



RON GALPERIN
CONTROLLER

May 20, 2021

Honorable Eric Garcetti, Mayor
Honorable Michael Feuer, City Attorney
Honorable Members of the Los Angeles City Council

Re: Increasing Local Investment in Los Angeles

As the City gradually reopens and recovers from the COVID-19 pandemic, reviving the local economy and increasing jobs should be a top priority. **The nexus between where the City purchases its goods, the sales taxes it pays, and how the local share of sales taxes is allocated presents an opportunity to increase local business participation in City contracting.** The following letter details how the City can incorporate sales taxes into its procurement process in a way that leads to more investment in Los Angeles.

The City purchases many goods yearly

Among Council-controlled departments, commodities purchases topped \$574 million in FY 2020. The top spending categories include software (\$41.3M), automobiles (\$24.9M), construction machinery and equipment (\$22.4M), asphalt (\$18.9M) and helicopters/related equipment (\$16.8M). City employees use these materials, supplies and equipment during the normal course of their duties.

In addition, the proprietary departments—Port (POLA), Airports (LAWA), and Water and Power (LADWP)—anticipated \$6.4 billion in non-salary expenses for FY 2021. Although this figure also includes expenditures for services, the capital-intensive nature of the proprietary departments' activities means that they also purchase a significant amount of goods.

Purchases are subject to sales and use taxes

Like other buyers, the City pays sales and use taxes on the tangible goods, which is most often applicable to the materials, equipment and supplies that make up commodities purchases. Sales taxes in Los Angeles are currently 9.5%, consisting of the statewide sales tax rate (7.25%) and an additional district sales tax rate (2.25%). **Relative to our commodities**

purchases between FY 2018 and FY 2020, Council-controlled City departments paid between \$32 million and \$39 million annually in sales and use taxes.

The City receives a share of sales tax revenue from all transactions that occur within city limits. Retailers engaged in business in California are generally required to pay sales tax on all retail sales and report the place of sale in their tax returns. The State then allocates a share (1%) of statewide sales taxes to local governments based on the reported place of sale. In FY 2020, the City received \$534 million as its local share of statewide sales taxes generated from all purchases made in Los Angeles.

To level the playing field between California retailers and out-of-state merchants, the State also requires buyers to pay an equivalent use tax on taxable items where sales taxes were not paid. The local share of use tax is allocated to the “place of first use” reported by consumers on their state tax return.

More local contracting opportunities needed

As of April 2021, there were over 62,000 active registered businesses with the City’s Business Assistance Virtual Network (BAVN) in order to bid on City contracts. In addition, businesses in L.A. County may qualify to be certified as a Local Business Enterprise (LBE) or a Small Local Business (SLB), which allows City departments to provide preference points when evaluating their bids. As of April 2021, there were 1,219 LBEs and 855 SLBs registered in BAVN.

According to the Bureau of Contract Administration, the City awarded 377 contracts (worth \$403M) in FY 2019 to LBEs. However, only 25 contracts were the result of the City’s local business preference program, while the remaining 352 contracts would have been awarded to the LBEs even without the preference. While the City Council has enacted reforms to address this issue (as elucidated below), more can be done to capture additional tax revenue and keep it in Los Angeles.

Taxes too often go elsewhere

An unintended consequence of buying from vendors located outside of Los Angeles is that the local government’s share from sales taxes paid by the City goes to other jurisdictions. For example, the City spent \$22.6 million in FY 2020 for asphalt and other related goods and services from a vendor based in Carlsbad, San Diego County. The City paid \$1.4 million in sales taxes for these purchases. Because the vendor is located in Carlsbad, \$150,499 of the \$1.4 million in sales taxes paid was likely allocated to the city of Carlsbad.

Based on our estimate shown below, Council-controlled City departments paid out \$7 million in sales taxes that were allocated to other jurisdictions in California for commodities purchased from FY 2018 to FY 2020. At the same time, the City paid \$4.1 million in sales taxes that were allocated back to the City’s General Fund because they were for commodities purchased from Los Angeles-based vendors.

Estimated Allocation of Local Sales and Use Taxes Paid on Commodities Purchases			
Fiscal Year	LA City	Other CA Jurisdiction	Grand Total
2018	\$1,168,439	\$2,338,901	\$3,507,340
2019	\$1,280,233	\$2,259,637	\$3,539,870
2020	\$1,659,487	\$2,430,421	\$4,089,908
Grand Total	\$4,108,159	\$7,028,960	\$11,137,118
Percentage	37%	63%	100%

Sales tax data from POLA paints a similar picture, which spent \$352.7M on goods and services from FY 2018 to FY 2020, \$66.6M (19%) of which was spent on local vendors within city limits. The result was that \$394,263 in the local share of sales and use taxes was paid out to other jurisdictions, while \$128,544 was allocated back to the City's General Fund. **It is not possible to produce similar estimates for LAWA and LADWP because they do not track sales taxes paid for their transactions.**

Estimated Allocation of Local Sales and Use Taxes Paid on POLA's Purchases			
Fiscal Year	LA City	Other CA Jurisdiction	Grand Total
2018	\$43,523	\$104,218	\$147,740
2019	\$43,277	\$134,093	\$177,370
2020	\$41,745	\$155,952	\$197,697
Grand Total	\$128,544	\$394,263	\$522,807
Percentage	25%	75%	100%

The connection between where the City buys its goods and the allocation rules for sales taxes highlights an important point: **buying from Los Angeles-based businesses not only increases local investment; it increases the City's share of sales tax revenue.**

Reforms help local businesses

Recognizing that where the City spends matters, the Council enacted preference programs designed to increase local business participation in City contracting. Departments can award

certified LBEs and SLBs a preference of up to 8% and 10% respectively during the procurement evaluation process.

However, even with these preference programs, most of the City’s commodities dollars are spent on vendors located outside of Los Angeles. **Between FY 2018 through FY 2020, only 18% of the City’s commodities spending went to vendors within Los Angeles.**

Payments for Commodities Purchases by Vendor Billing Address					
Fiscal Year	LA City	Other LA County Locations	Other CA Locations	Outside CA	Grand Total
2018	\$78,129,743	\$151,096,140	\$90,593,031	\$180,865,508	\$495,672,883
2019	\$84,808,710	\$146,835,222	\$95,294,120	\$175,086,869	\$502,024,921
2020	\$119,530,214	\$127,567,823	\$97,160,122	\$230,549,567	\$574,807,727
Grand Total	\$277,457,128	\$425,499,185	\$283,047,273	\$586,501,944	\$1,572,505,530
Percentage	18%	27%	18%	37%	100%

To further enhance contracting opportunities for local businesses, the City Council has adopted changes to the City’s local business preference program. These changes include:

- Combining the LBE, SLB and Transitional Job Opportunity Programs into a single Local Business preference program.
- Modifying qualifying contract thresholds for the program, giving departments the authority to award up to a 12% preference during the procurement evaluation process.

As Los Angeles is set to host the 2026 World Cup and 2028 Olympic Games, the City and other regional government partners are planning to work together to make these events successful. These combined regional efforts could include significant contracting opportunities. If well-coordinated, contracting by the City, the County and Metro could become the basis for potential cooperative purchasing agreements that combine our collective power in a way that benefits the regional economy.

City Council recommendations

While the City Council recently made changes to the local business preference program, it should also consider increasing the bid preference further to account for the local allocation of sales taxes paid to Los Angeles-based vendors. In addition, changes should be made to the City’s contracts to encourage vendors to use Los Angeles-based locations as the place of sale when possible.

To enact these changes, we propose the following recommendations:

1. INSTRUCT the General Services Department, Bureau of Contract Administration and other related departments to assess the feasibility of incorporating the allocation of the 1% local sales tax into the procurement process. This may be in the form of a 1% price discount during the bid evaluation for qualifying local bidders selling taxable goods to the City or a 1% increase to the maximum bid preference that can be awarded to Local Businesses located in Los Angeles.
2. REQUEST the City Attorney to draft a standard provision to include in the City's contracts that requests vendors to use a City-based location as the principal place of negotiation or shipment whenever feasible, and if doing so does not impose an additional cost to the City and the vendor.
3. REQUEST the Mayor's Chief Procurement Officer to work with the County, Metro and other regional government partners to analyze spending data and identify common purchasing categories that can be used for potential cooperative purchasing agreements in the future.

Department recommendations

In addition, departments should collect information to enhance the City's ability to determine the amount of sales taxes paid out to other jurisdictions and increase local purchasing while recycling sales taxes paid into the General Fund.

1. LAWA and LADWP should begin recording sales taxes paid in their transactions to account for sales taxes paid for local and non-local purchases; and
2. If presented with the same bid scores between a qualified goods vendor located in Los Angeles and other qualified vendors located outside of the City, departments should choose a vendor located in Los Angeles in order to increase local investment and maximize the amount of local sales taxes allocated back to the City.

The City has an opportunity to increase local purchasing by adopting and implementing these recommendations. We can support local businesses and recycle an increasing share of sales taxes paid into our General Fund, which will benefit all Angelenos.

Respectfully submitted,



RON GALPERIN
L.A. Controller