

# Legislative Analysis



## MICHIGAN-BASED BUSINESS PREFERENCE IN SCHOOL CONTRACTING

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**House Bill 5639 (Substitute H-1)**

**Sponsor: Rep. Dudley Spade**

**Committee: Education**

**First Analysis (5-7-08)**

**BRIEF SUMMARY:** The bill would allow the boards of intermediate districts, school districts, and charter schools to give a preference of up to 10 percent of the amount of a contract to Michigan-based businesses when they are responding to competitive bids for school construction, supplies, materials, and equipment.

**FISCAL IMPACT:** The bill would have no direct fiscal impact on local school districts or the state. However, in allowing districts to give preference to Michigan-based firms, it could increase contract costs by up to 10 percent for school districts, but also could increase state revenue to the extent that it generated additional business for Michigan firms.

### **THE APPARENT PROBLEM:**

Currently, all school officials and boards of education in Michigan public schools must seek competitive bids for projects or purchases costing just over \$19,000—an amount that increases annually, in line with the rate of inflation in the economy.

Competitive bidding is governed by Section 1267 of the Revised School Code, although the code, itself, does not contain a definition of "competitive bid." Instead, a description of the "competitive bid" process—both its rationale and its protocols—is found in Attorney General Opinion 3303 of 1959. There, the Office of the Attorney General writes: a school board is required to request bids "to obtain a cross-section view of the particular market with which it is concerned, and apprise itself of the integrity and technical qualifications of the prospective contractors." The opinion notes that "the aim of the board should be to *secure the most able and efficient performance, from the most responsible contractor, on terms beneficial to the public.* The lowest bid does not always respond to this test."

The Thrun Law Firm, P.C. (offering counsel to hundreds of Michigan school districts) advises school board members when seeking the "lowest responsible bidder" to consider the school district's direct experience with the contractor, as well as the experience of other school districts with that contractor; the contractor's history of satisfactory performance, of reasonable change orders, and of questionable or unfounded litigation; and finally, the recommendation of the architect and/or construction manager based on past experience with the contractor. Ultimately, school officials must award the work to the lowest responsible bidder. If the low bidder is deemed responsible, the award should be made to that low bidder. Failure to do so can result in penalties, including the

imposition of a fine in an amount equal to (not more than) 10 percent of the cost of the project, or imprisonment for up to one year, or both.

At times, Michigan firms are underbid by out-of-state firms during the competitive bidding process—sometimes by only a few hundred dollars—an occurrence that often happens along the borders of the state. For example, in Lenawee County at the Intermediate School District, an Ohio firm underbid a Michigan-based firm by \$400 on a \$428,600 project in June 2007.

Because public schools depend on the support of the local business community, and local taxpayers make local public schools possible, school officials prefer to work with local Michigan-based companies whenever possible. Some school officials have suggested the statute be changed to allow them (but not require them) to exercise their discretion by extending a preference of up to 10 percent of a contract's total value to a Michigan-based company that over-bid an out-of-state competitor.

### ***THE CONTENT OF THE BILL:***

House Bill 5639 (H-1) would amend the Revised School Code (MCL 380.623a et al.) to allow the boards of intermediate districts, school districts, and public school academies (or charter schools) to give a preference of up to 10 percent of the amount of a contract to Michigan-based businesses when they are responding to competitive bids for school construction, supplies, materials, and equipment.

"Michigan-based firm" is defined to mean a firm that would qualify for a preference in a procurement contract with the State of Michigan under Section 261(1) of the Management and Budget Act, as determined by the Department of Management and Budget.

[Section 261(1) of that act states: "The department shall provide for the purchase of, the contracting for, and the providing of supplies, materials, services, insurance, utilities, third party financing, equipment, printing, and all other items as needed by state agencies for which the legislature has not otherwise expressly provided. In all purchases made by the department, all other things being equal, preference shall be given to products manufactured or services offered by Michigan-based firms, if consistent with federal statutes. The department shall solicit competitive bids from the private sector whenever practicable to efficiently and effectively meet the state's needs. The department shall first determine that competitive solicitation of bids in the private sector is not appropriate before it shall use any other procurement methods for an acquisition."]

Under House Bill 5639 (H-1), if the Michigan-based firm otherwise met the requirements of the contract solicitation, and with these preferences was the lowest responsible bidder, the school boards could award the contract to the Michigan-based firm, rather than to the lowest bidder. If two or more Michigan-based firms were the lowest responsible bidders on a contract with these preferences, all other things being equal, the school board could award the contract to the Michigan-based firm with the lowest responsible bid.

In addition, currently under the Revised School Code, the board of an intermediate school district, a school district, or a charter school cannot purchase an item or a group of items in a single transaction costing \$17,932 or more, unless competitive bids are obtained, and the purchase is approved by the board. That threshold is increased annually in line with inflation. The bill would increase the competitive bid threshold for a single transaction from \$17,932 to \$20,102.

***ARGUMENTS:***

***For:***

In February 2008 Michigan's unemployment rate was 7.2 percent, the highest rate in the United States, a rate that has often ranked at or near the top during the past two years. According to the Department of Labor and Economic Growth, there are 350,000 unemployed people in Michigan, and another estimated 100,000 residents are marginally employed. The Department of Labor and Economic Growth also reports there are 23,000 jobs unfilled in Michigan.

In order to match Michigan jobs with Michigan residents, 12 bills were recently passed by the House of Representatives to require recipients of state contracts and economic development incentives to hire Michigan residents first whenever possible, and not to knowingly hire those workers who are in the United States illegally.

This bill has a similar aim, but it is voluntary. It allows Michigan school officials to increase their efforts to hire qualified Michigan residents, in order to bring down the state's unemployment rate.

Further, when Michigan employers benefit from local contracts (such as being paid by local public schools for a construction project), their employees spend their paychecks locally. Their economic behavior as consumers strengthens the community whose parents and children the public school serves, and upon whom the very existence of the public school depends. Consequently, a "percentage disregard" policy is both effective and efficient, if it is limited in both its scope and its application.

***Against:***

The bill is a good one, but it should be amended in two ways. First, the total amount of money a school board spends each year to maintain its "percentage disregard" in order to favor local contractors should be capped. Second, the bill should be amended to clarify the definition of "Michigan-based business," a term far too vaguely defined in the legislation.

***Against:***

Opponents of the bill worry that any "percentage disregard" policy would promote a culture of inflated costs in which local contractors purposely over-value their work when offering bids in order to increase their profit, knowing full well that local school officials would select them despite their higher cost. Opponents say public policy should be entirely market driven, and should avoid monetary rewards for less than fully competitive behavior. Consequently, the bill's opponents urge that fellow policymakers reframe the policy problem to ask: Why

are the out-of-state bidders lower? Is the problem prevailing wage rates? Tax burdens? Regulatory costs? If so, opponents say these costs should be lowered, rather than adopt a policy that continues and perhaps exacerbates higher costs to taxpayers.

***POSITIONS:***

The Lenawee Intermediate Schools supports the bill. (5-6-08)

The Michigan Association of School Administrators and Intermediate School District Administrators support the bill. (5-6-08)

The Michigan Association of School Boards supports the bill. (5-6-08)

The Michigan Elementary and Middle School Principals Association supports the bill. (5-6-08)

The Kalamazoo, Muskegon, Ottawa Intermediate School Districts support the bill. (5-6-08)

The American Federation of Teachers-Michigan supports the bill. (5-6-08)

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■ This analysis was prepared by nonpartisan House staff for use by House members in their deliberations, and does not constitute an official statement of legislative intent.