

HOUSE RESEARCH

September, 1985

Information Brief

Douglas Wilson, Legislative Analyst
296-9253

MINNESOTA'S SMALL BUSINESS PROCUREMENT ACT

Minnesota's Small Business Procurement Act, also referred to as the Set-Aside Program, was enacted in 1975 to ensure that small businesses receive a share of state procurement contracts. The program is now seen as an economic development tool to aid small businesses in general and specifically those small businesses that are owned and operated by socially or economically disadvantaged persons.

This Information Brief describes the program (pp. 1-3), explains how it is administered (pp. 4-5), and summarizes the results of the program (pp. 5-6). An appendix is also included which lists the major changes in programs made by the 1984 and 1985 Legislature.

DESCRIPTION OF THE SMALL BUSINESS PROCUREMENT ACT

The Act is Intended to Help Two Types of Businesses

1. Small business:

- A for-profit business entity not affiliated with or subsidiary of a business dominant in its field
- A business having 20 or fewer full-time employees, or not more than the equivalent of \$1,000,000 in annual gross revenues

2. SED business:

- A small business owned and operated by a "socially or economically disadvantaged person" (SED business), defined as a person who has been "deprived of the opportunity to develop and maintain a competitive position in the economy because of social or economic factors"
- These SED businesses include: businesses owned and operated by minorities (Black, Hispanic, Asian, Alaska Native, and Indian), women, persons who have suffered a substantial physical disability, and businesses in a federally designated labor surplus area
- For the purposes of the Small Business Procurement Act, SED businesses include sheltered workshops and work activity programs.

The Act Comprises Three Components

This description is of the current law, including the changes made by the 1985 Legislature. A description of changes made by the Legislature in 1984 and 1985 is found in Appendix 1, page 7.

1. Procurement of Goods and Services

- At least 25 percent of the value of anticipated total state procurement made by the Procurement Division of the Department of Administration must be awarded to small businesses. These contracts are not set aside for small business, but state procurement is monitored to determine if statutory requirements are met.
- At least nine percent of the value of total procurement by the Department of Administration must be awarded, if possible, to SED businesses. (The six percent is part of, not in addition to, the 25 percent requirement since SED businesses are also small businesses by definition.) At least three percent of all procurement must be set aside for bidding by only SED businesses. The remaining portion of the goal may be attained through a program where a five percent preference in bids is allowed for SED businesses, the set aside mechanism or other bidding process authorized by Chapter 16B.
- If SED businesses are not to account for the nine percent goal, contracts shall be awarded to other small businesses.

2. Consultant, Professional and Technical Services

- Every state agency must designate at least 25 percent of the value of anticipated procurements for consultant, professional or technical services for award to small businesses with their principal place of business in Minnesota.
- At least six percent of the procurement for consultant, professional or technical services must be set aside for SED businesses. This six percent is part of, not in addition to, the 25 percent requirement since SED businesses are defined as small businesses.

3. Certain Contracts over \$200,000

- In contracts for construction or for consultant, professional or technical services in excess of \$200,000 awarded by state agencies, at least ten percent of the value of the contract must be subcontracted to a SED business or at least ten percent of the value of the contract must be expended for purchases of materials or supplies from SED businesses.
- If there are not SED businesses that may satisfactorily subcontract ten percent of the value of the total contract or supply materials or supplies, the ten percent requirement must be made up in the award of other contracts by the same agency.
- This ten percent requirement does not apply when the prime contractor is a SED business.

Statutory Controls on the Program

1. Equitable Allocation of Benefits

- The Department of Administration must attempt to vary the designated procurements for goods and services so that a variety of goods and services are supplied to the state by small business and a proportional geographic distribution of awards is attempted.
- The commissioner may not designate more than 20 percent of any commodity class for set-aside or preference awards for SED businesses.
- A SED business is no longer eligible for the set-aside or preference programs if the business has already been awarded more than three-tenths of one percent of the total value of procurements made by the Department of Administration in any fiscal year.
- SED businesses are eligible to participate under this program for a maximum period of five years after the receipt of their first award and are not eligible to participate in the program again for a period of five years. This limitation does not apply to sheltered workshops or work activity programs.
- At least 50 percent of the value of the contract awarded to a SED business must be performed by that business or another SED business.
- Brokers and third party lessors are not eligible to participate in these programs.

2. Performance and Cost

- Prior to making an award under the set-aside or preference program, the commissioner must evaluate whether the SED business can produce or perform the product or service.
- The cost of the procurement under a set-aside program must not exceed five percent over the estimated cost of the goods or services if purchased in the open market.
- All other laws and rules pertaining to solicitations, bid evaluations, contract awards, and other procurement matters apply equally to set aside and preference awards for small businesses.

ADMINISTRATION OF THE PROGRAM

Responsible Agencies

The Department of Administration is responsible for administering the program for most state agencies. The Minnesota Department of Transportation and the University of Minnesota are required to have similar set-aside procurement programs.

The Department of Energy and Economic Development also participates in these programs. Along with the Department of Administration, they are responsible for publicizing the programs and ensuring that small businesses across the state are aware of the set-aside programs. In addition, when an eligible business is identified as having trouble performing the requirements of a contract, the Department of Energy and Economic Development's Small Business Assistance Center is responsible for assisting that business so it can meet contract requirements in the future.

A 13-member Small Business Procurement Advisory Council has been created to advise the Commissioner of Administration on the program, review complaints or grievances from small businesses regarding the program and review reports submitted by the Commissioners of Administration and Energy and Economic Development.

Certification Process

To become eligible for the programs described above, small businesses and SED businesses must be certified.

1. SED businesses

The Department of Administration uses a "self-certification" system for SED businesses. These businesses must submit an application form to the Department which includes the following information: name and place of business, type of product produced or service provided, number of employees, the preceding year's gross revenues, a list of owners and whether the business wants to be certified as a small business or a business owned and operated by a socially or economically disadvantaged person. A financial statement from the preceding year is also required. The Department then checks to see if the information on the application and other material that the Department requests is valid.

Once a SED business is certified, that business is added to a list maintained by the Procurement Division for each commodity or service class.

2. Small businesses

The Department does not require small businesses to fill out a similar application form. The Department's policy is that since they have not had trouble in meeting the set-aside goal for small businesses, it is not necessary to require the certification form. A simple questionnaire sent to all businesses that contract with the state is used to determine how many of the businesses meet the definition of "small business."

Bidding Process

When requests from state agencies for the purchase of a product or service are submitted to the Procurement Division, the SED lists are used to designate whether certified businesses can meet the requirements of the request. "Invitations to bid" are sent to eligible businesses along with an estimated price.

Bids are returned to the Procurement Division and the lowest bidder is awarded the contract except in the case of the preference program. The lowest bid cannot exceed the estimated price by more than five percent.

If there are no satisfactory bids submitted, the contract must be rebid. The contract may be open for bids from SED businesses or from all businesses during the rebidding process.

Annual Reports

Two annual reports are required to be submitted to the Governor and Legislature regarding the Small Business Procurement Program.

The Department of Administration prepares a report which summarizes the past fiscal year's statistics. The report includes the number of small business identified for the program, the total number and value of contracts awarded to SED businesses, the additional cost to the state of awarding the contracts and information regarding contracts that had to be rebid.

The Department of Energy and Economic Development prepares a report which describes efforts to publicize the program and the methods used by the Department to assist businesses unable to meet contract requirements.

MEETING THE GOALS OF THE PROGRAM

The participation of small businesses and SED businesses in state procurement of goods and services has generally increased since the program started in 1975.

The requirements for participation have also increased significantly as is demonstrated in Table 1.

TABLE 1
STATUTORY REQUIREMENTS

	<u>1975-79</u>	<u>1980-83</u>	<u>Present</u>
Procurement Award Goals for Small Businesses	10%	20%	25%
Procurement Award Goals for SED Businesses	1%	3%	9%

The Department of Administration has had few problems in meeting the requirements for contract awards for goods and services to small businesses. As shown in Table 2, statutory requirements for contract awards have been met in every year since 1978. Contract awards to SED businesses have met the statutory requirements in all but one year since 1978. In 1982, 2.1 percent of state procurement was awarded to SED businesses which fell short of the three percent requirement.

TABLE 2
PROCUREMENT OF GOODS AND SERVICES FOR SMALL BUSINESSES AND SED BUSINESSES
1976-1984¹

Fiscal Year	<u>1978</u>	<u>1979</u>	<u>1980</u>	<u>1981</u>	<u>1982</u>	<u>1983</u>	<u>1984</u>
Total Procurement	\$81.6	\$86.3	\$91.7	\$88.1	\$129.7	\$123.7	\$148.1
<u>SMALL BUSINESS</u>							
Set-Aside Required	10%	10%	20%	20%	20%	20%	25%
Procurement Awarded	21.2	21.2	30.0	21.3	35.6	34.6	45.0
Percent Awarded	26.0%	24.6%	32.7%	24.2%	27.5%	28.0%	30.4%
<u>SED BUSINESS</u>							
Set-Aside Required	1%	1%	3%	3%	3%	3%	6%
Procurement Set Aside for SED Businesses	\$2.7	\$2.4	\$3.5	\$3.7	\$4.0	\$6.9	\$10.9
Percent Set Aside	3.3%	2.8%	3.8%	4.2%	3.1%	5.6%	7.3%
Procurement Awarded to SED Businesses ²	\$1.6	\$1.9	\$2.8	\$2.9	\$2.7	\$5.9	\$8.6
Percent Awarded	2.0%	2.2%	3.1%	3.3%	2.1%	4.8%	5.8%
Number of SED Businesses Participating	43	47	75	NA	88	129	222

Source: Department of Administration.

¹All monetary figures are in millions of dollars. Because of rounding, some percentages may not agree with Department of Administration data.

²These figures may be slightly lower than the actual awards to SED businesses. In the rebidding, a few procurement contracts are awarded to SED businesses, but most of the rebid contracts are awarded to regular vendors.

APPENDIX 1

MAJOR CHANGES TO THE SMALL BUSINESS PROCUREMENT ACT
1984 AND 1985

1984

- Instead of requiring that approximately 25 percent of state procurement be set aside for small businesses, new language required that at least 25 percent be awarded to small businesses.
- A preference program was established allowing a 5 percent preference in the bid amount on selected state procurements for SED businesses. Prior to 1984, the Department of Administration had the authority to allow a 5 percent preference for up to 1.5 percent of total state procurement but the 1984 legislation required that 3 percent of total state procurement be set aside for this program.
- The set-aside program which required that 3.75 percent of total state procurement be designated for Minnesota's correctional industries, established in 1983, was discontinued. The Departments of Administration and Corrections have worked out an agreement for state purchases of correctional industries' products.

1985

- Instead of the requirements that 6 percent of procurement be awarded through a set-aside program and 3 percent be awarded through a preference report, the Department of Administration may meet the total nine percent goal, if possible, through a combination of set aside, preference or any other bidding procedure authorized by statute. A minimum of 3 percent of total procurement must still be awarded through a set aside program.
- The former requirement that 10 percent of the value of contracts over \$200,000 be subcontracted to SED businesses has been changed so that the agency has the option of either subcontracting 10 percent of the value of the contract to an SED business or purchasing materials and supplies equal to 10 percent of the value of the contract from SED businesses.
- Sheltered workshops and work activity programs have been added to the definition of SED businesses.