

Report Documents State of Small Business, Examines Key Issues

Between 2000 and 2005, job growth in Littleton, Colorado, a suburb of Denver, expanded at a rate of 35 percent. Job growth in Littleton surpassed the state's as a whole, as well as Denver's and comparable suburban areas. Littleton's success is featured in the chapter on "economic gardening" in the 2006 edition of *The Small Business Economy for Data Year 2005*. This annual report by the Office of Advocacy examines the

economic contributions of small businesses using data from a variety of sources. Next year's report will benefit from new data on veteran business ownership.

Economic developers in Littleton pioneered the economic gardening concept. This strategy bucks conventional wisdom and emphasizes growing small businesses in place instead of trying to attract branches of established

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In December, Office of Advocacy staff members participated in the American Legislative Exchange Council's States and Nation Policy Summit, in Phoenix, Arizona. Pictured here, from left, are Arizona State Senator Barbara Leff; Advocacy's Regulatory and Legislative Counsel for Regional Affairs, Sarah Wickham; and Region IX Advocate Mike Hull.

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Regulatory News

EPA Issues Relief to Small Business TRI Reporters

On December 18, 2006, the Environmental Protection Agency (EPA) signed a final rule to expand the number of Toxics Release Inventory (TRI) filings that qualify for the short Form A. The final rule provides needed relief to small businesses while maintaining the integrity of the TRI database. This major small business achievement is the culmination of a 15-year effort that started with a petition filed by the Office of Advocacy with EPA in August 1991. EPA's reform will help America's small businesses—especially manufacturers—remain competitive, while still informing communities of the use of toxic materials by local firms.

Chief Counsel for Advocacy Thomas M. Sullivan commended EPA's action: "EPA's reformed TRI rule rewards firms that take aggressive steps to prevent any leaks or emissions of toxics by allowing them to use a short form to notify the community that the firms use toxics in their manufacturing process. EPA's burden reduction recognizes that the United States must take steps to level the playing field for small firms and search for reforms that eliminate unnecessary paperwork while maintaining or improving environmental protection."

Form A is the shorter of two reporting options, Form A and Form R. In 1994, the EPA created the shorter and less burdensome Form A, with Advocacy's support. The form was intended to ease the paperwork burden on TRI fil-

ers whose total production-related wastes are less than 500 pounds. In 1999, EPA excluded the Form A option for all reports of persistent bioaccumulative toxic (PBT) chemicals.

The final rule would raise the reporting threshold to 2,000 pounds of releases for reporters of non-PBT chemicals. It would also extend the use of Form A to businesses that manage less than 500 pounds of PBT chemicals and have zero emissions or discharges to the environment. Given the large controversy about the rule in the environmental community, legislation to repeal the final rule is expected to be introduced in the next Congress.

For a history of Advocacy's involvement, see "What's New" at www.sba.gov/advo or www.sba.gov/advo/laws/comments/tri06.html.

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Message from the Chief Counsel

New Advocacy Research Tracks Developments in Small Business Lending

by Thomas M. Sullivan, Chief Counsel for Advocacy

Access to credit is vital to small business survival and growth. A competitive small business loan market is fundamental to a strong and growing small business community in the U.S. economy. The Office of Advocacy tracks small business finance statistics to examine the major developments that shape small business lending.

In December, Advocacy published two finance studies. *Small Business and Micro Business Lending in the United States, for Data Years 2004-2005* is the office's major annual lending report. *A Survey Based Assessment of Financial Institution Use of Credit Scoring for Small Business Lending* is a research report on credit scoring, a tool that lenders increasingly use to evaluate loan applications. The two reports provide a wealth of information about small business finance.

Several major developments marked the continued evolution of the small business loan market during the past decade. These include interstate banking; the emergence of some 30 huge national and regional financial institutions (with over \$50 billion in domestic assets each); new banking services utilizing new technologies in information collection, processing, and dissemination; and financial modeling in credit evaluation and risk management. These innovations have all contributed to a dynamic small business loan market, offering a greater variety of products and services. Financial service providers, large and small, are competing to develop and utilize new lending techniques to explore profitable opportunities in small business loan markets. As a result, regional

and national lenders have gained entry into local small business loan markets, and a national market for general purpose loans (a combined product of credit line and credit cards for working capital purposes) has emerged.

“Small lenders’ future competitiveness will hinge on their ability to take advantage of new technology and lending techniques.”

The market for micro business loans (those under \$100,000) has undergone rapid growth during the past 10 years. The number of micro business loans outstanding from commercial banks grew over

200 percent: from less than 5 million in 1995 to more than 17 million in June 2005. By comparison, larger small business loans (from \$100,000 to under \$1 million) jumped by 80 percent.

Although many of the smallest loans are traditional loans made by small lenders, the growth in this category is made up primarily of credit cards, credit lines, or combined products, all of which have been heavily promoted by major financial institutions. The growth in credit card use comes as a result of these lenders' efforts to take advantage of new technologies and new lending techniques—especially credit scoring and Internet banking—to provide financial services to small business owners.

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Office of Advocacy economists Dr. Charles Ou and Victoria Williams completed the current edition of *Small Business and Micro Business Lending in the United States* in December. They have been Advocacy's small business finance team for many years.

Research Notes

New Report on Small Business and Economic Development Focuses on Houston Area Firms

Houston's newer and growing economic subcenters have relied more on small business as their cornerstone than the older central business district and the Galleria area, according to a new report from the Office of Advocacy. The report's findings also suggest that while small firms support urban economic growth, as development proceeds they grow substantially.

"Houston's history of economic growth offers some interesting lessons for the rest of the country," said Thomas M. Sullivan, chief

counsel for advocacy. "Its experience shows that encouraging small firm growth plays an important role in urban economic development."

The Economic Role of Small Businesses Using Large Data Sets: An Analysis of the Contributions of Small Firms to Urban Growth was written by University of Houston researchers Steven Craig and Janet Kohlhasse, with funding from the Office of Advocacy. It examines the evolution of the urban economy into employment subcenters around the city. The report was released

during a luncheon sponsored by the Greater Houston Partnership.

Among its findings, the report documents that the newer subcenters have been economically diverse, as most broad industrial classifications were well-represented in each subcenter. Moreover, the authors interpret their evidence to suggest that small firms are a crucial element in urban economic development as their success is likely to lead to economic growth for the entire local economy.

Growth and Decline Trends For Small Business

Small business growth and decline trends tend to persist and are not easily reversed, according to a study by the Office of Advocacy. A team of authors, Rich Perline, Robert Axtell, and Daniel Teitelbaum of NuTech Solutions, wrote *Volatility and Asymmetry of Small Firm Growth Rates Over Increasing Time Frames* with funding from Advocacy. Perline and Axtell presented the report to the Center for Economic Studies of the U.S. Census Bureau in December.

"We know that overall, small business is a dynamic sector of the economy," said Chad Moutray, chief economist of the Office of Advocacy. "This study shows that the growing and declining firms tend to stay in the same mode over time. Consequently, policies that affect growth or decline can have an impact on small businesses over a longer term than originally anticipated."

The report followed up on a study from 2005 that examined

firm growth rates by size of firm and industry type. That report found that firm growth tends to be relatively more concentrated among fast- and slow-growth firms. The current study examined growth rates over a five-year period, using special tabulations of the Census Bureau's Business File dataset.

For More Information

Both reports are available on Advocacy's website:

- *The Economic Role of Small Businesses Using Large Data Sets: An Analysis of the Contributions of Small Firms to Urban Growth*, by Steven Craig and Janet Kohlhasse of the University of Houston, www.sba.gov/advo/research/rs287tot.pdf; and

- *Volatility and Asymmetry of Small Firm Growth Rates Over Increasing Time Frames*, by Rich Perline, Robert Axtell, and Daniel Teitelbaum of NuTech Solutions, www.sba.gov/advo/research/rs285tot.pdf.

Finance Trends,

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Small lenders' future competitiveness will hinge on their ability to take advantage of new technology and lending techniques. Credit scoring is one such technique. Advocacy's new study on banks' use of credit scoring shows that the institutions that made the most use of this new lending technique found that it improved their ability to manage credit risk. It also contributed to their small business lending overall. The use of credit scoring has allowed risk-based pricing of loans; this "democratizes" lending, meaning that riskier loans can now be made to start-ups or small business owners with little credit history.

These two reports delve into the trends that underlie small business finance and show that the small business lending market continues to be quite dynamic.

For More Information

Advocacy's new lending report, *Small Business and Micro Business Lending in the United States, for Data Years 2004-2005*, is online at www.sba.gov/advo/research/sbl_05study.pdf. Previous editions dating to 1994 are also online. The report was written by Advocacy economists Charles Ou and Victoria Williams. It uses both Consolidated Reports of Condition and Income (call reports) from June 2005 and Community Reinvestment Act (CRA) reports for 2004 to review small business lending activity. This year's edition has been expanded to include savings banks, as well as savings and loan institutions.

A Survey Based Assessment of Financial Institution Use of Credit Scoring for Small Business Lending, written by Charles Cowan and Adrian Cowan with funding from the Office of Advocacy, can be found at www.sba.gov/advo/research/rs283tot.pdf.

SCORE Counsels Small Business Owners

Thinking of starting a business? SCORE offers free online information on how to start, manage, and grow a business. The SCORE small business website is often the first place where entrepreneurs seek information about launching a business. Last year, more than 1.3 million people visited www.score.org, up from 405,000 people in 2000.

SCORE's 1,300 online counselors provide expert advice in more than 600 business areas. They gave nearly 100,000 email consults in 2005. In addition, SCORE provides information, articles, and business research for women, minorities, young entrepreneurs, and veterans.

Thousands of visitors to the SCORE website continue to sign up for one of SCORE's monthly electronic newsletters. *SCORE eNews*, which offers the latest trends and resources to help small businesses succeed, reaches nearly 65,000 subscribers. More than 38,000 people receive *SCORE Expert Answers*, which provides marketplace trends and advice from small business experts and industry leaders.

For more information, visit www.score.org.

Data Updates from the 2006 Edition of *The Small Business Economy*

One of the most widely used references in *The Small Business Economy* is Table A.1. U.S. Business Counts and Turnover Measures, reproduced below. (It appears on pages 116-117 of the book.) These data are gathered from many sources and are useful to researchers, policymakers, and small business advocates.

Table A.1 U.S. Business Counts and Turnover Measures, 1980–2005

Year	Business and Self-Employment Counts				Business Turnover Measures		
	Employer firms	Nonemployers	Self-employment ² (thousands)	Nonfarm business tax returns	Employer births	Employer terminations	Business bankruptcies
2005	e 5,992,400	e 19,856,800	10,464	e 29,004,800	e 671,800	e 544,800	39,201
2004	e 5,865,400	e 19,462,300	10,431	e 28,329,900	e 642,600	e 544,300	34,317
2003	5,767,127	18,649,114	10,295	27,269,500	612,296	540,658	35,037
2002	5,697,759	17,646,062	9,926	26,347,100	569,750	586,890	38,540
2001	5,657,774	16,979,498	10,109	25,631,200	585,140	553,291	40,099
2000	5,652,544	16,529,955	10,215	25,106,900	574,300	542,831	35,472
1999	5,607,743	16,152,604	10,087	24,750,100	579,609	544,487	37,884
1998	5,579,177	15,708,727	10,303	24,285,900	589,982	540,601	44,367
1997	5,541,918	15,439,609	10,513	23,857,100	590,644	530,003	54,027
1996	5,478,047	NA	10,489	23,115,300	597,792	512,402	53,549
1995	5,369,068	NA	10,482	22,555,200	594,369	497,246	51,959
1994	5,276,964	NA	10,648	22,191,000	570,587	503,563	52,374
1993	5,193,642	NA	10,279	20,874,800	564,504	492,651	62,304
1992	5,095,356	14,325,000	9,960	20,476,800	544,596	521,606	70,643
1991	5,051,025	NA	10,274	20,498,900	541,141	546,518	71,549
1990	5,073,795	NA	10,097	20,219,400	584,892	531,400	64,853
1989	5,021,315	NA	10,008	19,560,700	NA	NA	62,449
1988	4,954,645	NA	9,917	18,619,400	NA	NA	62,845
1987	NA	NA	9,624	18,351,400	NA	NA	81,463
1986	NA	NA	9,328	17,524,600	NA	NA	79,926
1985	NA	NA	9,269	16,959,900	NA	NA	70,644
1984	NA	NA	9,338	16,077,000	NA	NA	64,211
1983	NA	NA	9,140	15,245,000	NA	NA	62,412
1982	NA	NA	8,898	14,546,000	NA	NA	69,242
1981	NA	NA	8,735	13,858,000	NA	NA	48,086
1980	NA	NA	8,642	13,021,600	NA	NA	43,252

e = estimate

NA = Not Available.

Sources: U.S. Small Business Administration, Office of Advocacy, from data provided by the following sources: employer firms from the U.S. Department of Commerce, Bureau of the Census with 2004 and 2005 estimates based on Census Bureau and U.S. Department of Labor data; nonemployers from the Census Bureau with 2004 and 2005 estimates based on U.S. Department of the Treasury, Internal Revenue Service (IRS) data; self-employment (unincorporated, primary occupation, monthly averages) from the U.S. Department of Labor, Bureau of Labor Statistics; nonfarm business tax returns from the IRS; employer births and terminations from the Census Bureau with 2004 and 2005 estimates based on Census Bureau and Department of Labor data; bankruptcies from the Administrative Office of the U.S. Courts (business bankruptcy filings).

Small Business Economy, from page 1

large businesses from other places. Chapter 6, by Steve Quello and Graham Toft, finds the strategy has worked in diverse places around the country.

The Small Business Economy was released at a National Economists Club event in Washington, D.C., on December 7. Overall, it shows that U.S. small businesses fared well in the economy of 2005, despite the economic shocks of Hurricanes Katrina and Rita. “As a whole, the economy bounced back, led by resilient small businesses,” said Chad Moutray, chief economist for the Office of Advocacy. “The estimated 671,800 small business starts in 2005 were higher than the estimated 544,800 closures, leading to a new high of 5.99 million employer firms in the United States. Clearly small businesses had a good year.”

The report’s seven chapters probe numerous small business issues in depth. Chapter 1 looks at the **overall economy**. It finds that the key indicators to the economy’s performance—output and productivity—both rose in 2005.

Chapter 2, on **small business financing**, finds that favorable financial conditions supported U.S. economic growth in 2005 despite hurricanes and energy price increases. Net borrowing increased by 19 percent, a pace comparable to that of 2003-2004. Commercial banks expanded lending and eased terms on commercial and industrial loans.

Procurement is the focus of Chapter 3. Small businesses continued to benefit from the federal acquisition of goods and services from small firms in 2005, and also from changes that helped clarify the federal procurement environment.

Chapter 4 focuses on **women in business**. It finds that between 1997 and 2002, the number of women-owned firms increased by 19.8 percent, and the number of

women-owned employer firms, by 8.3 percent. Women owned 6.5 million, or 28.2 percent, of nonfarm U.S. firms.

Chapter 5 studies the impact of **entrepreneurial education** (and education generally) on entrepreneurship. It finds the highest levels of entrepreneurship among individuals with at least a bachelor’s degree. Recent research also points to a link between entrepreneurship education and venture creation.

Best practices of **economic gardening**, described in Chapter 6, emphasize three things:

- Infrastructure—building the community assets essential to commerce and overall quality of life;
- Connectivity—improving the interaction among business owners and critical resource providers; and
- Market information—accessing competitive intelligence on

markets, customers, and competitors comparable to the intelligence that has historically been available to large firms.

A summary of federal agency compliance with the **Regulatory Flexibility Act** in its 25th year appears in Chapter 7.

The full report is available on Advocacy’s website at www.sba.gov/advo/research/sb_econ2006.pdf. Earlier editions are available at www.sba.gov/advo/research/sbe.html. The print version may be purchased from the Government Printing Office bookstore: <http://bookstore.gpo.gov/actions/GetPublication?stocknumber=045-000-00298-5>.



On December 7, 2006, Chief Economist Chad Moutray spoke before the National Economists Club (NEC) in Washington, DC, to release *The Small Business Economy: A Report to the President for Data Year 2005*. His remarks focused on the importance of education to entrepreneurship and on “economic gardening,” an economic development strategy that stresses local, fast-growing entrepreneurial firms. He also addressed the current state of the economy for small businesses. This is the third time the NEC luncheon has served as a release venue for this annual publication.

Tax News

Small Businesses Benefit from IRS Refund

In May 2006, the Internal Revenue Service announced that taxpayers (individuals, businesses, and tax-exempt organizations) can request a refund of the long distance telephone excise taxes paid during the 41-month period between March 2001 and August 2006.

Individuals must request the refund on their 2006 tax return. To claim the refund, individual taxpayers can determine the actual amount they paid during the period or take a standard refund. The standard refund amount is \$30 to \$60 depending on the number of exemptions claimed by the individual taxpayer. Sole proprietors who report \$25,000 or less in gross receipts on their 2006 tax return may also opt to claim the standard refund amount.

Other filers must complete Form 8913, Credit for Federal Telephone Excise Tax Paid. To complete this form, taxpayers must determine the actual amount of refundable long-distance telephone taxes they paid for the period, or they may use a formula.

The special formula provided by the IRS permits businesses and tax-exempt organizations to compare two telephone bills from 2006 to determine the percentage of their telephone bill that represents the tax. Businesses and tax-exempt organizations should use phone bills with a statement date in April 2006 and September 2006. Taxpayers calculate the telephone tax as a percentage of their April 2006 bill (which included the excise tax for both local and

long-distance service) and their September 2006 telephone bills (which only included the tax on local service). The difference between these two percentages is applied to quarterly or annual telephone expenses to determine the amount of the refund.

For businesses and tax-exempt organizations with 250 or fewer employees, the maximum refund is 2 percent of the total telephone expenses incurred during the period. For businesses and tax-exempt organizations with more than 250 employees, the maximum refund is 1 percent of their total telephone expenses for the period.

Additional information can be found on the IRS's website: www.irs.gov/newsroom/article/0,,id=164305,00.html.

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