United States Senate Committee on Small Business and Entrepreneurship
Republican Consensus Recommendations to
The Joint Select Committee on Deficit Reduction
October 2011

Pursuant to the Budget Control Act of 2011 (BCA) (P.L. 112-25), which established a deadline of October 14, 2011 for Standing Committees of the Senate and House of Representatives to provide their recommendations to the Joint Select Committee on Deficit Reduction (JSCDR), this document encompasses the consensus recommendations of the Republican members of the U.S. Senate Committee on Small Business and Entrepreneurship (Small Business Committee) regarding deficit reduction legislation.

The Small Business Committee's jurisdiction includes all legislation and issues related to the Small Business Administration (SBA), and thus, this submission includes specific recommendations related to potential savings within the SBA's programs and operations that we believe are possible under discretionary spending caps, which would contribute to deficit reduction. Additionally, the Small Business Committee is charged with addressing all problems facing American small business enterprises, and as such, the Committee is appropriately including recommendations on the top issues presently facing small businesses, namely tax burdens, the rising cost of health care, and growth in burdensome regulations, all of which are contributing to pervasive uncertainty that is stifling job creation and investment.

We urge the JSCDR to consider our recommendations against the following backdrop: small businesses report losing an estimated $2 trillion in lost profits and asset valuation since the recession started in December 2007, with an average loss of $253,000 for each of the eight million U.S. businesses with sales between $100,000 and $10 million. Some $6.5 trillion in homeowners' equity has been lost in the housing crash, approximately $1 trillion of it just in the past year. The loss is particularly hard on middle-income households and small-business owners who use their homes as collateral for loans.

During the 12-months ending in March of this year, entrepreneurs have started up the fewest new U.S. businesses in more than a decade, according to government figures. Weak start-up growth has dire implications for jobs because small and mid-size businesses have driven employment gains in the U.S. for years. Between the recession that ended in late 2001 and the start of the most recent recession in late 2007, businesses that employed fewer than 500 workers added nearly 7 million employees. It is imperative that we create an economic environment that will enable small business to return on the path to prosperity, economic growth and job creation.

I. Small Business Tax Policy

While the Small Business Committee does not have jurisdiction over matters related to taxation, it is incumbent on us to advocate on behalf of the nearly 30 million small businesses that are impacted by the JSCDR's decisions. It is the strong view of the Republican Members of the Small Business Committee that, for the long-term health of our economy and job growth, we must achieve comprehensive tax reform as soon as possible. Nonetheless, we also feel that the JSCDR should not undertake efforts to propose a comprehensive tax reform plan, as the timeline established by the BCA to prepare its recommendations does not provide adequate allowance for a full vetting of the breadth and depth of issues necessary to achieve comprehensive tax reform. To illustrate our concern that comprehensive tax reform cannot be undertaken in a span of a few weeks, one need look no further than the 1986 tax reform that took two years to finalize and enact (from January 1984 State of the Union to October 22, 1986 enactment), through a grueling process in which the House Ways and Means Committee heard from more than 450 witnesses, and the Senate Finance Committee held 33 days of hearings. It is imperative that Congress and the tax-writing Committees, which have been holding a series of tax reform hearings, and the Obama Administration, undertake and complete comprehensive tax reform with due deliberation and dispatch.

We recommend that any tax reform must be genuinely comprehensive, encompassing not only corporate rates, but also the individual rates at which pass-through entities are taxed because 90 percent of American businesses are pass-through entities such as S corporations or sole proprietorships. These businesses must be free to choose the form of their business and not be forced into C corporation status, and thus be subject to an additional layer of taxation as some have proposed. We also must prevent increased taxes on small businesses, which already account for 50 percent of income above $250,000 and pay taxes at the highest rates. America's small businesses must share in the benefits of the simplified tax code that comprehensive tax reform should generate.

Guiding Principles

To be truly comprehensive, a tax reform plan must follow certain fundamental principles. These principles are:

- **Pro-Growth.** The tax code should be pro-growth, with the fewest number of economic distortions, and should raise sufficient revenue to finance our nation's spending priorities.
- **Simplicity.** Our tax code should be simplified to reduce the burden of compliance. It is unacceptable that, while small businesses generate over two-thirds of net new jobs, tax compliance for them costs 67 percent higher than for large corporations. The current tax code is so complex that taxpayers and businesses spent 7.6 billion hours and about $140 billion trying to comply with tax-filing requirements in 2008, according to the President's Economic Recovery Advisory Board August 2010 report.
- **Permanence.** The tax code must contain permanent provisions. We have to end the fiscal "shell game" where we extend tax cuts for only a year or two at a time or make them temporary to mask their true long-term costs. The list of expiring tax provisions has grown so large that the annual exercise of renewing them is also now a major revenue exercise.
- **Savings and Investment.** The tax code should promote savings and investment, the drivers of long-term growth.
- **Competitiveness.** The tax code must not be a barrier to American business competitiveness in the global economy. We have the second highest corporate tax burden in the industrialized world today. We have to help our businesses access capital and compete in export markets, while making America a more attractive place to invest.

- **Fairness.** Our tax code must distribute the tax burden fairly. If the JSCDR were able to generate a comprehensive tax reform plan in the limited time allotted to it, that comprehensive tax reform plan must follow these guidelines to receive favorable Congressional consideration.

The JSCDR should use this opportunity to do away with onerous provisions that will hurt small businesses such as the 3 percent withholding mandate. The Internal Revenue Service (IRS) has proposed changing the effective date of the 3 percent withholding mandate to January 1, 2013 for new and materially modified contracts, and to January 1, 2014 for all contracts (new and existing). The Administration has proposed an additional year's extension to January 1, 2014. While delay is helpful, small businesses that engage in contracting affected by this rule still must begin incurring costs to implement the necessary compliance systems, and the JSCDR should help prevent them from having to take on these unnecessary added costs by simply eliminating the mandate.

The JSCDR must also avoid certain areas of the tax code, such as new or added taxes on the Internet. The JSCDR must not propose a value-added tax. The JSCDR must not harm charitable giving and American home ownership by capping itemized deduction levels, which could affect the charitable tax deduction and home mortgage interest deduction. The JSCDR must not propose forcing pass-through entities into C corporation form and thus subjecting them to a second layer of taxation.

With an already-fragile economy growing at just 1 percent last quarter, and unemployment persistently above 9 percent, the JSCDR must avoid tax increases that would further stifle economic growth. Small businesses are already facing extremely difficult times financially and they cannot afford to pay more.

II. Small Business Health Care Policy

In the wake of passing the more than $1 trillion-spending Patient Protection and Affordable Care Act (PPACA) (P.L. 111-148), health care costs continue to rise unabated, with the average family plan premium increasing by 9 percent this year. Wages and salaries cannot keep up with these increases, and businesses can ill-afford to absorb these costs on behalf of employees. This situation makes it even more critical that efforts are made to rein in health spending, specifically as it pertains to small businesses, who lack economies of scale and the ability to negotiate with insurance companies in a meaningful way. The proposals herein would both lower health care (and health insurance) costs, as well as free up the private sector to innovate more efficient ways of paying for health care.

Our health care recommendations could considerably lower the deficit, improve the jobs outlook and the economy at large. While these proposals include aspects under the jurisdiction of other committees, Small Business Committee Republican members find it imperative that the JSCDR address the following concerns.

Specific Proposals

The Republican Members of the Small Business Committee strongly urge the JSCDR to adopt the following proposals:

1. **Scale back PPACA spending.** The United States could save well over a trillion dollars by scaling back PPACA. Over the next ten years, PPACA will increase spending by at least $678 billion on new programs and $674 billion on expansion to existing programs.

   Under the new law as passed, health spending beginning in 2014 is completely open-ended – meaning it could be much larger than CBO projections. CBO also projected that PPACA would reduce the labor market by half a percent by 2020, meaning 800,000 fewer people will be working, because of the health care law. This new spending in PPACA should be seriously curtailed in the current budget environment to alleviate additional pressure on the states, and improve labor markets and employment.

   Although an ideal situation would be to repeal PPACA, scaling it back is a reasonable proposal that the JSCDR should consider.

2. **Address waste, fraud, and abuse in public programs.** In order to truly address high health care costs, we must address fraud, waste, and abuse in Medicare and Medicaid. Experts have estimated that certain providers defraud Medicaid of as much as $30 billion a year, and Medicare is faring even worse. We should be able to recover some of this lost money and prevent improper payments without harming seniors, or pursuing more across-the-board cuts to health care providers who are already struggling to maintain quality services in the face of sweeping reductions in reimbursement as a result of PPACA.

   Steve Malanga of the Manhattan Institute described some of the fraud: "Unscrupulous doctors billing for over 24 hours per day of procedures, phony companies invoicing for phantom services, pharmacists filling prescriptions for dead patients, home health-care companies demanding payment for treating clients actually in the hospital…" Better technology and tracking systems could easily find and eradicate this kind of fraud. The JSCDR should take bold steps to eliminate such waste and fraud in public programs in order to shore up their finances and help ensure their solvency for future generations.

3. **Medical liability reform.** We must rein in frivolous lawsuits in the health care system. In 2009, CBO reported that Senator Hatch's proposed medical liability reform bill would save $54 billion over a ten year period, but two years later, nothing has been done to address medical liability reform. The savings would be larger in the new ten-year budget window, not to mention the savings not quantified by CBO – those that will be experienced by health care providers, patients, plan sponsors, and other actors within the system. Those who are unwilling to reduce spending on existing health care programs should, at a minimum, be willing to entertain ideas such as medical liability reform, which would increase the efficiency of spending without denying services to program beneficiaries.

It is critical to note that CBO only quantifies savings to the Federal government. Comprehensive medical tort reform would also save tens of billions for states, doctors, patients, and the medical system as a whole. While some Members have concerns over the 10th Amendment and states' rights issues as they might pertain to a national medical liability reform initiative, so long as we make the national policy a floor and allow any state to substitute their own more comprehensive plan, we will not be imposing upon states' rights.

III. Regulatory Reform

The Senate Small Business Committee Republicans request that the JSCDR include small business regulatory reform as part of its final legislative proposal to the U.S. Congress. For far too long America's small businesses have been forced to comply with onerous one-size-fits-all Federal regulations that disrupt their ability to prosper and create jobs.

The annual cost of Federal regulations in the United States stands at a staggering $1.75 trillion, with small business facing an annual regulatory cost of $10,585 per employee. This "hidden tax" severely diminishes small businesses' ability to invest, grow, hire, and compete.

Implementing small business regulatory reform as part of the debt reduction package will encourage economic growth and spur job creation thus reducing the federal deficit. The Senate Small Business Committee Republicans encourage the members of the JSCDR to seize this opportunity and include small business regulatory reform as part of the final deficit reduction proposal.

IV. Small Business Administration Programs and Budget

For the purposes of deficit reduction, and specifically the establishment of discretionary spending caps, the Republican Members of the Small Business Committee have identified programs and operations of the SBA that can be eliminated or substantially reduced without undermining the SBA's ability to serve small businesses. While the portion of the Federal budget dedicated to the SBA is extremely small – just 0.026 percent – we believe that it is incumbent on Congress to cut waste and inefficiency in all areas of the Federal government, including at the SBA.

<u>Specific Proposals</u>

In accordance with our responsibilities under the BCA, the Republican Members of the Small Business Committee believe that in order to limit discretionary spending, the following savings can be realized at the SBA: :

1. **Return the 504 and 7(a) loan programs to zero-subsidy status by giving the SBA authority to set fee rates sufficient to eliminate the necessity for subsidies.** In the past, the SBA's flagship capital access programs, the 504 and 7(a) loan programs, have operated without subsidy, because fees paid by borrowers were sufficient to cover SBA

expenses related to defaults. However, in recent years, hundreds of millions of dollars have been necessitated through appropriations because the fees the SBA is permitted to charge, under statute, do not bring in enough revenue to support the program. In their budget requests for both FY 2011[1] and FY 2012[2], the Administration expressed support for providing the SBA with the flexibility to adjust fees in the program to enable it to be self-sustaining over time. Thus, the SBA's 504 and 7(a) loan programs should revert to zero-subsidy status by giving the SBA authority to set fee rates sufficient to eliminate the need for subsidies, resulting in ***projected savings of $215 million per year***.

2. **Rescind Certain Intermediary Lending Pilot Program (ILPP) Funds.** The ILPP was created in the *Small Business Jobs Act of 2010* (H.R. 5297, P.L. 111-240) (*Jobs Act*). Under the program, if an entity is selected to become an ILPP lender, it can obtain up to a million dollar loan from the SBA. The ILPP lender has to repay the funds in 20 years, at an exceptionally low one percent interest rate. ILPP lenders make loans of up to $200,000 to small businesses. As the small businesses repay the debt, the ILPP lenders make additional loans. Therefore, the ILPP program is a revolving loan program. The *Jobs Act* allocated eight million for loans to ILPP lenders for FY 2011, an additional $8 million for FY 2012, and $6.5 million to administer the program. Accordingly, a full 28.9 percent of the appropriations for the ILPP are dedicated to administrative expenses. Moreover, the loans that are made to small businesses through the ILPP may be available through other options, such as conventional lending; traditional SBA lending; the United States Department of Agriculture Intermediary Relending Program; or through the *Jobs Act's* Treasury State Small Business Credit Initiative (SSBCI). The SSBCI provides $1.5 billion in grants to states for use in small business lending programs of their choice, including revolving loan programs. In an effort to reduce federal expenditures and duplication, without harming ILPP lenders who have already received awards through the program, we recommend rescinding unobligated balances of the appropriations that would otherwise go to future ILPP award recipients, and also rescinding $3,250,000 in administrative costs, resulting in total ***projected savings of $11 million in FY2012.***

3. **Require the Director of the Office of Management and Budget (OMB) and the Secretary of the Department of Treasury (Treasury) to make recommendations to Congress on assessing interest, penalties, administrative fees, and similar items, on delinquent debts.** As part of our nation's debt collection process, the Treasury and others assist various agencies in collecting delinquent debt owed to them, through various programs like the Treasury Offset Program (TOP) or Treasury's Cross-Servicing Program (CSP). Under TOP, Treasury collects debts through administrative offsets against a variety of federal payments. Each time an offset is made, Treasury charges an $18 fee for the service. Under the CSP program, Treasury utilizes a variety of collection methods. Examples include demand letters, repayment agreements, administrative wage garnishment, and reports to consumer credit bureaus. For this service, Treasury charges

[1] http://www.sba.gov/sites/default/files/Congressional_Budget_Justification.pdf, page 3.

[2] http://www.whitehouse.gov/sites/default/files/omb/budget/fy2012/assets/sba.pdf, page 1165.

an administrative fee of 28 percent of the debt collected. While agencies typically have the authority to add the $18 and 28 percent fees to the debtor's balance, not all agencies do so. For those that do not, the costs of Treasury's services are absorbed by the agencies, and hence paid by taxpayers, to the detriment of our national deficit. The Director of OMB and the Secretary of Treasury should be directed to: (a) examine agencies' practices in assessing interest, penalties, administrative fees, and similar items on delinquent debts; (b) report to Congress on the status and practices of those government entities which it performs collections for; and (c) make recommendations on whether agencies that are not adding these fees to the delinquent debt should be required to do so moving forward.

4. **Eliminate the Small Business Development Center (SBDC) Drug-Free Workplace Grants (also known as Paul D. Coverdell Drug-Free Workplace Program).** This program, which provides grants to intermediaries to offer financial and technical assistance to small businesses seeking to establish drug-free workplace programs, is duplicative of the Department of Labor's Working Partners for an Alcohol- and Drug-Free Workplace Program. Further, the SBA and its Inspector General have also recommended the elimination of this program. Therefore, the SBDC's Drug-Free Workplace Grants should be eliminated, resulting in ***projected savings of $1 million a year***.

5. **Eliminate the Defense Transitional Assistance (DETA) Grants.** These grants, which provide matching funds to Base Realignment and Closing (BRAC) communities for targeted small business technical assistance programs, are ineffective and no longer in demand. In fact, the SBA has been unable to use the allocated funding in recent years, given the lack of interest in the program. Rather than returning the excess funding to the Treasury, the SBA has distributed unused funds to the SBDCs. Further, the Department of Defense provides transition assistance to closed bases, which has been more appealing to economic development officials in affected communities. Therefore, DETA grants should be eliminated for ***projected savings of $2 million per year***.

6. **Eliminate the SBDC Veterans Grants.** This program, intended to help veteran entrepreneurs by providing targeted technical assistance, has no performance metrics, and is duplicative of existing programs already deployed in SBDCs nationwide. Additionally, at the time that this program was established, there were only eight regional veterans' business centers around the nation that received funds from the SBA to provide assistance to veterans; their number has almost doubled to a total of 15 in 2011. The SBA and its Inspector General have recommended elimination of this program, and the SBDC network has expressed its interest in its termination, as well. Therefore, the SBDC veterans grants should be eliminated for ***projected savings of $1 million per year***.

7. **Eliminate the SBDC Energy Grants/Small Business Sustainability Initiative.** This program, established to provide businesses with energy assistance, has no performance metrics. The SBA and its Inspector General have recommended elimination of this program, and the SBDC network has expressed its interested in its termination, as well.

Therefore, the SBDC Energy Grants/Small Business Sustainability Initiative program should be eliminated for ***projected savings of $1 million per year***.

8. **Replace the National Women's Business Council with a National Women's Business Bipartisan Task Force.** Under current law, the National Women's Business Council receives funding to employ an executive director and four additional employees, who may receive compensation up to the GS-15 level. As most other advisory committees across the government and the SBA (such as the Interagency Veteran's Task Force) operate without staff, the advisory mission under this program can be achieved without separate, authorized funding. Thus, the National Women's Business Council should be replaced with a National Women's Business Bipartisan Task Force for ***projected savings of $920,000 per year.***

9. **Terminate long-term, unauthorized pilot initiatives, such as the Regional Innovation Clusters Initiative and the Emerging Leaders (E-200) program.** These programs are duplicative of other programs at the SBA and Department of Commerce. Further, no performance metrics exist, and because the SBA funds these initiatives through contracts, rather than competitive grants, the SBA has the ability to unilaterally direct funds at the discretion of the SBA. These initiatives have been operating for three years with no request for authorization by the SBA. Therefore, long-term, unauthorized pilot initiatives should be eliminated for ***projected savings of $10 million per year***.

10. **Eliminate the Program for Investment in Microentrepreneurs (PRIME).** This program provides funding to organizations that help low-income entrepreneurs who lack sufficient training and education to establish small businesses. PRIME is duplicative of other SBA entrepreneurial development programs such as Microloan technical assistance, the Women's Business Center program and the SBDC program. The program has no performance metrics, and has also been recommended for elimination by the SBA and its Inspector General. Therefore, PRIME should be eliminated for ***projected savings of $8 million per year***.

11. **Eliminate the 7(j) Technical Assistance Program.** This program provides counseling and training to qualifying businesses through grants and cooperative agreements. The program is duplicative of the existing federal technical assistance programs, specifically Procurement Technical Assistance Centers, which provide small businesses with technical assistance specific to government contracting. Further, the program lacks performance metrics. Therefore, the 7(j) Technical Assistance Program should be eliminated for ***projected savings of $3.2 million per year.***

12. **Reduce the SBA's Operating Costs.** The SBA's operating costs have risen in nearly every area, and the growing expenditures within the bureaucracy account for 79 percent of the increase in the SBA's budget from FY 2008 to FY 2010. A 30 percent reduction *in the increase* in operating costs since FY 2008 would yield over $20 million, yet not have a significant impact on the SBA's ability to serve small businesses. Therefore, a 30 percent reduction in the increase in the SBA's operating costs since FY 2008 would yield ***projected savings of $23.6 million in FY2012 alone***.

13. **Eliminate the Office of Faith-Based and Community Partnerships.** This program. has no performance metrics and is duplicative of White House-led efforts. Therefore, the SBA's Office of Faith-Based and Community Partnerships should be eliminated for ***projected savings of $50,000 per year***.

14. **Eliminate the Office of Policy and Strategic Planning.** The functions of this office can be absorbed by specific program offices, and policy advisors in the Office of the Administrator, without a negative impact on the Agency's operations. Therefore, the SBA's Office of Policy and Strategic Planning should be eliminated for ***projected savings of $240,000 per year***.