Local Purchasing Preferences

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Local governments spend a lot of money, and their procurement and contracting policies can be important mechanisms for advancing other public aims. Many cities, counties, and states give a preference to local businesses in their procurement decisions as a means of supporting and growing their local economies.

At least 45 states, plus the District of Columbia, have procurement policies designed to give a preference to businesses that meet certain characteristics, such as those that are owned by veterans, pay certain wages, use environmentally sustainable practices, or manufacture within the state. Of these, about half have adopted an explicit preference for businesses that are small and/or local. In addition, more than thirty states have policies aimed at steering purchasing to minority- and women-owned businesses.

Looking beyond state governments, large numbers of counties, cities, and towns have procurement policies of their own.

These policies vary considerably. Some apply broadly, while others focus on construction contracts, others on goods and services, and others only in certain narrow situations. Some are absolute preferences, or more commonly, percentage preferences. These say that if a company meets certain qualifications, it doesn't have to have the lowest bid in order to win a contract, just be within a certain percentage—usually 5 percent, but as high as 15 percent—of the lowest bid. (This useful chart compiled by Oklahoma, offers a flavor of the range of policies, but we note that it is incomplete and misses many preferences based on local or minority ownership.)

Many cities and states with procurement policies have established certification programs as a way to create a database of companies that qualify for a preference. A 2014 survey by the National Association of State Purchasing Officials found that, of respondents, 19 states have a certification program for small businesses, and 32 have a certification for minority-owned businesses.

Thirty-seven states have also enacted "reciprocal laws." These require public contracting agencies, in determining the lowest responsible bidder, to add a percent increase to each out-of-state bidder's bid price equal to the percent of preference given to local bidders in the bidder's home state. For instance, if the low bidder is from a state that grants a 10 percent preference to its own in-state bidders, the procurement agency must add 10 percent to that bidder's price when evaluating the bid.

Although procurement policies are prevalent, simply having a policy on the books is rarely very effective on its own. In the places where these policies are truly working as economic development, it's most often the result of more than just a new ordinance. Local procurement policies are most effective when they include firm definitions, well-developed goals, and clear tracking and reporting, and when they have buy-in across the local administration. For further examples of how different governments are tackling procurement, and what works, see the "Rules" section below, as well as our recent feature article, "Procurement Can Be a Powerful Tool for Local Economies, but Takes More Than a Policy Change to Work."

Economic Benefits

Giving preference to local suppliers, even if it means spending a little more, can actually benefit a city's finances. When local governments spend their money with locally owned firms, those firms in turn rely on and generate local supply chains, creating an "economic multiplier" effect. Each additional dollar that circulates locally boosts local economic activity, employment, and, ultimately, tax revenue. Numerous economic impact studies have quantified this effect. One of them, a 2009 study from

California State University at Sacramento, found that the State of California generated approximately $4.2 billion in additional economic activity and 26,000 new jobs between 2006 and 2007 by contracting with disabled veteran-owned businesses and local small businesses instead of larger companies.

Another study, from Civic Economics, looked at Arizona, and found that at a locally owned office supply company, 33.4 percent of revenue remained in the local economy, compared with just 11.6 percent at national company with a presence in the state. The study also looked at the potential impact of the City of Phoenix contracting with the local firm. It found that given a one-year, $5 million contract for office supplies, with the local company, an additional $1 million would stay in the area economy. With the national company, just $580,000 of that $5 million would recirculate locally.

In Britain, a county council found that vendors based within the county spent 76 percent of their county contracts locally, on wages paid to local employees and goods and services purchased from local businesses, while vendors based outside the county spent only 36 percent locally. The council, which has an annual procurement budget of £ 245 million, concluded that, if it shifted just 10 percent of its current spending with non-local suppliers to local suppliers, it would generate an additional £ 34 million (about $ 65 million) for the local economy. (This example and many other case studies can be found in the New Economic Foundation's guide, "Public Spending for Public Benefit: How the public sector can use its purchasing power to deliver local economic development").

Legal Challenges

While local procurement policies have occasionally faced legal challenges, courts have generally upheld them. This is especially true when the local government can show how the statutes will advance a legitimate local or state interest, such as expanding the local economy.

These legal challenges are often brought by out-of-state companies, which most frequently argue that the policy conflicts with one of four clauses in the U.S. Constitution: The Commerce Clause, the Privileges and Immunities Clause, the Equal Protection Clause, or the Due Process Clause.

One example is the case of Smith Setzer & Sons v. South Carolina Procurement Review Panel. Smith Setzer & Sons, a manufacturer of reinforced concrete pipes headquartered in North Carolina, was the lowest bidder on many South Carolina contracts, but lost them to South Carolina firms due to a 5 percent preference for in-state bidders. The company sued, but in a case that went up to the Fourth Circuit Court of Appeals, lost.

The Court concluded that states could discriminate in favor of local or in-state firms when the state is acting as a "market participant"—that is, when the state itself is the customer. In this case, the Court reviewed the statute and determined, "Rules stating a preference that such [tax] monies [generated from citizens of the state] be recycled within the local economy, either through the purchase of locally-produced products or through purchases from local vendors, rather than funneled out of state, reflect legitimate state concerns." In addition, it pointed to an econometric study done by the state, which showed that though South Carolina could save $50,000 by purchasing from Smith Setzer & Sons, the state would suffer an economic loss of $2.1 million if it did so.

For more information on legal challenges, two good resources are:

- "Buy Healthy, Buy Local: An Analysis of Potential Legal Challenges to State and Local Government Local Purchase Preferences," Amy S. Ackerman. The Urban Lawyer, Fall 2011.
- "Legal Challenges to In-State Contracting Preferences," Terrance Adams. OLR Research Report, Nov. 2012.

Trade Agreements

A bigger threat to local procurement policies may lie in international trade agreements. These agreements, and the rules of the World Trade Organization that oversees them, contain provisions that make local preferences vulnerable to challenges, and in some cases, even aim to explicitly undo them.

"One of the key provisions in almost all free trade agreements," explains Naomi Klein in her book This Changes Everything, "involves something called 'national treatment,' which requires governments to make no distinction between goods produced by local companies and goods produced by foreign firms outside their borders."

The case of the Green Energy Act in Ontario, Canada, is one example of the impact of such a provision. Seeking a policy that would strengthen both its renewable energy sector and its local economy, Ontario created a wind and solar program that also required a percentage of the labor and materials of new projects to be based in Ontario.

The program worked: Ontario became the largest solar producer in Canada, and by 2014, had more than 31,000 new clean energy jobs. Then, however, Japan and the EU complained to the WTO that the program's domestic content requirement violated the General Agreement on Tariffs and Trade (GATT). Ontario lost an appeal, and fearing retaliation, pulled the buy-local provisions from its program.

On top of these existing threats, two new major trade agreements, the Trans-Pacific Partnership (TPP) and the Transatlantic Trade and Investment Partnership (TTIP), are looming, and provisions in them directly target local procurement programs. As a report from the Institute for Agriculture and Trade Policy found, "The European Union has made the opening of U.S. procurement programs to bids by European firms one of its priority goals for the TTIP... the EU has been insistent on the inclusion of procurement commitments at all levels of government, for all goods, and in all sectors."

In undermining local procurement programs, provisions like these also remove a community's agency and decision-making power from the people who live in it.

For more information on how trade agreements threaten local procurement policies:

- "Local Economies on the Table," Karen Hansen-Kuhn. The Institute for Agriculture and Trade Policy, Nov. 13, 2014.

Additional Resources

- "Procurement Can Be a Powerful Tool for Local Economies, but Takes More Than a Policy Change to Work." (Aug. 26, 2015)
- Non-profit groups, educational institutions, hospitals, faith organizations, and others can also adopt local purchasing preferences. Here's an example from the Evangelical Lutheran Church of America.
- "Local Food for Local Government: Considerations in Giving Preference to Locally Grown Food." Public Health Law and Policy, 2012.
- "Buying Local: Tools for Forward-Thinking Institutions," Anthony Pringle. Columbia Institute, LOCO BC, and ISIS Research Center at the Sauder School of Business, Dec. 2013.

Rules

Local Purchasing Preference — Phoenix

Phoenix is an example of a city that opted to start small. Rather than adopting a change in procurment policy, in 2012, the City of Phoenix altered its process for informal procurements—smaller contracts—instead. The city rolled out its Local Small Business Enterprise Program, which created a database to register small and local businesses. Further, the city said that LSBEs would get the first opportunity to submit quotes for all purchases of goods and services under $50,000. CONTINUE READING →

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Local Purchasing Preference — San Diego

Under the City of San Diego's Small Local Business Enterprise Program, public works contracts valued at $1 million and above include a mandatory subcontractor participation requirement for certified SLBEs, contracts valued between $500,000 and $1 million have a 5 percent bid discount for SLBEs, and contracts valued between $250,000 and $500,000 are only open to certified SLBEs. Other forms of contracts, such as those for goods and services, contain similar elements. CONTINUE READING →

Local Purchasing Preference – Madison, WI

On purchases over $5,000, the city of Madison, Wisconsin, grants local businesses a 1% price preference on bids and a 5% point preference on RFPs (request for proposal). CONTINUE READING →

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Local Purchasing Preference – Los Angeles

On contracts of $100,000 or less, the city of Los Angeles grants a 10% preference to small, local businesses. A small, local business is defined as one that is independently owned and operated, located in the county of Los Angeles, and not "dominant in its field of operations." Los Angeles County also grants small, local businesses a 5% preference on county contracts. CONTINUE READING →

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Local Purchasing Preference – Indiana

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Local Purchasing Preference — Montgomery County, Md.

In Montgomery County, Md., the Local Small Business Reserve Program designates certain solicitations only for LSBRP bidders, and aims to direct 20 percent of county contracts under $10 million to those firms. Under the program, "local" is defined as businesses that are either located only in the county, or businesses with locations both inside and outside of the county, but for which the county-based location accounts for over 50 percent of the total number of employees or over 50 percent of gross sales. The county has registered more than 1,220 local small businesses in its vendor system, and in 2012, it spent $83.7 million with LSBRP-certified businesses, or 16.7 percent of its total contract dollars.
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Local Purchasing Preference — Cleveland

Cleveland has a variety of local procurement programs designed to drive contracting and purchasing to locally owned businesses. As a result of these developed policies, in 2014, the city spent 39 percent of its total $147 million in contracting with businesses that are either local and small, or local and minority- or female-owned. CONTINUE READING →

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Local Purchasing Preference — California

California state law grants local, independently owned, small businesses a 5 percent preference when competing for state contracts. The law also sets for state agencies a goal of making at least 25 percent of their purchases with small businesses.
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Indiana grants a 15% preference to small, independent businesses, as defined below, and gives all other local businesses a preference of 1-5%, depending on the size of the contract.
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Local Purchasing Preference – Western Australia

Note: In 2008, the Australia-United States Free Trade Agreement (AUSFTA) caused the Government of Western Australia to substantially amend its Buy Local Policy to eliminate the preference for regionally produced goods over U.S. exports.
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