

Office of Economic Research

Research Publications 2004

January 2005

Created by Congress in 1976, the Office of Advocacy of the U.S. Small Business Administration (SBA) is an independent voice for small business within the federal government. Appointed by the President and confirmed by the U.S. Senate, the Chief Counsel for Advocacy directs the office. The Chief Counsel advances the views, concerns, and interests of small business before Congress, the White House, federal agencies, federal courts, and state policy makers. Economic research, policy analyses, and small business outreach help identify issues of concern. Regional Advocates and an office in Washington, DC, support the Chief Counsel's efforts.

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Office of Economic Research



Research Publications 2004

Office of Advocacy
U.S. Small Business Administration
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Foreword

This report summarizes the publications produced by the Office of Advocacy's Office of Economic Research in 2004. It is the purpose of this office to document the importance of small business to the U.S. economy and to focus particular attention on policy issues of relevance to them.

Have we accomplished our mission in the past year? One gauge to measure our success is the level of attention our research and data have received in the past year from academics, policymakers, and the media. Certainly, 2004 was an active year for economic research, and we were fortunate to have a number of people take notice of our activities to further the debate and/or to enlighten the user.

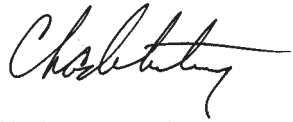
We have learned through focus groups, for instance, that many of our publications are regularly used in speeches, lectures, and academic research. The *Small Business by the Numbers: Answers to Frequently Asked Questions* document, as an example, is often cited, and more and more faculty are using it as a reference tool in their classrooms. The office this year worked aggressively to bring *The Small Business Economy* series up to date, and a new regular publication, *Quarterly Indicators: The Economy and Small Business*, provides a current snapshot of economic trends relevant to small firms.

One of the highlights of the past year was the "Entrepreneurship in the 21st Century" conference co-sponsored with the Ewing Marion Kauffman Foundation. This forward-looking conference focused on issues the small business owner will face in the coming years. The videos and proceedings publication of the conference have been well received.

Other studies, too, have garnered significant attention in 2004. Henry Beale presented data about regulatory burdens on small, home-based businesses. Steven Craig and Pauline Hardee documented the impact that banking consolidation has had on small business credit availability. Robert Fairlie showed steady growth in self-employment over the past two decades. Innovation and Information explored the various tax expenditures that small and large firms take advantage of. Stephen Pociask reported on how small businesses spend their telecommunications dollar. Eagle Eye Publishers analyzed procurement data, and other reports focused on small business data.

The media have taken an increasing interest in Advocacy's research. In 2004, studies generated interest in major newspapers such as the *Washington Post*, *The New York Times*, *The Wall Street Journal*, the *Chicago Tribune*, the *Los Angeles Times*, *The Arizona Republic*, and the *Denver Post*, and key business magazines and journals such as *Inc.*, *Business Week*, and *Fortune Small Business*. Advocacy's data have been featured in radio and television interviews across the country.

We hope that you will find it useful to have our economic research publications chronicled in one place. All of our research and data can be found online at <http://www.sba.gov/advo/research>. For regular updates on our research as it is released, you might want to join Advocacy's research listserv, which can be found at <http://web.sba.gov/list>.

A handwritten signature in black ink, appearing to read "Chad Moutray", with a long horizontal flourish extending to the right.

Chad Moutray, Ph.D.
Chief Economist and Director
Office of Economic Research

Contents

Forewordiii

Office of Economic Research Research Publications 2004 1

 Banking/Finance 1

 General Small Business 1

 Innovation and Technology 5

 International Trade 6

 Procurement 6

 Regulation 8

 Tax 9

 Women and Minorities 10

 Veterans 10

Index 12

Office of Economic Research

Research Publications 2004

The Impact of Bank Consolidation on Small Business Credit Availability

Steven G. Craig and Pauline Hardee; Research Summary #234; February 2004

<http://www.sba.gov/advo/research/rs234tot.pdf>

Banking/Finance

The banking industry has been undergoing an extensive period of consolidation, accelerated since the federal interstate banking legislation of 1994. As small firms are the source of most job growth and since the bulk of small business credit is primarily from banks, the effects of institutional change on small business credit are a major economic issue. This research investigates the consequences to small business credit from banking consolidation by examining two separate components of the credit process—credit limits and credit levels, using primarily the Survey of Small Business Finances of 1998. The research found that credit access had been significantly reduced for small businesses, but that actual credit balances had fallen by less than the fall in credit limits. These results suggest that while small businesses are less likely to borrow from the banking sector in markets with a greater degree of banking consolidation, when they do so they take advantage of improvements in pricing to borrow greater amounts. Small businesses have increasingly turned to nonbank sources of financing to satisfy their credit needs. Interestingly, this nonbank option seems to be more important for small businesses with negative rather than positive equity.

Why Do Small Firms Choose Quasi-Integration? The Case of the Home-Building Industry

James R. Dewald, Jeremy Hall, and James J. Chrisman; Working Paper

Office of Advocacy Best Paper Award, United States Association for Small Business and Entrepreneurship Conference; January 2004

<http://www.sba.gov/advo/stats/wkp04jrd.pdf>

General Small Business

This article explores the variables that drive small firms to choose quasi-integration as an alternative to vertical integration in situations of high asset frequency. It provides new insights by focusing on (1) the preferences of small, vulnerable firms, and (2) an institutionalized form of quasi-integration. The findings indicate that the preference for quasi-integration is driven by asset specificity, bargaining power, and opportunistic expectations. The implications are that preferences for quasi-integration go beyond simple efficiency considerations.

General Small Business

The Small Business Economy: A Report to the President

Various contributors, Kathryn Tobias, ed.

2001 Edition; February 2004: http://www.sba.gov/advo/stats/sb_econ2001.pdf

2002-2003 Edition; August 2004: http://www.sba.gov/advo/stats/sb_econ02-03.pdf

2004 Edition; November 2004: http://www.sba.gov/advo/stats/sb_econ2004.pdf

From 1982 to 2000, the Office of Advocacy prepared *The State of Small Business: A Report of the President* for the White House. This successor, Advocacy-generated publication highlights data and research of importance to small firms for each year. With these 2001-2004 editions released in 2004, the series is now up to date. Highlights include discussions of the economy, small business financing, innovation and technology transfer, procurement, regulation, and women and minorities.

Small Business Resources for Faculty, Students, and Researchers: Answers to Frequently Asked Questions ("Academic FAQ")

Chad Moutray, Chief Economist; March 2004

<http://www.sba.gov/advo/stats/arsbfaq.pdf>

This document addresses a number of questions about small business research and data from the perspective of a faculty member, student, or researcher. It includes a discussion of the importance of education and entrepreneurship, a brief listing of journals and recommended readings, links to data sources, and information about research funding.

Quarterly Indicators: The Economy and Small Business

Chad Moutray, Chief Economist

First Quarter 2004; May 2004: <http://www.sba.gov/advo/stats/sbqei0401.pdf>

Second Quarter 2004; September 2004: <http://www.sba.gov/advo/stats/sbqei0402.pdf>

Third Quarter 2004; November 2004: <http://www.sba.gov/advo/stats/sbqei0403.pdf>

This regular publication pulls together data from a variety of sources to highlight quarterly economic trends relevant to small businesses.

Small Business by the Numbers: Answers to Frequently Asked Questions

Chad Moutray, Chief Economist; June 2004

<http://www.sba.gov/advo/stats/sbfaq.pdf>

This document serves as a summary of other research materials and provides a series of quick, easy-to-recite facts for an external audience to recognize the importance of small business in the economy. As such, it is an excellent "introductory" publication for individuals to acquaint themselves with Advocacy research and data.

Entrepreneurship in the 21st Century: Conference Proceedings

Various contributors; Cosponsored with the Ewing Marion Kauffman Foundation;
July 2004

http://www.sba.gov/advo/stats/proceedings_a.pdf (Part I)

http://www.sba.gov/advo/stats/proceedings_b.pdf (Part II)

http://www.sba.gov/advo/stats/proceedings_c.pdf (Part III)

http://www.sba.gov/advo/video/adv_video.html (Videos)

On March 26, 2004, the Office of Advocacy and the Kauffman Foundation cosponsored a forward-looking conference on entrepreneurship and significant issues of importance to small business owners in the near and distant future. Several themes emerged from the conference. First, new innovative entrants play a critical role in maintaining the U.S. competitive economic balance and provide the tools for economic development in local communities. Second, while much progress has been made by 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. Fourth, 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. The proceedings book is available online in three parts, and the entire conference was captured on video.

Small Business Economic Indicators for 2003

Brian Headd, Economist; August 2004

<http://www.sba.gov/advo/stats/sbei03.pdf>

This annual report serves a quick reference guide to current data on small business activity (e.g., new firms, employment, income, and failures) in the nation and at the state level. An overview of the economic conditions in 2003 is presented, and tables provide a historical perspective on a variety of data observations.

Self-Employed Business Ownership Rates in the United States: 1979-2003

Robert W. Fairlie; Research Summary #243; December 2004

<http://www.sba.gov/advo/research/rs243tot.pdf>

Published figures from the U.S. Department of Labor, Bureau of Labor Statistics (BLS) tell only part of the story of the self-employed. The figures exclude the incorporated self-employed, an increasingly popular tax status, and generally do not include owner demographics. Fortunately, microdata are available for users to generate customized figures. Microdata are used here to produce more complete self-employment figures and to follow trends in self-employed business owner demographics. This study finds that self-employment numbers have grown slowly and steadily since the late 1970s, and self-employment rates have been relatively stable. In recent years, both the counts and rates of male, female, Latino, African American, White, and Asian self-employed have increased.

Development of Business Data: Tracking Firm Counts, Growth, and Turnover by Size of Firms

Catherine Armington; Research Summary #245; December 2004

<http://www.sba.gov/advo/research/rs245tot.pdf>

Just over a few decades ago, data on U.S. industries were mainly focused on agriculture and manufacturing; thus, comprehensive data on small business were not available. Tremendous efforts were undertaken by individuals and organizations to obtain the extremely valuable data by firm size that are taken for granted today.

Documentation was needed to chronicle the creation of these data sources so that users could understand the strengths and weaknesses of the data and so that later efforts to produce new data sources could benefit from the previous experience. This report shows that creating firm size data on the dynamic U.S. economy has been difficult. Administrative data include delays for the purposes of capturing births, closures, corporate restructuring, mergers and spin-offs. Within the last quarter century, great progress has been made by government data agencies in overcoming the challenges to develop dynamic firm size data that will allow policymakers and academics to understand the role of new and small businesses in the U.S. economy.

Small Firms and Technology: Acquisitions, Inventor Movement and Technology Transfer

Innovation and Technology

CHI Research, Inc.; Research Summary #233, January 2004

http://www.sba.gov/advo/research/rs233_tot.pdf

Small firms are integral to the innovation process even when they are not responsible for the final or breakthrough technology. This study seeks to determine the extent to which large firms rely on small firms and their achievements in developing new technologies. Small firms are a vital element of new technology in many industries. Their importance is not immediately apparent when all industries are considered, because small firms tend to be excluded from such key capital-intensive industries as automotive, aerospace, and oil research. In newer high technology industries, such as biotechnology, medical electronics, medical equipment, and telecommunications, large firms frequently rely on small firms' discoveries and inventions.

A Survey of Small Businesses' Telecommunications Use and Spending

Stephen B. Pociask, TeleNomic Research, LLC; Research Summary #236; March 2004

<http://www.sba.gov/advo/research/rs236tot.pdf>

This report provides new and much needed data on small businesses' use of and expenditures on telecommunication services. These data provide an important reference to inform policy decisions. Small businesses spend a considerable amount for telecommunication services. The level of expenditures varies by industry and firm size. As in so many other areas of regulation, small firms are affected by telecommunication policies in a manner disproportionate to their size.

Trends in Electronic Procurement and Electronic Commerce and Their Impact on Small Business

Innovation and Information Consultants, Inc; Research Summary #240; June 2004

<http://www.sba.gov/advo/research/rs240tot.pdf>

See the description in the "Procurement" section above.

International Trade

Costs of Developing a Foreign Market for a Small Business: The Market & Non-Market Barriers to Exporting by Small Firms

Palmetto Consulting, Inc.; Research Summary #241; November 2004

<http://www.sba.gov/advo/research/rs241tot.pdf>

In response to the globalization of businesses, there has been a proliferation of international market searching and penetration by small business owners. In 2001, 230,736 small and medium-sized firms with fewer than 500 workers exported goods. Small and medium-sized companies account for 97 percent of all U.S. exporters; their exports were valued at \$182 billion, or 29.2 percent of all U.S. goods exported. The author studied the experiences of nine U.S. exporters in South Carolina. Feedback from the chief executive officers of these firms suggests that psychological, personal, and opportunity costs, such as the time involved in learning how to perform the logistics of exporting and overcoming the fear of exporting are often more important than out-of-pocket costs. Hence, developing a process to communicate information to small firms seems to be important in helping firms export more effectively.

Procurement

Characteristics of Federal Government Procurement Spending with Veteran-Owned Businesses: FY 2000 - FY 2003 (3Q)

Eagle Eye Publishers, Inc.; Research Summary #239; June 2004

<http://www.sba.gov/advo/research/rs239tot.pdf>

To track progress toward this goal, the General Services Administration (GSA) has introduced codes into its Federal Procurement Data System (FPDS) indicating ownership by veterans or by service-disabled veterans. The authors created a new database of prime contracts to veteran-owned firms to compare with the GSA's official database. Through a careful recoding procedure and analysis, they found that the coding in the FPDS substantially understated the number of veteran-owned businesses and the level of procurement going to them. Federal agencies are actually providing far more contracts and dollars to veteran-owned firms than they are reporting. An improved strategy to identify and include in the FPDS those veteran-owned firms identified by the authors could triple the contract dollars now being recorded. Although the number of veteran-owned firms recognized in the FPDS is steadily increasing, better education and marketing by both agencies and veterans themselves is needed to remedy the underutilization of these firms.

Trends in Electronic Procurement and Electronic Commerce and Their Impact on Small Business

Procurement

Innovation and Information Consultants, Inc; Research Summary #240; June 2004

<http://www.sba.gov/advo/research/rs240tot.pdf>

This report examines the extent to which businesses are utilizing Internet and electronic information technologies in government procurement. It examines whether the transition to electronic commerce has helped or handicapped small businesses in obtaining at least 23 percent of federal purchases annually, as Congress has mandated. It also investigates whether small businesses in industries that successfully adopt e-commerce have an advantage in competing for procurement dollars, and it includes a survey of existing evidence on the implementation of electronic procurement in these industries. The researchers conducted interviews with a small sample of respondents to shed light on some of the findings of the data analysis and literature review.

The Future of Small Businesses in the U.S. Federal Government Marketplace

Major Clark, III, Assistant Chief Counsel, and Chad Moutray, Chief Economist

Journal of Public Procurement (journal), Volume 4, Number 3, 2004

Advocacy Working Paper Version: <http://www.sba.gov/advo/stats/wkp04mccm.pdf>

The federal government purchased goods and services valued at approximately \$100 billion from small businesses in FY 2003, which was up from previous years. Moreover, in FY 2003, the federal government exceeded its small business contracting goal of 23 percent. Despite such achievements, implementation of the acquisition reforms enacted in the 1990s has limited small businesses' access to the federal procurement market. Federal agencies have, for instance, not met their goals for women, minorities, or veterans, and contract bundling and purchase cards may restrict small business opportunities. Meanwhile, both judicial actions and a reduction in the number of acquisition workers complicate matters. This paper discusses each of these issues and offers five recommendations that, if fully implemented, should ensure a brighter future for small businesses in the federal government marketplace.

Procurement

Analysis of Type of Business Coding for the Top 1,000 Contractors Receiving Small Business Awards in FY 2002

Eagle Eye Publishers, Inc.; Research Summary #246; December 2004

<http://www.sba.gov/advo/research/rs246tot.pdf>

The Individual Contract Action Report (ICAR), maintained by the General Services Administration's (GSA's) Federal Procurement Data System (FPDS) is the government's master contract database of how agencies spend available procurement dollars. Information entered into the FPDS plays a critical role in measuring the success or failure of small business procurement policies each year. A review of the transaction records coded as being awarded to small businesses in the ICAR file identified large vendors as some of the actual recipients. This calls into question the reliability of the FPDS in determining contractor size. Drawing extensively from data in the ICAR file, this study provides a preliminary statistical assessment of the extent to which names of large businesses appear among the awards made to the 1,000 largest small business contractors in FY 2002. Of the top 1,000 small business contractors in FY 2002, Eagle Eye Publishers' analysis found 44 parent companies it identified as either large firms or "other." Contracts to these two groups taken together had a total value of \$2 billion. The coding problem could have been a result of erroneously assigned type-of-business codes, or of a large firm's acquisition of a smaller firm during the fiscal year, or of a small firm's growing out of its size classification, among other possible reasons.

Regulation

Home-Based Business and Government Regulation

Henry B.R. Beale, Microeconomic Applications, Inc.; Research Summary #235; February 2004

<http://www.sba.gov/advo/research/rs235tot.pdf> (Full Report)

<http://www.sba.gov/advo/research/rs235app.pdf> (Appendices)

The home-based business sector is substantial in size: 53 percent of small businesses are based in the home (Pratt, 2000). Some home-based ventures are the incubators of successful ventures that evolve to locations outside the home, while other occupations are well matched to the home environment—bed and breakfasts and infant and toddler day care, small offices, or cottage industries. This study finds that, at the federal level, Internal Revenue Service regulations penalize home-based businesses in their treatment of deductions. At the local level, zoning laws and prohibitions present home-based businesses with a significant entry barrier. The report notes, however, that some states have improved the environment for home-based businesses.

Small Businesses as Culprits and Clients: A Comparison of Brownfield Redevelopment in Los Angeles and Kuala Lumpur

Carol S. Armstrong; Research Summary #238; June 2004

<http://www.sba.gov/advo/research/rs238tot.pdf>

This study compares brownfield (contaminated property) redevelopment in two cities, Los Angeles and Kuala Lumpur, Malaysia; and it identifies why brownfields are understood differently by small-scale manufacturers. Small manufacturing firms in both the United States and Kuala Lumpur are generally unaware of brownfield policies. Small firms in the United States feel antagonized as "culprits" by their local and national governments, while small firms in Malaysia are treated as "clients." Both cities perpetuate their problems by keeping small firms disengaged from the brownfield solution. The study discovered that the "culprit-vs.-client" paradox of small and medium-sized enterprises exists in both cities, but that Malaysia might be more successful with their cleanup, since small businesses there are treated as stakeholders in economic development and encouraged to innovate toward international environmental standards in order to remain competitive globally.

Regulation

The Impact of Tax Expenditure Policies on Incorporated Small Business

Innovation and Information Consultants, Inc.; Research Summary #237; April 2004

<http://www.sba.gov/advo/research/rs237tot.pdf>

This report identifies 10 programs that the Joint Committee on Taxation (JCT) and Treasury classify as tax expenditures to analyze in detail. In addition, while not "true" tax expenditures, the foreign tax credit and deduction for travel and entertainment expenses are also analyzed since they provide businesses with tax benefits. All of these programs account for at least 70 percent of the total tax expenditures provided to corporate taxpayers in the United States over the past few years. The study finds that small firms benefit from certain tax expenditure programs, although as a general matter, by a 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 that witnessed a 0.11 percent reduction.

Tax

Women and
Minorities

Self-Employed Business Ownership Rates in the United States: 1979-2003

Robert W. Fairlie; Research Summary #243; December 2004

<http://www.sba.gov/advo/research/rs243tot.pdf>

See the description in the "General Business" section above.

Veterans

Characteristics of Federal Government Procurement Spending with Veteran-Owned Businesses: FY 2000 - FY 2003 (3Q)

Eagle Eye Publishers, Inc.; Research Summary #239; June 2004

<http://www.sba.gov/advo/research/rs239tot.pdf>

See the description in the "Procurement" section above.

Entrepreneurship and Business Ownership in the Veteran Population

Waldman Associates; Research Summary #242; November 2004

<http://www.sba.gov/advo/research/rs242tot.pdf>

In recent years, increasing attention has been called to the entrepreneurial needs of America's veterans, particularly those veterans who have service-connected disabilities. Section 702 of P.L. 106-50 tasked the Office of Advocacy to develop information on the use of programs to assist small businesses owned and controlled by veterans and service-disabled veterans. This study addresses these and other questions: (1) What is the current state of programs for veterans and/or service-disabled veterans who wish to start a small business or who currently own or operate a small business? (2) What is the level of entrepreneurship interest and activity in the veteran population? (3) What are the characteristics of businesses that veterans own or wish to start? (4) What obstacles do veterans encounter in starting or managing a small business? The author provides new data on these questions from a survey of veterans.

Self-Employed Business Ownership Rates in the United States: 1979-2003

Robert W. Fairlie; Research Summary #243; December 2004

<http://www.sba.gov/advo/research/rs243tot.pdf>

See the description in the "General Business" section above.

Evaluating Veteran Business Owner Data

Veterans

Joseph Sobota, Assistant Chief Counsel; Research Summary #244; December 2004

<http://www.sba.gov/advo/research/rs244tot.pdf>

Veteran business owners as a group have received increasing attention in recent years, particularly since enactment of the Veterans Entrepreneurship and Small Business Development Act of 1999, P.L. 106-50. This legislation included provisions calling for the development of more information about businesses owned by veterans and by service-disabled veterans and about the role they play in the nation's economy.

Unfortunately, data available for these groups of entrepreneurs are limited. The last authoritative Census Bureau data on veteran-owned firms dates from 1992. Currently, there are some lists of businesses that include veteran status; however, their information is thought to be incomplete, and at best they include data on only a small fraction of all veteran-owned businesses. The purpose of this study is to examine currently available data sources on veteran business ownership, to compare the quality of major data sources, to review existing literature on veteran business ownership, and to make recommendations. Policymakers need good data in order to make informed decisions on how best to serve veteran entrepreneurs. This study attempts to advance this purpose.

Index

- aerospace industry, 5
- Armington, Catherine, 4
- Armstrong, Carol, 9
- automotive industry, 5
- banking, 1
- Beale, Henry B. R., 8
- biotechnology, 5
- brownfield redevelopment, 9
- CHI Research, Inc., 5
- Chrisman, James J., 1
- Clark, Major, 7
- coding, for procurement, 8
- commerce, electronic, 7
- consolidation, 1, 3
- contract bundling, 7
- Craig, Steven G., 1
- credit, 1
- data needs, 3
- Dewald, James R.,
- Eagle Eye Publishers, Inc., 6, 8
- economic data, 4
- economic development, 9
- economic indicators, 2, 3
- economy, 2
- electronic commerce, 7
- electronic procurement, 7
- entrepreneurship, 3
- environment, 9
- exporting, 6
- failures, 3
- Fairlie, Robert, 4
- Federal Procurement Data System, 6, 8
- financing, 2
- firm size data, 4
- foreign tax credit, 9
- frequently asked questions, 2
- General Services Administration, 6
- globalization, 6
- Hall, Jeremy, 1
- Hardee, Pauline, 1
- Headd, Brian, 3
- home-based business, 8
- Individual Contract Action Report, 8
- industry data, 4
- innovation, 2, 3, 5
- Innovation and Information Consultants, Inc., 7, 9
- Internal Revenue Service, 8
- Internet, business use of, 7
- Joint Committee on Taxation, 9
- Kauffman Foundation, 3
- Kuala Lumpur, Malaysia, brownfields in, 9
- lending, 3
- Los Angeles, California, brownfields in, 9
- manufacturers and brownfields, 9
- medical electronics, 5
- minorities in business, 2, 3
 - self-employment of, 4
 - procurement from, 7
- Moutray, Chad, 2, 3, 7
- new firms, 3
- oil research, 5
- Palmetto Consulting, Inc., 6
- Pociask, Stephen B., 5
- policy on small business, 3
- procurement, 2, 6, 7
 - business coding in, 8

- electronic, 7
- purchase cards, 7
- quasi-integration, 1
- regulation, 2, 3, 8, 9
 - and home-based businesses, 8
- self-employment, 4
- South Carolina, exporting in, 6
- Survey of Small Business Finances, 1
- taxes, 9
 - and home based businesses, 8
- technology, 3, 5
- technology transfer, 2
- telecommunications, 5
- TeleNomic Research, 5
- travel and entertainment deduction, 9
- United States Association for Small Business and Entrepreneurship, 1
- Veteran Entrepreneurship and Small Business Development Act of 1999, 11
- veterans and veteran-owned businesses, 10, 11
 - procurement from, 6, 7
- Waldman Associates, 10
- women-owned businesses, 2, 3
 - procurement from, 7
 - self-employment, 4
- zoning regulations and home-based businesses, 8