

HOUSE BILL REPORT

EHB 2257

As Passed House:

March 16, 2005

Title: An act relating to requiring state agencies to contract for goods and services in a manner consistent with the state's best interests.

Brief Description: Requiring state contracts to be in the state's best interests.

Sponsors: By Representatives Williams, Conway, Morrell and Wood.

Brief History:

Committee Activity:

Commerce & Labor: 3/2/05 [DPS];

Appropriations: 3/5/05 [DP2S(w/o sub CL)].

Floor Activity:

Passed House: 3/16/05, 61-35.

Brief Summary of Engrossed Bill

- Requires the Office of Financial Management to develop and implement procurement policies and procedures necessary to determine whether certain contracts and subcontracts are in the state's best interests.
- Also requires the Office of Financial Management to study the benefits of adopting procurement policies giving Washington businesses a price preference when determining the lowest responsible bidder on state contracts.

HOUSE COMMITTEE ON COMMERCE & LABOR

Majority Report: The substitute bill be substituted therefor and the substitute bill do pass. Signed by 4 members: Representatives Conway, Chair; Wood, Vice Chair; Hudgins and McCoy.

Minority Report: Do not pass. Signed by 3 members: Representatives Condotta, Ranking Minority Member; Sump, Assistant Ranking Minority Member; and Crouse.

Staff: Jill Reinmuth (786-7134).

HOUSE COMMITTEE ON APPROPRIATIONS

Majority Report: The second substitute bill be substituted therefor and the second substitute bill do pass and do not pass the substitute bill by Committee on Commerce & Labor. Signed by 20 members: Representatives Sommers, Chair; Fromhold, Vice Chair; McDonald, Assistant Ranking Minority Member; Buri, Clements, Cody, Conway, Darneille, Dunshee, Grant, Haigh, Kagi, Kenney, Kessler, Linville, McDermott, Miloscia, Priest, Schual-Berke and Walsh.

Minority Report: Do not pass. Signed by 8 members: Representatives Alexander, Ranking Minority Member; Anderson, Assistant Ranking Minority Member; Armstrong, Bailey, Hinkle, Hunter, Pearson and Talcott.

Staff: David Pringle (786-7310).

Background:

State Procurement

The State of Washington contracts with individuals and companies outside of state government to provide certain services to the state and its residents. The state's purchasing authority is generally organized into categories based on the type of service. These categories include the following:

- Personal services. This term refers to professional or technical expertise provided by a consultant to accomplish a specific study or project.
- Purchased services. These services are ones provided by a vendor to accomplish routine, continuing and necessary functions.
- Information services. These services include data processing, telecommunications, office automation, and computerized information systems.
- Public works. This term refers to the construction, repair, or alteration of buildings and other real property.
- Highway design and construction. This term includes both architectural and engineering services, as well as construction services related to highways.
- Printing services. This term refers to the production of printed materials.

In addition, beginning July 1, 2005, the state may contract for services historically and traditionally provided by state employees, so long as the state complies with the contracting out provisions of the Civil Service Reform Act of 2002.

Laws governing state procurement that give preference to domestic goods or prohibit purchasing foreign goods have been challenged on one or more grounds. These include arguments that such laws are: (1) invalid exercises of state power under the Foreign Commerce Clause and/or the Foreign Affairs Power; (2) preempted by federal law; or (3) in violation of international agreements on government procurement.

Foreign Commerce Clause

The United States Constitution reserves to Congress the power "to regulate Commerce with foreign Nations, ..." The U. S. Supreme Court has struck down state laws that regulate commerce in a manner that promotes businesses in the state at the expense of businesses in other states or foreign countries. However, the U. S. Supreme Court has also recognized that, when a state acts as a market participant, rather than a market regulator, it is not subject to the restraints of the Commerce Clause. Other federal and state courts, relying on the "market participant doctrine," have generally upheld state "Buy American" laws.

Foreign Affairs Power

With regard to foreign policy, the federal government also has exclusive authority. The U. S. Supreme Court has said that the President has the "lead role" as well as "a degree of independent authority to act." The Court has struck down at least one state law as an "intrusion by the state into the field of foreign affairs which the Constitution entrusts to the President and the Congress."

Federal Preemption

The U.S. Supreme Court has found that state laws in conflict with federal laws or with foreign policies and diplomatic objectives of the President and Congress are preempted.

International Agreements

The Agreement on Government Procurement (GPA) is one of many World Trade Organization (WTO) agreements to which the United States is a party, and is one of several agreements that apply to Washington and certain other states. The GPA is a plurilateral agreement, meaning that only some WTO members are parties to the agreement. For example, Ghana, India, Mexico, and the Philippines are members of the WTO, but are not parties to the GPA.

In Washington, state agencies subject to the GPA include certain executive branch agencies such as the Department of General Administration and the Department of Transportation, as well as state universities. State contracts subject to the GPA currently include contracts of \$477,000 or more for goods and services, and contracts of \$6,725,000 or more for construction services.

Article III of the GPA deals with national treatment and non-discrimination. It provides, in part that:

- Parties to the agreement must give the products, services and suppliers of other parties treatment no less favorable than that accorded to domestic products, services and suppliers.
- Parties must not treat locally-established suppliers less favorably than other suppliers on the basis of foreign affiliation or ownership.

- Parties must not discriminate against locally-established suppliers on the basis of the country of production of the good or service being supplied.

According to the WTO Analytical Index for the GPA, there are no decisions of competent WTO bodies interpreting this article of the GPA. (In 1994 the European Union and Japan filed formal complaints against the United States in the WTO, claiming that Massachusetts' Burma law violated certain provisions of the GPA. In 1999, at the request of the European Union and Japan, these proceedings were suspended. Later, they automatically lapsed.)

Under the federal Uruguay Rounds Agreement Act (Act), Congress approved the WTO agreement and other agreements annexed to that agreement, including the Agreement on Government Procurement. The Act provides that no state law may be declared invalid on the ground that it is inconsistent with any of the Uruguay Round Agreements, except in an action brought by the United States for that purpose. The Act also sets forth procedures for dispute resolutions involving other WTO members and legal actions by the United States against states to declare state laws invalid as inconsistent with any of the Uruguay Round Agreements.

Laws and Executive Orders in Other States

Laws relating to offshore outsourcing of state contracts have been enacted in at least six states (Alabama, Colorado, Illinois, Indiana, North Carolina, and Tennessee). Executive orders or directives relating to offshore outsourcing of state contracts have been issued by the governors of at least six states (Alaska, Michigan, Minnesota, Missouri, New Jersey, and North Carolina). These laws and executive orders and directives address offshore outsourcing of state contracts in various ways, including:

- limiting the authority of state agencies to enter into contracts for services that will be performed at sites outside the United States;
- authorizing state agencies to give price preferences on contracts for services that will be performed within the state;
- encouraging state agencies to enter into contracts for services that will be performed within the state;
- requiring state agencies to consider economic and other impacts of contracts for services that will be performed at sites outside the United States; and
- requiring contractors and subcontractors to disclose information about contracts for services performed at sites outside the United States.

Summary of Engrossed Bill:

Policies to determine whether certain contracts are in the state's best interests must be developed, and a study of the indirect benefits of policies giving Washington businesses a price preference must be conducted. The contracts addressed by the "best interests" policies and the "price preference" study are contracts for personal services, purchased services,

information services, public works, highway design and construction, and goods. They also include civil service contracts.

"Best Interests" Policies

The Office of Financial Management (OFM), in consultation with representatives of state agency management, business, labor, and agricultural groups, must develop and implement procurement policies and procedures necessary to determine whether certain contracts and subcontracts are in the state's best interests.

These policies and procedures must require consideration of the following when making decisions to enter into contracts:

- the extent to which the contract will be performed at a location outside the United States;
- the extent to which international trade agreements are applicable to the contract;
- the extent to which awarding the contract to a Washington business will result in job creation or retention or other economic benefits;
- the extent to which the contract involves solicitation or disclosure of personal information; and
- the extent to which decisions to locate certain facilities in Washington by businesses based in other countries and other states has resulted in job creation and other economic benefits.

"Price Preference" Study

The OFM, in consultation with representatives of state agency management, business, labor, and agricultural groups, also must study the indirect benefits of adopting procurement policies giving Washington businesses a price preference when determining the lowest responsible bidder on certain contracts. These benefits must include job creation and retention, capital investment, tax revenue, and economic stimulus. The OFM must report its findings, and any recommendations for legislation on price preferences, to the Legislature by December 1, 2005.

Appropriation: None.

Fiscal Note: Requested on the substitute bill on March 3, 2005.

Effective Date: The bill takes effect 90 days after adjournment of session in which bill is passed.

Testimony For: (Commerce & Labor) (As presented for HB 2144) This bill establishes a four-part test to determine whether contracted services are in the best interests of Washington, its residents, and its economy. It requires the best use of state resources, including an assessment of whether or not a contract will cost jobs or change the quality of life. It is sensible and fair.

Job growth is a priority. Economic security should not be imperiled without carefully considering the consequences. Before creating jobs overseas, the state should consider the impacts at home.

This bill is modeled after an executive order in another state. Other states have already acted, and Washington should be at least as progressive and protective.

Workers have suffered many consequences related to offshore outsourcing. For example, when fabrication jobs were lost on the Narrows Bridge project, it was a blow to the workers and to the state economy.

The bill should be amended to address offshore outsourcing of public works contracts, including fabrication various parts, and to creative incentives for using state-based contractors.

(With concerns for HB 2144) Faculty research and student exchange programs are a concern. It may be that the only practicable location for such programs and related contracts is clearly and justifiably a location outside the Unites States.

Testimony For: (Appropriations) The bill has been changed from an outright ban on offshoring, and is still a work in progress. State contracts are an investment of public money, and should be used to build the state economy. We can provide examples of how this is the case.

Testimony Against: (Commerce & Labor) (As presented for HB 2144) The "best interests" of the state are in the eye of the beholder, especially with regard to taxpayer money. Although the bill is lifted, in part, from an executive order in Michigan, it does not include all parts of the Michigan order. The Michigan order also required disclosure, as well as debarment of vendors that failed to comply. It also specified that the best interests must be determined in a manner consistent with federal and state law. The bill should not slide into a prohibition on offshore outsourcing.

Another concern is the process for developing the procurement policies. Instead of the process outlined in the bill, there should be a process under the Administrative Procedures Act so that the entire community of interest could participate, and the result could be fair and balanced.

Testimony Against: (Appropriations) This removes the low cost value from state contracting. It abandons the open trade policies of the three previous Governors. Only about 1 to 2 percent of state contracts are with overseas entities. We object to the 5 percent price preference provision - it violates our reciprocity agreements with about 30 other states. This adds both process and costs to the state contracting system. Purchasing managers should not have to also serve as economic development directors.

Persons Testifying: (Commerce & Labor) (In support of HB 2144) Representative Brendan Williams, prime sponsor; Ron Piksa, Iron Workers District Council of the Pacific Northwest;

Bev Hermanson and Bob Doyle, Washington Federation of State Employees; and Dave Johnson, Washington State Building & Construction Trades Council.

(With concerns on HB 2144) Gail Stygall, University of Washington Faculty.

(Opposed to HB 2144) Kris Tefft, Association of Washington Business.

Persons Testifying: (Appropriations) (In support) Bob Doyle and Bev Hermanson, Washington Federation of State Employees.

(Opposed) Kris Tefft, Association of Washington Business; and Lew McMurrin, Washington Software Alliance.

Persons Signed In To Testify But Not Testifying: (Commerce & Labor) None.

Persons Signed In To Testify But Not Testifying: (Appropriations) None.