



BROKEN PROMISES

The Stalled Agenda
for American
Small Business

A report prepared by the

House Small Business
Committee Democrats

Nydia M. Velázquez, Ranking Democratic Member

BROKEN The Stalled Agenda **PROMISES** for American Small Business

Table of Contents

- I. Introduction
- II. Core Issues
 - Access to Capital
 - Business Checking
 - Economic Stimulus
 - Energy
 - Federal Contracting
 - Health Care
 - Regulatory/Paperwork Reduction
 - Pension Reform
 - The SBA Office of Advocacy
 - Taxes
 - Technology
 - Workforce Development
- III. The Wins that Weren't
- IV. Conclusion

Our Nation's Troubled and Turbulent Economy

Our nation is currently experiencing one of its worst recessions since World War II. In fact, of the 10 recorded recessions in our nation's history, only the 1973-1975 and the 1981-1982 have been longer and deeper than the current economic downturn. Unfortunately, the constant stream of bad news comes from all sectors of the economy.

Unemployment has grown to 6 percent, with 1.1 million Americans now jobless compared to a year ago. Consumer confidence, which for the past two years has been sustaining the economy, has dropped by nearly one-fifth. The stock market, reporting record growths during the boom of the 1990s has lost \$5.2 trillion in market value – a loss of more than 35 percent. The 23 percent average annual decline in the S&P 500 Index under President Bush is the sharpest decline on record since the Hoover Administration.

And last month was the worst September performance for the Dow Jones industry average since 1937. This decline in the stock market cost 401(k) and other defined contribution retirement plans over \$210 billion in 2001. This economic faltering is due, in large part, to the overemphasis placed by the Bush Administration and the Congressional Republican leadership on policies that benefit corporate America, while ignoring this nation's driving economic force – small business.

While the Bush Administration and Congressional Republicans have put their faith and our nation's economic well-being in the hands of big business, it is Main Street small business – not Wall Street – that steers this country's economy. Statements like "As General Motors goes, so goes the nation," could not be further from the truth. Small businesses do for this economy what big business cannot – they produce 75 percent of all new jobs, represent 99 percent of all employers and employ 53 percent of the private workforce. They provide almost 70 percent of workers with their first jobs and initial on the job training, and account for nearly 50 percent of all sales in this country. Clearly, small business is big business in America.

Small firms are also an essential vehicle for women, minorities and immigrants to enter the economic and social mainstream. In fact, minorities now own nearly 15 percent of all American businesses, or more than 3 million firms. In 1997, these firms had more than \$591 billion in revenue, created more than 4.5 million jobs and produced about \$96 billion in annual payroll.

Equally impressive is the growth phenomenon of women-owned businesses. This year, there are an estimated 6.2 million majority-owned, privately held women-owned businesses in the U.S., accounting for almost 30 percent of all privately-held firms. These firms generate \$1.15 trillion in sales and employ 9.2 million workers. From 1997 to 2002, the number of women-owned firms grew at twice the rate of all U.S. firms, employment grew at 1.5 times the national average, and sales rose at the same rate.

These statistics clearly show that small businesses are the lifeblood of the American economy. It is distressing that the dominant role small enterprise plays in the economy has been largely lost on the Bush Administration and the Congressional Republican leaders. Instead of pouring energy into the most stable and productive sector of our economy – small business – they have focused their efforts on trying to save big business.

Given the current economic climate and the wave of corporate scandals our country has witnessed over the last several months, it is easy to hold the belief that big business can either keep this country running – or grind it to a screeching halt. The Enron and Worldcom debacles point to how big businesses can wreak havoc on our economic system. The corporate malfeasance, the lack of trust in CEOs and the jitters caused by a mercurial stock market have shown that putting our trust in big business might not be in the best interest of our economy – or our country as a whole. Clearly the proper course should have been one that focused more heavily on the needs of small business and how to help this critical sector of our economy grow.

While both the Congressional Republican leadership and President Bush have spent much of 107th Congress publicly touting the importance of small business, very little was done to turn their rhetoric into reality. In fact, President Bush was in office for a little more than a year before he even announced his small business agenda, and this came several months after House Democrats had issued their own agenda in January. To date, nothing has been accomplished on the President's agenda entitled, American Small Businesses: Driving Innovation and Creating Jobs, unveiled on March 19, even though many of the issues the President cited enjoyed wide bipartisan support in Congress.

The lack of action on a small business agenda is not only obvious in the White House but also in the House of Representatives. The House Small Business Committee passed only six bills of which only two have been signed into law. This is in drastic contrast to the 106th Congress when 27 small business bills passed the House and 20 bills became law, addressing a wide array of small business concerns, from access to capital and regulatory relief to entrepreneurial development and technical assistance.

How the Bush Administration and the Republican Leadership Have Failed Small Business

“Broken Promises: The Stalled Agenda for American Small Business,” issued by the Democratic staff of the Small Business Committee is an analysis of the 107th Congress and the issues affecting small business. The report re-examines 12 topics detailing the problems confronting small business, the possible bipartisan solution, and how the failure of both the Congressional Republican leadership and the Bush Administration to act has affected small business.

This latest report also brings to light an interesting trend – when House Republicans did focus on an issue that had small business implications, they only viewed it only from a big business perspective, often producing solutions that either failed to aid small business or in some situations, exacerbated the problem.

It also evaluates the few alleged “wins” for small businesses. In many instances, these wins had very little effect at all on small business, were big business “wins” portrayed as victories for small enterprise, or in some cases, were outright misrepresentations. This issues report reflects how very little was accomplished for small business this year, despite promises by the Administration and the Republican Congressional leadership. Ultimately, the failure to push forward a small business legislative agenda has resulted in the mainstay and powerhouse of our economy without the tools they need to fuel a rebound in the near future.

Access to Capital

One of the most important components for small business success is the ability to gain access to capital. Financing that is affordable and easy to obtain is often difficult for small businesses to find. The Federal Reserve's most recent study on small business financing found that 82.5 percent of them used some form of credit. Smaller companies tend not to depend on traditional sources of capital, but rather rely on personal savings, loans from family and friends, and credit cards. Credit cards are actually the number one way small businesses are financed in their start-up phase. Since credit cards carry higher-than-average interest rates – normally between 18 and 25 percent, and sometimes higher – these small businesses often struggle to stay afloat financially.

The Growing Credit Crunch

With the economy currently in a recession and no real recovery in sight, the need for access to capital has increased at a time when its availability has decreased. All businesses, both large and small, need adequate access to capital for success. Whether it is costs associated with employees, start-up, expansion, or purchasing or repairing equipment, there are always new expenses that crop up for small business owners. The burden falls even harder on small businesses that require financing in order to stay competitive with larger companies in the marketplace. And traditionally, small businesses have limited equity capital, fewer assets to pledge as collateral, uncertain earnings, and higher failure rates, which make it more difficult for them, compared to large corporations, to secure the capital they need.

Financial Modernization: Not enough for Small Business

This credit crunch has continued despite the passage in 1999 of the Financial Modernization Act, also known as Gramm-Leach-Bliley. This legislation reworked our nation's depression-era banking laws that had erected firewalls between financial services and commerce. The goal of financial modernization was to create a more flexible system allowing small businesses greater options and access to an array of financial services. Whether this goal has been attained is still questionable. In the end, bank consolidation through financial modernization may have shifted this nation from a credit system in which small businesses' relationships with their local bankers played a key role in obtaining financing, to a system with a heightened dependency on credit scoring. This shift only further exacerbates the credit challenges confronted by small business.

Key Role of SBA Programs

Given today's financial climate, the Small Business Administration (SBA) loan programs are critical to small business growth and development. By providing \$99 in private funds for every \$1 of public funds, SBA loan programs are the government's best bargain. Currently, these programs represent 40 percent of all long-term lending to small businesses nationwide. This translates into jobs and a net return on investments for our local communities.

The essential role these loan programs play have apparently been overlooked by the Bush Administration and the Republican House Leadership in the 107th Congress. This is reflected in recent policy decisions, including the budget which proposes to cut the SBA loan programs in half. Such a deep cut will remove \$5 billion worth of resources and capital from an already weakened U.S. economy. According to the American Small Business Alliance (ASBA), the

Bush cut to these loan programs will translate into the loss of almost 200,000 American small business jobs nationwide.

While many lawmakers simply focus on the impact of interest rates, equal emphasis must be placed on the borrower's loan fees, which can cost tens of thousands of dollars. In recent years, Congress has decreased the federal commitment to these loan programs through budgetary cutbacks. In the past decade alone, government loan financing dropped from almost half a billion dollars in the 1990s to only \$88 million last year. As the federal commitment to such critical sources of capital wanes, the shortfall is made up by small businesses that are required to pay additional fees. This increase in fees has cost small businesses billions of dollars, and shows our government's failure to follow through on its financial obligation to our nation's small enterprise.

OMB's Enron Accounting

The capital crunch facing our nation's small businesses was made worse by the Enron-like accounting practices of the Bush Administration's Office of Management and Budget (OMB). OMB is effectively "cooking" the federal books on government backed loans for small businesses. Every time a small firm receives an SBA-backed loan, they are overcharged. This translates into a stealth small business tax of \$2,500 to \$18,000 per loan. These funds sit idly in the U.S. Treasury when they could certainly be better spent helping small businesses expand. The overcharging is so problematic that a recent study by the General Accounting Office (GAO) has estimated that small businesses and lenders have been taxed by almost \$1.5 billion in the last 10 years.

Credit Rationing by the Administration

Not only are small businesses now being grossly overcharged by these fees, but they are also facing a recent decision by the Bush Administration to institute credit rationing. This rationing will result in a decrease of billions of dollars in capital at a time when investment is critical. The result of this latest move by the Administration will mean less economic growth in a time of recession. It will also leave many small firms undercapitalized, which is a main factor in business failures.

Conclusion

The only way small businesses can gain the momentum they need to revive our lagging economy is through access to capital. Through funding assistance, small businesses are able to grow, create jobs and continue as the catalyst of our economic growth. Unfortunately, due to the Bush Administration's recent policies and the Congressional leadership's failure to fix them – or block them entirely – the capital crunch for small firms has only intensified.

Business Checking

Capital is a necessary but often elusive ingredient in the small business formula for success. Small businesses face an array of barriers to accessing the capital they need for start-up, operation and expansion. One of these barriers, which could be easily solved by Congress, is a Depression-era law that prohibits interest-bearing checking accounts.

The law, enacted as part of the Banking Act of 1933, was meant to keep banks solvent during the Great Depression. Almost 70 years later, the law is still in effect, despite evidence that it is no longer valid – or necessary. In fact, a 1996 joint report issued by the Federal Reserve Board, the Federal Deposit Insurance Corporation, the Office of the Comptroller of the Currency and the Office of Thrift Supervision stated that the law prohibiting payment on business checking accounts “no longer serves a public purpose.”

Outdated Law Hurts Small Enterprise

This law creates a double standard – one for small business and another for large companies. Small businesses are banned from receiving interest on their business checking accounts when large corporations can exploit loopholes in the system, by utilizing their vast resources, and employing accounting charades, to avoid the ban. While small businesses are forced to struggle with this law and hope for a change, corporate America continues to reap the benefits.

The obvious solution to this problem is to repeal the law banning the earning of interest on checking accounts. In a 2001 survey conducted by the National Federation of Independent Business (NFIB), 86 percent of small business owners said they should be able to earn interest on their checking accounts.

Simple Solution to Business Checking Problem

In March, President Bush announced his small business agenda. In it, one of the focal points was repealing the ban on interest bearing checking accounts. He stated that “for many small businesses, the interest income on checking account balances would defray other significant costs.” But to date, there has been no concrete action by the White House to turn this rhetoric into reality.

To right this small business wrong legislatively, two bills introduced by the House – one during the first session and another during the second – repealed this antiquated law. The Small Business Interest Checking Act of 2001 (H.R. 974), and the Business Checking Act of 2002 (H.R. 1009), have the support of small business and banking associations, but they have yet to be made law by this Congress and Administration.

Conclusion

While it has been more than a year since the House passed H.R. 974, the legislation waits for the House leadership to give it the priority it deserves. There is a simple legislative solution to solve this problem, yet small businesses must remain in a competitive disadvantage with corporate America until Congress decides to act. Until this legislation moves, small businesses will just have to continue paying the price in increased expenditures and less capital for a law that no longer serves any valid purpose.

Economic Stimulus

The terrorist attacks of September 11 sent the U.S. economy, already in a slump, into a full recession. The nation's priorities instantly shifted in the weeks immediately following the attacks from our economy to our security. But attention then failed to refocus on one of the sectors hardest hit by the 9/11 attacks – American small businesses. While large corporations have the resources to weather unforeseen economic changes and are helped by government bailouts, small businesses, operating on such slim profit margins, struggle to stay afloat.

9/11's Immediate Impact on Small Business

While shockwaves from the attacks reverberated throughout the country and unemployment rose to a ten-year high of 6 percent, those in the travel/tourism and related industries started to sink. Estimates were that the small aviation companies lost approximately \$300-\$400 million and were forced to furlough thousands of employees in the months directly after the attacks. Similarly, September 2001 was one of the worst months for restaurants in the industry's history and hotels posted losses of \$10 million a day.

The ripple effect stretched across many small business sectors and industries. Airlines were grounded for several days and months passed before they resumed normal flight schedules. Some local flight school airports and smaller private plane airports were forced by the government to close down entirely. As air travel by Americans declined sharply, air transport companies – the majority of which are small and minority-owned businesses – saw their customer base evaporate.

Airline Bailout

The House Republican leadership acted quickly to pass an airline bailout bill. The measure gave this nation's airlines \$5 billion in immediate cash assistance and \$10 billion in loan guarantees to keep several major carriers from collapsing. While the airline industry received a multibillion dollar bailout from the government, nothing was done to help small businesses recover.

Current State of the Economy

Now, more than a year later, there is serious talk of the economy having a double dip recession. Maury Haris, an economist with global investment banking giant UBS Warburg, puts the chances of a double dip recession at one in four. Today, there are over 1.1 million fewer people employed than a year ago, most of them former employees of the travel and tourism industry. The motor coach industry, which is dominated by small businesses and provides an essential service to a low-income demographic, saw a 30 percent reduction in passenger travel in the last year. Travel agencies continue to struggle and many were forced to close down – one-eighth of this country's local, family-owned travel agencies have shut down in the last 13 months.

Small Business Help is Stalled

Shortly after the House passed its airline bailout bill, the House Committee on Small Business marked up and passed bipartisan legislation to help this nation's small businesses survive the economic downturn. The American Small Business Emergency Relief and Recovery Act of 2001 (H.R. 3230), would have provided sustainability grants, low- and no-interest loans, and technical assistance to small businesses across the nation.

This was a sound bipartisan legislative solution to help small businesses based on testimony by small firms on the hardships they faced after the terrorist attacks. Even after it was reported out of the House Small Business Committee, the Republican leadership refused to allow this critical bill consideration on the House floor. A similar proposal passed the Senate, yet the House leadership refused to allow the bill's debate on the House floor.

Conclusion

The airline bailout was a necessary step to help this struggling industry, but Congress and the Administration stood by for months and did nothing to help small businesses. This is just another example of how the Bush Administration and Republican Congressional leaders consistently put the needs of Wall Street and corporate America over Main Street. Even a year post-September 11, many small firms continue to search for assistance as our economy shows few signs of a strong rebound in the near future.

Energy

America's small businesses now account for more than half of all energy consumption in North America. High energy consumption is the sign of a strong economy, yet high energy prices contributed to the ongoing recession in the small business sector. For more than 30 years, domestic energy consumption has grown at twice the rate of domestic production. This supply shortfall will only continue to grow in the coming years, causing rolling blackouts, price spikes and job losses for small businesses across the country. The Bush Administration has failed to ensure that our country has ready access to secure supplies of clean, affordable energy sources so that small businesses can continue to thrive and contribute to our nation's economy.

The growth and development of small businesses depends on an affordable and reliable energy supply. Energy supplies are now stretched and many small businesses are struggling to pay their bills. In fact, electricity demand increased by 13 percent between 1996 and 2000 alone. Short supplies of electricity and natural gas, and the inflated price of petroleum, have caused severe economic hardships for small businesses. American small enterprises need solutions to help them face the rising energy costs associated with running a business.

Energy Efficient Technology

It is apparent that the federal government must increase funding for research and development of new technologies in energy. Large businesses have the capability to employ engineering staff or consultants to manage their use of electricity, but small business owners often struggle to reduce their electricity costs without expert advice or consultation.

There is tremendous potential for small businesses to lead the nation in reducing energy consumption through the development of new energy-efficient technologies. Through energy saving techniques such as solar power and water heaters, small businesses can save billions of dollars every year. Using energy efficient technologies, small businesses can assess in real time their energy usage and costs and can, in turn, modify their behaviors accordingly. The Administration's energy plan does not sufficiently increase funds for R&D in the area of energy efficiency, forcing small businesses to run their operations without the understanding of, and access or ability to utilize new energy saving technologies.

Tax Incentives

Small businesses also need increased tax incentives to aid them in affording the new energy efficient technologies. Even when such products exist, small businesses are unable to afford them because the purchasing and installation costs are often prohibitively high. Tax incentives for energy efficient products and practices are the best way to help them conserve energy and keep their energy costs down. Unfortunately, the Bush Administration has not emphasized greater energy efficiency as a high enough priority. In addition, it has failed to help small businesses take their energy matters into their own hands by providing tax and other incentives when they use energy-efficient techniques in their day-to-day business operations.

Energy Supply

Renewable energy and new technologies cannot be addressed without looking at the broader issue of supply. Across the nation, energy costs are on the rise with small businesses – especially those that use higher-than-average amounts of fuel or electric power, or depend heavily on shipping – struggling to keep up. The Department of Energy (DOE) predicts 65 percent foreign oil dependence by 2020. Security concerns since the September 11 attacks have caused us to question the wisdom of our dependence on foreign supplies of energy. The Bush Administration’s only response to this issue has been to propose opening up the Arctic National Wildlife Refuge (ANWR) for exploration. Unless the Administration pursues long-term, environmentally sound energy production solutions, small businesses will continue to falter in their attempts to keep up with increasingly high energy costs.

Securing America’s Future Energy Act

The Bush Administration’s energy plan, Securing America’s Future Energy Act (H.R. 4) ignores high-tech, energy-efficient solutions in favor of increased oil, gas, coal, and nuclear production. The House passed a version of Bush’s plan to represent the first comprehensive energy legislation in ten years. Rather than addressing the needs of small businesses, the Republican leadership in the House included \$34 billion in subsidies to big oil and gas corporations, while providing negligible incentives for small businesses. Instead of depending on oil, coal and nuclear power for our energy needs, we should be adopting an energy policy that is based on efficiency, renewable energy and responsible supply. Small businesses could lead in the areas of energy efficiency and renewable energy while keeping down their energy costs, if provisions are included in the stalled conference report, that support these crucial activities.

Conclusion

Without a comprehensive national energy policy that addresses their needs, small businesses will continue to struggle with high energy prices which impact their bottom line. Until the Bush Administration moves forward with a national energy policy that capitalizes on the benefits small businesses can offer our nation, we will not see the true contribution that they can make to our floundering economy.

Federal Contracting

The U.S. government is the largest buyer of goods and services in the world with more than \$219 billion in purchases in 2001. And the federal marketplace continues to expand its reach by billions each year, growing by almost \$20 billion from FY 2000 to FY 2001.

Even though federal procurement dollars rose 10 percent over this time, opportunities for small businesses – including small, minority- and women-owned firms – did not keep pace with this growth, rising only two percent. Small businesses continue to be shut out of the federal marketplace due to a flawed contracting system, which has led to the growing practice of contract consolidation.

While on the campaign trail and after he took office, President Bush specifically addressed contract consolidation. Despite his promises to open the federal marketplace to small firms, he has taken no concrete action to date. Legislative solutions remain stalled in Congress by the Republican leadership, and a law enacted in 2000 to help women-owned businesses secure federal contracts has yet to be implemented by the Bush Administration.

In 2001, for the second year in a row, the federal government overall failed to meet its small business goal of 23 percent, costing small businesses an estimated \$417 million in federal contracts. In addition, federal agencies overall failed to meet any of their specific contracting goals for minority- and women-owned firms, costing these businesses approximately \$7 billion in just one year.

The President's Empty Pledge

When the President unveiled his small business agenda in March of this year, he called for real reform and an end to contract consolidation, stating that “wherever possible, we’re going to insist we break down large federal contracts so that small business owners have got a fair shot at federal contracting.” It was the first time that a President had publicly pledged to help small businesses gain better access to the federal marketplace by battling contract consolidation.

Unfortunately, no action has been taken by the White House or any federal agency head despite the president’s statements. In fact, when Small Business Committee Democrats asked to work with the President to restructure 10 big contracts displacing small businesses, their request went unanswered.

Citing the President’s Small Business Agenda and the detrimental effect contract bundling has on small business, the Small Business Administration’s (SBA) Office of Advocacy even released a report in early October showing that the number and size of bundled contracts issued by federal agencies has reached a 10-year high. The report also revealed how small businesses received only 16.7 percent of bundled federal contract dollars in fiscal year 2001.

Legislation Fighting Contract Consolidation

There are legislative solutions that have been introduced in Congress to fight contract consolidation. In April of 2001, the Small Business Opportunity Enhancement Act of 2001 (H.R. 2867) was introduced and enjoys broad bipartisan support. This bill would give the SBA more authority to recommend strategies to enhance small business prime contracting opportunities early in the procurement process. Even though this legislation was reported

unanimously out of Committee during Small Business Week this past May, it was pulled from the House floor schedule that same week by the Republican leadership and has never been given further consideration.

Another piece of legislation introduced in 2000, the Small Business Contract Equity Act (H.R. 1324), would strengthen the SBA's role in holding an agency accountable for meeting its small business goals. Essentially, the bill would tie the ability of a federal agency to bundle contracts directly to its statutory small business goals. If an agency fails to achieve its goals, it would be unable to bundle contracts for one full fiscal year. This legislation has also won support from both sides of the aisle, but it has not even been marked up by the House Small Business Committee.

Administration Still Blocks Implementation of Women's Procurement Program

The federal marketplace remains largely closed to women-owned firms, even though a law has existed for 2 years, which the Bush Administration fails to implement, that would provide billions of dollars of contracting opportunities to them. Enacted in December of 2000, P.L. 106-554, the Women's Procurement Program would provide women-owned businesses with a vehicle to gain entry into the federal marketplace by allowing agencies to restrict competition on contracts in certain industries. In support of the program, a draft study performed by the SBA revealed that 66 out of the 71 industries surveyed were underrepresented by women-owned businesses.

Women-owned businesses account for nearly 30 percent of all privately held firms. However the federal government – in failing to meet its women-owned business goal of 5 percent in 2001 – cost these firms \$5.5 billion in federal contracts. If the Women's Procurement Program had been implemented by the Administration, the women-owned business goal would have been reached and such firms could play a greater role in our economic recovery.

Conclusion

Federal agencies' commonplace use of contract consolidation has caused a steep decline in small business opportunities. Small businesses have worked with the U.S. government for decades, providing quality products at competitive prices. With our economy in a weakened state, now is the time to ensure the door to federal contracting opportunities is open.

Although the President made a pledge to help small business, there has been no attempt by his Administration to curb contract consolidation. The Republican leadership has stalled efforts to move critical bills that would provide small businesses greater access to the federal marketplace. Without support from top Administration officials at federal agencies, along with legislation to fix the flawed procurement system now in place, small businesses will remain a player on the sidelines of the federal procurement arena.

Health Care

With the skyrocketing costs of health care, small employers are struggling now more than ever to offer affordable health care options to their employees. Congress and the Administration have failed small business in its health care reform efforts on two levels.

First, Congress and the Administration have failed to expand access to affordable health care insurance for small businesses. Such options include establishing federally regulated Association Health Plans (AHPs) or expanding tax breaks for health care insurance coverage for employers.

Second, the Administration has not addressed Medicare reform problems and their effect on small business health care providers. Small business health care providers are being ignored by the Administration as the President's agencies continue to adopt burdensome regulations while promoting a prescription drug card proposal that will harm many small business health care providers.

Access to Coverage: Association Health Plans

Association Health Plans (AHPs) are one way Congress can help small businesses to lower health care costs. Small businesses are being priced out of the health care market and Congress and the Administration have failed to help the 24 million uninsured Americans working for small businesses.

AHPs allow small business employers to join forces through trade and professional associations to purchase affordable health benefits. AHPs empower small businesses with the same tools that large corporations currently have in offering comprehensive health care benefits to their employees. By joining together, small employers will provide enhanced coverage through reduced administrative costs, increased bargaining power, and economies of scale.

Although AHPs have received broad support from small employers, Congress and the Administration have failed to act. This comes at a time when premiums in 2002 are expected to rise by 13 percent for employers who offer insurance. AHPs will create an affordable option for the 53 percent of small businesses that currently cannot afford to offer insurance coverage to their employees.

Legislation has been introduced in the House and Senate, the Small Business Health Fairness Act (H.R. 1774 and S.858), containing safeguards to ensure that AHPs meet solvency requirements and prevent the "cherry-picking" of employers with healthy employees. In 2002, Speaker Hastert claimed that Republicans "would focus on enacting market reforms that will give millions of Americans access to health care through AHPs." Despite these promises, the legislation in the House has stalled despite the fact that AHPs would make quality health insurance more affordable and accessible for small business owners and their employees.

Access to Coverage: Deductibility of Health Insurance Costs

Many small businesses in America are not offering certain health insurance options because the owners are not eligible to participate. Currently, the tax code unfairly discriminates against small business owners who offer the popular Code Section 125 cafeteria plan coverage to their

employees. Cafeteria plans offer comprehensive benefits under which employees may choose their own “menu” of benefits consisting of cash and qualified benefits. However, under the code, sole proprietors or partners who sponsor a cafeteria plan for their employers are not eligible to participate in the plan. Additionally, self-employed individuals are prohibited from participating in cafeteria plans.

Although small business owners are eligible to participate in other types of health coverage purchased from insurers, the code does not offer the same benefit for cafeteria plans. In contrast, all employees in large corporations are eligible to enjoy the benefits of deducting health insurance premiums from their income because each participant is considered an “employee” under Code Section 125.

The net effect of this provision is to discourage small business owners from offering cafeteria plan coverage to their employees. Rather than offering plans which allow employees greater choice, employers are forced to select health insurance options which they are eligible to participate in even though they would prefer to implement a cafeteria plan. Despite the existing inequity, Congress and the Administration have continued to ignore the needs of small employers while maintaining the beneficial tax treatments that large corporations already receive.

Medicare Reform – Regulatory Burdens on Small Business Health Care Providers

The Administration and its agencies have failed to implement effective Medicare reform to account for the needs of small businesses providing health care services. Under the Regulatory Flexibility Act (RFA), the Centers for Medicare and Medicaid Services (CMS), is required to consider the impact of any Medicare regulations on small businesses. CMS has consistently implemented regulations that fail to adequately address the unnecessary burdens on small health care providers, such as physicians, portable X-ray providers, community pharmacists, or the residual effects on Medicare beneficiaries.

The most common complaint among small businesses is the complex and burdensome Medicare regulations. Some physicians estimate they are spending one hour on Medicare forms and administrative requirements for every one to four hours of patient care. This administrative burden, in conjunction with the overall 5.4 percent decrease in Medicare payment to physicians, has forced many small business health care providers to restrict the number of Medicare patients they serve.

In a survey by the Washington State Medical Association (WSMA) of nearly 200 of its members, approximately 45 percent said they will stop taking new Medicare patients and 12 percent said they will drop all Medicare patients because of increased regulation and decreased compensation. As the Administration continues to enact Medicare regulations while failing to recognize the needs of small businesses, these problems will only get worse as more providers will be forced to stop providing services to any existing or new Medicare patients.

Medicare Reform – Prescription Drug Card Harms Community Pharmacies as well as Medicare Beneficiaries

Another initiative that will particularly harm small health care providers and Medicare beneficiaries is the president’s Medicare prescription drug discount card plan (H.R. 4954). The Administration initially attempted to override the legislative process and establish the drug card plan through the U.S. Department of Health and Human Services (HHS). The President’s

proposal was successfully challenged in the courts, but the President has gone forward with a second drug card proposal through HHS. The problem is that the proposed discount card program fails to attack the root of the prescription drug problem while having harsh effects on community pharmacies.

Rather than target the pharmaceutical companies that are experiencing record profits, the Administration has tried to address the problem through its prescription drug card plan. The proposal was developed by a select group of big business “pharmacy benefits managers” (PBMs) in a closed-door session with the Administration. Despite substantial evidence that prescription drug discount cards do not pass savings along to the patients who enroll in them, the Administration forged ahead. In fact, on October 7, 2002, prescription drug companies hiked their prices on a similar discount drug program already in place. The driving force behind marketing the prescription drug discount cards is the rebates the middle-man (PBMs) receives from the big drug manufacturers for promoting their products and brands. A GAO investigation in December 2001 verified that prices for prescription drugs using discount cards are not significantly different than prices available at local pharmacies and over the Internet.

The structure of the proposed discount card program means that pharmaceutical companies are likely to steer beneficiaries to mail-order for medication which could cost community pharmacies between \$30 million and \$50 million a year in profits. It is estimated that the President’s proposal could cause as many as 20 percent of drugstores to go out of business. The discount drug card approach may also limit the access seniors have to medication consultation services by providing enrollees with financial incentives to use mail-order pharmacies. The overall effect of burdensome regulations and ineffective reform will ultimately mean less access to medication for seniors and the loss of many community pharmacies in America.

Conclusion

Small businesses have few options when it comes to offering health care coverage to their employees. They are confronted with the difficult task of purchasing coverage from insurers who have nearly monopolistic power over the market. To compound the problem, the tax code unfairly prevents them from taking advantage of the tax breaks that corporations can use to offer comprehensive coverage to their employees. Not only has the Administration failed to remedy the problem, but it has also pushed for legislation that will only increase the burdens on small businesses. Additionally, the Administration’s proposed Medicare reforms will force many small business providers to either stop offering services to Medicare beneficiaries or go out of business altogether. These failures only reflect how the President and the 107th Congress have continued to ignore the needs of the small business community in their health care reform efforts.

Regulatory/Paperwork Reduction

Regulatory compliance and paperwork consistently rank as one of the top ten concerns facing small businesses in America today. Statistics show that compliance and paperwork are perhaps the most costly and burdensome challenges for small firms to overcome.

In an October 2001 report, the Small Business Administration (SBA) estimated that large firms (with over 500 employees) spend \$4,463 per employee to comply with federal regulatory and paperwork reduction. However, costs to small businesses (with fewer than 20 employees) are nearly 60 percent greater at \$6,975 per employee.

When the President unveiled his small business agenda this year, “cleaning up the regulatory burdens on small business,” was at the top of his list. He stated that “every agency is required to analyze the impact of new regulations on small businesses before issuing them.” Unfortunately, even with his promises, the President has done nothing to reduce these burdens.

Failing to Reduce the Paperwork Burden on Small Business

More than two decades ago, Congress recognized the need to minimize the paperwork burden on small business and passed the Paperwork Reduction Act (PRA). The goal of this legislation was to minimize the cost and time required of small business owners to comply with federal paperwork while maximizing the usefulness of the information requested.

The Paperwork Reduction Act regulates the collection of information by federal agencies, making them “more accountable for reducing the burden of federal paperwork on the public.” An agency cannot require reporting from small businesses without first receiving approval from OMB. This check was put in place to ensure that federal agencies do not ask for unnecessary or redundant information that would be time consuming and costly for small firms.

The PRA was reauthorized and expanded in 1995 to set goals of paperwork reduction on small firms at 10 percent for the first year and 5 percent for each subsequent year. Unfortunately, the paperwork burden on small business has continued to rise and in 2000 had reached 180 million hours. The Republican leadership’s failure to act has resulted in the expiration of the PRA’s reauthorization.

Given the remarks of the President pushing for fairness relating to small business and federal paperwork, it is disappointing that minor changes were made to help small businesses better cope with paperwork burdens by the Small Business Paperwork Reduction Act (H.R. 327), which does little more than create an OMB working group to find ways to reduce paperwork. The legislation does nothing to reduce burdens or to increase transparency, which are important to ensure fair paperwork requirements.

Federal Regulatory Burden on Small Business Will Continue to Increase

While paperwork compliance is a challenge for small business, so are agency regulations. Often regulations are created without taking into account the effect they will have on small business. Like the PRA, the Regulatory Flexibility Act (RFA) was also enacted in 1980 to ensure that agencies examine the impact their regulations have on small businesses.

The most recent improvement to RFA was the Small Business Regulatory Enforcement Fairness Act (SBREFA). SBREFA was a step towards better protecting small business from burdensome government regulations. This statute established a formal procedure for rule development by two of the most problematic agencies – the Environmental Protection Agency (EPA) and the Occupational Safety and Health Administration (OSHA).

These entities have a significant economic impact on small business. Through SBREFA, before the final acceptance of a regulation both EPA and OSHA must lead a discussion about the proposed rule with affected small businesses. This has resulted in improved regulations that have a less detrimental effect on small companies. SBREFA is certainly a strong start, but much more needs to be done to bring fairness to the federal rulemaking process.

Other agencies with an array of regulations that impact small businesses include the Federal Communications Commission (FCC), the Centers for Medicaid and Medicare Services (CMS) and the Internal Revenue Service (IRS). Last year, the FCC developed more rules than any other federal entity that would apply to – and affect – small business. CMS also has a long list of regulations developed without taking small business concerns into account. These agencies are responsible for the majority of regulatory burdens on small businesses, and until their regulatory challenges are addressed, small businesses will continue to see a significant impact from federal regulations on their operations.

There is bipartisan legislation to enhance SBREFA, such as the Small Business Review Panel Technical Amendments Act of 1999 (H.R. 542). This would amend provisions of SBREFA to ensure “full analysis of potential impacts on small entities of rules proposed by certain agencies.” One of these agencies is the IRS, which places the largest regulatory burden on small businesses. Unfortunately this bill, which was introduced in the first session of the 107th Congress, did not even receive a hearing. In addition, a similar bill with an identical goal was introduced in the Senate, the Agency Accountability Act of 2001 (S. 849).

Conclusion

Given the lofty rhetoric and the statements about reducing the regulatory and paperwork burden on small business by the House Republicans and the Administration, it is difficult to believe that they have allowed the Paperwork Reduction Act (PRA) to lapse. Their failure to move forward any improvements to SBREFA calling for increased enforcement as it relates to the worst regulatory offenders, including the IRS, CMS, and the FCC, will also result in a growing gap between the compliance costs placed on small businesses and those that are more easily absorbed and managed by their corporate counterparts.

Pension Reform

With the plummeting stock market, working Americans are becoming more aware of the harsh reality of failing to adequately save for retirement. As such, it is extremely important for small businesses to offer comprehensive retirement coverage to recruit and maintain its workforce. Many small businesses, however, cannot afford to sponsor employee benefit plans due to the extremely complex reporting requirements and inequities in the tax code favoring large corporations. Although Congress recognized these problems and worked in a bipartisan manner to offer concrete solutions in the Portman-Cardin pension bill (H.R. 10 – passed by a vote of 407 – 24 in the House in 2001), the Administration ignored the needs of small businesses and adopted a “one size fits all” approach to pension reform in its 2001 tax bill.

In the Administration’s tax bill, Economic Growth and Tax Relief Reconciliation Act of 2001 (EGTRRA, P.L. 107-16), the President had the perfect opportunity to reduce the gap in pension coverage between large and small employers. However, the president ignored bipartisan efforts as seen in the comprehensive Portman-Cardin bill, and instead pushed through his tax bill that failed to address small business pension issues and whose primary beneficiaries are the highly compensated executives of corporate pension plans. Not only has the Administration and the House failed to ease the burden on small employers, but it also continues to support legislation that will only exacerbate these problems. The Pension Security Act passed by the House in 2002, intended to punish the corporate malfeasance of Enron-like corporations, will only increase the burdens on small businesses. It is another example of how the President and the House leadership have failed to examine the unintended consequences such legislation has on small businesses.

Small Business Pension Coverage – Start-up Costs

The greatest impediment to small businesses in offering retirement coverage are the start-up costs associated with implementing a 401(k), SIMPLE (Savings Incentive Match Plan for Employee), or other pension plan. For small businesses, setting up a plan can cost up to \$20,000, if not more, due to complex rules and regulations. Small employers are confronted with the difficult task of setting up pension plans in a tax structure designed for large corporations.

To remedy the problem of start-up costs for small businesses, Congress originally proposed a \$6,000 credit for small businesses for the costs associated with implementing a pension plan for its employees (H.R. 738). Despite clear support for the change, the President’s bill provides for only a \$500 credit for three years to defray the costs of setting up a pension plan.

Small Business Pension Coverage – “One Size Fits All” Punishes Small Businesses

As the pension system has become increasingly complex, many small employers hesitate to offer coverage due to compliance and liability concerns. For those employers who can afford to set up plans, they must comply with the numerous reporting and testing requirements under ERISA (Employee Retirement Income Security Act). These requirements, which were designed for large corporate plans, are the same regardless of whether a business has five or 5,000 employees. Previous versions of the President’s tax bill repealed and modified a wide range of these unnecessary and outdated rules and regulations. However, despite bipartisan support, the vast majority of these provisions were left out of the final tax bill. To complicate the issue even

further, the House has passed the Pension Security Act of 2002, which increases the reporting requirements for employers who sponsor a pension plan.

One of the reporting requirements for employer sponsored pension plans is the complicated annual Form 5500 which must be filed with the Department of Labor. Congress and the IRS originally designed these forms to account for the assets of plans managed by large corporations. Congress has introduced numerous bills to create a Form 5500 that is simpler and catered to the make-up of small business pension plans. However, despite numerous meetings with the House leadership, the President did not make this a priority and small employers are still forced to hire expensive tax professionals to file these annual reports.

Small employers who elect to adopt 401(k) plans are also subject to a myriad of nondiscrimination, minimum coverage and “top heavy” requirements which unfairly discriminate against small employers due to economies of scale and liability costs. These requirements are so complex that small firms end up paying considerably more per employee to establish, administer, and monitor such plans than large firms. Despite bipartisan support to repeal the complex top heavy rules, these provisions were never included in any finalized bills coming out of the House. Though the President’s scaled-down tax bill included some of the proposed changes, small businesses are still subject to the complex top heavy and other testing requirements.

Pension Coverage – Inequity in Contribution Limits

Due to the complex testing and reporting requirements, many small employers elect to sponsor Savings Incentive Match Plan for Employee (SIMPLE) because they are easier to administer than 401(k) or profit sharing plans. These plans have fewer reporting requirements and are specifically targeted to small businesses. A major drawback to SIMPLEs are that employees and owners can only deduct \$7,000 (in 2002) for contributions while participants in a corporate sponsored 401(k) plan are eligible to deduct \$11,000 (in 2002). Congress and the President had the opportunity to harmonize the contribution limits of the 401(k) limits and SIMPLE plans. Instead, the focus of the President’s tax bill was only on increasing the contribution limits for 401(k) plans, which are generally favored by big businesses. This continued disparity in the contribution limits between SIMPLE and the 401(k) plans will only widen the gap in the pension coverage between employees of small and large employers.

It is estimated that less than one-third of employees working for firms with fewer than 25 employees are covered by a retirement plan, and only about one-half of employees working with firms between 25-99 people are covered. By comparison, over 80 percent of employees working for firms with over 100 employees are covered by a plan.

Conclusion

Currently, the tax code and complex reporting requirements for pensions favor big businesses while making it extremely expensive for small businesses to set up and operate retirement plans. The Administration had a perfect vehicle in the popular Portman-Cardin bill to make retirement security available to millions of workers by expanding small business retirement plans and allowing workers to save more for retirement. The bill provided for repeal of the top heavy rules, reporting simplification, and increased contribution limits which targeted both big and small businesses. Instead, the President enacted a pension reform bill designed for big business and continues to push bills with a focus on big business while leaving small businesses behind.

The SBA Office of Advocacy

Although small businesses are a driving force in our economy, policymakers often overlook the important role they play in the marketplace. Small businesses lack the resources to pay for the high-priced lobbying organizations used by corporate America to make their voices heard. In the end, small business needs are usually drowned out by a sea of special interests.

Acknowledging this disparity, Congress established the Small Business Administration's Office of Advocacy in 1976. Advocacy's main role was to act as a collective voice for small business in policy deliberations across the federal government. With its Congressional mandate, the SBA's Office of Advocacy was made a policymaking partner with other federal agencies to speak for, protect and preserve the interests of small business.

Advocating For Small Business Interests

The Office of Advocacy has been termed "the premier federal government advocate for small businesses." As a small business ally, the Office is tasked with bringing credible facts about small enterprise to Congress, the Administration and other lawmakers. Another primary function of Advocacy is to represent small business concerns in the government regulatory and rulemaking process, sometimes taking issue with the Administration for policy decisions that hurt small firms.

Advocacy has proven to have extensive reach into the policy-making arena. From 1994 to 2001, it issued over 100 reports and economic studies, testified before Congress more than 30 times, intervened in over 200 agency rulemaking proceedings, reviewed over 5,000 regulations, and filed the first amicus curiae brief in the history of the Office. It also reduced the regulatory burden on small business by \$16 billion through comments on regulatory proposals and the successful implementation of the Small Business Regulatory Enforcement Fairness Act.

An Independent Voice for Small Business

The main reason for the Office of Advocacy's success is simple – it stays true to its core mission of protecting the interests of small businesses and this nation's entrepreneurs. This simplicity has been its guiding force and its greatest strength. Perhaps most importantly Advocacy, unlike any other federal agency, has the unique ability to take positions that are contrary to the Administration.

To safeguard this independence as much as possible, Advocacy can submit reports, correspondence and testimony directly to Congress, unlike other agencies that must first clear documents through the Office of Management and Budget (OMB). This has allowed the Chief Counsel of Advocacy to expose injustices and criticize policy rather than bend under the pressure of the Administration and the OMB.

Attacks on Advocacy's Independence

While Advocacy has fought to maintain its independence, its current structure is counterproductive to keeping it free from external influence. Since Advocacy's funding is currently part of the SBA's overall budget, it is subject to use at the discretion of the Administrator. In the past, Advocacy has fallen victim to funding raids. When there is a

shortfall in the SBA's budget, the Administrator often looks to the Office of Advocacy to make up the difference.

Another barrier to Advocacy's independence is the lack of authority given to the Chief Counsel to hire and assemble the necessary team to advocate on behalf of small business. Therefore, the two critical aspects of SBA's Office of Advocacy's management – finances and hiring – are basically an extension of the SBA, which has a distinct and separate mission from that of the Office of Advocacy.

This proves especially problematic when the Office of Advocacy needs to carry out one of its prime functions – to oppose the policies of the President and federal agencies when they are harmful to small business. This can pit Advocacy against agencies and the Administration, when these are the very entities that oversee and determine its funding levels and hiring. In some instances, Advocacy has been a target of retribution – and silencing – by the Administration when its findings or policy recommendations differ from those of the President or his agency cabinet officials.

Attempts to Make Advocacy More Independent

During the first session of the 107th Congress, the Senate passed the Independent Office of Advocacy Act of 2001 (S. 395). The bill calls for Advocacy's statutory independence as well as adequate financial resources, including a separate authorization for appropriations. While this legislation would alleviate the SBA Administrator's influence over Advocacy's budget, it fails to give Advocacy true control over its funding and hiring.

During the second session of the 107th Congress, the House took up the Small Business Advocacy Improvement Act of 2002 (H.R. 4231). This bipartisan bill included a provision that would allow Advocacy to submit its budget directly to Congress, as the FDIC and the International Trade Commission currently do. This would solve the problem of interference by *both* SBA's Administrator and OMB. However, when H.R. 4231 was considered on the floor, this provision was removed at the last minute by the Republican leadership.

Conclusion

Both H.R. 4231 and S. 395 fail to adequately address the needs of the Office of Advocacy to maintain and obtain greater autonomy. In addition, there has been no further movement on either piece of legislation, including a motion to go to conference, since the bills passed in their respective bodies earlier this Congress. As a result, small business' ally in the Executive Branch – the SBA Office of Advocacy – will continue the fight for the independence it needs to effectively represent and protect the interests of small enterprise in America.

Taxes

For small businesses, taxes and the costs associated with complying with tax laws continue to be major concerns. With the slowing economy, targeted tax relief for small businesses can encourage investment and innovation, help small business in the new high-tech economy, and provide incentives for worker training. As part of his agenda, President Bush pledged to provide such relief through increased expensing, simplification of the tax code, and permanent repeal of the estate tax. Despite President Bush's promises for small business tax relief, he has failed to deliver.

A number of proposals were introduced this Congress to address the tax issues facing small businesses. Bills such as the Small Employer Tax Relief Act (SETRA) (H.R. 1037) and the Small Business Expensing Improvement Act (H.R. 657) focused on changing the myriad of tax code provisions, which not only favor large corporations, but also prevent small businesses from expanding. Tax problems for small businesses include deductions for equipment purchases, meals and entertainment expenditures, and business expansion expenses. The comprehensive SETRA addressed these issues by simplifying the relevant tax code provisions while providing significant tax relief to small business. However, this straightforward proposal and similar bills never moved out of the House, and the President failed to include these provisions as part of either his tax cut or his 2002 stimulus package.

Effective Tax Reform – Expense Treatment

Small businesses are reluctant to make capital expenditures due to the small number of tax benefits and complicated tax depreciation schedules. One of the greatest needs of small businesses is the ability to immediately expense the cost of investing in new capital, rather than depreciating it over numerous years. Currently, small businesses with investments under \$200,000 can expense \$25,000. The problem is that a majority of small business owners exceed the current expensing limits of \$25,000 in just three months.

The President has claimed that increasing the expensing amount for small businesses is a top priority on his agenda. Yet a number of bills have been introduced to increase the exemption level and have gone nowhere. Bills were introduced in the House, including the Small Business Expensing Improvement Act and SETRA, which would have raised the annual limit on expensing and increased the phase-out amount from \$25,000 to \$35,000 or \$50,000. Additionally, an increased expensing provision was originally included in the President's stimulus package, but it was later removed.

Immediate expensing allows additional investments for small firms to be expensed, enabling those businesses to expand and create new jobs. It lowers the cost of capital for tangible property and eliminates depreciation record-keeping requirements. A change will also increase small business owners' ability to compete in today's high technology markets. The failure of the President to act has harmed small businesses, especially in light of the numerous tax havens that already exist for large corporations that compete with small firms.

Fairness in the Tax Code – Meal and Entertainment Expenses

Small businesses typically rely on close personal relationships and customer service to compete for sales rather than on expensive advertising campaigns. In an effort to prevent the corporate three-martini lunch, Congress made meal and entertainment expenses only deductible up to 50

percent. In effect, this limited deduction has punished small businesses for abuses committed by corporate executives. SETRA proposed raising the deduction to 80 percent so that small business owners could deduct a critical expense in running their business. The House leadership failed to include this language in the president's tax cut or the stimulus package. This has left small businesses to choose between business development costs, which are partially deductible, and other less effective measures that are fully deductible.

Fairness in the Tax Code – Standard Home Office Deduction

While corporations can fully deduct their operation costs, home-based small businesses cannot deduct such costs. Adding to this inequity in deductibility is the fact that many small business owners do not even take the legitimate deductions because of the complex paperwork involved in doing so. The complicated record-keeping required by the IRS to qualify for a home office deduction is a barrier to many small business owners who would qualify, but don't have the time and staff to complete the paperwork.

Congress has failed to eliminate this problem. The barrier could be easily removed if a "standard deduction" for home-based businesses were allowed. Like the 1040 individual standard deduction, it would be optional. Owners could choose to continue to elect the standard deduction or deduct the depreciated amount plus operation costs, as they are currently allowed to do.

Fairness in the Tax Code – Fruitless Searches for Business Opportunities

One of the integral steps in growing small businesses is the search for new ventures and/or acquisitions. While a corporation that makes expenditures for new ventures may deduct them at a loss when it abandons its efforts, an unincorporated taxpayer, such as a sole proprietor or partner in a small business, is generally precluded from deducting expenditures for or investigating a new venture. This is one of many examples showing the benefits that corporations receive under the Internal Revenue Code that small proprietors do not.

Conclusion

Small businesses play an important role in our country's economic structure. However, small businesses continue to be adversely affected by our complex tax system which unfairly favors large corporations. By providing targeted tax relief to small business, the government can create the growth incentives necessary for them. Rather than follow the guidelines of SETRA, the Administration and the House instead pushed through a 2001 tax bill and a 2002 stimulus package that failed to adequately address the needs of small businesses. These bills provided broad tax relief for wealthy Americans, but did not include targeted proposals such as expensing, and home office deductions which would reduce these barriers to small business growth.

Technology

In today's 21st century marketplace, the role technology plays – both as a sector of the economy and in ensuring that small businesses are able to remain competitive – is increasingly critical. However, according to a recent survey, only 27 percent of small businesses with Web sites are currently selling their products and services via the Internet, and these sites average less than three web-based orders per month.

Small Business and Small IT Companies

Today, many small businesses are still very much on the outside looking into the world of electronic commerce. Small businesses face both access and affordability challenges in trying to secure high-speed Internet access (broadband), so key to maintaining an edge in the electronic marketplace. Resolving the issue of access is only one part of a complicated equation that is slowly reflecting the small business sector falling behind. A recent survey revealed that only 2 million small businesses out of 25 million, or less than 10 percent, have Web sites and far less than half of this small percentage actually participate in e-commerce. Conservative estimates of U.S. e-commerce reveal that it will account for as much as 8 percent of total retail sales by 2007, representing nearly \$200 billion. The electronic marketplace is a growing source of revenue and needs to be tapped into by small businesses.

Not only are small firms experiencing barriers to e-commerce, but small technology companies face similar hurdles. Small IT companies laid the groundwork for the Internet, and have transformed computer technology in doing so. In fact, the Internet's discovery phase was fueled by the innovation of small business IT start-up companies. But according to experts, the next build out phase will be done by large corporations that have the resources to manage a project of this scope. Small IT companies are then left questioning the role they will play in the future of Internet technology and the expansion of e-commerce.

Republican Leadership Big Business Giveaways

The response of the House leadership to the technology issues facing small businesses was to move the Internet Freedom and Broadband Deployment Act of 2001 (H.R. 1542), that provides substantial benefits for some of this nation's largest telecom conglomerates, while almost eliminating small telecom companies. In addition, this bill rolls back important competition provisions mandated by the Telecommunications Act of 1996.

The 1996 Telecommunications Act segregated the market into long distance and local voice and data services. It also prohibited the Bell companies from shifting to a long distance market before they had proven their local networks were open to competition. This legislation paved the way for many outstanding small businesses to step in and lead the charge for technology enhancements while decreasing the cost of long distance services in many states across the country.

This major rollback has been disguised as only a minor change, simply allowing the big telecom companies to access small technology firms' markets for "data" purposes only, even though small businesses, in turn, are unable to access the local networks of big companies. Since there is no differentiation between voice and data, the reality is that the move by the House Republican leadership will strip the 1996 Telecommunications Act of important safeguards, allowing companies to once again create monopolies that before resulted in the high cost of telecom

services and stifled telecom innovations. This will be especially devastating to the small technological firms that have played so critical a role in the recent IT explosion.

While giving advantages to these large telecom firms, the legislation fails to increase access or affordability for small businesses. It also imposes barriers fostered by a lack of competition, including the elimination of choice in phone service (fewer than 10 percent of phone customers have a choice in local services), the inability to bring down prices, and the lack of penalties for poor service.

Cost was cited as the most significant barrier in implementing new software by 65 percent of small businesses surveyed, and more than 20 percent consider the high cost of implementation as the biggest roadblock to installing new technologies in general. Unfortunately, under the legislation passed by the House, these costs will continue to climb for small businesses.

Administration Assistance to Big Telecom Companies

While the Republican leadership has worked to provide giant telecom companies with advantages, the Bush Administration is pursuing its own measure to help big business at the expense of small firms.

The Bush Administration has signaled that it will revisit the requirements of the 1996 Telecommunications Act and will propose new changes to negate key portions of it. First, the Administration intends to play a shell game with Internet service by reclassifying it so that it is no longer subject to the 1996 Act's agreement allowing big telecoms to immediately offer these services. Second, the FCC is planning to relax the current measurements that determine if these big telecom companies have met the Act's terms to allow them access to local networks without opening their networks. The result is that the Administration is attempting to accomplish through regulation what the House Republicans have been unable to do legislatively.

Conclusion

Much of our economic growth and prosperity depends on the increasingly important role played by the technology sector. This sector was revolutionized and dominated by small business. But the legislative actions of the 107th Congress and the Bush Administration will eliminate a significant portion of small telecom companies, while leaving other small businesses to falter in the technological dark ages.

Workforce Development

The skilled labor needs of small businesses continue to go unaddressed by Congress. It is estimated that between now and 2010, 17 million jobs will be added to the U.S. labor force. Of these, the majority will be in small firms. Small business owners currently represent 99.7 percent of all employers. In addition, they provide 67 percent of workers with their first job and initial on-the-job training.

Finding skilled workers has become increasingly difficult for all employers. According to the Bureau of Labor Statistics, occupations requiring a postsecondary vocational award, which accounted for 29 percent of all jobs in 2000, will account for 42 percent of total job growth from 2000 to 2010. While this trend will pose a challenge to all employers, it will be particularly burdensome for small business owners who do not have the time or the means to conduct personnel searches, or the resources to lure skilled workers away from larger companies that can provide employees with higher salaries and better benefits.

Shortage of Workers and High Cost of Wages

According to the National Association of Manufacturers, despite the slowing economy, 80 percent of manufacturers continue to experience a moderate to serious shortage of qualified job candidates. The service, technical, and contracting industries are currently experiencing similar problems. The auto industry estimates that dealers are presently unable to fill more than 60,000 automotive technician positions. The heating, ventilation, air conditioning, and refrigeration industry expects to be unable to fill 104,000 jobs by 2004. And, the National Roofing Contractors Association says it is facing an “acute shortage of skilled workers.” This problem will only worsen as aging workers begin to retire in the next few years with insufficient apprentices to replace them.

Another obstacle to small business owners attracting and keeping a skilled workforce is cost. It can cost tens of thousands of dollars to train just one employee. For example, the Machinists, Diemakers, and Mold Makers estimate that it costs approximately \$84,000 to provide one year of training to one employee. For a metalworker, whose training can last up to four years, the cost to the employer can be as high as \$200,000. These factors combine to make the obtaining and retaining of a skilled workforce almost impossible for small business owners. Without properly trained workers, small businesses cannot compete with their larger counterparts, both here and abroad. As a result, this country stands to lose its edge in the increasing competitive global economy.

Job Training

Recognizing this, Labor Secretary Elaine Chao in July expressed her view for a 21st Century workforce by highlighting the need to work with employers to identify the skill sets they need in their employees and to implement training programs to fill their needs. While these remarks were vastly reassuring to the thousands of small business owners who cannot find properly trained workers to staff their operations, the Department of Labor has proposed a \$500 million cut in funding for job training programs authorized by the Workforce Investment Act (WIA). In addition, vocational education programs – another major source of potential workers for small business owners – continue to go underfunded by the Republican Administration.

Welfare-to-Work

Former welfare recipients constitute another pool of potential workers. With proper training, these individuals could provide a great benefit, not only to their employers, but also to society. According to National Small Business United (NSBU) there is an untapped pool of welfare-to-work participants who are willing and able to work, but are ignored. NSBU also points out that the benefits of utilizing welfare-to-work candidates clearly outweigh the negatives. However, the Welfare-to-Work initiative expires at the end of this fiscal year and the Administration and Republican leadership are not inclined to renew it. In addition, House Republicans had an opportunity to facilitate the training of welfare recipients in the Welfare Reform Act (HR. 4737), however, this bill not only failed to improve and expand training opportunities, it reduced the amount of time an individual can receive job training from one year to four months.

Skilled Workforce Enhancement Act

Perhaps the best prospect small business owners have for obtaining and retaining skilled workers is the Skilled Workforce Enhancement Act, SWEA (H.R. 877). SWEA would provide small employers, defined as companies with 250 or fewer employees, with an incentive to assume the expensive task of training the next generation of skilled laborers by allowing them to take a tax credit of up to \$15,000 per year per apprentice. This, in turn, would ease the mounting pressure on critical industries, expand career opportunities for workers, and provide consumers with a reliable and well-trained workforce. Unfortunately, the Ways and Means Committee has failed to move this critical small business workforce legislation. In fact, they have refused to even hold a hearing on this simple bill that could benefit countless small businesses across the nation.

Conclusion

Finding and retaining a qualified workforce are constant issues faced by small businesses. Many large corporations are able to lure workers away with better benefits and higher salaries. And as long as the Administration and the Republican leadership continue to oppose important job training programs, such as WIA, Welfare-to-Work, and Vocational Education, along with important legislation, like the Skilled Workforce Enhancement Act, small businesses will continue to struggle in their search for a trained workforce.

The Wins That Weren't

During the 107th Congress, there were several legislative initiatives and other steps touted by the House Congressional leadership and the Bush Administration as “wins” for small business. But in reality, most of these wins have only a minor impact on small enterprise while others are actually big business wins. This section of the report will detail several small business legislative initiatives, from the signing into law of the Small Business Liability and Brownfields Revitalization Act, to the federal contracting black beret incident, to the repeal of the ergonomics law and detail how these did little to address the real needs of small business in America.

Brownfields Legislation Overlooks Redevelopment

Some of the best properties for commercial development in the country are so-called Brownfields – older industrial properties that require a minimum amount of clean-up before they can be put to productive use. As communities confront problems associated with urban sprawl and economic expansion, Brownfields can offer solutions by putting existing or fallow properties back to work for small businesses looking for good places to start up or grow into.

Unfortunately, the Administration's record on helping small business take advantage of these untapped resources is poor and contradictory. Although the Administration and House Republicans have claimed a win for small businesses with the passage of the Small Business Liability Relief and Brownfields Revitalization Act, there is great uncertainty regarding how many, and how much, small businesses will actually benefit.

Contrary to its title, one of the Act's most significant provisions applies not to Brownfields, but to Superfund sites, and not just to small businesses, but to any potentially responsible party, regardless of its size. Any company, whether it is the corner grocery or Exxon-Mobile, can escape liability under the De Micromis exemption if it can prove that it disposed of less than 110 gallons of hazardous liquid or fewer than 200 pounds of hazardous material. However, even under such conditions the President has the ability to overturn the exemption from liability if he determines that the liquid or materials, “have contributed significantly or could contribute significantly, either individually or in the aggregate, to the cost of the response action of natural resource restoration with respect to the facility.” So even if a business owner believes he or she may be exempt from liability, that may not be the case.

The provision designed specifically to help small businesses – those with 100 employees or less – provides relief from liability to small business owners who can demonstrate that their waste disposal was limited to municipal solid waste, or household garbage, such as food and paper – clearly items that would not be considered hazardous to being with. Even in cases in which a small business owner has disposed only of household garbage, he or she may be barred from receiving an exemption from liability for failing to “comply with any request for access or information or any administrative subpoena... or has impeded or is impeding, through action or inaction, the performance of a response action with respect to the facility.” Some small business owners have indicated they feel more confident of escaping liability under existing “innocent party” protections.

The bottom line is, this bill may or may not benefit small businesses that have disposed of a negligible amount of garbage at one of approximately 650 eligible Superfund sites across the country. Exactly how many small businesses fall into this category and will, as a result, benefit

from the De Micromis or the Municipal Solid Waste exemptions, no one seems to know. Even organizations, such as the National Federation of Independent Businesses, which listed the passage of this Act as one of its top three priorities, cannot estimate how many small firms will be helped by either of these measures.

Army Black Beret Contract Promised to American Business, Given to Foreign Competitor

One of the greatest barriers small businesses face is trying to penetrate the federal marketplace as domestic opportunities go to foreign competitors. Last year alone, 22,159 federal procurement actions worth over \$8 billion went to overseas contractors rather than American small businesses. Perhaps the most glaring example of this has been the Army's purchase of berets.

Several units of the U.S. military wear berets: green for the Special Forces, maroon for paratroopers (airborne units), light blue for United Nations Forces, dark blue for Air Force Security Police, and black for Army Rangers. The Rangers pride themselves on being part of a very select group – only one out of 200 Army recruits becomes a Ranger. For the Rangers, the black beret has been a symbol of their accomplishments, “earned, not issued.”

In October of 2000, the Army made the announcement that effective June 14, 2001 (the first anniversary of the Army in the new millennium), the black beret would be its official headgear. In this announcement, the Army also stated that the Rangers could choose another color for their berets. This decision was met with backlash from nearly every group involved, including the select groups that had historically worn it and veterans.

The Army's move to add this garment was hastily made and executed, and cost American taxpayers nearly \$30 million. The Army claimed that due to the initial design of the beret, only 25 percent of the production contracts could be awarded to U.S. companies. Instead of assisting in the development of additional sources for domestic production, possibly through helping small business to obtain the very expensive machinery required for the berets' manufacturing, the Department of Defense chose to award the remaining 75 percent of contracts to foreign manufacturers in Romania, South Africa, India, Canada, Sri Lanka, and China.

The award of the beret contracts to foreign companies violated specific statutes for military apparel. In fact, no Defense Department contracts may involve taxpayer money to purchase military apparel manufactured outside the United States from non-U.S. materials. Due to unfair competition abroad where companies take advantage of low wages, and lax environmental and labor laws, the U.S. apparel industry has fallen victim to a steady decline, bordering on crisis levels. Since the Army rushed to have the berets in place by June 14, 2001, it waived the requirements of this statute designed to protect the U.S. industrial base.

Once the contract came under scrutiny, the Army backtracked. The Chinese-made berets were the most expensive ones, and the contract was cancelled. The Army also cancelled the berets from India and Sri Lanka due to quality issues. Today, the Army has over 600,000 foreign-made berets in one warehouse that it has been unable to sell. Once these contracts were cancelled, the Army pledged to rectify the situation by awarding the next contract to small business.

Unfortunately, the Army did not live up to this promise. When they issued a new contract for additional berets, they did, in fact, restrict participation to only small, U.S. companies. The Army ultimately awarded two contracts – one to a U.S. company, and one to a Canadian company. While much attention has been placed on the American business that received a portion of the contract, what has been lost is that half of the contract was awarded to a foreign competitor who only operates a front operation in the U.S.

The Department of Defense (DoD) has one of the worst records of any federal agency in working with small business – DoD consistently fails to meet its small business, women-owned business and minority-owned business goals. A senior Bush Administration political appointee, DoD's Assistant Secretary of Defense, Pete Aldridge, testified before the Committee on Small Business this spring. During questioning, Secretary Aldridge said the agency has not been able to meet its goals because there are not enough “qualified” small businesses to perform the work required by the DoD. But when given the opportunity to use small businesses that could perform the work requested by the DoD, the Army violated federal statute and awarded the contract to foreign competitors, rather than do the right thing and employ America's small businesses.

Cash vs. Accrual Method Applies to Few

The Administration is slowly starting to realize that the accounting methods used by large corporations do not necessarily work for all small businesses. Under the current system, small businesses are forced to spend billions of dollars a year to comply with the costly, complicated and time-consuming accrual method of accounting required by the Internal Revenue Service (IRS). While the accrual method may accurately reflect the income of corporations, the most effective method of accounting for most small businesses is the cash method.

In recognition of this fact, the IRS issued new rules (IRS Notice 2001-76) providing that small business service providers with average gross receipts of \$10 million or less will be allowed to use the cash method of accounting. The problem is that the ruling only allows for small businesses in the service industry to use the cash method of accounting, while many small businesses still must comply with the cumbersome accrual method rules.

The cash method of accounting is the most practical method for many small businesses because it recognizes income and expenses when the cash is actually paid to the company or by the company. In contrast, the accrual method requires recognition of income before the cash is received – income is recognized to a business when the right to the money arises (i.e. bill is sent to customer) even though it may never ultimately be received. The accrual method does not prevent tax fraud and unfairly burdens small businesses that must either retain an accountant or tax lawyer, or hire a full-time employee who is skilled at using the accrual method.

A number of bipartisan bills were introduced in the House, including the Small Employer Tax Relief Act of 1999 (H.R. 2087), which included provisions to allow more small businesses to use the cash method. Instead of pushing these bills, the House leadership put the priorities of big business first and passed tax and stimulus bills focused on expanding tax havens, pension opportunities, and other benefits to large corporations.

Contractor Responsibility Ineffective, Helps Big Business

It is the primary responsibility of federal agencies, as stewards of taxpayer dollars, to make sure that the government's contracts are awarded to businesses with high ethical standards. This has been a guiding principle in federal procurement for decades.

While most federal contractors are honorable, live by the rules, and provide the taxpayer with products of superior quality, there are “bad actors,” or those who, among other things, fail to pay their employees appropriate wages, or engage in business practices destructive to the environment.

In an effort to ensure the federal government works with companies that are reputable, agencies are required to verify the “responsibility” of these businesses to perform federal contracts. Prior to the award of a contract, this check is done so that the government acquires the highest quality products possible. Criteria for this evaluation include checking that the proposed contractor has the financial resources to perform the work, satisfactory performance evaluations, and a record of ethical business practices.

Turning the ideal of paying taxpayer money to contractors with only the highest integrity into a reality has been more difficult than anticipated. In fact, the current system is subjective, with no clear directive. The criteria used to determine whether a prospective contractor is reputable are completely at the discretion of the agency’s contracting officer. This leads then to evaluation results that vary from contracting officer to contracting officer and from agency to agency. There is no consistency in the process of determining whether a contractor is responsible. For example, a business that has made a mistake and later corrected it is treated equal to a truly “bad actor.”

In 1999, the Office of Management and Budget (OMB) made an attempt to shed light on the responsibility evaluation criteria of “substantial record of business integrity and ethics.” Although the goal was to clarify this statement, the result only muddied the waters.

President Bush did repeal the regulation promulgated by OMB’s proposed change. While this was heralded as a small business win, the reality is that large businesses are affected to a much greater extent.

In fact since 1990, fines, penalties, restitution, and settlements for 43 of the government’s top contractors – all big businesses – have totaled nearly \$3.4 billion. These 43 contractors accounted for over 45 percent of all contracting dollars awarded in 1999. Sixteen of these 43 companies have been convicted of 28 criminal violations. Two of the top ten have at least two criminal convictions. But only one of these 43 businesses was actually debarred – the ultimate penalty for bad actors – for a total of just five days.

Despite regulations designed to safeguard the government from unethical contractors, there are clearly loopholes used by some of the biggest firms with poor track records of business integrity that allow them to continue working with our government. The repeal of the regulation to clarify the criteria through which responsibility of government contractors is evaluated does nothing to help small businesses. In effect, what the repeal does is give large businesses additional opportunities to take advantage of the procurement system.

Post 9/11 Disaster Assistance for Small Business in Loans, Not Grants

Small businesses negatively impacted by the events of 9/11 did receive assistance under the Department of Defense and Emergency Supplemental Appropriations Act of 2002, however, due to the way in which the aid program is structured, and how it is being administered, this assistance will not provide suffering small business owners with the resources to recover.

Rather than providing small business owners with the low-interest loans and grants they were seeking, the Administration and Republican leadership instead tried to meet the needs of the small business community on the cheap by including only \$75 million in the Defense Appropriations bill “for emergency expenses for the cost of loan subsidies... for disaster recovery activities and assistance related to the terrorist acts.”

These funds are administered through the newly created STAR Program, which is a temporary subsidiary of SBA’s 7(a) General Loan Program. While the details of the program sound very promising, the reality is that little, if any, of the funds will actually help those small business owners who need it most. The reason for this is quite simple. First and foremost, because the assistance is being channeled through the SBA’s General Loan Program, as opposed to the Disaster Loan Program, small business owners seeking assistance have to meet the same rigorous credit and business requirements that they would have to meet for a conventional loan. The STAR loan would also be subject to the same high interest rates associated with a conventional loan, providing no real savings to the recipient.

There is also a growing concern that lenders will be unwilling to participate in the program. SBA is gaining the unfortunate reputation of failing to live up to its commitment to cover its obligations, leaving lenders holding the bag on defaulted loans. As a result, more and more lenders are refusing to make 9/11-related loans as they are riskier and there is no assurance that SBA will honor its commitment to guarantee them should the borrower fail to repay.

While the Administration has held up the STAR program as a prime example of its efforts to provide struggling small business owners with assistance, it has targeted the funding for this very program as a means for making up a shortfall in fiscal year 2003 funding for SBA’s permanent loan programs.

More than a year has passed since the tragic events of September 11. However, thousands of small businesses that suffered significant physical and economic damage as a result of the terrorist attacks continue to go without relief. The Administration would like us to believe it has exhausted all means to help these small business owners when, in reality, the aid it has offered is scarce, hard to access, and in the process of being rescinded.

Ergonomics Repeal – A Big Win for Corporate America

One of the most important assets for any small business is its employees. Unlike corporate America, which has a vast pool of workers, small businesses, operating on a slim profit margin, must depend on key employees to provide a healthy and productive workforce to ensure survival in the marketplace.

Because of this, losses due to work-related injuries have a greater impact on small business. One of the reasons employees miss days at the office is due to work-related musculoskeletal disease (MSD). Annually, more than 600,000 employees lose time away from their job as a result of these injuries. Sometimes the severity of MSD puts people out of work for months, or leads to permanent disabilities. Ultimately, this creates a less productive workforce.

In fact, one out of every three dollars spent in this country on workers’ compensation goes towards MSD. The direct cost attributed to this disease is between \$15 billion and \$20 billion annually, and each year the total cost ranges upwards of \$60 billion. These costs fall especially hard on small business owners who, unlike their corporate counterparts that substitute one

employee for another, must utilize valuable resources, take on the work themselves, or simply allow the job to go undone. Because of this financial burden, reducing workplace injuries not only protects workers, but also makes good business sense.

In early January, Congress moved to repeal an ergonomics regulation issued under former President Clinton. While this has been heralded as a big win for small business, the reality is that corporate America, which stood much more to gain from the repeal, was the true winner. In fact, under the ergonomics rule, in some instances small business would have gotten preferential treatment over large corporations.

The examination of MSD and the development of an ergonomics rule began 10 years ago under the Bush Administration when it was initiated by then-Secretary of Labor, Elizabeth Dole. The culmination of this work occurred in November of 2000 with the issuance of Clinton's ergonomics rule. This immediately set off a firestorm of resistance, as big business fought efforts to provide workers with greater protections. They attacked the ergonomics rule in Congress and in the courts because they had the most to lose. Corporate America perpetuated many misconceptions about the rule – the worst being its labeling as a one-size-fits-all approach that would severely impact small businesses.

By using the process outlined by the Small Business Regulatory Fairness Act (SBREFA), OSHA sat down with small business owners to craft a regulation that took into account their unique needs. Moreover, the rule included a number of provisions designed specifically to address the concerns of small business. First and foremost, the ergonomics rule exempted businesses with 10 or fewer employees – or 65 percent of all small businesses – from recordkeeping requirements.

In addition, requirements for job hazard analysis and permanent controls on problem jobs were phased-in over two and four years. There was also the option for small firms to implement a “Quick Fix” rather than a full ergonomics program. The Quick Fix option would have allowed small business owners to correct a specific job or employee condition rather than make major changes throughout the workplace. Finally, the rule would have enabled small employers who already had ergonomics programs in place to continue them under a grandfather clause.

This approach was reliable and practical – not the one-size-fits-all that big business had claimed. It also allowed the regulation to be tailored to individual companies that reflect the industries' best practices. It only required action from employers in those industries to identify problems while other employers – in those industries that were not identified as a problem – were only required to act when someone was hurt.

Most importantly, this regulation was projected to save \$9.1 billion annually in workers' compensation, and this would have helped small businesses increase efficiency. MSD has a measurable impact on the careers of American workers. When small businesses are able to prevent these injuries, they improve overall productivity. The ergonomics rule would have provided a framework to hold big businesses accountable for the treatment of their employees. While making the reasonable exceptions to suit the unique needs of small businesses, Congress repealed the ergonomics rule because of a charge led by big business lobbies representing corporations that would have to invest billions to institute policies for worker protections.

President Bush's Executive Order Fails to Break New Ground

A main priority on the President's small business agenda was reducing the regulatory burden that weighs down small business. President Bush called on his Administration officials, namely the head of the Office of Management and Budget (OMB), to respond to the regulatory complaints lodged by small enterprise.

In keeping with his promise to reduce the federal regulatory burden on small business, the President issued Executive Order 13272, Proper Consideration of Small Entities in Agency Rulemaking, this past August. It basically calls for agencies to establish policies and procedures to promote compliance of the Regulatory Flexibility Act (RFA). It also calls on Advocacy to take three specific actions – notify agency heads about the requirements of RFA, provide training to agencies about the act, and provide comment on draft rules an agency proposes to OIRA at OMB. Finally, it outlines the responsibilities of federal agencies in complying with the RFA.

Given the President's demand that federal agency officials enforce the RFA, the Executive Order essentially fails to have any real or significant impact on federal rulemaking as it relates to small businesses. It is simply a restating of current law. The Executive Order requires federal agencies to prepare documentation about abiding by a statute with which they already comply. The procedures federal agencies adopt will be published, but are not necessarily binding. Federal agencies will also have to provide copies of significant rules to the Office of Advocacy, which they are currently required to do as directed by RFA. In addition, the agency – not Advocacy – determines if the rule is significant or not. In an agency's final rule, it will have to respond to Advocacy's comments, when current law – specifically the Administrative Procedures Act – requires federal agencies to respond to any relevant comments made in the final rule anyway.

Laws like the RFA and the Administrative Procedures Act already require agencies to take into account the impact their rules will have on small enterprise in America. The Executive Order simply highlights the need for agencies to take this action, but fails to make significant change to the current system or strengthen enforcement of statutes that would create a better rulemaking environment for small firms.

Federal Prison Industries (FPI) Still Competing with Small Business

Small business owners regularly face the challenge of unfair competition. Whether it is big corporations that receive preferential tax treatment or foreign competitors that fail to abide by the same rules, small enterprise in America finds it is often at an unfair disadvantage. What small businesses may not have expected is unfair competition from their own government. And this is exactly what is occurring when small firms are forced to compete with Federal Prison Industries (FPI).

FPI was created with the laudable goal of using work as a means of rehabilitation for inmates, giving them basic, yet valuable skills. Unfortunately, this honorable attempt to give these individuals a second chance has turned into an industry focused more on profit, rather than rehabilitation.

Today, due to advantages like direct borrowing from the Treasury, low cost labor, exemptions from the Labor Department's Occupational Safety and Health Administration (OSHA), subsidies from the Bureau of Prisons, and preferential treatment in federal contracting, FPI has built an empire that, in the last five years, has doubled the number of industries in which it participates.

If FPI was a private company, it would rank as the 45th largest federal contractor, being slightly larger than Halliburton. While the stranglehold FPI has on the federal contracting arena might be justified, FPI currently only benefits 17 percent of its prisoners. This is clearly a high price to pay for small businesses when inmates – the original focus of the program – are getting so little in return.

Bipartisan legislation, the Federal Prison Industries Competition in Contracting Act of 2001 (H.R. 1577), was introduced to correct this problem. It attempts to level the playing field for small businesses in their competition with FPI by phasing out its current preferential treatment. Rather than pursuing this common sense solution to an inequity facing thousands of small firms, Republican leaders instead passed a watered-down version of the bill that only applies to one agency – the Department of Defense – leaving half of the federal market operating within the old system.

In addition, the proposed changes still give FPI the ability to know the competitor's prices, quantity, and time of delivery, and then have the opportunity to beat it. Such a practice in the private sector would be equivalent to insider trading. Attempts to rectify the sham proposal during the 2003 Department of Defense reauthorization were blocked by the House leadership when they would not allow debate on any items related to this issue.

Small businesses are simply asking for fair competition with FPI. Small enterprises have shown time and time again that even given the financial, workforce, and subsidy benefits that FPI enjoys, they can still compete. Small business is simply requesting that FPI no longer receives the contractor preference currently in place. Unfortunately, even this minor request for fairness has gone unanswered by the Republican leadership.

Ineffective Tax Reform – Repeal of the Estate Tax

The House leadership and the Administration approached the estate tax problem with a focus on the wealthiest Americans. Throughout the estate tax debate, Speaker Hastert continually asked Congress, “Why should the government penalize our farmers and small businesses?” The President's final 2001 tax bill left many small businesses asking that same question.

Small businesses are particularly vulnerable to the effects of the estate tax because the assets are invested in the business, rather than in cash form. Thus, when the estate tax comes due, the children inheriting the business are forced to either liquidate the assets or sell the business to pay the taxes. The Administration and House leadership ignored bipartisan efforts, such as the Working Family Tax Relief Act of 2001 (S. 9) and the Small Business Tax Fairness Act of 2001 (H.R. 546), to address the estate tax issue in light of the needs of these family-owned small businesses. These proposals would have increased the exemption level for small businesses from the estate tax rather than creating a swift reduction for the wealthiest estates.

The House leadership was so intent on addressing the estate tax to benefit wealthy Americans that their inability to compromise created an unworkable piece of legislation. The Administration's failure to focus on the needs of small businesses created a final tax bill that slowly phases out the estate tax in 2010, only to have it reappear a year later. As such, small business owners should either plan on dying in 2010 or their children may be forced to sell the business to cover the costs of the estate tax. Under the rhetoric of protecting small businesses, the president's tax bill leaves many small firms in limbo while ensuring tax breaks for the wealthiest one percent of Americans.

The Bush Tax Cut and Stimulus Package – No Help for Small Business

President Bush's 2001 tax relief plan and 2002 stimulus package failed to address one of his most important constituents: small businesses. The Administration's 2001 tax cut (Economic Growth Tax Relief and Reconciliation Act of 2001, EGTRRA) had numerous tax reforms, but most of these changes were targeted to wealthy Americans and large corporations, including the reduction in tax rates. Similarly, the 2002 stimulus package failed to include effective tax code reforms for small businesses.

Rather than enact targeted tax reform for small firms, the president's 2001 tax bill cut the rates for individuals, with no provisions for small businesses. President Bush argued that the reduction in the top tax rate was essentially a tax break for small businesses. He said that "According to the Treasury Department, nationwide there are more than 17.4 million small business owners and entrepreneurs who stand to benefit from dropping the top rate from 39.6 to 33 percent." Yet IRS data for 1999 shows that only 864,306 taxpayers actually paid even a penny in taxes at the 39.6 percent top tax rate, thus disproving the president's statement. In fact, under President Bush's tax cut, 90 percent of taxpayers, including many small business owners, would receive less than \$1,600 in tax cuts.

In 2002, the House leadership and Administration again ignored proposals specifically focused on small businesses including the Small Business Expensing Improvement Act (H.R. 657) and the Small Employer Tax Relief Act (H.R. 1037), and instead pushed through the President's stimulus package, the Job Creation and Worker Assistance Act of 2002 (JCWAA). Despite President Bush's claims that the stimulus package was aimed at small businesses, it has been estimated that half of all small businesses in this nation – more than 13 million – saw no relief. Additionally, the bill failed to include a number of small business provisions promised by the President. These broken promises include increased expensing, full deductibility of health care premiums, and other targeted tax credits for small businesses.

No Voice for Small Business in Trade Promotion Authority

American small businesses are perhaps the most resourceful and innovative enterprises in the world. Small business could amply compete with foreign competitors, even though overseas operations have the advantages of lower wages and less stringent labor and environmental laws, if they only had a more visible role at the trade negotiating table, allowing their voice – and interests – to be heard and protected.

Trade Promotion Authority (TPA) is the trade negotiating practice that makes it easier for the President to make trade agreements. While TPA is supposed to help our workers, farmers, businesses, and economy by enhancing employment opportunities, opening markets to American goods and services, and increasing choices and lowering costs for consumers, the trade deals that are often struck benefit big business and corporate America. For the first time, this bill actually prevents our negotiators from including enforceable workers' rights or environmental protections in future trade agreements. In addition, this prohibition on enforceable measures only applies to the labor and environmental and provisions of the bill, not to commercial provisions, such as copyrights, that would affect big businesses. In fact, small businesses have been set up to be uniquely disadvantaged with the passage of TPA.

Another small business disadvantage linked to TPA stems from international competition. For the most part, small firms do not have the necessary resources to compete with large international corporations. TPA fails to establish regulations to protect small business from unfair competition with our trading partners. This leads to an excess of imports that harms small businesses in two fundamental ways – a drop in their products' prices results in a reduced profit margin, and a cutback in production that could essentially drive them out of business.

In order to solve this problem, TPA created the Trade Adjustment Assistance for Firms Program (TAA). The TAA is a technical assistance program designed to pay the cost of consultants or industry-specific experts for projects that can improve a firm's competitiveness. Aside from TAA, no other program exists to provide financial assistance for small businesses that were – or will be – dislocated due to international competition. The TAA requires that a small business obtain certification as a trade-injured firm before it can receive assistance. This requires a business to show it has been operational for two years, faces import competition, and has experienced financial difficulties due to this competition. Certification can take months, leaving small businesses without aid while they wait, and once certification is complete, the TAA will only pay 50 percent (or up to \$75,000) of the consultant's fees.

One of the main reasons TPA benefits big business over small is that the voice of Corporate America is heard when trade deals are made. Small businesses could stand to gain from official U.S. representation at the negotiating table, but none exists.

In an effort to address this issue, the Small Business Export Enhancement Act of 2001 (H.R. 1782) was introduced with broad bipartisan support. The bill would have established an Assistant U.S. Trade Representative (USTR) for Small Business within the Office of the United States Trade Representative. The Assistant USTR for Small Business would have served several important functions including promoting the trade interests of small enterprise, removing foreign trade barriers, and enforcing existing trade agreements.

The components of this bill were included in the initial version of the Trade Promotion Reauthorization bill, but the final legislation failed to include this critical provision. The lack of House Republican leadership on this issue has now denied small business a strong voice in trade deals and a seat at the table when billion-dollar trade agreements are made.

Ex-Im Bank Fails to Support Small Business

Typically, the focus of international business is on corporate giants that operate in countries around the world. Yet small businesses are beginning to make deeper inroads in the global marketplace. Over the past decade, the number of small businesses trading overseas has more than tripled. One recent survey reported that more than 200,000, or 97 percent, of all U.S. exporters were small businesses.

However, small firms continue to face obstacles when trying to penetrate overseas markets. The environment is competitive – foreign export credit agencies are increasingly aggressive in supporting their own exports. In the face of this tough competition, the U.S. government created the Export-Import (Ex-Im) Bank, the chief U.S. government agency tasked with financing American exports. The Ex-Im Bank supports American enterprise by providing loan guarantees and insurance to commercial banks so they can make trade credits available to exporters.

For more than 60 years, the Bank has supported over \$400 billion in U.S. exports, and has helped large companies expand their reach – and their profits. Aside from corporate aid, one of the Bank’s other Congressional mandates since its inception in 1945 is to expand the number of U.S. small businesses that utilize its programs. But it was just nine years ago – after facing much resistance from Ex-Im itself – that Congress required the Bank to allocate at least 10 percent of its resource dollars to small business assistance.

Unfortunately, Congress’ intent continues to be thwarted. Operating on a \$1 billion budget and making loan guarantees of close to \$15.5 billion, more than 80 percent of the Ex-Im funds are distributed to Fortune 500 companies, including Boeing, General Electric, ExxonMobil, AT&T, Motorola, General Motors and Raytheon. These multinationals are responsible for the most job-cutting in America, moving production overseas where they can find cheap labor. For example, Boeing has laid off more than 100,000 employees during the past decade, even after the company earned over \$18 billion and paid top executives over \$100 million in compensation and stock options. In addition, to receive Ex-Im assistance, only 51 percent of the content of the exports has to be made in the United States. This means that large corporations can actually use the Ex-Im subsidies to move their operations overseas.

While big businesses reap the benefits, small businesses receive little help from the Ex-Im Bank. According to the Cato Institute, the Bank supports less than one percent of all small and medium exporting firms in the United States. Even though small and medium-sized companies keep valuable production and jobs at home, they must compete with large corporations for the Ex-Im Bank’s attention, only later to receive a small piece of the funding pie.

Unfortunately, the latest Ex-Im Bank reauthorization bill (H.R. 2871) does little to help small businesses overcome these disadvantages. In order to address the discrepancies, an amendment was offered to H.R. 2871 to create an Office of Small Business Exporters within the Ex-Im Bank at no additional cost to the taxpayer. Even though the amendment was originally accepted, this critical small business provision was removed at the last minute by the Republican leadership.

In addition, the Administration recommended the final version of the bill cut the Ex-Im budget by 25 percent. Since small businesses receive only minimal assistance, this cut will primarily represent the loss of millions of dollars in lending and securities for small business expansion. This move by the Administration also means that large loans set aside for big corporations will be protected, while smaller, riskier loans will be eliminated first.

In an attempt to increase the level of lending to small businesses, a bipartisan amendment was adopted to increase their targeted loan volume to 25 percent. Instead of supporting the interests of small firms, the Republican leadership cut the volume from 25 to only 20 percent, which is the current inadequate lending levels of the Ex-Im to small business.

Small and medium-sized firms that sustain our economy are also those in the greatest need for trade finance, which is the valuable service provided by the Ex-Im Bank. Not only will the Ex-Im Bank reauthorization cuts negatively impact small business, but the small business loan volume was held at present levels to promote the status quo. When the Administration and House Republican leadership were presented with the opportunity to expand the Bank’s targeted lending to small firms, they chose to continue the corporate welfare strategy that has governed the Ex-Im Bank’s mission for decades.

Promises Made, Promises Broken

Our economy, coming out of the 1990s boom, is now facing an uphill battle to recovery as consumer confidence plummets and manufacturing has been in a steep decline. With unemployment hovering at around 6 percent, the U.S. economy still falters. Our weakened economic state is compounded by increasing health care costs and a credit system in which small business owners find it difficult to find the capital they need to grow and expand.

The economic indicators have become so troubling that among leading experts, there is talk of a double dip recession. It now appears that the positive effect of the Bush Administration's policies and the House Republican leaders economic plan never really materialized. This is due, in large part, not only to their lack of focus on small businesses – the powerhouse of the American economy – but also to their constant vigilance over big business.

This strategy is a faulty one as many of the current economic woes, like the stock market plunge, can be traced directly to the corporate scandals of the past year, which have driven investors away. In addition, the Bush Administration and the Republican Congressional leadership have no real accomplishments to show that aid small business. Their failure to ensure that the needs of small businesses are factored into the economic equation has cost our nation thousands of jobs while depriving the single most important driver in our economy from having the necessary resources to spur growth.

It is during times of recession that small businesses are especially important to our economic recovery. While corporate America sheds jobs and moves production overseas during difficult economic times, small businesses provide stability and innovation as they are an integral part of the economic renewal process. In fact, it is when our economy dips into recession that the number of small business start-ups spike.

Small businesses hauled this country out of the last Bush recession and they can do it again – with the proper tools. Unfortunately, as detailed in this report, the Bush Administration and the Congressional Republican leadership, in collaborating with Wall Street, has left Main Street small business without these tools. At every critical juncture in the economic decisionmaking process – whether it was opening up access to capital, expanding health care options, tax, regulatory or pension reform, or providing an economic stimulus package, the Bush Administration and the House Republican leadership chose to pursue a pro-big business agenda over one favoring this nation's small enterprise. This choice has kept small businesses from reaching their true potential and has prevented them from laying the foundation for the next economic recovery.