

CITY AND COUNTY OF SAN FRANCISCO
BOARD OF SUPERVISORS
BUDGET AND LEGISLATIVE ANALYST

1390 Market Street, Suite 1150, San Francisco, CA 94102 (415) 552-9292
FAX (415) 252-0461

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TO: Government Audit and Oversight Committee
FROM: Budget and Legislative Analyst 
SUBJECT: November 13, 2014 Government Audit and Oversight Committee Meeting

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Item: 3
File: 14-0999

Departments:
 City Administrator, Contract Monitoring Division
 Human Rights Commission

EXECUTIVE SUMMARY

Legislative Objectives

- Ordinance to amend the City's Administrative Code to change the Local Business Enterprise (LBE) and Non-Discrimination in Contracting Ordinance to (1) codify the transfer of implementation and enforcement of Chapter 14B from the Human Rights Commission to the City Administrator and Contract Monitoring Division; (2) require the Mayor to annually set an aspirational City-wide LBE participation goal of not less than 40% of the value of upcoming contracts; (3) increase the LBE certification size thresholds for small and micro LBEs; (4) increase the bid discount allowed to SBA-LBEs on contracts between \$10,000 and \$10,000,000; (5) require Administrative Code, Chapter 56 development agreements to include a LBE utilization plan and be subject to certain Chapter 14B provisions; (6) authorize preparation of an implementation plan for, and feasibility study of a LBE contractor advance program to fund loans to subcontractors; (7) increase the Surety Bond Program limit from \$750,000 to \$1,000,000; (8) require the City to make good faith efforts to obtain at least three bids from LBEs for contracts under the threshold or minimum competitive amounts; (9) allow implementation of a Mentor-Protégé Program to foster partnerships between established successful contractors and LBEs; (10) require separate LBE participation requirements on design and construction portions of design-build construction contracts; (11) repeal Ordinance No. 97-10 relating to completion of the Bayview Branch Library Construction Project; and (12) make various other changes in Chapter 14B.

Fiscal Impact

- Increasing thresholds for micro and small LBE firms and eliminating barriers to bidding on City work will assist in increasing the pool of City-certified LBEs. If more firms are certified as LBEs, there should be more competition to secure City work, potentially reducing bid costs. However, more LBE certified firms could qualify for bid discounts or preferences, potentially increasing the cost to the City by an undetermined amount.
- The Contract Monitoring Division is currently reviewing the amount of staff and resources needed to implement the proposed revisions, but may require up to 4-5 additional Contract Compliance Officers, a total annual cost including fringe benefits of approximately \$600,000. These positions would be supported with both General Fund and non-General Fund monies. All additional funding requests would be subject to Board of Supervisors appropriation approval.
- In addition, increasing the guaranty surety bond limits from \$750,000 to \$1,000,000 will potentially increase the required budget allocations from all participating departments, and/or decrease the number of guarantees available to LBE contractors, although the specific cost increases have not been determined.

Policy Consideration

- On July 28, 2014, the Controller's Office of Economic Analysis submitted a Local Business Enterprise Threshold Analysis to the City Administrator which found that the Consumer Price Index (CPI) is the best measure to use to revise LBE thresholds. Given that thresholds had not been recalculated since the inception of the ordinance in 2006, a CPI adjustment would reflect a 17.1% increase. On October 23, 2014, the Local Business Enterprise Advisory Committee (LBEAC) recommended that the LBE criteria thresholds be increased by 17.1% across all industry categories and these thresholds be reviewed every three years, for cost of living increases. In contrast, the proposed amendments would increase the thresholds by 43% for some but not all industries for the micro and small firms to be certified as LBEs, with no increases for SBA-LBEs and does not provide for future increases in these thresholds.

Recommendations

1. Based on the Risk Manager's recommendation regarding the City's Surety Bond Program, amend the proposed ordinance on page 62, lines 5 and 10 to delete \$1,000,000 and replace with \$750,000, which is the current threshold.
2. Amend the proposed ordinance on page 64, line 14 to also require the City Administrator to submit the implementation plan, including feasibility study on the LBE advance payment program to the Board of Supervisors by June 1, 2015.
3. Amend the proposed ordinance on pages 16 and 17 to (a) increase by 17.1%, each of the existing micro, small and SBA firms gross annual receipts criteria to be eligible for LBE certification as summarized in Table 4 below and (b) require these thresholds be automatically reviewed every three years by the Controller's Office for cost of living adjustments.
4. Approve the proposed ordinance, as amended.

MANDATE STATEMENT

Charter Section 2.105 authorizes all legislative acts by written ordinance or resolution, subject to majority vote of the members of the Board of Supervisors.

BACKGROUND

Chapter 14B of the City's Administrative Code, entitled the Local Business Enterprise and Non-Discrimination in Contracting Ordinance, specifies the City's local business contracting preference and non-discrimination programs. In accordance with Chapter 14B, because San Francisco's small businesses generally experience proportionately higher costs than larger businesses or businesses located outside the City, these small local businesses are at a competitive disadvantage to compete for public contracts. Therefore, Chapter 14B programs are designed to assist qualified local small businesses in competing for the award of City contracts by (a) adding points to proposals for contracts that are awarded based on the highest score, or (b) applying discounts to proposals for contracts that are awarded based on the lowest costs. In addition, Chapter 14B provides contracting set asides, subcontracting goals, City payment provisions, and training programs to assist small local businesses to compete for City contracts.

DETAILS OF PROPOSED LEGISLATION

The proposed ordinance would amend Chapter 14B of the City's Administrative Code to comprehensively change the existing Local Business Enterprise (LBE) and Non-Discrimination in Contracting Ordinance to:

- (1) Codify the transfer of implementation and enforcement of Chapter 14B from the Human Rights Commission to the City Administrator and Contract Monitoring Division;
- (2) Require the Mayor to annually set an aspirational City-wide LBE participation goal of not less than 40% of the value of upcoming contracts;
- (3) Increase the LBE certification size thresholds for small and micro LBEs;
- (4) Increase the bid discount or bonus allowed to Federal Small Business Administration (SBA) LBE economic thresholds on contracts between \$10,000 and \$10,000,000;
- (5) Require Administrative Code, Chapter 56 development agreements to include a LBE utilization plan and be subject to certain Chapter 14B provisions;

(6) Authorize preparation of an implementation plan for and feasibility study of a LBE contractor advance program to fund loans to subcontractors;

(7) Increase the Surety Bond Program limit from \$750,000 to \$1,000,000;

(8) Require the City to make good faith efforts to obtain at least three bids from LBEs for contracts under the threshold or minimum competitive amounts;

(9) Allow for the implementation of a Mentor-Protégé Program to foster partnerships between established successful contractors and LBEs;

(10) Require separate LBE participation requirements on design and construction portions of design-build construction contracts;

(11) Repeal Ordinance No. 97-10 relating to completion of the Bayview Branch Library Construction Project; and

(12) Make various other changes in Chapter 14B.

(1) Transfer from Human Rights Commission to City Administrator

Currently Chapter 14B specifies that the Human Rights Commission is responsible for implementation and enforcement of Chapter 14B. However, on July 12, 2012, the Mayor transferred the duties and functions of the Human Rights Commission to the City Administrator. The proposed ordinance would amend Chapter 14B to be consistent with current practices to require the City's contract procedures be under the City Administrator.

The proposed amendments would also allow the City Administrator to adopt future rules, regulations, guidelines and other actions necessary to implement and enforce the provisions under Chapter 14B. However, under the proposed amendments, the Director of the Human Rights Commission would still be responsible for Section 14B.9(D) and 17(E) to investigate and issue findings regarding possible unlawful discrimination by a bidder or City contractor in selecting subcontractors for City contracts.

(2) Mayor annually sets aspirational City-wide LBE participation goal of at least 40%

Chapter 14B currently requires the Mayor to notify City departments of the City-wide LBE goals by July 1st of each year. However, such City-wide annual LBE goals have not been established for approximately the past ten years. As a City-wide LBE goal, there is no enforcement of this provision. Instead, each City department contract currently specifies LBE percentage participation based on the availability of certified LBEs in the City's database for each industry as related to each contract. Ms. Maria Cordero, Executive Director of the Contract Monitoring

Division in the Office of the City Administrator, estimates that approximately 25-35% of the City’s subject contracts are currently awarded to eligible LBEs.

Under the proposed amendments, each year the Mayor would set and report to the Board of Supervisors a City-wide LBE participation aspirational goal as a percentage of the overall dollar value of contracts to be awarded in the upcoming fiscal year, based on prior fiscal year LBE utilization data and current LBE availability, but not less than 40%.

(3) Increase the LBE certification size thresholds for micro and small LBEs

Currently, LBE businesses are certified by the City based on gross annual receipts that are less than specified limits which differ by industry based on the average gross receipts of that firm over the past three years. Table 1 below summarizes the current maximum annual earnings for individual types of micro, small and SBA eligible LBE firms.

Table 1: Current Annual Thresholds for Micro, Small and SBA Firms to be Eligible for Certification Based on Gross Annual Receipts over 3 Years

Industries	Micro	Small	SBA
General Contractors/Construction	\$7,000,000	\$14,000,000	\$33,500,000
Specialty Construction Contractors	3,500,000	7,000,000	17,000,000
Goods/Equipment & General Services	3,500,000	7,000,000	17,000,000
Professional Services incl Arch/Engineer	1,250,000	2,500,000	7,000,000
Trucking and Hauling	1,750,000	3,500,000	8,500,000

According to the Controller’s Office, these annual thresholds for certifying eligible LBE firms have not changed since 2006, despite increasing costs. The proposed amendments would change the annual maximum gross annual receipts criteria for certifying micro LBE firms as shown in Table 2 below.

Table 2: Proposed Annual Thresholds in Prior 3 Fiscal Years for Micro LBE Certification

Maximum Gross Annual Receipts	Current	Proposed	Increase (\$/%)
General Contractors/Construction	\$7,000,000	\$10,000,000	\$3,000,000/43%
Specialty Construction Contractors	3,500,000	5,000,000	1,500,000/43%
Goods/Equipment & General Services	3,500,000	3,500,000	0
Professional Services incl Arch/Engineer	1,250,000	1,250,000	0
Trucking and Hauling	1,750,000	1,750,000	0

The proposed amendments would also change the maximum annual gross receipts criteria for certifying small LBE firms as shown in Table 3 below.

Table 3: Proposed Annual Thresholds in Prior 3 Fiscal Years for Small LBE Certification

Maximum Gross Annual Receipts	Current	Proposed	Increase (\$/%)
General Contractors/Construction	\$14,000,000	\$20,000,000	\$6,000,000/43%
Specialty Construction Contractors	7,000,000	10,000,000	3,000,000/43%
Goods/Equipment & General Services	7,000,000	10,000,000	3,000,000/43%
Professional Services incl Arch/Engineer	2,500,000	2,500,000	0
Trucking and Hauling	3,500,000	3,500,000	0

The maximum annual gross receipts criteria for certifying SBA LBEs would not change under the proposed amendments.

According to the office of the sponsor of the proposed ordinance, the proposed 43% increases for some of the industries were based on stakeholder input.

(4) Increase bid discount for SBA LBEs on contracts between \$10,000 and \$10,000,000

Currently, for contracts between \$10,000 and \$10,000,000, the bid discount is 10% for Small or Micro LBEs and 2% for SBA LBEs. Under the proposed amendments, the bid discount would remain the same at 10% for Small or Micro LBEs, but would increase from 2% to 5% for SBA LBE contracts of between \$10,000 and \$10,000,000, as long as no Micro LBE or Small LBE is

adversely impacted. For contracts between \$10,000,000 and \$20,000,000, the bid discounts for Small, Micro or SBA LBEs would remain the same at 2%.

(5) Require development agreements to include LBE utilization plan and compliance

The proposed ordinance would add a new provision to Chapter 14B to require development agreements entered into pursuant to Chapter 56 of the City's Administrative Code¹ to include a detailed LBE utilization plan that requires the setting of a LBE utilization requirement in conformance with the City-wide LBE participation goal, compliance with good faith outreach requirements and nondiscrimination provisions and includes reporting, monitoring and enforcement provisions. To date, the City has entered into four development agreements under Chapter 56, including (a) Park Merced, (b) Trinity Plaza, (c) California Pacific Medical Center (CPMC), and (d) Pier 70.

(6) Implementation of a contractor advance payment program to fund loans to subcontractors

Under the proposed ordinance, the City Administrator, in consultation with the Controller, would submit an implementation plan, including a feasibility study to the Mayor by June 1, 2015 to develop a LBE advance payment program to fund temporary loans to LBE subcontractors for approved invoices on City-funded contracts. Ms. Cordero advises that currently, no City-sponsored loan program exists to assist LBE subcontractors, such that these LBE subcontractors often have to rely on private bank's lines of credit to fund their operations and pay their employees, although the LBE subcontractors may have completed their specific work on a City-funded contract. Given that the Board of Supervisors has a significant interest in the proposed LBE contractor program, the City Administrator should also submit the implementation plan, including feasibility study to the Board of Supervisors by June 1, 2015.

(7) Increase the Surety Bond Program limit from \$750,000 to \$1,000,000

With respect to the City's Surety Bond Program, the proposed ordinance would increase the limit to which the City may guaranty agreements from up to \$750,000 to up to \$1,000,000. According to Mr. Matt Hansen, the City's Risk Manager, the City's Surety Bond Program provides technical assistance and underwriting of bid and performance bonds for construction contractors. The Program is currently funded by contributions from the major City departments that undertake construction contracts, including the Public Utilities Commission, Department of Public Works, Port, Airport and Recreation and Park.

¹ Chapter 56 of the City's Administrative Code addresses public planning of private development projects in the City to enhance public benefits beyond those achievable through existing ordinances and regulations by entering into voluntary development agreements between the developer and the City.

Mr. Hansen reports that the current Program limit of \$750,000 has sufficient capacity to support all requests to date and is not expected to be a barrier to LBE contractor's receiving Surety Bond Program assistance in the future. In fact, Mr. Hansen advises that the Program should not be increased at this time because such an increase will impact the previously conducted actuarial analysis, potentially increasing budget contributions from all participating departments, and/or decreasing the number of guarantees available to LBE contractors. Therefore, Mr. Hansen recommends that the Surety Bond Program not be increased to \$1,000,000 at this time.

(8) Make good faith efforts to obtain at least three bids from LBEs for contracts under threshold

The proposed amendments would add a new San Francisco First Program which would require City departments to make good faith efforts for contracts greater than \$10,000 to obtain at least three LBE bids for all public works contracts under the threshold amount (\$400,000) or for professional or general services or commodities contracts under the minimum competitive amount (\$100,000). If three bids from LBEs are not obtained, City departments must document a finding explaining why three bids were not obtained.

(9) Establish a Mentor-Protégé Program between established successful contractors and LBEs

In accordance with the proposed ordinance, the Director of the Contract Monitoring Division would establish a Mentor-Protégé Program to foster partnerships between established, successful contractors and LBEs to provide training, networking and mentoring opportunities with the goal to improve LBE participants' ability to compete effectively for City contracts and allowing mentor contractors' exemption of the good faith outreach requirements. Ms. Cordero advises that this City Mentor-Protégé Program would be modeled on the existing Caltrans mentor-protégé program, and could begin in early 2015.

(10) Require separate LBE participation on design-build contracts

The proposed ordinance specifies that the Director of the Contract Monitoring Division shall establish separate LBE participation requirements on design and construction portions of work for Design-Build construction contracts with the City.

(11) Repeal provisions relating to completion of Bayview Branch Library Construction Project

The proposed ordinance would specifically repeal Ordinance No. 97-10 which granted bid discounts to joint venture partnerships with LBE firms to facilitate the completion of the Bayview Branch Library Construction Project, which was completed in early 2013.

(12) Make various other changes in Chapter 14B

Numerous other changes are incorporated in the proposed ordinance to correct and clarify existing and proposed provisions in Chapter 14B, including (a) exempting agreements awarded under emergency conditions, (b) deleting provisions concerning San Francisco Payroll Taxes as a criteria to establish a principal place of business, (c) adding definitions, (d) allowing joint venture partners to be in different industries if such partners are also acting as the prime contractor, (e) provide the Director of the Contract Monitoring Division with discretion to certify or renew a certification of a business for a shorter period of time based on unique attributes of individual businesses, (f) allow Director of Contract Monitoring Division to suspend or revoke LBE certification that fails to submit requested documents or cooperate in any investigation regarding continued eligibility, (g) increase contractors requirement to maintain all records for monitoring compliance by two years from three to five years, (h) replace the Mayor with the City Administrator as the designated official to resolve LBE contracting issues, and (i) require the Director of Contract Monitoring Division to make a finding justifying the LBE subcontracting requirement if set at less than 20%.

The proposed ordinance would apply to all eligible contracts advertised for bid or initiated on or after July 1, 2015.

FISCAL IMPACT

The proposed ordinance states that stimulating the expansion of small firms or development of new enterprises fosters economic growth and independence for San Francisco and its taxpayers. This expansion of local small businesses advances the public interest, contributes to the economic well-being of all San Franciscans and tends to minimize the burden on the General Fund to provide for general welfare.

In addition, one of the major goals of the proposed ordinance is to increase the pool of City-certified LBEs in order to increase the number of qualified LBE prime contractors and subcontractors who will be eligible to bid on City contract work. Increasing the thresholds for micro and small LBE firms and eliminating some of the barriers to bidding on City work, as proposed in this ordinance, will assist in potentially increasing the pool of City-certified LBEs. If more firms are certified as LBEs, there should be more competition to secure City work, potentially reducing the bid costs to secure that work. However, as more firms are certified as LBEs, more firms could likely qualify for specified bid discounts or preferences, ultimately increasing the cost to the City by an undetermined amount.

The Contract Monitoring Division under the City Administrator would be responsible for implementing and enforcing the provisions of Chapter 14B. Ms. Jennifer Johnston, Deputy City Administrator, estimates that the proposed amendments will require additional contract

compliance and monitoring staff to (a) handle greater workloads as more firms are LBE eligible, (b) develop the new Mentor Protégé Program, (c) conduct a feasibility study to develop a LBE advance payment for temporary loans to LBE subcontractors, (d) establish separate LBE participation requirements for Design-Build construction contracts, and (e) address the numerous changes. Ms. Johnston advises that the Contract Monitoring Division is currently reviewing the amount of staff and resources that may be needed to implement the proposed revisions, but may require up to 4-5 additional Contract Compliance Officers, which currently have annual salaries of \$98,488, or a total annual cost including fringe benefits of approximately \$600,000. These positions would need to be supported with both General Fund and non-General Fund monies. All additional funding requests would be subject to Board of Supervisors appropriation approval.

In addition, Mr. Hansen estimates that the increase from \$750,000 to \$1,000,000 in the limit to which the City may guaranty surety bond agreements will potentially increase the required budget allocations from all participating departments, and/or decrease the number of guarantees available to LBE contractors, although the specific cost increases have not been determined.

POLICY CONSIDERATION

One notable policy question for consideration is the amount of the increase in the LBE thresholds as shown above in Tables 1, 2 and 3.

On July 28, 2014, the Controller's Office of Economic Analysis staff submitted a Local Business Enterprise Threshold Analysis to the City Administrator. This analysis found that the Consumer Price Index (CPI) is the best measure to use to revise LBE thresholds, as the CPI reflects all determinants subject to inflationary and market pressures, including inflation, cost of living and price. Based on the Controller's analysis that thresholds had not been recalculated since the inception of the ordinance in 2006, a CPI adjustment would reflect a 17.1% increase.

In addition, on October 23, 2014, the Local Business Enterprise Advisory Committee (LBEAC)² recommended that the LBE criteria thresholds be increased by 17.1% as recommended by the Controller's Office, across all industry categories. In addition, the LBEAC recommended that these thresholds be reviewed by the Controller every three years, for cost of living increases. In contrast, as shown in Tables 2 and 3 above, the proposed amendments would increase the thresholds by 43% for some but not all industries for the micro and small firms to be certified as LBEs, with no increases for SBA-LBEs. The proposed ordinance also does not provide for future increases in these thresholds.

² The Local Business Enterprise Advisory Committee is comprised of 14 members, appointed by the Mayor, representing small, micro and large businesses, community based organizations and enterprise department contract management staff..

Based on the Controller’s analysis and the recommendations of the LBEAC, the proposed ordinance should be amended to increase the annual thresholds for each of the micro, small and SBA firms that are eligible for LBE certification by 17.1%, as summarized in Table 4 below. Similarly, amend the proposed ordinance to require that these thresholds be reviewed by the Controller every three years for cost of living adjustments.

Table 4: Recommended 17.1% Threshold Increases Based on Controller and LBEAC Recommendations

Industries	Micro	Small	SBA
	Proposed	Proposed	Proposed
General Contractors/Construction	\$8,200,000	\$16,400,000	\$39,000,000
Specialty Construction Contractors	4,100,000	8,200,000	20,000,000
Goods/Equipment & General Services	4,100,000	8,200,000	20,000,000
Professional Services incl Arch/Engineer	1,500,000	3,000,000	8,000,000
Trucking and Hauling	2,000,000	4,000,000	10,000,000

RECOMMENDATIONS

1. Based on the Risk Manager’s recommendation regarding the City’s Surety Bond Program, amend the proposed ordinance on page 62, lines 5 and 10 to delete \$1,000,000 and replace with \$750,000, which is the current threshold limit.
2. Amend the proposed ordinance on page 64, line 14 to also require the City Administrator to submit the implementation plan, including feasibility study on the LBE advance payment program to the Board of Supervisors by June 1, 2015.
3. Amend the proposed ordinance on pages 16 and 17 to (a) increase by 17.1% the annual thresholds for each of the existing micro, small and SBA firms gross annual receipts criteria to be eligible for LBE certification as summarized in Table 4 above and (b) require that these thresholds be automatically reviewed every three years by the Controller’s Office for cost of living adjustments.
4. Approve the proposed ordinance, as amended.