STATE OF THE SMALL BUSINESS ECONOMY

HEARING

BEFORE THE

SUBCOMMITTEE ON ECONOMIC GROWTH, TAX, AND CAPITAL ACCESS

OF THE

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HOUSE OF REPRESENTATIVES

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STATE OF THE SMALL BUSINESS ECONOMY

THURSDAY, FEBRUARY 16, 2017

HOUSE OF REPRESENTATIVES,
COMMITTEE ON SMALL BUSINESS,
SUBCOMMITTEE ON ECONOMIC GROWTH,
TAX, AND CAPITAL ACCESS,
Washington, DC.

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

Present: Representatives Brat, Chabot, Kelly, Gonzáles-Colón, Fitzpatrick, Velázquez, Evans, and Clarke.

Chairman BRAT. Welcome to the Committee on Economic Growth, Tax, and Capital Access in the 115th Congress. I call this hearing to order. Thank you all very much for coming today.

This is my first hearing as Chairman of this Subcommittee. I could not be more excited as we begin a new Congress, a new presidential administration, and, with the right policies, a new chapter for the American economy. And thank you all for coming to share with us today.

As a former economics professor, I am particularly pleased that we have such a distinguished panel here today to help us explain what the economic indicators are telling us and how they reflect what we hear back home from our constituents every day.

It has been said time and again, both at this Subcommittee and in the Full Committee, but I believe it cannot be stressed enough, small businesses are the backbone of the American economy. They represent 48 percent of workers in the private sector and 99.9 percent of all firms. You do not have to be an economist to understand the equation: When small businesses succeed, our country succeeds. And it is just that simple.

The economy grew at an anemic rate of 1.6 percent in 2016, and 1.5 percent over the last decade or so. This rate is half of the historical average.

During this period of slow growth, 155 million Americans faced higher costs due to the Affordable Care Act. Americans also spend $1.89 trillion a year just to comply with Federal regulations.

Finally, for most small businesses, the effective tax rate is more than 47 percent. All of these issues have converged to affect the economy at large.

Although it is important to label the problem, Congress is actively working to implement solutions. We are starting the process to repeal and replace the Affordable Care Act. We are passing regulatory reform bills such as the Regulatory Accountability Act of

2017, and utilizing the Congressional Review Act to repeal burdensome Obama-era rules. The administration is also taking actions, such as their "two out, one in" regulatory approach to help cut some of the red tape faced by small businesses.

The unified Republican government is committed to helping the Nation's economy escape this slow growth, and we are backing up our words with action.

American small businesses are not in business to comply with Washington, though it can sometimes feel that way. Rather, they are in business to earn a profit so they can make a living for themselves and for their families. In turn, they create jobs for their fellow Americans and help strengthen the economy.

As I am certain we will hear this morning, healthcare reform, regulatory relief, simplifying and lowering taxes, and getting Washington out of the way would unleash the power of our small businesses so they can do what they do best: to grow and create jobs.

We look forward to hearing from our witnesses and thank them all for being here today. We will certainly benefit from their perspectives on the state of the small business economy.

I now yield to the ranking member for his opening statement.

Mr. EVANS. Thank you, Mr. Chairman.

Small businesses are the backbone of the American economy. There are 29.6 million small businesses in the United States who employ about 58 million people, nearly 50 percent of all private sector employees in the U.S. When our small businesses succeed, America succeeds. Today here will give us a great opportunity to hear from successful small business owners about what works and what does not, and discuss policies that will help this sector grow.

The American economy, as strong as it has been in years, while we are seeing steady and sustainable growth, certain sections, such as manufacturing and construction, continue to struggle. It is imperative that we do more in these areas. However, we should also remember the dire straits of our economy after the 2008 fiscal crisis.

The Great Recession was the largest economic disaster our Nation faced since 1929. Housing prices plummeted more than 30 percent. Businesses of all sizes shed jobs. In 2009, unemployment reached 10 percent nationally. That staggering number does not even include discouraged workers who left the workforce or the unemployed who took jobs where they were overqualified.

Small businesses felt these challenges acutely. In the first three quarters of 2009, small firms accounted for almost 60 percent of the net job loss. As the recession caused lending to tighten, entrepreneurs increasingly struggled to access the capital. In late 2009, one survey found that 78 percent of small business owners reported being negatively affected by the access to capital.

Eight years later, economic indicators tell a completely different story. Real gross domestic product continues to increase year after year. In 2016, the GDP increased due in part to increase in consumer spending and residential investment. Unemployment has remained below 5 percent for well over a year. In fact, last November, unemployment dipped to 4.6 percent, the lowest it has been since 2007.

We have also seen considerable job growth. Over the course of the Obama administration, America gained 11 million new jobs. His presidency saw 75 percent straight months of job creation, the lowest continuing that is stretched in job growth since 1939. This period of growth continues with January adding approximately 246,000 new jobs, including 62,000 small business jobs. Median household income surged in 2015 for the first time since 2007. The 5 percent increase we saw in 2015 showed the economy is improving, yet income remains 2.7 below its 1999 peak.

Moreover, these gains have been uneven with recovering progressing much slowly in certain industries and regions, showing that there is still a great deal of work to be done.

Small businesses also have to see improvement over the last 8 years. Commercial credit conditions have eased. Demand for loans have increased as the economy has recovered. However, there remains wide differences in credit demand between small and large revenue firms. Lack of capital is one of the primary reasons businesses flounder.

I hope today's hearing will help us better understand small companies' lending needs so that we can improve their options. The improvement in the economy has led small business owners to enter 2017 with more optimism about the economic future than they have in decades. However, they remain concerned about health care, taxes, and other regulations. That is why it is imperative that we ensure small businesses have a seat at the table when we discuss major policy reforms.

I look forward to working with the chairman and all members and colleagues on this Committee to craft bipartisan legislation policy that will help sustain and shift in small business growth.

I yield back my time, Mr. Chairman.

Chairman BRAT. Thank you.

If Committee members have an opening statement prepared, I ask they be submitted for the record.

I would like to take a moment to explain the timing lights for everyone with us today. Speakers will have 5 minutes each to deliver your testimony. The light starts out green. When you have 1 minute remaining, the light will turn yellow. And finally, at the end of your 5 minutes, it will turn red. I ask that you all try to adhere to that time limit as best as possible. And so let us begin.

Our first witness this morning is Dr. Stan Veuger, resident scholar at the American Enterprise Institute. His research interests include political economics and public finance. Dr. Veuger is a board member of the Netherland American Foundation in Washington, and a senior editor at the Bulwark, a quarterly public policy journal.

Dr. Veuger, you have 5 minutes, and you may begin. Thank you.

STATEMENTS OF STAN VEUGER, PH.D., RESIDENT SCHOLAR, AMERICAN ENTERPRISE INSTITUTE; VICTOR HWANG, VICE PRESIDENT, ENTREPRENEURSHIP, EWING MARION KAUFFMAN FOUNDATION; HOLLY WADE, DIRECTOR, RESEARCH AND POLICY ANALYSIS, NFIB RESEARCH FOUNDATION; BOB BLAND, CEO AND FOUNDER, MANUFACTURE NY

STATEMENT OF STAN VEUGER

Mr. VEUGER. Thank you, Chairman Brat, Ranking Member Evans, members of the Committee. Thank you for inviting me to testify here today on the state of the small business economy.

The U.S. economy is still on the long way back to recovery from the 2007-2008 financial crisis. And while conventional measures such as real GDP per capita have surpassed their pre-crisis peak, a number of severe weaknesses remain. Some of these are plausibly the result of the long and deep recession the country went through, while others are symptoms of more long-run trends. As an example of the former, the number of long-term unemployed workers is still significantly above the pre-crisis level. Weaknesses of the latter variety are arguably more worrisome, as there is no reason to believe that they will, with enough time, heal and disappear.

Two examples of this type of long-run weaknesses are trends and levels of concentration within industries, and trends in the entry of new firms. Levels of concentration have been trending up. Entry of new firms has been trending down. And that I think should be of particular concern to the Committee.

During the same period something else has happened and that is what I will focus my testimony on today. Uncertainty surrounding economic policy has been elevated for quite some time now. Now, this type of policy uncertainty was widely discussed in the popular press during the crisis, after the crisis, and it has also received significant attention from academic researchers.

Now, theoretical research has taught us that policy uncertainty can affect consumption, investment, as well as broader activity. And while those theoretical insights have been around for a while, going back to Milton Friedman and work even before that, recent research has also shown that these effects do, indeed, exist. And in the real world it can be shown to do so empirically.

For example, hire policy uncertainty from 2008 on has been found to be associated with a deeper and longer recession. The political stalemates in the U.S. contributed to the length of the recession as did shocks from Europe. In work with Daniel Shoag of Harvard, I, myself, found that increases in local, State-level uncertainty over the period was strongly correlated with the effects of the recession unemployment, and that correlation is very robust to arrange other potential explanations for bad labor market outcomes.

And while there is certainly a feedback loop between outcomes and policy uncertainty, there are fiscal institutions and preparations that stayed and most of the Federal Government can take to limit those increases in uncertainty.

This type of policy uncertainty is of particular concern to small businesses which are in a sense more risk averse by sheer size, typically less diversified than multinational firms. And I think that this is why this is an area that should be a concern of interest to this Committee as it starts to legislate in this new Congress.

Some of the things the Committee has already contributed to I think have been very positive on this front. For example, the Small Business Regulatory Flexibility Improvements Act which passed as part of H.R. 5 requires more careful consideration before new rules and regulations are implemented, demands that their impacts on small businesses be considered more specifically, and I think that those are good initiatives.

Similarly, the HALOS Act, which passed the House last month is helpful in limiting the reliance that small business owners and managers have on their own private capital and allow for them to raise more outside capital, reducing potentially their levels of risk aversion and the trouble they run into when dealing with inevitable levels of policy uncertainty.

And so as I conclude, I would like to ask the Committee as it proceeds to consider more legislature, to consider these potential sources of policy and regulatory uncertainty. For example, while I think that fundamental corporate tax reform is way overdue, it is, I think, important to proceed in a way that does not disrupt firm operations in unnecessary matters. But there are always going to be winners and losers from this kind of fundamental policy change, but I would ask for well-considered transition measures and certainly well thought-out measures as they may have unintended consequences.

And with that I would like to thank you again for giving me the chance to speak.

Chairman BRAT. Thank you, Dr. Veuger. We appreciate your testimony.

Our next witness is Victor Hwang, Vice President of Entrepreneurship at the Ewing Marion Kauffman Foundation in Kansas City, Missouri. Mr. Hwang is co-author of The Rainforest: The Secret to Building the Next Silicon Valley, and the follow-up, The Rain Forest Blueprint: How to Design Your own Silicon Valley, which examine how the innovation ecosystem in the Bay Area can be replicated in other parts of the country. Prior to joining the Kauffman Foundation, Mr. Hwang co-founded Liquidity, a nanotech firm that makes filters for safe drinking water.

Thank you for being here with us today, Mr. Hwang. You may begin. Thank you.

STATEMENT OF VICTOR HWANG

Mr. HWANG. Chairman Brat, Ranking Member Evans, and members of the Committee, thank you for the invitation to testify.

I am pleased to share insights and recommendations from the Kauffman Foundation about the state of entrepreneurship in America. I will describe the bad news, share some good news, and talk about how to address these challenges.

First the bad news. America is suffering from an entrepreneurship deficit. It is slowly but surely eroding our quality of life and our national competitiveness. I personally experienced the challenges of starting and growing new businesses. My parents were entrepreneurs. For most of the past decade I have been an entrepreneur and investor in Silicon Valley, and over the past year I have gotten a big-picture perspective as the head of Entrepreneurship at the Kauffman Foundation.

Based on our work at Kauffman, we believe this entrepreneurship deficit comes from a long-term decline in business dynamism, or the pace at which firms start and grow. As a case in point, Americans are starting new businesses at roughly half the rate they were a generation ago. The implications of the steps are profound. Recent research is starting to show how the entrepreneurship deficit is connected to some of America's biggest challenges: slower productivity, lower wages, stagnant job growth, and rising inequality.

A recent report expands on the connection between the long-term decline in entrepreneurship and the effect on productivity and growth. That lackluster productivity drags wages and living standards down. Put simply, fewer startups mean a lower quality of life for all Americans.

Now, some good news. After a long hangover from the Great Recession, entrepreneurship is finally rebounding in America. According to the Kauffman Index of Entrepreneurship Series, entrepreneurship is up across all three measures: new business creation, growth, and local small business activity. Kauffman's Main Street Entrepreneurship Index is nearing a two decade high, driven by a jump in small business survival rates. Today, almost half of all new businesses are making it to their fifth year of operation.

Both the long-term decline and the recent uptick in entrepreneurship have been shaped by three megatrends. These trends are affecting entrepreneurship today and we believe will for decades to come. We call these trends the new demographics, the new map, and the new nature of entrepreneurship.

Demographically, the U.S. population is increasingly becoming more racially diverse, yet the American entrepreneurial population does not reflect these changes. Today, 80 percent of American entrepreneurs are white, and 65 percent are male. That is a big gap for racial minorities and women. That gap costs the country about 10 million jobs.

The map of entrepreneurship, the second face of entrepreneurship, is increasingly urban. While entrepreneurial activity is growing in midsize cities outside of major metro areas like Silicon Valley, it is still lagging in rural communities. And technology is changing the nature of entrepreneurship. In the past, as companies scaled their revenue, jobs could scale at a similar pace. Today, companies can rapidly grow revenue and value while job growth lags behind.

In response to the entrepreneurship deficit and these trends, the Kauffman Foundation today launched the Zero Barriers to Startup Challenge. We believe that entrepreneurship is a fundamental human right. You should not need a formal degree. It should not matter your race, your gender, or where you live. You should be able to do it quickly, inexpensively, without confusion, and without barriers imposed by others.

Unfortunately, there is a big gap today between that vision and the reality. You can help people—current entrepreneurs and those with an idea—afraid to make the leap by taking that Zero Barriers to Startup Challenge with us. The Kauffman Foundation encourages members of Congress to host entrepreneur town halls, to tour entrepreneur support organizations, and to invite entrepreneurs to testify before this Committee and others about the barriers they face. Listen to the grassroots and act on the solutions.

When barriers hinder Americans from pursuing their entrepreneurial dreams our whole nation suffers. That is no longer conjecture. There is accumulating research evidence for it. Together, let's commit to zero barriers to entrepreneurship so that all Americans, regardless of who they are or where they are from, can turn their ideas into reality. Thank you very much.

Chairman BRAT. Thank you, Mr. Hwang. We appreciate your testimony very much.

Our third witness this morning is Holly Wade, Director of Research and Policy Analysis at the National Federation of Independent Business, NFIB, in Washington, D.C. At NFIB, Ms. Wade provides analysis on public policy issues and economic trends affecting small business. She also produces the monthly small business economic trends survey with NFIB's chief economist, which surveys their members' plans for expansion, sentiment on the United States economy, and top priorities.

Ms. Wade, thank you very much for being here, and you may begin.

STATEMENT OF HOLLY WADE

Ms. WADE. Good morning, Chairman Brat, Ranking Member Evans, and members of the Subcommittee on Economic Growth, Tax, and Capital Access. Thank you for the opportunity to testify today on the state of the small business economy.

Over the past 10 years, small business owners have struggled to bounce back from the Great Recession. The economic recovery has been painfully slow for many, at first due to poor sales, but quickly overtaken by issues related to taxes, regulations, and the cost of health insurance.

NFIB's Small Business Economic Trend Survey found small business owners stuck in a below average rut with the survey's optimism index exceeding its 43-year average reading only five times since July 2007. Three of those above average ratings were recorded in the last 3 months.

Owners' optimism failed to materialize as average GDP growth remained relatively flat at 2 percent over the last 8 years, and government policies continue to increase the cost of doing business.

In response to the combination of policy constraints and anemic GDP growth, few small business owners found economic conditions supportive of investing in or growing their business. The poor business climate is further exacerbated by heightened level of economic and government uncertainty.

NFIB's 2016 Small Business Problems and Priorities Survey found that two of the top 10 most severe problems affecting small business owners are uncertainty related. Uncertainty about economic conditions and government actions are ranked fourth and sixth out of 75 business problems, respectively, and about one-quarter of small business owners find each a critical problem in operating their businesses, all creating significant barriers to economic growth in the small business sector.

Post-election, small business owner sentiment improved dramatically with more owners optimistic about the outlook for business conditions and business expansion. The rosier outlook has translated into more favorable expectations for sales growth and hiring to support expected gains in sales and revenue.

As owners' confidence in the economy and economic policies rise, owners will be more likely to invest in and grow their business. Owners hold high expectations that Congress will now create a friendlier business climate for them to succeed.

The three main concerns of small business owners for operating their businesses are taxes, compliance and disruption cost of regulations, and the rising cost of health insurance. All three of these issues consume valuable resources from small business owners, including their time, time diverted away from operating their business, and profits, which is the main source of financing for capital investment and business operations.

For example, NFIB's newly released survey on regulations find that half of small employers report that regulations are a problem in operating their business, with 25 percent of them finding it a serious problem. When asked what specifically impacts them the most, 28 percent of small employers cite compliance costs as their biggest problem. However, 18 percent are most burdened by understanding how to comply with the regulations, and 17 percent most burdened by the extra paperwork requirements. And for over half of small employers, the volume of regulations is their biggest challenge compared to 37 percent who are most troubled by a few specific ones.

The volume of regulations is particularly important in that most small employers take on the responsibility of learning about new government requirements themselves instead of delegating the task to an employee. The more time they spend learning about and complying with government regulations, the less time they have in operating their business.

NFIB hears from small business owners year-round about the various challenges they face operating their business, and their stories are reflected in the survey results published by the Foundation. But given the right set of policies, policies that lower government cost hurdles for small business owners, they are in a great position to invest in and grow their business.

I appreciate this opportunity to discuss the current state of the small business economy and the challenges it faces going forward, and I look forward to working with the Committee to support small businesses and the U.S. economy. Thank you.

Chairman BRAT. Thank you, Ms. Wade. We appreciate your testimony. Thank you for coming in today.

I now yield to the ranking member for the introduction of our next witness.

Ms. VELÁZQUEZ. Thank you, Mr. Chairman. It is my great pleasure to welcome Bob Bland, who is a Brooklyn-based fashion designer, entrepreneur, community organizer, and working mother, and my constituent. She is the CEO and founder of Manufacture NY, a fashion incubator and factory hybrid dedicated to providing independent designers with the resources and skill to streamline their production process and transform local manufacturing into the most affordable, innovative option for all. An international speaker and advocate for domestic manufacturing, ethical supply chains, and design entrepreneurship education, Ms. Bland has presented Manufacture NY as a case study in Copenhagen, Seoul, Los Angeles, Las Vegas, Washington, D.C., and New York City.

Welcome, Ms. Bland.

STATEMENT OF BOB BLAND

Ms. BLAND. Thank you, Chairman Brat, Ranking Member Evans, and thank you so much to Ranking Member Velázquez for your kind invitation to speak today.

Since the Great Recession, virtually all small, creative, and manufacturing businesses in the Nation have had the same challenges: access to affordable industrial space with long-term leases, relocation grants for those who are displaced, affordable housing with a reasonable commuting distance of their workplace, low-interest working capital and lines of credit to grow their small businesses, and competitive equipment procurement and training programs so that we, as entrepreneurs, can adapt to a rapidly changing global landscape.

Design and manufacturing jobs specifically are more than just jobs. They are an inclusive pathway to meaningful careers and the potential for business ownership, regardless of previous educational background or socioeconomic status. With an average salary of $59,000 per year, they are more likely to include benefits and have a clear path for growth, both in terms of skills training and the opportunity to advance.

The New York City fashion ecosystem is a great template for a unique and creative dynamic ecosystem that could be used in innovation economies in other cities, and that is some of the work that Manufacture NY specifically has done, is going to other cities, most recently North Las Vegas, for instance, and seeing how can we create that same sort of innovative manufacturing ecosystem around the country. And we need to have programs in place where we can do this, not just independently as we have been doing, but actually have Federal support to create these innovation economies around the country.

Small businesses and entrepreneurs are the engine of our Nation's economy and drivers of innovation, and we cannot compete without having better workplace benefits, and we definitely cannot compete with larger companies that are able to afford those benefits because of the economies of scale. Freelancers and microbusinesses, and when we are talking about microbusinesses, saying that 25 people and under is a microbusiness, is actually quite funny to a lot of small business owners because that is most of our small businesses are much smaller than what the SBA currently defines as a small business or microbusiness. So we also need to look at how we define what a microbusiness is and how we are offering support for even smaller businesses than 25 employees and under.

And we do not have the infrastructure to support workers with caregiving responsibilities. I am here with my daughter today who is 2-1/2 months old because I cannot afford to get care for her as an entrepreneur and as a business owner myself, so I have simply had to bring her with me everywhere for the last 2-1/2 months because there is no option for me as a business owner to take maternity leave. And so this is an example of something where the Federal Government could offer benefits across the board in terms of paid family leave. And I have been informed of the Family Act, which would create self-sustaining family insurance for all workers modeled after successful State programs.

And then also I would just say a national family leave policy would really reduce the burden on businesses, particularly businesses owned by women where we are really stopped from moving forward by our duties of care both for our children and then also elder care as well that disproportionately affects women.

In terms of the SBA and what they offer, I have personally participated in programs around the SBIR, which is essentially an equity-free venture capital fund, and I highly recommend that we continue on with those programs. With the SBA's innovateHER program that they did in partnership with Microsoft, we participated in that and we need to advance those sort of programs.

And then also, the Growth Accelerator Fund was a program through the SBA that actually supported the creation of incubators and accelerators around the country, and it really was a driver for new businesses. So I highly recommend those programs.

And then also, the Manufacturing Innovation Institutes under the Obama administration were an incredible driver for manufacturing, and particularly advanced manufacturing, and I would recommend that those continue forward, as well as manufacturing communities. And I know there is bipartisan legislation available around a manufacturing communities bill in both the House and the Senate. Thank you.

Chairman BRAT. Thank you, Ms. Bland. We appreciate your testimony.

Now we will begin the first round of questioning. I now recognize myself for 5 minutes.

I was going to defer, but as an economist and professor for the last 20 years in economics, I do want to just add some preliminary remarks. Everyone is referring back to the Great Recession, and there has been a grand misdiagnosis that the economy has been anemic because of that, and then what caused that. We usually call it a financial crisis. But I think it is important to go back to the history of what happened, and in what order it happened, and I do not think there is any debate the last financial crisis started in the housing market. Right? That, I think, is unquestionable.

And so then we get to the crux of the good policy, and why in the world would bankers make mortgages, to folks with no incomes? Right? And the answer throughout the history of American economic history is they would not. Right? Something would be very strange. In the old days, the banker would go meet the neighbors and say, hey, does this person have a good job and a good credit history and a good ethical reputation? Oh, good. Okay, I will give you $100,000 for a mortgage.

So what changed to the housing market, which Greenspan and Bernanke argued and they are not overly political. It is not a political argument. They said that was the asset class that had never—it was the gold standard, right? The housing sector was the gold standard. And so how in the world did the gold standard—the asset class that had never had any issues, right, every other asset class has—fall into such ruin? That did go over and fall into the financial crisis, and there—I am not condoning Wall Street or anything, just so we are clear on the politics. When you get to the financial crisis, there was ethical, you know, misconduct all across the board.

But I think it is important to go back and look at what caused the housing crisis because that is what got us into this low-growth environment, and in my view, a lot of it was caused by bad Federal policy. Fannie and Freddie, bankers no longer had to take the risk, right? That is their main job is risk assessment. Instead of assessing risk, they would get their fee for making a mortgage and hand off the risk immediately to Fannie and Freddie. And when Fannie and Freddie take on that risk, who owns the risk? You do because you backstopped. The American people do, right? You backstopped through the government, Fannie and Freddie.

So I just think it is important to get that backstop in mind. That was wrong Federal Government policy, and policies which wrongly incentivize the housing market which caused the financial crisis. And so with that in mind, I will just start with Dr. Veuger and work our way down.

We are kind of working on three big buckets right now: healthcare efficiencies, tax reform going forward, a corporate rate and individual rate, and then immediate expensing. And then the third is just the basket of regulatory reforms.

In your view, where is the biggest bang for the buck? Where should we be spending most of our time up here? Or do you got to do all three? I mean, just in your experience, if you could share a little, and then Mr. Hwang next.

Mr. VEUGER. I think focusing on all three is complicated. There is only so much output that the legislative branch can produce. So of those three I would probably focus on tax reform. I think that is a good—you know, it clarifies matters because it is a broad issue or touches upon a lot of the problems we discussed.

I think regulatory reform is important, but because so much of it is driven by—it is not clear to me what beyond what the House has already done, what it can do there to really make significant progress in one specific bill or one specific initiative that does not—maybe it is because there are so many subparts. I would say tax reform should be the top priority.

Chairman BRAT. Mr. Hwang?

Mr. HWANG. We launched today the Zero Barriers movement specifically to deal with this issue of: "What are all the things that get in the way?" If you look at the burdens of real entrepreneurs, there are so many, and there are so many headwinds that they face. And so with the Zero Barriers movement, what we are trying to launch is a realization, an acceptance of the fact that this stuff starts at the grass roots. It is city by city. It is county by county, district by district, state by state. When we think about these problems, we tend to ask, "Well, what is the one thing we can do?" But ultimately, it has got to be something where we empower the community of entrepreneurs and people that fight for entrepreneurs to come up with the answer. So what we are doing is harvesting the answers, gathering them, empowering people back in their communities, and supporting experiments around the country at the local level, even hyperlocal, to try to figure out what works and overcome these barriers.

Chairman BRAT. Great.

Ms. Wade, NFIB?

Ms. WADE. Unfortunately, all three are incredibly important for small business owners, our members. When we surveyed for the 2016 Problems and Priorities Survey, health insurance cost is the number one problem. Fifty-two percent say it is a critical issue in operating their business. Burdensome regulations is the second most critical issue facing small business owners, and then under that is Federal taxes on business income. So all three are the top three important issues that they face.

When it comes to tax reform, which is incredibly important, you know, tax reform should start with small businesses because they need parodies. Small businesses should not be paying more than larger corporations in the Federal Tax Code. And so tackling tax reform is incredibly important, and all the variety of ways that it is important for small businesses, but regulations and health insurance costs are equally as important.

Chairman BRAT. Thank you. Thank you very much. Sorry, as the chair I went over my own time limit. I see my time has expired, and I would like to now yield to the ranking member, Mr. Evans, for 5 minutes.

Mr. EVANS. Thank you, Mr. Chair.

Ms. BLAND. Oh, do I not get to——

Mr. EVANS. Ms. Bland, would you like to answer the question?

Ms. BLAND. Okay. Yeah. As an entrepreneur and a small business owner myself and a woman, I just want to say that we work with—we have launched over 150 small businesses in the last 4 years and they are primarily women and person-of-color-owned businesses. And what we see as the two big things are the healthcare situation, and really just social safety net in general, giving people the support they need to start launching their business by ensuring that they have their own personal health insurance and then also a place to live, a place to work. You know, that sort of support is needed throughout the first 2 years of a small business' launch.

And then additionally, with the taxes, yes, I would totally agree that my tax rate as a small business owner is way too high, and it just seems impossible for me to continue, particularly when I am trying to create job growth. When I am trying to hire more employees, it is especially onerous and impossible for me to continue creating more jobs and still even break even.

Mr. EVANS. Let me follow up a little bit. As you know, many economists have talked about employer-based health insurance can lead to job lock where employees stay in their job solely for the benefits.

The Affordable Care Act effectively eliminates job lock. As an entrepreneur, how important was the availability of health insurance coverage in your decision in starting up your business?

Ms. BLAND. Well, originally when I started my business is was prior to the Affordable Healthcare Act, and it has actually really helped me to have flexibility as a business owner to be able to say to my employees—beucauses my business has less than 50 employees, so I am not required to have health insurance. And so being able to direct them to the New York market to be able to get their health insurance, and then knowing that they have that security has been incredibly beneficial, both in making sure that they have care even when I cannot afford to subsidize it for them, but then, also, from an ethical perspective, knowing that I do not have employees on the job that are going to get sick and have nowhere to go. So I would say it has been very beneficial.

Mr. EVANS. I would like to piggyback to Mr. Stan—last name again?

Mr. VEUGER. Veuger.

Mr. EVANS. Veuger. Sorry about that. About this issue of policy uncertainty and the drag on the economy. I am fascinated with what you have talked a little bit about. Can you, you know—I heard what the chairman said as he laid out the three particular issues, but I sense that the issue of policy uncertainty is probably the common denominator in the decisions that are made. Can you speak a little bit to that in terms of the impact of the issue around policy, particularly if you talk about the Affordable Care Act? Can you talk a little bit about that?

Mr. VEUGER. Yes. I think one priority for this Congress should be to be careful as, you know, it works toward the stated goal of repealing and replacing the Affordable Care Act. I think we need to be careful not to unnecessarily disrupt, especially the individual market, which is pretty vulnerable to even announcements of future policy. There are significant weaknesses in the individual market as it stands, and I would worry that if Congress goes ahead with repeal of the Affordable Care Act or significant parts of it without having a clear direction of where policy is going afterwards in mind, I would worry what the individual market would be. And that is sort of true for the small group market, too, that that would unravel in a way that would be detrimental.

Mr. EVANS. Mr. Hwang, real quick, I have not much time, but there is a real gap for racial minorities and women. What impact do you think a lack of diversity has on the small business community?

Mr. HWANG. We have done research on this. As I mentioned in my earlier testimony, there would be about 10 million jobs more if women and minorities were creating companies at the same rate as others. So it is a profound gap. It is also not just in terms of the gross economy. It is also in terms of the level of innovative products. There is research that shows that diverse teams tend to make more innovative solutions together. And I think that goes a lot to the core of the American fabric. What makes us competitive is the ability to bring in a diversity of ideas and talents to bear on problem solving.

Mr. EVANS. Thank you, Mr. Chair. I yield back the remainder of my time.

Chairman BRAT. Thank you very much.

The gentlelady from Puerto Rico is now recognized for 5 minutes.

Ms. GONZÁLEZ-COLÓN. Thank you, Mr. Chairman.

This is going to be for the full panel. Even though the interest rate has been low for quite some time, many small business owners say that they have issues obtaining credit. Why is this the case and maybe are some solutions for that?

Ms. BLAND. As a small business owner who has had issues obtaining credit, I can definitely tell you that even for my business that fosters so many other businesses and is seen as a case study for what this entrepreneurial incubator ecosystem should look like, the simple matter is if you do not have—you know, let's say I want to get a $200,000 loan. If I do not have $200,000 in security, I am not getting a loan. It is as simple as that. You have to be able to back your own loan. And why would I need a $200,000 loan if I already had $200,000. You know?

So it is something where even with all the great programs out there, it is kind of a feel-good thing where most of my businesses, when they go after all of these low-interest loans, at this point they still do not end up qualifying for them because what they need is really a mix of a loan and then something that allows for more risk, like a venture capital type solution. But again, with most of these businesses, particularly in the manufacturing sector where the growth pattern is a little slower and the overhead is a little higher, it is hard for them to get venture capital as well. So there are a lot of businesses that are caught in the middle of this and they simply cannot just bootstrap or crowdsource, and we are really missing out, particularly in the manufacturing sector.

Ms. GONZÁLEZ-COLÓN. Mr. Hwang?

Mr. HWANG. Mr. Kauffman, the founder of our foundation, started his business with $5,000. And one of the questions to ask is: could someone obtain $5,000 as a bank loan today? And it is very, very hard. There has been a tremendous decline in community-scale banking. Yet there has been a tremendous aggregation in capital for risk. 80 percent of the venture capital in the United States is concentrated in three States: California, New York, and Massachusetts. So there is an unlevel playing field for capital right now, and there are several reasons that we can hypothesize around this.

One is around the lack of community connection. The chairman had talked earlier about how you could go to your neighbors and people you had relationships with, and they trusted each other to pay back these loans. The disconnection of capital—the community—and the people that are in these local environments—has caused a problem because it has made people more risk-averse in lending capital.

There is also, I think, a scale in difference between how we think of capital, both at the macro level and the micro level. Battleships can handle storms better than dinghies, and startups are dinghies. And it is hard for dinghies to get people to throw them these lifelines when they need them. And so I think an attention to the effect and the impact of policies on small-scale lending, not just big-scale lending, is very, very important.

Ms. GONZÁLEZ-COLÓN. I will piggyback on that. How, in your experience working in Silicon Valley and all your research you have done for your books, can rural American territories replicate that in terms of entrepreneurship?

Mr. HWANG. That is a complex answer and there are many different aspects to that. But I think primarily one of the things that we know innovation derives from, and we know startup companies are born out of, are highly interconnected environments. If we can build more opportunities for flows of information, people, and connections in communities, that is where capital comes from. It is from the flow of people with resources. It is from the trust that is built in these communities.

So we can use new technological tools. We can build communities. We can make significant efforts to try to increase the interactions between people who have resources and those who do not. That is a very core way of getting a level playing field.

Ms. GONZÁLEZ-COLÓN. I yield back my time, Mr. Chairman.

Chairman BRAT. Thank you.

The gentlelady from New York, Ms. Clarke, is now recognized for 5 minutes.

Ms. CLARKE. Thank you, Mr. Chairman Brat, and I thank our ranking member, Mr. Evans. I thank our panelists of experts for their testimony here this morning.

Today we have heard testimony of the state of small businesses in our economy. As we all know, and it is not just cliche, small businesses are the lifeblood of our economy. There are millions of Americans that are allowed to provide for their families and help our economy grow. In recent years we have seen the effects of the Great Recession slowly recede into the distance. Wages have increased slightly, median household income is on the rise, and capital is being lent with greater ease. However, these trends are not true for all Americans. Minority communities remain disproportionately affected by the Great Recession and face difficulty obtaining jobs, receiving raises, and accessing capital. The Small Business Administration has programs in place that take into account the unique challenges that minorities and women face in accessing capital and entering the entrepreneurial realm. Yet, these programs are not all of the cure.

So Mr. Hwang, in your testimony, you stated that one of the megatrends affecting the spread of entrepreneurship is the increase in American diversity. As you stated, the entrepreneurship gap between white males and everyone else is wide and costs our company greatly, to the tune of 10 million jobs. Aside from cutting taxes and regulations, what can Congress do to ensure that all Americans are able to contribute and utilize their entrepreneurial acumen to inure to our economic growth. Give us a little bit more about your concept about zero barriers.

Mr. HWANG. Sure. So what you are talking about is the biggest challenge facing our field today and the biggest mission of our foundation: how do we overcome these gaps? And I wish I had all the answers for you. This is obviously a very complex question, but I think one of the very key pieces of this is that there are hard and soft barriers. There are the hard ones, which are regulatory and legal, and the challenges—local, county, State, Federal—that get in the way of entrepreneurs, but there are also invisible ones, which are the social barriers, the disconnected parts of communities where people do not interact, where you do not get the flow of talent and ideas between different parts of communities. We see that all over the country. You have certain places where entrepreneurship has, unfortunately, become almost a privileged activity and it feels like it is something that is accessible and obtainable only by people who are lucky enough to understand how to do it. And it should not be that way. It should be democratized where everyone has access to it.

We are going to be working on this and finding new ways to do this. And ultimately, it is not about us at a foundation or people in Washington solving this; it has got to come from the grassroots. But can we find better ways to empower the grassroots to come up with these types of solutions, which can then turn into policies and actions that we can implement?

Ms. CLARKE. Do you see closing that gap as something that is doable perhaps through the interconnectedness of social media, the Internet, and deployment of broadband to remote areas where perhaps it does not currently exist?

Mr. HWANG. I think it is part of it. I think new technologies are able to connect people who have not been connected before, but we have also seen increasing silos happen because of new technology. You see groups that tend to be more isolated than ever because they chat and tweet to each other rather than to others.

Ms. CLARKE. Double-edged sword.

Mr. HWANG. It is a double-edged sword. And I think one of those fundamental challenges is: how do we use technology in a way to nurture the very fabric that makes innovation happen and small businesses grow? I think that is an open question. And we are going to be looking at this issue closely and launching experiments. Last year we launched experiments in 12 organizations, totaling $4.3 million, through what we called the Kauffman Inclusion Challenge, into organizations across the U.S. trying to solve this issue of gender and racial barriers. We are going to be doing more of these and we are going to learn from that process.

Ms. CLARKE. Very well.

Quickly, just one question to Ms. Bland. Small employers must fight harder to attract and retain talented employees than their larger counterparts. Can you explain how the ability to offer healthcare benefits can help your business stay competitive?

Ms. BLAND. Yes. It is the single difference for me oftentimes when I am hiring between whether I get the first tier, very best in class employee, for instance, a pattern maker that I really wanted that I knew had the best skills in the industry. Her one caveat was she must have health insurance, and that was the difference. So at that time I actually put together a healthcare plan for my employees specifically so I could hire her and then extended it to them.

But again, there is so much in terms of overhead and regulations and everything that goes on in administering that plan. Sometimes it would be easier if there was an independent plan like the Affordable Healthcare Act where people can just go on a market and pick their own plan, especially if I do not have enough bandwidth as an employer to do the administration on that. You know?

Ms. CLARKE. Chairman, I yield back.

Chairman BRAT. Thank you very much.

The gentleman from Mississippi, Mr. Kelly, is recognized for 5 minutes.

Mr. KELLY. Thank you, Mr. Chairman. And thank you for such a distinguished panel.

My oldest son is a senior in college this year, and the share of entrepreneurs age 20 to 34 has declined from 35 percent in 1996 to 23 percent in 2013. I am hearing a lot of things. I had a small business. I ran my own law office. The question was not how much money I made that first year; it was how much I lost that first year and whether I could sustain to go into a second year, and that is truly. And I had a brand new baby about the age of yours, Ms. Bland, that my wife was also working, but she was putting more money into my business than I was, than we could afford. And so we had the same struggles and the same daycare that we could not afford, but she had to work. And so I understand those things.

But I say all that to say, being an entrepreneur and owning a small business is hard, and there is risk associated with that. And it is that great pioneer spirit of Americans who are willing to take a loss, to take a risk, to not be able to afford things that you want to do. Those are the things that made America great, will keep America great, and all those things.

So what can we do to spread the risk? Okay, make a level playing field so that all people, regardless of where they live or where they come from, so that all have an equal opportunity; not necessarily buy their risk, but at least make a level playing field so everyone else has, and especially in rural areas, which are much different.

And I think, Mr. Hwang, if you can start.

Mr. HWANG. Yeah, I appreciate your comments, especially on the pioneer spirit. Kansas City happens to be at the very edge of the frontier. That is where people gathered as they made the westward journey for 6 months into what was essentially no man's land at the time. And so the ability of people to organize resources in the pioneer spirit as they moved west is a great metaphor for the entrepreneurial spirit, which is how do you create something out of nothing?

As I think about how we level the playing field and spread the risk—as you were talking about your son in college—one issue is that the way we educate people today is on how to fill jobs, how to find jobs, as opposed to how to make jobs and make a living and survive. And I think to talk about that shift and how we teach people the skills for getting jobs, versus how you create something that did not exist before, is a big shift that cuts across so many aspects of society, including education.

So my personal feeling on this, and I think many in the Foundation share this, is this really cuts across many issues. It includes education policy. It is also the way we deal with capital allocation and capital resources, and policies and burdens that fall on entrepreneurs. I think the ability to honor the individuals, the pioneers, and to understand rules and laws that affect them, to understand the access issues they face is sort of flipping things upside down. We tend to focus on the top instead of the bottom. But when we think about entrepreneurs, we have got to focus on the bottom and what is it like to be in the situation when you started.

Mr. KELLY. Do any of the other panel wish to comment?

Ms. BLAND. At Manufacture NY, we have worked on a variety of innovative internships, apprenticeships, and workforce training programs specifically around blending, STEM training, and wearable technology with traditional manufacturing. And so I am a manufacturing wonk. But I think it can extend to other types of entrepreneurship, that we need to create training programs that work around people's schedules, work around their lives, that start a little earlier on. So while folks are still in high school, that they can start doing workforce training programs so that there is not a gap. Not everyone, you know, of course, we would love if everyone could go to college, but for some folks, particularly in the design and manufacturing industries, there might be a more hybrid program that is needed so that it is training them specifically for the career that they want to go into. And I think there is a lot to be explored in that area.

Mr. KELLY. Thank you.

And I think, Dr. Veuger, and I apologize, us southerners do poorly with names, you know, all the bright minds in Mississippi and in a lot of rural areas, they all want to go to law school. How do we encourage them to understand that maybe that is not the best way to use your talents to do that? How do we encourage that entrepreneur spirit at a young age so that they understand to have a 2-year degree but to be able to create something or build something is being much more successful than having a law degree, which I have, which I hope I never use again. But how do we create that as a Congress? How do we create that entrepreneur spirit, or can we?

Mr. VEUGER. Well, I think one specific remedy here is to make it less profitable to be a lawyer. I think limiting the disruptions caused by the Federal Government, of course, reduces the demand for lawyers to some extent. So I think that is a good place to start.

Mr. KELLY. Mr. Chairman, I yield back. Thank you.

Chairman BRAT. Mr. Kelly, that was outstanding. Thank you.

I do want to thank all the panelists, all the members here today. I think this really was great and the diversity of ideas across everyone who testified today, we really appreciate you all being here with us and sharing your perspectives.

I ask unanimous consent that members have 5 legislative days to submit statements and supporting materials for the record.

Without objection, so ordered.

This hearing is now adjourned, and thank you all very much.

[Whereupon, at 11:57 a.m., the Subcommittee was adjourned.]

APPENDIX

AMERICAN ENTERPRISE INSTITUTE

Statement before the House Committee on Small Business
Subcommittee on Economic Growth, Tax and Capital Access
On the State of the Small Business Economy

Policy Uncertainty and the Small-Business Economy

Stan Veuger
Resident Scholar

February 16, 2017

The Small Business Economy

The U.S. economy is still on the long way back to recovery from the 2007-2008 financial crisis. While conventional measures such as real GDP per capita have surpassed their pre-crisis peak, a number of weaknesses remains. Some of these are plausibly the result of the long and deep recession the country went through, while others are symptoms of more long-run trends. As an example of the former, the number of long-term unemployed workers is still significantly above its pre-crisis level. Weaknesses of the latter variety are arguably more worrisome, as there is no reason to believe that they will, with enough time, disappear.

Two examples of the latter are trends in levels of concentration within industries, and in entry of new firms. The former - illustrated by Figure 1 - suggests that small businesses have been losing ground in the US economy for quite some time now.

Industry	Revenue Earned by 50 Largest Firms, 2012 (Billions $)	Revenue Share Earned by 50 Largest Firms, 2012	Percentage Point Change in Revenue Share Earned by 50 Largest Firms, 1997-2012
Transportation and Warehousing	307.9	42.1	11.4
Retail Trade	1,555.8	36.9	11.2
Finance and Insurance	1,762.7	48.5	9.9
Wholesale Trade	2,183.1	27.6	7.3
Real Estate Rental and Leasing	121.6	24.9	5.4
Utilities	367.7	69.1	4.6
Educational Services	12.1	22.7	3.1
Professional, Scientific and Technical Services	278.2	18.8	2.6
Administrative/ Support	159.2	23.7	1.6
Accommodation and Food Services	149.8	21.2	0.1
Other Services, Non-Public Admin	46.7	10.9	-1.9
Arts, Entertainment and Recreation	39.5	19.6	-2.2
Health Care and Assistance	350.2	17.2	-1.6

Note: Concentration ratio data is displayed for all North American Industry Classification System (NAICS) sectors for which data is available from 1997 to 2012.
Source: Economic Census (1997 and 2012). Census Bureau.

Figure 1 Change in Market Concentration by Sector, 1997-2012. Source: Council of Economic Advisors (2016).

The latter – illustrated by Figure 2 – shows that perhaps as a consequence, or maybe as a cause, entry by new firms has been on the decline for quite some time as well. During this same period, as Figure 3 shows, something else happened: uncertainty surrounding economic policy was elevated compared to the preceding decades.

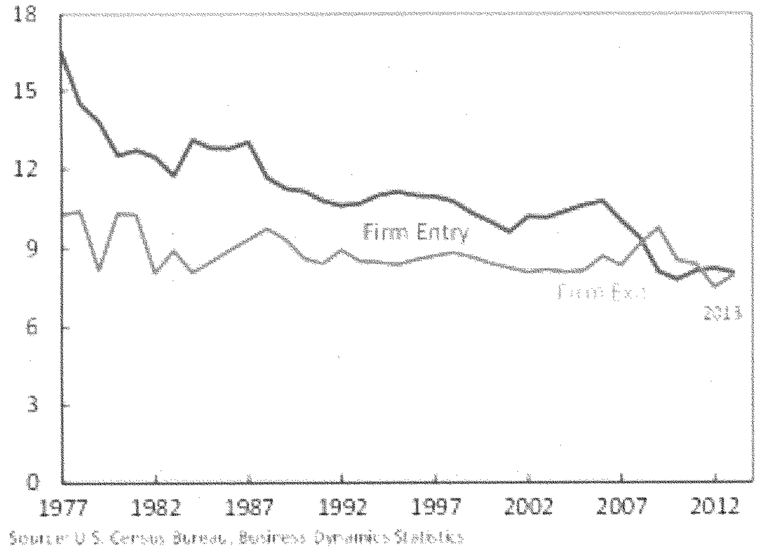

Figure 2 Firm Entry and Exit Rates, 1977-2013. Source: Council of Economic Advisors (2016).

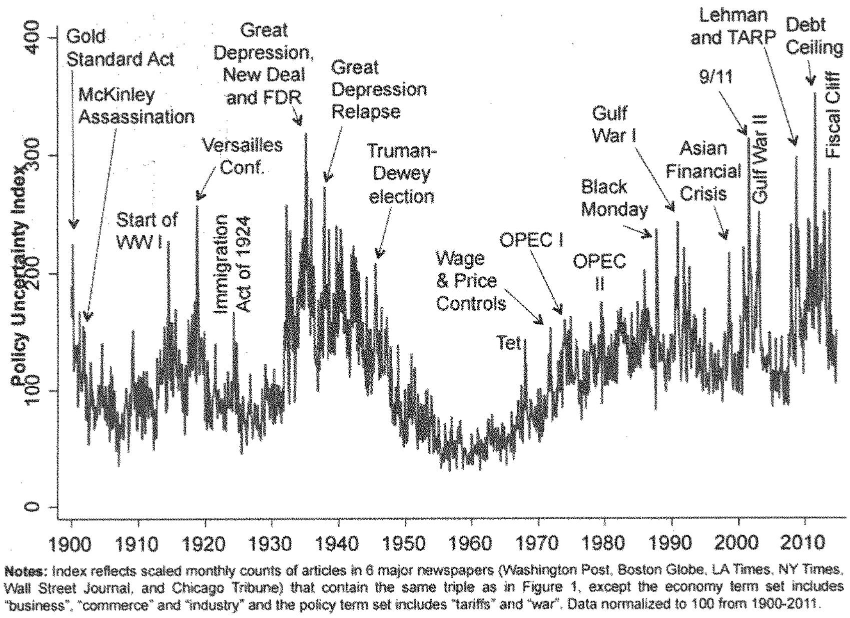

Figure 3 Uncertainty in the Long Run. Source: http://www.policyuncertainty.com.

Policy Uncertainty and Economic Performance[1]

A popular explanation for the significant duration of the 2007-2009 recession's recovery was the increase in economic-policy uncertainty during the period. Widely discussed in the popular news amidst analyses of the impact of Federal Reserve policy, health care reform, the rise of the Tea Party movement (see Madestam et al., 2013), debt ceiling disputes and state and federal spending levels, such uncertainty also received attention from researchers looking into its possible effects on the U.S. economy during the aftermath of the financial crisis.

Baker et al. (2016), for example, show that higher policy uncertainty from 2008 on was associated with a deeper and longer recession. In their analysis of news and government documents, Dominguez and Shapiro (2013) find that the political "stalemate" in the US contributed to the length of the recession, as did shocks from Europe. Similarly, Bachmann and Sims (2012) establish that consumer and firm confidence is of the utmost importance during downturns. Schaal (2011) is able to reproduce many of the dynamics of the Great Recession by introducing uncertainty shocks into a dynamic search model of heterogeneous firms, while Stock and Watson (2012) use a dynamic factor model to establish that heightened uncertainty worsened the recession significantly.

Moving away from the specific experience of the Great Recession for now, theoretical research has shown that policy uncertainty can affect consumption, investment (Rodrik, 1991) as well as broader economic activity (Bloom, 2009; Fernandez-Villaverde et al., 2015; Baker et al., 2016). While the foundations for believing that policy uncertainty can have negative effects on the broader economy have existed in the economics literature for some time (Friedman, 1968; Bernanke, 1983), recent research has introduced new ways to measure indicators of uncertainty, opening the door for empirical work. For example, Bertola et al. (2005) find that increased income uncertainty makes consumers postpone durable good purchases, while Julio and Yook (2012) examine corporate investment around national elections and find evidence that firms reduce investment when election outcomes are less certain. Baker et al (2016) develop a method for measuring policy uncertainty based upon newspaper coverage, expiring tax provisions, and economic forecaster disagreement, which has been used to examine past trends in policy uncertainty in the U.S. For example, Gulen and Ion (2012) use this index to show that policy uncertainty is negatively related to investment, both at the firm and industry levels, and that this uncertainty has had a substantial impact on corporate investment since the 2007 financial crisis. Meanwhile, Bachmann et al. (2013) use survey data to confirm that increases in uncertainty have a large and protracted impact on aggregate manufacturing production.

[1] This section draws heavily on Shoag and Veuger (2016) and earlier versions of that article.

All of these studies focus, in principle, on variation in uncertainty over time. In work with Daniel Shoag of Harvard (Shoag and Veuger, 2016), I seek to explain the cross-section of macroeconomic outcomes within the U.S. by studying policy uncertainty at the state level. We find that increases in local uncertainty over this period are strongly correlated with the effects of the recession, and that the correlation between uncertainty at the state level and employment losses is highly robust across alternate measures. While there is certainly a feedback loop between economic outcomes and uncertainty, we show that increases in local uncertainty are partially driven by preexisting state institutions, and that these pre-determined uncertainty amplifications cause unemployment increases.

Our baseline results suggest that if uncertainty levels in all states had been the same as those of the five states facing the lowest levels of uncertainty in 2009, they would have been associated with a national unemployment rate that was 0.8 and 1.2 percentage points lower. The key lessen from these findings is that, like structural change and demand driven channels, variation in policy uncertainty can partially explain the geographic pattern of the recession. Importantly, our results show that well-designed institutions and resilient public-sector operations can reduce policy uncertainty and produce better macroeconomic outcomes.

These various negative effects of heightened policy uncertainty are, if anything, of even more importance to small businesses. While economists often model firms as being risk-neutral, owned by a large number of shareholders with fully diversified portfolios, that is obviously not the case for the overwhelming majority of small businesses. As a consequence, small-business owners are likely to be more vulnerable to the risk induced by uncertain business environments. This makes it even more important for the committee to focus its attention on reducing policy uncertainty where that is possible.

Policy Uncertainty and the New Congress' Agenda

A number of the initiatives of the new Congress will be helpful in attaining this goal of creating more certainty about the business environment. The Small Business Regulatory Flexibility Improvements Act, for example, passed as a part of H.R. 5, the Regulatory Accountability Act, requires more careful consideration before new rules and regulations, demands that their impact on small business be considered more specifically, and mandates periodic of rules that significantly impact substantial numbers of small businesses. The HALOS Act, which also passed the House last month, is helpful on the other side of the ledger: by making it easier for startup firms to connect with angel investors and gain access to capital, the negative impact from heightened policy uncertainty will be somewhat dampened.

Despite measures like this, some measures of uncertainty have spiked since in the last few months. Figure 4, for example, shows that the Baker-Bloom-Davis monthly economic policy uncertainty index peaked in November to reach its highest level since August 2011, when the Eurozone crisis and arguments over raising the debt ceiling posed threats to economic stability, and has continued at an elevated level since.

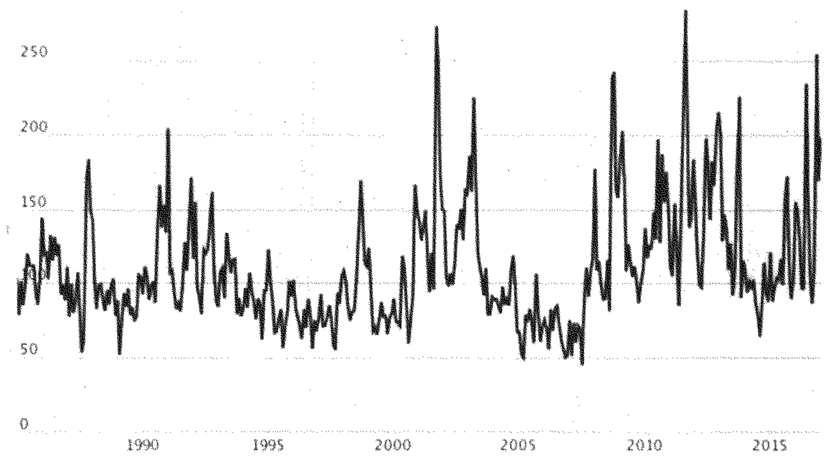

Figure 4 Economic Policy Uncertainty Index. Source: http://www.policyuncertainty.com.

Now, some of this can be attributed to the fact that we just recently had an election, and other potential uncertainty indicators – the VIX, for example - paint a different picture. That said, it does point to concerns about upcoming legislative and executive activity. For example, while repeal of the Affordable Care Act has long been a priority for Republicans, individuals and small businesses may worry about what would come next. Changes in immigration policy may induce uncertainty about the ability of startups to hire skilled employees. The recent executive order that imposed a travel ban on citizens of a number of Muslim-majority countries, including at least initially green-card holders, has left the over 10 million legal permanent residents in the country – owners, managers, employees, and customers of small businesses - wondering about their true status. Corporate tax reform, while long overdue and with the potential to add to potential growth and to improve the investment climate, will inevitably create winners as well as losers.

On the whole, James Madison's words in Federalist 62 still ring true today: "Great injury results from an unstable government. The want of confidence in the public councils damps every useful undertaking, the success and profit of which may depend on a continuance of existing arrangements. What prudent merchant will hazard his fortunes in any new branch of commerce when he knows not but that his plans may be rendered unlawful before they can be executed? What farmer or manufacturer will lay himself out for the encouragement given to any particular cultivation or establishment, when he can have no assurance that his preparatory labors and advances will not render him a victim to an inconstant government?"

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Testimony of Victor Hwang

Vice President of Entrepreneurship

Ewing Marion Kauffman Foundation

Before the

U.S. House Committee on Small Business, Subcommittee on Economic Growth, Tax and Capital Access

The Entrepreneurship Deficit

February 16, 2017

Chairman Brat, the Ranking Member and members of the Committee, thank you for the invitation to testify at this hearing about the small business economy.

I'm pleased to share some insights and recommendations from the Kauffman Foundation about the state of entrepreneurship in America. First, I'll describe the bad news. Then I'll share some good news. Finally, I'll talk about how we can address these challenges.

First, the bad news. America is suffering from an Entrepreneurship Deficit. It's slowly but surely eroding our quality of life and our national competitiveness.

I've personally experienced the challenges of starting and growing new businesses. My parents were entrepreneurs. For most of the past decade, I've been an entrepreneur and investor in Silicon Valley. And over the past year, I've gotten a "big picture" perspective as the head of entrepreneurship of the Kauffman Foundation, an institution that funds research on entrepreneurship, educates policymakers, and supports entrepreneurial success.

So what is causing this Entrepreneurship Deficit? Based on our work, we believe the deficit comes from a long-term decline in what economists call business dynamism, the pace at which firms start and grow. As a case in point, Americans are starting new businesses at roughly half the rate they were a generation ago.[1]

The implications of this deficit are profound. Recent economic research is starting to show how the Entrepreneurship Deficit is connected to some of America's biggest challenges: slow productivity growth, lower wages, stagnant job growth, and rising inequality. The data indicate that entrepreneurs create economic opportunities for others in society, like a circle in the water that ripples outward, in a continuing process that facilitates upward mobility. And each year, as our research suggests, the new and young businesses started by entrepreneurs create nearly all of the net new jobs in

[1] Haltiwanger, John. "Top Ten Signs of Declining Business Dynamism and Entrepreneurship in the U.S." NBER, August 2015.

our country.[2] Another recent report expands on the connection between the long-term decline in entrepreneurship and the effect on productivity and growth. That lackluster productivity drags wages and living standards down.

Put simply—fewer startups mean a lower quality of life for Americans.

But there's a gap between what we know and what we do. For the most part, entrepreneurs are left out of the policy debate. Our national discussions tend to fall along the same political fault lines of the past. Meanwhile, entrepreneurship remains far below what's needed.

The Three Megatrends

To make this case, I'd like to highlight some interesting new data. At the Kauffman Foundation, we have identified three megatrends that are reshaping entrepreneurship. We call these trends the New Demographics of Entrepreneurship, the New Map of Entrepreneurship, and the New Nature of Entrepreneurship. These trends present both challenges and opportunities to solving the long-term decline of entrepreneurship.

First, the New Demographics.

The U.S. population is increasingly becoming more racially diverse. Yet, the American entrepreneurial population does not reflect these changes. Today, 80.2 percent of American entrepreneurs are white and 64.5 percent are male.[3] That's a big gap for racial minorities and women. And it costs the country.

If minorities started businesses at the same rate as non-minorities, the United States would have more than one million additional employer businesses and as many as 9.5 million more jobs.[4] The persistent gender business gap has cost our country an additional 1.7 million businesses.[5]

The second megatrend is the New Map of Entrepreneurship.

The New Map is characterized by two things. First, entrepreneurship is increasingly an urban phenomenon. And second, entrepreneurial activity is growing outside the largest metropolitan areas traditionally associated with entrepreneurship—like Silicon Valley.[6]

Over time, America has become a more urban nation. Fewer people live in rural areas today than they did in the past. But for those Americans living outside our nation's largest cities, we need to ensure there is economic opportunity where they live. Entrepreneurship is part of the answer.

The final megatrend is the New Nature of Entrepreneurship.

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[2] Haltiwanger, John, Ron Jarmin, and Javier Miranda. "Who Creates Jobs? Small vs. Large vs. Young." NBER Working Paper, August 2011.

[3] Morelix, Arnobio, Victor Hwang, and Inara Tareque. "Zero Barriers: Three Mega Trends Shaping the Future of Entrepreneurship." Kauffman Foundation, February 2017.

[4] Ibid

[5] Ibid

[6] Ibid

Technology is changing everything, including entrepreneurship. In the past, as companies scaled their revenue, jobs could scale in almost the same fashion. That is no longer true and will be even less true in the future.

Take for example two businesses that were leading innovators in their day: Kodak and Facebook. In 1962, Kodak's sales first surpassed $1 billion dollars. At the time, Kodak employed 75,000 workers. When Facebook reached $1 billion in revenue in 2013, it employed about 6,300 workers.[7]

This is not exclusive to Facebook. This is only one example of what we know from research covering millions of companies and almost twenty years of data: the most innovative, high-productivity companies are not creating as many jobs as they did in the past.[8]

The State of Entrepreneurship

Now, some good news. Earlier this morning, the Kauffman Foundation held its eighth annual State of Entrepreneurship Address, where we assessed the health of American entrepreneurship and launched a new initiative to empower bottom-up change.

There is some positive movement on the short-term indicators. After a long hangover from the Great Recession, entrepreneurship is finally rebounding in the United States.[9] According to the Kauffman Index of Entrepreneurship Series, entrepreneurship is up across all three measures: new business creation, growth, and local small business activity.

Kauffman's Main Street Entrepreneurship Index, which measures local small business activity, is nearing a two-decade high, driven by a jump in small business survival rates. Today, almost half of all new businesses are making it to their fifth year of operation. This marks a major turnaround from the Great Recession, when business survival rates dropped to a low of 42.9 percent.[10]

While the recent uptick in entrepreneurship is indeed good news, it exists within the long-term decline I referenced.

Also concerning is the fact that new and young businesses today employ fewer workers on average than they used to. According to the Kauffman Main Street Entrepreneurship Index, small businesses have gotten even smaller over the last 20 years. The smallest of those small businesses—companies with one to four employees—make up 53.1 percent of all established small businesses.

Zero Barriers

[7] Morelix, Arnobio, Victor Hwang, and Inara Tareque. "Zero Barriers: Three Mega Trends Shaping the Future of Entrepreneurship." Kauffman Foundation, February 2017.

[8] Decker, Ryan, John Haltiwanger, Ron Jarmin, and Javier Miranda. "Declining Business Dynamism: Implications for Productivity?" Brookings Hutching Center on Fiscal & Monetary Policy, September 2016.

[9] Morelix, Arnobio, Victor Hwang, and Inara Tareque. "Zero Barriers: Three Mega Trends Shaping the Future of Entrepreneurship." Kauffman Foundation, February 2017.

[10] Fairlie, Robert, Arnobio Morelix, Inara Tareque, Joshua Russell, and E.J. Reedy. "2016 Kauffman Index of Main Street Entrepreneurship." Kauffman Foundation, November 2016.

As it becomes evident that the Entrepreneurship Deficit is one of America's biggest challenges, what can we do about it, and what can Congress do about it?

To start, we cannot afford to linger in the same debates and arguments of the past. The Entrepreneurship Deficit is causing hardships every day for people in your districts—fewer jobs, lower wages, and a lower quality of life.

As a response, the Kauffman Foundation today launched the Zero Barriers to Startup Challenge.

Our founder, Ewing Kauffman, believed that individuals have a fundamental right to take an idea they have and turn that into a business reality. To be an entrepreneur, you shouldn't need a formal degree. You shouldn't need expensive experts to navigate the process. It shouldn't matter your face, your gender, or where you live. You should be able to do it quickly, inexpensively, without confusion, and without barriers imposed by others.

Unfortunately, there is a big gap between that vision and today's reality.

The Zero Barriers to Startup Challenge is a collaborative, nationwide effort to identify barriers, big and small, that get in the way of new business creation. The Kauffman Foundation will team up with entrepreneurs, policymakers, and others nationwide to identify the key barriers to starting a business and then work together to identify and design solutions.

You can help people—current entrepreneurs and those with an idea afraid to make the leap—by engaging in this process. The Kauffman Foundation encourages members of Congress to host an "Entrepreneurs' Town Hall" in your district, to tour entrepreneur support organizations, and to invite entrepreneurs to testify before this committee and others about the barriers they face.

After listening to entrepreneurs, we encourage you to act on the solutions, conversation by conversation, city by city, district by district.

We also support continued public investments in data collection. The Kauffman Foundation was able to identify the three megatrends because data was available from the U.S. Census Bureau, the Bureau of Labor Statistics, and other federal agencies.

Access to timely, quality data is so important to understanding how we can best help entrepreneurs that Kauffman invested in the creation of the Census Bureau's Annual Survey of Entrepreneurs. This and other public data collection efforts need to continue.

When barriers hinder Americans from pursuing their entrepreneurial dreams, our whole nation suffers. That's no longer conjecture; there is accumulating research evidence for it. Together, let's commit to lowering barriers to entrepreneurship so all Americans, regardless who they are or where they're from, can turn their ideas into reality.

Thank you, and I look forward to answering your questions.

TESTIMONY BEFORE THE UNITED STATES CONGRESS
ON BEHALF OF THE

NATIONAL FEDERATION OF INDEPENDENT BUSINESS

NFIB
The Voice of Small Business®

Testimony of

Ms. Holly Wade,
Director of Research and Policy Analysis

before the

Committee on Small Business Subcommittee on Economic Growth, Tax and Capital Access

on the subject of

State of the Small Business Economy

on the date of

February 16, 2017

Good morning Chairman Chabot, Ranking Member Velázquez and members of the Committee on Small Business Subcommittee on Economic Growth, Tax and Capital Access. Thank you for the opportunity to testify today on "State of the Small Business Economy".

My name is Holly Wade, and I serve as the director of research and policy analysis for the NFIB Research Foundation. NFIB is the nation's leading small business advocacy association, representing members in Washington, D.C. and all 50 state capitals. Founded in 1943 as a nonprofit, nonpartisan organization, NFIB's mission is to promote and protect the right of its members to own, operate, and grow their businesses.

Small businesses are the bedrock of the U.S. economy with roughly 28 million small firms, of which, 5.8 million are small employers.[1] Small businesses account for about half of U.S. gross domestic output and about half of the private sector employment. Their contribution to the U.S. economy is vital to the creation a strong foundation for the middle class, offering job opportunities and contributing to their local communities. Small businesses provide goods and services in every market, in every geographic region, and throughout every demographic across the country.

General Small Business Conditions

Over the past 10 years, small-business owners have struggled to bounce back from the great recession. The economic recovery has been painfully slow for many, at first due to poor sales but quickly overtaken by issues related to taxes, regulations and the cost of health insurance.

NFIB's Small Business Economic Trends survey found small-business owners stuck in a below-average rut, with the survey's headline optimism index exceeding its 43-year average reading on a monthly basis only five times since July 2007, three of those recorded in the last three months.[2] Owners' optimism failed to materialize as average GDP growth remained relatively flat at 2 percent over the last eight years and government policies continued to increase the cost of doing business. In response to the combination of policy constraints and anemic GDP growth, few small-business owners find economic conditions supportive of investing in or growing their business and new business formation has languished.

The poor business climate is further exacerbated by heightened levels of economic and government uncertainty. NFIB's 2016 Small Business Problems and Priorities survey found that two of the top ten most severe problems affecting small-business owners are uncertainty related.[3] Uncertainty about economic conditions and government actions are ranked fourth and sixth out of 75 business problems, respectively, and about one-quarter of small-business

[1] Small Business Administration, Office of Advocacy, Frequently Asked Questions. https://www.sba.gov/sites/default/files/advocacy/SB-FAQ-2016_WEB.pdf

[2] Dunkelberg, William C. and Holly Wade, *NFIB Small Business Economic Trends*, Series, NFIB Research Foundation.

[3] Wade, Holly, *Small Business Problems and Priorities,* August 2016. NFIB Research Foundation.

owners find each a "critical" problem in operating their businesses. The Small Business Economic Trends Uncertainty Index also reached record high levels leading up to the 2016 presidential elections, all creating significant barriers to economic growth in the small-business sector.[4]

Post-election, small-business owner sentiment improved dramatically with more owners optimistic about the outlook for business conditions and business expansion. The rosier outlook has translated into more favorable expectations for sales growth and hiring to support expected gains in sales. As owners' confidence in the economy and economic policies rises, owners will be more likely to invest in and grow their business. Owners hold high expectations that Congress will now create a friendlier business climate for them to succeed.

Tax Costs and Complexity

The three main concerns of small business owners fore operating their businesses are: taxes, compliance and disruption costs of regulations and health insurance costs.

Small-business owners are inundated with a complex and costly tax structure that wastes their time and resources. According to NFIB's 2016 Small Business Problems and Priorities survey, five of the top ten most severe small business problems are tax related.[5] The adverse impact of federal taxes on business income ranks third out of 75 issues and is a "critical" problem for nearly three in ten small-business owners, important because profits are the major source of capital for growing their firms.

Tax complexity also creates major consternation among small-business owners. About 27 percent find tax complexity a "critical" problem, the fifth most burdensome issue. Because of the tax code's complexity, most small-business owners must use a tax preparer to file their business-related taxes to ensure compliance, an unnecessary cost to provide tax revenue to the government that "simplification" could eliminate.

Tax-related costs compete with owners' ability to use limited profits for primary business activities. Profits are the main funding mechanism for owners purchasing new equipment, expanding facilities, hiring and stocking inventory. Tax-related cost pressures are especially problematic for newer firms that almost solely rely on profits for operation and expansion costs as they are generally not able to access traditional lending sources. But regardless of the firm's age, tax burdens take a heavy toll on owners' ability to operate their businesses.

Regulatory Obstacles

Regulation is another area of angst for many small-business owners. One-third of small-business owners find unreasonable govern-

[4] Dunkelberg, William C. and Holly Wade, *NFIB Small Business Economic Trends,* Series, NFIB Research Foundation.
[5] Wade, Holly, *Small Business Problems and Priorities,* August 2016, NFIB Research Foundation.

ment regulations a critical problem in operating their businesses. Regulation is the second-most severe problem for small-business owners after the cost of health insurance. NFIB's newly released survey on regulations finds that while small-business owners are affected by every level of government, the federal government is the largest contributor to the problem for half of small employers. Another 30 percent are most affected by state-level regulations and 17 percent, local regulations.[6] Twenty-eight percent of small employers cite compliance costs as their biggest regulatory problem, followed by 18 percent most burdened by understanding how to comply with the regulations. Extra paperwork is the biggest regulatory problem for 17 percent of small employers. One of the many regulatory problems facing small employers is simply the volume of regulations they must comply with. The volume of regulations is the largest problem for 55 percent of small employers compared to 37 percent who are most troubled by a few specific regulations coming from one or two sources. The volume of regulations is important in that most small employers must take on the responsibility of learning about new government requirements themselves instead of delegating the task to an employee because their staff is too small.

Rising Cost of Health Insurance

Small-business owners rank the cost of health insurance as their most severe issue in operating their business out of 75 potential issues with 52 percent of small-business owners finding it a "critical" problem. The high cost of health insurance is the main reason owners do not offer employer-sponsored health insurance and the main reason owners discontinue providing the benefit. And for those offering health insurance, many owners annually confront the arduous task of adjusting profit expectations, insurance plans, cost-sharing and other mechanisms to help absorb often erratic changes in premium costs.

The rising cost of health insurance has forced many small employers to rethink the viability of offering health insurance to their employees. Since 2008, the offer rate for small businesses with less than 50 employees has dropped precipitously. Small-business owners are less likely to commit themselves to offering a long-term, high-cost benefit. The offer rate for this group has fallen 14 percentage points from 43 percent offering in 2008 to 29 percent in 2015.[7]

The small business health insurance tax credit was a targeted approach in the healthcare law to help curb health insurance costs for offering small employers and was intended to provide an incentive to start offering for those that do not. However, the tax credit was largely ineffective on both fronts as its design is exceedingly restrictive, complicated, and only offers limited and temporary relief to a larger small-business cost problem. The tax credit serves

[6] Wade, Holly, *Regulations,* NFIB National Small Business Poll Series, February 2017, NFIB Research Foundation.
[7] U.S. Department of Health and Human Services, Agency for Healthcare Research and Quality, Medical Expenditure Panel Survey, series.

as a windfall for the few who qualify and take the time, or pay an accountant, to file for it.

Small Business Financing

Small business's ability to access financing is a vital component of a healthy small-business sector. Small businesses rely on financing for general business operations but also expansion activities and reinvestment. But since the recession, loan demand remains historically weak, even with record low interest rates still available. Historically high numbers of firms remain on the "credit sidelines", seeing no good reason to borrow over the past eight years. However, if the positive expectations for real sales and business conditions of the last three months are translated into actual spending on capital equipment, expansion and inventory investment, borrowing activity should pick up. NFIB does have concerns about small business access to financing as the economy picks up with fewer small and regional banks available to them. Small-business owners are often more successful accessing credit through smaller banks, and it is yet unclear whether bank consolidation will have a significant impact on small business lending.

Conclusion

NFIB hears from small-business owners year round about the various challenges they face operating their business. The primary step in developing pro-growth policies is to first, "do no harm', especially when it comes to artificially increasing the cost of doing business whether in the form of higher taxes, health insurance costs or more regulations, to name a few. Small-business owners are in great position to invest in and grow their business given the right set of policies. Most attention must be paid to the benefits of regulation that use up valuable human and financial capital.

I appreciate the opportunity to discuss the current state of the small-business economy and the challenges it faces going forward. I look forward to working with the Committee to support small businesses and strengthen the U.S. economy.

MANUFACTURE NEW YORK

State of The Small Business Economy
Testimony - Bob Bland
Co-Chair, Women's March on Washington
CEO + Founder of Manufacture New York

Members of Congress, thank you for convening this session on the State of the Small Business Economy, and to all representatives who share a tireless commitment to retaining equitable opportunities for working and middle-class small business owners and their families.

My name is Bob Bland, and I am the CEO & Founder of Manufacture New York, and the Co-Chair of the Women's March on Washington. Five years ago, I founded Manufacture New York as a 29 year old female designer, entrepreneur & young mother with a vision of an inclusive, sustainable 21st century apparel & textile industry where collaboration & colocation of local talent provided the engine for truly revolutionary leaps forward in domestic manufacturing.

Since the Great Recession, virtually all small creative & manufacturing businesses in New York City have had the same challenges—access to affordable industrial space with long term leases, relocation grants for those who are displaced, affordable housing within a reasonable commuting distance, low interest working capital & lines of credit to grow our small businesses, and competitive equipment procurement and training programs so that we can adapt to a rapidly changing global landscape.

Fashion design & manufacturing jobs are more than just jobs—they are an inclusive pathway to meaningful careers and the potential for business ownership, regardless of previous educational background or socioeconomic status. With an average salary of $59,000, they are more likely to include benefits and have a clear path for growth, both in terms of skills training and opportunities to advance. The New York City fashion ecosystem is a unique creative and dynamic cultural powerhouse that touches lives internationally on a daily basis.

While in 1931, New York City's iconic Garment District was home to the highest concentration of apparel manufacturers' in the world, employing 1 million locals at its height, it has since contracted to 15,000 total apparel manufacturing jobs in the city, which contextually, still accounts for 30% of all New York City manufactures. This can look like a bleak picture, but we would are sitting on several global opportunities for significant job growth in NYC at the intersection of fashion, sustainability and technology if we seize the moment.

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www.manufactureny.org

New York City is home to 900 fashion company headquarters, employs 180,000 people and pays $11B in wages and $2B in tax revenue annually. From the smallest emerging design startups to the largest department stores and luxury conglomerates, Manufacture New York has experienced significant interest in the conceptualization, research, development and commercialization of a shared set of resources and best practices to capture value and provide accountability at all stages of our supply chain.

New York City has a unique proximity to a talented, experienced and passionate workforce; headquarters of major brands and media outlets in web, print, television and radio; and the emergence of Silicon Alley as a hotbed for VC funding of related technology companies. From biomaterials (Modern Meadow) to wearable technology (Ringly) to the connected devices revolution known as the Internet of Things (IoT), major 21st century manufacturing opportunities for New York City exist where fashion (apparel, textiles, footwear, jewelry, home goods) collides with previously distant sectors like consumer electronics, health care, transportation and defense.

Since Superstorm Sandy decimated our working waterfront, unemployment, under-employment and lack of sector-specific skills training remains a major barrier for economic prosperity in South Brooklyn, particularly among 18-24 year olds who are just entering into their professional lives and older residents looking for opportunities in new, growing businesses. We must work inclusively with community stakeholders and local partners to develop entirely new types of internships, apprenticeships and workforce training programs that blend STEM training in wearable technology and material science with apparel and textile manufacturing so that together, we can create a fresh start for urban manufacturing and new generation of leaders in entrepreneurship & innovation.

The Obama Administration worked diligently to establish a national network of Manufacturing Innovation Institutes ("MII"), and we look forward to participating in future institutes, as these sort of public-private partnerships are essential to long term innovation and job opportunities in advanced manufacturing. The United States lost 40% of our middle class jobs nationally during the 30-year exodus of domestic manufacturing, and it will take significant, sustained public and private investments across administrations, with all key stakeholders working together, to restore our prosperity and economic security as a nation. We urge Congress to continue funding and growing these programs.

In August 2016, Senator Kirsten Gillibrand announced the bipartisan Made in America Manufacturing Communities Act. In order to earn the "Manufacturing Communities" designation, communities would demonstrate the significance of manufacturing in their region and develop strategies to utilize their "Manufacturing Communities" designation in making investments in six areas:

- Workforce training and retraining;
- Advanced research;
- Infrastructure and site development;

- Supply chain support;
- Promotion of exports and foreign direct investment; and
- Operational improvement and capital access for manufacturers that supports energy or process efficiency, equipment or facility upgrades, or the development of business incubators, among other activities.

Senator Gillibrand's bipartisan legislation is cosponsored by Senators Mark Kirk (R-IL), Jerry Moran (R-KS), Richard Blumenthal (D-CT), and Christopher A. Coons (D-DE), and a bipartisan House version was introduced by U.S. Representative David Cicilline (D-RI), Richard Hanna (R-NY), Tom Reed (R-NY), Tim Ryan (D-OH), John Katko (R-NY), Cheri Bustos (D-IL), John Garamendi (D-CA), and Lloyd Doggett (D-TX), We urge the House of Representatives to move this legislation forward and make the Manufacturing Communities program a permanent incentive for Made In USA small business growth.

Manufacture New York also advocates for a healthy domestic manufacturing sector at large. Not only do manufacturing jobs pay better than comparable service jobs, but they currently provide skilled work for roughly 12 million Americans.

Domestic manufacturers object to NAFTA & TPP-style trade agreements that not only outsource American manufacturing jobs to low-wage, unregulated countries, but they offer little in the way of oversight for overseas labor conditions.

Our objections to this trade deal include the fact that TPP countries like Vietnam are known for ongoing labor and human rights abuses. It's questionable whether TPP labor standards can actually be verified or enforced in such countries.

Additionally, free trade agreements like TPP do not include enforceable provisions to prohibit currency manipulation. Deliberate currency undervaluation by America's trading partners has cost the U.S. millions of jobs over the last two decades. TPP would have also gut Buy America provisions in U.S. law by allowing firms in any TPP country to bid on U.S. procurement, including Chinese state-owned firms located in Vietnam. Thus, U.S. tax dollars for apparel and textiles could go to China instead of to U.S. producers.

Made In USA manufacturing is the backbone of the innovation economy, giving creatives + technologists the tools to commercialize their ideas and create new startups that fuel job growth in our NY metropolitan region and across the country.

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