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CITY COUNCIL MEETING

July 7, 1982

As previously requested, information relating to local bidder preference was presented to Council for its perusal by City Attorney Stein. No action was taken by the Council on the matter.

K-10.

MEMORANDUM

To: Honorable Mayor and Council Members
From: Ron Stein, City Attorney
Re: Local Bidder Preference
Date: June 21, 1982

Attached hereto, please find the material that I received from the City of Sacramento regarding the calculation of the 1% sales tax returned to a City in determining who is the lowest responsible bidder.

Your comments will be appreciated.


RONALD M. STEIN
CITY ATTORNEY

RMS:vc

attachments

cc: Assistant City Manager
City Clerk ✓
Finance Director



CITY OF SACRAMENTO

DEPARTMENT OF LAW
812 TENTH STREET SACRAMENTO CA 95814
SUITE 201 TELEPHONE (916) 449-5346

June 17, 1982

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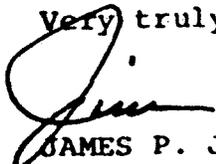
Mr. Ronald M. Stein
City Attorney
P. O. Box 320
Lodi, CA 95241

Dear Ron:

I enclose a copy of Lee Savage's opinion, with attachments, relating to local bidder preference. I thought that we had developed a written provision for consideration of the local sales tax in our bid specifications. However, I am in error on this, and we do not specifically include such a provision. We do follow the policy of taking the local sales tax into account. As we discussed, the facts only rarely permit a local bidder to take advantage of this policy.

I hope this material is of some help.

Very truly yours,


JAMES P. JACKSON
City Attorney

JPJ/p

Enclosures

JUN 21 1982



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March 25, 1977

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Lloyd Connelly, Councilman
City of Sacramento
Sacramento, California

In re: Your Inquiry of Whether the City Can
Give Local Bidders Preference

Dear Lloyd:

My research revealed no case exactly on point in regard to your inquiry with respect to whether the City could give a local bidder a fixed percentage preference over non-local bidders. However, the point was the subject of a paper written in 1963 by Allen Grimes, then City Attorney of Modesto, for the League of California Cities. I have attached the pertinent pages of the paper for your information.

Since the Grimes' paper was written, the California Buy American Act (former Government Code § 4300-4305) was ruled unconstitutional in Bethlehem Steel Corp. v. Bd. of Commissioners (1969) 276 Cal.App.2d 221. The Attorney General subsequently issued an opinion stating that the reasoning of the court in Bethlehem Steel applied to the California Preference Law (former Government Code § 4300-4334); therefore, the California Preference Law was unconstitutional (53 Ops Atty Gen 72, February 11, 1970). Each of these was a law purporting to give preference to products from "preferred" areas. The reasoning may be applicable to preference to suppliers from "preferred" areas, such as within the City limits.

It would appear that while there is no case directly on point, a local preference such as that suggested in your inquiry would be subject to attack on several legal grounds. However, there is a possible advantage which may be gained by local bidders by virtue of the fact that it may be legal for the City to take into account the fact that the City receives a one percent rebate on sales tax paid by it on supplies purchased within the City of Sacramento. By coincidence, this was the subject of an opinion which we were in the process of preparing at the time we received your inquiry. A copy of the opinion is attached.

Very truly yours,

LELIAND J. SAVAGE
Deputy City Attorney

LJS:kn
Cc: Jack Crist
Attachments

all subcontractors performing work in excess of 1/2 of one percent of the general contractor's bid on public works or improvements. Penalties are cancellation of contract or assessing the general contractor with a penalty in an amount not more than 10% of the amount of the subcontract involved or both cancelling the contract and assessing the penalty."

4. Legality of Providing a Local Preference.

- a. The legal question is whether a statutory charter or ordinance provision authorizing requiring the granting of a local preference is valid and constitutional?

(1) The first case I'm able to find dealing with this subject is that of People v. Coler, 166 N. Y. 144, 59 N. E. 776, aff'd 68 N. Y. Supp. 767.

Here the Court stated that,

"Preference...within a state has been held to violate... the United States Constitution."

The preference held to be invalid was a state law incorporated in a local public works contract requiring stone used for construction purposes to be dressed or worked in the State of New York. Contractor used stone not so dressed in performing a public works contract with the city. In an action of mandamus he was held entitled to receive payment for full performance of the contract notwithstanding.

- b. In the case of Schrey v. Allison Steel Manufacturing Co. (Arizona) 255 P(2d) 604, an Arizona state statute provided in letting bids for public works contracts, bidders who paid state and county taxes within the State of Arizona for two successive years immediately prior to the making of the bid shall be given preference over bidders who have not paid such taxes whenever the bid of the competing contractor is less than 5% lower than the taxpaying bidder.

The Court found the legislation valid and constitutional notwithstanding

the contentions that it was in violation of the equal protection privilege and immunities clauses of the U. S. Constitution, that the classification was unreasonable, and that it amounted to a gift to public funds.

- c. I'm informed (but have been unable to substantiate) that the law department of the City of Chicago rendered an opinion in 1948 that a State of Illinois statute making a 10% differential in favor of coal mines, in that state was unconstitutional.
- d. I'm advised that City Attorney Grady Rawls of the City of Albany, Georgia, rendered a legal opinion that a local preference law was invalid, stating,

"Law on competitive bidding is to assure that the City receives the highest quality at the lowest price. In my opinion if the commodity is available locally and is acceptable quality and at a fair price, it should be acquired locally. The converse is true. That is to say, if for any reason there are not enough local suppliers of a product to insure genuine competitive bidding, then the Purchasing Department should afford outside suppliers an opportunity along with the local suppliers."

- e. The latest and most interesting ruling on this subject is an opinion rendered by Mr. Harold W. Kennedy, County Counsel of the County of Los Angeles, dated March 18, 1963. The question presented to him by the County Purchasing Agent was that an ordinance had been proposed that the Purchasing Agent shall buy from a local dealer if the prices quoted by him do not exceed by more than 5% the lowest price quoted on the same article by a non-local dealer. Whether by "local dealer" is meant a dealer having his place of business in the County or in the State is unimportant, Kennedy said, because in our opinion, under either alternative such an ordinance would be invalid.

The County Counsel relied strongly on the opinion of the California District Court of Appeal in the case of Lambert v. Fenelon (1938) 25 Cal App(2d) 142, 77 P(2d) 268.

"In that case the county auditor filed a requisition with the purchasing agent of

Orange County for an '19 inch carriage L. C. Smith Standard typewriter' for use in the auditor's office. The purchasing agent refused to comply, but threatened to buy a typewriter of another make, in order to comply with a resolution of the Board of Supervisors ordering the purchasing agent to give an equitable distribution of supplies and equipment among the firms of Orange County when and where practical. The Superior Court found that because the typists in the auditor's office were more familiar with this brand of typewriter than any other, it was to the interest of the county to have this particular typewriter supplied instead of any other make.

"In affirming the judgment, the District Court of Appeal said at page 145:

'A discretion in the purchase of county supplies necessarily exists, but is one which must be reasonably exercised for the public good, and we may assume for the purposes of this decision that such discretion rests with the purchasing agent. The purpose of the statutes which provide for the appointment of a purchasing agent and define his duties is not only to relieve the board of supervisors from the details involved in purchasing necessary supplies, but to concentrate these matters in one office to the end that supplies may be purchased in quantities, that the best prices may be obtained, that waste may be eliminated, and that this phase of the county business may be more economically and efficiently administered in the public interest. It is easy to see that this purpose would often be defeated if the announced policy of distributing patronage to various firms in accordance with their turn, as this policy was interpreted by this appellant, were to be sustained as lawful and as necessarily sufficient. ***The discretion given is likewise one to be exercised in the public interest and not as a means of distributing patronage. Doubtless a discretion may be exercised in determining whether or not an article is needed, but the need is here conceded and no discretion remained to be exercised in that respect. It may be assumed that a discretion also exists with respect to what quality of article is needed in respective cases, and as between a high-priced article and one of lower price.

Where such a discretion exists a difference in price or quality may properly determine the exercise thereof. But where articles are standardized to the extent that quality and price are the same, that particular reason for the exercise of discretion no longer exists.

"Where there is no reasonable argument that any benefit will result to the county by paying a higher purchase price for an article where an article of equal value can be purchased for less, then, in the language of the Lambert case, any reason for the exercise of discretion no longer exists."

Mr. Kennedy stated, "We see no legal difference in a policy to give every dealer his turn and to prefer local dealers."

Interestingly, Mr. Kennedy concluded that the reasoning in Lambert v. Fenelon, supra, would also support the conclusion that the county itself is subject to the limitation that it does not permit the Board of Supervisors, under its charter or state law, to adopt such a provision. Mr. Kennedy found no authorization in state law which supported any such authority as being vested in the Board of Supervisors. He concluded that while the State Legislature may provide that in making purchasing policies other than that in the best interests of the County may be followed, the County, by ordinance, may not legally do so.

5. Recommended Policy.

National and state purchasing agents associations are unanimous in condemning preference provisions to local bidders. The best statement found on this subject is contained in a September, 1963, issue of Capps News, California Association of Public Purchasing Officers, quoting from the Public Management Journal of the National City Managers' Association, July, 1963, issue as follows:

"'Buy Local' Policy Hikes Costs

"In a recent memorandum to the mayor and city council members, Wayne F. Anderson, city manager, Evanston, Illinois, outlined four reasons against giving preferential treatment to local vendors regarding city purchases. Anderson pointed out that: (1) When a 'buy local' policy raises the city's cost of supplies and equipment, every household in the city is required to pay more taxes for the benefit

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of, at the most, several hundred local vendors. (2) Competition for the city's business is lowered because outside vendors are likely to decide against bidding where the local bidder is given preferential treatment. (3) The existence of a 3 to 5 per cent preference differential allows a local vendor to quote a higher price than he otherwise would and therefore to exploit the city. (4) a City that establishes a 'buy local' policy must realize that its commercial houses and manufacturers would lose business if other cities did the same thing. The city and economy as a whole are best served by a free flow of goods and as few barriers to free competition as possible. An award may be made to a local vendor even though his bid is not low if other cost considerations, such as ease of selection, pickup and delivery speed, and service and maintenance, make it advantageous to buy from him."

It is submitted that the only justifiable and proper policy is to provide for a local preference only when, considering all relevant factors in making a purchase, the bids of a local supplier is equal to that on non-local suppliers.

6. Conclusion.

Based on analysis of the foregoing opinions and authorities, the writer concludes that neither California cities nor counties have the legal authority to enact legislation to provide for local preference. Moreover, it is the writer's opinion that a provision in a city or county charter authorizing such a preference is invalid as in violation of the equal protection and privilege and immunities clauses of the Constitution, an unreasonable classification, and a gift of public fund of this doctrine applies to a governmental agency.

Q. Miscellaneous.

1. Confidential Nature of Prospective Bidders.

Former City Attorney Dion Holm of San Francisco has ruled that in the absence of statute ordinance or charter provision authorizing it, the Department of Public Works may not legally withhold the names of prospective bidders on public works and such lists are open to inspection under the provisions of California Government Code Section 1227. However, he further ruled that an ordinance authorizing the withholding of the names of prospective bidders or public works could validly be adopted to prevent possible collusion in bidding. (September 14, 1961).



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March 16, 1977

MEMORANDUM

TO: JACK CRIST, Director of Finance
FROM: LELIAND J. SAVAGE, Deputy City Attorney
RE: CONSIDERATION OF CITY SALES TAX REBATE IN DETERMINING THE
LOWEST RESPONSIBLE BIDDER FOR CITY CONTRACTS

QUESTION PRESENTED

In determining who is the "lowest responsible bidder" for purposes of awarding city contracts, is it permissible to take into account the one percent sales tax rebate the city receives from sales tax paid to suppliers located within the City of Sacramento?

ANSWER

Yes. Consideration of the sales tax rebate is a permissible method of determining the lowest bidder as required by City Charter Section 252. It does not constitute an illegal local preference bidding system.

ANALYSIS

I. Consideration of sales tax rebate in determining the "lowest bid" does not constitute an illegal local preference.

Under Section 252 of the City Charter, any city contract for supplies, equipment or the undertaking of a public project amounting to more than \$5,000, is subject to competitive bidding requirements which mandate that the contract be awarded to the "lowest responsible bidder."

Under a typical local preference bidding system, local suppliers are given a percentage preference or advantage over non-local bidders. A "bidding preference" has been defined as "some advantage, preference or privilege accorded to a locality, class of bids, or a competitor." There appears to be no local privilege, preference or advantage in using the sales tax rebate to calculate the lowest bid submitted, since all suppliers,

local and non-local, would be treated the same from an economic point of view. The supplier submitting the lowest responsible bid will be awarded the contract. For example, if the preference were five percent, any local bidder bidding less than five percent higher than a competing non-local bid would be awarded the contract, assuming other relevant factors are equal.

When the City purchases supplies from a supplier located outside the City, it pays six percent sales tax on the purchase price. When the City purchases the same supplies for the same price from a supplier located within the City, it pays the same rate of sales tax; however, state law provides for a one percent tax rebate.

If the sales tax rebate is taken into account, the ultimate economic cost to the City would be less if the City purchased the supplies from a local supplier. For example, if the City buys \$10,000 worth of supplies from a supplier located outside the city, the total price including tax is \$10,600. The same purchase from a Sacramento firm would also cost \$10,600. However, the City would receive \$100 back in its local sales tax rebate, reducing the total economic cost to the City to \$10,500. In this situation, the local supplier would be the low bidder and, assuming it qualifies as a "responsible bidder," it should be awarded the contract.¹

Neither the City Charter nor the City Code set forth specific guidelines or criteria for determining the "lowest" bid. Consideration of sales tax rebates does not impair or modify competitive bidding. Bidder responsibility and economic cost remain the only permissible criteria for letting contracts.

1. As the following figures show, any local bid lower than \$10,095.20, would cost the City less than a non-local bid of \$10,000:

<u>Sacramento Bidder</u>		<u>Non-Local Bidder</u>	
\$10,095.20	Bid	\$10,000.00	Bid
<u>+ 605.70</u>	6% Sales Tax	<u>+ 600.00</u>	6% Sales Tax
10,700.90	Gross Price	\$10,600.00	Total Cost to City
<u>- 100.90</u>	1% Local Rebate		
\$10,600.00	Total Cost to City		

MEMO TO JACK CRIST

March 16, 1977

Page 3

There does not appear to be any California authority on this point. Other jurisdictions have decided cases which are closely analogous in favor of taking into account the lowest economic cost. In Austin vs. Housing Authority of the City of Hartford (1956) 122 A.2d 399, the Supreme Court of Errors of Connecticut upheld a municipality's consideration of projected insurance dividends in calculating the lowest bid for city insurance coverage. Company X submitted a bid for a fixed five-year gross premium of \$86,997.45. Company Y submitted a gross premium bid of \$114,567. However, Y stated it would pay an estimated dividend of \$57,283.50 over the five-year period; X offered no dividends. The court concluded that while X's bid of \$89,997.45 was the lowest of all the bids which made no deduction from gross premiums for dividends, Y's bid of \$114,567 minus the \$57,283.50 in projected dividends was the lowest net premium bid.

Consideration of the sales tax rebate in calculating the lowest bid appears to be closely analogous to consideration of dividend refunds in the bidding process in Austin. In both cases net economic cost, rather than monetary face value determines the lowest bid. The court allowed inclusion of dividends in calculating the lowest net premium bid in spite of the fact that the amount of the dividend refunds were speculative. Insurance dividends are based on the return of the unused or unabsorbed premium, and in this particular case, dividends were estimated on the basis of the returns to policyholders over a period of the ten preceding years. 122 A2d 399, 401. The sales tax rebate, on the other hand, is not a projected figure, but rather a certain cash return. This appears to provide even stronger justification for including the tax rebate in calculating the lowest bid.

In Market Maintenance Co. Inc. vs. City of Newark (1960) 164 A2d 367, the New Jersey Superior Court, Appellate Division, upheld the City's inclusion of a 1 percent "prompt payment discount" in computing the lowest bid. The plaintiff submitted a lump sum bid of \$87,600 on the window washing contract. The combined bids of four other bidders amounted to \$88,219, but two of them offered discounts with the bid for a net price bid of \$87,089.47 - some \$511 less than plaintiff's bid.²

2. It should be noted that in this particular case, there was little uncertainty as to the inclusion of the discount in the ultimate bid price. In awarding the bids, the City accompanied its acceptance with a contract binding itself to pay the net sums of the bids after discount within 20 days of invoice.

The court concluded that consideration of the discount was a lawful exercise of the authority of the Business Administrator in determining "which bid in given circumstances is most advantageous to the city, and so the lowest bid..." "[T]he mere fact that alternative [payment] proposals are sought does not of itself invalidate the bidding. (citations omitted)" 164 A2d. 367, 369.

II. Consideration of the sales tax rebate in the bidding process is within the proper discretion of the City Council, and is presumed to be valid.

The determination of who is the lowest responsible bidder lies within the judgment of the governing body and will not be disturbed by the courts unless the decision was induced by fraud or shown to be an arbitrary, unreasonable misuse of discretion. Diablo Beacon Painting & Publishing vs. Concord, (1964) 229 Cal.App.2d 505, Cyr vs. White, (1947) 83 Cal.App. 2d 22.

The court stated in Diablo Beacon Painting & Publishing vs. Concord:

"In determining whether to accept a bid for a public contract, public officers as a rule perform not merely ministerial functions, but duties of a judicial or discretionary nature, and the courts in absence of fraud or an abuse of discretion, will not ordinarily interfere, so long as the officers comply with the controlling constitutional or legislative provisions." (229 Cal.App.2d 505, 508)

Thus a presumption of validity attaches to the determination of the lowest responsible bidder which can only be overcome by proof that the governing body acted without justification or fraudulently. When measured against this standard, consideration of the sales tax rebate in the bidding process would not seem to be sufficient grounds for judicial intervention. It is not contrary to constitutional, statutory, or charter provisions.

Secondly, the sales tax rebate is a reasonable factor to include in determining the low bid. It is easily calculated, and non-discriminatory.

Finally, consideration of the sales tax rebate leads to a more precise measure of the ultimate economic cost of a bid. Arguably, Section 252 of the City Charter which requires selection of the lowest responsible bidder requires that the sales tax

MEMO TO JACK CRIST
March 16, 1977
Page 5

rebate be included in the factors considered when determining the lowest responsible bidder.

CONCLUSION

The City may take into account the fact that the City will receive a 1 percent sales tax rebate from sales tax paid to supplier located within the City of Sacramento.

JAMES P. JACKSON
City Attorney

By: Leiland J. Savage
LEILAND J. SAVAGE
Deputy City Attorney

LJS:plf