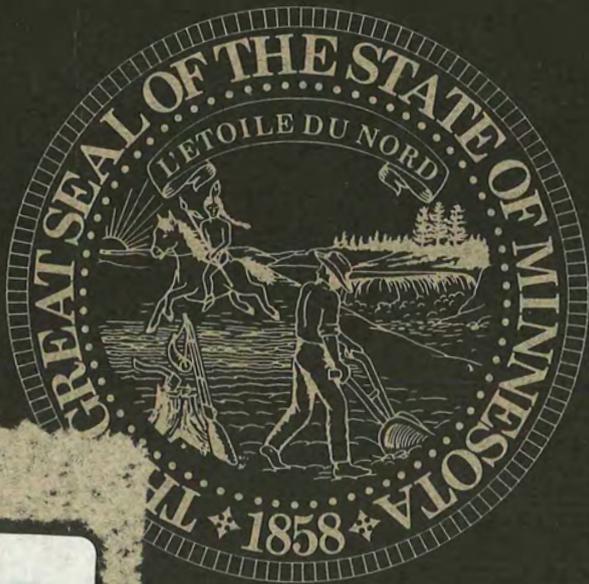


STATE OF MINNESOTA

Department of
Administration

MANAGEMENT
ANALYSIS DIVISION



900135

A Study of
Discrimination
Against Women-
and Minority-owned
Businesses

and of Other
Small-business
Topics

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**Minnesota Department of Administration
Management Analysis Division
January 1990**

203 Administration Building, 50 Sherburne Avenue, St. Paul, Minnesota 55155

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Executive Summary

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EXECUTIVE SUMMARY

State programs to benefit businesses owned by women and minorities were struck down by the United States Supreme Court in 1989, in *Richmond vs. Croson*. The Court held that the Equal Protection Clause of the Fourteenth Amendment to the Constitution requires states to have evidence of discrimination against women and minority businesses prior to enacting remedial legislation. In addition, the Court held that race- or gender-neutral alternatives must have been considered and rejected as inadequate and that any race or gender remedy must be narrowly tailored to minimize adverse impact on other groups.

Minnesota adopted a program to assist women- and minority-owned small businesses in 1975. As it developed, a certain amount of government purchasing was set aside for award to socially or economically disadvantaged firms or those firms were granted a bonus or preference in the bidding process. The 1989 Legislature suspended the program after the Supreme Court decision and replaced it with temporary legislation creating a race- and gender-neutral program for disadvantaged businesses. That legislation also required the commissioner of administration to conduct a study addressing several questions and to report the study results to the Legislative Commission on Small Business Procurements. The Management Analysis Division of the Department of Administration conducted the study. This report and its appendix contain the findings, conclusions and recommendations of the study. It is organized in four sections to answer each of the major questions posed by the legislature.

Question 1. Is there sufficient justification under a strict scrutiny standard to establish a narrowly tailored purchasing program for the benefit of any socially disadvantaged groups?

Conclusions

Major conclusions of the study are:

- Sufficient evidence of discrimination exists both in the record of government purchasing and in private-sector activities to satisfy the judicial requirements of the *Richmond vs. Croson* decision and subsequent cases.
- This evidence of discrimination is not uniform across race and gender lines for each category of product or service. An analysis of purchasing records indicates that in many categories no statistically significant disparity exists for various racial groups. The lack of disparity can mean either that the firms are being employed in

relative proportion to their availability or that there are no minority-owned firms available in that line of work.

- There are differences in degree of discrimination between gender and racial groups. Blacks, more than any other group, report that their firms have been subject to discrimination. Black business owners indicate the most difficulty in obtaining equity and debt financing. They report the most difficulty establishing banking relationships and generally securing adequate financing.
- Specific problems may be addressed by race- or gender-neutral programs. For example, an effort to simplify government regulations would assist all businesses, but would particularly benefit Asian- and American Indian-owned businesses, which report more difficulty in coping with government regulations. A program aimed at providing easier access to debt and equity capital would assist more black-owned businesses than other groups.
- Specific programs would not eliminate the underutilization found in government purchasing. Female-owned firms consistently are the most underutilized, according to the purchasing study, yet these firms also report fewer specific problems than their white male or minority counterparts. As a result, programs designed to eliminate business problems would assist white male- and minority-owned firms more than female-owned firms.
- Past race- and gender-based set-aside and preference programs have directly benefited these firms in several ways. First, the underutilization of Black business owners disappeared in several of the categories. For other groups, the number of categories where a disparity was found did not change, but the size of the disparity was smaller.
- The set-aside or preference programs did not have a larger impact on the disparity because firms located in labor surplus areas or counties with low median income received a disproportionately large share of contracts let under the programs.
- Data on purchasing programs is maintained by the state and metropolitan agencies and the University of Minnesota in disparate fashion, which makes the compilation of consistent information costly and time consuming.

Recommendations

Major recommendations of the study are:

1. A race- and gender-based program to benefit female- and minority-owned businesses should be enacted by the legislature.
2. A race- and gender-based program should reflect the varying population of women- and minority-owned firms by type of business.
3. The Department of Administration should be delegated authority to identify the categories of purchasing that qualify for a race- and gender-based purchasing

reference program, based on the availability of firms. Measurement benchmarks should be established at a level higher than current availability to prevent discouraging new minority- and women-owned firms from entering the field. These findings should apply to state and metropolitan agency and University of Minnesota purchasing. The department should be required to revise this category eligibility based on new data at least once every five years. Additional resources may be needed to accomplish this task.

4. Higher purchasing preference should be granted to firms qualifying under race and gender standards than to firms qualifying under labor surplus, median income or other standards. This would increase women- and minority-owned firms' opportunities to be awarded government contracts and would reduce their underutilization.

5. The Department of Administration or another agency should be required to develop consistent methods of classifying purchase types and of data collection on the implementation of these programs for state and metropolitan government and the University of Minnesota. This agency should also be required to prepare a biennial report to the legislature on the administration of the law. Additional resources may be needed to accomplish this standardized reporting.

6. Additional efforts should be made by state government to increase sensitivity toward and awareness of women- and minority-owned firms by both government and non-government purchasing organizations.

7. State agencies with regulatory oversight of lending institutions should be directed to review institutional lending practices to see if discrimination exists and what additional steps would be necessary to eliminate it. Federal agencies should be asked to do the same.

Question 2. Should the definition of small business be revised?

Conclusions

Major conclusions of the study were:

- The current definition of small business does not recognize the different competitive conditions within the various types of business and therefore does not identify businesses that are considered small within a particular industry.
- The industry-specific definitions of small business used by the United States Small Business Administration are too large for use in Minnesota.
- The Department of Administration is developing expertise in identifying firms that are disadvantaged in relation to their markets as they implement the 1989 legislative provision creating the category of "economically disadvantaged" businesses eligible for purchasing preference. That expertise can be used to identify firm size considered small within an industry.

Recommendation

The major recommendation of the study is:

1. The Department of Administration should be delegated authority to establish size definitions of small business by type of business. The definitions should recognize the differences between various industries caused by the size of the market for their goods or services and the relative size and market share of their competitors. Additional resources to develop those definitions and to monitor the need for changes may be needed.

Question 3. Are there alternative programs to stimulate growth opportunities for small business?

Conclusions

Major conclusions of the study are:

- Minnesota currently offers small business a variety of resources ranging from education and training to financing and set asides in government purchasing. Preference programs for economically disadvantaged businesses allow firms to qualify for a 5 percent purchasing preference on the basis of economic conditions of the geographic location of the owner or his (her) employment and on the economic conditions facing the firm.
- The Minnesota program is based on economic conditions and is race- and gender-neutral on its face.
- The cities of Birmingham, Ala., and Milwaukee, Wis., are re-introducing social factors into the definition of economic disadvantage by including presumptions of disadvantage when certain social factors are present, even though the presumptions are subject to challenge.
- Minnesota's current five-year limitation on participation in preference programs may exclude a number of small businesses that both start small and remain small throughout their lifespan. The five-year limitation appears to arbitrarily decrease the opportunities for a firm to sell to government, if economic disadvantage continues for the firm.
- Studies have shown that new businesses have a strong interest in additional governmental services, particularly those providing training and financing. A large variety of programs ranging from financing to technical assistance exist throughout the state. In addition to education and training, the desire for working capital financing assistance was clear in data from the 1987 New Firms Survey. The data does not make it clear whether current programs are not widely known by small business entrepreneurs, if their focus is not correct or if there is simply more demand for these programs than can be met.

Studies have also shown that coping with government regulations is reported as a major problem by almost one-quarter of business owners.

Recommendations

Major recommendations of the study are:

1. The evaluation of existing programs to assist small business being prepared by the Department of Trade and Economic Development should be completed before determining if additional resources are necessary for small business education and technical assistance programs.
2. The Department of Trade and Economic Development should be directed to examine whether additional programs are necessary to provide working capital financing for small business.
3. The five-year limitation on eligibility for the economically disadvantaged business preference program should not apply to a firm that qualifies on the basis of its lack of economic resources.
4. The Department of Administration should expand its efforts to assist small business to understand government purchasing procedures and to consider whether those procedures can be made simpler for small businesses.

Question 4. Should the state have a preference program incorporating urban and rural areas of high unemployment?

Conclusions

Major conclusions of the study are:

- Economically distressed areas that are smaller than a labor surplus area or a county can be identified. As a result, firms located in such areas could be granted the same type of preference now given to firms located in labor surplus areas and median income counties.
- Use of unemployment data correlated to census tract information will allow designation based on unemployment levels, as is the case with the labor surplus area designation. The difference will be that the unemployment data used for labor surplus designation will be more current.
- Unemployment estimates for census tracts or other areas with less than 25,000 population are based on 1980 Census data. There is no evidence that the data will not correctly identify areas of high unemployment; 1980 data is relied on for other state programs, such as Neighborhood Revitalization.

Recommendations

Major recommendations of the study are:

1. Designation of geographic areas smaller than cities or counties should be adopted as areas of economic distress, in addition to those currently authorized, for purposes of allowing a preference for qualifying business firms in the government purchasing process.
2. Census tracts should be the basis for designation. Unemployment data, assessed by the same standards used for the labor surplus designation, should be the standard for qualification.
3. Preferences granted to firms as a result of this designation should be the same as preferences granted as a result of the labor surplus area designation.

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Introduction

INTRODUCTION

In 1975, the Minnesota Legislature adopted a program to benefit small businesses owned and operated by persons who were socially or economically disadvantaged. A socially or economically disadvantaged business was one “. . . deprived of the opportunity to develop and maintain a competitive position in the economy because of social or economic conditions” [M.S. 16.082]. This disadvantage could arise from cultural, social or economic circumstances, or from background, or from physical location when the owner resides or is employed in an area declared to have a labor surplus.

In 1980, the definition was amended to include “racial minorities, women, or persons who have suffered a substantial physical disability” [M.S. 645.445, Subd. 5]. In 1988, the definition was expanded to include persons residing or employed in a county where the median income for married couples is less than 70 percent of the state median income for married couples [M.S. 645.445, Subd. 5].

The Department of Administration was initially required to award 10 percent of the total value of purchased goods and services to small business. Ten percent of *those* purchases were to be awarded to small businesses owned and operated by socially or economically disadvantaged (SED) persons.

By 1989, the small business purchasing had changed, so the commissioner of administration was directed to award 25 percent of purchasing to small business. Nine percent of the value of all procurements was to go to Minnesota small business operated by persons who were socially or economically disadvantaged. In addition to the set aside, the commissioner had authority to award a 5 percent preference in the amount bid to small business owned by socially or economically disadvantaged persons.

Prime contractors on construction contracts exceeding \$200,000 were required to subcontract 10 percent of the contracts to eligible SED businesses. The same 10 percent subcontracting requirement applied to agencies entering into contracts for consultant, professional or technical services exceeding \$200,000. In addition, agencies that had authority to locally purchase items up to \$1,500 were required to award 10 percent of these purchases to eligible businesses.

Department of Transportation

In 1977, the legislature directed the Department of Transportation to conduct a program for socially and economically disadvantaged businesses [M.S. 161.321]. Two percent of the department's road construction projects were set aside for small businesses, SED small businesses or contractors that guaranteed they would use such

small businesses as subcontractors. (The department also administers a federally mandated set-aside program for socially and economically disadvantaged businesses.)

University of Minnesota

First mandated in 1979, the University of Minnesota's program required that 20 percent of its awards be made to small business, 15 percent of which were to be awarded to eligible SED businesses [M.S. 137.31].

Metropolitan agencies

An SED set-aside program was implemented Jan. 1, 1989, involving the metropolitan agencies [M.S. 473.142].

Eligible to participate in this program were all businesses owned and operated by women, racial minorities and physically disabled persons, rehabilitation facilities and work activity programs. The program did not include businesses whose owners resided in labor surplus areas or counties with 70 percent median income.

The agencies were required to attempt to award 9 percent of all purchases to eligible businesses. The agencies were required to award some set-aside contracts and had the authority to make 5 percent preference awards. They also were to attempt to award 6 percent of all consultant, professional or technical services contracts to eligible businesses and, for certain contracts exceeding \$200,000, they were required to attempt to ensure that 10 percent of the contract was subcontracted to eligible businesses.

The Croson Decision

These programs, which included race- and gender-based criteria, were suspended in April 1989 after the decision of the United States Supreme Court that struck down a race-based program in the City of Richmond, Va. The 1989 Legislature adopted a temporary race- and gender-neutral program for economically disadvantaged businesses, which is currently being implemented by the state, university and metro agencies.

Study Purpose

The United States Supreme Court decision in the case of *City of Richmond vs. J.A. Croson*, 109 S. Ct. 706 (1989), struck down the City of Richmond's ordinance creating a program to "set aside" 30 percent of the city's prime contracts for minority contractors. The Court found the ordinance violated the Equal Protection Clause of the Fourteenth Amendment to the United States Constitution because the city did not justify its unequal treatment of persons based on their racial classification. Shortly after this decision, the Minnesota program granting women- and minority-owned firms a preference in state purchasing and providing for set asides was challenged in state court and the State of Minnesota agreed to suspend the race- and gender-based programs pending legislative action.

The Minnesota Legislature responded by adopting a temporary race- and gender-neutral purchasing program to assist firms deemed to be "economically disadvantaged."¹ It also created a Small Business Procurements Commission to recommend changes in small business programs and directed the commissioner of administration to conduct a study of small business programs. The commissioner was directed to:

1. Review recent Supreme Court decisions to determine whether there is sufficient justification under a "strict scrutiny" standard to establish a narrowly tailored purchasing program for the benefit of any socially disadvantaged groups, and make recommendations to the commission regarding legislation and program operation.
2. Make recommendations for revising the definition of small business found in M.S. 45.445.
3. Make recommendations on alternative programs to stimulate growth opportunities for small business.
4. Assess the feasibility of establishing a preference program that incorporates urban and rural areas of high unemployment.

The Department of Administration's Management Analysis Division conducted a study addressing the four questions posed by the legislation. Because of the separable nature of the questions, this report is divided into four sections addressing each question individually. A detailed methodological appendix has been prepared and is bound separately.

¹ *Minn. Laws 1989, Chapter 352.*

Methodology

The project team members were Charlie Ball, Michele Jimenez and Jeff Rathermel, led by Ken Nickolai. Assistance was provided by Bob Baldwin, Barbara Deming, Virginia Dodds, Nancy Hoglund, M. Jill Lafave, Richard Manthey, Kate O'Connell, Karen Patterson and Mary Williams. The team used various methods to gather and analyze data and develop recommendations. The methods included:

- Random sampling of the purchasing files of state government, metropolitan agencies and the University of Minnesota.
- A survey of women- and minority-owned business firms conducted by the University of Minnesota Survey Research Center to identify any patterns of discrimination.
- A survey of 15,000 business firms in Minnesota to identify race and gender of ownership to estimate the population of women- and minority-owned firms operating in the State of Minnesota.
- Analysis of the 1987 New Firms Study published by the Center for Urban and Regional Affairs for information on differences between white male-, female- and minority-owned firms.
- Application of statistical tests to more than 2,500 data sets to meet the requirements of the Croson decision.
- Personal interviews with more than 40 individuals involved in the small business and government procurement fields.
- Literature searches for relevant research on the topics of small business development, testing for race and gender discrimination and the role of government programs in the development of women- and minority-owned business.
- Analysis of relevant case law in the field of discrimination including Croson and subsequent cases, as well as cases on employment discrimination and the validity of the use of statistical testing.

Definitions

Some of the terms used repeatedly in this report have special meanings within the context of procurement programs designed to address discrimination. Those terms and their meanings are:

Croson decision: A United States Supreme Court decision declaring that states and cities may not give special benefits to business firms owned by women and minorities unless they have evidence that women- and minority-owned firms have been discriminated against.

Statistically significant disparity: The difference between the proportion of the dollar value of government purchasing that went to women- or minority-owned firms and the proportion of those firms available for that work, if the difference is statistically large enough to reject the assumption that discrimination did not occur. This is the Court's declaration of evidence of discrimination against women- and minority-owned firms, from the Croson decision.

Underutilization: The employment of women- and minority-owned firms at a rate sufficiently less than expected, so that there is a statistically significant disparity (see definition above).

Set aside: A requirement that a certain percentage of the products and services bought by the state every year be obtained from businesses with specific characteristics. For example, state law requires that 25 percent of all products and services must be bought from small business each year.

Purchasing preference: The granting of a bonus to business firms with certain characteristics, to increase the chance that their good or service will be purchased in a competitive bidding opportunity. For example, a firm whose owner resides in a county with high unemployment is granted a 5 percent bonus when it submits a bid. As a result, its bid will be awarded the contract if it is no more than 5 percent higher than the lowest bid made.

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Question 1.

Is there sufficient justification under a strict scrutiny standard to establish a narrowly tailored purchasing program for the benefit of any socially disadvantaged groups?

SUFFICIENT JUSTIFICATION:

Background

Applicable legal standards

State and local government programs establishing set-aside and preference purchasing to encourage minority-owned businesses are subject to judicial review under the requirements of the Fourteenth Amendment to the U.S. Constitution.² In January 1989, the U.S. Supreme Court held in *Richmond vs. Croson*³ that it would apply the strict scrutiny standard⁴ in reviewing programs established to assist specified racial groups, even if the programs had been adopted with the stated purpose of remedying prior discrimination.

Subsequent to the *Croson* decision, the Supreme Court upheld a lower court decision that concluded that a gender-based program to benefit women-owned businesses violated the Equal Protection Clause.⁵

"No state shall . . . deny to any person within its jurisdiction the equal protection of the laws."

³ *City of Richmond vs. J.A. Croson*, 109 S. Ct. 706 (1989).

⁴ *The Supreme Court examines actions taken by states in several ways, depending on the nature of the interest affected. The strict scrutiny standard subjects state action to the most searching review. In the Croson case, Justice O'Connor applied this standard, saying, "Absent searching judicial inquiry into the justification for such race-based measures, there is simply no way of determining what classifications are 'benign' or 'remedial' and what classifications are, in fact, motivated by illegitimate notions of racial inferiority or simple racial politics." 109 S. Ct. 721. A less rigorous standard has been applied to gender-based classifications, but the Supreme Court affirmed a lower court decision that concluded that a Michigan program to benefit women-owned businesses could not pass the standard of being substantially related to achieve an important government function. See Michigan Road Builders Assn., Inc., vs. Milliken, 834 F.2d.583 (C.A. 6 1987), Aff'd, 109 S. Ct. 1333 (1989).*

⁵ *Michigan Road Builders Assn., Inc., vs. Milliken*, 834 F.2d.583 (C.A. 6 1987), *Aff'd*, 109 S. Ct. 1333 (1989).

After these decisions, legal scholars appear to agree only that the cases leave many unanswered questions.⁶ However, before a state uses race or gender criteria for a beneficial remedial program, it is prudent to establish several facts, including:

1. Discrimination against persons in the class of individuals to be assisted by the program.
2. Government participation in the discrimination, or passive participation in the otherwise established discrimination.
3. Consideration of nonrace- or gender-based alternative remedies and the reasons for their rejection.
4. Intention of the remedy to benefit groups experiencing discrimination, and limited duration of the remedy, to minimize adverse impact on others affected.

In *Croson* and subsequent cases, the Court indicates that it expects states to use statistical means similar to those used by the courts in employment discrimination cases, when they seek to employ race or gender classifications to establish a presumption of discrimination.⁷ That is, a significant statistical disparity must be shown between the available qualified pool of minority-owned firms and their actual rate of employment. Justice O'Connor wrote: "(W)here special qualifications are necessary, the relevant statistical pool for purposes of demonstrating exclusion must be the number of minorities qualified to undertake the task."⁸

The statistical disparity necessary to establish a presumption of discriminatory impact is, then, based on the number of potential participants in the market. It appears prudent that a state program using race or gender categories be based on distinctions between identifiable groups and the markets in which they participate, distinctions drawn as narrowly as the data will reasonably permit.

Justice O'Connor's opinion also discusses the City of Richmond's failure to examine neutral alternatives and questioned the broad sweep of the remedy used. The Court mentions such evidence as the impact on minority firms of perceived race-neutral problems such as deficiencies in working capital, inability to meet bonding requirements, unfamiliarity with bidding procedures and the disabilities caused by an

⁶ See Rosenfeld, *Decoding Richmond: Affirmative Action and the Elusive Meaning of Constitutional Equality*, 87 Mich. L. Rev. 1729 (1989); *Constitutional Scholars Statement on Affirmative Action after City of Richmond vs. J.A. Croson Co.*, 98 Yale L.J. 1711 (1989).

⁷ Quoting the discrimination case of *Hazelwood School District vs. U.S.*, 433 U.S. 299 (1977), the Court said, "(W)here gross statistical disparities can be shown, they alone in a proper case may constitute prima facie proof of a pattern or practice of discrimination" 109 S. Ct. at 726.

⁸ 109 S. Ct. at 726.

inadequate track record. It appears that evidence on such topics indicating a difference between majority and minority firms would be a useful indication of whether a race-neutral program would successfully aid these nonwhite firms.

In *Croson* and its subsequent cases, the Court has placed the burden on states to document the extent of discrimination more thoroughly than previously and to take steps to examine the feasibility of race- and gender-neutral alternatives. If a race- or gender-based program is still considered necessary after this review, the Court also requires that the program be narrowly drawn to target its benefit and minimize its impact on others in society.

Methods of analysis

To satisfy the requirements necessary to sustain any race- and gender-based program under applicable judicial standards, two methods of analysis were used, one analyzing quantitative purchasing and availability information and the second gathering more qualitative data. Both approaches were used in an effort to identify as completely as possible the experience of female and minority business owners in Minnesota.

Quantitative analysis was used to identify any statistically valid evidence that women- and minority-owned firms are being underutilized. In other words, are they winning awards at a rate sufficiently different from their proportion in the marketplace that an inference of discrimination arises?

The utilization study examined purchasing data from state and metropolitan agencies and the University of Minnesota to determine the proportion of government dollars spent and the proportion of the total opportunities being given to women- or minority-owned businesses. Where possible, a further breakout of the data was made to identify the extent to which those awards were made using either set-aside or purchasing preference programs and those awards won without any special consideration. With this information, ratios were calculated that indicated the proportion of contracts awarded to Black-owned businesses, women-owned businesses, etc.

The ratio was then compared to the ratio of the number of black-owned, women-owned, etc., businesses in a particular type of business compared with all firms in that line of business.⁹ A statistical test was then performed on the difference to determine whether the difference was statistically significant to the extent required by the Court.

The second method of analysis was the use of qualitative surveys. The Center for Urban and Regional Affairs (CURA) published a study of new business firms in 1987.¹⁰ That study was based on a survey of more than 1,000 Minnesota businesses that were started between 1979 and 1984. The participating businesses responded to questions concerning the severity of problems encountered in starting a new business, the characteristics of the persons involved in the start-up team and major areas of support or difficulty caused by government programs. Brenda Miller, one of the study authors, contracted to examine their data base to analyze the responses based on race and gender, to see if the nature of business problems differed among white males, women and minorities.

The number of minority firms in the data base was too small to identify experience by specific racial classifications such as American Indian business owners or Asian business owners.

That 1987 CURA study also provided a base of information against which survey results from the 1989 survey of women- and minority-owned businesses could be compared. To broaden the information about specific women- and minority-owned businesses, a questionnaire was sent to women- and minority-owned businesses. The firms were identified from government certification lists and from affiliate membership lists. Many of the questions from the 1987 survey were repeated, in order to compare the frequency of response and to identify any patterns of different experiences between white male-owned firms and others. Other questions were added in an effort to elicit any evidence of perceived discrimination within the industry group and to gauge the effectiveness of government programs to aid these firms, including the usefulness of set-aside and preference purchasing efforts. This

⁹ *Because credible estimates of minority- and women-owned firms were unavailable, this ratio was calculated using the results of a survey of Minnesota businesses conducted by the University of Minnesota Survey Research Center. Forty-one major three-digit Standard Industrial Classification (SIC) codes were identified with the assistance of personnel in the Materials Management Division of the Department of Administration. The basis for selection was the likelihood that they were codes representing areas of major government purchasing. A sample of those firms was asked to complete a survey about ownership and firm size.*

¹⁰ *1987 New Firms Study, Paul Reynolds and Brenda Miller.*

survey was conducted by the University of Minnesota Survey Research Center under contract with the Department of Administration.

Data gathering¹¹

The data-gathering process for this portion of the study consisted of gathering statistics on state, University of Minnesota and metropolitan agency purchasing, and the use of surveys to estimate the population of women-owned and minority-owned businesses as well as to identify any patterns of discrimination. University and metropolitan agency data was sought because the legislature included them in the mandate to use purchasing practices to further social and economic goals.

Data was sought for the most recent complete two years of purchasing. The Statewide Accounting System provided information about state government purchasing. It provided totals by state purchasing code and the itemization of the number of times purchases were made (opportunities) and dollars awarded to women- and minority-owned firms. This data base does not contain information necessary to identify whether an award was made using either set aside or preference.

In order to gain a more detailed analysis of state government purchasing activity, random samples were taken from information about purchasing activity. Sources were the Department of Administration's centralized state purchasing and construction files and the Department of Transportation's construction, consulting and engineering files. Random samples were also taken from files maintained by the Metropolitan Council, Metropolitan Waste Control Commission, Metropolitan Transit Commission, Metropolitan Airports Commission (construction only), University of Minnesota and the Mosquito Control District.¹²

¹¹ *A detailed description of the nature of the data sources used and their limitations is contained in the appendices to this report.*

¹² *Because of time constraints and the fact that there is no consistency in either the extent of computerization of this information or the reference codes by which it is kept, it was not possible to completely analyze all aspects of purchasing by the state and metropolitan agencies. For example, the University of Minnesota Hospital files were not examined because it operates a purchasing program separate from the rest of the university. Another example is the nonconstruction spending records of the Metropolitan Airports Commission, which were not computerized; it was determined that the efforts to take a nonstratified random sample would not be worthwhile at this time.*

When possible, samples were taken from data that had been segmented into product or service categories. Where records were fully computerized or were filed separately, that process allowed a random sample to be taken by type of service or product. When information was not organized in a manner allowing for that stratification, a traditional random sample of the entire file population was conducted. All information on purchases by type of product or service was categorized by relevant SIC code to assure comparability.

Two survey tools were used to gather data for the study. The first was a survey of 15,000 major businesses, seeking to identify the race and gender characteristics of ownership and to provide an estimate of firm size. The second survey consisted of a series of qualitative questions about business problems. It was sent to 1,600 identified women- or minority-owned businesses. Both surveys were conducted by the University of Minnesota Survey Research Center under contract with the Department of Administration.

SUFFICIENT JUSTIFICATION:

Findings

Analysis of state and metropolitan agency purchasing

The Croson and subsequent decisions call for a statistical analysis of the use of women- and minority-owned firms to determine whether there is a statistically significant difference between the rate at which those firms are employed and the number of firms available for work in the marketplace. This study examined purchasing data from numerous sources within state government, the University of Minnesota and metropolitan agencies to identify the rate at which they utilized women- and minority-owned firms. To develop a current estimate of the population of women and minority firms, a survey was made of 41 major types of businesses, seeking information on the race and gender of their ownership and the size of the firm.¹³ The results of this data collection show that statistically significant disparities exist for many types of firms in Minnesota. Disparity was examined in terms of the percentage of total dollars being awarded to vendors with specified ownership characteristics and in terms of the percentage of opportunities (number of awards) compared with the percentage of women- and minority-owned firms available to perform the work.¹⁴ A final look was made to identify any difference between awards when set-aside or preference programs were used and when they were not.

The Croson decision considers a statistically significant disparity, or underutilization, as evidence of discrimination. A lack of significant disparity could mean one of two things: first, that there are no women- or minority-owned firms available to perform that type of work; or second, that women and minority firms are

¹³ *The 41 lines of business were selected to include firms most likely to be engaged in business with government.*

¹⁴ *The Supreme Court specified the comparison of the proportion of dollars awarded and the proportion of firms available. In addition to this test, information was gathered to compare the proportion of opportunities (number of awards) and the proportion of women- and minority-owned firms available for work.*

already being employed in relative proportion to their availability in that line of work.

The overall occurrence of underutilization is shown in Table 1. It is easiest to understand by way of example. When the category of nonresidential building construction was examined in the records of the Department of Administration, an underutilization of female-owned firms was found. In every other data base examined, when that agency spent money on nonresidential building construction, an underutilization of female-owned firms was also found. Table 1 shows that a disparity in use of female-owned businesses was found 100 percent of the time in the category of nonresidential building construction. No disparity was found in that category for Black- or Hispanic-owned businesses; 40 percent of the time a disparity was found for American Indian-owned firms, and 80 percent of the time for Asian-owned firms.

Table 1. Incidence of disparity in government purchasing, by product category

<u>Type of Product/Service</u>	<u>Female</u>	<u>Black</u>	<u>Hispanic</u>	<u>Indian</u>	<u>Asian</u>
	(percent)				
Nonresidential building const.	100	0	0	40	80
Highway and street construction	100	0	20	0	0
Heavy construction, exc. highway	100	100	0	0	0
Plumbing, heating, A/C contractor	80	0	0	100	0
Painting, paper hanging	100	0	0	0	0
Electrical work	100	0	0	0	0
Masonry	100	0	0	0	0
Carpentry and floor work	100	0	0	0	0
Roofing, siding and sheetmetal	100	0	0	0	0
Concrete work	100	0	0	0	0
Water well drilling	100	0	0	0	0
Misc. special trade contractors	100	0	0	0	0
Printing trade services	100	0	0	0	0
Trucking and courier services	100	25	0	25	0
Passenger transportation arr.	50	0	0	0	0
Freight transportation arr.	100	0	0	0	0
Telephone communications	100	33	33	33	0
Motor vehicle parts and supplies	100	0	0	0	25
Furniture/furnishings	100	0	0	0	20
Professional/commercial equip.	100	33	33	17	100
Electrical goods	100	40	20	0	100
Hardware, plumbing and heating equipment	100	50	50	0	50

(continued)

Table 1. Incidence of disparity in government purchasing, by product category (continued)

<u>Type of Product/Service</u>	<u>Female</u>	<u>Black</u>	<u>Hispanic</u>	<u>Indian</u>	<u>Asian</u>
			(percent)		
Misc. durable goods	100	33	0	0	33
Paper and paper products	100	0	0	0	100
Groceries and related products	100	20	20	20	0
Hotels/motels	100	0	0	0	0
Laundry and cleaning	100	50	50	0	50
Mailing, reproduction and stenography	100	0	0	0	100
Services to buildings	100	80	20	0	100
Misc. equipment rental and leasing	100	50	0	0	0
Computer and data processing services	100	100	100	0	100
Auto repair	100	33	33	0	0
Auto services, except repair	100	0	0	0	0
Reupholstery and furniture service	100	100	0	0	0
Medical and dental labs	100	0	0	0	0
Engineering and architectural services	100	20	80	0	100
Accounting services	100	0	0	0	0
Research and testing services	100	0	0	0	0
Management and public relations services	80	80	20	0	100

Table 2. Statewide Accounting System data

	<u>Total</u>	<u>Categories with under-use</u>	<u>Percent</u>
Aleut	11	4	35
Asian	15	13	87
Black	19	15	79
Female	22	22	100
Hispanic	17	12	71
American Indian	17	5	29

Tables 2 through 5 show the number of purchasing categories by agency in which the gender or racial group business participates, and the number of those categories in which there is statistically significant underutilization. The last column represents the percentage of the categories in which they participate that show significant statistical disparities.

The broadest look at purchasing by state government is obtained from the Statewide Accounting System (SWAS) (Table 2). No information about the use of preference or set aside is available from the system, but it covers the broadest range of products and services purchased by the state.¹⁵ Tables 2 through 5 indicate the total number of purchasing categories in which women or minority firms were available and then the number of times a statistically significant underutilization of their firms was found.

¹⁵ *SWAS data included some of the data examined from the departments of Administration and Transportation files, but SWAS data covers the range of purchases made by all agencies of state government.*

Table 3 represents purchasing by the Department of Administration for itself and for other entities of state government as an organization of central procurement for many items used by state government. It also shows purchasing of construction, engineering and consulting services by the Department of Transportation.

Detail was also available from this data base to allow examination of the impact on women and minority firms when set aside or preference was used in purchasing. When state purchases made by the Department of Administration with the use of set aside or preference were removed from the totals, the number of statistically significant categories increased for Black-owned firms from three to five and, in many cases, the size of the existing disparity increased for other categories.¹⁶

For construction and Department of Transportation contracts, when contracts let using set aside or preference are removed from the totals, the number of categories where underutilization exists does not change, but the amount of the disparity does increase.

¹⁶ *The change in the size of the disparity may be seen in the tables contained in the appendices to this document.*

Table 3. Other state government data

	<u>Total</u>	<u>Categories with under-use</u>	<u>Percent</u>
Central procurement purchases made by the Department of Administration			
Aleut	2	0	0
Asian	11	9	81
Black	16	3	18
Female	17	17	100
Hispanic	11	5	45
American Indian	7	2	28
Construction contracts (with prime contractors) let by the Department of Administration			
Aleut	3	0	0
Asian	6	1	16
Black	6	1	16
Female	12	11	92
Hispanic	7	0	0
American Indian	10	1	10
Construction, engineering and consulting contracts let by the Department of Transportation			
Aleut	2	0	0
Asian	4	2	50
Black	3	1	33
Female	7	7	100
Hispanic	7	0	0
American Indian	4	2	50

Table 4. Metropolitan agencies

	<u>Total</u>	<u>Categories with under-use</u>	<u>Percent</u>
Metropolitan Council			
Aleut	2	0	0
Asian	16	8	50
Black	18	2	11
Female	22	21	95
Hispanic	15	2	13
American Indian	11	0	0
Metropolitan Mosquito Control District			
Aleut	2	0	0
Asian	7	3	43
Black	5	1	20
Female	9	9	100
Hispanic	5	0	0
American Indian	3	0	0
Metropolitan Waste Control Commission			
Aleut	1	0	0
Asian	9	5	55
Black	8	3	38
Female	10	10	100
Hispanic	6	1	16
American Indian	7	1	14
Metropolitan Airports Commission - Construction contracts only			
Aleut	2	0	0
Asian	5	1	20
Black	6	1	16
Female	9	9	100
Hispanic	5	0	0
American Indian	8	1	13
Metropolitan Transit Commission			
Aleut	2	0	0
Asian	11	7	63
Black	12	3	25
Female	14	13	93
Hispanic	10	2	20
American Indian	8	1	13

Table 5. University of Minnesota - nonconstruction¹⁷

	<u>Total</u>	<u>Categories with under-use</u>	<u>Percent</u>
Aleut	3	0	0
Asian	21	9	43
Black	22	3	14
Female	31	31	100
Hispanic	22	3	14
American Indian	14	1	7

Tables 4 and 5 display the results of the purchasing analysis of metropolitan agencies and the University of Minnesota. It was possible to identify purchases made using the set-aside or preference program for Metropolitan Waste Control. Removing set-aside or preference purchases increased from three to four the number of categories in which Black-owned businesses were underutilized. For other races and females, the total number of categories in which they were underutilized remained unchanged.

Effect of set aside or preference

When awards made with the use of set aside or preference were sampled, white male-owned firms qualifying under the labor surplus or 70 percent median income designation received a disproportionately large share of even these awards.

For example, of the 10 SIC codes in the sample where set-aside and preference data was sufficient for statistical testing, white male-owned firms received a statistically significant higher proportion of the awards in four categories. In two categories, they received awards approximating their presence in the market, and in four categories they received less than a proportionate share. In seven of the 10 categories, white male-owned firms received 50 percent or more of awards made using set aside or preference in that category.

¹⁷ All construction contracts are let by the university using a 5 percent flow down, which requires the use of women- and minority-owned firms for at least 5 percent of the project. These files are not computerized. It was determined that a manual random sample of these files would not produce additional information beyond that reported by the university in its annual report to the legislature.

For the set-aside or preference program to reduce the underutilization of women- and minority-owned firms, it would be necessary that white male-owned firms be awarded a less than proportionate share of set-aside or preference awards in all categories.

Estimating the number of women- and minority-owned firms

In order to complete the analysis and determine whether women- and minority-owned firms were being underutilized, it was necessary to estimate their population. The 1982 Census of women- and minority-owned businesses had two major problems. First, the estimate of women-owned firms was biased upward because of a methodological problem. Second, the data was collected to present the business population in broad categories such as agriculture and construction, not by more discrete lines of business.

To then estimate the population of women and minority businesses in Minnesota, a survey of 15,000 businesses was conducted by the University of Minnesota Survey Research Center, using a random sample of firms classified in 41 major SIC codes. The survey indicates the proportion of women- and minority-owned businesses operating in these lines of businesses (Table 6).

Methodological note

In computing the results of these surveys, a Black female business owner would appear in both the category "Black" and the category "Female." Using this method provides the most accurate picture by category, but will slightly overstate the proportion of firms available indicated on Table 6. It is important, when reading Table 6, to remember that "Number reported" represents the number of responses, by category, to the survey, and not the total population of firms available. The best estimate of the population of firms is the percentage of firms available in that line of work contained under the heading "Share of total" on Table 6.

Table 6. Women- and minority-owned business population estimates, by SIC code

<u>Race/gender of business owner</u>	<u>Number reported (sample size)</u>	<u>Share of total (sample proportion)</u>
154: Nonresidential building construction		
Female	55	19.16%
Black	2	0.70%
Hispanic	0	0.00%
American Indian	3	1.05%
Aleut	0	0.00%
Asian	5	1.74%
Disabled	6	2.09%
Other (including white male)	216	75.26%
Total	287	100.00%
161: Highway and street construction		
Female	33	23.57%
Black	0	0.00%
Hispanic	1	0.71%
American Indian	1	0.71%
Aleut	0	0.00%
Asian	0	0.00%
Disabled	6	4.29%
Other (including white male)	99	70.71%
Total	140	100.00%
162: Heavy construction, except highway		
Female	62	25.73%
Black	4	1.66%
Hispanic	2	0.83%
American Indian	1	0.41%
Aleut	0	0.00%
Asian	0	0.00%
Disabled	5	2.07%
Other (including white male)	167	69.29%
Total	241	100.00%

(continued)

Table 6. Women- and minority-owned business population estimates, by SIC code (continued)

<u>Race/gender of business owner</u>	<u>Number reported (sample size)</u>	<u>Share of total (sample proportion)</u>
171: Plumbing, heating and air-conditioning contractors		
Female	94	23.50%
Black	0	0.00%
Hispanic	3	0.75%
American Indian	4	1.00%
Aleut	2	0.50%
Asian	1	0.25%
Disabled	6	1.50%
Other (including white male)	290	72.50%
Total	400	100.00%
172: Painting and paperhanging contractors		
Female	47	20.98%
Black	0	0.00%
Hispanic	1	0.45%
American Indian	0	0.00%
Aleut	0	0.00%
Asian	1	0.45%
Disabled	1	0.45%
Other (including white male)	174	77.68%
Total	224	100.00%
173: Electrical work		
Female	110	30.47%
Black	1	0.28%
Hispanic	1	0.28%
American Indian	1	0.28%
Aleut	1	0.28%
Asian	1	0.28%
Disabled	3	0.83%
Other (including white male)	243	67.31%
Total	361	100.00%

(continued)

Table 6. Women- and minority-owned business population estimates, by SIC code (continued)

<u>Race/gender of business owner</u>	<u>Number reported (sample size)</u>	<u>Share of total (sample proportion)</u>
174: Masonry, stonework and plastering contractors		
Female	72	23.08%
Black	2	0.64%
Hispanic	0	0.00%
American Indian	1	0.32%
Aleut	0	0.00%
Asian	3	0.96%
Disabled	5	1.60%
Other (including white male)	229	73.40%
Total	312	100.00%
175: Carpentry and floor work		
Female	58	30.37%
Black	0	0.00%
Hispanic	2	1.05%
American Indian	1	0.52%
Aleut	0	0.00%
Asian	0	0.00%
Disabled	3	1.57%
Other (including white male)	127	66.49%
Total	191	100.00%
176: Roofing, siding and sheetmetal work		
Female	32	20.78%
Black	0	0.00%
Hispanic	2	1.30%
American Indian	0	0.00%
Aleut	0	0.00%
Asian	0	0.00%
Disabled	0	0.00%
Other (including white male)	120	77.92%
Total	154	100.00%

(continued)

Table 6. Women- and minority-owned business population estimates, by SIC code (continued)

<u>Race/gender of business owner</u>	<u>Number reported (sample size)</u>	<u>Share of total (sample proportion)</u>
177: Concrete work		
Female	51	26.02%
Black	1	0.51%
Hispanic	0	0.00%
American Indian	1	0.51%
Aleut	0	0.00%
Asian	0	0.00%
Disabled	0	0.00%
Other (including white male)	143	72.96%
Total	196	100.00%
178: Water well drilling		
Female	13	21.31%
Black	0	0.00%
Hispanic	0	0.00%
American Indian	0	0.00%
Aleut	1	1.64%
Asian	0	0.00%
Disabled	1	1.64%
Other (including white male)	46	75.41%
Total	61	100.00%
179: Miscellaneous special trade contractors		
Female	78	27.46%
Black	2	0.70%
Hispanic	0	0.00%
American Indian	2	0.70%
Aleut	0	0.00%
Asian	1	0.35%
Disabled	4	1.41%
Other (including white male)	197	69.37%
Total	284	100.00%

(continued)

Table 6. Women- and minority-owned business population estimates, by SIC code (continued)

<u>Race/gender of business owner</u>	<u>Number reported (sample size)</u>	<u>Share of total (sample proportion)</u>
279: Printing trade services		
Female	32	45.71%
Black	1	1.43%
Hispanic	1	1.43%
American Indian	0	0.00%
Aleut	0	0.00%
Asian	0	0.00%
Disabled	0	0.00%
Other (including white male)	36	51.43%
Total	70	100.00%
348: Medical instruments and supplies		
Female	10	19.23%
Black	1	1.92%
Hispanic	1	1.92%
American Indian	0	0.00%
Aleut	0	0.00%
Asian	2	3.85%
Disabled	2	3.85%
Other (including white male)	36	69.23%
Total	52	100.00%
421: Trucking and courier services		
Female	135	35.34%
Black	1	0.26%
Hispanic	0	0.00%
American Indian	1	0.26%
Aleut	0	0.00%
Asian	0	0.00%
Disabled	3	0.79%
Other (including white male)	242	63.35%
Total	382	100.00%

(continued)

Table 6. Women- and minority-owned business population estimates, by SIC code (continued)

<u>Race/gender of business owner</u>	<u>Number reported (sample size)</u>	<u>Share of total (sample proportion)</u>
472: Passenger transportation arrangement		
Female	124	65.96%
Black	0	0.00%
Hispanic	0	0.00%
American Indian	0	0.00%
Aleut	0	0.00%
Asian	1	0.53%
Disabled	3	1.60%
Other (including white male)	60	31.91%
Total	188	100.00%
473: Freight transportation arrangement		
Female	21	29.58%
Black	1	1.41%
Hispanic	2	2.82%
American Indian	0	0.00%
Aleut	0	0.00%
Asian	4	5.63%
Disabled	0	0.00%
Other (including white male)	43	60.56%
Total	71	100.00%
481: Telephone communications		
Female	22	28.57%
Black	2	2.60%
Hispanic	1	1.30%
American Indian	1	1.30%
Aleut	0	0.00%
Asian	0	0.00%
Disabled	3	3.90%
Other (including white male)	48	62.34%
Total	77	100.00%

(continued)

Table 6. Women- and minority-owned business population estimates, by SIC code (continued)

<u>Race/gender of business owner</u>	<u>Number reported (sample size)</u>	<u>Share of total (sample proportion)</u>
501: Motor vehicle parts and supplies (wholesale)		
Female	42	16.73%
Black	1	0.40%
Hispanic	0	0.00%
American Indian	1	0.40%
Aleut	0	0.00%
Asian	2	0.80%
Disabled	2	0.80%
Other (including white male)	203	80.88%
Total	251	100.00%
502: Furniture and home furnishings (wholesale)		
Female	43	25.60%
Black	0	0.00%
Hispanic	1	0.60%
American Indian	0	0.00%
Aleut	0	0.00%
Asian	1	0.60%
Disabled	3	1.79%
Other (including white male)	120	71.43%
Total	168	100.00%
504: Professional and commercial equipment (wholesale)		
Female	46	15.18%
Black	2	0.66%
Hispanic	2	0.66%
American Indian	1	0.33%
Aleut	0	0.00%
Asian	6	1.98%
Disabled	4	1.32%
Other (including white male)	242	79.87%
Total	303	100.00%

(continued)

Table 6. Women- and minority-owned business population estimates, by SIC code (continued)

<u>Race/gender of business owner</u>	<u>Number reported (sample size)</u>	<u>Share of total (sample proportion)</u>
506: Electrical goods (wholesale)		
Female	61	22.02%
Black	3	1.08%
Hispanic	1	0.36%
American Indian	0	0.00%
Aleut	0	0.00%
Asian	5	1.81%
Disabled	4	1.44%
Other (including white male)	203	73.29%
Total	277	100.00%
507: Hardware, plumbing and heating equipment (wholesale)		
Female	52	23.21%
Black	2	0.89%
Hispanic	2	0.89%
American Indian	0	0.00%
Aleut	0	0.00%
Asian	1	0.45%
Disabled	5	2.23%
Other (including white male)	162	72.32%
Total	224	100.00%
509: Miscellaneous durable goods (wholesale)		
Female	23	25.84%
Black	1	1.12%
Hispanic	0	0.00%
American Indian	0	0.00%
Aleut	0	0.00%
Asian	2	2.25%
Disabled	1	1.12%
Other (including white male)	62	69.66%
Total	89	100.00%

(continued)

Table 6. Women- and minority-owned business population estimates, by SIC code (continued)

<u>Race/gender of business owner</u>	<u>Number reported (sample size)</u>	<u>Share of total (sample proportion)</u>
511: Paper and paper products		
Female	42	28.38%
Black	0	0.00%
Hispanic	0	0.00%
American Indian	0	0.00%
Aleut	0	0.00%
Asian	4	2.70%
Disabled	3	2.03%
Other (including white male)	99	66.89%
Total	148	100.00%
514: Groceries and related products		
Female	55	23.81%
Black	2	0.87%
Hispanic	1	0.43%
American Indian	1	0.43%
Aleut	0	0.00%
Asian	0	0.00%
Disabled	6	2.60%
Other (including white male)	166	71.86%
Total	231	100.00%
701: Hotels and motels		
Female	177	62.99%
Black	1	0.36%
Hispanic	2	0.71%
American Indian	1	0.36%
Aleut	0	0.00%
Asian	1	0.36%
Disabled	6	2.14%
Other (including white male)	93	33.10%
Total	281	100.00%

(continued)

Table 6. Women- and minority-owned business population estimates, by SIC code (continued)

<u>Race/gender of business owner</u>	<u>Number reported (sample size)</u>	<u>Share of total (sample proportion)</u>
721: Laundry, cleaning and garment services		
Female	114	55.07%
Black	2	0.97%
Hispanic	1	0.48%
American Indian	0	0.00%
Aleut	0	0.00%
Asian	2	0.97%
Disabled	2	0.97%
Other (including white male)	86	41.55%
Total	207	100.00%
726: Funeral service and crematories		
Female	42	26.25%
Black	0	0.00%
Hispanic	0	0.00%
American Indian	0	0.00%
Aleut	0	0.00%
Asian	0	0.00%
Disabled	4	2.50%
Other (including white male)	114	71.25%
Total	160	100.00%
733: Mailing, reproduction and stenographic services		
Female	80	39.22%
Black	0	0.00%
Hispanic	1	0.49%
American Indian	1	0.49%
Aleut	0	0.00%
Asian	4	1.96%
Disabled	1	0.49%
Other (including white male)	117	57.35%
Total	204	100.00%

(continued)

Table 6. Women- and minority-owned business population estimates, by SIC code (continued)

<u>Race/gender of business owner</u>	<u>Number reported (sample size)</u>	<u>Share of total (sample proportion)</u>
734: Services to buildings		
Female	113	47.28%
Black	4	1.67%
Hispanic	2	0.84%
American Indian	0	0.00%
Aleut	0	0.00%
Asian	5	2.09%
Disabled	5	2.09%
Other (including white male)	110	46.03%
Total	239	100.00%
735: Miscellaneous equipment rental and leasing		
Female	45	37.50%
Black	1	0.83%
Hispanic	0	0.00%
American Indian	0	0.00%
Aleut	0	0.00%
Asian	0	0.00%
Disabled	1	0.83%
Other (including white male)	73	60.83%
Total	120	100.00%
737: Computer and data processing services		
Female	72	24.32%
Black	4	1.35%
Hispanic	5	1.69%
American Indian	0	0.00%
Aleut	0	0.00%
Asian	6	2.03%
Disabled	5	1.69%
Other (including white male)	204	68.92%
Total	296	100.00%

(continued)

Table 6. Women- and minority-owned business population estimates, by SIC code (continued)

<u>Race/gender of business owner</u>	<u>Number reported (sample size)</u>	<u>Share of total (sample proportion)</u>
753: Automobile repair		
Female	83	24.41%
Black	2	0.59%
Hispanic	1	0.29%
American Indian	0	0.00%
Aleut	1	0.29%
Asian	0	0.00%
Disabled	3	0.88%
Other (including white male)	250	73.53%
Total	340	100.00%
754: Automobile services, except repair		
Female	39	32.50%
Black	3	2.50%
Hispanic	0	0.00%
American Indian	0	0.00%
Aleut	0	0.00%
Asian	0	0.00%
Disabled	3	2.50%
Other (including white male)	75	62.50%
Total	120	100.00%
764: Reupholstery and furniture repair		
Female	27	50.00%
Black	1	1.85%
Hispanic	0	0.00%
American Indian	0	0.00%
Aleut	0	0.00%
Asian	0	0.00%
Disabled	1	1.85%
Other (including white male)	25	46.30%
Total	54	100.00%

(continued)

Table 6. Women- and minority-owned business population estimates, by SIC code (continued)

<u>Race/gender of business owner</u>	<u>Number reported (sample size)</u>	<u>Share of total (sample proportion)</u>
807: Medical and dental labs		
Female	16	17.20%
Black	1	1.08%
Hispanic	2	2.15%
American Indian	0	0.00%
Aleut	0	0.00%
Asian	2	2.15%
Disabled	1	1.08%
Other (including white male)	71	76.34%
Total	93	100.00%
871: Engineering and architectural services		
Female	49	14.29%
Black	1	0.29%
Hispanic	4	1.17%
American Indian	0	0.00%
Aleut	0	0.00%
Asian	16	4.66%
Disabled	4	1.17%
Other (including white male)	269	78.43%
Total	343	100.00%
872: Accounting services		
Female	81	19.90%
Black	1	0.25%
Hispanic	0	0.00%
American Indian	1	0.25%
Aleut	0	0.00%
Asian	0	0.00%
Disabled	9	2.21%
Other (including white male)	315	77.40%
Total	407	100.00%

(continued)

Table 6. Women- and minority-owned business population estimates, by SIC code (continued)

<u>Race/gender of business owner</u>	<u>Number reported (sample size)</u>	<u>Share of total (sample proportion)</u>
873: Research and testing services		
Female	53	31.55%
Black	0	0.00%
Hispanic	0	0.00%
American Indian	0	0.00%
Aleut	1	0.60%
Asian	2	1.19%
Disabled	3	1.79%
Other (including white male)	109	64.88%
Total	168	100.00%
874: Management and public relations services		
Female	90	28.57%
Black	4	1.27%
Hispanic	1	0.32%
American Indian	0	0.00%
Aleut	0	0.00%
Asian	6	1.90%
Disabled	2	0.63%
Other (including white male)	212	67.30%
Total	315	100.00%

Table 7. Frequency of discrimination

	<u>Female</u>	<u>Black</u>	<u>Hispanic</u>	<u>Indian</u>	<u>Asian</u>
	(percent)				
Those reporting race or gender discrimination	30	57	41	29	49
Reported instances of discrimination					
0	2	6	0	0	0
1-5	68	39	44	71	69
5-10	11	11	31	19	19
More than 10	19	44	25	10	12
Those reporting being discouraged from entering business because of race or gender	20	32	26	15	22

Survey of women- and minority-owned firms

Women- and minority-owned businesses in Minnesota were surveyed to identify their business problems and to determine if any discernible patterns of discrimination existed.¹⁸ Sixty-four percent of these firms responded to the survey.¹⁹ More than one-third of those business owners stated they believed their business had been subjected to discrimination because of their race or gender, and 19 percent said they had been discouraged from beginning their business because of their race or gender. The extent of reported discrimination varied by race or gender (Table 7). A larger percentage of Black business owners reported experiencing discrimination than did other groups. Black business owners reported they had experienced more separate incidents of discrimination than members of other groups.

¹⁸ The survey was conducted by the University of Minnesota Survey Research Center under contract with the Department of Administration. A complete description of the survey and its methods is found in the appendices.

¹⁹ Firms that had terminated business were eliminated from the calculation. The total number of firms that responded was 687.

Table 8. Sources of discrimination

<u>Source of discrimination</u>	<u>Female</u>	<u>Black</u>	<u>Hispanic</u>	<u>Indian</u>	<u>Asian</u>
	(percent)				
Purchasing (nongovernment)	23	40	47	39	56
Purchasing (government)	29	30	41	48	22
Prime contractors	32	43	35	39	44
Subcontractors	18	23	12	13	11
Lending institutions	33	48	35	22	17
Bonding	5	28	2	9	11

Business owners who reported discrimination were asked to identify the primary sources of that discrimination. As Table 8 indicates, these responses also show considerable variation by race or gender.

In an effort to gain more specific information, these business owners were asked to respond to questions about the nature of the discrimination they reported (Table 9).

Business owners were also asked whether they had reported any discrimination they experienced to organizations such as human rights offices or trade associations. The frequency with which such experiences were reported was quite low (Table 10).

Table 9. Forms of discrimination

<u>Form of discrimination</u>	<u>Female</u>	<u>Black</u>	<u>Hispanic</u>	<u>Indian</u>	<u>Asian</u>
	(percent)				
Late notice	26	46	20	41	35
Bid not accepted	29	46	33	32	18
Shopping on bid ²⁰	29	56	27	27	24
Using higher bid	30	54	66	50	35

Table 10. Reporting discrimination

	<u>Female</u>	<u>Black</u>	<u>Hispanic</u>	<u>Indian</u>	<u>Asian</u>
	(percent)				
Percent reporting action was taken to report the discrimination	6	10	0	4	6

²⁰ "Shopping on bid" refers to the practice of using one firm's bid to secure more favorable quotations from other companies.

Table 11. Major problems experienced

<u>Area of major problem</u>	<u>Female</u>	<u>Black</u>	<u>Hispanic</u>	<u>Indian</u>	<u>Asian</u>
	(percent)				
EQUITY FINANCING (1987 white male - 42%) ²¹	26	55	39	44	44
DEBT FINANCING (1987 white male - 37%)	27	49	36	33	38
BANKING RELATIONS (1987 white male - 21%)	17	37	19	24	30
CASH FLOW (1987 white male - 34%)	26	32	26	24	32
SECURING BONDING (Not included in 1987)	13	35	14	21	21
GOV. REGULATIONS (1987 white male - 21%)	24	25	22	32	34
FINDING QUALIFIED EMPLOYEES (1987 white male - 24%)	26	34	21	20	38

²¹ The analysis by Brenda Miller conducted under contract with the Department of Administration on the 1987 Study of New Firms in Minnesota published by the Center for Urban and Regional Affairs provides baseline data on white male-owned firms for comparison with the results of the 1989 survey of women- and minority-owned firms.

Table 12. Major problems not resolved

<u>Area of major problem</u>	<u>Female</u>	<u>Black</u>	<u>Hispanic</u>	<u>Indian</u>	<u>Asian</u>
			(percent)		
EQUITY FINANCING (1987 white male - 22%)	30	58	42	35	25
DEBT FINANCING (1987 white male - 26%)	33	63	25	44	36
BANKING RELATIONS (1987 white male - 9%)	16	36	38	26	16
CASH FLOW (1987 white male - 18%)	16	34	21	18	21
SECURING BONDING (Not included in 1987)	31	50	44	44	31
GOV. REGULATIONS (1987 white male - 23%)	25	46	23	35	44
FINDING QUALIFIED EMPLOYEES (1987 white male - 30%)	24	33	32	32	25

Women- and minority-owned firms were also asked a series of questions about the nature of the problems they faced when they started the business (Table 11).

Respondents who experienced these major problems were also asked the extent to which they had been able to resolve the problem. Business owners could report the problem as fully resolved, partially resolved or not resolved. Table 12 reflects the percentage of business owners who had reported these major problems and who considered the problems unresolved.

The survey also sought information on prior set-aside and preference programs' effects on these firms. Fifty-nine percent of all survey respondents said they participated in purchasing preference programs. Forty-six percent reported that the preference program increased their nongovernment business. The preference programs were perceived as enhancing their firms' profitability by almost two-thirds of the respondents. Almost 40 percent said that they would be only marginally viable or not viable at all without the programs.

Table 13 sets out the results of that series of questions, showing the pattern of experience by race and gender.

Table 13. Impact of preference/set-aside programs

<u>Questions</u>	<u>Female</u>	<u>Black</u>	<u>Hispanic</u> (percent)	<u>Indian</u>	<u>Asian</u>
Participated in preference or set-aside programs? Answer - yes	58	72	52	61	67
If participated, were they awarded contracts or purchases because of programs? Answer - yes	62	57	74	69	56
Is the firm viable without the programs?					
Yes	68	33	55	42	64
Marginally	21	52	32	46	32
No	11	15	14	12	4
Has the program enhanced firm profits?					
Yes, a lot	15	21	36	18	25
Yes, a little	49	47	41	56	33
No	36	31	23	27	4
Has the program increased your non-government business?					
Yes, a lot	10	28	36	23	29
Yes, a little	32	33	36	32	13
No	58	40	27	46	58

1987 New Firms Study

The Center for Urban and Regional Affairs published a study by Paul Reynolds and Brenda Miller on new business firms in Minnesota. The data collected for that study was drawn from a sample of firms starting business in Minnesota between 1979 and 1984. Brenda Miller analyzed that data base to identify any major differences between firms begun by white males and those begun by white females or nonwhites. Her complete analysis is found in the appendices to this report. Because of the small sample size, she was not able to analyze data by specific race. Instead, the categories were white male, white female and minority. The major differences she discovered are discussed by category:

Type and location of business founded

Sixty-five percent of the firms in the sample were started by teams of one or more individuals that were at least 50 percent white male. Thirty percent were formed by teams that were 50 percent white females, and 4 percent by nonwhites. Firms most likely to be doing business with government were even more predominately founded by white males. Seventy percent of those firms were begun by white males, 24 percent by females and 6 percent by nonwhites.

This difference reflects the fact that white males, white females and nonwhites were found to be entering different types of businesses. Firms owned by racial minorities were more likely to be in the service category, both producer and consumer services, and less likely in retail. In contrast, female-owned businesses were underrepresented in manufacturing. White female- and white male-owned firms were as likely to be located in Greater Minnesota as in the Twin Cities metropolitan area, which was not true for nonwhite-owned firms. Of the sample, 83 percent of the nonwhite-owned firms were in the metropolitan area and, when firms most likely to be doing business with government were examined, all the nonwhite firms were located in the Twin Cities metropolitan area.

Patterns of business growth

The patterns of business development were identified in several ways. A distinction was drawn between high-growth and low-growth firms based on whether the firm had annual sales growth greater than \$100,000 per year. Eighty-five percent of female-owned firms examined were low-growth firms. This is significantly more than the 68 percent of white male-owned firms and 60 percent of nonwhite-owned firms that were in the low-growth category. The difference was even more pronounced for those firms most likely to be undertaking government business.

The second characteristic of business development was whether the business focused on serving a local Minnesota market or was exporting its goods or services beyond the state boundaries. Eighty percent of the female-owned firms were categorized as local market firms with low growth, in contrast with approximately 60 percent of the white male- and nonwhite-owned firms.

Experience and background of firm principals

Approximately 68 percent of the principals in white male-owned firms came from established organizations to start their new businesses, compared with 51 percent of those in female-owned and 58 percent in minority-owned firms. Principals from white female-owned firms were the most likely to have been recently unemployed or in "other" situations prior to starting the firm, while those from minority-owned firms were the most likely to have been in school just prior to starting a new firm. The principals' work experience in the industry also varied significantly by race and gender. Female principals and minorities had worked fewer years in the same industry than white males: 5.4 years for white females, 7.7 for minorities, compared with 9.0 years for white males. In addition to this difference in work experience, there was considerable difference in the level of educational attainment prior to starting a new firm. A much larger proportion of minorities who started new business firms had college or advanced degrees than either white women or white males. Fifty-four percent of minority principals had those degrees, compared with 44 percent of the white males and 28 percent of the females.

Start-up problems

Questions were asked in the survey to identify start-up-problem experience by these new firms and the extent to which those problems had been resolved. In all categories, female-owned firms reported a lower level of initially severe problems than did white males, while the frequency of problems reported by minority firms was consistently higher. The lower level of problems experienced by female-owned businesses was consistent with the fact that more of their businesses were in the local low-growth categories that, by their nature, generally experience fewer problems.

Financing

The sources of informal prestart financing varied by race and gender. Female-owned firms reported more financing from family and personal savings, while minorities reported financing their businesses through suppliers' credit and by forgoing salary.

White male-owned firms indicated more informal financing through money from friends and business associates. White male-owned firms received more financing in the form of machinery and equipment loans initially and working capital loans than did the others.

Other research

The survey to determine race and gender of business ownership conducted for this study and Brenda Miller's analysis of the 1987 New Firms Study found that women and minorities enter different types of businesses than do white males. This is corroborated by research published in several articles. Sue Birley wrote in the *Journal of Small Business Management*, "It is not surprising that many women enter markets which are 'not traditionally male dominated' — the service industry and, most commonly, retailing."²² John Heywood, writing in the *Review of Black Political Economy*,²³ found that retail and service sectors of the economy are the most competitive, and because market power is not concentrated in the hands of a few firms, these industries cannot maintain discriminatory barriers. He found the share of Black ownership in the most competitive industries to be almost 10 times the Black ownership in the industry groups that are highly concentrated and least competitive.

The differences in experience reported in the 1989 survey of women- and minority-owned businesses reflects differences found by Faith Ando in research for an article on access to capital and minority businesses.²⁴ Ando found that Black, Asian and Hispanic business owners all had roughly the same human and financial capital available to them, but that Black business owners were discriminated against by lending institutions when seeking business loans. Once a loan was obtained, all groups appeared to receive the same terms, but Black-owned firms had more difficulty in securing the initial approval than did other groups.

Finally, both the City of San Francisco and the City of Seattle have completed studies of discrimination within their jurisdictions during 1989 to meet the requirements of the Croson case. In both cases, underutilization was found, although the rate of underutilization differed by both race and gender as well as line of business. In response to its study, the City of San Francisco adopted a program giving a 5 percent preference to San Francisco (locally) based businesses and a 10 percent preference to local female- and minority-owned businesses. American Indians were removed from the list of nonwhite business owners eligible for a preference because there was not enough evidence of discrimination on a statistical basis. Preference goals by race and gender by industry were also created.

The report issued by the consultants for the City of Seattle recommended adjusting

²² Sue Birley, "Female Entrepreneurs: Are They Really Any Different?," *Journal of Small Business Management*, January 1989.

²³ John S. Heywood, "Market Structure and the Pattern of Black-owned Firms," *Review of Black Political Economy*, Spring 1988.

²⁴ Faith H. Ando, "Capital Issues and the Minority-owned Business," *Review of Black Political Economy*, Spring 1988.

the overall purchasing goals to reflect new information contained in the report on the availability of women- and minority-owned businesses. In addition, it recommended increasing the goals to 110 percent of availability to provide incentive for new women and minority entrants to the field. It also recommended that these adjustments be re-evaluated after no more than five years and that firms be graduated from the program after 10 years or when their average annual revenues for the prior three years exceeded 125 percent of the industry average.

Data availability

The state, metropolitan agencies and the University of Minnesota vary in the manner in which they maintain their records of purchasing transactions. For example, purchases on behalf of the state by the Department of Administration are recorded using a coding system containing more than 400 different codes. On the other hand, the University of Minnesota has developed a different coding system. Since the university files examined for this study were not computerized, the university coding system had not been used in preparing the files. Differences such as these were found in each agency. The Department of Jobs and Training was hired to assist in the preparation of this study by recategorizing all codes used by the Department of Administration into Standard Industrial Classification codes. Each of the other data bases was recoded by personnel in Management Analysis using the SIC manual and descriptive information contained in the sampled files.

SUFFICIENT JUSTIFICATION:

Conclusions

Sufficient evidence of discrimination exists both in the record of government purchasing and in private-sector activities to satisfy the judicial requirements of the Croson and subsequent cases. The evidence of public-sector discrimination is based on the statistically significant underutilization found in the sample. The evidence of private-sector discrimination is based on survey results, which are corroborated both by their comparison to the 1987 New Firms Study results and the wide variation in experience reported by race and gender.

This evidence of discrimination is not, however, uniform across race and gender lines. The analysis of purchasing indicates that in many categories no statistically significant disparity exists for various racial groups. The lack of disparity can mean either that the firms are already being employed in relative proportion to their availability or that there are no minority-owned firms available in that line of work.

The differences between gender and racial groups are also revealed in reported discrimination. Blacks believe their firms have been subject to discrimination more than any other group. Black business owners indicate the most difficulty in obtaining equity and debt financing. They report the most difficulty establishing banking relationships and generally securing adequate financing. This level of problems encountered and the difficulty in resolving them were consistently and substantially higher than those found in the 1987 survey of business firms. Blacks were also discouraged more than any other group from becoming business owners. In contrast, Asian business owners reported the most problems finding qualified employees and coping with government regulations. American Indian-owned businesses also reported a high level of unresolved problems coping with government regulations and substantial problems with both debt and equity financing. Female-owned firms, which showed almost uniform underutilization in every government purchasing category, reported fewer actual business problems such as securing debt and equity financing than the white male firms surveyed in 1987.

These differences provide evidence of discrimination that takes varying forms and affects the firms in different ways. Some of these specific problems might be addressed by race- or gender-neutral programs. For example, an effort to simplify government regulations would assist all businesses but would particularly benefit Asian- and Indian-owned businesses, which report more difficulty in coping with government regulations. A program aimed at providing easier access to debt and equity capital would assist more black-owned businesses than other groups. However, specific programs will not eliminate the underutilization found in

government purchasing. Female-owned firms consistently are the most underutilized, according to the purchasing study, yet these firms also report fewer specific problems than their white male or minority counterparts. As a result, programs designed to eliminate business problems will assist white male- and minority-owned firms more than female-owned firms. While such programs may make the job of managing the business easier, they will not address underutilization, since that underuse does not appear to be related to the level or type of business problems experienced.

Past race- and gender-based set-aside and preference programs have directly benefited these firms in several ways. First, the underutilization of Black business owners disappeared in several of the categories when contracts let because of set asides or preferences were included in the totals. For other groups, the size of the disparity was smaller because of the set-aside or preference programs. The set-aside or preference programs did not have a larger impact on the disparity because firms located in labor surplus areas or counties with low median income received a disproportionate share of contracts let under the set-aside and preference programs.

In addition to addressing the underutilization of women- and minority-owned firms, the set-aside and preference programs benefited these firms by increasing the firms' profits. A substantial percentage of Black, Hispanic and American Indian business owners responded that their firms would not be financially viable without the programs. The programs have, then, helped more of these businesses survive while, it appears, the programs have worked to supplement and enhance profitability of businesses owned by Asians or females.

While the set-aside and preference programs have provided some benefit to women- and minority-owned firms, the analysis of awards made under these programs indicates that women- and minority-owned firms do not secure a proportionate share of even these set-aside and preference awards.

Data on purchasing programs is maintained by the state, metropolitan agencies and the University of Minnesota in disparate fashion that makes the compilation of consistent information costly and time consuming.

SUFFICIENT JUSTIFICATION:

Recommendations

1. A race- and gender-based program to benefit female- and minority-owned businesses should be enacted by the legislature. There is sufficient evidence of discrimination against these firms to satisfy the tests established by the Supreme Court in its Croson decision.
2. A race- and gender-based program should reflect the varying population of women- and minority-owned firms by type of business.
3. The Department of Administration should be delegated authority to identify categories of purchasing qualifying for a race- and gender-based purchasing program operated by the state, university and metropolitan agencies. Selection should be based on the availability of firms. Benchmarks should be established at a level higher than current availability to prevent discouraging new minority- and women-owned firms from entering the field. The department should be required to revise the list of eligible purchasing categories based on new data at least once every five years. Additional resources may be necessary to implement this recommendation.
4. The purchasing preference granted firms qualifying under race and gender standards should be higher than the preference granted to firms qualifying on other grounds. A program establishing differing level of preferences — for example, granting a higher preference to socially disadvantaged firms while continuing the existing preference level for firms located in labor surplus areas or in counties with low median income — would assist women- and minority-owned firms in securing a more proportionate share of awards.
5. The Department of Administration or another agency should be delegated authority to develop consistent methods of classifying purchase types and data collection on the administration of these programs for state and metropolitan government and the University of Minnesota. The designated agency should be required to prepare a biennial report for the legislature on the administration of this law encompassing information from these entities. Resources may be needed to accomplish this comprehensive reporting and review.
6. Additional efforts should be made by state government to increase sensitivity toward and awareness of women- and minority-owned firms by both government and nongovernment purchasing organizations. One method of accomplishing this would be state-sponsored training marketed to both government and nongovernment purchasing organizations.
7. State agencies with regulatory oversight of lending institutions should be directed to review institutional lending practices to see if discrimination exists and what additional steps are necessary to eliminate it. Federal agencies should be asked to do the same.

**A Study of
Discrimination
Against Women-
and Minority-owned
Businesses
and of Other
Small-business Topics**

Question 2.

Should the definition of small business be revised?

REVISED DEFINITION:

Findings

M.S. 645.445 defines the term "small business" in the following manner:

[A] business entity organized for profit, including but not limited to any individual, partnership, corporation, joint venture, association or cooperative, which entity:

(a) Is not an affiliate or subsidiary of a business dominant in its field of operation; and

(b) Has 20 or fewer full-time employees; or

(c) In the preceding fiscal year has not had more than the equivalent of \$1,000,000 in annual gross revenues; or

(d) If the business is a technical or professional service, shall not have had more than the equivalent of \$2,500,000 in annual gross revenues in the preceding fiscal year.

A firm "dominant in its field of operation" is defined as a business having more than 20 full-time employees and more than \$1 million in annual gross revenues or \$2.5 million in annual gross revenues if a technical or professional service. The phrase "affiliate or subsidiary of a business dominant in its field of operation" is defined as a business that is at least 20 percent owned by a business dominant in its field of operation, or by partners, officers, directors, majority stockholders, or their equivalent, of a business dominant in that field of operation.

Members of the Small Business Procurement Advisory Council, whose statutory duties include advising the commissioner of administration on matters relating to small business procurement, have criticized this definition as being too restrictive. Council members have expressed concern that current limitations based on revenues and number of employees are too low and too inflexible. For example, the \$1 million revenue and 20-employee limitation apply equally to a construction company and computer sales company despite the very different nature of their businesses. Council members state that a business may need to be substantially larger in one type of industry to compete because of economies of scale, yet it may still be a small business within that industry.

The Small Business Administration (SBA) defines small business based on revenues and/or the number of employees for specific industries. For example, small businesses in wholesale are those having fewer than 500 employees for the past year.

In retailing, the definition changes to those with less than \$3.5 million in receipts, on average, for the prior three years. In contrast, construction firms qualify as small business if their average receipts have been less than \$17 million annually.

The State of Washington uses the SBA definitions. Program administrators in that state indicated that the advantage of this approach is the consistency between state and federal operations, reducing confusion and increasing the compatibility of data collection and enforcement. A disadvantage acknowledged by Washington officials was that the size limitations are quite large by state standards, so many firms qualify under the definition of small business.

On the other hand, California has adopted definitions that change by industry but that are not tied to the SBA definition. That state's law requires that ". . . the [size] definition shall vary from industry to industry to the extent necessary to reflect the differing characteristics of such industries" [Calif. Code Sec. 14837(c)]. The California Department of General Services has authority to implement this statutory section; the agency has developed size limitations within more than 100 lines of business to define small businesses.

Customizing definitions of small business to the state business conditions can provide a more accurate assessment of a small business within each line of business. The process, however, does require more analytical capability and administrative time than the application of either the SBA definition or the current flat size standards in Minnesota.

To implement the 1989 Minnesota legislation on economically disadvantaged business, the Department of Administration is using market share information to help define when businesses qualify as economically disadvantaged. A financial profile of a business is compared with a standard to determine the relative competitiveness of the industry. The profile identifies factors such as liquidity, leverage and market share. An assessment is then made of available financial support to determine the firm's eligibility for the program.

In the course of surveying businesses for preparation of this report, information was sought about firm size by line of business. Using three-digit SIC codes as the basis for classifying firms, the survey results indicate that while the majority of firms in each of the surveyed codes had revenues of less than \$1 million annually, there is substantial variation among the industries in firm size. For example, in SIC code 514 (groceries and related products), 44 percent of the firms had revenues of less than \$1 million annually, almost 19 percent had revenues between \$1 million and \$3 million annually and more than 22 percent of the firms had annual revenues in excess of \$9 million. Depending on the share of the total market held by the largest firms, the businesses with revenues of less than \$3 million all may be small businesses relative to the market.

The complete results by three-digit SIC code are shown in Table 14.

TABLE 14. Distribution of Minnesota firms within selected SIC codes, by annual gross revenue

	Gross revenue in millions of dollars					
	<1	1 to 3	3 to 5	5 to 7	7 to 9	>9
Non-residential building construction (SIC 154)	53.55%	22.34%	7.45%	3.19%	2.84%	10.64%
Highway and street construction (161)	61.43%	9.29%	10.71%	7.14%	1.43%	10.00%
Heavy construction, except highway (162)	64.81%	18.45%	6.44%	1.72%	1.29%	7.30%
Plumbing, heating and air-conditioning contractors (171)	84.18%	11.48%	1.53%	0.77%	0.26%	1.79%
Painting and paper hanging (172)	95.96%	2.24%	0.00%	0.45%	0.00%	1.35%
Electrical work (173)	85.39%	9.55%	1.69%	0.84%	0.00%	2.53%
Masonry, stonework and plastering contractors (174)	84.52%	11.29%	1.94%	0.65%	0.00%	1.61%
Carpentry and floor work (175)	90.91%	5.88%	3.21%	0.00%	0.00%	0.00%
Roofing, siding and sheet metal work (176)	79.74%	12.42%	4.58%	1.96%	0.65%	0.65%
Concrete work (177)	84.97%	10.88%	1.55%	1.55%	0.52%	0.52%
Water well drilling (178)	88.52%	8.20%	3.28%	0.00%	0.00%	0.00%
Miscellaneous special trade contractors (179)	78.85%	13.62%	4.30%	1.08%	0.36%	1.79%
Printing trade services (279)	71.01%	18.84%	2.90%	0.00%	1.45%	5.80%
Medical instruments and supplies (384)	48.98%	32.65%	0.00%	0.00%	2.04%	16.33%
Trucking and courier services (421)	79.14%	10.70%	2.67%	0.80%	0.27%	6.42%
Passenger transportation arrangement (472)	42.08%	46.99%	4.92%	1.64%	1.64%	2.73%

(continued)

TABLE 14. Distribution of Minnesota firms within selected SIC codes, by annual gross revenue (continued)

	Gross revenue in millions of dollars					
	<1	1 to 3	3 to 5	5 to 7	7 to 9	>9
Freight transportation arrangement (473)	50.75%	29.85%	5.97%	0.00%	0.00%	13.43%
Telephone communications (481)	42.65%	26.47%	4.41%	2.94%	0.00%	23.53%
Motor vehicle parts and supplies, wholesale (501)	56.72%	20.17%	5.46%	5.88%	0.84%	10.92%
Furniture and home furnishings (502)	62.11%	18.63%	3.73%	0.62%	0.62%	14.29%
Professional and commercial equipment, wholesale (504)	48.76%	16.96%	4.24%	5.65%	3.53%	20.85%
Electrical goods, wholesale (506)	52.11%	18.01%	6.51%	2.30%	1.15%	19.92%
Hardware, plumbing and heating equipment, wholesale (507)	52.27%	22.27%	5.45%	3.64%	2.27%	14.09%
Miscellaneous durable goods, wholesale (509)	66.27%	19.28%	3.61%	1.20%	0.00%	9.64%
Paper and paper products, wholesale (511)	48.18%	21.90%	4.38%	3.65%	2.19%	19.71%
Groceries and related products, wholesale (514)	44.59%	18.92%	6.76%	6.31%	0.90%	22.52%
Hotels and motels (701)	85.82%	9.09%	1.09%	1.09%	1.09%	1.82%
Laundry, cleaning and garment services (721)	88.73%	5.88%	1.96%	0.00%	0.00%	3.43%
Funeral service and crematories (726)	95.60%	3.14%	1.26%	0.00%	0.00%	0.00%
Mailing, reproduction and stenographic services (733)	87.94%	7.54%	2.51%	0.50%	0.50%	1.01%
Services to buildings (734)	95.69%	3.02%	0.86%	0.00%	0.00%	0.43%
Miscellaneous equipment rental and leasing (735)	80.00%	9.57%	0.00%	0.00%	0.87%	9.57%

(continued)

TABLE 14. Distribution of Minnesota firms within selected SIC codes, by annual gross revenue (continued)

	Gross revenue in millions of dollars					
	<1	1 to 3	3 to 5	5 to 7	7 to 9	>9
Computer and data processing services (737)	76.57%	12.94%	3.15%	2.45%	0.00%	4.90%
Automobile repair (753)	92.45%	5.44%	0.91%	0.00%	0.60%	0.60%
Automobile services, except repair (754)	91.38%	6.03%	2.59%	0.00%	0.00%	0.00%
Reupholstery and furniture repair (764)	92.59%	5.56%	0.00%	1.85%	0.00%	0.00%
Medical and dental labs (807)	85.56%	5.56%	2.22%	2.22%	1.11%	3.33%
Engineering and architectural services (871)	72.16%	17.37%	2.99%	2.40%	0.60%	4.49%
Accounting services (872)	94.26%	3.74%	0.50%	0.00%	0.25%	1.25%
Research and testing services (873)	69.57%	15.53%	2.48%	0.62%	0.62%	11.18%
Management and public relations services (874)	81.70%	10.13%	2.94%	2.29%	0.00%	2.94%

REVISED DEFINITION:

Conclusions

A definition of small business that recognizes the different competitive conditions within various lines of business would more accurately identify businesses that are considered small within an industry.

Adopting the SBA definitions would eliminate the administrative burdens of developing Minnesota-applicable definitions. However, devoting resources to examine the evidence of industry size and competitiveness to establish a Minnesota-specific definition would focus the benefits derived from a small business classification on those firms that are small in relation to the market and their competition.

The Department of Administration is developing expertise with this type of analysis as it works to refine the definition of economically disadvantaged under the 1989 law.

The department can use this experience to administratively determine appropriate size criteria for small business within different industries.

REVISED DEFINITION:

Recommendation

1. The Department of Administration should be delegated authority to establish size definitions of small business by type of business. The definitions should recognize the differences between various industries caused by the size of the market for their goods or services and the relative size and market share of their competitors. Resources to develop those definitions and to monitor the need for changes may be needed.

**A Study of
Discrimination
Against Women-
and Minority-owned
Businesses
and of Other
Small-business Topics**

Question 3.

**Are there alternative programs to stimulate
growth opportunities for small business?**

ALTERNATIVE PROGRAMS:

Findings

Minnesota government currently provides a variety of services to small businesses and offers an opportunity to increase their sales through the state purchasing programs.

M.S. 16B.19 directs the commissioner of administration to ensure that small businesses receive at least 25 percent of the anticipated total state procurement, including printing and construction. To accomplish that goal, the commissioner is to vary the goods and services procured so that a variety of goods and services produced by different small businesses are acquired each year. In addition, the commissioner is to designate small business procurements to encourage proportional distribution of the awards among the geographical regions of the state. Subdivision 2 of that section requires all state agencies to designate at least 25 percent of their anticipated consultant, professional or technical services for small businesses. Requirements of a similar nature apply to purchases made by the University of Minnesota.

In addition to this general designation of 25 percent of state purchases for small business, small businesses that are "economically disadvantaged" qualify for a 5 percent preference in the amount bid on all state procurements.²⁵ These economically disadvantaged firms are also to be used as subcontractors by successful bidders on state contracts awarded with a value in excess of \$200,000.²⁶

A small business qualifies as "economically disadvantaged" when:²⁷

- the owner resides or is employed in a county in which the median income for married couples is less than 70 percent of the state median income for married couples; or
- the owner resides or is employed in an area designated a labor surplus areas by the United States Department of Labor; or
- the owner lacks adequate external support necessary to operate a competitive business enterprise as evidenced by diminished ability to secure long-term or working capital financing; equipment, raw material or supplier trade credit; bonding and insurance; or if the business has not captured a proportionate share of the market for its goods or services; or

²⁵ M.S. 16B.19, Subd. 5.

²⁶ M.S. 16B.19, Subd. 6.

²⁷ M.S. 645.445.

- the business filed its first annual federal and state income tax returns that reflected its operation within the preceding five years or will file its first annual return that reflects its operation as a business within the next 12 months; or
- the business is a rehabilitation facility or work activity program.

To implement the provisions of the third criterion for qualification as “economically disadvantaged,” the Department of Administration is developing criteria to identify firms that lack the support necessary for competitive business. The process of identification begins with an economic profile of each company seeking certification under this section. The profile identifies the financial viability of the firm based on criteria such as liquidity, leverage and market share. When a firm captures its proportionate market share, it will be graduated from the program and lose its status as an economically disadvantaged small business.

The 1987 New Firms Study found that almost two-thirds of the firms it surveyed both started small and stayed small.²⁸ Under the current law, a firm will lose its eligibility for preference five years after the date of its first award or after five years of operation if it was certified under the new business provision of the law.

Since 1989, the University of Minnesota and metropolitan agencies accept the Department of Administration’s certification of firms as small businesses or as economically disadvantaged small businesses. However, if the Department of Administration certification was granted under labor surplus or county median income provisions of the law, the certification cannot be accepted by the metropolitan agencies, since they are not allowed to include labor surplus or county median income qualifying firms within their programs for economically disadvantaged businesses.²⁹

Other jurisdictions

Birmingham, Alabama: The city of Birmingham has created a Community Development Corporation with a capital loan fund to aid “economically disadvantaged” small businesses that are new firms and to help existing economically disadvantaged businesses expand. The program defines a socially or economically disadvantaged business owner using a variety of criteria.

Socially disadvantaged individuals are those who have been subjected to discrimination, prejudice or cultural bias because of their identity as a member of a group without regard to their individual qualities, including, but not limited to, Black Americans. Evidence of social disadvantage includes the following elements:

²⁸ 1987 New Firms Study, p. 94.

²⁹ M.S. 16B.226.

The individual's social disadvantage must stem from his or her cultural or educational background, developmental deprivation, dialectical variation from prevailing speech patterns, physical handicap, long-term residence in an environment isolated from the mainstream of American society, or other similar cause not common to small business persons who are not socially disadvantaged.

- Except for Black Americans, the individual must have personally suffered social disadvantage. Mere membership in a group that could be considered socially disadvantaged is not sufficient.
- Except for Black Americans, the individual's social disadvantage must be at least partially rooted in treatment that he or she has experienced in Birmingham.
- The individual's social disadvantage must be chronic, long-standing and substantial, not fleeting or insignificant.
- The individual's social disadvantage must have demonstrably impeded his or her entry to business, and/or career advancement.

When determining eligibility, the program administrator is to consider, among other things, the denial of equal access to business or professional schools, denial of equal access to curricula, exclusion from social and professional association with students and teachers, denial of educational honors, and social patterns or pressures that may have a discouraging effect on the pursuit of professional or business education and among other aspects of professional advancement, pay and fringe benefits, other terms and conditions of employment; retaliatory behavior by an employer; and social patterns or pressures that may have the effect of retarding professional or business management development.³⁰

Economically disadvantaged individuals are generally "socially disadvantaged individuals who have suffered an impaired ability to compete in the free enterprise system due to diminished capital and credit opportunities, as compared to others in the same or similar lines of business and competitive market area who are not socially disadvantaged." Evidence of economic disadvantage may include, but is not limited to, the following:

- The personal financial condition of the disadvantaged individual compared with those of other individuals.
- The financial condition of the applicant firm compared with those of other local firms in the same business owned by nonsocially disadvantaged individuals,

³⁰ Working paper, Office of Economic Development, City of Birmingham, Ala., December 1989, pp. 2-4.

including, but not limited to, liquidity, leverage, operating efficiency and profitability.

- The socially disadvantaged individual or applicant firm's access to credit capital necessary to operate a competitive business enterprise.
- A comparison of the applicant firm's business and financial profile with profiles of firms in the same or similar line of business and competitive market area.³¹

The city has also established a Construction Assistance Authority to set goals for nonwhite and/or female-owned business in both the public and private sectors. The authority is to establish an institute to provide assistance to the construction industry. Certification of firms not already certified under federal programs occurs through a rebuttable presumption that businesses owned by nonwhites and/or women are socially disadvantaged. Any other firm may be certified as economically disadvantaged upon showing it has suffered discrimination or is disadvantaged in the construction industry.

The Construction Assistance Institute programs include training, certification of nonwhite- and/or female-owned businesses and disadvantaged businesses, technical assistance to certified firms and program evaluation.

Milwaukee, Wisconsin: The city of Milwaukee has developed a program that combines business training with a purchasing preference. Disadvantaged business owners may go through a certified training program in the financial and business aspects of owning and successfully operating a construction-related business enterprise and receive a 5 percent purchasing preference. If a prime contractor uses the "trained" vendor on a city contract, the contractor gets preference points based on the amount of trained economically disadvantaged businesses used on the project. The maximum points a company may receive is a 5 percent preference.

Milwaukee defines a disadvantaged individual as one experiencing substantial difficulty in achieving business-related success in the Milwaukee area as a result of at least three of the following:

1. Disadvantage with respect to education — failure to attain a high school degree or its equivalent for good reason or attendance in schools that have repeatedly achieved ratings below national, state and community averages in educational standards, educational standardized test scores and student grade point averages.
2. Disadvantage with respect to employment — a pattern of nonachievement in hiring, promotion and other aspects of employment advancement due to factors beyond the individual's reasonable control, a lack of current knowledge and skills necessary for employment, career advancement or consistent earning of average

³¹ *Ibid.*, pp. 4-6.

Annual income below the median income level of adults of comparable age in the city.

3. Social disadvantage — experience of substantial difficulty in attaining employment or business success at least in part due to location of the individual's residence and lack of mobility, lack of traditional family structure, being raised in a household receiving or personally receiving income consistently at or below the poverty line, being raised in a household requiring or personally requiring significant governmental assistance or support during the person's childhood, physical handicap or other causes beyond the individual's reasonable control.

4. Disadvantage with respect to residence or business location — location in an enterprise zone within the city for a period of not less than one year of the applicant's residence or the principal office and business of which the applicant is the sole owner or one of the owners and a principal operator.

5. Lack of business training of the operation of a business concern in the construction field or another field of economic endeavor that has been designated by the director and in which the applicant has experience.

In addition to having at least three of the foregoing characteristics, a business owner must be experiencing an economic disadvantage that is judged by a lack of capital, failure to obtain credit and other financial indicators [City of Milwaukee Ordinances, Chapter 360].

Interest in government services

The 1987 Minnesota New Firms Study conducted by Professor Paul Reynolds and Brenda Miller asked owners of new business firms their interest in possible government services. This survey encompassed a wide variety of firms, the majority of which were owned by white males. Table 15 lists the types of services with the percent of those surveyed who indicated a high interest in such services. The results on this table include responses from both white and nonwhite business owners.

TABLE 15. Interest in and value of potential government services

	<u>Percent with high interest</u>	<u>Average interest</u>
Marketing skills development	26	1.59
General business		
management development	21	1.51
Working capital financing	29	1.50
Finance skill development	24	1.49
Personnel management		
development	22	1.48
Training new employees	18	1.24
Knowledge of		
government regulations	14	1.22
AVTI small-business programs*	16	1.19
Machinery, equipment financing	17	1.13
Small-business development centers	14	1.08
Community college		
small-business programs	12	1.08
Entrepreneurial training	13	1.06
Building construction financing	19	1.06
Skills in labor-management relations	10	0.95
Retraining existing employees	11	0.94
New technology for productivity gains	13	0.93
Venture, seed capital financing	16	0.92
Land acquisition financing	13	0.81
Employee ownership financing	9	0.78
New site locations within a county	8	0.71
Engineering, scientific skill		
development	6	0.70
New site locations within Minnesota	7	0.62
Energy audits, conservation projects	7	0.59
Applying company's research and		
development in new markets	8	0.57
Federal procurement assistance	9	0.57
Infrastructure financing	6	0.55
Tourism market development	10	0.54
Energy development opportunities	6	0.53
Joint research and development		
product development	6	0.53
Small-business incubator sites	6	0.51
Develop foreign export markets	6	0.39
Average	14	0.93

Note: Interest scale: High, 3; Moderate, 2; Low, 1; None, 0.

*AVTI refers to area vocational technical institutes, a post-high school training system in operation in Minnesota.

After presenting this table, Reynolds and Miller conclude:

The large number of new firms initiated each year in Minnesota suggest that the absolute number of potential clients for these services may be substantial. Assuming that 10,000 new business entities are initiated annually in Minnesota, as many as 600 may be interested in the least popular service. The more popular would attract the interest of 3,000 each year. The more popular programs are likely to be related to financial assistance or programs to provide training and development of management, administrative or supervisory skills.³²

The responses to the 1987 New Firms Survey indicate that small business owners are most interested in training and education and business management development programs from government. The survey data does not, however, indicate whether the many existing education and training programs are insufficient or whether their availability is not widely known.

The next most desired program area by these business owners was for government services in the area of working capital financing.

The legislature has recently directed the Department of Trade and Economic Development to establish a means of evaluating small business assistance providers and to establish model evaluation techniques and performance standards for the providers.³³ The department has solicited for proposals to implement this provision. Working capital financing assistance for small business was passed by the legislature in 1989 but its funding was vetoed.³⁴

The 1987 New Firms Study also found that 24 percent of all business owners surveyed indicated that coping with government regulations was a major problem. Government regulations also posed a major problem for 26 percent of the women- and minority-owned firms survey in 1989. Twenty-nine percent of all respondents indicated an interest in assistance with government procurement.

There are currently a number of state-, federal- or nonprofit-sponsored resources for small business, providing to some extent the services that business owners identified as useful.

³² *1987 Minnesota New Firms Study, P. 65.*

³³ *Minnesota Laws 1989, Chapter 335, Art. 1, Sec. 142.*

³⁴ *Minnesota Laws 1989, Chapter 335, Art. 1, Sec. 146-155.*

A primary resource for small business in Minnesota is the Small Business Assistance Office in the Department of Trade and Economic Development. That office provides extensive publications concerning the problems of starting and operating small businesses and consultation through a business assistance center. In addition, the United States Small Business Administration provides publications and consultation and conducts seminars on small business operation. Other specific programs available to those either seeking to start a small business or wanting assistance in managing an existing business include:³⁵

Financing for small business

- Small business loans through the Small Business Administration
- City loan programs funded through the U.S. Department of Housing and Urban Development.
- Small business loans through the Farm Credit system and the Farmers Home Administration
- Minnesota Department of Trade and Economic Development:
 - Community Development Corporation Program
 - Opportunities Minnesota Incorporated
 - Small Business Development Loan Program
 - Small Cities Economic Development Program
 - Rural Development Board
 - Minnesota Public Facilities Authority
- Greater Minnesota Corporation
- Indian Business Loan Program (Indian Affairs Council, Bemidji, Minn.)
- Venture Capital Small Business Investment Companies (operating under the auspices of the Small Business Administration)
- Nonprofit Initiative Funds (Nonprofit organizations sponsored by a McKnight Foundation grant)
- Midwest Minnesota Community Development Corp. (private development corporation in Detroit Lakes, Minn.)

³⁵ *This listing of programs was drawn from several sources, including A Guide to Starting a Business in Minnesota, published by the Minnesota Small Business Assistance Office, and The States and Small Business, A Directory of Programs and Activities, U.S. Small Business Administration, 1988. No attempt was made to evaluate the effectiveness of these programs.*

Insurance assistance

- Joint Underwriting Association
- Market Assistance Plan

(These are state government created programs to assist businesses having difficulty obtaining liability insurance.)

Information and training

- Minnesota Small Business Assistance Office (Department of Trade and Economic Development)
- Minnesota Waste Management Technical Assistance Program (Minnesota Technical Assistance Center)
- Minnesota Trade Office
- Minnesota Extension Service
- Small Business Development Center Procurement Assistance Program
- Small Business Management Programs
- Both individual and group training is available through the Technical Institutes throughout Minnesota and the Community College system
- Small Business Development Centers
- Resource centers for information and counseling located throughout the State University and Community College systems
- SCORE (Service Corps of Retired Executives) offering assistance to new or existing businesses

ALTERNATIVE PROGRAMS:

Conclusions

Minnesota currently offers small business a variety of resources ranging from education and training to financing and set asides in government purchasing. The preference programs for economically disadvantaged businesses allow firms to qualify for the 5 percent purchasing preference on the basis of economic conditions of the geographic location of the owner or his (her) employment and on the economic conditions facing the firm. The Minnesota program is based on economic conditions and is race- and gender-neutral on its face.

The cities of Birmingham, Ala., and Milwaukee, Wis., are re-introducing social factors into the definition of economic disadvantage by creating rebuttable presumptions of disadvantage when certain social factors are present.

The current five-year limitation on participation in the preference programs may exclude a number of small businesses that both start small and remain small throughout their lifespan. If a firm is certified as economically disadvantaged on the basis of insufficient economic resources to compete, the five-year limitation on participation appears to arbitrarily harm the opportunities for that firm to sell to government when that economic disadvantage continues for the firm.

Studies have shown that there is a strong interest by new businesses in additional governmental services, particularly those providing training and financing. A large variety of programs ranging from financing to technical assistance exists throughout the state. In addition to education and training, the desire for working capital financing assistance was clear in the 1987 New Firms Survey data. From that survey data, it is not clear whether the programs currently available are not widely known by small business entrepreneurs, if their focus is not correct or if there is simply more demand for these programs than can be met.

Surveys have also indicated that coping with government regulation is a major problem for business owners.

ALTERNATIVE PROGRAMS:

Recommendations

1. The evaluation of existing programs to assist small business being prepared by the Department of Trade and Economic Development should be completed before determining if additional resources are necessary for small business education and technical assistance programs.
2. The Department of Trade and Economic Development should be directed to examine whether additional programs are necessary to provide working capital financing for small business.
3. The five-year limitation on eligibility for the economically disadvantaged small business preference program should not apply to a firm that qualifies on the basis of its lack of economic resources.
4. The Department of Administration should expand its efforts to assist small business to understand government purchasing procedures and to consider whether those procedures can be made simpler for small businesses.

**A Study of
Discrimination
Against Women-
and Minority-owned
Businesses
and of Other
Small-business Topics**

Question 4.

**Should the state have a preference program
incorporating urban and rural areas of high unemployment?**

URBAN AND RURAL AREAS:

Findings

Small business owners who reside or who are employed within geographic areas experiencing economic problems can qualify for a preference in government purchasing. The economic basis for qualification is that the area either must have been designated a labor surplus area by the United States Department of Labor or the area must be within a county where the median income is below 70 percent of the state median income for married couples.³⁶

Twenty-three counties in Minnesota have a median income for married couples less than 70 percent of the statewide median. All are located outside the Twin Cities metropolitan region. Cities with a population larger than 25,000 and counties are eligible for designation as labor surplus areas by the Department of Labor when their average unemployment rate exceeds by 20 percent the national average for a two-year period. Because both these definitions are tied to specific political boundaries (cities and counties), business owners located or employed in pockets of high unemployment or of low income, which are located within otherwise economically healthy cities or counties, cannot qualify for a preference on the basis of economic conditions in the locale.³⁷

Information is available from several sources that would allow identification of economically disadvantaged areas smaller than either a city or a county. Unemployment information may be correlated with census tract data available for urban areas. Census tracts are areas containing 3,000 to 4,000 individuals; that information may be further subdivided into information on city blocks with Census Bureau information. Information for census tracts or smaller areas is based on the 1980 Census. Current unemployment information is available only for areas with population of 25,000 or more, but information for smaller geographic and

³⁶ M.S. 645.445, Subd. 5.

³⁷ A business may qualify on other grounds. For example, Minnesota businesses that are less than 5 years old and those where the owner lacks adequate external support necessary to operate a competitive enterprise may qualify for purchasing preference regardless of location within the state. See M.S. 645.445, Subd. 5.

population size units may be estimated. These estimates are based on 1980 Census Bureau information.

The Neighborhood Revitalization Program³⁸ is an example of a current state program combining unemployment and census tract information. Under this program, a "targeted neighborhood" can be an area including one or more census tracts. The neighborhood is eligible for participation if it meets two of the following three conditions:³⁹

- It has an unemployment rate twice that of the Twin Cities metropolitan area;
- The median household income in the area is no more than half the median household income for the Twin Cities metropolitan area; or
- Twenty-five percent or more of the residential dwellings are in substandard condition or 70 percent or more were built before 1940.

This law allows a city to expand the designated area to include portions of adjoining census tracts under specified circumstances.

Another means of identifying areas experiencing economic hardship using a designation other than labor surplus or county median income is the state enterprise zone program.⁴⁰ That program provides tax incentives to businesses located in distressed areas. Sixteen enterprise zones currently exist, two of which are located in the Twin Cities metropolitan area.

A geographic area qualifies for designation as an enterprise zone only if it exhibits two of five signs of economic distress:⁴¹ substandard housing; low household income measured by a poverty level population of 20 percent or greater; declining values for commercial and industrial property; per capita income 90 percent or less that for the state; and either unemployment rates 120 percent of the statewide average or declining total employment.

At least one jurisdiction has a government purchasing program connected to geographic areas smaller than cities or counties. In New York City, city-based firms may qualify if 25 percent of its employees live in a Community Board Area (a designated portion of the city) having either high unemployment or high nonwhite populations. A firm may also qualify if it performed at least 25 percent of its business

³⁸ *M.S. 469.201. This program is available for first-class cities.*

³⁹ *The law specifically requires application of 1980 Census information in the administration of these provisions.*

⁴⁰ *M.S. 469.166.*

⁴¹ *Other criteria apply as well, such as minimum population requirements, the existence of vacant or underutilized land, property value limits, and acreage limits on the size of the zone. For additional details, see M.S. 469.168.*

such designated areas during the past three years. The city also lets contracts to joint ventures between local community-based businesses and major construction firms when the community-based firms have performed 50 percent of their business in economically disadvantaged areas of the city in the past three years or when 50 percent of its employees live in the designated areas.

URBAN AND RURAL AREAS:

Conclusions

Areas experiencing economic distress smaller than the labor surplus area or the county level can be identified. If the purpose of the preference is to stimulate economic activity in distressed areas, firms located in areas smaller than cities or counties could be granted the same type of preference now given to firms located in labor surplus areas and median income counties to further that purpose. Use of unemployment data correlated to census tract information would allow designation based on unemployment levels as is the case with the labor surplus area designation. The difference would be that the data used for labor surplus designation would be more current. Unemployment information for census tracts or other areas with less than 25,000 population is estimated using 1980 census data. However, there is no evidence that the data will not correctly identify areas of high unemployment and 1980 data is relied on for other state programs, such as Neighborhood Revitalization.

URBAN AND RURAL AREAS:

Recommendations

1. Designation of geographic areas smaller than cities or counties should be adopted as areas of economic distress, in addition to those currently authorized, for purposes of allowing a preference for qualifying business firms in the government purchasing process.
2. Census tracts, with unemployment information correlated to them, should be the basis of the designation. Unemployment data, assessed by the same standards used for the labor surplus designation, should be the standard for qualification.
3. Preferences granted to firms as a result of this designation should be the same as preferences granted as a result of the labor surplus area designation.