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September 12, 1985

ATTORNEY GENERAL OPINION NO. 85-121

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Kansas City, Kansas 66101

Re: Cities and Municipalities -- Ordinances of Cities -- Validity of Local Preference Legislation

Synopsis: Where a city has exempted itself from all statutory restrictions relating to the procurement of goods and services, it is not required to let procurement contracts to the lowest bidder. Under such circumstances, the governing body may exercise unlimited discretion in procuring its needs, so long as it is not guilty of fraud. Therefore, such a city may negotiate contracts with vendors chosen by the council; adopt an ordinance prescribing residency qualifications which must be satisfied by prospective bidders; or enact an ordinance which prescribes a percentage preference in favor of resident bidders. Additionally, where a city expends only its own funds entering into such procurement contracts, the above-described local preference legislation would not violate the Commerce Clause, Equal Protection Clause or First Amendment to the United States Constitution. However, such legislation is subject to scrutiny under the Privileges and Immunities Clause of the United States Constitution, and a city must present sufficient justification for

discrimination against nonresidents who wish to transact business with the city.

K.S.A. 75-6111 confers authority upon municipalities to obtain tort liability insurance through negotiation, and no Kansas law requires cities to obtain insurance through competitive bidding. Under such circumstances, a city may provide for its insurance needs through negotiation, and the award of insurance contracts pursuant to a negotiation process does not, in and of itself, violate anti-trust laws. Cited herein: K.S.A. 13-1017, 50-101, 75-3740a, 75-6111; L. 1985, ch. 181; Kan. Const., Art. 12, §5; 15 U.S.C. §§1, 15, 15a, 15c, 34, 35, 36; U.S. Const., Art. I, Sec. 8, cl. 3; Art. IV, Sec. 2, cl. 1; 1st Amend.; 14th Amend.

* * *

Dear Mr. Watson:

You indicate that council members of the City of Kansas City have expressed an interest in procurement legislation favorable to local vendors, and request our opinion regarding several legal issues raised by such legislation. Your questions, and our responses thereto, are set forth below.

"1. Having already made the only Kansas statute mandating competitive public bidding (K.S.A. 13-1017) inapplicable to this city by charter ordinance No. 82, does Kansas state law allow the city of Kansas City, Kansas, to procure services, construction, and products, and make all other procurements paid for with non-federal dollars, simply by negotiating contract terms with and by awarding contracts to contractors and vendors chosen by the city for reasons personal to the council members, or to contractors and vendors chosen by the city who are either (1) bona fide residents and domiciliaries of Kansas City, Kansas; or (2) a partnership or association, each member of which is a bona fide resident and domiciliary of Kansas City, Kansas; or (3) a corporation which has been organized under the laws of Kansas or is authorized to do business in Kansas and which has its principal place of business within Kansas City, Kansas?"

K.S.A. 13-1017, which applies to cities of the first class having the mayor-council form of government, prescribes that improvement contracts in excess of $2,000 shall be let by competitive bidding. However, you indicate that the City of Kansas City has adopted a charter ordinance exempting itself from the provisions of K.S.A. 13-1017, and has reimposed competitive bidding requirements through a separate ordinary ordinance adopted under home rule powers. You indicate that this latter ordinance would be repealed if the city chose to negotiate contracts with vendors selected by the council.

In Case-Bros. v. City of Ottawa, 226 Kan. 648 (1979), the Kansas Supreme Court considered the legal requirements for letting of a construction contract by a city of the second class having the commission-manager form of government. The court noted that there was no statutory requirement that such a city use any bidding process in entering into a public improvement contract, and held as follows at Syllabus ¶1:

> "Where no statutory conditions or restrictions are imposed upon municipal officers in the matter of letting contracts, they are not obliged to let the work to the lowest bidder. They may exercise an unlimited discretion so long as they are not guilty of fraud."

In our judgment, the above-quoted rule is applicable to a city which has enacted a valid charter ordinance exempting itself from statutory restrictions upon the letting of contracts for public improvements. Accordingly, in our opinion where a city has exempted itself from all statutory restrictions relating to the procurement of goods and services, the city is not required to let procurement contracts to the lowest bidder. Under such circumstances, the governing body may exercise an unlimited discretion in procuring its needs, so long as it is not guilty of fraud.

"2. If the City of Kansas City, Kansas, opts to require competitive public bidding, does Kansas state law allow it to limit the bidders on its procurements of services, construction, and products, and all other procurements, to bidders who are either (1) bona fide residents and domiciliaries of Kansas City, Kansas; or (2) a partnership or association, each member of which is a bona fide resident and domiciliary of Kansas City, Kansas;

or (3) a corporation which has been organized under the laws of Kansas or is authorized to do business in Kansas and which has its principal place of business within Kansas City, Kansas?"

As indicated in the City of Ottawa case, supra, the governing body is vested with an unlimited discretion in letting procurement contracts. Accordingly, it may adopt an ordinance requiring competitive bidding, but prescribing qualifications of bidders in the manner you suggest.

"3. If the city of Kansas City, Kansas, opts to require competitive public bidding, may it incorporate into its competitive public bidding procedures a percentage preference of 5% in favor of bidders who are either (1) bona fide residents and domiciliaries of Kansas City, Kansas; or (2) a partnership or association, each member of which is a bona fide resident and domiciliary of Kansas City, Kansas; or (3) a corporation which has been organized under the laws of Kansas or is authorized to do business within Kansas City, Kansas, and which has its principal place of business within Kansas City, Kansas?"

For the reasons set forth in our response to question number 2, it is our opinion that the governing body may, pursuant to home rule powers granted by Article 12, §5 of the Kansas Constitution, adopt an ordinance providing for the percentage preference which you describe.

"4. Does the city of Kansas City, Kansas, run afoul of any of the following United States constitutional provisions if it adopts as policy any of the restrictions set out in questions 1, 2, or 3, above:

A. The Commerce Clause, U.S. Constitution, Art. I, Sec. 8, cl, 3."

The Commerce Clause of the United States Constitution, Article I, Section 8, Clause 3, states:

> "The Congress shall have the power . . . to regulate commerce with foreign nations and among the several states."

Recently, the United States Supreme Court upheld an executive order of the Mayor of Boston that construction projects funded in whole or in part by city funds be performed by a work force consisting of at least half bona

fide residents of Boston on the basis that (1) when a state or local government enters the market as a "participant" rather than as a "regulator," it is not subject to the restraints of the Commerce Clause; (2) insofar as the City expended only its own funds in entering into construction contracts for public projects, it was a market participant; (3) impact on out-of-state residents figures in the equation only after it is decided that the City is regulating the market rather than participating in it; and (4) only in the latter case need it be determined whether any burden on interstate commerce is permitted by the Commerce Clause. Kevin H. White, etc., et al. v. Massachusetts Council of Construction Employers, Inc., et al., 460 U.S. 204, 75 L.Ed.2d 1, 103 S.Ct. 1042 (1983).

The Court in White, supra, also stated, however:

> "Respondents ask us to decide whether the executive order offends the Privileges and Immunities Clause of Art. IV, §2, cl. 1, which provides: 'The Citizens of each State shall be entitled to all Privileges and Immunities of Citizens in several States.' . . . This question has not been, to any great extent, briefed or argued in this Court. We did not grant certiorari on the issue and remand without passing on its merits."

"B. Privileges and Immunities Clause." In 1984, a year after White, the United States Supreme Court decided a case involving a nearly identical fact situation to that found in White, but this time on the basis of the Privileges and Immunities Clause. Article IV, Section 2, Clause 1 of the U.S. Constitution, states:

> "The citizens of each state shall be entitled to all the Privileges and Immunities of Citizens in the several states."

In the case of United Building and Construction Trades Council of Camden County and Vicinity v. Mayor and Council of the City of Camden, et al., ___U.S.___, 79 L.Ed.2d 249, 104 S.Ct. 1020 (1984), the Court held that an ordinance of the City of Camden requiring that at least 40% of the employees and subcontractors working on city construction projects be Camden residents, is subject to

the Privileges and Immunities Clause. It further held that (1) a municipal ordinance is as much subject to the clause as is a state statute; (2) that the clause applies not only to laws that discriminate on the basis of state citizenship, but also to laws that discriminate on the basis of municipal residency; (3) the fact that in-state residents who do not live in Camden have no remedy under the clause, while out-of-state residents do, does not immunize the ordinance from constitutional review; (4) on remand, there must be a determination made of whether the ordinance burdens one of those privileges and immunities protected by the Clause, and if so, whether there is a "substantial reason" for the discrimination against citizens of other states. The Court stated:

> "As a part of any justification offered for the discriminatory law, nonresidents must somehow be shown to 'constitute a peculiar source of the evil at which the statute is aimed.'" 79 L.Ed.2d at 261.

Finally, the Court distinguishes the Commerce Clause from the Privileges and Immunities Clause in justifying the different conclusion it reached here than in White, supra:

> "The Commerce Clause acts as an implied restraint upon state regulatory powers. Such powers must give way before the superior authority of congress to legislate on (or leave unregulated) matters involving interstate commerce. When the state acts solely as a market participant, no conflict between state regulation and federal regulatory authority can arise. [Citations omitted]. The Privileges and Immunities Clause, on the other hand, imposes a direct restraint on state action in the interests of interstate harmony. [Citations omitted] This concern with comity cuts across the market regulator-market participant distinction that is crucial under the Commerce Clause. It is discrimination against out-of-state residents on matters of fundamental concern which triggers the clause, not regulation affecting

> interstate commerce. Thus, the fact that Camden is merely setting conditions on its expenditures for goods and services in the marketplace does not preclude the possibility that those conditions violate the Privileges and Immunities Clause." 79 L.Ed.2d at 259.

You suggest that the restrictions theorized in questions 1, 2 and 3, above, could be justified by the governing body of the City of Kansas City, Kansas, on the following grounds:

> "(1) the people of the city are benefitted when purchases are made from residents; (2) spending tax revenues within the city will promote new industry, reduce unemployment, and eventually increase the tax base of the city; (3) profits made on the transaction by local businesses will be taxed by the City and State, thus offsetting the higher purchasing costs; (4) wages paid to resident workers will be taxed in the City and State, generating even more tax revenues and further encouraging the local economy; (5) even more tax revenue will be generated through indirect suppliers and their employees and shareholders."

While the above-stated justifications may be valid, we are unable to conclude as a matter of law that they are sufficient reasons for discrimination under the Privileges and Immunities Clause. Specifically, three courts have held that, in order to justify a law which discriminates against nonresidents, data must be presented which compares the savings resulting from such a law (i.e., lower unemployment, secondary economic activity. etc.) with the costs which are associated therewith (i.e., higher bids on public works projects). W.C.J. Window Co., Inc. v. Bernardi, 730 F.2d 486, 498 (7th Cir. 1984); Laborers Local Union No. 374 v. Felton Const., 654 P.2d 67, 70 (Wash. 1982); Neshaming Constructors, Inc. v. Krause, 437 A.2d 733 (N.J. Superior Ct. 1981). Accordingly, the determination of whether nonresidents "constitute a peculiar source of evil" under a law establishing a local preference in the award of city contracts is a mixed question of law and fact, and such a question must be

presented to a trier of fact to determine whether there is any violation of the Privileges and Immunities Clause.

"C. Equal Protection." A number of courts have upheld statutory in-state purchasing preferences against equal protection challenges. Galesburg Const. Co. v. Board of Trustees, 641 P.2d 745 (Wyo. 1982); Equitable Shipyards, Inc. v. State, 611 P.2d 369 (Wash. 1980); Denver v. Bossie, 266 Pac. 214 (Colo. 1928); State ex rel. Collins v. Senatobia Blank Book and Stationery Co., 76 So. 258 (Miss. 1917). It has been held that local preference legislation requires only "rational basis scrutiny" under the equal protection clause, and that the encouragement of local industry is a legitimate state interest to which local preferences are rationally related. See Galesburg Const. Co. v. Board of Trustees, supra; Equitable Shipyards, Inc. v. State, supra. Accordingly, in our judgment the local preferences theorized in questions 1, 2, and 3, above, would not violate the Equal Protection Clause.

"D. First Amendment." Although the U.S. Supreme Court held in Elrod v. Burns, 427 U.S. 347, 49 L.Ed.2d 547, 96 S.Ct. 2673 (1976), and Branti v. Finkel, 445 U.S. 507, 63 L.Ed.2d 574, 100 S.Ct. 1287 (1980), that the discharge of non-policymaking public employees solely because of their political beliefs violates the First Amendment, the protections of that amendment have not been extended by the courts to public contractors. La Falce v. Houston, 712 F.2d 292 (7th Cir. 1983). See also Horn et al. v. Kean et al., 593 F.Supp. 1298 (D. N.J. 1984). Therefore, in our judgment a city does not violate the First Amendment by negotiating city contracts with vendors chosen by the city council, or by enacting residency qualifications or percentage preferences in favor of resident bidders.

"5. Does the city of Kansas City, Kansas, run afoul of federal or state antitrust laws if it adopts as policy any of the restrictions set out in questions 1, 2, or 3, above?"

None of the theorized restrictions contained in question nos. 1, 2, and 3, above, run afoul of the Sherman Act, 15 USC §1, et seq., nor of the Clayton Act, 15 U.S.C. ¶15, nor of Kansas restraint of trade statutes, K.S.A. 50-101 et seq. The Local Government Anti-Trust Act of 1984, 15 U.S.C. ¶¶34-36, immunizes cities from claims

for damages brought under the Sherman and Clayton Acts, but not from injunctive relief. Likewise, Chapter 181 of the 1985 Session Laws of Kansas immunizes Kansas cities from claims for damages brought under the Kansas Restraint of Trade Statutes, but not from injunctive relief.

In the case of Security Fire Door Company v. County of Los Angeles, 484 F.2d 1028 (9th Cir. 1973) plaintiff alleged a conspiracy among the county, county architect and a supplier of a dumb waiter system in violation of the Sherman Act when the county architect and supplier allegedly prepared specifications for the system in a manner which: (1) excluded from public competition all manufacturers of dumb waiters except the defendant supplier; (2) discriminated against all manufacturers except the defendant supplier; and (3) created a facade of free competition when in fact there was none. The court held that such acts may constitute a violation of the competitive bid statutes in California, but did not create an anti-trust problem. The court stated:

> "Once a purchaser's choice of product has been exercised competition is, of course, at an end. However, a purchaser is free to choose the product he desires without rendering himself an antitrust conspirator. The proscription against restraint of trade in this context seeks only to assure that the choice of product has been made freely under circumstances where the play of competition has been available rather than in response to anticompetitive factors such as coercion on the part of the supplier or agreements between suppliers not to compete with each other. If anticompetitive factors have foreclosed a free choice by the purchaser, he is not thereby converted into a conspirator. He is, instead, a victim.
>
> "Here the choice of product by the purchaser, Los Angeles County, was expressed in the specifications. There is nothing alleged in the complaint to suggest that this choice was made other than in an atmosphere of free competition among suppliers. So far as the complaint alleges, each supplier was perfectly free

> to tout the virtues of his particular dumbwaiter system in an effort to secure favorable specifications. It would appear that the architects simply favored the Guilbert system. In doing so they and their principals can hardly be charged with an antitrust conspiracy.
>
> "Security's complaint appears to be that under California's competitive bid statute the choice should not have been made at that time, and it should not have been based upon the characteristics and features specified as desirable; rather the choice should have awaited the outcome of the bidding procedure, and it should have been based upon factors of cost.
>
> "The competitive bid statute may well serve to limit the freedom of public purchasers to make specific choices on the basis of preference rather than cost. However, a violation of the letter or spirit of a competitive bid statute, unaccompanied by anti-competitive factors bearing upon the exercise of choice of product, does not create an antitrust problem. Even a direct contract for the Guilbert system, without any pretense of putting the job out to bid (and thus a clear violation of the competitive bid statute), would not in itself have constituted a restraint of trade under the Sherman Act if the selection of Guilbert had been made in an atmosphere free from anticompetitive restraints." 484 F.2d at 1030-31.

However, see also Richard Hoffman Corporation v. Integrated Building Systems, Inc., 581 F.Supp. 367 (N.D. Ill. 1984), wherein the court indicates that collusion between a city and a contractor with respect to the bidding process runs afoul of the Sherman Act.

"6. A. If the city of Kansas City, Kansas, incorporates into its competitive public bidding procedure a percentage preference of 5% in favor of bidders who are either (1) bona fide residents and domiciliaries of

Kansas City, Kansas; or (2) a partnership or association, each member of which is a bond fide resident and domiciliary of Kansas City, Kansas; or (3) a corporation which has been organized under the laws of Kansas or is authorized to do business in Kansas and which has its principal place of business within Kansas City, Kansas, would Vernon's Annotated Missouri Statutes, 1984 Supp., §34.076 require Missouri cities, such as Kansas City, Missouri, as well as the State of Missouri, to likewise incorporate into their competitive public bidding procedures a percentage preference of 5% in favor of Missouri bidders and against Kansas City, Kansas, bidders?

"B. If the city of Kansas City, Kansas, procures services, construction and products, and makes all other procurements paid for with non-federal dollars simply by negotiating contract terms with and awarding contracts to contractors and vendors chosen by the city who are either (1) bona fide residents and domiciliaries of Kansas; or (2) a partnership or association, each member of which is a bona fide resident and domiciliary of Kansas City, Kansas; or (3) a corporation which has been organized under the laws of Kansas and is authorized to do business in Kansas, and which has its principal place of business within Kansas City, Kansas, would Vernon's Annotated Missouri Statutes, 1984 Supp., §34.076 require Missouri cities, such as Kansas City, Missouri, as well as the State of Missouri, to likewise incorporate into their competitive public bidding procedures a total prohibition against Kansas City, Kansas, bidders?

"C. Does K.S.A. 75-3740a require the city of Kansas City, Kansas, to likewise retaliate against contractors and vendors from Missouri jurisdictions which incorporate into their competitive public bidding procedures a percentage or other type of preference in favor of contractors and vendors domiciled in that jurisdiction."

If the City of Kansas City, Kansas, adopts as policy any of the restrictions contained in question nos. 1, 2 or 3, above, V.A.M.S. 1984 Supp. §34.076 will come into play. It states:

> "34.076. Missouri contractors, public works, preference, when, exceptions -- minority employment required, when
> 1. To the extent permitted by federal laws and regulations, whenever the state

> of Missouri, or any department, agency or institution thereof or any political subdivision shall let for bid any contract to a contractor for any public works or product, the contractor or bidder domiciled outside the boundaries of the state of Missouri shall be required, in order to be successful, to submit a bid the same percent less than the lowest bid submitted by a reasonable contractor or bidder domiciled in Missouri as would be required for such a Missouri domiciled contractor or bidder to succeed over the bidding contractor or bidder domiciled outside Missouri on a like contract or bid being let in his domiciliary state and, further, the contractor or bidder domiciled outside the boundaries of Missouri shall be required to submit an audited financial statement as would be required of a Missouri domiciled contractor or bidder on a like contract or bid being let in the domiciliary state of that contractor or bidder.
>
> "2. Subsection 1 of this section shall not apply to any contractor who is qualified for bidding purposes with the department of highways and transportation and submits a successful bid wherein part of or all funds are furnished by the United States.
>
> "3. Subsection 1 of this section shall not apply to any public works or product transportation where the bid is less than five hundred dollars."

So long as the City of Kansas City, Kansas, and its citizenry are willing to live with the consequences, neither K.S.A. 75-3740a nor any other Kansas statute prohibits the city from imposing the restrictions theorized in question nos. 1, 2 and 3 above. It does appear, however, that the above quoted Missouri statute applies not only when the State of Kansas might adopt a preference system for local bidders, but also when the City of Kansas City, Kansas, might do so. It further appears that if the city of Kansas City, Kansas, totally excludes non-local

bidders from bidding, that Missouri jurisdictions must do likewise vis-a-vis Kansas City, Kansas bidders. Finally, should the City of Kansas City, Kansas, learn that a Missouri jurisdiction has adopted a local preference, the City of Kansas City, Kansas, must retaliate in kind pursuant to K.S.A. 75-3740a.

"7. Specifically in reference to the purchase of insurance, may the City of Kansas City, Kansas, divide its insurance needs into areas -- such as, automobile liability and worker's compensation as one area, and property and casualty insurance as another area -- and then simply select a local insurance agent or agents on a noncompetitive bid basis to render advice as to the types and amounts of coverages needed in each area and to provide such insurance to the city? By doing so, does the city of Kansas City, Kansas, run afoul of Kansas law, any of the United States Constitutional provisions set out in question No. 4, above, or of the federal or state antitrust laws?"

K.S.A. 75-6111 specifically confers authority upon municipalities to obtain tort liability insurance through negotiation, and no Kansas statute requires cities to obtain insurance through competitive bidding. Under such circumstances, a city may provide for its insurance needs through negotiation. [See Case-Bros. v. City of Ottawa, supra], and the award of insurance contracts pursuant to a negotiation process does not, in and of itself, violate anti-trust laws. See Security Fire Door Company v. County of Los Angeles, supra. Additionally, we are unaware of any law which would prohibit a city from awarding separate contracts for the different classes of insurance coverage which it purchases. However, any participation by a city in agreements by competitors (in this case insurance agencies) which affect the manner in which they allocate or compete for business would violate state and federal anti-trust laws.

In conclusion, where a city has exempted itself from all statutory restrictions relating to the procurement of goods and services, it is not required to let procurement contracts to the lowest bidder. Under such circumstances,the governing body may exercise unlimited discretion in procuring its needs, so long as it is not guilty of fraud. Therefore, such a city may negotiate contracts with vendors chosen by the council; adopt an ordinance prescribing residency qualifications which must be satisfied by prospective bidders; or enact an ordinance

which prescribes a percentage preference in favor of resident bidders. Additionally, where a city expends only its own funds entering into such procurement contracts, the above-described local preference legislation would not violate the Commerce Clause, Equal Protection Clause or First Amendment to the United States Constitution. However, such legislation is subject to scrutiny under the Privileges and Immunities Clause of the United States Constitution, and a city must present sufficient justification for discrimination against nonresidents who wish to transact business with the city. K.S.A. 75-6111 confers authority upon municipalities to obtain tort liability insurance through negotiation, and no Kansas law requires cities to obtain insurance through competitive bidding. Under such circumstances, a city may provide for its insurance needs through negotiation, and the award of insurance contracts pursuant to a negotiation process does not, in and of itself, violate anti-trust laws.

Very truly yours,

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