BUILDING AN OPPORTUNITY ECONOMY: THE STATE OF SMALL BUSINESS AND ENTREPRENEURSHIP

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BUILDING AN OPPORTUNITY ECONOMY: STATE OF SMALL BUSINESS AND ENTREPRENEURSHIP

WEDNESDAY, MARCH 4, 2015

HOUSE OF REPRESENTATIVES,
COMMITTEE ON SMALL BUSINESS,
Washington, DC.

The Committee met, pursuant to call, at 11:00 a.m., in Room 2360, Rayburn House Office Building. Hon. Steve Chabot [chairman of the Committee] presiding.

Present: Representatives Chabot, Hanna, Rice, Gibson, Curbelo, Hardy, Radewagen, Velázquez, Hahn, and Clarke.

Chairman CHABOT. Good morning. This hearing will come to order. I want to thank everyone for being here, especially our witnesses and our members.

Today, we are here to examine the state of small business. For the Members here, it is not the first or last time we will have this conversation. We have it every time we talk to our constituents. They are the ones, after all, who tell us the most about small business.

But in those conversations, we do not have C-SPAN cameras, we do not have stenographers, and it does not make it into the Congressional record. So we are having this hearing today for our constituents, as well as for the small businesses all across the country, to have a conversation for the record that we have already had many times back home, so that we, as Members of the Small Business Committee of the U.S. House of Representatives, can start the legislative work of getting government off the backs of the American people and off the backs of small businesses all across the country.

One out of every two employed Americans works at a small business. Seven out of every 10 new job opportunities are created by small businesses. When the federal government issues new rules, or raises taxes, or threatens to raise taxes, or increases health care costs, or prolongs a sense of uncertainty, this does not just impact the name on a store front; it impacts real people. It impacts every American worker that puts a roof over their head or food on the table by working at that small business.

We have heard some say that our economy has recovered. And it has somewhat. But when you look at the number of unemployed Americans and the number of those who may be "employed" but cannot find full-time work—in other words, they are working only part-time—it is clear that we are not where we should be.

As testimony today will reinforce, it is not another sweeping government program that will make life better for Americans who depend on small businesses. The answer is hidden in the thousands of pages of regulations and tax policies that are crushing the small business community. We must alter the mindset of the federal government so that it is always thinking about how its actions will impact our small businesses. That is what the Small Business Regulatory Flexibility Improvements Act was all about—requiring that all federal agencies consider the impact, both direct and indirect, that new rules or regulations will have on small businesses before they become final. And in another area, the labor force participation rate is at its lowest point in our history. The percentage of long-term unemployed is still much higher than before the recession. And maybe the most disturbing trend: every year of the Obama administration we have seen more businesses close than open, and that is something I think we really need to focus our time on. More businesses closing, dying, than opening or being born. In plain language, it means we have a problem.

Small businesses are the foundation of our economy. As a Committee, we are here to make life better for small businesses and the working families that rely on them. Today, we begin that important work.

I want to thank each of our witnesses for taking the time to be with us today, and I look forward to hearing your testimonies and asking some questions. And I would now yield to our ranking member, Ms. Velázquez, for her making an opening statement.

Ms. VELÁZQUEZ. Thank you, Mr. Chairman. And thank you for holding this important hearing.

Creating two out of three net new jobs, small businesses are vital to our overall economic health. Recent job data affirms this point, with small firms creating 78,000 jobs between December and January, significantly outpacing larger companies. In January, businesses with fewer than 500 employees added 81 percent of new private sector jobs. Over the last four months, smaller companies have been responsible for 83 percent of newly created positions. When compared to the 38 percent of new jobs small firms created in 2010, it is clear that the small business sector is finally firing on all cylinders and providing the fuel to power our economy forward.

For small businesses to grow, a number of ingredients must be in place. Access to affordable capital is one element. Whether it is a bank loan or a well-timed infusion of venture capital, small companies require capital to expand their operations, break into new markets, or launch new products. Thankfully, since the end of the Great Recession, the lending environment for small businesses has improved considerably. The majority of small firms that apply for credit in 2014 receive it, according to data from the Federal Reserve banks. Indexes that measure credit conditions for small companies reached record levels in the last quarter of 2014.

Despite this positive news, room for improvement remains. Smaller loans are still well below pre-recession levels. Those small businesses or startups who are just getting off the ground, continue encountering difficulties in securing credit. It is my hope the committee will focus on this issue in the coming weeks.

Beyond access to capital, in order to succeed, small firms need customers willing to purchase their products. There has been significant progress in this area as well. Consumer confidence has been climbing since June, peaking at an 11-year high in January. With fuel prices remaining low, it is anticipated that consumer spending will remain strong, providing demand for small firm goods and services. All of these factors suggest that our nation's entrepreneurs have made significant progress in recent months. As small businesses continue growing, expanding and adding workers to the payrolls, they will help strengthen our overall economy.

It will remain the function of this committee to support policies that foster this growth. In that regard, I look forward to working with the chairman, and all my colleagues, to continue our bipartisan work to strengthen the small business sector.

I just want to take this opportunity to thank all the witnesses for your valuable insight, and I yield back the balance of my time, Mr. Chairman.

Chairman CHABOT. Thank you very much.

The Committee members can submit opening statements for the record if they would like to do that.

And I would like to go ahead and introduce our panel at this time, as well as introduce our five-minute rule, which is basically you get five minutes to speak to us. We hold ourselves to five minutes as well. We even have a lighting system for that purpose. The green light will be on for four minutes. The yellow light comes on and lets you know you have a minute to wrap up, and then the red light will come on. We would ask you to tie it up at that point, if not earlier. We will give you a little leeway but not too much. And we will introduce the panel and then we will hear from the panel.

We will begin with Jon Clifton, who is a partner at Gallup, Inc. In this role, he manages Gallup's global government work and the Gallup World Poll, an ongoing study conducted in more than 160 countries, representing 98 percent of the world's adult population. He received his Bachelor's degree in Political Science and History from University of Michigan, and a Juris Doctorate from the University of Nebraska. We welcome you this morning.

Our second witness will be Ms. Cynthia Kay, who is owner and president of Cynthia Kay and Company in Grand Rapids, Michigan. Her company produces high quality media productions and communications elements that are used here in the United States and abroad. Ms. Kay serves on the board of MiQuest Foundation, whose mission is to promote a culture of entrepreneurship in Michigan. She serves on the executive board of the National Small Business Association, whom she is representing today. A graduate of Michigan State University—we have got a lot of Michigan folks here. Ms. Kay also holds a Master's degree in Communications from Western Michigan University.

And our third witness will be Mr. David Burton, who is a senior fellow in Economic Policy at the Thomas A. Roe Institute for Economic Policy at The Heritage Foundation. In this role, he focuses on tax matters, security law, entitlements, regulatory, and administrative law. He received a juris doctorate degree from University of Maryland School of Law and he holds a Bachelor of Arts degree in Economics from University of Chicago.

So we welcome all three, and I will now yield to the ranking member to introduce our fourth witness.

Ms. VELÁZQUEZ. It is my pleasure to welcome Ms. Elana Fine. She is managing director of the Dingman Center for Entrepreneurship at the University of Maryland's Robert Smith School of Business. Ms. Fine's primary focus is leading the center in its mission to broaden entrepreneurship. Her responsibilities include oversight of a venture incubator, an angel investor network, business competitions, and integration with Smith School entrepreneurship curriculum and research activities. She is also an adjunct faculty member and has an MBA from the University of Chicago. She was recently named a tech titan by Washingtonian Magazine. Welcome.

Chairman CHABOT. Thank you.

Mr. Clifton, you are recognized for five minutes.

STATEMENTS OF JON CLIFTON, PARTNER, MANAGING DIRECTOR, GOVERNMENT DIVISION, GALLUP; CYNTHIA KAY, OWNER AND PRESIDENT, CYNTHIA KAY AND COMPANY; DAVID BURTON, SENIOR FELLOW IN ECONOMIC POLICY, THOMAS A. ROE INSTITUTE FOR ECONOMIC POLICY, THE HERITAGE FOUNDATION; ELANA FINE, MANAGING DIRECTOR, DINGMAN CENTER FOR ENTREPRENEURSHIP, ROBERT H. SMITH SCHOOL OF BUSINESS

STATEMENT OF JON CLIFTON

Mr. CLIFTON. Thank you, Mr. Chairman, and members of the Committee. It is a pleasure to be here to discuss Gallup's analytics on the state of the U.S. economy, the attitudes of small business owners, and the current barriers to job growth and startups.

Gallup completed its first national representative survey of the world in 2006. Our biggest finding from this study is what the whole world wants is a good job. That finding compelled us to more thoroughly study the jobs situation around the world. Gallup now quantities the prevalence in quality of jobs in more than 140 countries each year, and Gallup also tracks employment daily in the United States, surveying roughly 30,000 adults per month and more than 350,000 people per year.

There are a number of signs from Gallup's data that the U.S. economy has been improving since the recession—economic confidence is improving, self-reported discretionary spending is steadily increasing, and people are reporting that hiring is outpacing firing in their workplaces. Despite this encouraging news, job creation remains a problem.

While official unemployment has fallen from roughly 10 percent in 2010 to roughly 6 percent today, using this metric to represent the total jobs picture would be misleading. Traditional unemployment includes only people who are looking for work, who are available for work, and who have not worked a single hour in the past week. This means that if a person is giving up looking for work or if a person has worked only a single hour in the past week, that person is not considered unemployed.

A different metric offered by Gallup quantifies the number of people employed full time for an employer—or what others might call a "good job"—as a percent of the total adult population. Known

as Payroll to Population, this metric stands at 44.3 percent today and has not meaningfully increased since 2010 when we started quantifying this metric.

One of the main reasons that the job situation has yet to recover is that according to the U.S. Census, the number of business deaths now exceeds the number of business births among employer firms for the first time since 1977 when this measurement began.

This leads us to the importance of small businesses and startups in this country. They contribute roughly 70 percent of all new jobs created in a single year. Considering their importance, Gallup works with Wells Fargo to track the opinions and behaviors of small business owners on a quarterly basis.

The good news is that the attitudes of small business owners are steadily improving. The Wells Fargo Gallup Small Business Index stands at +71 today, which is the highest index score since the onset of the recession. Now, 64 percent of small business owners report that their company's current financial situation is good, and 71 percent expect their company's financial situation to be good 12 months from now.

However, despite this positive trajectory, small business owners face clear challenges. When asked to name their most important challenge, the number one issue they report is finding new customers. That is 15 percent of the small businesses that we talked to. This is followed by mentions of the economy in general, which represents 12 percent, and in third is government regulations, which represents 10 percent. However, if we add those who cite healthcare and Obamacare at 8 percent, or just the government in general, which is at 6 percent, fully 24 percent of small business owners say the government is in some way their biggest challenge. Also worth noting, while many small business owners believe available credit is a major issue, only 3 percent say it is their most important challenge.

In addition to the barriers faced by small business owners, there are also barriers facing would-be entrepreneurs. One in four Americans have thought about starting a business but have abandoned the idea. For an economy with a negative net number of startups each year since 2008, this represents a missed opportunity to engage would-be entrepreneurs that could result in business startups. Three major barriers are keeping these would-be entrepreneurs from taking the plunge: 1) They prefer the security of a stable income, 2) they do not have enough money to start a business, and 3) they lack the knowledge on how to start a business. Because the majority of business owners fund their early stage businesses through personal savings, a steadily declining personal savings rate in the United States has negatively affected prospective entrepreneurs' ability to finance new businesses. Moreover, if they lack insight on where or how to begin, starting a business is even more difficult, and these prospective entrepreneurs are more likely to be more risk averse.

Creating good jobs and subsequently rebuilding America's middle class hinges on the success and failures of small businesses and startups. Existing small businesses are experiencing headwinds, caused primarily by challenging business realities, the overall economy, and a concern about government regulations. Would-be entre-

preneurs face barriers such as not having enough money to start a business and lacking knowledge about starting a business.

It would be wise for Congress and American leadership to consider all options to unlocking this invaluable economic institution. The American public would be behind them. Other than the U.S. military, there is no other institution in the United States that the public has more confidence in than small business. Thank you.

Chairman CHABOT. Thank you very much.

Ms. Kay, you are recognized for five minutes.

STATEMENT OF CYNTHIA KAY

Ms. KAY. Thank you. Good morning. My thanks to Chairman Chabot, Ranking Member Velázquez, and the members of the Small Business Committee, for asking me to testify today.

As you heard, I am the president of a communications company, but I think it is also important to note that I come from a family of small business owners. My dad co-owned a small dry-cleaning business. My sister and her husband own a boutique rental company in Raleigh, and my brother is an attorney. I am also proud to be representing the National Small Business Association.

As a small business owner for 27 years, I have experienced numerous economic downturns. Probably the last one was the most difficult. However, I am glad to tell you that business is booming for my company, and I am not alone. And SBA recently released its year-end economic survey, and it shows that the economic outlook is really better than it has been in quite some time. But, the majority of small firms expect a flat or recessionary economy in the coming year.

And SBA also held its Small Business Congress, where we identified our top 10 priorities for Congress. And the top priority is ensure corporate-only tax reform, include some kind of workable solution for the millions of pass-through small businesses.

In the interest of transparency, I need to tell you, my company is a C corp; however, 83 percent of all small firms are pass-throughs. They pay taxes for their business at a personal income level, so it is no surprise that taxes are consistently ranked as the most burdensome administratively, and payroll taxes the most burdensome financially.

Broad reform of the entire tax code is necessary, and frankly, I firmly believe that addressing just one piece of this is only going to lead to greater complexity and be at the expense of small business.

Even in the best of times, access to capital is a huge hurdle. When I started my business, I did what a lot of business owners do—I went to get a loan and I had to sign a personal guarantee against the equity of my house. And I have done that on a number of occasions. Years later, when my sister and her husband tried to get a loan, they encountered the same difficulties. In fact, my business and my family financed their startup, and this is not an unusual story. In fact, it is very typical. It is difficult to get credit in good times; it is even harder to get credit during trouble economic periods. In fact, in the last seven years, one in three small firms on average cannot get access to adequate financing. Capital is the

lifeblood of small business, and without it, the heart of America's economy is millions of small businesses stand poised to fail.

In recent years, Congress enacted important tax provisions for small business on a temporary basis. They have now expired, and Congress continues to delay these extensions. So in the absence of comprehensive tax reform, extending and making permanent tax important provisions has been NSBA's priority for quite some time.

Tax extenders are very significant to my business. You have all heard the saying, "Lights, camera, action." Well, that costs a lot of money, and we are constantly updating our equipment. In the past, we used section 179 expensing and it is really important that we are able to deduct the cost of an asset in the year that we buy it. Why? Because our equipment gets outdated much quicker than the five to seven years that it costs to depreciate it. And it does not just affect my company; it affects more than one in three NSBA members.

So on behalf of NSBA, I do want to thank you, Chairman Chabot, for all of your work in advancing the Small Business Regulatory Flexibility Improvements Act earlier this year. It is a very important piece of legislation, and NSBA is pleased to have supported it.

But there is still a lot to be done. That is why NSBA played a critical role in developing the role of a national regulatory budget to bring much-needed reform. Small businesses simply need the environment to grow and to create jobs, and frankly, we need lawmakers who are willing to tackle major issues that are facing our country, and do it together.

I began today by saying that the economy has improved, and it has. There is pent-up demand for goods and services, and potential small business owners are constantly calling me and asking about owning a small business. And while I tell them that it is great to own a small business, I also tell them about the significant challenges. It is no wonder that many people, when they look at the obstacles, walk way.

At NSBA, we stand ready to work with you to help ease the burdens of using proactive solutions. Again, I want to thank you for the opportunity to speak, and I am happy to answer any questions.

Chairman CHABOT. Thank you very much.

Mr. Burton, you are recognized for five minutes.

STATEMENT OF DAVID BURTON

Mr. BURTON. My name is David Burton. I am senior fellow in Economic Policy at The Heritage Foundation. I would like to express my thanks to you, Mr. Chairman and Ranking Member Velázquez, for the opportunity to be here this morning. The views I express are my own and not necessarily those of The Heritage Foundation.

After complying with the multitude of state and federal regulations that business owners have to comply with, they should have some time left over to actually run their businesses. Entrepreneurs should not have to be lawyers to run their businesses. Unfortunately, that is about where we find ourselves these days, and if we want to return to sustained prosperity in the United States, we need to change that.

Entrepreneurship matters. It fosters discovery, innovation, and job creation. It leads to more productive production processes that improve productivity and lead to increases in real wages. Entrepreneurs develop new and better and less products and improve consumer well-being. They make markets more efficient. New firms account for most of the net job creation in the United States, and the vast majority of the economic gains from innovation and entrepreneurship accrue to the general public, rather than entrepreneurs.

But entrepreneurship is in decline. Business exits, as we heard, now exceed business formations. But there are many other indicia of entrepreneurial health that also indicate that we place an unprecedented burden on small startup businesses. Accordingly, job creation, productivity improvements, and welfare-enhancing innovation have slowed, and the decline is an important reason for our anemic economic performance.

The reasons for this decline are many fold. One policy change or a few are not going to solve the problem, because the problem is caused by the accumulated and combined weight of hundreds of regulatory and statutory requirements imposed on small startup businesses.

The problems fall into eight basic categories.

1. Poor tax policies that raise the cost of capital impose high taxes on risk-taking and impede economic growth. Moreover, the tax system is monstrously complex, which has a disproportionate impact on small and startup firms.

2. Access to capital. Securities law and banking regulations and practices that limit the ability of small firms to get the capital that you need to launch or grow. After all, if you cannot get the capital to launch, all the other impediments to entrepreneurship are generally academic or mute.

3. The healthcare system is the most costly in the world. More costly than any other OECD country. And the Patient Protection and Affordable Care Act, also known as Obamacare, imposes high costs on firms with 50 or more employees.

4. Environmental and energy regulations raise the cost of energy, including electricity and limited development of energy resources.

5. The cost of complying with a broad range of increasingly burdensome and complex regulations. These rules have a disproportionate and adverse effect on small firms who can ill-afford to use scarce resources to comply with state or federal regulatory requirements instead of growing their business. They also tend to be the people who are least experienced in regulatory compliance.

6. We have increasingly complex and increasingly opaque labor and employment laws that raise the cost and risk of employing people, and they reduce wages and cost jobs.

7. The U.S. immigration system is broken, and it is difficult for firms to gain access to talented foreign workers and for immigrant entrepreneurs to launch businesses in the United States.

8. And lastly, the U.S. legal system is the most costly in the world, imposing high and potentially ruinous costs on small firms and creating a whole series of regulatory risks.

If we want to return to a prosperous American with opportunity for all and rising real wages, then Congress needs to systematically

address these issues with alacrity. The key to reducing the decline in entrepreneurship is to systematically reduce the legal impediments to entrepreneurship. Since the decline is caused by the combined weight of many poor public policies, the solution requires systematically improving public policy in a wide variety of areas.

My written testimony sets forth 97 specific proposals that I believe if adopted will transform the American economy, lead to resurgence in entrepreneurial activity, strong economic growth, real wage increases, and renewed prosperity. I will be glad to discuss any of those specific recommendations in greater detail if time allows. Thank you very much.

Chairman CHABOT. Thank you very much.

Ms. Fine, you are recognized for five minutes.

STATEMENT OF ELANA FINE

Ms. FINE. Chairman Chabot, Ranking Member Velázquez, and members of the Committee. Thank you for inviting me to testify before you today.

I am Elana Fine, managing director of the Dingman Center for Entrepreneurship at University of Maryland's Robert H. Smith School of Business.

Throughout my career in technology consulting and investment banking, I have worked with hundreds of startups and venture-backed companies, and am therefore well versed in their challenges and opportunities.

To provide a little context, the Dingman Center is one of the nation's preeminent institutions where the research, education and practice of entrepreneurship are pursued vigorously. We develop and execute curricular and extracurricular programs to inspire and equip the next generation of entrepreneurs. Our programs are focused on guiding student entrepreneurs from idea to launch.

My role at the Dingman Center includes oversight of our student venture incubator, the Dingman Center Angels Investment Network, business competitions, and relationships with the broader startup community. I also serve as an adjunct faculty member at the Smith School.

I have been asked to give an overview of entrepreneurial activity from a university perspective. I recognize that the macro level of activity can be hard to quantify and to really assess whether we are headed in the right direction. Based on the pop culture success of television shows, like Shark Tank, the proliferation of technology incubators and downtown innovation hubs, it might seem like everyone is working on a startup. Then we look at the statistics, like the Kauffman Index, and entrepreneurial activity, which shows a decline from 2011 to 2013, and we wonder if we are doing enough.

From this perspective, a decline in entrepreneurial activity might also be seen as an indicator of an improving economy as employers have better job prospects. As we would say in startup terms, we just do not know the metrics that matter. So I am here today to give you a more grassroots perspective on what I see as some leading indicators of the future of entrepreneurship.

We informally think about our student ventures in three categories. The first category is dorm room high group startups, like

Facebook, which although an outlier, raised the visibility of student entrepreneurship and has inspired a generation.

The next category we think about are the students starting businesses while in school that they do not often continue beyond graduation. Every year we see a panoply of new apparel companies, mobile applications, tutoring services, dating sites, and food concepts. We have seen university support increase to match student interest and demand in these activities. The data from the Dingman Center shows interest in our ventures-creation activities grew from 161 students in 2012–2013, to almost 400 students in this academic year. Students run these businesses for two to three years until graduation. The company might not be a success in standard terms, but as educators, we have provided a skillset we expect will be used for a startup now or even 10 years from now.

Our best example in this category is University of Maryland alumnus Kevin Plank, who ran a campus flower delivery service called Cupid's Valentine. After graduation, instead of solving the problem of expensive flowers, Plank decided to solve the problem of soggy cotton t-shirts and turned his savings from Cupid's Valentine into the seed money for Under Armour, which is now a multibillion dollar company employing thousands.

The last category of students feed the entrepreneurial labor pool. These students are not working on their own idea but won internships at local startup companies. The challenge is that startups can rarely pay market rates, so they often have to forego these opportunities to take higher paying internships.

All of the students represent future entrepreneurs, but I caution focusing too much on the first category. Instead, there are a number of initiatives that can increase exposure and odds of success. For example, the National Science Foundation's I-Corps program is a model of a federally-funded program that could increase the odds of success among early-stage university spinouts.

On campuses, we need similar programs that can build on our current momentum. These programs might provide scholarships for students or loan forgiveness so students can choose to work at startup firms.

We also need more funding opportunities that others have mentioned. Without an initial ten to a hundred thousand dollars, it is nearly impossible for a young entrepreneur, who is burdened with student loans with no savings or credit, to build a product and test acquisition strategies. Banks, angel investors, and even granting institutions do not have vehicles to fund these businesses.

As you embark on your Committee's activities, I encourage you to consider the following: Seed programs that expose more students to entrepreneurial activities and equip them with the tools to vet ideas early; recognize that failure rates will always be high and that success in entrepreneurship can also be viewed by total births and deaths, because it means there are more companies in the field; consider programs that provide nondiluted funding to a broader spectrum of businesses, and think creatively about apprentice-like programs and high-growth startups that might increase the entrepreneurial labor pool.

Thank you for your time and opportunity to discuss student entrepreneurship. I am happy to answer any questions you might have.

Chairman CHABOT. Thank you very much. And I will recognize myself now for five minutes.

I will start with you, Ms. Kay. My understanding is you have—and this is according to your written testimony—you have eight employees, yet you have had to hire five outside experts from an accountant to a corporate lawyer to an HR lawyer and on and on. Is that not kind of out of whack? Where are we going wrong, the need for a business to expend so much of their capital and resources just complying with the law, rather than the substance of what makes them profitable and able to be successful and hire as many people as you possibly can? So I will leave that up to you.

Ms. KAY. Well, one of the things I always say is that as a small business owner, you wear lots of hats. You are doing everything. You are the HR department. You are the sales department. You are doing the work. And we certainly cannot be expert in all of these things. So unlike large companies that have a staff of people to do things in house, I do have an accounting firm. I actually checked the numbers this past year, and it was a good year. We did not have a lot of issues. The cost of it was $16,000 for a small company. Corporate lawyer and HR lawyer, there are so many things that are happening on the HR front that it is almost impossible for us to stay up with all of the regulations.

And I think it is important that you know that small business owners want to be in compliance. We want to comply with the law. We simply do not have the expertise. Mr. Burton here talked about needing lawyers to do the things. Simply reading all of the documents and going through the forms is extremely complex. So while smart business people can be creative and entrepreneurial, we are not regulation specialists, and we need people to help us.

Chairman CHABOT. Thank you very much.

Mr. Burton, I will turn to you next. You had mentioned that you had 97 proposals, and I commend you for that. If you could limit that to what you consider to be the three most significant, that if we could actually accomplish, that would do the most to benefit small businesses in this country, what three—I mean, if you need four, that is okay. If you can only come up with two, that is okay. But I am thinking three because that is usually what we do.

Mr. BURTON. I will do it. But part of the problem is it is not any one or two rules. I mean, you have hundreds, literally, of rules that small businesses had to comply with, all of which, when you look at them together—I mean, by itself—may be reasonable. But the combined weight of hundreds of rules is killing people, like Cynthia. And if you just get rid of four of the hundreds, you have done something useful but not solved the problem.

The written testimony I wrote sort of divides things into intermediate, so there is smaller chunks, and then big picture stuff. So, for example, fundamental tax reform would be in a category of something that could be transformational, but there is a whole series of small things. For example, making 179 expensive, liberalizing the S corporation rules, fixing the independent contractor employee distinction, fixing the characterization of capital versus

labor income for self-employment purposes. In the securities law area, there is a whole host of things that would enable businesses to raise money. For example, preempting Blue Sky laws on Reg A, fixing Title 3 of the Jobs Act, and protecting Regulation D so that people can raise money in private placements. There is a move afoot to severely restrict the ability of firms to raise private placements.

And then there is just not piling on massive paperwork requirements in the employee-employer relationship, and there is a whole host of things going on there—the Protected Concerted Activity Initiative by NLRB, the criminal background screening rules which—you know, there is a reason why. Maybe there is a problem there, but a 157-footnote document is not guidance; it is just obfuscation, and we need to fix it and not make things totally here. But the list is almost endless. And you need to address a lot of things, not any one or two.

Chairman CHABOT. Let me turn to you, Mr. Clifton. I am almost out of time. I have got about 30 seconds.

You had mentioned that, I think, the largest real category that small businesses—the challenge they face is basically dealing with the federal government regulations and that sort of thing. They would like to get new customers, but that is the highest single thing, but if you add the other things together—Obamacare, et cetera—has that been pretty consistent over the years, do you know? I mean, this exasperation with dealing with government in general and the regulations? Is that pretty consistent over time? Is it getting better or worse, or do you know?

Mr. BURTON. No, it has been very consistent. In fact, just this study, the data that I shared today, is actually the aggregate of what has happened over the past five quarters. So it is a very stable number.

Chairman CHABOT. Okay. Very good. Thank you.

My time has expired. I now yield to the gentlelady from New York.

Ms. VELÁZQUEZ. Thank you, Mr. Chairman.

Ms. Fine, many economists have long discussed that employer-based health insurance can lead to job lock where employees stay in their job solely for the benefits. The ACA effectively eliminates job lock, and some have projected that it will increase entrepreneurial activity. What impact do you believe the ACA will have on entrepreneurs' decisions to start a new business?

Ms. FINE. I would expect that it would increase the interest in starting new ventures because of the reduction of job lock. In general though, I would say for most entrepreneurs, particularly high-growth entrepreneurs, if they have an idea that they are passionate about and they see a window of opportunity for and they think that—most likely they think they are going to be the next Mark Zuckerberg, whether or not they have health care probably will not stop them, but it does reduce one of the barriers as some of the fellow panelists mentioned about training and other things. It might be one thing that they do not have to worry about anymore.

Ms. VELÁZQUEZ. Thank you.

In this committee room, Ms. Fine, we often hear that taxes and regulations are the biggest challenges for small firms. As an actual practitioner in entrepreneurship, I wanted to ask your views on this: What are the greatest challenges facing your students as they try to get their companies off the ground?

Ms. FINE. Yeah, I will say that is not top—those two things are not top of mind. What is top of mind is funding, and I will echo Cynthia's comments about finding customers and just where do I find them, how do I access my network, who is really going to trust me as a small business with not much of a balance sheet. The old kind of adage that you never get fired for buying IBM. To me, those are the biggest hurdles for our entrepreneurs.

Ms. VELÁZQUEZ. Thank you.

Ms. Kay, if Congress were only to reform corporate taxes, how would that impact small businesses?

Ms. KAY. Well, I think you need to look at what it is for small businesses. I think I mentioned 83 percent are pass-through.

Ms. VELÁZQUEZ. Pass-through. Mm-hmm.

Ms. KAY. And so for them, you know, only reforming corporate tax is really not going to impact small business. And what we end up seeing, and I will be the first to tell you I am not a technical expert; that is why I have accountants. But I see so many of the tax burdens. If we do not take care of this large segment of small businesses—and as I mentioned, I am a C corp, so it does not affect me—but so many of my supplier and customers are, that I see that as a huge issue.

Ms. VELÁZQUEZ. So closing so-called loopholes, many of which are used by small companies, such as bonus depreciation 179 expensing, closing those loopholes are favored by many. How would this impact small businesses?

Ms. KAY. I think the biggest issue we have is uncertainty. If we do not know that we are going to be able to use, for example, 179 expensing, we are left in a position where we are unable to make reasonable decisions—buying decisions, financial decisions about our company. So what is most important to us, frankly, we would love to see those become permanent, but is certainty. That would be the biggest thing that would help us to move our businesses forward.

Ms. VELÁZQUEZ. But if we do not take up comprehensive tax reform, it means that we might have winners and losers. So for the 83 percent of pass-throughs, if we eliminate tax loopholes, such as 179 and bonus depreciation, there will be losers. How can we support having that equation where we are going to provide tax reform for some but at the expense of others?

Ms. KAY. Well, as I said, I think we are most interested in comprehensive tax reform.

Ms. VELÁZQUEZ. Okay. Very good.

Ms. KAY. But in the absence of that, we are looking for many of these other things, like tax extenders.

Ms. VELÁZQUEZ. Okay, so it is over. Thank you.

Chairman CHABOT. The lady's time has expired.

The gentleman from Florida, who is the chairman of the Subcommittee on Agriculture, Energy, and Trade, Mr. Curbelo is recognized for five minutes.

Mr. CURBELO. Thank you very much, Mr. Chairman, for scheduling this important hearing. And I thank the witnesses for their insightful testimony.

I am passionate about small business, because I believe that small businesses afford opportunities to those who need them the most, oftentimes through casual encounters. Think about that young person who might have dropped out of college. Their neighbor might be a small business owner and they might get a job that way. Think of a recently-arrived immigrant who is looking for a way to get ahead. Small businesses tend to hire those types of individuals.

So I want to ask a question on the EB5 Regional Center pilot program that Congress established in 1992. I want to ask Mr. Burton specifically. For those who are not fully familiar with the program, under the EB5 program, investors are required to put up at least one million dollars or $500,000 in high unemployment areas, and these are foreign investors. In return, they receive a two-year green card for themselves and their immediate family. If the project succeeds and at least 10 U.S. jobs are created, the investors gain permanent residency. If the project fails, they lose their green cards and absorb the losses of that failure.

This program is expected to sunset at the end of this year. Mr. Burton, do you have any thoughts on whether this program should be extended, or are there other programs like this that Heritage may support for entrepreneurial immigrants?

Mr. BURTON. I personally think something along the lines of the EB5 program where you are basically allowing people who invest capital in the United States and create jobs in the United States to enter the United States lawfully makes a great deal of sense. I am confident The Heritage Foundation will probably reach that conclusion, but right now the institution is undergoing a review of immigration law and trying to develop a fairly comprehensive approach to it. But personally, I think that the EB5-type approach, although there are little problems with it and I am not an EB5 guru, it definitely makes sense, and I am sure that we would be happy to work with you to develop an approach.

Mr. CURBELO. Thank you, Mr. Burton.

Does anyone else on the panel have any thoughts or insights onto this EB5 program? If you do not, that is okay.

I had another question, Mr. Burton. I also reviewed and listened to your testimony. I think one obstacle or barrier to small businesses is missing, and that is transportation infrastructure. We all know how fundamental it is to have a robust and modern transportation infrastructure in our country is for our economy according to a recent report by INRIX. In 2013, traffic congestion robbed the U.S. economy of $124 billion according to this group. Without significant action to alleviate congestion, this cost is expected to increase 50 percent, to $186 billion, by 2030.

Do you have any thoughts on our nation's transportation infrastructure system, its effects on small business, and what we should do here in Congress to improve it, if anything at all?

Mr. BURTON. Having an adequate freight and passenger transportation system is important to all businesses, large and small. We tend to take those things for granted until they are not working

right. The Heritage Foundation certainly supports having a robust transportation network, but in general, we would like to shift the responsibility for that towards the states which are more familiar with their local traffic and transportation needs than the federal government.

Mr. CURBELO. Thank you.

Yes, please, Mr. Clifton.

Mr. CLIFTON. On your commentary about the regulation that was done in 1992, one of the things that Gallup has been working on for some time now is studying what entrepreneurs look like. So when it comes to passing regulation that might force people who are not inherently entrepreneurs to therefore become entrepreneurs might set them up for failure. And so we have been studying thousands of individuals, and actually calling individuals, like Ms. Kay herself, and we have found that they are very different than the general public. And so what we need to do is be much more intentional about who we are seeking out in terms of being entrepreneurs, because these rare individuals, as I mentioned from our data, from our research, look very different. So any regulation that might draw someone to be an entrepreneur who should not be one would not be wise.

Mr. CURBELO. Thank you very much. And my time has expired. Thank you, Mr. Chairman.

Chairman CHABOT. Thank you. The gentleman's time has expired. I am sure that Mr. Clifton did not mean to insult anybody here.

But in any event, the gentlelady from New York, Ms. Clarke, is recognized for five minutes.

Ms. CLARKE. Thank you, Mr. Chairman. And I thank the ranking member, as well as our witnesses, for their testimony today.

Today's hearing is a very important one. Entrepreneurship is the spirit from which small businesses are born. And so we in Congress must continue to do our part to keep the spirit of entrepreneurship alive and thriving in this country.

I would like to thank the witnesses again for their assessments on today's state of the economy and small businesses. We have made great progress in the scope of macroeconomic growth since 2008, with a 5 percent GDP growth in the third quarter of 2014, and an unemployment rate that fell to 5.6 percent in December of last year. However, it is clear that there is still a lot of room for continued economic improvement, particularly concerning hourly wages, as well as the volume of smaller loans to startups and small businesses.

So my first question to the panel is household medium income adjusted for inflation is hovering around $52,000, which is well above the $56,800 number—excuse me, hovering around $52,000, which is well below the $56,800 number from the year 2000. Hourly wages for private sector employees rose 1.7 percent in December 2014 from a year earlier. What can we do to increase the household medium income? And furthermore, what can we do to see a more significant rise in the hourly wages for all private sector employees across the board?

Mr. BURTON. I have some thoughts on that.

Ms. CLARKE. Thank you, Mr. Burton.

Mr. BURTON. There is sort of two key points to getting ordinary people's incomes back up. One is making the economy more productive, and there are a couple keys to that. Entrepreneurship, new technologies is one. A second piece of it getting more capital in the hands of ordinary people so they are more productive. A farmer with a big combine is more productive than a guy with a hoe. But that is true throughout the economy.

So there are policies that we can take, particularly tax and securities regulation, banking policies, that will help people get the capital they need. But we also need to eliminate—from an employer's point of view you have costs, and from an individual's point of view you have wages. But in between there, there are a lot of costs that employers now have to bear that are not going into the wages of their employees, and we need to try to shrink those costs that are not ending up in people's pockets, and there are a lot of ways to do that.

Ms. FINE. I can comment briefly on this just from a perspective of the technology industry. I think we know that higher tech jobs pay more, and so thinking about additional training so that we can increase the technical competence of our workers so that they will be better skilled for higher-paying jobs would be one perspective from my experience working with a lot of startup companies who want to build technology but cannot necessarily find the trained workers.

Ms. CLARKE. Okay. Let me go on to my next question then.

While the volume of loans larger than one million dollars has recovered since the Great Recession, the volume of loans below one million dollars has barely recovered. Small businesses and startups often seek out lines of credit that are less than $100,000. How can we work to make sure that smaller businesses that need smaller loans can actually access this capital that is critical in a startup or even transitioning phase for a business?

Mr. BURTON. I have two quick specific things. One is we can enable small businesses to use peer-to-peer lending, like prosper and lending club. The SEC basically shut that down for small businesses. And there are a couple of different ways to go about that. I discussed some in this, but I can go into greater detail. And I think that is an area where we may be able to achieve bipartisan cooperation in the Congress under strong interest in financial services, I think.

The second is I think you all could ask a GAO study on banking practices that disproportionately affect small businesses. The community bankers in particular constantly say the regulators when they audit them are doing various things, but then when you call them up and ask them for specifics, they are not forthcoming. I have not been able to figure out what the truth is. And maybe GAO can. And I think, again, that is an area where we can have genuine bipartisan cooperation trying to figure out what are the true impediments to small business borrowing. And I would be glad to work with the Committee on that.

Chairman CHABOT. Thank you. The gentlelady——

Ms. CLARKE. Thank you, Mr. Chairman.

Chairman CHABOT. Thank you. The gentlelady's time is expired.

The gentlelady from American Samoa, Ms. Radewagen, who is the chair of the Subcommittee on Health and Technology is recognized for five minutes.

Ms. RADEWAGEN. Thank you, Mr. Chairman.

My question is for Mr. Clifton. Ms. Kay and Mr. Burton both put a little more emphasis on access to capital as being a significant problem facing small businesses. Do you think that your research shows that other problems, such as taxation or overregulation has become a bigger impediment? Or does your data suggest a genuinely improving capital access market?

Mr. CLIFTON. Thank you for the question.

Our data would suggest there is an overemphasis on credit and its availability. Most small businesses and would-be entrepreneurs start their businesses with their own money or from money that they have borrowed from a family member.

The other thing is there are studies that suggest—one from Harvard—is that making too much available credit again can draw in people who should not be entrepreneurs. Would-be entrepreneurs are very clear about what their challenges are, and one of them is they do not know where to start. I think one thing that you could extrapolate from that is the fact that there is too much regulation for them to shift through, and any way to take that down or to help them with programs like at the University of Maryland where there are educational opportunities to help them navigate the complex ways to start a business would be very helpful, and the emphasis should be on those things.

Ms. RADEWAGEN. Thank you.

I have another question for Ms. Kay. You mentioned both you and your sister have started businesses, and I am wondering, did either of you use any of the products or services offered by SBA? Why or why not?

Ms. KAY. Actually, we did not. And I will be honest with you. I looked at SBA loans and quite frankly, the length of time that it would have taken and the complexity of going through the process was significant. So for us, it was easier to sign a personal guarantee and take a loan against a home and be in business and do what I really love doing, which is the work of doing business. For my sister, both she and her husband, highly educated, great work history, banks simply would not lend to them. And I do not think this is an unusual situation. And SBA has also found that what people are using is savings and credit cards. And we know that neither one of those is really a good long-term solution for starting a business.

Ms. RADEWAGEN. Thank you. Thank you, Mr. Chairman. I yield back.

Chairman CHABOT. Thank you. Who is next?

If you are ready, we can go to you now, or if you would like to wait until the next one, that would be okay, too. Because you would be next.

Okay. We will go on this side. We will come back. Thank you.

The gentleman from Nevada, Mr. Hardy, who is the chairman of the Subcommittee on Investigations, Oversight, and Regulations is recognized for five minutes.

Mr. HARDY. Thank you, Mr. Chairman.

As a small business owner myself for the past 20 years, I understand some of the issues that are out there. My question is I am a firm believer that business creates business. Not in all cases, but in most cases. We rely on each other to support our businesses. So to through that process, what can Congress do to maybe get out of the way? Or I do not think Congress has anything to do with job creation personally, but I think what can we do to get out of the way of small businesses so they feel like they are free to invest in that entrepreneurship or expand that business that needs to be expanded or create that new one? Any ideas on that?

Ms. KAY. Well, one of the things that I think is really critical is simplicity. When you run a small business, it really is all about time and money, and we only have so much of both of those things. And anything where there is huge complexity that is involved means we are taking time away from doing business to deal with regulations or HR issues. So reducing the complexity of doing business for me is huge. And I know for a lot of other business owners as well. And it is interesting that you use the terminology "get out of the way," because when I spoke to fellow business owners in Michigan and told them that I was coming, several of them said those exact words—could you tell them to move out of the way so that we can actually get work done?

So anything that could be done to improve simplicity and give us certainty about where we are going so we are not revisiting issues time and time again I think would be important.

Mr. HARDY. Thank you.

In many instances in your written testimony, you have discussed over burdensome regulations. Being on that regulation oversight Committee, I have a great desire to move some deregulation out of this place. Can you give me some specifics that have actual documentation where we can help somewhere along the line? Anybody?

Mr. BURTON. Absolutely. I mean, there is probably 80 in my written testimony, and I would be glad to go through them with you or your staff. But in the tax area, there is a lot of statutory changes that need to be made, but some of them are regulatory, particularly governing who is an employee versus an independent contractor. Whether income in an S corp or partnerships are subject to self-employment tax or not. In the securities regulation area, it is almost all regulatory, and there is a lot of things. There are also some things that need to be stopped. The SEC is proposing rules, for example, Reg D, which is how most small businesses raising capital from investors raise capital these days, a trillion dollars a year, basically requiring about three forms instead of one, and then a whole host of obligations that never existed before. Sort of undo the Jobs Act Regulation. There is that. There is, with crowdfunding, a four-page statute on the House side became a 30-page statute. In the Senate it became a 600-page rule in the SEC. And that is meant for the smallest companies in America. I mean, it is just ridiculous. There is a long, long list.

Mr. HARDY. My staff will be in contact with you and make sure that we cover those.

Mr. BURTON. I would be glad to do it. Yeah.

Mr. HARDY. One of the other things, Mr. Burton, in your testimony, we talk about the 97 issues out there that are restricting,

one of those being about the states' lands being devolved from the Bureau of Land Management and turned back to the states. As you know, in the State of Nevada, where I come from, almost 86 percent of our state is held by the federal government, which keeps us from having that equal footing that all other states have to be able to be independent. Can you give me some ideas of what we need to emphasize and how we can make that work and happen?

Mr. BURTON. Yes and no. Everything in my testimony, except the energy and environmental stuff, I have personal experience on and can go on way beyond you guys' time limits. On that, I basically borrowed it from my colleague at The Heritage Foundation, a gentleman named Nick Loris. And if you want to go very deep into the weeds on land management, he can help you. I know that there is a strong interest in terms of trying to reduce impediments, primarily in the West, to using federal lands by small businesses, and they have some pretty good ideas about how to do it.

Mr. HARDY. I have one other question I want to hit. This is probably for Mr. Clifton.

How can we can have a very strong economy without job growth? We look at these reports and we continue to hear that unemployment is going down, but on the other hand, where are the jobs? Where is this coming from? Is there something different in the way we are doing reporting today than we were that is causing this effect? Because there are still hundreds or tens of millions of people out of jobs out there.

Chairman CHABOT. The gentleman's time has expired, but you can answer the question, whoever it was directed to. Mr. Clifton.

Mr. CLIFTON. Thank you for the question.

We are not calculating the unemployment figure any differently than we have since we have been doing that in terms of the U.S. government. The challenge is the people that are working part-time who want full time or who are minimally employed or who are no longer in the workforce because they have given up, are not included. So that figure that we look at today at about 5.6 percent as unemployment does not reflect the 20 million people out there that would like to have a good job. So that is the data around that.

And can you have a good economy without more people that are fully employed? The answer to that is no. What would be great is if the U.S. economy looked more like states like Nebraska and North Dakota. When we look at their Payroll to Population, Nebraska's hovers at around 50 percent and North Dakota's hovers around 54 percent. America's is at 44.3 percent. That is too low. Thank you.

Chairman CHABOT. Thank you. The gentleman's time has expired.

The gentlelady from North Carolina, Ms. Adams, is recognized for five minutes.

Ms. ADAMS. Thank you, Mr. Chair. And thank you, ranking member, for holding this important meeting.

Creating jobs and growing our economy is one of my top priorities, and small businesses certainly are a significant part of that equation.

I have a few questions for Ms. Fine. I have been an advocate for a long time for women-owned businesses, and according to the

State of Women-Owned Businesses Report, my state, North Carolina, was among the top three with the fastest growing growth in the number of women-owned firms. We have estimated about 267,000 women-owned businesses generating about $35 billion in yearly income. Based on your experience, how can we keep this momentum going to further increase the number of women-owned businesses, and more specifically, African-American women?

Ms. FINE. Yes, thank you for the question.

I would say this is obviously something that we see, and we are trying to tackle this challenge as well, because we just do not see enough women. I think a couple of things is, one, just more exposure. There are not as many role models of successful, well-known entrepreneurs, so I think finding and celebrating those successes is very important. Second, I think is just starting earlier to address that you really can teach entrepreneurship. You can at least expose somebody to entrepreneurship the same way that you do to anything, like Math, Science, et cetera, so I think there are a lot of great programs of like what the Network for Teaching for Entrepreneurship is doing and getting programs into middle school and high schools. I think that taking some of those programs and even finding them even more for young women would be very important. And just having I think in general inspiring women to think bigger about what they can do as entrepreneurs because they actually have a lot of the great talent and skillset that is very important to being successful.

Ms. ADAMS. Thank you. I was going to follow up with a question about students. I worked with young women for 40 years at Bennett College in Greensboro, but you have kind of touched on that, so I will not ask that question. But, you know, with Facebook and Twitter and all of the access that they have that are integral to entrepreneurship, I am sure they are using that as well.

One of the biggest challenges, and you have mentioned access, but oftentimes, small businesses are really not aware of the federal resources available to them, or any resources for that matter. So how should the federal government in your thinking, or other entities, work better to educate and connect small businesses to those resources that can help them succeed?

Ms. FINE. Obviously, I do put the onus of that a little bit on the entrepreneurs. Sometimes I am a little bit surprised that entrepreneurs do not take the step to look for all the resources available. I think there is this perception that anything related to a government loan, SBA, et cetera, a patent, for example, takes a really long time and is a complicated process. So I think being more transparent about the processes and trying to make them faster and more efficient so that entrepreneurs do not feel that they are missing a window of opportunity would be a start.

Ms. ADAMS. Well, and I agree with you. I am thinking though, the federal government is a complicated kind of process and it can be a little, I guess, intimidating in terms of applications and that kind of thing. So perhaps if we could do more. Not just letting them know what is available but how to apply and the kinds of things and the steps that need to be taken. But thank you very much for your comments.

Mr. Chair, I yield back.

Chairman CHABOT. Thank you. The gentlelady yields back.

The gentleman from New York, Mr. Hanna, who is the chairman of the Subcommittee on Contracting and Workforce, is recognized for five minutes.

Mr. HANNA. Thank you, Chairman.

You know, it is easy to demagogue regulations. And to speak to 179, which I am in favor of, one man's loophole is another man's following the law. Right? So what is the complaint? And you find in government that in the effort—that every level to control every outcome will wind up with something that started out reasonably fluid that turns into something that is one barrier after another, but we have no way to measure the marginal change in one's ability, or a company or an entrepreneur's ability to deal with it. But we know that structurally everything is a burden.

Mr. Clifton talked about entrepreneurs and some people are suited, some are not. I would suggest to you that the best way to figure that out is to try, and we made it very hard for people to try.

But Mr. Burton, there is a thing called the Raines Act, which I imagine you are familiar with. How do states and local municipalities—everybody has a hand in this and everybody is making marginally some kind of problem for the guy who wants to go in business, or lady. And I am just curious, because it is easy to sit back and complain about government, and I am happy to do that, but in a practical world, how do you accept the notion that some things have to go wrong in order—if you agree with me—in order for other things to go overwhelmingly right? In other words, how do you measure opportunity versus control?

Mr. BURTON. Well, three quick things. First, sort of on the business level, you are absolutely right. You have to let people fail. You have to let people have the opportunity to not succeed in their business or you will not get the positive aspects of entrepreneurship. And sometimes the SEC forgets that. State regulators can be among the worst. For example, Massachusetts prohibited people in Massachusetts from buying the original Apple IPO because investing in the Apple computer company was too risky and they wanted to protect their people. So some of the goofiest regulations imaginable are at the state and local level, not at the federal level.

Mr. HANNA. It was the breakup of Microsoft, too, which made no sense.

Mr. BURTON. But I agree with you. It is easy to complain, and we need to craft constructive solutions, which is why I tried to do that in my written testimony. Specifics. What regulation? What problem? And it is one of my frustrations with the bankers who constantly say it is the regulators, but they never have any solutions. And there are two possible reasons for that on the bank credit side. One is they are using it as an excuse. It is not really the regulators; it is them. And it could be for legitimate business reasons. Or the second reason is there is something going on there that we have not found out about.

One other thing I thought I might mention. We talked about bank credit, but some of the most dynamic companies that are leading to huge employment gains and other social gains are the people looking for outside investors, not just banks. Because banks do not invest in startups, generally. They might lend to you person-

ally, but they are not going to invest in startups. So people who are looking for outside investors and therefore, running into the securities laws are the source of much of the social gain from innovation and entrepreneurship, and we need to try to knock down some of those barriers.

Mr. HANNA. What do you think, Mr. Clifton?

Mr. CLIFTON. What is the question specifically?

Mr. HANNA. Well, I mean, you talk about entrepreneurs. It is my opinion that we do not give people enough opportunity to succeed or fail; that the barriers to entry to business today are so prohibitive, and that at some point it becomes personal and other things become easier to do. People drop out of the system because they lose energy. They frankly become victims of the bureaucracy. But it is hard to measure that and understand it.

And I am familiar with a number of banks and have been in business for a long time, and they would tell you that it is easier to loan big money than little money; that it is easier to avoid small entrepreneurs than it is to engage them because they can move on and make marginally less with a hell of a lot less aggravation. So have you seen that?

Mr. CLIFTON. Well, so I think what you are asking is how do we quantify sort of this phenomenon about government regulations and its impact with small businesses. And that ultimately, I believe, is why I am here. Because the way that we have attempted to quantify it is by simply asking small businesses, "What is the biggest problem you face today?" And I think when we quantify that we see that 25 percent of them, in an open-ended fashion, say back to us, it is government regulation, the government in general, or it is something to do with Obamacare or healthcare.

Mr. HANNA. And for Ms. Kay, it would be certainty.

Mr. CLIFTON. And I would further say that if that is not the reality, it is at least the perception, and perception is a reality. And so that is something that maybe from a communications standpoint we would need to address.

Mr. HANNA. Thank you. My time is expired.

Chairman CHABOT. Thank you. The gentleman's time has expired.

The gentleman from South Carolina, Mr. Rice, who is chair of the Subcommittee on Economic Growth, Tax, and Capital Access is recognized for five minutes.

Mr. RICE. Thank you. What a pleasure to listen to you today. It is, unfortunately, the same things I hear from small businesses back in my district. I was a tax lawyer and CPA for 25 years before I came here. I formed or advised 1,000 small businesses. I know what they have to deal with, and these are the same problems I have heard all along.

Mr. Clifton, you said the biggest problem people referenced was finding customers, and actually, if you look at what has happened since 2008 when the president came into office, median household income has declined 8.7 percent. Interestingly, in that same period of time, the pay of the average government worker has gone up 12 percent. But at the same time we have had energy costs, because we have put up roadblocks through EPA and warm and cold and all these things. Energy costs have gone up about 10 to 20 percent.

Food costs, because they rely on energy costs, have gone up 15 percent. Healthcare cost, with Obamacare, some because of Obamacare, some otherwise, have gone up 15 to 20 percent. And so you have got this squeeze on the middle class where their incomes are down almost 10 percent, all their costs are going up 15–20 percent, and is it really any wonder that there is a lack of customers? Because people have less money to spend. And when you see the economy going up—I mean, excuse me, the stock market going up and people say, "Oh, look, the economy is going great," but the average middle class family is not feeling that. In fact, they are feeling quite the opposite. And they are really the customer base. I mean, two-thirds of the United States economy is based on consumer spending.

Am I analyzing that correctly, Mr. Clifton?

Mr. CLIFTON. I think that is accurate. I mean, if you look at kind of the root of what is happening here, is the fact that real household incomes have not increased. And when we look at the data, the data very clearly suggests that most would-be entrepreneurs or small businesses do start their businesses with their own money or capital from friends and family.

Mr. RICE. I am not even talking about business owners; I am talking about their customers. Their customers are broke.

Mr. CLIFTON. I do not disagree with that analysis.

Mr. RICE. All right, now, Ms. Kay, you talked about uncertainty. It pains me when you look at some of the things we do here in Congress, for example, with the tax extenders, the 179 deduction. That is designed to be an incentive for small businesses to invest, to grow the economy, to spend money to grow the economy, to make their business more productive to grow the economy. How can it act as an incentive when we pass it two weeks before the end of the year? People do not know it even is there, so how is that an effective incentive? That is not a very good job by Congress, is it, Ms. Kay?

Ms. KAY. Well, it certainly is not helpful. And I think when I talk about certainty, I am not talking about next week or next month or two months down the road. I am talking about long-term certainty. I am talking about the ability for us to plan a year out. And you are absolutely correct. When you wait until the last two weeks of a year, there are a number of people who are astute enough that they are going to take advantage of it, but for many small business owners, it is too late. And I think that what we are really looking for—and you talk about winners and losers. We understand that there are going to be some winners and some losers. I think what we are looking for is we are looking for some fairness, and we are looking for some long-term certainty so we know what the rules are so we can make some plans. And then I think you will find that people will invest in their companies. When I talked about——

Mr. RICE. I only have 40 seconds, so I just want to——

Ms. KAY. Okay.

Mr. RICE. You know, tax extenders. We talk about tax extenders when we should be talking about tax reform.

Ms. KAY. We should be.

Mr. RICE. We talk about repealing Obamacare when we should be talking about how we are going to replace it. We talk about—and then we have things like the Highway Trust Fund that is running out of money, and we do not know how we are going to build our infrastructure and we put Band-Aids on it every nine months. We talk about the Social Security Trust Fund and the Medicare Trust Fund. All these things create uncertainty to the economy, and how does that affect consumer spending, Mr. Clifton? It hurts it, does it not?

Mr. CLIFTON. Absolutely.

Mr. RICE. It hurts business investment, does it not?

So I am glad that we here in Congress are not doctors or lawyers because I think we would be sued for malpractice before it was over with.

Finally, Ms. Fine, you said that——

Chairman CHABOT. The gentleman's time is expired but the chair will extend an additional minute if there is no objection.

Mr. RICE. Thank you. Thank you, Mr. Chair. Thank you.

You said that we needed to do more to help entrepreneurs. And if you mean more government programs and more government regulation, I think you can see the effect of this on the economy already. I think the best thing we can do to help new entrepreneurs is in fact do less. Thank you very much.

Chairman CHABOT. Thank you.

The gentleman from New York, Mr. Gibson, is recognized for five minutes.

Mr. GIBSON. Well, thanks, Mr. Chairman. I appreciate the panelists. I think this has been a very informative hearing. I appreciate a lot of what has been discussed here this morning.

I would tell you that a lot of it, as Mr. Rice mentioned, jives with what I hear back home. Concerns with taxes, levels of taxes, complexity of the code, concern with certainty, in particular the expensing piece of it. I have heard this morning also concerns about the regulatory state and expression of desire of reform and relief. I have heard access to credit mentioned, all these things. Every time I visit a small business and listen to the owners and their employees—lower healthcare costs and energy costs, particularly for the Northeast, the energy costs are a concern. All of this if we are competing. Even our small businesses may be competing nationally or possibly even internationally. And so all this bearing on the problem. I appreciate being added to this Committee to allow a voice for my people.

And so I do have an initial question here, and I just want to again reiterate, I appreciate what has been said already. Why I say that is I think you have given us more data points of where the Committee is already thinking about going in terms of legislation, and so we appreciate your time, and I think it is meaningful.

Mr. Burton, you mentioned 97 points. I have this one situation in our district where I have got a small business, about 200 actually, so more in the upper end of the small business. But sterling credit. And they have a tremendous relationship with a community bank. Sterling record. And they had a very exciting project to expand, and they could not make it happen because of Dodd-Frank.

And so among your 97 points, do any of them address explicitly that situation and other magnification on issues of access to credit?

Mr. BURTON. Absolutely. There is a number of things. Some of it is credit, but also, they could seek equity investment. There are lot of things in my testimony about equity investment. There are things about eliminating the artificial limitation of credit unions' ability, which would give them another financial institution they could go to. I do not go a lot into it because I did not think it was sufficiently small business oriented, more financial services, but there is a lot of interest on the part of the House Financial Services Committee on a bipartisan basis in terms of trying to reduce the restrictions on community banks which might help. Peer-to-peer lending is another opportunity, and there are two different ways to do that. Either fix Title 3 of the Crowdfunding Act with respect to debt securities, or create a new regulatory regime so organizations like Prosper and Lending Club can lend to small businesses without having to use banks as intermediaries, and in fact, go around the banks. So there are a lot of things that could be done.

Mr. GIBSON. Well, thank you. And we are listening. And I think some of these things we are already looking to move on, but that is helpful.

Last question here, and it is really one I am curious of your feedback. Last Congress, we worked together and enacted a bipartisan piece of legislation that helped with job training, and explicitly, I am now thinking about my small business owners who are especially manufacturers that were very frustrated with their new recruits and their lack of preparation for some of the work that they want them to do. So the intention of the new bill was to try to address that; bring closer this activity that often leads to either a degree or certification in individuals who are going to start working. Because we know there is going to be activity to get a degree or certification. We want it to actually be meaningful. So more internships. Is there any feedback for us yet on this new law or is it too early?

Mr. BURTON. I am not sure, personally.

Mr. CLIFTON. I mean, from our data, that would suggest that that is the right direction because you have such a large percentage of would-be entrepreneurs that are asking for help in terms of how to get started.

But I think it is also the signal of another thing. And so when we look at what is crossed in terms of business deaths and business births, another thing that might be happening is sort of this decline in the spirit of free enterprise. And there are a number of conversations in terms of leadership within the government that are looking to young people, such as forgiving their school debts, their loans, if they come to work for the government. And so there is nothing wrong by that because what we are doing is celebrating the heroes and the sheroes that want to get into the government. But what it fails to do is we are not sending the strong enough signals that there are those heroes and sheroes that will start the big next businesses that will create the jobs that will restart this economy.

Mr. GIBSON. That is a good point. And my time is expired. And so I will yield back. Thank you.

Mr. RICE. Thank you to the gentleman.

Now, I yield to the ranking member, Ms. Velázquez. She has a couple of additional questions.

Ms. VELÁZQUEZ. Just two more questions.

Mr. Clifton, I would like to ask, what percentage of survey respondents are would-be entrepreneurs? What percentage are startups in businesses less than three years, and what percentage are existing businesses older than three years?

Mr. CLIFTON. Those data are available from the Small Business Administration, but I think I might be able to provide a data point that is more helpful.

Ms. VELÁZQUEZ. For the survey, the Gallup Survey.

Mr. CLIFTON. We interview 600 small businesses per quarter with Wells Fargo. We pull the list from Dunn and Bradstreet and the waiting scheme that we do is based on their revenue and their location.

Ms. VELÁZQUEZ. So you do not have a breakdown in terms of would-be entrepreneurs, which percentage are startups in business less than three years and which percentage are those older than three years?

Mr. CLIFTON. Correct. We do not collect those data. They are available from the SBA. But I think a data point that is even more helpful is our analytics suggest that the percentage of people that have the rare talent to be that sort of incredible Wayne Huizenga-type that can start three global Fortune 500 companies, we believe it is somewhere three in 1,000 people that have that inherent talent.

Ms. VELÁZQUEZ. So none of the businesses—in your survey, none of the 600 are would-be entrepreneurs?

Mr. CLIFTON. Correct. That is a separate survey that we do.

Ms. VELÁZQUEZ. Okay.

Mr. CLIFTON. So 25 percent of Americans said that they have seriously considered——

Ms. VELÁZQUEZ. I am confused, because the focus of the hearing is on would-be entrepreneurs and what hinders business creation. So I do not know if my next question has any basis, but in your opinion, is the Gallup Poll a good measure of the top challenges for startups, or more challenges facing existing businesses?

Mr. CLIFTON. In my opening remarks, I addressed both. And they——

Ms. VELÁZQUEZ. But yet, in your sample, you do not have any would-be entrepreneurs.

Mr. CLIFTON. No, that is not—so in my opening statement, I addressed that we interviewed 25 percent of Americans that said they were would-be entrepreneurs. And they faced three significant barriers in order to start a business. So yes, I addressed both separately.

Ms. VELÁZQUEZ. So, Ms. Fine, in your work with entrepreneurs, how much do you hear that regulations like those from EPA, OSHA, factor into the decision of whether an entrepreneur starts a new business?

Ms. FINE. Like I mentioned before, I mean, we work with startups, entrepreneurs, at such an early stage of their business. Like we would tell anyone, these are all regulatory forces that they

have to investigate, and I think it is more of understanding if the business models works, given those regulations. So they have to go look at those and understand it. And that is a part of the discovery they need to do. And I would count that as part of them starting as entrepreneurs. It does not keep them from starting that process necessarily, but it might keep them, based on what they find, from figuring out if they have a viable business model.

Ms. VELÁZQUEZ. Thank you. Thank you, Mr. Chairman.

Mr. RICE. Thank you, Ms. Velázquez.

Mr. Burton, I want to ask you—maybe you are not the right person on the panel to ask this question, but do you think that the Dodd-Frank banking law prevents a community bank from making loans to small businesses that they would otherwise make?

Mr. BURTON. I think aspects of the Dodd-Frank Act clearly reduce community bank lending to small businesses. But I am not sure that is the central problem.

Mr. RICE, Okay. Ms. Kay, same question to you.

Ms. VELÁZQUEZ. Will you yield just for a second? It is on the community banks and Dodd-Frank.

Mr. RICE, Sure.

Ms. VELÁZQUEZ. I serve on the Financial Services Committee, and I was there when we were working on the legislation. Do you know that community banks who have assets of $10 billion or less are exempted?

Mr. BURTON. Yes. And that is one of the reasons why I said it was not necessarily the central problem. There are other aspects of Dodd-Frank that are problematic, but again, in terms of small business capital formation, I am not sure Dodd-Frank is the biggest problem we have on access to capital.

Mr. RICE. Ms. Kay, do you think Dodd-Frank prevents community banks from making loans to small businesses that they would otherwise make that they deem an acceptable risk but they would not make it with the Dodd-Frank banking regulation?

Ms. KAY. I would love to answer that question, but I am really not qualified to do that.

Mr. RICE. Okay. Same question to you, Mr. Clifton.

Mr. CLIFTON. We do not have data on that specifically.

Mr. RICE. Okay. All right. Thank you very much.

Look, this has been a wonderful hearing. You all have done a great job of educating me. Thank you so much for taking your time to come here to Washington to explain your perspective on the challenges facing small businesses today. I really cannot thank you enough.

And with that, I ask unanimous consent that members have five legislative days to submit statements and supporting materials for the record.

Without objection, so ordered.

This hearing is now adjourned.

[Whereupon, at 12:33 p.m., the Committee was adjourned.]

APPENDIX

GALLUP

Testimony of

Jon Clifton, J.D.

Partner, Managing Director

Gallup Government

Before the

U.S. House of Representatives

Committee on Small Business

Hearing on

Building an Opportunity Economy: State of Small Business and Entrepreneurship

March 4, 2015

Good morning, Mr. Chairman and Members of the Committee. It is a pleasure to be here to discuss Gallup's analytics on the state of the U.S. economy, the attitudes of small-business owners and the current barriers to job growth and startups.

The Importance of Jobs and Gallup's Tracking of the Job Situation

Gallup completed its first nationally representative survey of the world in 2006. Our biggest finding from this study was that what the whole world wants is a good job. This finding compelled us to more thoroughly study the global jobs situation. Gallup now quantifies the prevalence and quality of jobs in more than 140 countries each year. Gallup also tracks employment daily in the United States, surveying roughly 30,000 adults per month and more than 350,000 people per year.

The State of the U.S. Economy

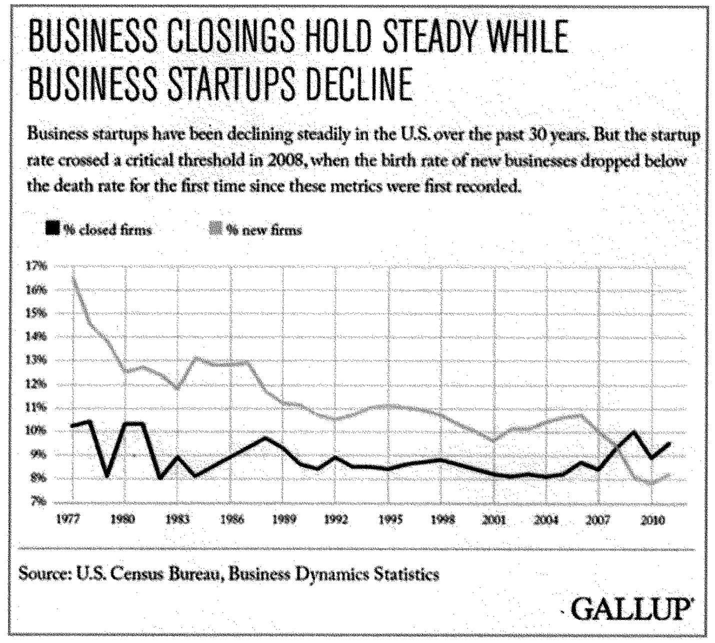
There are a number of signs from Gallup's data that the U.S. economy has been improving since the recession: Americans' attitudes toward the economy are improving, self-reported discretionary spending is steadily increasing and people are reporting that hiring is outpacing firing in their workplaces. Despite this encouraging news, job creation remains a problem.

While official unemployment has fallen from roughly 10% in 2010 to roughly 6% today, using this metric to represent the total

jobs picture could be misleading. Traditional unemployment includes only people who are looking for work, who are available for work and who have not worked a single hour in the past week. This means that if a person has given up looking for work or if a person has worked only a single hour in the past week, that person is not considered unemployed. A different metric offered by Gallup quantifies the number of people employed full time for an employer—often referred to as a “good job—as a percentage of the total adult population. Known as Payroll to Population (P2P), this metric stands at 44.3% today and has not meaningfully increased since early 2010, when Gallup started tracking this daily.

Barriers to Job Growth

One of the main reasons that the jobs situation has yet to recover is that, according to the U.S. Census, the number of business deaths now exceeds the number of business births among employer firms for the first time since 1977, when this measurement began.



The Current State of the Small Business Economy

This leads us to the importance of small businesses and startups in this country. They contribute roughly 70% of all new jobs created in a single year. Considering their importance, Gallup works with Wells Fargo to track the opinions and behaviors of small-business owners quarterly.

The good news is that the attitudes of small-business owners are steadily improving. The Wells Fargo/Gallup Small Business Index stands at +71, which is the highest index score since the onset of the recession. Sixty-four percent of small-business owners report that their company's current financial situation is good and 71% expect their company's financial situation to be good 12 months from now.

However, despite this positive trajectory, small-business owners face clear challenges. When asked to name their most important challenge, the No. 1 issue they report is finding or attracting new

customers (15%). This is followed by mentions of the economy in general (12%) and government regulations (10%). However, if we add those who cite healthcare/Obamacare (8%), our just government in general (6%), fully 24% of small-business owners say the government is in some way their biggest challenge. Also worth noting, while many small-business owners believe available credit is a major issue, only 3% say it is their most important challenge.

Barriers to Startups

In addition to the barriers faced by current small-business owners, there are also barriers facing would-be entrepreneurs. One in four Americans have thought about starting a business, but have abandoned the idea. For an economy with a negative net number of startups each year since 2008, this represents a missed opportunity to engage would-be entrepreneurs that could result in business startups. Three major barriers are keeping these would-be entrepreneurs from taking the plunge: 1) they prefer the security of a stable income, 2) they do not have enough money to start a business and 3) they lack the knowledge on how to start a business. Because the majority of business owners fund their early-stage businesses through personal savings, a steadily declining personal savings rate in the United States has negatively affected prospective entrepreneurs' ability to finance new businesses. Moreover, if they lack insight on where and how to begin, starting a business is even more difficult, and these prospective entrepreneurs are more likely to be more risk averse.

Conclusions

Creating good jobs and subsequently rebuilding America's middle class hinges on the success and failure of small businesses and startups. Existing small businesses are experiencing headwinds caused primarily by challenging business realities, the overall economy and a concern about government regulations. Would-be entrepreneurs face barriers such as not having enough money to start a business and lacking knowledge about starting a business. It would be wise for Congress and American leadership to consider all options to unlocking this invaluable economic institution. The American public would be behind them. Other than the military, there is no other institution in the United States that the public has more confidence in than small businesses.

Attachments

Figure 1

Gallup's U.S. Economic Confidence Index -- Monthly Averages

January 2008 through January 2015

Gallup Daily tracking

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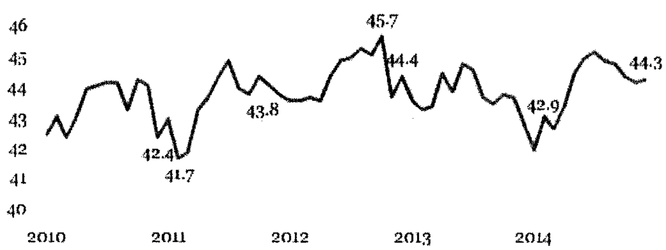
Figure 2

U.S. Payroll to Population Employment Rates

Monthly trend, January 2010-December 2014

■ % of adult population employed full time for an employer



Gallup Daily tracking

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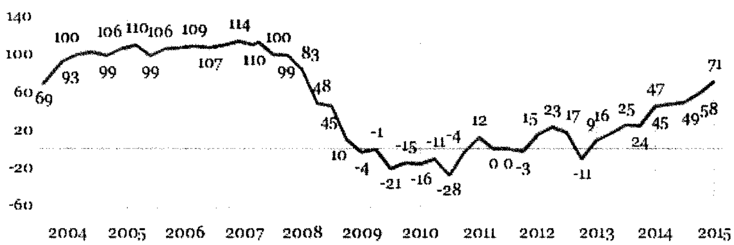
Figure 3

Wells Fargo/Gallup Small Business Index

The Small Business Index consists of owners' ratings of their business' current situation and their expectations for the next 12 months, measured in terms of their overall financial situation, revenue, cash flow, capital spending, number of jobs, and ease of obtaining credit.



Index conducted since August 2003 and quarterly from December 2003-January 2015

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Figure 4

Wells Fargo/Gallup Small Business Index -- Most Important Challenge

What do you think is the most important challenge facing you as a small-business owner today? (Open-ended)

	Qtr 4 2013-Qtr 4 2014
Attracting customers/Targeting business opportunities/Finding work/New business	15%
The economy	12%
Government regulation	10%
Healthcare/Obamacare	8%
Financial stability/Cash flow	8%
Hiring qualified/Good staff and retaining them	7%
Costs/Fees of running the business/Having enough money for capital investment	7%
Taxes	7%
Government (general)	6%
Competition/Larger corporations/Internet	5%
Other	3%
Credit availability	3%
None/Nothing	2%
Employee benefits	1%

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Figure 5

Now I am going to read you a list of institutions in American society. Please tell me how much confidence you have in each one -- a great deal, quite a lot, some, or very little?

Sorted by most to least confidence in 2014

	% A "great deal" and "quite a lot" of confidence
The military	74
Small business	62
The police	53
The church or organized religion	45
The medical system ^	34
The U.S. Supreme Court	30
The presidency	29
The public schools	26
Banks	26
The healthcare system ?	23
The criminal justice system	23
Newspapers	22
Organized labor	22
Big business	21
News on the Internet	19
Television news	18
Congress	7

June 5-8, 2014

^ Based on 510 respondents
? Based on 517 respondents

GALLUP

Testimony of Cynthia Kay
Owner & President

Cynthia Kay and Company Media Production

On behalf of the National Small Business Association

NSBA
National Small Business Association®

House Committee on Small Business Hearing:

"Building an Opportunity Economy: The State of Small Business and Entrepreneurship"

March 4, 2015

Good afternoon. My thanks to Chairman Chabot, Ranking Member Velazquez and the members of the Small Business Committee for inviting me to testify today on the health and vibrancy of the American economy, and challenges that small businesses like mine face as it pertains to the creation, sustainability, and future growth of our businesses.

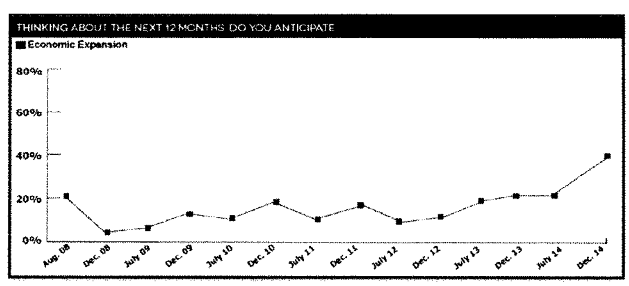
My name is Cynthia Kay and I am President of Cynthia Kay and Company based in Grand Rapids, Michigan. CK and CO is a full-service media production and corporate communications consulting company. The company is a certified Women's Business Enterprise. While we are truly a small business, with a full-time staff of eight, we are the production company of choice for a number of global companies, such as Herman Miller, Siemens Industry, Wiley Publishing as well as many non-profits. I also come from a family of small-business owners. My father co-owned a small dry-cleaning business. My sister and her husband own a boutique rental company in Raleigh, North Carolina and my brother is an attorney.

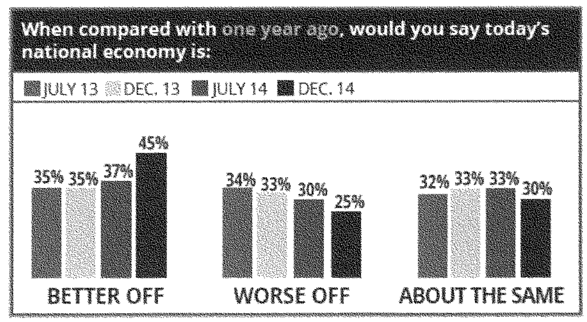
I am proud to be here representing not only my company, but also the National Small Business Association (NSBA)—the nation's first small-business advocacy organization. NSBA is a uniquely member-driven and staunchly nonpartisan organization—where I currently serve as Vice Chair of Advocacy. I also served as chair of the Small Business Association of Michigan, one of NSBA's regional affiliates in 2010-2011. One of the things that I believe NSBA does brilliantly is to conduct surveys to provide data that really give a snapshot of the current issues facing small business and long term trending data.

NSBA has members in all sectors and industries of the U.S. economy from retail to trade to technology—our members are as diverse as the economy that they fuel. Small employers comprise 99.7 percent of all employer firms in the U.S. One in two workers in the private workforce run or work for a small business, and one in four individuals in the total U.S. population is part of the small-business community. Those are certainly impressive figures.

NSBA Year-End Economic Survey Results

As a business owner for the past 27 years, I have experienced first-hand a number of economic downturns, none more difficult than the past one. The good news is that business is booming for my company and I am not alone. The NSBA's recently released 2014 Year-End Economic Report shows that today's economic outlook for America's small-business owners is better than it has been in quite some time. And, today more small-business owners anticipate economic expansion in the coming year than have at any point in the last seven years.





When asked to compare today's economy with one year ago, 45 percent, up from 37 percent just six months ago, say it is better—that is the highest this indicator has been since we started asking the question. Although, there is a noted improvement on small-business owners' economic outlook, we are still not out of the woods yet and the majority of small firms still expect a flat or recessionary economy in the coming year.

Of course, small businesses like mine still face significant challenges, and despite the gains in economic outlook, the report found little change over the last six months when it comes to small-business owners' confidence about the future of their own business as well as job growth.

I had the opportunity to participate with business owners from across the country in the NSBA Small Business Congress held earlier this month in Phoenix, Arizona. After lengthy debate and voting by our members, NSBA unveiled its Top-10 priorities for the 114th Congress and the number one priority for small firms is ensuring corporate-only tax reform includes some kind of workable solution for the millions of pass-through small businesses. In the interest of transparency you should know that my company is a C-Corporation, but so many of my suppliers and fellow business owners are S-Corporations.

Taxation of Pass-through Entities

As I mentioned, most small businesses that I work with are sole proprietorships, subchapter S corporations or limited liability companies. Most of the remainder are partnerships (either limited or general). There also are some business trusts. All of these businesses (83 percent, according to NSBA data) pay taxes on their business at the personal income level, or are so-called "pass-through" entities that are subject to individual tax rates – not corporate tax rates. It should come as no surprise then that according to NSBA data income taxes are consistently ranked the most burdensome administratively, while payroll taxes were ranked the most burdensome financially, by small firms.

Some small businesses—such as mine—are C corporations that are subject to the corporate income tax, but these are a relatively small percentage and a large portion of these companies' net income before compensating the owners' is usually consumed by paying the owners' salary. This salary is also subject to the individual tax rates as, of course, are any dividends paid by the corporation to its shareholders. Thus, even for small C corporations, individual tax rates are key.

Broad reform of the entire tax code is necessary, not just for corporate entities. Allowing the

smallest businesses to pay a much higher tax on their business income than a multinational, multi-billion corporations undercuts any semblance of fairness. Many proposals have called for reducing the corporate tax rate while eliminating various business deductions and credits, which—if not examined more closely—sounds like a fine plan. However, many pass-through entities, small businesses, utilize these tax benefits that would be on the chopping block. So now many of my suppliers would be facing the same, high tax rate on their business income, and would no longer be eligible to take advantage of some important tax credits and/or deductions. The result is a tax increase on these firms while large corporations would be given a tax cut.

I firmly believe that addressing just one piece of the puzzle—such as corporate tax reform—will only lead to even greater complexity and a massive tipping of the scales in favor of the nation's largest companies at the expense of small businesses.

Imposing higher tax rates on small firms will stymie any growth from what is widely recognized as the source of much of the economic growth and dynamism in the U.S. economy: small business. For the overwhelming majority of small businesses, individual marginal tax rates are much more important than corporate marginal tax rates. Since small businesses disproportionately contribute to job creation, raising individual marginal tax rates can be expected to have a disproportionate negative impact on job creation. It is this kind of shortsightedness that has made the IRS a major foe of small firms and why so many of us support broad tax reform.

If Congress overhauls the tax system by dramatically broadening the base —cutting the breaks that litter the tax code—and lowering rates, we would see real economic growth and raise revenues.

Access to Credit and Capital

Even in the best of times, access to capital is one of the largest impediments facing America's small businesses, hindering both aspiring and thriving entrepreneurs. In fact, the small-business members of NSBA consistently identify access to credit and capital as one of the top issues impacting their firms.

When I started my business, the only way to get a loan was to sign a personal guarantee using the equity in my house. I did that several times over the years to obtain capital. This perennial problem is only exacerbated during troubled economic periods, such as those many businesses are still experiencing today. In fact, over the last seven years, one-in-three small firms on average cannot access adequate financing for their business.

One of the biggest barriers to small-business financing is requiring debt be secured by equity in fixed assets. Many small and startup businesses lack the kind of equity necessary for traditional bank loans. This gap in debt-equity financing especially hinders startup and growing businesses, as these entrepreneurs typically do not have the assets necessary to acquire sizeable loans.

When my sister and her husband wanted to buy their business they also encountered these type of difficulties, even though they are highly educated and had great work history. Our family and

my business ended up financing their startup. While this was many years ago, and things have improved slightly, you should know small businesses still see the lack of available capital among their top challenges. This comes at a time when small businesses believe the economy is improving and they are willing to take on additional debt in the form of financing. Without financing, we cannot expand our businesses and hire more employees.

If capital availability is a problem for your business, what is the effect on your operations?

	DEC. 2014	JULY 2014	DEC. 2013	JULY 2013
Unable to grow business or expand operations	34%	33%	36%	36%
Unable to finance increased sales	18%	15%	17%	18%
Reduced the number of employees	16%	18%	20%	20%
Unable to increase inventory to meet demand	13%	10%	11%	10%
Reduced benefits to employees	11%	12%	13%	14%
Other (please specify)	3%	2%	3%	3%
Closed stores or branches	1%	3%	3%	4%
Not a problem / No effects	56%	57%	54%	50%

Another barrier to capital for small businesses is that banks too often shy away from the small-business community. Smaller loans generally are less-profitable for banks and typically have higher default rates. Additionally, the proper valuation and credit worthiness of small businesses are notoriously difficult to determine. Ongoing bank consolidation has led to fewer community banks and fewer character-based loans which has limited small businesses in getting financing. In fact, small-business loans have steadily been declining: in 1995, small loans represented 40 percent of bank loan dollars but today it is only 23 percent.

What types of financing has your company used within the past 12 months to meet your capital needs?

	DEC. 2014	JULY 2014	DEC. 2013	JULY 2013
Credit cards	36%	30%	33%	31%
Earnings of the business	35%	32%	34%	35%
Used no financing	27%	28%	27%	30%
Community Bank Loan	20%	19%	19%	18%
Vendor credit	19%	15%	17%	16%
Private loan (friends or family)	18%	17%	17%	17%
Large Bank Loan	17%	19%	20%	13%
Leasing	6%	6%	6%	5%
Other	5%	5%	5%	5%
Credit Union Loan	4%	2%	3%	2%
Small Business Administration (SBA) loan	3%	4%	3%	5%
Selling/pledging accounts receivable	3%	2%	2%	2%
Private placement of debt	2%	2%	3%	2%
Venture capital/Angel investors	2%	n/a	n/a	n/a
Online or non-bank lender	1%	1%	1%	n/a
State/Regional Loan and Incentive Programs	1%	1%	1%	1%
Crowdfunding	1%	1%	0%	n/a
Private placement of stock	1%	2%	1%	1%
Public issuance of stock	0%	0%	0%	0%

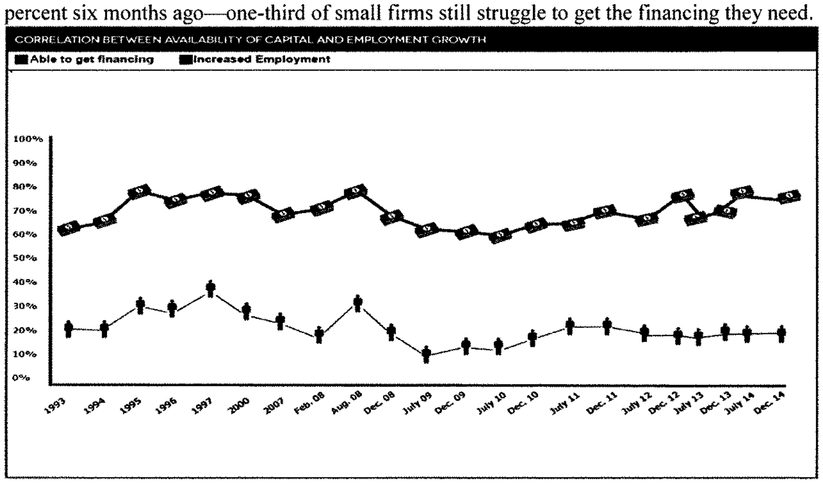
When asked how the absence of capital is negatively impacting their business, there was a concerning trend whereby more small-business owners report a lack of financing is hindering their ability to finance increased sales or increase inventory to meet demand. Nearly one-in-five small firms cannot meet increased sales demand due to an inability to garner financing.

While insufficient access to capital has long been a lament in the small-business community, the current capital vacuum has created a new predicament for small-business owners: Use credit cards or bust. When asked what kind of financing their

company used, there was a notable jump among small firms that rely both on credit cards and earnings of the business. These two are the most quickly accessed forms of financing which could indicate newer businesses seeking financing as well as new opportunities for existing businesses that may not have the track record required by other financing tools.

Among those surveyed, there are a handful of other contributing factors to the increase in credit card usage as well, including: a five-percentage-point increase among firms who report there was an increase on their line of credit or credit card in the last six months; a drop among small firms who say the terms of their credit cards worsened in the past six months; and the average interest rate dropped from 13.94 percent in July 2014 to 13.05 percent today.

According to NSBA data from as far back as 1993, there is a clear correlation to a small-business owner's ability to hire and his/her ability to get financing. Although the number of firms that report being affected by the credit crunch continues to drop—down to 61 percent from 66 percent six months ago—one-third of small firms still struggle to get the financing they need.



Capital is the lifeblood of small business and without it, the heart of America's economy—its millions of small businesses—stands poised to fail.

Tax Extender Permanency

In recent years, Congress has enacted dozens of important tax provisions for small businesses to encourage job creation, investment, research and international competitiveness. However, due to budgetary and political restraints, too many of these provisions were enacted on a temporary basis, requiring repeated extensions and creating layers upon layers of complexity and instability rendering any kind of reasonable tax planning nearly impossible for small business. Now, however, these provisions have been expired since the end of last year and by Congress

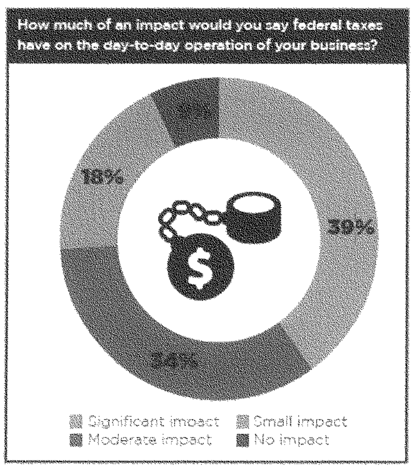
continuing to further delay there extensions, it punishes our work, investment, risk-taking and entrepreneurship. Absent comprehensive tax reform, extending and making permanent important business tax provisions has long been on NSBA's priority list.

Which of the following deductions or credits do you take advantage of? (Check all that apply)	
Sec. 179 expensing	34%
Home mortgage interest deduction	31%
Home office deduction	22%
Bonus depreciation	20%
15-year straight-line cost recovery for qualified leasehold improvements, qualified restaurant buildings and qualified retail improvements	13%
R&E (Also called R&D) credit	8%
Energy efficiency credits	5%
Start-up costs deduction	5%
Work Opportunity Tax Credit	3%
None of the Above*	27%
Other	4%

*The ongoing debate over the so-called "tax extenders" holds significant importance for small businesses as the majority, 73 percent, report utilizing some kind of tax benefit covered under the extenders umbrella.

As a media production company, tax extenders are of major significance to my business. You have heard the saying "lights, camera, action" well, all of that costs a great deal of money and the technology is constantly changing. The high-definition cameras we bought two years ago are no longer state-of-the art. Today 4K cameras are the new format and 3D graphics are being replaced by Cinema4D. We are constantly buying or updating equipment and the out-of-pocket expense is significant.

In the past, we have been able to utilize Section 179 expensing. It is critically important for my company, as we invest in new equipment; we are able to deduct the cost of the asset in the year that we purchase it, especially since technological equipment needs updating sooner than the 5 to 7 years that it is required to be depreciated over. And this is not just affecting my company, more than one in three NSBA members, according to NSBA's 2014 Taxation Survey, take advantage of this break as it simplifies tax accounting, helps with cash flow and reduces the cost of capital.



Now, even if I wanted to take advantage of Section 179 I can't because on Dec. 31, 2014 it expired, along with more than 55 other tax provisions commonly referred to as "tax extenders." The loss of some of these vital credits has and will negatively impact job creation, investment, research and international competitiveness. It's no wonder so many small firms, according to the aforementioned Taxation Survey, say federal taxes have a significant impact on the day-to-day operation of their business—and no wonder why so many small firms are beyond frustrated with the Tax Code.

Regulatory Reform

Often cited as one of the biggest challenges facing manufacturers and small businesses, coercive, combative, and expensive federal regulations hurt our economy as we spend countless

hours trying to understand, interpret and comply with the overwhelming array of federal regulations.

Firms with fewer than 20 employees spend 36 percent more per employee than larger firms to comply with federal regulations at $10,585 per employee per year, according to the SBA Office of Advocacy.

Time and again, I hear from my small business clients and suppliers about their desire to have a more simplified approach to complying with federal regulations and their paperwork requirements. Yet, more often than not, small-business owners find themselves buried under mountains of paperwork when they could be helping their customers, hiring new employees and expanding their businesses.

For a small business, I have to have a lot of advisors. Just to give you a sample. I use an accounting firm, an insurance firm, a corporate lawyer, an HR lawyer. In the past, I used an environmental lawyer for issues with a building I wanted to buy. And the list goes on. It's not that I don't love lawyers, my brother is one, but each one of these resources is costing my company money and the time to deal with all of the regulations.

Personally, I think we tend to be an easy target since unlike big corporations—which have hordes of accountants, benefits coordinators, attorneys, personnel administrators, etc. at their disposal—small businesses often are at a loss to keep up with, implement, afford, or even understand the overwhelming regulatory and paperwork demands of the federal government.

Small business owners are smart people, but we often experience a hard time dealing with the complexity of ambiguous terms, intricate technical language and difficult sentences. The increased burden causes us to have trouble understanding the requirements. This forces us to spend more time trying to interpret the rules and ensure we are completing the forms accurately thus avoiding being fined by the agency for noncompliance. The best thing for small businesses is simplicity: simplicity in instructions, in requirements, in consequences and an overall reduction in the size of the paperwork and the time necessary to complete the forms.

While small-business owners agree compliance assistance is necessary, it also must be streamlined and put into plain-language. It is unrealistic for small businesses to comply if the only methods of communication are huge envelopes that are packed with books and pamphlets. Although small-business owners appreciate the efforts and hard work put into creating detailed instruction manuals, agency officials must consider the time it will take for the recipient to read through a 195- page instruction manual and decipher poorly organized, difficult to read forms that contain an abundance of technical terms. Most small-business owners do not have the training or experience to translate legalese and decipher the convoluted directions that accompany most government forms. Small-business owners are smart, entrepreneurial, creative and quick students. We are not, however, regulation specialists.

On behalf of NSBA, I would like to thank you, Chairman Chabot, for all your work in advancing the Small Business Regulatory Flexibility Improvements Act of 2015 (H.R. 527) earlier this year. This important piece of legislation strengthens the voice of small business in the federal

rulemaking process and makes agencies fully quantify the impact of major rules by requiring federal agencies to consider indirect economic effects, in addition to direct effects, when writing regulations, guidance and policy statements. NSBA was pleased to support H.R. 527 as it improves transparency and ensures that agencies thoughtfully consider the impact of regulations on small businesses.

More can still be done and for this reason, NSBA played a critical role in developing the idea of a National Regulatory Budget—another 114th Congress priority—to bring much needed reform, transparency, and priority setting within the regulatory process. Reining in excessive regulations will provide a boost to, and certainty for entrepreneurs as we work to compete, expand and create jobs.

Cybersecurity

Given the increasingly commonplace occurrence of hacking and cyber-crimes, coupled with the fact that, over the past few years in a difficult economy, small-business owners are handling more of their firm's IT operations, cybersecurity is a growing concern for small business.

Has your business been the victim of a cyber-attack (i.e. computer virus, malware/spyware, website hack, credit card or banking hack or trojan, etc.)?

	DEC. 2014	2013
Yes	50%	44%
No	50%	56%

The Year-End Economic Report emphasizes the fact that in an increasingly technology-reliant global marketplace, cybersecurity issues and vulnerabilities can bring commerce to a screeching halt. What NSBA found is truly startling. Today, half of all small businesses report they have been the victim of a cyber-attack – up from 44 percent just two years ago. Among those who were targeted 68 percent report being a cyber-victim more than just once.

In fact, my company is included in that fifty-percent, as CK and CO has been the target of an attack. Hackers tried to get access to our corporate banking account. Fortunately, the attempt was foiled by our bank. But we continue to get phishing e-mails and other suspect communications. I am especially vigilant about cybersecurity because we serve larger, global customers. We have numerous non-disclosure and confidentiality agreements in place because we are creating video and other communications regarding new products they are launching and financial information they need to communicate to employees and stakeholders. This information in the wrong hands could be devastating to our customers.

Small-business owners are becoming increasingly tech savvy, but limited resources and knowledge still leave many vulnerable to cyber-threats. In 2013, cyber-attacks cost small businesses on average $8,699

Approximately how much did this cyber-attack cost your business?

	DEC. 2014	2013
Average Estimated Cost	$20,751.97	$8,699.48
Average Money Stolen from Bank Account	$19,948.11	$6,927.50

per attack. Today, that number skyrocketed to $20,752 per attack. For those firms whose business banking accounts were hacked, the average losses were $19,948 today–up significantly from $6,927 in 2013. This huge jump in cost is likely due to the increased sophistication in phishing and hacking schemes as well as an improved economy that finds greater funds available in many small firms' bank accounts than was there just two years ago.

As small businesses become increasingly dependent on services and applications that connect to the internet, they also become a larger target for cybercriminals looking to exploit vulnerabilities to steal money and credit card credentials, intellectual property, personally identifiable information as well possibly destroy data and disrupt operations. The truth is, it is not a question of if a business will be the target of an attack; it is a question of when. For many small firms, a cybersecurity incident could lead to an entire network being down for many days until the full extent of the problem is known and then fixed. Several of the suppliers I work with would not be able to withstand the loss of income, or have insurance to help defray those costs or any liabilities that might occur as a result of the breach. A highly public breach could also damage the business's brand and lead to long-term loss of income.

Conclusion

Small businesses, despite a more positive overall economic outlook, continue to struggle with hiring and garnering quality, affordable capital. Not only are our elected officials not doing enough to improve the U.S. economic situation, oftentimes, they are causing economic stagnation by their inability or unwillingness to deal with serious issues facing the country and preoccupation with reelection.

Small businesses simply need the environment to grow and create jobs: economic stability; predictability, fairness and transparency in taxes and health care costs; common-sense regulations that don't unfairly disadvantage small firms; and lawmakers willing to tackle the major issues facing our country, and to do so together.

Looking ahead to the coming year, the Year End Economic Report finds the majority of small firms—60 percent—anticipate increases in revenue, and slightly fewer—54 percent—anticipate increases in profits, both number the highest percentages in the past seven years. Additionally, small-business owners are projecting modest growth in hiring and continued growth in employee compensation in the coming 12 months.

I began today by saying the economy has improved. It has. The phone is ringing for many small businesses like mine and there is pent up demand for products and services. As a small-business owner, I need to be able to focus my time and effort on "doing business" and meeting these needs. But, I and other owners can only do that if it gets easier and simpler. There is not a month that goes by that a potential small-business owner reaches out to me to ask advice about starting a new business. As I am sure you can tell I am direct. I tell them how great it is to be a small-business owner, but I also tell them about the significant challenges. Many decide to go back to work with a larger firm and not take the chance because they fear the burdensome regulations and the cost. These are potential small businesses that could help us continue the recovery and create new jobs.

Despite this overall vast improvement in outlook from existing small-business owners, we are facing a significant dearth of new start-ups. As our friends at Gallup point out, the rate of new firm births is being outpaced by firm deaths. Specifically, according to Gallup, 400,000 new businesses are being born annually nationwide, while 470,000 per year are dying. They go on to report that until 2008, startups outpaced business failures by about 100,000 per year. But in the past six years, that number suddenly turned upside down.

I have to believe that a good portion of this is due to the growing set of hurdles over which would-be entrepreneurs must jump: the inability to garner financing; the vast web of local, state and federal regulatory requirements; the massive local, state and federal tax burden; the growing cost of health care and new requirements on employers which are riddled with errors; the threat of lawsuit and liability in any number of areas, both from government and private citizens; the high cost of protecting your intellectual property; and the list goes on and on.

These are all areas where lawmakers can intervene and ease the burden on existing small firms and likely make entrepreneurship once again a sought-after life trajectory for many Americans who today are opting to work for someone other than themselves. I've been doing this for 27 years and it still keeps me awake at night – it is no wonder that people who have never done it before and looking at what they are up against walk away.

At NSBA, we stand ready to work with you in helping to ease these burdens with proactive solutions such as broad tax reform, the National Regulatory Budget and many other proposals that will make running a small business easier.

Again, I would like to thank Chairman Chabot and the members of the Small Business Committee for the opportunity to speak today. I would be happy to answer any questions you may have.

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CONGRESSIONAL TESTIMONY

"Building an Opportunity Economy: The State of Small Business and Entrepreneurship"

Testimony before

The Committee on Small Business
United States House of Representatives

March 4, 2015

David R. Burton
Senior Fellow in Economic Policy
The Heritage Foundation

My name is David R. Burton. I am Senior Fellow in Economic Policy at The Heritage Foundation. I would like to express my thanks to Chairman Chabot, Ranking Member Velázquez, and members of the committee for the opportunity to be here this morning. The views I express in this testimony are my own, and should not be construed as representing any official position of The Heritage Foundation.

After complying with the multitude of state and federal legal requirements, business owners should still have time left over to actually run their businesses. Entrepreneurs shouldn't have to be lawyers to run businesses in the United States. Unfortunately, that is just about where we find ourselves today. It is not where we want to be if we desire a return to sustained prosperity.

Entrepreneurship matters. It fosters discovery, innovation and job creation. It leads to more productive production processes that improve productivity and real wages. Entrepreneurs develop new and less expensive products that improve consumer well-being. They make markets more efficient. New firms account for most of the net job creation in the United States. Moreover, the vast majority of economic gains from innovation and entrepreneurship accrue to the public at large, rather than entrepreneurs.

Entrepreneurship is in decline. Business exits now exceed new business formations. Many other indicia of entrepreneurial health also indicate that we have placed an unprecedented burden on small and start-up businesses. Accordingly, job creation, productivity improvements and welfare-enhancing innovation have slowed.

The reasons for this are manifold. One policy change – or even a few – will not solve the problem because the problem is caused by the combined weight of hundreds of regulatory or statutory burdens imposed on small and start-up enterprises.

The problems fall into eight basic categories.

1. **Poor Tax Policy.** Poor tax policies raise the cost of capital, impose high taxes on risk taking and impede economic growth. Moreover, the tax system is monstrously complex, imposing inordinately high compliance costs on small and start-up firms.

2. **Inadequate Access to Capital.** Securities laws and, to a lesser extent, banking laws and practices, restrict entrepreneurs' access to the capital needed to launch or grow their businesses. After all, without capital to launch a business, other impediments to entrepreneurial success are moot.

3. **Expensive Health Care.** The U.S. health care system is the most costly in the world and the Patient Protection and Affordable Care Act (Obamacare) imposes high costs on firms with 50 or more employees.

4. **Burdensome Energy and Environment Laws.** Environmental and energy regulations raise the cost of energy and limit development of energy resources.

5. **High and Growing Regulatory Costs.** The cost of complying with increasingly burdensome and complex regulations continues to grow rapidly. These rules have a disproportionate adverse impact on small and start-up companies that can ill afford to use scarce resources on regulatory compliance rather than growing their business.

6. **Onerous Labor and Employment Laws.** Increasingly complex and opaque labor and employment laws raise the cost and risk of employing people. They reduce wages and cost jobs.

7. **Bad Immigration Rules.** The U.S. immigration system makes it difficult for firms to gain access to talented foreign workers and for immigrant-entrepreneurs to enter the United States to start a business.

8. **Costly Legal System.** The U.S. legal system is the most costly in the world, imposing high and potentially ruinous costs on small firms.

If we want a return to a prosperous America with opportunity for all and rising real wages, then Congress needs to systematically address these issues with alacrity.

The remainder of this testimony examines in greater detail why entrepreneurship matters, the evidence that entrepreneurship is in decline and the reasons for the decline. It makes 97 specific recommendations to remove barriers to entrepreneurship and economic growth.

Entrepreneurship Matters

Entrepreneurship matters.[1] It fosters discovery and innovation.[2] Entrepreneurs also engage in the creative destruction of existing technologies, economic institutions and business production or management techniques by replacing them with new and better ones.[3] Entrepreneurs bear a high degree of uncertainty and are the source of much of the dynamism in our economy.[4] New, start-up businesses account for most of the net job

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[1] For an introduction to the literature, see Paul Westhead and Mike Wright, *Entrepreneurship: A Very Short Introduction* (Oxford University Press: 2013).

[2] Israel M. Kirzner, *Competition and Entrepreneurship* (University Of Chicago Press: 1973); Israel M. Kirzner, "Entrepreneurial Discovery and the Competitive Market Process: An Austrian Approach," *Journal of Economic Literature*, Vol. 35, No. 1 (1997); Randall Holcombe, *Entrepreneurship and Economic Progress* (Routledge: 2006); William J. Baumol, *The Microtheory of Innovative Entrepreneurship* (Princeton University Press: 2010).

[3] See, e.g., Joseph Schumpeter, *Capitalism, Socialism, and Democracy* (1942), pp. 81-86 http://digamo.free.fr/capisoc.pdf; W. Michael Cox and Richard Alm, "Creative Destruction," *Concise Encyclopedia of Economics* (Liberty Fund: 2007) http://www.econlib.org/library/Enc/CreativeDestruction.html; Henry G. Manne, "The Entrepreneur in the Large Corporation," in *The Collected Works of Henry G. Manne*, Vol. 2 (Liberty Fund: 1996).

[4] Frank H. Knight, *Risk, Uncertainty, and Profit* (1921) http://www.econlib.org/library/Knight/knRUP.html.

creation in the economy.[5] Entrepreneurs innovate, providing consumers with new or better products. They provide other businesses with innovative, lower cost production methods and are, therefore, one of the key factors in productivity improvement and real income growth.[6] In terms of the neo-classical growth model, entrepreneurship is an important factor affecting the rate of technological change and the marginal productivity of capital.[7] The vast majority of economic gains from innovation and entrepreneurship accrue to the public at large, rather than entrepreneurs.[8] Entrepreneurs are central to the dynamism, creativity and flexibility that enables market economies to consistently grow, adapt successfully to changing circumstances and create sustained prosperity.[9]

Entrepreneurship is in Decline

Entrepreneurship is in decline. Business exits now exceed new business formations.[10] The share of firms aged 16 years or more has increase by 50 percent over the last two decades.[11] High-Tech companies are shedding more jobs than they are creating.[12]

[5] Magnus Henrekson and Dan Johansson, "Gazelles as Job Creators: A Survey and Interpretation of the Evidence," *Small Business Economics*, Vol. 35 (2010), pp. 227–244 http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1092938; Ryan Decker, John Haltiwanger, Ron Jarmin, and Javier Miranda, "The Role of Entrepreneurship in US Job Creation and Economic Dynamism," *Journal of Economic Perspectives*, Vol. 28, No. 3 (Summer 2014), pp. 3–24 http://pubs.aeaweb.org/doi/pdfplus/10.1257/jep.28.3.3; Salim Furth, "Research Review: Who Creates Jobs? Start-up Firms and New Businesses," Heritage Foundation Issue Brief #3891, April 4, 2013 http://www.heritage.org/research/reports/2013/04/who-creates-jobs-startup-firms-and-new-businesses.

[6] Ralph Landau, "Technology and Capital Formation," in *Technology and Capital Formation*, Dale W. Jorgenson and Ralph Landau, editors (MIT Press, 1989).

[7] See, e.g., Robert M. Solow, *Growth Theory: An Exposition* (Oxford, 2000). Legal institutions, human capital and other factors are also important determinants of economic growth. See N. Gregory Mankiw, David Romer and David N. Weil, "A Contribution to the Empirics of Economic Growth," *The Quarterly Journal of Economics*, Vol. 107, No. 2 (May, 1992), pp. 407-437 http://www.fordham.edu/economics/mcleod/mankiw-romer-weil-a-contribution.pdf; Robert J. Barro, *Economic Growth* (MIT Press: 2nd edition, 2003).

[8] Yale economist William Nordhaus has estimated that 98 percent of the economic gains from innovation and entrepreneurship are received by persons other than the innovator. See William D. Nordhaus, "Schumpeterian Profits in the American Economy: Theory and Measurement," Cowles Foundation Discussion Paper No. 1457, April 2004 https://cowles.econ.yale.edu/P/cd/d14b/d1457.pdf. Even if he is wrong by a factor of ten, this would still mean that 80 percent of the gains from entrepreneurship go to the public rather than the entrepreneur.

[9] See, Decker *et al*, *supra*; C. Mirjam van Praag and Peter H. Versloot, "What is the Value of Entrepreneurship? A Review of Recent Research," *Small Business Economics*, Volume 29, Issue 4 (December 2007) , pp 351-382 http://link.springer.com/article/10.1007%2Fs11187-007-9074-x; G. R. Steele, "Laissez-faire and the Institutions of the Free Market," *Economic Affairs*, September 1999 http://www.lancaster.ac.uk/staff/ecagrs/Laissez%20faire.pdf.

[10] Ian Hathaway and Robert Litan. "Declining Business Dynamism in the United States: A Look at States and Metros," Brookings Institution, May 2014 http://www.brookings.edu/~/media/research/files/papers/2014/05/declining%20business%20dynamism%20litan/declining_business_dynamism_hathaway_litan.pdf.

[11] Ian Hathaway and Robert Litan, "The Other Aging of America: The Increasing Dominance of Older Firms," Brookings Institution, July 2014 http://www.brookings.edu/~/media/research/files/papers/2014/07/aging%20america%20increasing%20dominance%20older%20firms%20litan/other_aging_america_dominance_older_firms_hathaway_litan.pdf; see also Decker *et al*, supra.

Although recovering with the substantial recovery in equity market values over the past several years and the regulatory improvements in the 2012 JOBS Act "IPO On-Ramp" provisions,"[13] Initial Public Offerings (IPOS) remain substantially below the previous two decades.[14] Although there is improvement since the depths of the recession, small and start-up businesses continue to struggle.[15] The decline in entrepreneurship is one of the key factors causing anemic U.S. economic performance.

Causes of the Decline in Entrepreneurial Activity

There are multiple reasons for the decline in entrepreneurial activity.[16] Reasons for the decline include poor tax policies that raise the cost of capital and impose high taxes on risk-taking,[17] a monstrously complex tax system that imposes inordinately high compliance costs on small and start-up firms,[18] inadequate access to capital,[19] a health

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[12] John Haltiwanger, Ian Hathaway and Javier Miranda, "Declining Business Dynamism in the U.S. High-Technology Sector," Kauffman Foundation, February 2014 http://www.kauffman.org/~/media/kauffman_org/research%20reports%20and%20covers/2014/02/declining_business_dynamism_in_us_high_tech_sector.pdf.

[13] Title I, The Jumpstart Our Business Startups Act, Public Law 112–106, April 5, 2012 http://www.gpo.gov/fdsys/pkg/PLAW-112publ106/pdf/PLAW-112publ106.pdf.

[14] David R. Burton, "Reducing the Burden on Small Public Companies Would Promote Innovation, Job Creation, and Economic Growth," Heritage Foundation Backgrounder No. 2924, June 20, 2014 http://www.heritage.org/research/reports/2014/06/reducing-the-burden-on-small-public-companies-would-promote-innovation-job-creation-and-economic-growth.

[15] Wendy Guillies, "Kauffman Foundation 2015 State of Entrepreneurship Address," February 11, 2015 http://www.kauffman.org/~/media/kauffman_org/resources/2015/soe/2015_state_of_entrepreneurship_speech.pdf; John Dearie and Courtney Geduldig, *Where the Jobs Are: Entrepreneurship and the Soul of the American Economy* (Wiley: 2013); William C. Dunkelberg and Holly Wade, "NFIB Small Business Economic Trends," August 2014 http://www.nfib.com/Portals/0/PDF/sbet/sbet201408.pdf.

[16] For an international survey of regulatory impediments to entrepreneurship and a literature survey, see *Doing Business 2014: Understanding Regulations for Small and Medium-Size Enterprises* (World Bank: 2013) http://www.doingbusiness.org/~/media/GIAWB/Doing%20Business/Documents/Annual-Reports/English/DB14-Full-Report.pdf.

[17] See, e.g., J.D. Foster, "The Simple Economics of Pro-Growth Tax Reform," Heritage Foundation Backgrounder #2816, June 19, 2013 http://www.heritage.org/research/reports/2013/06/the-simple-economics-of-pro-growth-tax-reform; Christopher J. Conover, "Congress Should Account for the Excess Burden of Taxation," Cato Institute Policy Analysis No. 669, October 13, 2010 http://object.cato.org/sites/cato.org/files/pubs/pdf/PA669.pdf; Robert Carroll, "The Excess Burden of Taxes and the Economic Cost of High Tax Rates," Washington, Tax Foundation, Special Report No. 170, August 2009, http://www.taxfoundation.org/files/sr170.pdf; William M. Gentry, "Capital Gains Taxation and Entrepreneurship," American Council for Capital Formation, November, 2010 http://accf.org/capital-gains-taxation-and-entrepreneurship/; Patrick Fleenor and J.D. Foster, "An Analysis of the Disincentive Effects of the Estate Tax on Entrepreneurship," Tax Foundation Background Paper #9, June 1, 1994 http://taxfoundation.org/sites/taxfoundation.org/files/docs/bp9.pdf.

[18] See, e.g., Jason J. Fichtner and Jacob M. Feldman, "The Hidden Costs of Tax Compliance," Mercatus Center, George Mason University, May 20, 2013 http://mercatus.org/sites/default/files/Fichtner_TaxCompliance_v3.pdf; Nicole V. Crain and W. Mark Crain, "The Impact of Regulatory Costs on Small Firms," U.S. Small Business Administration, Office of Advocacy, September 2010, Table 4, p. 29 http://www.sba.gov/sites/default/files/The%20Impact%20of%20Regulatory%20Costs%20on%20Small%20Firms%20(Full)_0.pdf; J. Scott Moody, Wendy P. Warcholik and Scott A. Hodge, "The Rising Cost of Complying with the Federal Income Tax," Special Report No. 138, December 2005

care system that is the most complex and costly in the world,[20] a legal system that is the most costly in the world,[21] high and growing regulatory costs,[22] labor and employment laws that raise the cost and risk of employing people,[23] environmental and energy regulations that raise the cost of energy and limit development of energy resources,[24] and an immigration system that makes it difficult for firms to gain access to talented foreign

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http://taxfoundation.org/sites/default/files/docs/sr138.pdf; Dan R. Mastromarco and David R. Burton, "The Internal Revenue Code: Unequal Treatment Between Large and Small Firms," November, 2001 http://www.nsba.biz/docs/nsba_tax_equity_report.pdf.

[19] See SEC Commissioner Daniel M. Gallagher, "Whatever Happened to Promoting Small Business Capital Formation?," September 17, 2014 http://www.sec.gov/News/Speech/Detail/Speech/1370542976550#.VFfbl8mGklQ or http://www.heritage.org/events/2014/09/commissioner-gallagher; Stuart R. Cohn and Gregory C. Yadley, "Capital Offense: The SEC's Continuing Failure to Address Small Business Financing Concerns," *New York University Journal of Law and Business*, Vol. 4, No. 1, pp. 1-87 (2007) http://scholarship.law.ufl.edu/cgi/viewcontent.cgi?article=1257&context=facultypub; "2013 State of Entrepreneurship Address: 'Financing Entrepreneurial Growth'," Kauffman Foundation Research Paper, February 5, 2013 http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2212743; *The Oxford Handbook of Venture Capital*, Douglas Cumming, Editor (Oxford: 2012); Sampsa Samila and Olav Sorenson, "Venture Capital, Entrepreneurship, and Economic Growth, *Review of Economics and Statistics*, February, 2011, Vol. 93, No. 1, pp. 338-349 http://martinprosperity.org/media/agrawal/3SorensonSamila.pdf; Dane Stangler, "High-Growth Firms and the Future of the American Economy, Kauffman Foundation, March 9, 2010 http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1568246; David R. Burton, "Proposals to Enhance Capital Formation for Small and Emerging Growth Companies," Testimony before the Capital Markets and Government Sponsored Enterprises Subcommittee of the Committee on Financial Services, United States House of Representatives, April 11, 2014 http://www.heritage.org/research/testimony/2014/04/capital-formation-for-small-and-emerging-growth-companies .

[20] *Health at a Glance 2013: OECD Indicators*, Organization for Economic Co-operation and Development, 2013, Table 7.2.1. Health expenditure as a share of GDP, 2011, p. 157, (17.7 percent of GDP in the U.S. compared to the next most expensive, the Netherlands, at 11.9 percent of GDP and the OECD average of 9.3 percent of GDP) http://www.oecd.org/els/health-systems/Health-at-a-Glance-2013.pdf.

[21] See, e.g., David L. McKnight and Paul J. Hinton, "International Comparisons of Litigation Costs: Europe, the United States and Canada," May 2013, U.S. Chamber Institute for Legal Reform by NERA Economic Consulting Figure 1: 2011 Liability Costs as a Fraction of GDP, p. 1 (liability costs of 1.66 percent of GDP compared to the next most expensive, Canada, at 1.19 percent and the Eurozone average of 0.63 percent) http://www.instituteforlegalreform.com/uploads/sites/1/NERA_FULL.pdf.

[22] See, e.g., James L. Gattuso and Diane Katz, "Red tape rising: Five years of regulatory expansion," Heritage Foundation Backgrounder #2895, March 26, 2014 http://www.heritage.org/research/reports/2014/03/red-tape-rising-five-years-of-regulatory-expansion; Wayne Crews, "Ten Thousand Commandments: An Annual Snapshot of the Federal Regulatory State," Competitive Enterprise Institute, April 29, 2014 http://cei.org/10KC; Nicole V. Crain and W. Mark Crain, The Impact of Regulatory Costs on Small Firms, Small Business Administration Office of Advocacy, September 2010, http://www.sba.gov/sites/default/files/The%20Impact%20of%20Regulatory%20Costs%20on%20Small%20Firms%20%28Full%29_0.pdf; John W. Dawson and John J. Seater, "Federal Regulation and Aggregate Economic Growth," *Journal of Economic Growth*, Volume 18, (June 2013), pp 137-177 http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2223315&download=yes.

[23] See, e.g., The Impact of State Employment Policies on Job Growth: A 50-State Review, The U.S. Chamber of Commerce, 2011 https://www.uschamber.com/sites/default/files/legacy/reports/201103WFI_StateBook.pdf; Gattuso and Katz, *op. cit.*

[24] Gattuso and Katz, *op. cit.*; Crews, *op. cit.*

workers and for immigrant-entrepreneurs to enter the United States to start a business.[25]

Helping to Restore Prosperity by Removing Impediments to Entrepreneurship

The key to reversing the decline in entrepreneurship is to systematically reduce the legal impediments to entrepreneurship. There is not any one policy change – or even a few – that will lead to a sudden renaissance in entrepreneurship. Since the decline is caused by the combined weight of many poor public policies, the solution requires systematically improving public policy in a wide variety of areas.

The remainder of this testimony sets forth 97 recommendations that would, if adopted, transform the American economy and lead to a resurgence in entrepreneurial activity, strong economic growth, higher real wages and renewed prosperity. The recommendations relate to tax policy, securities regulation and capital access, health care, energy and environmental regulation, administrative law and regulation, employment and labor law, immigration and the legal system.

POOR TAX POLICY

The tax system imposes very high compliance costs that disproportionately harm small firms. Moreover, the tax system dramatically impedes capital formation and economic growth.

Intermediate Term Objectives

1. **Expensing of Investment in Machinery and Equipment.** Amend Internal Revenue Code §179 to permanently allow annual capital expenses of up to $1 million to be deducted when incurred. Expensing would simplify small firms' tax returns, reduce compliance costs, reduce small firms' cost of capital and aid cash flow.[26]

2. **Retirement Account Simplification.** Very few small employers offer retirement accounts because of the complexity, high compliance costs and regulatory risk of doing so.[27] This makes it more difficult for them to attract employees and more difficult for both the small business owners and their employees to save for

[25] For a recent discussion of the literature, see Sari Pekkala Kerr, William R. Kerr and William F. Lincoln, "Firms and the Economics of Skilled Immigration," National Bureau of Economic Research Working Paper 20069, April 2014 http://www.nber.org/papers/w20069.
[26] David Burton, "Constructive Small Business Expensing Bill Introduced," *The Daily Signal*, April 11, 2014 http://dailysignal.com/2014/04/11/constructive-small-business-expensing-bill-introduced/; Curtis Dubay, "Ways and Means Committee Following Right Approach on Tax Extenders," *The Daily Signal*, May 27, 2014 http://dailysignal.com/2014/05/27/ways-means-committee-following-right-approach-tax-extenders/.
[27] Kathryn Kobe, "Small Business Retirement Plan Availability and Worker Participation," Small Business Administration, Office of Advocacy, March 2010, Table 2 (only 28 percent of firms with under 100 employees offered some kind of retirement plan in 2006) https://www.sba.gov/sites/default/files/rs361tot.pdf.

retirement. This is one of the most complex areas of the tax law and desperately in need of simplification.[28]

One possible solution would be to amend the Internal Revenue Code to create a Small Business Uniform Retirement Account as a voluntary alternative for employers with 500 or fewer employees to replace: (1) simplified employee pensions (SEPs), (2) salary reduction simplified employee pensions, (3) SIMPLE IRA plans, (4) SIMPLE 401(k) plans, (5) Keogh plans, (6) regular 401(k)s (with respect to employers with 500 or fewer employees), (7) profit-sharing plans (with respect to employers with 500 or fewer employees), (8) money purchase pension plan (with respect to employers with 500 or fewer employees), and (9) employee stock ownership plans (with respect to employers with 500 or fewer employees). The Small Business Uniform Retirement Account would (1) have check the box eligibility, (2) uniform employee eligibility, (3) automatic enrollment of employees with an option to opt-out, (4) no non-discrimination, coverage or key employee rules, (5) allow contribution levels to be chosen by the employee, (6) be maintained through a financial institution and (7) be available to employees and self-employed persons (including partners and LLC members).

3. **Reduce the Top Long-term Capital Gains Tax Rate to 20 percent.** Evidence shows that a capital gains rate much above 20 percent actually reduces federal revenues. In addition, a high capital gains tax rate reduces the willingness of investors to invest in relatively risky start-up and growth companies and impedes capital formation. The top long-term capital gains tax rate should not exceed 20 percent (including the Obamacare investment income tax).[29]

4. **Permit Cash Method Accounting for Firms with up to $10 million in Gross Receipts.** Cash method accounting is simpler and aids cash flow.[30]

5. **S Corporation Liberalization.** Permit S corporations to have more than one class of stock, non-resident alien shareholders (subject to 30 percent withholding on dividends) and more than 100 shareholders. The latter is particularly important if S corporations are going to have practical access to the crowdfunding or Regulation A+ provisions in the JOBS Act which will allow companies to raise small amounts from a large number of investors using the internet once the SEC

[28] See generally, David C. John, "Pursuing Universal Retirement Security Through Automatic IRAs and Account Simplification," Testimony before The Committee on Ways and Means, United States House of Representatives, April 17, 2012 http://www.heritage.org/research/testimony/2012/04/pursuing-universal-retirement-security-through-automatic-iras-and-account-simplification.

[29] J.D. Foster, "Obama's Capital Gains Tax Hike Unlikely to Increase Revenues," Heritage Foundation Backgrounder #2391, March 24, 2010 http://www.heritage.org/research/reports/2010/03/obamas-capital-gains-tax-hike-unlikely-to-increase-revenues; Stephen J. Entin, 'President Obama's Capital Gains Tax Proposals: Bad for the Economy and the Budget," Tax Foundation January 21, 2015 http://taxfoundation.org/blog/president-obama-s-capital-gains-tax-proposals-bad-economy-and-budget.

[30] Then Ways and Means Committee Chairman Dave Camp proposed this in his Tax Reform Act of 2014 discussion draft. See section 3301 http://waysandmeans.house.gov/uploadedfiles/ways_and_means_section_by_section_summary_final_022614.pdf.

promulgates rules implementing the JOBS Act. It is preferably for the S corporation rules to emulate the partnership rules so there would be no shareholder limit but S corporation status would not be available to publicly traded corporations. See Internal Revenue Code §7704.

6. **Repeal the Obamacare Health Insurance Tax.** Obamacare imposes an excise tax on health insurance premiums that effectively is aimed at small businesses because larger firms self-insure (with or without stop-loss insurance) and therefore do not pay health insurance premiums. It is roughly equivalent to a 2.5 percent tax. This tax should be repealed.[31]

7. **Reduce Tax Rate of Pass-Through Entity income to the Corporate Tax Rate.** Reduce the tax rate paid on income from S corporations and other pass-through entities (e.g. LLCs) to no more than the top corporate tax rate (currently 35 percent).

8. **Increase the Incentive Stock Option (ISO) Cap Limitation from $100,000 to $250,000.** Internal Revenue Code section 422(d) limits incentive stock options to $100,000 in aggregate stock value (not gain). This limits the utility of ISOs as a means to attract talent.

9. **Full Deductibility for Health Insurance Purchased by the Self-Employed.** Currently, health insurance costs incurred by the self-employed (which includes partners and LLC members) are deductible for income tax purposes but not for purposes of the 15.3 percent self-employment tax. This creates a special tax burden on the self-employed not borne by anyone else in the economy. There should be parity for the self-employed with those who are employed. Internal Revenue Code §162(l)(4) should be repealed.

10. **Clarify Rules Governing to What Extent Distributions from Pass-Through Entities are Subject to Payroll Taxes.** This issue has existed since at least the 1980s and it has never been adequately resolved. It causes a lot of audits and a lot of uncertainty. Reasonable, clear and uniform rules governing "reasonable compensation" and investment income should be adopted for partnerships, S corporations and C corporations.

11. **Clarify Employee/Independent Contractor Rules.** This issue has existed since at least the 1970s and it has never been adequately resolved. It causes a lot of audits and a lot of uncertainty. This is of even greater importance given the employer mandate in Obamacare. Provisions should be adopted allowing the employer to choose in ambiguous cases, subject to 1099 reporting and moderate

[31] David R. Burton, "Obamacare's Health Insurance Tax Targets Consumers and Small Businesses," Heritage Foundation Issue Brief #4075, October 31, 2013. http://www.heritage.org/research/reports/2013/10/obamacare-s-health-insurance-tax-targets-consumers-and-small-businesses.

backup withholding, whether a payee is an employee or a contractor.[32]

12. **Estate and Gift Tax Reduction.** The unified credit should be increased so that $10 million is effectively excluded from the estate and gift tax. For 2015, the amount that is effectively excluded is $5.4 million. Family farms and businesses should not either have to be sold to pay estate taxes when parents die or incur huge life insurance premiums to provide the means of paying the tax.

Longer-Term Objectives

13. **Fundamental Tax Reform.** Fundamental tax reform would reduce compliance costs considerably and result in dramatically higher rates of capital formation, economic growth and job creation. The goal is a simple, flat rate, territorial consumption tax to replace the individual and corporate income tax and the estate and gift tax. Preferably, it would be border adjusted (i.e. destination principle) so it does not create an artificial tax incentive to produce goods and services outside of the United States. This can take one of four forms. (1) A Hall-Rabushka-Armey-Forbes flat tax, (2) A consumed income tax (also known as an expenditure tax, cash-flow tax, inflow-outflow tax or the new flat tax), (3) a national sales tax or (4) a Business Transfer Tax or BTT or, potentially, some combination of these.[33]

14. **Estate and Gift Tax Repeal.** Family farms and businesses should not have to be sold to pay estate taxes when parents die or incur huge life insurance premiums to provide the means of paying the tax. Repealing the estate and gift tax should be a part of fundamental tax reform.[34]

INADEQUATE ACCESS TO CAPITAL

Extraordinarily complex securities regulation and banking regulation impede the ability of small firms to raise the capital needed to start-up or grow.[35]

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[32] For general background see "Present Law and Background Relating to Worker Classification for Federal Tax Purposes," Joint Committee on Taxation, [JCX-26-07] May 8, 2007 http://www.jct.gov/x-26-07.pdf.

[33] David R. Burton, "Four Conservative Tax Plans with Equivalent Economic Results," Heritge Foundation Backgrounder #2978, December 15, 2014 http://www.heritage.org/research/reports/2014/12/four-conservative-tax-plans-with-equivalent-economic-results.

[34] William W. Beach, "Seven Reasons Why Congress Should Repeal, Not Fix, the Death Tax," Heritage Foundation Web Memo #2688, November 9, 2009 http://www.heritage.org/research/reports/2009/11/seven-reasons-why-congress-should-repeal-not-fix-the-death-tax; John L. Ligon, Rachel Greszler and Patrick Tyrrell, "The Economic and Fiscal Effects of Eliminating the Federal Death Tax," Heritage Foundation Backgrounder #2956, September 23, 2014 http://www.heritage.org/research/reports/2014/09/the-economic-and-fiscal-effects-of-eliminating-the-federal-death-tax.

[35] For a full discussion of items 15-48, see David R. Burton, "Steps to Improve Entrepreneurs' Access to Capital and Why It Matters," forthcoming, Heritage Foundation; see also David R. Burton, "Proposals to Enhance Capital Formation for Small and Emerging Growth Companies," Testimony before the Capital Markets and Government Sponsored Enterprises Subcommittee of the Committee on Financial Services, United States House of Representatives, April 11, 2014

Intermediate Term Objectives

Regulation A

15. **Preempt State Registration and Qualification Laws governing Regulation A Company Securities.** Either define NSMIA[36] covered securities to include securities sold in transactions exempt pursuant to Regulation A or define qualified purchasers to include all purchasers of securities in transactions exempt under Regulation A, or both. State blue sky laws have effectively destroyed the usefulness of Regulation A.[37]

16. **Simplify the Statutory Small Issues Exemption.** Specifically, amend Securities Act section 3(b)(1) so that "Tier I" Regulation A offerings have reasonable requirements for offering statements and periodic disclosure and provide that the provisions are self-effectuating without having to wait for the promulgation of SEC regulations.[38]

17. **Eliminate the Section 12(g)(1) Holders of Record Threshold for Regulation A Securities.** Currently the limit stands at 500 holders of record (for non-accredited investors). If this is not increased, even relatively small issuers will be unable to raise additional capital. The cap should not apply to small issuers using Regulation A who will raise small amounts from a large number of investors. Otherwise, many will bump up against the limit and be unable to raise any additional capital. Crowdfunding investors are currently exempt from section 12(g) for the same reasons.

18. **Prohibit Investor Limitations (as a Percentage of Income or Net Worth) under Regulation A.** This has been proposed by the SEC in its proposed rule implementing the JOBS Act. It has no statutory basis.

Regulation D

19. **Establish a Statutory Definition of Accredited Investor for Purposes of Regulation D Offerings.** It should (a) set the income and net worth requirements for natural persons at current levels and (b) establish specific bright line tests for sophistication.[39]

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http://www.heritage.org/research/testimony/2014/04/capital-formation-for-small-and-emerging-growth-companies ; Gallagher, *supra*.

[36] The National Securities Markets Improvement Act of 1996.

[37] Rutheford B Campbell, Jr., "Regulation A: Small Businesses' Search For 'A Moderate Capital'" Vol. 31, No. 1, *Delaware Journal of Corporate Law* (2006), pp. 77-123 http://uknowledge.uky.edu/law_facpub/126/.

[38] David R. Burton, "Regulation A+ Proposed Rule Needs Work," Daily Signal, April 08, 2014 http://dailysignal.com/2014/04/08/regulation-plus-proposed-rule-needs-work/.

[39] David R. Burton, "Don't Crush the Ability of Entrepreneurs and Small Businesses to Raise Capital," Heritage Foundation Backgrounder No. 2874, February 5, 2014,

20. **Preempt State Registration and Qualification Laws Governing Rule 505 Securities.** Either define NSMIA covered securities to include securities sold in transactions exempt under Rule 505 (in addition to Rule 506) or define qualified purchasers to include all purchasers of securities in transactions exempt under Rule 505 (in addition to Rule 506), or both.[40]

21. **Define Reasonable Steps to Verify for Purposes of Rule 506(c) Offerings as including Self-Certification under Penalty of Perjury.** The SEC rule promulgated to implement Title II of the JOBS Act went too far, requiring companies to obtain sensitive private tax return and financial information from investors.[41]

22. **Prevent the Promulgation of the Regulation D Amendments Proposed in July 2013.** These proposed rules would require issuers to file three Form Ds instead of one and meet many additional requirements. The proposed rule undermines the laudable aims of the JOBS Act.[42]

Crowdfunding[43]

23. **Eliminate the Audit Requirements for Crowdfunding Offerings over $500,000 required by Securities Act Section 4A(b)(1)(D)(iii).** Such requirements are not imposed on much larger Regulation D or Regulation A offerings.

24. **Permit Funding Portals to be Compensated Based on the Amount Raised by the Issuer.**

25. **Make it Clear that Funding Portals are not Issuers and not Subject to the**

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http://www.heritage.org/research/reports/2014/02/dont-crush-the-ability-of-entrepreneurs-and-small-businesses-to-raise-capital.

[40] Rutheford B Campbell, Jr., "The Wreck of Regulation D: The Unintended (And Bad) Outcomes for the SEC's Crown Jewel Exemptions, 66 *Business Lawyer* 919, August, 2011 http://moritzlaw.osu.edu/students/groups/oseblj/files/2013/01/7-Campbell.pdf.

[41] David R. Burton, Comments on Proposed Rule "Eliminating the Prohibition Against General Solicitation and General Advertising in Rule 506 and Rule 144A Offerings," http://www.sec.gov/comments/s7-07-12/s70712-118.pdf.

[42] David R. Burton, "Regulation D Rule Would Harm Entrepreneurs and Economic Growth," *Daily Signal*, November 13, 2013 http://dailysignal.com/2013/11/13/regulation-d-rule-would-harm-entrepreneurs-and-economic-growth/.

[43] For a discussion of the problems with the proposed crowdfunding rules and Title III of the JOBS Act, see comment letter of David R. Burton regarding crowdfunding, February 3, 2014 http://www.sec.gov/comments/s7-09-13/s70913-192.pdf and comment letter of Rutheford B Campbell, Jr., regarding crowdfunding, February 14, 2014 http://www.sec.gov/comments/s7-09-13/s70913-278.pdf. See also, *Crowdfunding: A Guide to Raising Capital on the Internet*, Steven Dresner, Editor (Wiley: 2014) and David R. Burton, "Steps to Improve Entrepreneurs' Access to Capital and Why It Matters," forthcoming, Heritage Foundation.

Issuer Liability Provisions. The SEC has adopted an interpretation of the JOBS Act in its proposed rule that would make funding portals, in effect, insure investors against issuer fraud.

26. **Repeal the Restriction on Providing Investment Advice Entirely or, Alternatively, Explicitly Permit "Impersonal Investment Advice."** Make it clear that a portal may bar an issuer from its platform if the portal deems an offering to be of inadequate quality without fear of liability to issuers or investors and that this would not constitute providing prohibited investment advice.

27. **Reduce the Administrative and Compliance Burden on Funding Portals.**

28. **Allow Intermediaries to Rely on Good Faith Efforts by Third Party Certifiers.** Allow intermediaries to rely on good faith efforts by third party certifiers for purposes of complying with the investment limitation in Securities Act section (4)(a)(6)(B).

29. **Reduce the Mandatory Disclosure Requirements on Crowdfunding Issuers.** There are 21 specific disclosure requirements ((a) through (v)) most of which have multipart requirements. Issuers using the crowdfunding exemption will be among the smallest companies, unable to cost effectively comply with these requirements, many of which have no statutory basis.

30. **Amend the Bank Secrecy Act to Make it Clear that Federal "Know Your Customer" do not Apply to Finders, Business Brokers or Crowdfunding Web Portals that do not Hold Customer Funds**. This provision, including the proposed rule, would impose huge costs on funding portals that are likely to make them uneconomic.

31. **As an alternative to items 23 through 29, Congress May do Better by Simply Starting Over and Replacing the Existing Title III with a More Reasonable Statute.**

Creating Strong Secondary Markets

32. **Create the Regulatory Framework for Venture Exchanges.** Amend section 18(b) of the Securities Act to treat all securities as covered securities that (1) are traded on established securities markets, (2) are not penny stocks and (3) have continuing reporting obligations as (a) a registered company, (b) pursuant to Regulation A or (c) pursuant to Regulation Crowdfunding. An established securities market should be defined to include those on electronic markets such as OTC Markets, FINRA's OTCBB or a SEC designated alternative trading system (ATS).

33. **Allow Companies to Transparently Pay Market Makers to Initiate and Maintain Quotations in Securities.**

Reducing Regulatory Burdens on Small Public Companies

34. **Increase the Smaller Reporting Company Threshold to $300 Million and Conform the Accelerated Filer Definition.**

35. **Make all Emerging Growth Company Advantages Permanent for Smaller Reporting Companies.**

36. **Improve the Disclosure Requirements under Regulation S-K for Smaller Reporting Companies.**[44]

Improve Access to Borrowing

37. **Repeal the Restrictions on Credit Union Lending to Small Businesses.** Section 107A of the Federal Credit Union Act[45] imposes a limit on credit union business lending (which is almost exclusively small business lending). The limit is equal to 1.75 times the section 216 net worth requirement of 7 percent. Thus, no more than 12 ¼ percent of loans can be to small businesses. This arbitrary limit should be repealed.

38. **Permit Peer-to-Peer Lending Portals to Provide Loans to Small Businesses without Filing a Registration Statement.**

39. **Amend Securities Act Section 4A(b) (JOBS Act Title III) to Provide that Companies Issuing Crowdfunding Debt Securities are not Subject to Reporting Obligations that are Inappropriate for Debt Securities.**

40. **Require a GAO Study of Bank Regulations and Bank Regulator Practices that may have a Disproportionate Adverse Impact on Small Business Lending.**

Improving the Administration of the Securities Laws

41. **Improve SEC Collection and Publication of Data on the Regulation of and Regulatory Costs Incurred by Small Public Companies.** Improve SEC collection and publication of data on private placements and Regulation A offerings, including the regulation of, and regulatory costs incurred by, issuers, the amount of capital raised and the nature of the investors.

42. **Improve SEC Collection and Publication of Data Regarding Enforcement Actions.** Improve SEC collection and publication of data regarding enforcement

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[44] David R. Burton, "Reducing the Burden on Small Public Companies Would Promote Innovation, Job Creation, and Economic Growth," Heritage Foundation Backgrounder No. 2924, June 20, 2014 http://www.heritage.org/research/reports/2014/06/reducing-the-burden-on-small-public-companies-would-promote-innovation-job-creation-and-economic-growth.

[45] 12 USC 1757a.

actions taken with respect to private, Regulation A and small public company offerings, disclosure obligations and secondary market activity.

Other Improvements

43. **Amend the Securities Act to Create a Statutory "Micro Offering" Safe Harbor.** This safe harbor would provide that any offering is deemed not to involve a public offering for purposes of Securities Act section 4(a)(2) if the offering (1) is made only to people with whom an issuer's officers, directors or 10 percent or more shareholders have a substantial pre-existing relationship; (2) involves 35 or fewer purchasers; or (3) has an aggregate offering price of less than $500,000 (within a 12 month period).

44. **Create a Statutory Exemption to the Broker-Dealer Registration Requirements for Finders.** The exemption would provide that those who are not "engaged in the business of effecting transactions in securities for the account of others" or of "buying and selling securities" are exempt and, as an integral component of that exemption, provide a bright-line safe harbor such that small finders are not deemed to be engaged in the business of being a securities broker or a dealer.

45. **Create a Statutory Exemption for Business Brokers to the Broker-Dealer Registration Requirements.** The House has passed legislation accomplishing this result, although an exemption approach would be preferable to the registration approach adopted in this legislation.[46]

46. **Amend the Investment Advisers Act of 1940 to include Advisers of Small Business Investment Companies (SBICs) in the Class of Venture Capital Funds and Private Funds that are Exempt from SEC Registration.**

47. **Increase the SEC Rule 701 Threshold to $20 Million.**

Longer-Term Objectives

48. **Rationalize and Integrate the Various Private Market Exemptions.** Return to the basic principles of securities regulation, namely preventing fraud and misrepresentation and requiring the disclosure of material facts relevant to investment decisions. Oppose merit review where federal or state regulators substitute their investment judgment for that of the investing public. Eliminate extraneous reporting and regulation that is not directed at preventing fraud or the disclosure of material facts relevant to investment decisions. Provide for scaled disclosure so that disclosure requirements for smaller firms are less burdensome. Replace the patchwork quilt of exemptions, with various and sometimes conflicting requirements. Replace it with a coherent, rational system of

[46] David R. Burton, "Don't Overregulate Business Brokers," Heritage Foundation *Backgrounder* No. 2883, February 19, 2014, http://www.heritage.org/research/reports/2014/02/dont-overregulate-business-brokers.

exemptions and reasonable scaled disclosure that considers the cost of compliance, the investor protection benefits of the added disclosure, the cost to investors of being denied investment opportunities by investment restrictions and the cost to the public of lost economic growth, capital formation, innovation and job creation caused by over-regulation.[47]

EXPENSIVE HEALTH CARE

Health care costs are much too high and represent a substantial drag on economic growth and the ability of employers to provide improved cash compensation to their employees. Policies should be adopted to promote health care cost containment by creating a consumer driven system that preserves choice and provides incentives to economize.

Intermediate Term Objectives

49. **Amend the Definition of "Excepted Benefits" In HIPPA, ERISA and the Tax Code to Unambiguously Exempt from Federal Regulation All Indemnity Health Insurance Policies and All Stop Loss and Reinsurance Policies for Health Care Risks.** An indemnity insurance policy pays the policyholder for a claim and then it is up to the policyholder to decide how the money is spent. Most health care indemnity insurance policies are considered "excepted benefits" under HIPAA. There has recently been renewed interest in such policies both as an alternative to Obamacare and as a way to make consumers more cost and value conscious when purchasing medical care. Last year, HHS issued regulations adding the stipulation that indemnity policies sold in the individual market only qualify as excepted benefits if the applicant attests in his coverage application that he has other, Obamacare compliant coverage.[48] However, Congress did not grant HHS the authority to impose restrictions beyond those specified in the statute. Congress should amend the law to unambiguously exempt all indemnity health policies from federal regulation.

    Employers that self-insure their health plans typically purchase "stop-loss" and "reinsurance" policies to limit their potential losses. Nowhere in federal law is there explicit authorization for the federal government to regulate such policies as "health risks." However, there are indications that the Obama Administration is looking for ways to do just that. Thus, the definition of excepted benefits should also be amended to clearly prevent such an expansion of federal regulatory authority. Doing so is particularly important to small businesses, as self-insurance will become an increasingly attractive option for small employers seeking to escape Obamacare's costly requirements, but the feasibility of small employers self-insuring is dependent on their ability to purchase appropriate stop-loss and reinsurance coverage.

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[47] David R. Burton, "Steps to Improve Entrepreneurs' Access to Capital and Why It Matters," forthcoming, Heritage Foundation.
[48] 45 CFR §148.220(b)(3).

50. **Exempt Health Insurers from the Requirement to Include Obamacare's Package of Mandated "Essential Benefits" in Policies Sold in the Small-Group Market and in the Non-Group Market Outside of the Exchanges.** Obamacare's costly "essential benefits" package of mandated minimum benefits is imposed on all individual and small-group policies, but not on large-group policies, nor on self-insured plans (regardless of employer size). If large and self-insured employers are exempt from this costly burden, then small employers who buy group plans from commercial insurers should also be exempt. Furthermore, a business owner cannot participate in an employer-group health plan unless he is an employee of the business. Thus, many owners of small businesses must buy their own coverage on the individual market, even if they offer an employer-sponsored group plan to their workers. Given that coverage sold on the exchanges comes with government subsidies, for the government to impose benefit requirements on such coverage may be fiscally unwise, but is at least logically justified. However, there is no justification for imposing such discriminatory and costly requirements on *unsubsidized* coverage sold in the individual market *outside* the exchanges, particularly when those purchasing such coverage are principally small business owners and other self-employed individuals.

51. **Exempt Employers with 100 or Fewer Full-Time Workers from the Employer Mandate.** Raising the firm size threshold for Obamacare's employer mandate from 50 to 100 full-time workers would greatly reduce the prospect of employers trying to manipulate employee head-count and hours worked so as to avoid triggering the employer mandate. Furthermore, by the time that a small business has grown to employ 100 workers it is better able to feasibly adopt other strategies — most notably self-insurance — for managing its employee health benefits costs. Such a change would also reduce the issues surrounding the definition of "full-time" (e.g., 30 versus 40 hours per week) and the counting of part-time hours in calculating firm size on a FTE basis. Finally, such a change would remove one of Obamacare's largest impediments to job creation.

52. **Liberalize Health Savings Accounts (HSAs) and Flexible Spending Arrangements (FSAs).** Allow individuals and their employers to contribute greater amounts to HSAs and FSAs.[49]

Longer-Term Objectives

53. **Repeal Obamacare.**[50]

54. **Adopt Patient-Centered Health Care Tax Reforms.** Replace the tax exclusion

[49] Alyene Senger, "HSAs Could Bring Health Costs Down; Too Bad Obamacare Destroys Them," *Daily Signal*, May 18, 2012 http://dailysignal.com/2012/05/18/hsas-could-bring-health-costs-down-too-bad-obamacare-destroys-them/.

[50] Edmund F. Haislmaier, "Should Obamacare be Repealed, Replaced or Left Alone?," December 11, 2014 http://www.heritage.org/research/commentary/2014/12/should-obamacare-be-repealed-replaced-or-left-alone.

for employer-sponsored coverage, the deduction for self-employed coverage and other current health care tax provisions with a new individual tax benefit for health care coverage available to individuals regardless of their employment situations.[51]

BURDENSOME ENERGY AND ENVIRONMENT LAWS

Energy and environmental regulations exceed reasonable levels and do more to impede job creation and economic growth than to protect public health.[52]

Intermediate Term Objectives

55. **Require Timely Environmental Review.** The environmental review requirements for projects on federal lands under NEPA take entirely too long. Congress should place a 270-day time limit on National Environmental Policy Act (NEPA) reviews, ensuring a quick, efficient review process for energy projects on federal lands.[53]

56. **Prohibit Implementation of the "WOTUS" Rule and Clearly Define Federal Jurisdiction under the Clean Water Act.** Congress should immediately prohibit the implementation of the proposed EPA and Army Corps of Engineers "waters of the U.S." rule. Congress should also define what waters are covered under the CWA to provide clarity and to prevent EPA and Corps overreach. The definition should generally limit federal authority to regulating traditional "navigable waters."[54]

57. **Prohibit the EPA from Revoking a Validly Issued CWA permit.** Under Section 404 of the Clean Water Act (CWA), a permit is required before dredged or fill material is discharged into covered waters. The EPA claims it can revoke one of these permits at any time, even after it has been lawfully issued by the Army Corps of Engineers, meaning there is no such thing as a final permit.

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[51] See, Edmund F. Haislmaier, Robert E. Moffit, Nina Owcharenko, and Alyene Senger, "A Fresh Start for Health Care Reform," Heritage Foundation Backgrounder No. 2970, October 30, 2014, http://www.heritage.org/research/reports/2014/10/a-fresh-start-for-health-care-reform?ac=1.

[52] For a general discussion of environmental and energy issues, see *Solutions 2014: Environment*, The Heritage Foundation http://solutions.heritage.org/environment/; Romina Boccia, Jack Spencer and Robert Gordon, "Environmental Conservation Based on Individual Liberty and Economic Freedom," Heritage Foundation Backgrounder #2758, January 14, 2013 http://www.heritage.org/research/reports/2013/01/environmental-conservation-based-on-individual-liberty-and-economic-freedom.

[53] See *Solution, 2014, Environment, op. cit.*

[54] Daren Bakst and Rachael Slobodien , "The EPA and the Corps's CWA Interpretive Rule: A Regulatory End Run," Heritage Foundation Issue Brief #4296, November 18, 2014 http://www.heritage.org/research/reports/2014/11/the-epa-and-the-corpss-cwa-interpretive-rule-a-regulatory-end-run ;
Ron Arnold, "Proposed Water Rule Could Put 'Property Rights of Every American Entirely at the Mercy' of EPA," *Daily Signal*, November 12, 2014 http://dailysignal.com/2014/11/12/proposed-water-rule-put-property-rights-every-american-entirely-mercy-epa/.

58. **Change the Process for Developing the National Ambient Air Quality Standards (NAAQS).** The EPA sets NAAQS for six principal pollutants that must be reviewed every five years, and must disregard costs in setting the standards. Even when existing standards are not close to being fully implemented, more stringent standards are proposed. Congress should repeal the current five-year review process and make any decisions to change standards itself. The EPA should not be making unilateral decisions that can have such a devastating impact on the economy, employment and the well-being of Americans. In making decisions regarding the standards, Congress should consider the impact of stricter standards and the incredible success that has already been achieved in air quality.

59. **Stop Agency Accounting of Social Cost of Carbon (SCC).** The SCC inflates the alleged benefits of proposed energy-efficiency regulations by adding the supposed monetary benefits of the regulations' reduced CO_2 emissions. This prevents the economic development of energy and infrastructure projects.[55]

60. **Repeal or Revise MACT Regulations.** In February 2012, the EPA finalized new mercury and air toxics standards that would force utilities to use maximum achievable control technology (MACT) standards to reduce mercury emissions and other hazardous air pollutants (HAPs). More commonly known as the Utility MACT regulation, the EPA began the process to regulate mercury emissions in 1998, but during its evaluation, it did not find demonstrable direct health benefits from regulating other HAPs. The EPA estimates this rule could cost more than $10 billion per year by 2015, but the Electric Reliability Coordinating Council estimates it could cost as much as $100 billion per year. The EPA claims this rule would produce $53 billion to $140 billion in annual benefits, but the mercury reductions would produce at most $6 million in benefits. Utility MACT will raise electricity costs substantially and directly result in the shutdown of many smaller coal-fired electric utilities and the compliance deadline is April 2015.[56]

61. **Prohibit EPA Greenhouse Gas Regulations (GHG).** Along with a host of other regulations, the EPA now regulates GHG emissions (most notably carbon dioxide) for newly constructed power plants and is expected to do so for existing power plants. This rule would effectively eliminate the construction of new coal-fired power plants and raise the cost of electricity. Congress should permanently prohibit any federal regulators from using GHG emissions as a reason to regulate economic activity.

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[55] Kevin D. Dayaratna, Nicolas Loris and David W. Kreutzer, "The Obama Administration's Climate Agenda: Underestimated Costs and Exaggerated Benefits," Heritage Foundation Backgrounder #2975 November 13, 2014 http://www.heritage.org/research/reports/2014/11/the-obama-administrations-climate-agenda-underestimated-costs-and-exaggerated-benefits.

[56] David W. Kreutzer, Nicolas Loris and Kevin D. Dayaratna, "Cost of a Climate Policy: The Economic Impact of Obama's Climate Action Plan," Issue Brief #3978, June 27, 2013 http://www.heritage.org/research/reports/2013/06/climate-policy-economic-impact-and-cost-of-obama-s-climate-action-plan.

Longer-Term Objectives

62. **Devolve Federal Land Management to States.** Care and protection of public lands, with a few exceptions, should be devolved to states and private groups. Doing so would give responsibility to those closest to the land and with the most to lose from mismanagement or gain from wise use.[57]

63. **Repeal New Source Review (NSR).** Repealing NSR would create incentives for both small and large utilities to install technology upgrades to improve plants environmentally and to increase electricity supply with new coal, natural gas, or nuclear power plants.

64. **Narrow NEPA Review.** Reviews should be limited to major environmental issues that are not dealt with by any other regulatory or permitting process.

65. **Reform the Endangered Species Act.** Shift reliance to the states and focus federal efforts by requiring a Commerce Clause basis for an "endangered species" listing and prioritizing species. The ESA has been very disruptive to small business activity, especially in the West.

HIGH AND GROWING REGULATORY COSTS

Regulations impose costs estimated to be as much as $2 trillion or more than 10 percent of the Gross Domestic Product. Agencies are evading the current requirements to conduct cost benefit analysis and to seek public comment on proposed rules.[58] Regulatory costs have a disproportionate adverse impact on small firms.

Intermediate Term Objectives

66. **Apply Small Business Regulatory Enforcement Fairness Act (SBREFA) to All Agencies, including Independent Agencies.**

67. **Shut Down Agency Evasion of the Administrative Procedure Act through the Use of "Guidance."** All regulations, even if they are called "guidance," should be subject to APA notice and comment provisions.

68. **Require Apply Cost-Benefit Analysis for Rules Promulgated by Independent Agencies and Make All Agency Rules Subject to OMB OIRA Clearance.** Independent agencies should be subject to CBA just like regular executive branch agencies. Some of the most important and expensive rules are being promulgated

[57] Nicolas Loris, "Federal Regulations and Federal Ownership Limit Oil Production Potential," Heritage Foundation Issue Brief #4212, May 7, 2014 http://www.heritage.org/research/reports/2014/05/federal-regulations-and-federal-ownership-limit-oil-production-potential.

[58] For a general discussion of administrative law and regulatory issues, see James L. Gattuso and Diane Katz, "Red tape rising: Five years of regulatory expansion," Heritage Foundation Backgrounder #2895, March 26, 2014 http://www.heritage.org/research/reports/2014/03/red-tape-rising-five-years-of-regulatory-expansion.

by independent agencies. These rules should also be subject to review by the Office of Management and Budget (OMB) Office of Information and Regulatory Affairs (OIRA).

69. **Require Regulatory Assessment of Legislation before Congress.** Just as Congressional Budget Office review is required for any on-budget spending measures, a regulatory assessment should be required for any legislation imposing regulatory burdens.

Longer-Term Objectives

70. **Enact the REINS Act.** All major rules (i.e. those with an economic impact of $100 million or more) should have to be approved by Congress before they are implemented.

71. **Sunset Existing Regulations.** Require all existing regulations to expire automatically if not specifically re-adopted through a notice and comment rulemaking.

ONEROUS LABOR AND EMPLOYMENT COSTS

The morass of laws governing the employer-employee relationship has become extremely complex. These costs and the risk and cost of lawsuits raise the cost of employing people, retards job creation and reduce wages. The NLRB has adopted a series of rules designed to promote unionization that are unwarranted by the National Labor Relations Act.

Intermediate Term Objectives

72. **Reverse EEOC Guidance on Criminal Background Screening.** The EEOC has issued "guidance" requiring employers to do an "individualized assessment" each time they conduct a criminal background screen for employment to determine whether to do the screen and whether to rely on it. Its 55 page, 100 plus footnote "guidance" requires a business to balance a multitude of factors and provides no meaningful guidance. The EEOC has launched hundreds of enforcement actions in this area. Businesses should be able to protect themselves, their customers and their employees by preventing, for example, rapists or thieves from entering their customers' homes.[59]

[59] Hans A. von Spakovsky, "EEOC Loses Again on Background Checks," Heritage Foundation Issue Brief #4203, April 21, 2014 http://www.heritage.org/research/reports/2014/04/eeoc-loses-again-on-background-checks; Hans A. von Spakovsky, "The Dangerous Impact of Barring Criminal Background Checks: Congress Needs to Overrule the EEOC's New Employment "Guidelines"," Legal Memorandum #81, May 31, 2012 http://www.heritage.org/research/reports/2012/05/the-dangerous-impact-of-barring-criminal-background-checks.

73. **Reverse EEOC Guidance on Credit Report Screening.** People in financial difficulty should not be handling, for example, large amounts of cash. In many contexts, credit screening is relevant and employers should be able to take reasonable steps to protect themselves.

74. **Reverse the NLRB Joint Employer Doctrine Treating Franchisee Employees as Employees of the Franchisor.** Many small businesses own franchises. And the franchise model is often the quickest way for start-up enterprises to grow. The NLRB joint employer doctrine would treat many employees of small business franchisees as employees of the franchisor - even though they are not – so that unions may more easily unionize small employers.[60]

75. **Allow Reasonable Educational Attainment Requirements for EEO Purposes.** Most people would be surprised that the EEOC regards, for example, having a high school diploma requirement as unlawful discrimination unless the business can prove that the high school diploma is a "business necessity."

76. **Oppose OSHA Efforts to Regulate Family Farms.** Children should be able to work on their parents' family farm without having to comply with complex OSHA regulations.

77. **Reverse NLRB "Protected Concerted Activity" Interpretations (§7 of NLRA).** The NLRB has, for example, held that a business requiring its employees to be courteous to customers and one another is an unlawful infringement on the free speech rights implicit in the protected concerted activity protections in the NLRA.[61] This is part of their protected concerted activity initiative and their social media initiative and applies to virtually all employers.

78. **Reverse NLRB "Ambush Elections" Rule.** This rule would allow unions to force an election in as few as 10 days.[62] The House passed legislation to accomplish this result.

79. **Prohibit DOL Advice (or Persuader) Rule.**[63] The House passed legislation to

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[60] James Sherk, "Unions Are Waging War on These Small Businesses," December 28, 2014 http://dailysignal.com/2014/12/28/the-unions-are-waging-war-on-these-small-businesses/; Stephen Moore, "Obama, Unions, Trial Bar Take Aim At Franchise Model," September 23, 2014 http://www.heritage.org/research/commentary/2014/9/obama-unions-trial-bar-take-aim-at-franchise-model.
[61] *Knauz BMW*, NLRB Case No. 13-CA-46452, September 28, 2011.
[62] James Sherk, "Proposed Union Rules Harm Workers and Job Creation," Heritage Foundation Backgrounder #2584, July 20, 2011 http://www.heritage.org/research/reports/2011/07/proposed-union-rules-harm-workers-and-job-creation; Testimony of David R. Burton on "The Future of Union Organizing," House Committee on Education and the Workforce, Subcommittee on Health, Employment, Labor, and Pensions " September 19, 2013 http://edworkforce.house.gov/uploadedfiles/burton.pdf.
[63] John Malcolm, "Labor Department's Persuader Rule Undermines Employers' Rights and Threatens the Attorney–Client Relationship," Heritage Foundation Backgrounder #2838, August 26, 2013

accomplish this result.

80. **Amend FLSA as per the Working Families Flexibility Act.** The House passed legislation to accomplish this result.

81. **Oppose Permitting Union Official to Accompany OSHA Inspectors at Non-union Workplaces.**

82. **Allow Employers to Keep Investigations Confidential While Ongoing**. NLRB "Guidance" puts employers in difficult, untenable position.

83. **Address Micro-Unions.** Unions should not be permitted to manipulate voting units, organizing only particular, very small departments because they could not win a broader vote. Such an approach could result in even smaller employers having to deal with many different unions.[64]

84. **Increase NLRB Jurisdictional Threshold Amounts.** The NLRA allows the National Labor Relations Board to decline jurisdiction over small companies Those thresholds are generally $50,000 in annual revenue or a retail store with $500,000 in annual revenue. At a minimum, those thresholds should be adjusted for inflation to $400,000 or $4 million for enterprises and retail stores, respectively. Alternatively Congress can pass legislation exempting small businesses. This would reduce compliance costs and regulatory risk due to the NLRB.

85. **The Rewarding Achievement and Incentivizing Successful Employees Act (RAISE) Act.** Permit unionized employers to give performance-based raises without union consent. This would reduce the burden of collective bargaining on workplace productivity.[65]

86. **Reduce Certain OSHA Fines.** For small businesses, provide that a first-time OSHA violations that does not endanger the health/safety of employees result only in a warning rather than a fine.

Longer-Term Objectives

87. **Repeal Davis-Bacon.**

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http://www.heritage.org/research/reports/2013/08/labor-departments-persuader-rule-undermines-employers-rights-and-threatens-the-attorneyclient-relationship; Burton, op. cit.

[64] See Testimony of David R. Burton on "The Future of Union Organizing," House Committee on Education and the Workforce, Subcommittee on Health, Employment, Labor, and Pensions , September 19, 2013 http://edworkforce.house.gov/uploadedfiles/burton.pdf.

[65] James Sherk and Ryan O'Donnell, "RAISE Act Lifts Pay Cap on Millions of American Workers," Heritage Foundation Backgrounder #2702, June 19, 2012 http://www.heritage.org/research/reports/2012/06/raise-act-lifts-pay-cap-on-millions-of-american-workers.

BAD IMMIGRATION RULES

U.S. businesses should be able to obtain skilled employees from abroad. Changes to the legal immigration system, however, should only follow after steps to improve border security and enforce U.S. immigration laws have been taken and shown tangible success.[66]

Intermediate Term Objectives

88. Create STEM Visas. Increase the number of available visas for foreign-born students graduating from a U.S. university with an advanced degree in a STEM field (science, technology, engineering and mathematics).[67]

89. Increase the cap for H-1B visas (for skilled workers).[68]

90. Support the immigration of highly-skilled entrepreneurs.

91. Ensure that the administrative burden for obtaining employment-related visas is reasonable.

Longer-Term Objectives

92. Create a simplified, rational, integrated skills-based visa program.

COSTLY LEGAL SYSTEM

Our legal system is the most costly in the world. This places American businesses generally at a competitive disadvantage. Lawsuits are potentially ruinous for small firms. Agencies use the threat of grossly disproportionate penalties to force compliance even with unlawful or otherwise questionable enforcement actions.

Intermediate Term Objectives

93. Update Equal Access to Justice Act. EAJA allows small entities to recover costs when the federal government's position was not substantially justified. In its

[66] "Advancing the Immigration Nation: Heritage's Positive Path to Immigration and Border Security Reform," The Heritage Foundation Immigration and Border Security Reform Task Force, Heritage Foundation Backgrounder #2813, June 14, 2013 http://www.heritage.org/research/reports/2013/06/advancing-the-immigration-nation-heritages-positive-path-to-immigration-and-border-security-reform.

[67] Jessica Zuckerman and Landon Zinda, "STEM Jobs Act: Next Step for High-Skilled Immigration Reform," Heritage Foundation Issue Brief #3792 December 4, 2012 http://www.heritage.org/research/reports/2012/12/stem-jobs-act-next-step-for-high-skilled-immigration-reform.

[68] Derrick Morgan and David Inserra, "A Conservative Pathway for Immigration Reform," November 4, 2014 http://www.heritage.org/research/commentary/2014/11/a-conservative-pathway-for-immigration-reform.

current form, it rarely results in attorneys fee recovery. EAJA needs to be reformed so it does what was intended. The standard needs to be broadened by enacting a provision analogous to Civil Rights Attorney's Fees Awards Act (42 U.S.C 1988(b)).

94. **Create a Small Business Patent Court.** Create a specialized court able to resolve patent disputes quickly and inexpensively on an accelerated basis. This would let small firms defend against patent trolls and defend their intellectual property. Aspects of practice in European courts, small claims courts and the U.S. District Court for the Eastern District of Virginia should be incorporated into this plan. This could be a pilot for a more efficient court system.

Longer-Term Objectives

95. **Tort Reform.**

96. **Over-criminalization Reform.** Reduce the criminal penalties imposed for regulatory violations.[69]

97. **Civil Money Penalty Reform.** The EPA, for example, will threaten fines of $75,000 per day unless a small firm complies with their dictates.[70] With that much downside, a small firm really has no choice but to comply. This is unjust.

[69] John Malcolm, "Criminal Law and the Administrative State: The Problem with Criminal Regulations," Legal Memorandum #130, August 6, 2014 http://www.heritage.org/research/reports/2014/08/criminal-law-and-the-administrative-state-the-problem-with-criminal-regulations.
Michael B. Mukasey and Paul Larkin, "The Perils of Overcriminalization," Legal Memorandum #146 February 12, 2015 http://www.heritage.org/research/reports/2015/02/the-perils-of-overcriminalization; Paul Larkin, "The Extent of America's Overcriminalization Problem," Legal Memorandum #121, May 9, 2014 http://www.heritage.org/research/reports/2014/05/the-extent-of-americas-overcriminalization-problem.

[70] See *Sackett v. EPA*, 132 S. Ct. 1367; 182 L. Ed. 2d 367 (2012) http://www.supremecourt.gov/opinions/11pdf/10-1062.pdf; Paul J. Larkin Jr., "Sackett v. EPA: Supreme Court Takes Up Property Rights Case," January 09, 2012 http://dailysignal.com/2012/01/09/sackett-v-epa-supreme-court-takes-up-property-rights-case/.

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Testimony of Elana Fine, Managing Director, Dingman Center for Entrepreneurship, University of Maryland's Robert H. Smith School of Business Before the U.S. House of Representatives Committee on Small Business

March 4, 2015

Chairman Chabot, Ranking Member Velazquez and members of the committee,

Thank you for inviting me to testify before you today. I'm Elana Fine, managing director of the Dingman Center for Entrepreneurship at University of Maryland's Robert H. Smith School of Business. I have a bachelor's degree in finance from the University of Maryland and an MBA from University of Chicago's Booth School of Business. Throughout my career in technology consulting and investment banking, I've worked with hundreds of startups and venture-backed companies and am therefore well versed in understanding the challenges and opportunities facing startup companies.

To provide a little context, the Dingman Center is one of the nation's preeminent institutions where the research, education and practice of entrepreneurship are pursued vigorously. We develop and execute curricular and extra curricular programs to inspire and equip the next generation of entrepreneurs. Twenty-eight years ago, before entrepreneurship was as en vogue as it is now, a visionary dean named Rudy Lamone, partnered with Michael Dingman, founder of Signal Corporation to establish the Dingman Center. As one of the first university-based entrepreneurship centers in the country, the Dingman Center has consistently been the gold standard for teaching entrepreneurship. This past fall, the Global Consortium for Entrepreneurship, a member organization of more than 200 entrepreneurship centers worldwide, awarded the Dingman Center its 2014 NASDAQ award for Entrepreneurial Excellence, for our unique breadth of campus, regional, national and international programs.

My role at the Dingman Center includes oversight of our student venture incubator, the Dingman Center Angels investor network, business competitions and integration with the Smith School entrepreneurship curriculum. I'm responsible for developing relationships with the broader community of entrepreneurs, alumni and corporate partners to build a bridge between our campus and the local startup ecosystem. I also serve as an adjunct faculty member of the Smith School.

Our programs are focused on guiding student entrepreneurs through the venture creation process. We listen to their initial ideas, match them with experienced advisors and mentors, provide a toolset to conduct customer research and develop new business models, suggest ways to prove their concept in small ways and provide access to seed capital. In our 28-year history, thousands of students have walked through our doors to start a business or just to be exposed to entrepreneurship in a small way.

I've been asked to give an overview of entrepreneurial activity from a university perspective. I recognize that the macro level of activity can be hard to quantify and assess whether we are headed in right direction. Based on the pop culture success of television shows like "Shark Tank" and "Silicon Valley," the proliferation of technology incubators, co-working spaces, and downtown innovation hubs, and the newsworthy valuations of companies such as Uber, SnapChat and WhatsApp, we might believe that everyone is working on a startup. Then we look at statistics like the Kauffman Index on Entrepreneurial Activity, which showed a decline from 2011 to 2013 and wonder if we are doing enough. Or we look at 2013 statistics from the Global Entrepreneurship Monitor and see that Sub-Saharan Africa has more than double the early stage entrepreneurial activity of North America. However, this activity is more ne4cessity driven than innovation driven due to lack of other job prospects. From this perspective, a decline in entrepreneurial activity might also be seen as an indicator of an improving economy as employees have better job prospects and don't have to spend their life savings to hang their own shingle. The data is hard to analyze because we don't know the right level of entrepreneurial activity. As we would say in startup terms, we still don't know the metric that matters. So, I'm here today to give you a more grassroots perspective on what I see as leading indictors for the future of entrepreneurship.

At the Dingman Center, we separate our students into three categories and focus on creating programs that will make the most significant impact on these various groups. The first category is the one that has created the "Social Network" misconception—the belief that there are thousands of Mark Zuckerbergs in dorm rooms across campus who will launch the next Facebook. Students, venture capitalists, entrepreneurship centers and policy makers must recognize that Facebook is an outlier. We would never be successful if we were trying to pick the next Facebook, so we spend more of our time on the other groups.

The next category we think about are the students starting businesses while in school. Every year we see panoply of new apparel companies, mobile applications, tutoring services, dating platforms, and food concepts. We have seen university support increase to match student interest and demand in these venture creation activities. Although a small sample, the data from the Dingman Center shows interest in our venture creation programs grew from 161 students in 2012/2013 to almost 400 students in 2014/2015. Students run these businesses for two to three years until graduation where they often decide that this isn't the right business to pursue after graduation. The company might not be a success in standard terms, but as educators we have provided a skill set that we expect will be used for a startup now or 10 years from now.

Our best example of this category is University of Maryland alumnus Kevin Plank, who ran a campus flower delivery service called Cupid's Valentine. After graduation, instead of solving the problem of expensive flowers, Plank decided to solve the problem of soggy cotton t-shirts and turned his savings from Cupid's Valentine into the seed money for Under Armour. In the many times I

have heard Plank tell his story, he has cited the lessons he learned from his first student business and the courage that business gave him to start Under Armour when he had the idea for a stretchy performance t-shirt. Although we hope to have many Kevin Planks walk through the doors of the Dingman Center, we would also like to see more of them stick with their student businesses, which I'll address later.

The last category of student entrepreneurs feed the entrepreneurial labor pool. These students might work on their own businesses or hold internships at local startup companies. The challenge for these students in that startups can rarely pay market rates, so they often have to forego opportunities to take higher paying internships or even summer jobs at pizza shops. We've created several programs to subsidize these students to work at startups to try to replicate the Silicon Valley culture where employees often spin out their own startups. We believe it is the cycle and culture of entrepreneurship that creates innovation hubs, rather than any one specific program.

All of these buckets of students represent the future entrepreneurs, but I caution focusing too much on the first category. Instead, there are a number of initiatives than can increase exposure and odds for success of the last two categories. For example, the National Science Foundation's ICorps program is a perfect example of federally funded programs that can increase the odds of success among early stage university spinouts. ICorps is designed to help federally funded academic researchers with ground-breaking innovations determine the commercial viability of their innovations. This same approach, based on Silicon Valley-tested startup best practices, is now being implemented across many agencies. While it started at NSF, NIH, DOE and other agencies are embracing the process. This program has the potential to fundamentally change the way we transfer technology from our world-class universities and federal labs. Furthermore, the same program has potential to greatly improve the highly regarded SBIR/STTR programs that were created to support small business innovation.

However, programs like ICorps focus on innovation that leads to entrepreneurship. On campuses, we need similar programs that increase the entrepreneurship that leads to innovation—those the encourage students to test the waters on identifying a problem in the market and designing and testing a solution. We know there are more than enough problems to solve. Sample programs might provide scholarships to students pursuing entrepreneurial activities or loan forgiveness so students can choose to work at startup firms. As we seed more entrepreneurs, we will also need more funding mechanisms to substitute for what we often call a friends-and-family round of financing. Without an initial $10,000 to $100,000 it is nearly impossible for a young entrepreneur, who is burdened by student loans and has no savings or credit, to build a product and test customer acquisition. Banks, angel investors and even granting institutions do not have vehicles to fund the typical student businesses. Corporations, like Capital One recognize this need and are leading the way for local entrepreneurs by providing $500 to $2,500 seed grants for our student entrepreneurs.

In addition to exposing young people to the entrepreneurial process, matching them with experienced mentors and increasing their access to funding, we also need to be creative about how to limit downside risk. The success and wealth of Bill Gates, Steve Jobs and Mark Zuckerbergs of the world certainly attracts entrepreneurs, but the downside risk keeps many capable operators on the sidelines. We characterize and celebrate entrepreneurs for their ability to take risks, but there could be innovations that never get to market because the perceived risk to someone's family might be seen as too high. I'd encourage the committee to consider policies that limit downside risk along with those that encourage the upside risk.

Therefore, as you embark on your committee's activities, I'd encourage you to consider the following thoughts and recommendations:

- Few of us are stock pickers. Instead of picking winners and hoping for short-term rewards, we need to seed programs that expose more students to entrepreneurial activities and equip them with the tools to vet ideas early and increase the odds of success.
- Recognize that failure rates will always be high and that success in entrepreneurship can also be viewed by total births and deaths because it means there are more companies in the field.
- Consider programs that provide non-dilutive funding substitutes to friends-and-family funding and angel funding for a broader spectrum of businesses. Keep in mind that entrepreneurs are like marathon runners and come in all shapes and sizes.
- Think creatively about "apprentice"-like programs in high growth startups that might increase the entrepreneurial labor pool.
- Consider how to limit downside risk that might keep capable entrepreneurs on the sidelines.

In a Washington Post article, I wrote that teaching entrepreneurship is like teaching a child to drive. You give them a little taste off the side in a shallower waters and if it takes, they feel comfortable to take the risk off the higher diving board. This is how we teach entrepreneurship - we expose our students to a non-linear way of thinking and problem solving. Our challenge, as outlined above, is no transition these students from the safe risk-taking environment of an academic institution, to the business world. I look forward to working with you to create policies to build on the momentum we are seeing on campuses nationwide.

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