form for public works, State, and/or joint municipal contracts. Currently there is no system in place to readily calculate the dollar value of purchases made from local vendors using the LPO method.

Purchasing Card

The purchasing card is used by approximately 320 city employees to purchase low dollar commodities and supplies. Using the purchasing card enables designated city agency staff to purchase efficiently and cost effectively when compared to the purchase order or LPO methods. Most purchasing cardholders have established single transaction limits set at \$1,000 or less. However, several City personnel have higher single transaction limits, up to \$5,000, to accommodate higher volume purchases such as vehicle work supplies and equipment acquired by Fleet Services. The City purchased approximately \$6 million worth of goods and services using purchasing cards in 2005. Approximately \$2.7 million of that was from vendors with a local address and \$3.3 million was non-local.

2005 Purchasing Statistics

The City of Madison’s 2005 non-payroll related expenditures are summarized in the following table:

<u>2005 Purchases by Vendor Address</u>				
	<u>Madison</u>	<u>Dane County</u>	<u>Other</u>	<u>Total</u>
Public Works Projects	\$22,000,000	\$ 6,000,000	\$ 4,000,000	\$ 32,000,000
Other Goods and Services	\$56,000,000	\$ 6,000,000	\$32,000,000	\$ 94,000,000
Total Non-Payroll Expenditures	\$78,000,000	\$12,000,000	\$36,000,000	\$126,000,000
	62%	10%	28%	100%

As shown here, a total of roughly \$32 million was spent in 2005 for public works projects. Of that amount, nearly \$22 million or 67% was paid to City of Madison contractors, and another \$6 million or 18% was paid to Dane County contractors. As a result, roughly 85% of public works contractors paid in 2005 were located within the City of Madison or within Dane County.

The City of Madison also purchased approximately \$94 million of non-payroll, non-public works goods and services during 2005. Of that amount, \$56 million or 60% was paid to vendors who have a City of Madison address. Another \$6 million or 6% was paid to vendors who have an address within Dane County.

Approximately \$32 million of all non-payroll purchases were from businesses with addresses outside Dane County. Many of these purchases are products where purchases were made using State contracts or for which no reasonably competitive local supplier is available. Some notable examples include:

<input type="checkbox"/> Gillig Corporation	\$4,200,000	Metro Transit buses
<input type="checkbox"/> Rehrig Pacific Company	\$2,200,000	recycling carts
<input type="checkbox"/> Frontier FS Cooperative	\$1,700,000	Fleet Services fuel
<input type="checkbox"/> Hartney Fuel	\$1,200,000	Metro Transit fuel
<input type="checkbox"/> Bruce Municipal Equipment	\$1,200,000	heavy equipment
<input type="checkbox"/> Pierce Manufacturing	\$1,100,000	Fire vehicles
<input type="checkbox"/> Siemens	\$1,000,000	Metro Transit computer systems
<input type="checkbox"/> RNow	\$ 844,000	recycling vehicles
<input type="checkbox"/> North American Salt Co.	\$ 514,000	road salt
<input type="checkbox"/> Dell Computers	\$ 494,000	network computers and equipment

It is important to note that Wisconsin Statutes Section 62.15(1) regulates the bidding for public works projects. It outlines that all public construction, the estimated cost of which exceeds \$25,000, shall be let by contract to the lowest bidder. Therefore, public works projects over \$25,000 may not be subject to a local purchasing preference policy.

Additionally, statutorily independent governing boards govern several City-related operations included in the purchasing figures presented here. These include the Madison Cultural Arts District (Overture Center), the Madison Library Board, and the CDA (Housing Operations). These entities are not legally required to adhere to City of Madison purchasing policies and procedures. However, City purchasing staff does encourage their participation, and many times these agencies will take part in City of Madison bid solicitations. Nearly \$24 million or 25% of non-public works purchases were contracted for by Overture, Library, and CDA/Housing.

Other Local Purchasing Preference Policies

Some municipalities such as Columbus, OH, Albuquerque, NM, and Lansing, MI have adopted local procurement policies and/or ordinances to assist with allocating purchasing dollars as a means to support local economic development. These policies vary by municipality. However, all of the above cities provide for a specified percentage preference to local vendors during a competitive bid process.

Columbus, OH gives a local bidder a 5% preference when compared to the lowest bid submitted by a non-local bidder if the government’s purchase is under \$10,000, and a 1% preference if the purchase is over \$10,000. The buy local preference credit is limited to \$10,000.

Albuquerque City Code provides a resident and local preference of 5% for purchases up to \$5,000,000 excluding bids for construction.

The City of Lansing's Ordinance provides that purchases greater than \$15,000 will allow a Lansing-based business within 5% of the low bid a chance to match the low bid and receive the contract. Construction contracts greater than \$500,000 are exempt from the Local Preference Ordinance.

Suggested Appropriate Level of Preference

Resolution 06-00701 resolves that: 1. The Comptroller's office staff provides a report regarding a suggested appropriate level of preference given in the bidding or Request for Proposal (RFP) process.

It is important to adopt a clear definition of what constitutes a local vendor. Determining the definition of a local vendor may be the most difficult yet important part of creating a local purchasing preference policy. Should "local" be defined as within the City limits of Madison, within the urban area, within the borders of the County or within the local economic region? And what constitutes a "local business?" Is it one with a local address, local ownership, local employment or local property? The following are some possible definitions to consider:

1. **The vendor's sales outlet or address must be located within the City of Madison.** This is a straightforward definition that would be the least difficult to monitor and to enforce. This was the base definition for virtually all of the local purchasing preference policies staff reviewed. A potential drawback to this definition, however, is that a national chain that has a store or branch in the City of Madison would be considered local, which may limit the intended impact of a local preference purchasing policy.
2. **The vendor's principal owner or shareholder resides within the City of Madison.** This definition might be useful as a second option when considering local vendors. One unintended impact of this definition is that a local resident may own a business that is not located in the area, employ no local residents, and still be considered local. This option is more difficult to verify or monitor as purchasing staff would need to rely on self-certification or would need additional staff to research residency and ownership in order to certify a vendor as local.
3. **A combination of business address, owner address, and percentage of local employees could also be used to define a local vendor.** This option would have the same difficulties in verification as the previous depending on the selected criteria, and would require additional staffing to certify and enforce.

After the definition of local vendor has been established, the following appropriate levels of preference could be considered (see the attachment following this report for detailed examples):

1. **Defined Percentage Method (without a limit)** - A specified percentage (1-5% found to be common) might be an allowable evaluating factor for local vendors. In competitive bidding situations where the low local bidder was within the specified percentage of the overall low bidder, the local bidder could receive an evaluating score or credit higher than that of the lowest non-local bidder. Given this method, the City would award the bid to a higher priced local bidder, (see attachment Example A).

A primary concern with this percentage method without limit is the additional costs that would result by providing a credit to local bidders, especially if there is no dollar cap placed on purchases. Many governmental units currently using a specified percentage without a limit have a local sales tax, where the additional spending in the local economy helps to recoup some or all of the additional expenses incurred by awarding to a higher priced local contractor.

2. **Defined Percentage Method (with a limit)** – This method incorporates the same principles as the Defined Percentage Method without limits reported above, also using a specified percentage of 1-5%. However, this second option also provides for a maximum dollar amount of local preference. For example, defined percentages are applied up to a maximum pre-established dollar preference limit (see attachment Example B).

Another variation of this method is to decrease the percent of preference given to the local bidder as the size of purchase increases. For example, the first \$25,000 of purchases bid would be given the same local preference as the no limit option above. For contracts greater than \$25,000, the percentage preference would be decreased by an established percentage (see attachment Example C). Incorporating limits for a local purchasing preference should reduce cost impacts to the City without significantly affecting a local preference policy.

3. **Defined Percentage Method to Match** – This method varies slightly from the other two methods described above in that the local vendor, given all other things equal, is granted an opportunity to match the low non-local bidder or proposer.

A defined percentage of (1-5%) is still provided for local preference. However, rather than awarding the bid to a local bidder at a higher price, the local vendor is allowed an opportunity to match the non-local low bid or proposal. In the other methods presented above, the local vendor was able to win the bid at a higher cost to the City, whereas this method provides a preference to the local bidder without additional costs incurred by the City (see attachment Example D).

It is noteworthy to mention that, during the typical bidding or RFP process, cost is only one of several evaluation criteria. All methods described above assume that all other evaluating criteria are equal. Receiving the maximum evaluation score for cost would not necessarily guarantee contract award if a local bidder preference policy applies.

Encouraging Local Purchasing with LPO's and P-Cards

Resolution 06-00701 also resolves that: 2. The Comptroller's office staff provides possible policies to encourage local purchasing through Limited Purchase Orders (LPOs), Purchasing Cards or other purchase orders and any other method of purchasing items that do not require a RFP or bidding process.

In lieu of or in conjunction with a formal adopted policy, the following procedures could be effectuated to encourage local purchasing for other purchases that do not require a RFP or bidding process:

1. Purchasing staff could prepare and incorporate local purchasing procedures within the general purchasing and purchasing card manuals, LPO instructions and the City's website. These policies would be disseminated during scheduled training sessions with other agency staff responsible for purchasing goods and services.
2. Department heads and supervisors could encourage, recommend, and approve local purchasing decisions made within their respective agencies when purchasing staff is not involved.

Additional Costs or Cost Savings

Resolution 06-00701 also resolves that: 3. The Comptroller's office staff report additional costs or costs savings that may be a result of a local purchasing policy.

Generally, a local preference purchasing policy will result in additional costs to the municipal government. To the extent that a higher price is paid for a commodity, the extra cost is borne by local taxpayers. And while the cost of adding a local preference to bid evaluation procedures would be insignificant, an effective program will also typically result in additional administrative costs to certify local vendor status. This additional cost may be modest if a simple "local address" definition is used, but a more sophisticated definition would require increased staffing to maintain a program to certify local vendors.

During 2005, approximately 62% of non-payroll related purchases were paid to vendors with a City of Madison address, with an additional 10% to Dane County vendors, without a local preference purchasing policy in place. At this time, it is impossible to determine the level of additional costs that would be incurred if a local preference policy were established. Additional direct costs would depend upon the definition of "local vendor" and which "defined percentage method" is adopted. Some of the methods described in this report could be costly if preference amounts or percentages are not limited as computed in the attached examples. Additional staff time would be needed to verify or register local vendors, to evaluate and score bid proposals, to prepare documentation to implement a local purchasing preference policy applied to competitive bid purchases.

In order to assist municipal purchasing staff, the Wisconsin Association of Public Purchasers is presently discussing a project that involves purchasing licensed software to assist with creating a bidding registry. Participating municipalities would share the costs of the proposed system. This may provide some future mechanism for purchasing staff to verify local vendors or principal owner addresses to assist in monitoring a local preference policy.

Economic Benefits to the City of Madison

Resolution 06-00701 also resolves that: 4. The Comptroller's office staff reports the economic benefits to the City of Madison of a local purchasing policy.

Our review has not identified a direct budgetary benefit for the City of Madison resulting from the implementation of such a policy. Several other municipalities giving preference to local vendors receive additional sales tax revenues, which helps to offset any additional spending increases. That is not the case in Wisconsin, however. Here, the related sales and income taxes flow primarily to the State and Federal governments, with some sales tax also returned to Dane County. There is no direct revenue that flows to the City as a result of local commodity sales. Thus, any local preference policy that results in higher administrative costs and prices paid for municipally purchased goods would likely have a net negative impact on local taxpayers.

It is clear that such a policy could provide some tangible benefit to the local economy and business owners. The redirection of municipal purchases to local vendors could result in increased sales and profits for the local businesses involved, and to the extent that these businesses purchase their products, in turn, from other local businesses and employ local residents, there is a stimulation of the local economy that would result. The magnitude of this local multiplier effect has not been determined.

Administrative Challenges

Resolution 06-00701 also resolves that: 5. The Comptroller's office staff reports the administrative challenges of a local purchasing policy.

To implement a new local purchasing preference policy, additional staff time would be needed to modify procedures, to prepare LPO and purchasing card instructions, to update website information and to properly train staff. Evaluation and bid award processing times may be lengthened depending on the complexity of the "local vendor" definition and "defined percentage method" adopted.

The most significant administrative challenge would be the certification and verification of "local" vendor status if a complex definition were adopted. There is no local vendor registry presently available, and additional staff time would be needed to develop and maintain this data. This may also require the purchase of software for the purpose of registering vendors and evaluating bid proposals.

Any local preference purchasing policy should address and carefully consider the City's ability to take advantage of State contracts when the selected vendor is not deemed local. Currently, State awarded competitive bid contracts are used on a regular basis in order to provide best value purchasing without any significant investment of City staff time. Any policy which eliminates our current ability to take advantage of this resource would result in a substantial increase in the workload of City purchasing staff and the need to increase staffing to complete the present volume of purchasing in a timely manner.

City purchasing staff estimates that it would take approximately six months to fully implement a local preference purchasing policy. During that time period, staff would revise the language contained in RFP and standard contract forms, design local vendor registration and evaluation forms, communicate the policy changes to the vendor community and City agency staff, modify LPO and purchasing card instructions and update all purchasing manuals and website information.

We hope that the information contained in this report is helpful in your decision making process. If you have additional requests for information or questions, we would be happy to assist in developing additional data as we work to provide cost effective purchasing assistance to City agencies, for the benefit of Madison's citizens and taxpayers.

ATTACHMENT:

Example A.

Option 1: Defined Percentage With No Limit – Potential Cost to City			
Size Of Contract	1% Preference	3% Preference	5% Preference
\$25,000	\$250	\$750	\$1,250
\$100,000	\$1,000	\$3,000	\$5,000
\$500,000	\$5,000	\$15,000	\$25,000
\$1,000,000	\$10,000	\$30,000	\$50,000
\$4,000,000	\$40,000	\$120,000	\$200,000

Example B.

Option 2: Defined Percentage With Limit – Potential Cost to City			
Size Of Contract	1% Preference	3% Preference	5% Preference
\$25,000	\$250	\$750	\$1,250
\$100,000	\$1,000	\$3,000	\$5,000
\$500,000	\$5,000	\$10,000	\$10,000
\$1,000,000	\$10,000	\$10,000	\$10,000
\$4,000,000	\$10,000	\$10,000	\$10,000

*Based on maximum preference of \$10,000

Example C.

Option 2: Defined Percentage With Limit – Potential Cost to City			
Size Of Contract	1% Preference	3% Preference	5% Preference
\$25,000	\$250	\$750	\$1250
\$100,000	\$1,000	\$1,500	\$2,000
\$500,000	\$5,000	\$5,500	\$6,000
\$1,000,000	\$10,000	\$10,500	\$11,000
\$4,000,000	\$40,000	\$40,500	\$41,000

*Based on 1-5% preference for first \$25,000, and 1% preference thereafter

Example D.

Option 3: Defined Percentage to Match – Potential Cost to City			
Size Of Contract	1% Preference	3% Preference	5% Preference
\$25,000	\$0	\$0	\$0
\$100,000	\$0	\$0	\$0
\$500,000	\$0	\$0	\$0
\$1,000,000	\$0	\$0	\$0
\$4,000,000	\$0	\$0	\$0