

TESTIMONY BEFORE THE UNITED STATES CONGRESS
ON BEHALF OF THE
NATIONAL FEDERATION OF INDEPENDENT BUSINESS

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Testimony of

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before the

**Committee on Small Business Subcommittee on Economic
Growth, Tax and Capital Access**

on the subject of

State of the Small Business Economy

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Good morning Chairman Brat, Ranking Member Evans and members of the Committee on Small Business Subcommittee on Economic Growth, Tax and Capital Access. Thank you for the opportunity to testify today on “State of the Small Business Economy”.

My name is Holly Wade, and I serve as the director of research and policy analysis for the NFIB Research Foundation. NFIB is the nation’s leading small business advocacy association, representing members in Washington, D.C. and all 50 state capitals. Founded in 1943 as a nonprofit, nonpartisan organization, NFIB’s mission is to promote and protect the right of its members to own, operate, and grow their businesses.

Small businesses are the bedrock of the U.S. economy with roughly 28 million small firms, of which, 5.8 million are small employers.¹ Small businesses account for about half of U.S. gross domestic output and about half of the private sector employment. Their contribution to the U.S. economy is vital to the creation a strong foundation for the middle class, offering job opportunities and contributing to their local communities. Small businesses provide goods and services in every market, in every geographic region, and throughout every demographic across the country.

General Small Business Conditions

Over the past 10 years, small-business owners have struggled to bounce back from the great recession. The economic recovery has been painfully slow for many, at first due to poor sales but quickly overtaken by issues related to taxes, regulations and the cost of health insurance.

NFIB’s Small Business Economic Trends survey found small-business owners stuck in a below-average rut, with the survey’s headline optimism index exceeding its 43-year average reading on a monthly basis only five times since July 2007, three of those recorded in the last three months.² Owners’ optimism failed to materialize as average GDP growth remained relatively flat at 2 percent over the last eight years and government policies continued to increase the cost of doing business. In response to the combination of policy constraints and anemic GDP growth, few small-business owners find economic conditions supportive of investing in or growing their business and new business formation has languished.

The poor business climate is further exacerbated by heightened levels of economic and government uncertainty. NFIB’s 2016 Small Business Problems and Priorities survey found that two of the top ten most severe problems affecting small-business owners are uncertainty related.³ Uncertainty about economic conditions and government actions are ranked fourth and sixth out of 75 business problems, respectively, and about one-quarter of small-business owners find each a “critical” problem in operating their businesses. The Small Business Economic Trends Uncertainty Index also reached record high levels leading up to the 2016 presidential elections, all creating significant barriers to economic growth in the small-business sector.⁴

¹ Small Business Administration, Office of Advocacy, Frequently Asked Questions. https://www.sba.gov/sites/default/files/advocacy/SB-FAQ-2016_WEB.pdf

² Dunkelberg, William C. and Holly Wade, *NFIB Small Business Economic Trends*, Series, NFIB Research Foundation.

³ Wade, Holly, *Small Business Problems and Priorities*, August 2016. NFIB Research Foundation.

⁴ Dunkelberg, William C. and Holly Wade, *NFIB Small Business Economic Trends*, Series, NFIB Research Foundation.

Post-election, small-business owner sentiment improved dramatically with more owners optimistic about the outlook for business conditions and business expansion. The rosier outlook has translated into more favorable expectations for sales growth and hiring to support expected gains in sales. As owners' confidence in the economy and economic policies rises, owners will be more likely to invest in and grow their business. Owners hold high expectations that Congress will now create a friendlier business climate for them to succeed.

Tax Costs and Complexity

The three main concerns of small-business owners for operating their businesses are: taxes, compliance and disruption costs of regulations and health insurance costs.

Small-business owners are inundated with a complex and costly tax structure that wastes their time and resources. According to NFIB's 2016 Small Business Problems and Priorities survey, five of the top ten most severe small business problems are tax related.⁵ The adverse impact of federal taxes on business income ranks third out of 75 issues and is a "critical" problem for nearly three in ten small-business owners, important because profits are the major source of capital for growing their firms.

Tax complexity also creates major consternation among small-business owners. About 27 percent find tax complexity a "critical" problem, the fifth most burdensome issue. Because of the tax code's complexity, most small-business owners must use a tax preparer to file their business-related taxes to ensure compliance, an unnecessary cost to provide tax revenue to the government that "simplification" could eliminate.

Tax-related costs compete with owners' ability to use limited profits for primary business activities. Profits are the main funding mechanism for owners purchasing new equipment, expanding facilities, hiring and stocking inventory. Tax-related cost pressures are especially problematic for newer firms that almost solely rely on profits for operation and expansion costs as they are generally not able to access traditional lending sources. But regardless of the firm's age, tax burdens take a heavy toll on owners' ability to operate their businesses.

Regulatory Obstacles

Regulation is another area of angst for many small-business owners. One-third of small-business owners find unreasonable government regulations a critical problem in operating their businesses. Regulation is the second-most severe problem for small-business owners after the cost of health insurance. NFIB's newly released survey on regulations finds that while small-business owners are affected by every level of government, the federal government is the largest contributor to the problem for half of small employers. Another 30 percent are most affected by state-level regulations and 17 percent, local regulations.⁶ Twenty-eight percent of small employers cite compliance costs as their biggest regulatory problem, followed by 18 percent most burdened by understanding how to comply with the regulation. Extra paperwork is the biggest regulatory problem for 17 percent of small employers. One of the many regulatory

⁵ Wade, Holly, *Small Business Problems and Priorities*, August 2016, NFIB Research Foundation.

⁶ Wade, Holly, *Regulations*, NFIB National Small Business Poll Series, February 2017, NFIB Research Foundation.

problems facing small employers is simply the volume of regulations they must comply with. The volume of regulations is the largest problem for 55 percent of small employers compared to 37 percent who are most troubled by a few specific regulations coming from one or two sources. The volume of regulations is important in that most small employers must take on the responsibility of learning about new government requirements themselves instead of delegating the task to an employee because their staff is too small.

Rising Cost of Health Insurance

Small-business owners rank the cost of health insurance as their most severe issue in operating their business out of 75 potential issues with 52 percent of small-business owners finding it a “critical” problem. The high cost of health insurance is the main reason owners do not offer employer-sponsored health insurance and the main reason owners discontinue providing the benefit. And for those offering health insurance, many owners annually confront the arduous task of adjusting profit expectations, insurance plans, cost-sharing and other mechanisms to help absorb often erratic changes in premium costs.

The rising cost of health insurance has forced many small employers to rethink the viability of offering health insurance to their employees. Since 2008, the offer rate for small businesses with less than 50 employees has dropped precipitously. Small-business owners are less likely to commit themselves to offering a long-term, high-cost benefit. The offer rate for this group has fallen 14 percentage points from 43 percent offering in 2008 to 29 percent in 2015.⁷

The small business health insurance tax credit was a targeted approach in the healthcare law to help curb health insurance costs for offering small employers and was intended to provide an incentive to start offering for those that do not. However, the tax credit was largely ineffective on both fronts as its design is exceedingly restrictive, complicated, and only offers limited and temporary relief to a larger small-business cost problem. The tax credit serves as a windfall for the few who qualify and take the time, or pay an accountant, to file for it.

Small Business Financing

Small business’s ability to access financing is a vital component of a healthy small-business sector. Small businesses rely on financing for general business operations but also expansion activities and reinvestment. But since the recession, loan demand remains historically weak, even with record low interest rates still available. Historically high numbers of firms remain on the “credit sidelines”, seeing no good reason to borrow over the past eight years. However, if the positive expectations for real sales and business conditions of the last three months are translated into actual spending on capital equipment, expansion and inventory investment, borrowing activity should pick up. NFIB does have concerns about small business access to financing as the economy picks up with fewer small and regional banks available to them. Small-business owners are often more successful accessing credit through smaller banks, and it is yet unclear whether bank consolidation will have a significant impact on small business lending.

⁷ U.S. Department of Health and Human Services, Agency for Healthcare Research and Quality, Medical Expenditure Panel Survey, series.

Conclusion

NFIB hears from small-business owners year round about the various challenges they face operating their business. The primary step in developing pro-growth policies is to first, “do no harm”, especially when it comes to artificially increasing the cost of doing business whether in the form of higher taxes, health insurance costs or more regulations, to name a few. Small-business owners are in great position to invest in and grow their business given the right set of policies. Most attention must be paid to the benefits of regulation that use up valuable human and financial capital.

I appreciate the opportunity to discuss the current state of the small-business economy and the challenges it faces going forward. I look forward to working with the Committee to support small businesses and strengthen the U.S. economy.