

Congress of the United States
U.S. House of Representatives
Committee on Small Business
2361 Rayburn House Office Building
Washington, DC 20515-6515

MEMORANDUM

To: Members, Small Business Committee
From: Nydia M. Velázquez, Chairwoman
Date: February 11, 2019
Re: Full Committee Hearing: “Small Business Priorities for the 116th Congress”

On Wednesday, February 13 at 11:00 a.m. in Room 2360 of the Rayburn House Office Building, the Committee on Small Business will hold a hearing entitled “Small Business Priorities for the 116th Congress.” The purpose of the hearing is for small business owners to outline their priorities and provide the Committee with ideas about federal policies that will help them most grow their businesses. A priority setting hearing, the hearing will help inform future committee hearings, advocacy efforts, and legislative priorities for the Committee on Small Business for the 116th Congress. Witnesses will include:

- Mr. John Arensmeyer, Founder & CEO, Small Business Majority
- Ms. Sabrina Parson, CEO, Palo Alto Software
- Mr. J. Kelly Conklin, Co-Owner & Founder, Foley Waite LLC
- Mr. Thomas M. Sullivan, Vice President, Small Business Policy, Chamber of Commerce

Access to Capital

Entrepreneurs and small businesses consistently report access to affordable capital is essential for starting a small business, hiring employees, and expanding operations. As a result, understanding the link between capital availability and firm growth is essential. Without adequate access to funding, small firms often fail to realize their full potential, which inhibits growth in local communities and local economies. The challenges accessing both venture capital and traditional loans are similar for many small business owners and a variety of factors account for funding discrepancies. A growing number of studies indicate that limited financial, human resources, and awareness are responsible for these disparities in lending.

To help fill this void in the capital markets, Congress created several programs within the SBA, including the 7(a), 504 program, and the SBIC program. SBA programs are an important means through which small businesses access capital. Through public-private partnerships that share the lending risk, small businesses are able to tap into capital that is both affordable and accessible. SBA currently offers lending products designed for businesses at various stages of growth. SBA’s flagship lending product is the 7(a) loan guaranty program. Under this program, banks and other financial institutions make loans to small businesses that are subsequently partially guaranteed by SBA. The 504/Certified Development Company loan guaranty program uses CDCs, which are private, nonprofit corporations established to contribute to economic development within their

communities. The program provides long-term, fixed rate loans for major fixed assets such as land, structures, machinery, and equipment. Program loans cannot be used for working capital, inventory, or repaying debt. The Microloan program provides direct loans and grants to qualified non-profit intermediary microlenders who in turn, provide microloans of up to \$50,000 to small businesses. Microloan lenders also provide marketing, management, and technical assistance to Microloan borrowers and potential borrowers. Finally, SBA is currently administering the Community Advantage (CA) pilot program, which provides mission-based lenders access to 7(a) loan guaranties as high as 85 percent for loans up to \$250,000. Lenders also have access to SBA's network of enhanced management and technical assistance.

Besides the SBA programs, small firms can turn to venture capital (VC) for assistance. VC represents one type of equity investment in operating companies that are not publicly traded on a stock exchange. Because it is equitable in nature, VC investment is typically focused on early-stage, high-potential growth companies in the interest of generating a return through an eventual realization event such as an IPO or trade sale of the company. Venture capital is most attractive for new companies with limited operating history that are too small to raise capital in the public markets and too immature to secure a bank loan or complete a debt offering. However, VC investments tend to flow more towards male-owned businesses. In fact, of the \$85 billion VC invested in 2017, women-owned ventures received only 1.9 percent and received smaller average deal sizes when compared to men – 5 percent and 12 percent respectively.¹ Members will hear what more can be done to ensure small businesses are receiving access to capital and where improvements can be made. Finally, the hearing will offer an opportunity to gain greater insight in alternative methods of capital access and where there is a need for more clarity and oversight of small business lending.

Taxes

Overhauling the federal tax system has been and is still one of the most important legislative issues for small businesses. Addressing the tax code to promote growth and fairness in addition to making it simpler helps to steer business investment, job creation, and consumer spending. Tax policy plays a significant role not just for the economy as a whole but also for small firms. The current tax code offers small firms many advantages but it also remains a confusing and complex system.

The proliferation of changes to the tax code has become more common in recent years. In nearly every year since the 1986 tax reforms, Congress has enacted some type of tax code change. The constant reforms to the tax code on a near annual basis have consequences beyond the changes in credits, deductions, and small business expenses. It hinders small employers in their business planning and puts them in a position to make business decisions with little knowledge of what the future tax consequences will hold. For businesses that want to take advantage of new incentives, they must also spend resources to ensure they can claim newly created tax incentives. By simplifying the tax code, owners will save money immediately on less compliance costs, making it easier to invest in the business and employees.

The tax law passed in December 2017 often referred to as the Tax Cuts and Jobs Act, P.L. 115-97, raised more questions for taxpayers due to a sense of greater complexity. Much of the uncertainty

¹ Valentina Zarya, *Female Founders Got 2% of Venture Capital Dollars in 2017*, Fortune, Jan. 31, 2018, available at <http://fortune.com/2018/01/31/female-founders-venture-capital-2017/>.

created by the law was caused by the 20 percent deduction under Section 199A because the Internal Revenue Service (IRS) did not release proposed regulations until August 2018. The complexity regarding that specific provision surrounds who can claim the deduction and how much they can claim. There are many nuances and limitations a small business owner must be aware of in order to properly comply with the new law and to do so, many owners are turning to tax professionals for assistance. The hearing will give Members the opportunity to learn more about the tax law passed in December 2017 and what it means for small business taxpayers.

Retirement

The primary manner by which Americans secure retirement income beyond Social Security is through their employer. Retirement security not only insures against life's uncertain events, but it also adds to the nation's economic stability by helping secure the income and welfare of American families. Perhaps no other issue is more important to the nation's future than whether people will be adequately prepared for retirement. And yet, the country is faced with a number of challenges that cast doubt on whether the current population of working Americans will have sufficient resources to fund their expected retirement.

Complicating retirement plans is the fact that for the last several decades, the rate of personal savings in the United States has followed a steady downward trend. While retirement account balances have increased to prerecession levels, the recession left many workers uncertain of their future retirement plans and student loan debt is currently a burden upon many workers entering the workforce. What became clear in recent years is the importance of retirement security for millions of Americans.

Retirement coverage affects every American but additional steps need to be taken to ensure small business owners, nonprofits, and their employees are not forgotten. Thirty-five percent of private sector workers do not have access to retirement plans—either defined contribution plan or a defined benefit plans—through their employer.² This figure is even higher for millennials, totaling 41 percent.³ While operating on the margins, small businesses rely on benefits to hire and retain quality employees. It is for these reasons that small business retirement plans are instrumental to the health of the nation's economy and to ensure retirement security for the nation's workers.

There are three broad types of retirement plans that small businesses may offer their workers – 1) defined benefit plans (DB); 2) defined contribution (DC) plans; and 3) individual retirement accounts (IRA) based plans. Over the years, Congress has responded to concerns about lack of access to workplace retirement plans for employees of small businesses with legislation to lower costs, simplify requirements, and ease administrative burdens. This hearing will educate Members on the challenges facing small business owners and the importance of Congress taking action to improve the retirement system.

Infrastructure

² Pew Charitable Trust, RETIREMENT PLAN ACCESS AND PARTICIPATION ACROSS GENERATIONS (2017), available at https://www.pewtrusts.org/-/media/assets/2017/02/ret_retirement_plan_access_and_participation_across_generations.pdf.

³ *Id.*

The framework of physical and communications networks supports the flow of commerce and ensures the country remains an advanced industrial nation, making it imperative to have a reliable and modernized system. The nation's competitiveness in productivity levels, global industry, and innovation depends upon a strong infrastructure system because it provides the underpinning for businesses to buy, sell, and make their products or services. In the long term, plans must be in place to develop and maintain the framework of our economy that provides for stable transportation, communication, and information.

The infrastructure system has served as a critical role in spurring growth throughout the country's history. Early transportation systems, including canals, turnpikes, and railroads allowed commerce and people to spread across the country. Industries advanced as regions gained comparative advantage and could trade their products for other goods. Early electricity networks increased the speed and ease of communication, provided the technologies for many innovations, and serve as primary energy sources for most homes and businesses. Water supplies and sewage systems allow communities to accommodate large populations and maintain high a standard of living.

Infrastructure is considered a major component of the nation's economy and therefore a prime factor for an economic development strategy. In 2015, all modes of transportation moved an estimated 18.1 billion tons of goods worth about \$19.2 trillion on our Nation's transportation network. On a daily basis, 49 million tons of goods valued at more than \$53 billion are shipped throughout the country on all transportation modes.⁴ In addition, nearly 13 million Americans, approximately nine percent of the U.S. workforce, are directly employed by transportation related industries.⁵ In 2015, Americans drove 3.1 trillion miles commuting to and from work and conducting other activities.⁶ As such, it is imperative to link long term economic growth with federal infrastructure investments.

Long Term Economic Impacts of Infrastructure Investment

Investment in infrastructure promotes future economic opportunities. Employment is linked to the existence of these systems, as efficient supply systems reduce business operation and labor costs. These are in direct employment, such as contracting and road design as well as indirect jobs, such as through new retail developed as a result of road enhancement. In fact, 61 percent of the jobs directly created by investing in infrastructure would be in the construction sector, 12 percent would be in the manufacturing sector, and 7 percent would be in retail trade, for a total of 80 percent in these three sectors.⁷ Nearly 90 percent of the jobs in the three sectors most affected by infrastructure spending would be middle class jobs, defined as those paying between the 25th and 75th percentile of the national distribution of wages.⁸

⁴ U.S. Department of Transportation Bureau of Transportation Statistics, DOT RELEASES 30-YEAR FREIGHT PROJECTIONS (2016), available at <https://content.govdelivery.com/accounts/USDOT/bulletins/1395ec8>.

⁵ U.S. Department of Transportation Bureau of Transportation Statistics, TRANSPORTATION IN THE UNITED STATES: HIGHLIGHTS FROM 2015 TRANSPORTATION STATISTICS ANNUAL REPORT (2015), available at https://www.bts.gov/archive/publications/transportation_in_the_united_states_2015/index.

⁶ U.S. Department of Transportation, U.S. DRIVING TOPS 3.1 TRILLION MILES IN 2015, NEW FEDERAL DATA SHOW (2016), available at <http://www.trb.org/Main/Blurbs/171953.aspx>.

⁷ *Id.*

⁸ *Id.*

Businesses benefit from reduced production costs due to infrastructure investment. Economies of scale are created through small individual contributions that result in substantial capital facilities and networks. These systems substantially reduce the cost of operations for individual firms. Spending is further stimulated through these systems as transportation, communication, and information allows for efficient transactions. This is largely a result of increasing consumers' access to information, new products, and retail locations through a robust infrastructure system. International trade is one substantial area for economic growth, allowing for businesses to access larger market shares. To facilitate these transactions, not only are roads and airports critical, but also the interconnections linking them, such as distribution facilities and ports. Finally, new technological advancements, such as drones, need to be considered to modernize and remain competitive. Members will hear from witnesses about how critical a comprehensive infrastructure package is to grow the economy and give more entrepreneurs the ability to compete in global economy.

Rural Small Businesses and Investments

Rural small businesses and entrepreneurs face a host of unique circumstances that differ from their urban or suburban counterparts. For instance, rural areas continue to get older and depopulate. This is due to net outmigration by young people to urban areas as they seek greater educational and economic opportunities in our larger cities, with many individuals never returning. In fact, one-third of older-age counties are classified as persistent population-loss counties, much of which can be attributed to outmigration of young people.⁹ The net outmigration in rural areas leads to issues regarding workforce availability, small business creation, among others.

Workforce Development

Of the most pressing issue is a decline the mismatch between skills and available jobs, which has caused high than average rates of unemployment, and underemployment and subsequent despair in rural America. Employment opportunities in traditional sectors, such as construction, manufacturing, and resource-heavy industries, have steadily declined over the last several decades, necessitating the need for new workforce and entrepreneurship development opportunities that can spur growth. Encouraging a more collaborative effort through public-private partnerships and removing the barriers preventing a skilled workforce from remaining in rural communities are just two methods by which lawmakers can take. The hearing gives witnesses the opportunity to discuss the many ideas to improving workforce gaps in rural America.

Digital Divide

While technological advancements are making it easier for small businesses to operate and be competitive in today's economy, there is a comparative disadvantage for businesses operating in geographically hard to reach and sparsely populated parts that do not have access to the same connectivity as their counterparts in urban area. In fact, 12.6 million Americans are still lacking broadband access,¹⁰ making broadband buildout a top priority for small businesses all across the nation. The lack of access to broadband internet means our nation's rural residents are losing out on optimized efficiency in the realms of health care, education, energy, agriculture, and commerce.

⁹ U.S. Department of Agriculture, RURAL AMERICA AT A GLANCE 2018 EDITION (2019), available at <https://www.ers.usda.gov/webdocs/publications/90556/eib-200.pdf?v=5899.2>

¹⁰ Nick Corasaniti, *In New York, Bringing Broadband to Everyone by 2018*, The New York Times, Mar. 20, 2017, available at <https://www.nytimes.com/2017/03/20/nyregion/new-york-broadband-cuomo-internet.html>.

Although the lack of broadband access is one of the prime challenges facing rural communities, it also represents the biggest opportunity given the economic value-add to main street businesses and consumers. A 2016 report published by the Hudson Institute in conjunction with the Foundation for Rural Service found that investment by rural broadband companies contributed almost \$25 billion to the economies of the states in which they operated in 2015.¹¹ Of this, \$8.3 billion benefitted rural areas proving the need to include broadband modernization and build-out in an infrastructure plan. Members of the Committee will learn more about the opportunities broadband holds for small businesses across America.

Conclusion

New businesses play a vital role in both economic impact as well as job creation. These firms operate across the full spectrum of industries, providing a wide range of opportunities to generate high levels of economic and employment growth. With entrepreneurship and small business formation rates falling, it is important that we hear from the small businesses and take the necessary steps to increase opportunities for those in rural and urban America. The hearing will provide Members with an overview of the policy priorities of small business owners as they set the agenda for the 116th Congress.

¹¹ The Hudson Institute and The Foundation for Rural Service, THE ECONOMIC IMPACT OF RURAL BROADBAND (2016), <https://www.hudson.org/research/12429-hudson-institute-releases-report-on-economic-impact-of-broadband-in-rural-communities>.