

Memorandum

TO: DRIVING A STRONG ECONOMY
COMMITTEE

FROM: Paul Krutko

SUBJECT: SEE BELOW

DATE: January 13, 2006

**SUBJECT: CONTRACTING WITH SMALL AND LOCAL BUSINESSES IN FISCAL
YEAR 2005 - 2006**

RECOMMENDATION

Accept the annual report on the status of implementation of the Small Business Opportunity Program.

BACKGROUND

On January 14, 2003 the City Council adopted a resolution establishing a City policy to encourage small business with 35 or fewer employees to participate in City contracts. The Small Business Opportunity Program (SBOP), a citywide system of process improvements, outreach, education, and performance measures was established to implement the new policy. The SBOP is comprised of three elements identified as key through public outreach 1) performance measurements, 2) outreach and education, and 3) process improvements.

On May 4, 2004, Council augmented the Small Business Opportunity Program through the adoption of an expanded Local Preference Policy. Under the policy, when seeking bids for goods and services, the City of San Jose views those from local (within Santa Clara County) and local, small businesses (with 35 or fewer employees) more favorably than non-local competitors while still including factors such as cost and experience.

The City began tracking the impacts of the City's Small Business Opportunity Program (SBOP) and the City's revised Local Preference Policy on July 1, 2004. The following analysis discusses the level of local and small business participation in City agreements.

ANALYSIS

PARTICIPATION OF SMALL BUSINESS IN THE SAN JOSE ECONOMY

The following table (1) compares the relative performance of small businesses in San José's economy in 2002 and 2005.

Economic Performance of Small Business - Table 1

Measure	2002 (% of total)	2005 (% of total)	% Inc.
Small San José companies	52,000 (85%)	54,200 (88%)	4%
Employment at Small San José companies	119,000 (40%)	122,000 (40%)	3%
Business taxes from Small San Jose Companies	\$5.8 mil. (60%)	\$6.3 mil. (63%)	9%
Second quarter small company sales tax revenues (<\$2 M in sales)	\$9.9 mil. (38%)	\$12.8 mil. (42%)	29%

Small businesses as a group have grown, with the number of small San José companies increasing by 4% and employment at these companies growing by nearly 3%. Sales tax collected by smaller San José companies has also risen. Compared with the second quarter of 2002, small San Jose companies sales tax collections have increased by over 29%.

Overall, small businesses (defined as those with 35 or fewer employees) have been able to hold their relative position in the current economy and have even made strides compared to large companies.

CITY PERFORMANCE

Overview

The City began tracking the impacts of the City's Small Business Opportunity Program (SBOP) and implementation of the City's revised Local Preference Policy on July 1, 2004. Despite staff and budgetary reductions, implementation of the SBOP across the organization has generally been achieved, though additional work remains. In particular, additional integration of tracking into City processes will improve available information.

As discussed in the Council memorandum titled "Request for Proposal Procedures and Other Procurement Reforms" approved by the City Council on December 6, 2005, the purchase and implementation of an e-procurement and contract management system is necessary to ensure accurate data collection and reporting. As recommended in the aforementioned memorandum, through the centralization of contracting in the Finance Department (except for construction related contracting activity), the Departments of Finance and Public Works will be able to more effectively collect small and local contracting data citywide. A proposal for these changes will be brought forward as part of the 2006/07 budget process.

The following information has been gathered so far regarding the City's success in doing business with companies who can be broadly described as "suppliers."

Numerical Performance Review

Local Suppliers

Overall, the data in table 2 below indicates that the City awards a significant number of agreements to local suppliers. Total fiscal year expenditures were \$877 million awarded through approximately 4,100 agreements. Local suppliers captured roughly 1,850 agreements and \$342 million.

Local Suppliers - Table 2

4,100 awards for a total of \$877 million

	FY 2004/05
% by # of Awards	45%
% by Dollar Amt.	39%

Small Suppliers

Additional time and resources are necessary to more comprehensively track small business participation to the City's Purchasing and Business tax systems but some estimates can be made of City performance.

At present, the City's small business database has linked approximately 13% of the City's 4,000 active suppliers with information about the number of their employees. Because there is incomplete information, the data contained in tables 3a and 3b below is extrapolated from the limited sample that has been gathered.

While the number of suppliers for which the City has employment information has increased, it has not kept pace with the additions of new suppliers over the past year. A review of the process by which new suppliers are tracked will be undertaken. The acquisition of an e-procurement system and the centralization of most contracting in Finance should allow the collection of more accurate data on small and local suppliers.

The following table demonstrates that overall the City has done a good job of enabling small, local suppliers to effectively compete to provide goods and services to the City. Smaller firms are generally more likely to handle smaller agreements, which explains why the percentage of awards they receive is larger than the percentage of dollars being spent with them.

Small, Local Suppliers - Table 3a

	August 2004 (1 month)	December 2004 (6 months)	FY 2004/05 (12 months)
% by # of Awards	31%	44%	45%
% by Dollar Amt.	21%	17%	23%

In another demonstration of how effective the City has been in opening its doors to small businesses, the City's performance including all small suppliers (not just local, small businesses)

is even better. The following table shows that in FY 04/05 nearly three-quarters of City agreements go to small suppliers.

Small (local or not) Suppliers - Table 3b

	August 2004 (1 month)	December 2004 (6 months)	FY 2004/05 (12 months)
% by # of Awards	62%	70%	71%
% by Dollar Amt.	30%	41%	62%

The data above shows that there is significant variance over the year in the number and amount of awards made to local and small suppliers. This presents significant problems in reliably evaluating the City's achievements for short (quarterly) periods.

Local and Small Preference Review by Category

As part of the implementation of the Local Preference, the City also uses a separate system to track the number of suppliers which self-identify as local and both local and small. Specific performance information is presented for Fiscal Year 2004-2005 in three major categories: Finance/Purchasing, Public Works and Professional Services. The following tables summarize the available information by category:

Finance/Purchasing Awards

Contracts and Purchase Orders - Table 4

1836 awards for a total of \$103 million

	% by # of Awards	% by Dollar Amt.
Local Suppliers	38%	25%
Small Suppliers	15%	12%

Purchasing performance, in close cooperation with OED, has achieved more than a third of awards going to local Suppliers.

Public Works Consulting Contracts

Consulting Contracts- Table 5a

28 awards for a total of \$10.2 million

	% by # of Awards	% by Dollar Amt.
Local consultants	54%	68%
Small consultants	11%	3%

As indicated in the table above, local firms perform more than 50% of the consulting work for Public Works. Although the amount of work going to consultants has dropped in FY 0405 due to the City's effort to "contract in" professional services to maximize internal productivities and

reduce the impact of on-going budget reduction, the proportion of work that local consultants are performing remains over 50% of the total number of professional service contracts.

As indicated in the table below, a much smaller percentage of work is going to small firms that are local. The 11% of work going to local and small consultants represents 3 consulting contracts. In reviewing the selection scorecards for all 28-consultant selections, the points awarded through the Local Preference Policy did not influence the final selections. This will not necessarily be true in the future, but in the case of last year the point differential in the various selection processes was greater than the 10 points awarded through the Local Preference Policy.

It is important to note that there is a large local consultants pool to draw from and that explains the amount of work going to local firms. However, the same is not true for local and small consulting firms. Public Works maintains a database for various consultant categories (i.e. civil, electrical, architectural, archaeology, etc.) that have been pre-qualified and want to do business with the City. This database has a total of 376 consulting firms. Of this number, 118 firms are local and 39 are local and small, respectively. As evident from the above illustration, there is a small percentage of local and small firms relative to the local firms.

In conclusion, the lesser number of consulting contracts awarded to local and small firms appears to be related to the limited number of available consultants. Additional research work will be done to determine if there are local and small consultants that have not responded to our previous outreach efforts by registering with Public Works' consultant database. A more complete analysis will be conducted to develop future action items to improve the participation rate of local and small businesses.

Public Works Construction Awards

Construction Contracts - Table 5b
76 awards for a total of \$105.6 million

	% by # of Awards	% by Dollar Amt.
Local contractors	43%	20%
Small consultants	33%	15%

The Local Preference Policy does not apply to Construction contracts in accordance with the City Charter. Construction contracts are awarded strictly to the lowest bidder. The percentage of awards to local contractors remains relatively consistent with activity level over the last three years. However, for contracts less than \$1 million, the percentage contracts awarded to local firms has increased to over 50%. As concluded above, additional research is needed to determine the level of responses from local and small contractors to the bidding process, and more analysis will be performed in order to provide suggestions to increase construction contract awards to local and small contractors.

Professional Services Contracts Citywide

Consultants - Table 7

387 awards for a total of \$38.5 million

	% by # of Awards	% by Dollar Amt.
Local consultants	75%	82%

Professional services contracts show the largest percentage of local participation among the systems tracking local preference performance. More than three quarters of contracts are awarded to local companies.

Very few of the professional agreements correctly recorded small business information. This is due to the decentralized system for generating professional service agreements. Tracking of local, small supplier participation will be revisited to more consistently produce accurate information. This tracking system would also benefit from consolidation under Purchasing as referenced previously.

PUBLIC OUTREACH

Quarterly newsletters and workshops help inform the public about the Small Business Opportunity Program and the Local Preference. Staff also regularly leverages events held by outside organizations to further increase knowledge of the program.

Information on the citywide SBOP performance for FY 04/05 was presented to the Small Business Development Commission in November 2005. The final data by department represented in this report will be presented to the group in February.

OUTCOMES

Overall the results of the review of small and local business participation in City contracts are positive. With Committee approval of this report additional steps will be undertaken to encourage continued progress and improved City performance:

- Staff will provide annual reporting of performance to the Mayor and Council, and the Small Business Development Commission. Additional investments in Purchasing systems are likely to increase the accuracy of participation tracking information.
- Quarterly reporting provides an inaccurate impression of the City performance since the size and location of suppliers chosen varies significantly through the year.
- Additional research work will be done to determine if there are local and small consultants that have not responded to the City's previous outreach efforts by registering with Public Works' consultant database
- Public Works will complete an analysis to develop future action items to improve the participation rate of local and small businesses.

- Tracking of local, small, professional-services contractor participation will be revisited to more consistently produce accurate information.

A proposal will be brought forward as part of the 2006/07 budget process to centralize contracting in Finance except for construction related contracting activity and to procure an e-procurement system. If approved, implementation of the improved tracking system is scheduled to become effective January 2007.

COORDINATION

This report was coordinated with Public Works and Finance.

BUDGET IMPLICATIONS

No new budget implications. A proposal will be brought forward as part of the 2006/07 budget process to centralize contracting in Finance except for construction related activity and to procure an e-procurement system.

CEQA

This is not a project.

PAUL KRUTKO
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