

contract dollars consists as equipment, in the same manner as other computer services contracts. Removing the requirement for a specific percentage of services defeats the purpose of the rule and would unintentionally change the size standards applicable to nonmanufacturers of computer equipment and for computer services.

Size Standards Methodology:

Congress granted the SBA discretion to establish detailed size standards (15 U.S.C. 632(a)(2)). The SBA's Standard Operating Procedure (SOP) 90 01 3, "Size Determination Program" (available on SBA's Web site at <http://www.sba.gov/library/soproom.html>) sets out four categories for establishing and evaluating size standards: (1) The structure of the industry and its various economic characteristics; (2) the SBA program objectives and the impact of different size standards on these programs; (3) whether a size standard successfully excludes those businesses which are dominant in the industry; and (4) other factors if applicable. Other factors, including the impact on other agencies' programs, may come to the attention of the SBA during the public comment period or from the SBA's own research on the industry. No formula or weighting has been adopted so that the factors may be evaluated in the context of a specific industry. Below is a discussion of the SBA's analysis of the economic characteristics of an industry, the impact of a size standard on SBA programs, and the evaluation of whether a firm at or below a size standard could be considered dominant in the industry under review.

Industry Analysis: Section 3(a)(3) of the Small Business Act (15 U.S.C. 632 (a)(3)), requires that size standards vary by industry to the extent necessary to reflect differing industry characteristics. SBA has two "base" or "anchor" size standards that apply to most industries—500 employees for manufacturing industries and \$6 million in average annual receipts for nonmanufacturing industries. SBA established 500 employees as the anchor size standard for the manufacturing industries at SBA's inception in 1953 and shortly thereafter established a \$1 million average annual receipts size standard for the nonmanufacturing industries. The receipts-based anchor size standard for the nonmanufacturing industries was adjusted periodically for inflation so that, currently, the anchor size standard is \$6 million. Anchor size standards are presumed to be appropriate for an industry unless its characteristics indicate that larger firms have a much greater significance within

that industry than the "typical industry."

When evaluating a size standard, the characteristics of the specific industry under review are compared to the characteristics of a group of industries, referred to as a comparison group. A comparison group is a large number of industries grouped together to represent the typical industry. It can be comprised of all industries, all manufacturing industries, all industries with receipt-based size standards, or some other logical grouping.

If the characteristics of a specific industry are similar to the average characteristics of the comparison group, then the anchor size standard is considered appropriate for the industry. If the specific industry's characteristics are significantly different from the characteristics of the comparison group, a size standard higher or, in rare cases, lower than the anchor size standard may be considered appropriate. The larger the differences between the specific industry's characteristics and the comparison group's characteristics, the larger the difference between the appropriate industry size standard and the anchor size standard. SBA will consider adopting a size standard below the anchor size standard only when (1) all or most of the industry characteristics are significantly smaller than the average characteristics of the comparison group, or (2) other industry considerations strongly suggest that the anchor size standard would be an unreasonably high size standard for the industry under review.

The primary evaluation factors that the SBA considers in analyzing the structural characteristics of an industry are listed in 13 CFR 121.102 (a) and (b). Those factors include average firm size, distribution of firms by size, start-up costs, and industry competition. The analysis also examines the possible impact of a size standard revision on SBA's programs. The SBA generally considers these five factors to be the most important evaluation factors in establishing or revising a size standard for an industry. However, it will also consider and evaluate other information that it believes relevant to the decision on a size standard for a particular industry. Public comments submitted on proposed size standards are also an important source of additional information that the SBA closely reviews before making a final decision on a size standard. Below is a brief description of each of the five evaluation factors.

1. "Average firm size" is simply total industry receipts (or number of employees) divided by the number of

firms in the industry. If the average firm size of an industry is significantly higher than the average firm size of a comparison industry group, this fact would be viewed as supporting a size standard higher than the anchor size standard. Conversely, if the industry's average firm size is similar to or significantly lower than that of the comparison industry group, it would be a basis to adopt the anchor size standard or, in rare cases, a lower size standard.

2. "Distribution of firms by size" is the proportion of industry receipts, employment, or other economic activity accounted for by firms of different sizes in an industry. If the preponderance of an industry's economic activity is by smaller firms, this tends to support adopting the anchor size standard. A size standard higher than the anchor size standard is supported for an industry in which the distribution of firms indicates that economic activity is concentrated among the largest firms in an industry. In this rule, SBA is comparing the size of firms within an industry to the size of firms in the comparison group at which predetermined percentages of receipts are generated by firms smaller than a particular size firm. For example, assume for the industry under review that 50% of total industry receipts are cumulatively generated by firms of 200 employees and less. This contrasts with the comparison group (composed of industries with the nonmanufacturing anchor size standard of \$6 million) in which firms of 64 employees and less cumulatively generated 50% of total industry receipts. Viewed in isolation, the higher figure for the industry under review suggests that a size standard higher than the nonmanufacturing anchor size standard may be warranted. Other size distribution comparisons in the industry analysis include 40%, 60%, and 70%, as well as the 50% comparison discussed above.

3. "Start-up costs" affect a firm's initial size because entrants into an industry must have sufficient capital to start and maintain a viable business. To the extent that firms entering into one industry have greater financial requirements than firms in other industries, the SBA is justified in considering a higher size standard. In lieu of direct data on start-up costs, the SBA uses a proxy measure to assess the financial burden for entry-level firms. For this analysis, the SBA has calculated nonpayroll costs per establishment for each industry. This is derived by first calculating the percentage of receipts in an industry that is either retained or expended on costs other than payroll costs. (The