

# EXECUTIVE SUMMARY



## SIZE STANDARD EVALUATION

June 2015

# Rationale for Evaluation

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The Central Certification CERT Program (“CERT Program”), governed by the Central Certification CERT Program Collaborative Joint Powers Agreement Executive Board (“Executive Board”)<sup>1</sup>, has historically determined small business status by applying the size standards promulgated by the State of Minnesota Department of Administration (“Department of Administration”) Materials Management Division (“MMD”). In late 2013, the Department of Administration modified its standard (“Current MMD Standard”) for determining whether a business is a small business. Had the CERT Program adopted the Department of Administration’s new size standards, it would have rendered a significant number of businesses, formerly certified as “small,” ineligible to be re-certified as Small Business Enterprises. The CERT Executive Board sought to avoid this detrimental impact, viewing it as incompatible with the CERT Program’s mission of promoting the growth and development of local small, minority-owned, and women-owned businesses. Therefore, the CERT Program froze the Department of Administration’s previous small business size standards (“2012 MMD Standard”) and undertook an evaluation of the potential impact of adopting the Department of Administration’s new size standards.

## Overview: Methodology

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In order to determine which size standard best reflects the current marketplace for the local small businesses represented in the CERT Program, the following items were evaluated:

1. The process by which the Department of Administration determines its size standards.
2. The pool of businesses evaluated to determine the Department of Administration’s size standards.
3. The businesses within the CERT Program:
  - a. Every Sector represented in the CERT Program was evaluated to determine how many businesses are in each Sector;
  - b. Every NAICS Code reported by CERT businesses was evaluated to determine:
    - i. The average gross receipts (“AGR”)<sup>2</sup> for businesses per NAICS code; and
    - ii. The number of businesses per NAICS code.
4. The 2012 MMD Standard, Current MMD Standard, and SBA Size Standard (collectively, “code sets”) were each evaluated against the current businesses reported in the CERT Database to determine the impact of adopting each Code Set.

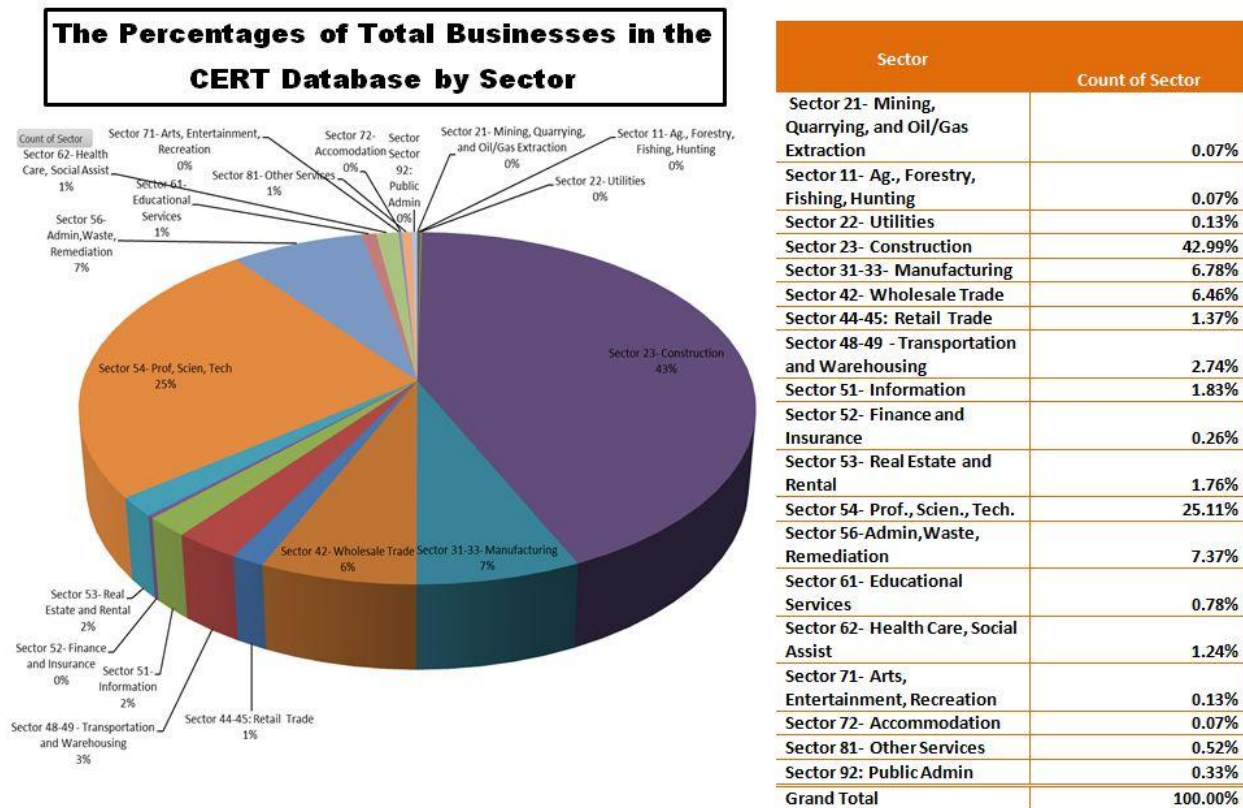
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<sup>1</sup> Central Certification CERT Program Collaborative Joint Powers Agreement Executive Board consists of representatives from the City of Saint Paul, Hennepin County, and Ramsey County.

<sup>2</sup> The Average Gross Receipts are the total amounts the organization received from all sources during its annual accounting period, without subtracting any costs or expenses. To determine whether a business is small, for the CERT Program, 3 years of gross receipts are averaged and that number is compared with the applicable size standard.

# Overview: Data Findings

At the time of evaluation, the CERT database comprised of 1,232 businesses.<sup>3</sup> There are a total of 252 NAICS codes (“code”) reported by CERT businesses in 24 Sectors. The CERT businesses have reported these codes as a primary or secondary code. Primary and secondary codes are evaluated during the certification process. The size standard associated with the primary code reported determines whether the reporting business will be considered small by that size standard and eligible for certification. Secondary codes are reported to note additional business activity, not considered primary. Appendix 1 below provides a view of the makeup of the CERT Program by Sector.



The data supports a finding that 6.3 % (99 CERT certified businesses) under the NAICS codes evaluated would graduate upon a move to the Current MMD standard. The data also supports a finding that 0.7% (11 CERT certified businesses) under the NAICS codes evaluated would graduate upon a move to the SBA standard. Appendix 2 below exhibits the number of businesses that would graduate per Sector, by Code Set, if adopted.

<sup>3</sup>During the 1<sup>st</sup> Quarter of 2014, the CERT database was reviewed for accuracy of data in the system. During this review, reports were pulled and reviewed for accuracy. After all the data was reviewed and the system updated accordingly, the most recent and accurate available data was pulled for this report. As a result, the 1,232 businesses represented in this report represent the CERT Database as of December 17, 2014. Since then, the database has continued to grow.

**Appendix 2. Project Number of Businesses to Graduate by Code Set**

NAICS Code Sector	# Graduated from Current MMD	# Graduated from SBA
Sector 11- Ag., Forestry, Fishing, Hunting	0	0
Sector 21- Mining, Quarrying, and Oil/Gas Extraction	0	0
Sector 22- Utilities	0	0
Sector 23- Construction	75	11
Sector 31-33- Manufacturing	7	0
Sector 42- Wholesale Trade	4	0
Sector 44-45: Retail Trade	1	0
Sector 48-49 - Transportation and Warehousing	1	0
Sector 51- Information	1	0
Sector 52- Finance and Insurance	0	0
Sector 53- Real Estate and Rental	0	0
Sector 54- Prof., Scien., Tech.	8	0
Sector 56-Admin,Waste, Remediation	2	0
Sector 61- Educational Services	0	0
Sector 62- Health Care, Social Assist	0	0
Sector 71- Arts, Entertainment, Recreation	0	0
Sector 72- Accommodation	0	0
Sector 81- Other Services	0	0
Sector 92: Public Admin	0	0
Grand Total	99	11

The report divides the 252 NAICS codes reported into the 24 Sectors represented in the CERT database. Each Sector reported:

1. Provides an overview of that Sector's business makeup.
2. Evaluates the impact on CERT businesses if the
  - a. Current MMD Standard were adopted;
  - b. 2012 MMD standard remained in effect; and
  - c. SBA standard were adopted.
3. Each NAICS code reported received an evaluation as to how close CERT businesses are to the respective size standard.
  - a. This evaluation notes businesses that within \$5 million, \$10 million, or \$15 million of the size standard; or
  - b. Businesses within \$1 million, \$3 million or \$5 million of the size standard.

For codes where no size standard has been set by the 2012 MMD, Current MMD, or SBA standards, if a business has reported that code as a primary or secondary code, it is included in the report. The business total will be noted, but, since no size standard exists for those codes, the impact could not be evaluated. This was done in an effort to ensure that all CERT businesses received an evaluation by NAICS code, where it can be done.

## Executive Board Determination

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Upon reviewing the findings, the Executive Board has made the following determinations:

1. To adopt the SBA Size Standard;
2. To pilot, for Sector 23 businesses, a “provisional status” available for graduating, or recently graduated Small Business Enterprises; and
3. During a 6 month planning phase, to create an implementation plan for implementing (1) the SBA standard and (2) the “provisional status”.

### Rationale for Adopting the SBA Size Standard

The SBA Size Standard provides a process that allows for determining whether a business is small by both AGR and/or number of employees. The SBA's rationale behind this flexibility is to allow for industry standards which “best represent the magnitude of operations of a business.” This rationale is aligned with the goal of the CERT Program. In addition, the SBA standard provides the following, which further aligns with the CERT Program:

1. Data used in determining the size standards is pulled directly from the 2002 Economic Census administered by the U.S. Census Bureau;
2. Specific benchmarks for determining the size standards, by industry, exist.<sup>4</sup>

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<sup>4</sup> There are three different “anchor size standards”: \$7.0 million for the services, retail trade, construction, and other industries with receipts based size standards, 500 employees for the manufacturing, mining and other industries with employee based size standards. “Anchor size standards” are essentially the benchmarks for SBA analysts in determining size standards. After establishing anchor standards for aggregate sectors (i.e. Sector 23-Construction), analysts can look at individual codes (i.e. 236115- Residential Building Construction,) and determine whether or not the processes behind the execution or production of those services or goods display ‘differing industry characteristics’ based on primary and secondary factors. Primary factors include: 1) Average firm size 2) Degree of competition within an industry 3) Start-up costs and entry barriers 4) Distribution of firms by size and 5) Small business share in Federal

## Rationale for the “Provisional Status”

It is the CERT Program mission to maximize opportunities for local small businesses through exceptional services, innovative practices, strategic partnerships, and ensuring social and economic justice to our local small businesses. As a local program, the CERT Program supports our local economic base. In the spirit of providing social and economic justice to our local small businesses, the CERT Program seeks to build and support small businesses to position them for the competitive marketplace. In an effort to best do this, the CERT Program needed to (1) be transparent with the changes taking place and (2) hear from the community ultimately impacted as it relates to what would best further our mission to support local small businesses.

The Executive Board met with various community stakeholders<sup>5</sup> The Executive Board also received feedback through surveys administered throughout the community. Through this feedback, concerns were presented as it relates to having a more restricted or more liberal size standard. The main concern pertains to capacity; capacity for the small businesses remaining in the program and capacity for businesses that would graduate out of the program.

As it relates to the capacity of the small businesses remaining in the program the CERT Program seeks to maximize opportunities for these businesses, while seeking to avoid the problem of having businesses grow too fast to the point where they are struggling. In the case of capacity for businesses graduating out of the CERT Program, the CERT program strives to better position these businesses to compete with the larger businesses in the marketplace.

As such, this program supports the creation of a “provisional status”. The rationale behind the “provisional status” is that those businesses that recently graduate out of the CERT Program are uniquely positioned to provide opportunities for local small businesses that could positively impact our local economic marketplace. In addition, such businesses may not yet be quite ready to compete with larger businesses in the same industry. As a result, the “provisional status” could provide a more streamlined pipeline from growth out of small business programs to a competitive position in the private sector. Appropriately positioning businesses to compete in the private sector, rather than setting them up for failure is a value of the CERT Program.

The “provisional status” would allow a recently graduated business to continue maintaining a certification status, provided it met specific criteria. The specific criteria for this status will be further developed during the implantation phase, noted below. A “provisional status” business would hold this status for a defined period of time. Below are suggested points of emphasis under which the “provisional status” criteria will be developed. In consideration for the provisional status, a business would:

1. Demonstrate a level of participation of other local small businesses<sup>6</sup>, on projects, both private and public sector, where subcontracting opportunities existed.
2. Provide documentation exhibiting inclusion of women and minorities in the business’ workforce.
3. Foster a mentor-protégé relationship with other small businesses.
4. Report both public and private sector business and workforce inclusion efforts.

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contracts. Secondary factors include: 1) Technological change, 2) Competition among industries 3) Industry growth trends, and 4) The impacts on SBA programs. To the extent that they do, the size standard for that individual code will be lower or higher than the anchor.

<sup>5</sup> Between January and June of 2015, the Executive Board met with associations such as the Association of Women Contractors, Associated General Contractors of Minnesota, Minnesota Sports Facilities Authority, and the National Association of Minority Contractors. In addition, surveys were created by working with community stakeholders, as well as the Federal Reserve Bank of Minneapolis.

<sup>6</sup> The CERT Program is a small business inclusion program. As such, all businesses that are CERT certified must be local, small businesses. Encompassed within this local, small business inclusion program are minority-owned business enterprise (MBE) and woman-owned business enterprise (WBE) certification designations.

The provisional status designation will be piloted on Sector 23. The rationale for this is because Sector 23 saw the greatest changes with the shift to the new applicable size standard.

### 6-Month Implementation Planning Phase

The effective date for these changes will be January 1, 2016. In an effort to support a smooth transition, the Executive Board has determined that a 6-month implementation phase for these changes will occur. During this implementation phase:

1. The provisional status criteria will be further developed with community outreach and input;
2. Businesses that will come upon recertification will be held to the 2012 MMD standard ;
3. Businesses applying for new certification will be held to the 2012 MMD standard.; and
4. If a business has graduated since February 20, 2014, the date of the first Executive Board Resolution pertaining to the size standard evaluation, on January 1, 2016, such a business may apply to be considered for a “provisional status”.