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Economists Overshadow Cherry Blossoms

It wasn't just the famed cherry blossoms that had Americans visiting Washington this spring. While some came for the blossoms, an equally enthusiastic group came to listen to the renowned small business economists, experts, and policymakers featured at the Office of Advocacy's Entrepreneurship in the 21st Century conference.

The presence of two television networks, a live radio show, film crew, and almost a dozen print reporters added to the aura of importance and excitement surrounding the event. Participants were not disappointed, as each of the panels and speakers presented an in-depth analysis of the importance of small business to the American economy now, and in the future.

Co-sponsored by the Ewing Marion Kauffman Foundation, the conference offered the latest research into the role small business plays in the economy. (Visit www.sba.gov/advo for videos of each session.) Panels addressed topics from the economic role small business plays, the changing demographics of ownership, and the small business contribution to technological innovation, to trends in finance and government policymaking.

Several themes emerged from the conference. First, new, innovative entrants play a critical role in maintaining the United States' competitive economic balance and provide the tools for economic development in local communities.

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Chief Counsel for Advocacy Thomas M. Sullivan at a working lunch with Hispanic business leaders during a recent visit to Dallas, Arlington, and Fort Worth, Texas.

Advocacy's RFA Training Efforts Continue

by Claudia Rodgers, Senior Counsel

Since July 2003, the Office of Advocacy has trained staff at 20 federal agencies on compliance with the Regulatory Flexibility Act (RFA) as required by Executive Order 13272. Employees come to the training with varying levels of expertise with the RFA, even though it has been in existence since 1980. Some are very familiar with the law's requirements, while others are unaware of what the RFA requires an agency to do when promulgating a regulation.

The three-and-a-half hour session includes group exercises in which participants review regulatory scenarios for their small business impact and critique mock regulatory flexibility analyses. By the end of the course there are many revelations and excited faces as agency employees better understand what they have to do to comply with the RFA and that the Office of Advocacy wants to help them along the way.

One important theme emphasized throughout the RFA training is for the agency to involve Advocacy early in the creation of a

regulation. We encourage agencies to work closely with our office and to seek our input in their determination of whether or not a draft rule will have a significant economic impact on a substantial number of small businesses. Agencies frequently make mistakes when making this determination. The training session helps explain the steps involved in reaching that decision. Another important theme reiterated during the training session is that agencies should "do it right on the front end" to avoid legal hassles and delays for noncompliance with the RFA after a rule is finalized. In addition to avoiding legal challenges, by considering the impact of their regulations on small business from the beginning, agencies are more likely to promulgate a rule that is less burdensome on small businesses and that results in better compliance.

In the course of training, several questions repeatedly come up. These questions address some of

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The Small Business Advocate

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The Small Business Advocate (ISSN 1045-7658) is published monthly by the U.S. Small Business Administration's Office of Advocacy and is distributed to Small Business Administration field staff and members of the U.S. Congress. *The Small Business Advocate* is available without charge from the Office of Advocacy, U.S. Small Business Administration, Mail Code 3114, Washington, DC 20416.

Send address changes to: *The Small Business Advocate*, Mail Code 3114, U.S. Small Business Administration, Washington, DC 20416. Include your current address label.

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Ten Frequently Asked Questions about the RFA

In the course of training, participants have repeatedly raised several questions. These questions address some of the more challenging parts of rule analysis, as well as areas that are commonly misunderstood. Many of them continue to pose problems for agency regulators.

1. What is the difference between direct and indirect impact?
2. Define "substantial number" and "significant economic impact."
3. Does an agency have to consider a rule's impact on international firms doing business in the United States?
4. How soon must an agency notify Advocacy after certifying a rule?
5. Does an agency have to choose the alternative that gives the most relief to small business?
6. Under what circumstances do interim final rules and direct final rules require an interim regulatory flexibility analysis (IRFA) or final regulatory flexibility analysis?
7. Is an IRFA required when the small business impact is positive?
8. Does Advocacy ever file an *amicus curiae* brief on behalf of an agency?
9. Where can an agency get small business data?
10. If the rule does not require notice and comment under the Administrative Procedure Act, does the RFA require it?

Message from the Chief Counsel

EPA Listens to Small Business Concerns on Construction and Development Water Quality Rule

by Thomas M. Sullivan, Chief Counsel for Advocacy

Once again, I had the opportunity to see how the Regulatory Flexibility Act (RFA) makes a difference for small business. On March 31, the U.S. Environmental Protection Agency (EPA) listened to small business and decided not to impose costly and largely duplicative new water quality requirements on construction and development sites. EPA based its decision in part on the comments and concerns raised by small construction companies and other small businesses.

EPA's Construction and Development (C&D) effluent rule was designed to curb pollution from storm water runoff at construction sites. As originally conceived, however, the draft proposed rule would have carried a price tag of almost \$4 billion per year, and its new requirements would have overlapped with existing storm water programs. There was even concern that the C&D proposal would damage ongoing state and local efforts to control runoff.

Fortunately, small business had a voice in the rulemaking process because of the 1996 amendments to the RFA, known as the Small Business Regulatory Enforcement Fairness Act (SBREFA). Under

SBREFA, EPA is required to convene a panel to formally consult with small businesses prior to issu-

“The panel recommended that EPA not impose the C&D requirements, and focus instead on improving public outreach and education about existing storm water rules, while doing a better job of enforcing those rules.”

ing a proposed rule. Small business owners volunteered their time to discuss the draft proposed rule and offer other options. After carefully evaluating cost and benefit data, the small business advocacy review panel concluded that the C&D requirements would add substantial complexity and cost to current storm water requirements, without a corresponding benefit to water quality. The panel recommended that EPA not impose the C&D requirements, and focus instead on improving public outreach and education about existing storm water rules, while doing a better job of enforcing those rules. EPA published a proposed rule that included

the options recommended by the panel.

In issuing its final decision not to go forward with the C&D rule, EPA properly followed the panel's advice. As a result, EPA correctly decided not to burden state regulators, construction firms, and the public with unnecessary, duplicative new federal requirements. EPA deserves the praise they get for listening, understanding, and acting. EPA's decision is right for small business, right for the environment, and right for the American people.

The experience of the C&D rule shows how going through the RFA's small business analysis can help an agency arrive at a better regulatory decision. SBREFA was enacted by Congress in recognition of the unique nature of small business and its importance in our economy. The diversity of small businesses means that one-size-fits-all regulatory proposals often only add new burdens without new benefits. By listening to the concerns of small business about the draft C&D proposal, EPA was able to understand and do what was best for all of the interests involved.

RFA Training, from page 2

the more challenging parts of rule analysis, as well as areas that are commonly misunderstood. (See box.) By addressing these and other important issues, the training helps agency regulators come to a better understanding of the work that needs to be done to comply with the RFA.

While it will take time to change the culture at many of the agencies, Advocacy's RFA training is already having an impact on the way agencies approach rule development. Agencies that have participated in RFA training are now engaging Advocacy earlier in the process, sending us draft documents, and recognizing that Advocacy can help

them locate small business data. With RFA training sessions planned for the 66 federal agencies and departments on Advocacy's priority list, we will begin to see more regulations written with an eye toward their impact on small entities.

Economic News

ICIC Champions Downtown Entrepreneurs

Why shouldn't business flourish in central cities? That's the attitude of the Initiative for a Competitive Inner City, or ICIC, based in Boston. Once the site of this country's economic engines, central inner cities gradually lost people, jobs, and wealth as Americans dispersed to the suburbs in the latter half of the 20th century. Now, this innovative organization is calling attention to the fast growing businesses that are bucking the trends of recent decades and flourishing in our nation's downtowns.

At its recent Inner City 100 Awards, ICIC recognized 100 fast-growing inner city companies. Leading the pack was the innovative Baltimore firm, 180s, which specializes in performance athletic wear. The firm has grown more than one hundred-fold since 1998 and ranks high on national lists of companies to watch.

The pool of entries reflects the vitality of inner city business. This year, 7,500 companies were nominated for the list, up from 215 in 1999, the year the awards began. The 2004 nominees represented 155 cities, and winning companies were based in 55 cities. Chicago and Boston had the most winners with six each, followed by Rochester with five, and El Paso and New York with four.

To be considered for the list, companies need to have at least 51 percent of operations located in economically distressed urban areas; have 10 or more employees; and have a five-year operating-sales history that included sales of at least \$200,000 in 1998, an increase in 2002 sales over 2001 sales, and 2002 sales of at least \$1 million. To view the 2004 ICIC Inner City100, visit their website, www.innercity100.org/2004.asp.

While the ICIC criteria recognize businesses with at least \$1 million in receipts, most of these companies started small, a significant part of them are run by minorities or women, and most have significant parts of their workforces drawn from the inner city.

Advocacy has a special interest in ICIC, since the office is a co-funder of a research project, "The State of Inner City Economies." The researchers are creating a statistical profile of inner city economies to better understand inner city competitiveness and are conducting a pilot program to test their findings. To learn more about the research project, contact Advocacy Senior Economist Ying Lowrey, ying.lowrey@sba.gov, (202) 205-6947.

Tax Programs Examined in New Advocacy Study

A new Advocacy-published study examines the effects of various tax expenditure programs that allow large and small firms the opportunity to reduce their tax liability. *The Impact of Tax Expenditure Policies on Incorporated Small Business*, by Innovation & Information

Consultants, examines numerous tax and tax credit provisions contained in the U.S. Internal Revenue code and their effects on the operation and after-tax profitability of large and small businesses. The report breaks new ground, since the implementation of these policies

and the way their effects are distributed between large and small firms has never been closely examined.

The report finds that small firms benefit from certain tax expenditure programs, although usually by a

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New FAQ Addresses Academic Queries

As college students become increasingly interested in becoming business owners, the classroom will need to become more small business-focused. This is one finding of Advocacy's nationwide focus groups of researchers. In addition, several groups have recognized the need for a single document to help new researchers, students, and professors get started conducting small business research.

The Office of Advocacy has responded by preparing "Small Business Resources for Faculty, Students, and Researchers: Answers to Frequently Asked Questions." This helpful, one-page resource lists the key citations, academic journals, data, and potential funding sources for small business research.

A copy of the publication is contained in this month's issue of *The Small Business Advocate*. It is also located on Advocacy's website at: www.sba.gov/advo/stats/arsbfaq.pdf. If you have any questions, please do not hesitate to contact Chad Moutray at (202) 205-6532 or email chad.moutray@sba.gov.

Small Business Resources for Faculty, Students, and Researchers: Answers to Frequently Asked Questions

Why should small business issues receive more attention in classrooms?

- Two-thirds of college students intend to be entrepreneurs at some point in their careers; however, business school textbooks stress large rather than small firm examples, something that has frustrated many students after graduation.
- Individuals with more education are more likely to become entrepreneurs, and they are also more likely to open a business employing more people.
- Classrooms, both within and beyond schools of business, are filled with potential innovators. The key is to provide the necessary skills that will allow them to foster these talents and start new businesses.

Sources: Students in Free Enterprise; Advocacy Focus Groups.

How important are small businesses to the U.S. economy?

Small firms ...

- Total approximately 23 million in the United States, with roughly 75 percent of the firms having no employees.
- Represent 99.7 percent of all employer firms.
- Employ half of all private sector employees.
- Pay 44.3 percent of the total U.S. private payroll.
- Generate 60 to 80 percent of net new jobs annually.
- Create more than 50 percent of nonfarm, private gross domestic product (GDP).
- Are employers of 39 percent of high tech workers (such as scientists, engineers, and computer workers).
- Made up 97 percent of all identified exporters and produced 29 percent of the known export value in FY 2001.

Sources: U.S. Department of Commerce, Bureau of the Census; Advocacy-funded research by Joel Popkin and Company (Research Summary 211); U.S. Department of Labor, Bureau of Labor Statistics, Current Population Survey; U.S. Department of Commerce, International Trade Administration.

Is there a link between entrepreneurship and economic activity?

- There is a strong correlation between national economic growth and the level of national entrepreneurial activity in prior years, according to the Global Entrepreneurship Monitor (GEM).
- In GEM countries, 71 percent of nascent or would-be entrepreneurs expect to create 1 to 20 jobs, and 21 percent expect to create at least 20 jobs in their new ventures.

- Colleges and universities with high levels of R&D expenditures lead to increased firm formations in the surrounding metropolitan areas. Such R&D expenditures contribute to economic growth via these new firms.

Sources: Global Entrepreneurship Monitor; Advocacy-funded research by BJK Associates (Research Summary 222).

Who is publishing on the importance of small business and entrepreneurship?

The following publications are noteworthy and relevant for individuals to learn more about small business economic research for both the classroom and further analysis.

Selected Advocacy Resources (www.sba.gov/advo/stats)

- *The State of Small Business: A Report of the President (1982 - 2000)* and *The Small Business Economy: A Report to the President (Forthcoming, 2001 - Present)*
- *Small Business Economic Indicators (1995 - Present)*
- *Small Firm Lending Studies (1994 - Present)*
- *State Small Business Economic Profiles (1996 - Present)*
- *The Third Millennium: Small Business and Entrepreneurship in the 21st Century*
- *Women in Business and Minorities in Business*
- Advocacy's Working Paper Series - The Research Papers in Economics (RePEc) also links to our series and others: <http://econpapers.hhs.se/paper/sbawpaper/>

Selected Advocacy Conference Proceedings

- *Tax Policy and Small Business: New Firm Formation, Growth and Survival (2001)*: www.sba.gov/advo/tax_conf.pdf
- *The Changing Banking Structure and Its Impact on Small Business (2000)*: www.sba.gov/advo/b_cf00proc.pdf
- *The Invisible Part of the Iceberg: Research Issues in Industrial Organization and Small Business (2000)*: www.sba.gov/advo/io_conf.pdf
- Acs, Zoltan J., ed. *Are Small Firms Important? Their Role and Impact*. Boston: Kluwer Academic Publishers, 1999. (Proceedings from a 1997 Advocacy conference of the same name.)

Selected Professional Journals

- *Entrepreneurship Theory and Practice*
- *International Small Business Journal*
- *International Journal of Venture Capital*
- *Journal of Applied Management and Entrepreneurship*
- *Journal of Entrepreneurial Finance and Business Ventures*
- *Journal of Business Venturing*
- *Journal of Small Business Management*
- *Small Business Economics*

The SBA's Office of Advocacy was created by an act of Congress in 1976 to protect, strengthen, and effectively represent the nation's small businesses within the federal government. As part of this mandate, the office conducts policy studies and economic research on issues of concern to small business and publishes data on small business characteristics and contributions. For instant access to small business resources, statistics, and research, visit the Office of Advocacy's home page at <http://www.sba.gov/advo/>.

Selected Publications

- Acs, Zoltan J. and David B. Audretsch. *The Handbook on Entrepreneurial Research*. Boston: Kluwer Publishers, 2003.
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- *Frontiers of Entrepreneurial Research*. Proceedings from the Babson-Kauffman Entrepreneurial Research Conferences, 1981 to Present. (Online database: www.babson.edu/entrep/fer/)
- Hart, David M., ed. *The Emergence of Entrepreneurship Policy: Governance, Start-Ups, and Growth in the U.S. Knowledge Economy*. Cambridge University Press, 2003.
- Holtz-Eakin, Douglas and Harvey S. Rosen, eds. *Public Policy and the Economics of Entrepreneurship*. Cambridge, Massachusetts: MIT Press, 2004.
- Katz, Jerome A., ed. *Databases for the Study of Entrepreneurship*. New York: JAI/Elsevier Science, 2000.
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- Lucas, Robert E. Jr., "On the Size Distribution of Business Firms." *Bell Journal of Economics*. 9(2), 1978. 508-523.
- Schumpeter, Joseph A. *The Theory of Economic Development*, Cambridge: Harvard University Press, 1934.
- Sexton, Donald L. and John D. Kasarda, eds. *The State of the Art in Entrepreneurship*. Boston: PWS/Kent Publishing, 1992.
- Sexton, Donald L. and Raymond W. Smilor, eds. *Entrepreneurship 2000*. Chicago: Upstart Publishing, 1997.

What are the sources of data for researching small business and entrepreneurship?

See these data sources for small business economic research.

U.S. Department of Commerce, Bureau of the Census

- 1997 Economic Census: www.census.gov/epcd/www/econ97.html
- 2002 Economic Census (Survey of Business Owners): www.census.gov/epcd/www/econ2002.html
- Center for Economic Studies (CES) Data and Working Papers www.ces.census.gov - CES Data is available at Research Data Centers for approved research proposals.
- Survey of Women- and Minority-Owned Enterprises: www.census.gov/csd/mwb/
- Statistics of U.S. Businesses (partially funded by Advocacy): www.census.gov/csd/susb/susb.htm
- County Business Patterns: www.census.gov/epcd/cbp/view/cbpview.html
- Survey of Income and Program Participation: www.sipp.census.gov/sipp/sipphome.htm

U.S. Department of Labor, Bureau of Labor Statistics

- Business Employment Dynamics: www.bls.gov/bdm/home.htm
- Current Population Survey: www.bls.gov/cps/home.htm and <http://dataferrett.census.gov/TheDataWeb/index.html>

Federal Reserve Board of Governors

- Federal Reserve Bulletin: www.federalreserve.gov/pubs/bulletin/default.htm

- Survey of Small Business Finances: www.federalreserve.gov/pubs/oss/oss3/nssbftoc.htm
- Survey of Consumer Finances: www.federalreserve.gov/pubs/oss/oss2/scfindex.html
- Senior Loan Officer Survey on Bank Lending Practices: www.federalreserve.gov/boarddocs/SnLoanSurvey/

Internal Revenue Service

- Statistics of Income Division: www.irs.gov/taxstats/

National Federation of Independent Business (www.nfib.com)

- Small Business Economic Trends
- Small Business Polls

Other Longitudinal Databases

- Global Entrepreneurship Monitor: www.gemconsortium.org
- Panel Study on Entrepreneurial Dynamics: <http://projects.isr.umich.edu/psed/index.cfm>

If I want to conduct small business economic research, what funding is available?

Traditional funding sources include the National Science Foundation (<http://www.nsf.gov/sbe/ses/>) and many colleges and universities that fund small business research. Subscription-based services provide information on grant opportunities.

The Office of Advocacy contracts with external researchers for many studies. These are set aside for small businesses, rather than colleges and universities. However, individual professors and students can submit proposals as consultants with their own firms. Potential contractors should consult FedBizOpps (<http://www1.eps.gov/spg/index.html>). Sign up on Advocacy's research listserv to receive e-mail notification of the Requests for Quotations (RFQ) or Requests for Proposals (RFP).

The Ewing Marion Kauffman Foundation (www.kauffman.org) and other organizations also fund small business research. Academic conferences often promote best-paper competitions that reward quality research, and internship opportunities allow students to gain practical experience while also researching small business issues.

If I want to start a business, where would I find more information?

Visit www.sba.gov and www.businesslaw.gov for detailed information about business opportunities and starting, financing, and managing a small business. These sites offer information on SBA training, local counseling partners, and legal issues.

Where can I get more information?

Receive Advocacy information by signing up with our listserv at <http://web.sba.gov/list>

- ADVOCACY COMMUNICATIONS**
- ADVOCACY NEWSLETTER**
- ADVOCACY PRESS**
- ADVOCACY RESEARCH**

Advocacy Conference: Entrepreneurship in the 21st Century



Conference participants came from state and local government, academia, think tanks, small businesses, and industry trade associations.



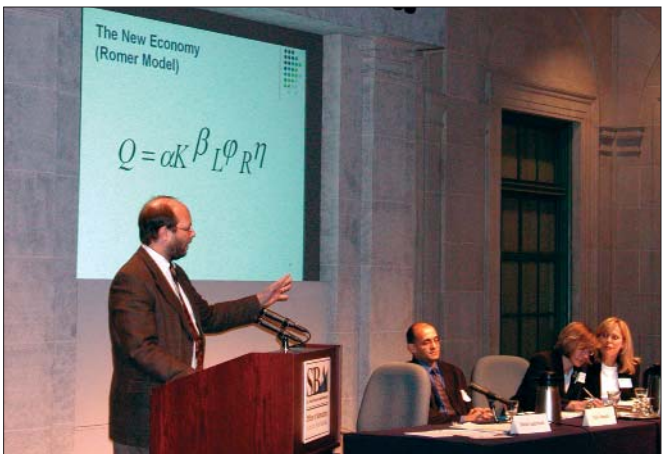
Participating in the finance panel were Allen Berger, Federal Reserve Board of Governors; Josh Lerner, Harvard Business School; and Greg Udell, Indiana University.



Questions and debate were lively, with plenty of audience participation.



Standing, from left: Carol Lopucki, Michigan Small Business Development Center (SBDC); Donald Wilson, Association of SBDCs; and Clinton Tymes, Delaware SBDC Network.



David Audretsch, standing, moderated the the panel on Small Business, Technology, and Innovation in the 21st Century, with Paul Almeida, Maryann Feldman, and Melissa Schilling.



SBA Administrator Hector Barreto, Chief Counsel Thomas M. Sullivan, U.S. Treasury Secretary John Snow, Kaufmann Foundation Vice President Robert Litan, Chief Economist Chad Moutray, and Deputy Chief Counsel Shawne McGibbon.

Economists, from page 1

Second, while much progress has been made for women and minorities, more can be done to promote entrepreneurship among them. Third, many forces—including technology, regulation, and consolidation—will change the environment for small business lending. The fourth theme is that small businesses face a number of burdens that are ripe for new policy solutions. Finally, policymakers will need access to quality data and research on small business to better inform their decisions in the future. For those who were unable to attend the conference, or to review the findings, videos of each session are now available on the Advocacy website, www.sba.gov/advo. Also included are videos of the keynote address by Treasury Secretary John Snow and remarks by Dr. Robert Litan, vice president for research and policy at the Kauffman Foundation. By late summer, the proceedings of the conference will also be available in printed form.

Tax Programs, from page 4

smaller amount than larger firms. Large firms with more extensive operations are better able to realize advantages from certain tax expenditure programs. The one tax expenditure program that clearly benefits small businesses more than large firms by a sizeable margin is the partial deduction for travel and entertainment expenses. Small firms realized an average reduction of 0.86 percent in their effective tax rate from this program, compared with large firms, which experienced a 0.11 percent reduction. Small businesses in the educational services (NAICS code 61), professional, scientific, and technical services (NAICS code 54), and the administrative and support, waste management and recreation service sectors (NAICS code 62) received the largest impact from the travel and entertainment deduction, realizing a reduction in their effective tax rates between 1.5 and nearly 5 percentage points.

The Section 179 deduction permits the depreciation of relatively small amounts of business property to be “super accelerated.” The professional, scientific, and technical service industry (NAICS code 54) utilized this benefit the most; over 35 percent of the industry’s accelerated depreciation impact came from their Section 179 deductions. Other small industries to benefit from this program include wholesale and retail trade (NAICS codes 42, 44-45), finance and insurance (NAICS code 52), and health care and social assistance (NAICS code 62). A research summary and the complete text of *The Impact of Tax Expenditure Policies on Incorporated Small Business* is available on Advocacy’s homepage at www.sba.gov/advo.

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