

What Factors Go Into Firms' Hiring Their First Employee?

by Elle Patout, Public Affairs and Media Manager

In a new research report from the Office of Advocacy, *Crossing the Employer Threshold: Determinants of Firms Hiring Their First Employee*, Dr. Robert W. Fairlie analyzes the factors that lead new businesses without employees to hire their first employee. Hiring their first employee is a significant aspect of small business job creation.

"As our economy continues to recover, it is job creation that will bring employment back to pre-recession levels," Chief Counsel Winslow Sargeant said. "This report illustrates some areas where policymakers can focus to improve employment numbers in startup companies and small firms."

The report strives to answer three critical questions about employers. First, what owner characteristics are associated with a business's decision to hire its first employee in the first several years of operation? Second, what business conditions are associated with that decision (for instance, assets, sales, or intellectual property)? And finally, does entrepreneurship training increase the likelihood that a non-employer will hire its first employee?

The report shows that employers are more likely to hire their first employee in the first three years after startup. Incorporated firms with available assets and/or intellectual property are more

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Advocacy visited Amethyst Technologies in Baltimore, Md., in December. Pictured here are Chief Counsel Sargeant with Sherwin Sapasap, quality management chief, USAMRICD; Dr. Kimberly Brown, CEO of Amethyst Technologies; Tracy Pinson, director of U.S. Army small business programs; and Lt. Col. Kevin Pitzer, Ph.D., deputy commander of USAMRICD. Story on page 2.

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Regional Roundup

Chief Counsel Visits Small High-Growth, High-Tech Business

On December 11, Chief Counsel for Advocacy Winslow Sargeant visited Amethyst Technologies LLC, a high-growth small business focused on program development and comprehensive compliance services and products to the biotechnology, pharmaceutical, healthcare, food and beverage industries, as well as to the federal government. Also in attendance from the Office of Advocacy were Region III Advocate Ngozi Bell and Assistant Chief Counsel Linwood Rayford.

This small technology company is based in Baltimore, Maryland, and is a contractor to the U.S. Army's Medical Research Institute of Chemical Defense

(USAMRICD). Principal scientists and leaders from the institute also participated in Advocacy's visit. Their discussion touched on the challenges to obtaining capital, working overseas, and finding and retaining workforce talent, as well as the dynamics of Amethyst's partnership with the U.S. Army.

Along with its government work, Amethyst also does a fair amount of overseas business. Amethyst is a prime example of how America's small businesses can help with public sector development while expanding into international markets and the export sector.

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Advocacy Gathers Small Business Input at New York City Roundtable

by Dillon Taylor, Assistant Chief Counsel

On December 16, the Office of Advocacy hosted a small business roundtable in New York City. Regional Advocate Teri Coaxum and Assistant Chief Counsel Dillon Taylor listened as small

business owners and representatives provided feedback regarding the Securities and Exchange Commission (SEC) proposed rule on crowdfunding. The SEC issued the proposal on October 23, 2013;

it provides the framework for the practice of crowdfunding—a method of financing by which small businesses and startups sell stocks to a wide variety of investors online through funding portals and broker dealers. The SEC is seeking comments from the public on over 200 issues. The deadline to comment is February 3, 2014.

Given the amount of detail contained in the proposed rule, input from the small business community at meetings like the New York City roundtable is helpful to the Office of Advocacy. On January 15, Advocacy will host another small business roundtable in Washington, D.C., on the proposal.

To learn more, see Advocacy's regulatory alert at www.sba.gov/advocacy/815/755252 or contact Assistant Chief Counsel Dillon Taylor: dillon.taylor@sba.gov or (202) 401-9787.



Assistant Chief Counsel Dillon Taylor facilitates a discussion of small business concerns with the SEC's crowdfunding proposal at the New York City roundtable.

Message from the Chief Counsel

The Year of Innovation: The Ride to Entrepreneurial Advancement

by Dr. Winslow Sargeant, Chief Counsel for Advocacy

The Chinese called it the Year of the Snake; but when I reflect back on 2013, I will remember it as the Year of Innovation. For the past 12 months, I traveled all over the country meeting the vibrant entrepreneurial spirits of our great nation. From Washington to Iowa, Pennsylvania to Arizona, I searched for our nation's big ideas and learned about the best practices to bring back to policymakers in Washington, D.C. After every site visit, after every roundtable, our country's small business owners and innovators never ceased to amaze me.

During my travels, I had the opportunity to tour Virtual Reality Applications Center in Iowa and meet Ron Nilson from Ground Force Manufacturing in Idaho. These visits introduced me to the brightest minds in America and some of the world's most cutting-edge technology. In Iowa, I stepped into a three-dimensional virtual reality simulation of the human body that is allowing surgeons to develop groundbreaking approaches to old techniques. In Idaho, I saw the world's largest water trucks, the world's largest fuel and lube trucks, and the most diverse line of mine support equipment in the industry. These are only a few of the examples during 2013 where our team learned about big ideas and best practices that our policymakers can use to continue to keep our country a world leader.

This year of innovation impressed on me the invaluable effect of technological advancement and the spellbinding influence our nation's entrepreneurs have on the future face of this country. As our economy moves forward, these same minds, these same small busi-

ness owners are the people who will keep America on the crest of the innovation wave into the future. Our country will remain the world's visionary as these entrepreneurs develop new inventions and start thriving business ventures. But with all great innovation come necessary regulations.

In 2014, the Office of Advocacy will continue its mission. Our office will uphold its critical role as an independent voice for small business in the federal government and the source of small business statistics. Advocacy will remain on the forefront of small business development, so we can inform agencies and Congress about how best to help America's small businesses continue to drive a thriving U.S. economy. Our steadfast involvement in the regulatory process will not waver. Our attorneys will continue to act as the voice

throughout the process, pursuing the best avenue for rules to accomplish their goal without disproportionately burdening small business. We will start 2014 with a renewed focus on more in-house research that is both timely and actionable. And our outreach will continue. By visiting our nation's small business owners, we will put our best foot forward. Advocacy's direct approach will keep our nation's leaders informed with the tools necessary to keep small businesses at their finest.

In 2014, the Year of the Horse, I know Advocacy's expeditions to our nation's small businesses will lead to new creative minds that will take our office on a ride to find the best ways to create jobs and build a solid economic foundation for future generations. Advocacy is ready for the adventures 2014 will bring.



Chief Counsel Sargeant, Ground Force Manufacturing CEO Ron Nilson, and Region X Advocate Jennifer Clark at the company in Post Falls, Idaho, in May.

Advocacy Files Comments on Two Fish and Wildlife Service Proposals

by *Kia Dennis, Assistant Chief Counsel*

On December 2, the Office of Advocacy submitted a comment letter to the U.S. Fish and Wildlife Service (FWS) on the proposed rule listing the Gunnison sage-grouse as endangered and designating critical habitat for the species. Advocacy's comments note that the economic analysis is unclear with regard to the rule's effects on private landowners' abilities to continue to participate in grazing and mineral leases. The critical habitat designation will increase the costs of these agreements, preventing these small entities from readily entering into similar agreements in the future. The agency's economic analysis also fails to address the potential costs to small municipalities particularly as it regards transportation. The development of habitat conservation plans can be increasingly expensive, and the real burden is placed on small municipalities. Advocacy suggested that the agency submit a supplemental economic analysis that considers the potential impacts noted.

On December 12, Advocacy commented on a proposed FWS rule revising the designated critical habitat for the Canada lynx. Advocacy's comments reflected concerns that the agency has improperly certified the proposed rule. Advocacy has spoken with small businesses in the forestry industry who believe that the agency has not fully considered the rule's impact on them. They contend that the agency has underestimated the impact on the forestry industry because it used old data. They also contend that

its characterization of the industry does not reflect its weakened status in the wake of the economic downturn. Hence it has a reduced ability to cope with additional regulatory burdens. Advocacy recommended that the agency conduct an initial regulatory flexibility analysis to obtain current, reliable information on the proposal's potential economic effects.

Advocacy's contact on these issues is Assistant Chief Counsel Kia Dennis: kia.dennis@sba.gov or (202) 205-6936.

To Learn More

These are the titles of the two proposed Fish and Wildlife Service rules Advocacy commented on:

- Endangered and Threatened Wildlife and Plants; Proposed Endangered Status for Gunnison Sage-grouse and Proposed Critical Habitat for Gunnison Sage-grouse.
- Revised Designation of Critical Habitat for the Contiguous U.S. Distinct Population Segment of the Canada Lynx.

Both of Advocacy's comment letters can be found at: www.sba.gov/advocacy/816.

Advocacy Testimony: Small Business Needs Improved Guidance on Reverse Auctions

by *Erik Gulbrandsen, Communications and Congressional Liaison*

Every year, the federal government spends hundreds of billions of dollars on products and services across the country, making it the largest goods purchaser in the United States. Although this is a great opportunity for small businesses, it is often times an unrealized one. Small businesses create 60 percent of the net new jobs in this country and employ half of the private-sector workforce. So if America provided more federal contracts to small businesses, it would grow

the economy of the United States. The federal government is already working to encourage small business participation in the procurement sector.

For example, a new GSA program by the federal government will hopefully increase the availability of government contracts to small businesses. The reverse auction program puts a request of goods and services online and gives businesses the opportunity to bid on providing the goods and services.

Through the auction process, federal agencies award contracts to the lowest bidder while increasing the savings to the American taxpayer.

Although the intention of the program is good, the results have had mixed reviews. Many believe it works for the purchase of goods or simple services. However, when entering into more complex agreements and services, some believe the program is flawed.

Continued on page 5.

Regulatory News

Advocacy Comments on NIST's Preliminary Cybersecurity Infrastructure

by Major L. Clark, Assistant Chief Counsel

In February 2013, President Obama issued Executive Order 13636—Improving Critical Infrastructure Cybersecurity. The executive order outlined steps to reduce the risk of cyberattack on power, transportation, and telecom networks. On October 22, the U.S. Department of Commerce's National Institute of Standards and Technology (NIST) released its Preliminary Cybersecurity Framework. The framework is the first step in helping critical infrastructure owners and operators reduce the risk of cyberattack. It outlines a set of

steps that can be customized to various sectors and adapted by both large and small organizations while providing a consistent approach to cybersecurity.

On December 16, the Office of Advocacy submitted a comment letter to NIST on the preliminary cybersecurity framework. The letter cited small business stakeholders' concerns in four areas: cost, compliance, education, and enforcement. While several additional steps must be taken before a final framework is adopted, Advocacy believes that the education and best practice

processes should not be delayed. This is because of the seriousness of cybersecurity and because small businesses seem to be the frequent victims of cyberattacks.

To Learn More

The executive order is located at www.whitehouse.gov/the-press-office/2013/02/12/executive-order-improving-critical-infrastructure-cybersecurity. Additional information about the preliminary framework is available on NIST's website: www.nist.gov/cyberframework.

Advocacy's letter is located at www.sba.gov/advocacy/816/781561. Advocacy's contact on this issue is Assistant Chief Counsel Major Clark: major.clark@sba.gov or (202) 205-7150.

Reverse Auction Testimony *from page 4.*

In December, the Office of Advocacy's Assistant Chief Counsel Major Clark testified on the subject during a joint hearing of two subcommittees, the House Small Business Subcommittee on Contracting and Workforce and the Veterans' Affairs Committee's Subcommittee on Oversight and Investigations. In his testimony, Clark stated that the Office of Advocacy is not in opposition to reverse auctions in the federal marketplace; however, the office is committed to making sure that small business stakeholders have full opportunity to participate.

Moving forward, Advocacy believes we can continue to

encourage participation by small businesses in the federal procurement process. For this particular program, Advocacy believes it is necessary that the Office of Federal Procurement Policy give clear guidance for reverse auctions to small businesses. Once small businesses fully understand how reverse auctions will be carried out, they will not only be able to participate in them, but they will also be able to gain these lucrative contracts.

To Learn More

GSA's reverse auction program: <http://reverseauctions.gsa.gov>
Joint subcommittee hearing website: <http://smallbusiness.house.gov/calendar/eventsingle.aspx?EventID=362983>

Assistant Chief Counsel Clark's testimony: www.sba.gov/advocacy/2675/776581

Positive Small Business Indicators in 2013 and the Challenge Ahead

by Janemarie Mulvey, Ph.D., Chief Economist and Director of Economic Research

The Year in Review: Implications for Small Businesses

Two important economic indicators released late in 2013—employment and interest rates—give us some optimism about small business and economic growth trends. Both of these indicators are key to consumer spending, which drives two-thirds of our nation's economic activity.

At 7 percent, the unemployment rate in November 2013 was at its lowest level since 2008. Small businesses are responsible for 63 percent or 4.3 million of the 6.9 million jobs created since the recovery began. Interest rates rose slightly during the year but remain at historical lows. This has benefited the interest-sensitive construction and automobile industries, which had suffered sharp downturns following the Great Recession. In November 2013, building construction employment reversed its downturn and increased 3.3 percent over the prior year; 85 percent of these jobs are in small businesses. While automakers are typically large businesses, 74 percent of jobs in motor vehicle and parts are found in small businesses; these have benefited from 5.4 percent employment growth in this sector.

In addition to these promising trends, lower interest rates and dwindling inventories have led to double-digit increases in home prices in major metropolitan areas. The S&P/Case-Shiller Index of property prices in 20 cities climbed 13.6 percent from October 2012, the biggest 12-month gain since February 2006. Home equity is an important source of capital for small business, so improvement

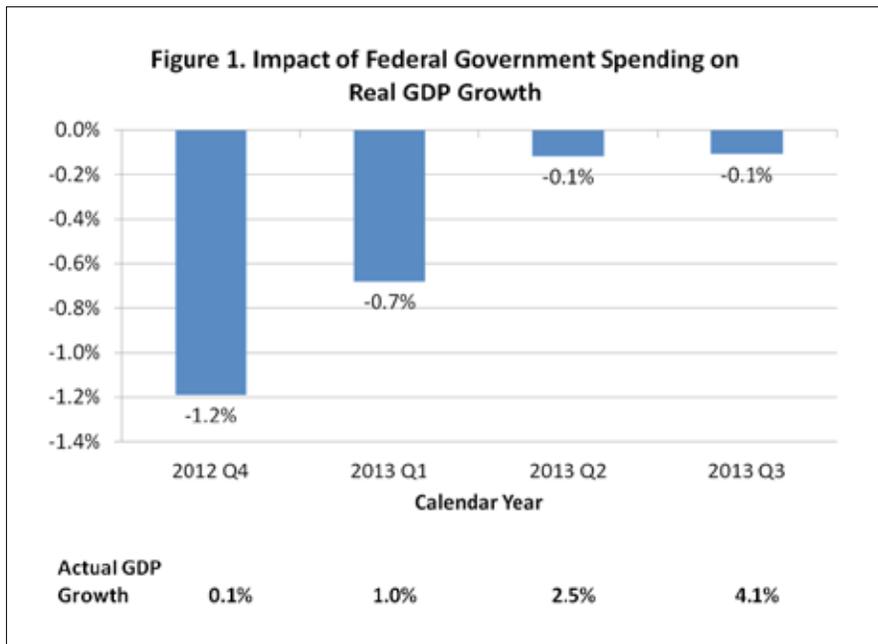
in home prices and home equity should boost access to capital.

Small business lending also improved in 2013. Bankers continued to ease their lending standards to small firms, demand for loans increased, and delinquency rates decreased. Small business loans (excluding those for commercial real estate) increased by 2.2 percent between September 2013 and a year earlier (the most recent data).

These many reasons for economic optimism were tempered by reductions in federal spending. Most economists agree this kept economic growth from its full potential. Reductions in federal spending in the fourth quarter of 2012 decreased real gross domestic product (GDP) by about 1.2 percent (Figure 1). As a result the economy grew only 0.1 percent during that quarter. While the impact of the sequester's automatic spending

cuts waned throughout the year, the Congressional Budget Office (CBO) estimates that the nation generated 5 million fewer jobs from its full potential in part due to the FY2013 sequester.

The scheduled FY2014 budget sequester would have caused additional dampening of economic activity this year had it not been for some relief due to the federal budget deal enacted in late December. Specifically, the budget agreement raises the discretionary spending cap for domestic and military programs by \$62 billion in FY2014 and FY2015. These higher caps are paid for through various fees and revenue provisions over the next 10 years, leading to a projected net \$23 billion of deficit reduction. The new budget also extends the sequester another two years past the original 2021 target end date.



Source: U.S. Department of Commerce, Bureau of Economic Analysis, Gross Domestic Product Third Quarter Estimate, December 20, 2013.

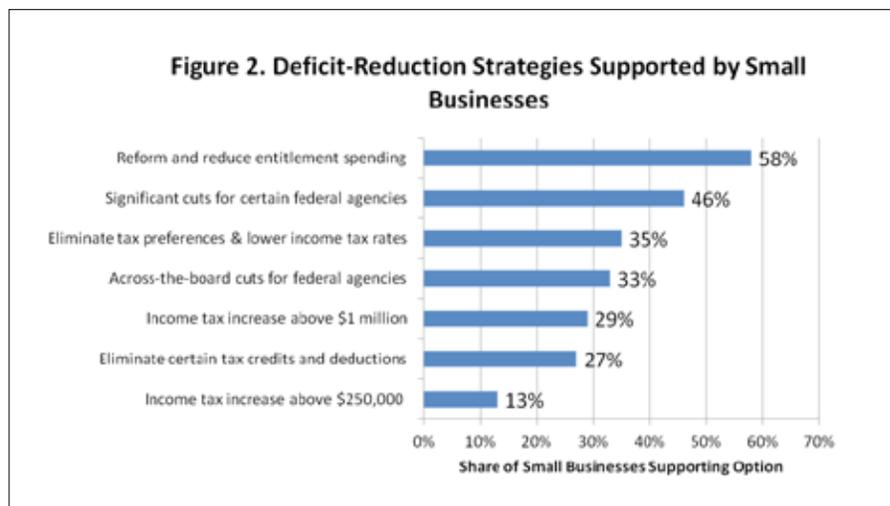
The Year Ahead: Fiscal and Monetary Policies Pose Challenges for Small Businesses

Looking forward into 2014, small businesses' success will depend on the strength of demand for their goods and services. In order to expand their operations and hire more workers, small businesses must feel certain that the economy will continue to grow. Thus, strong consumer confidence and less uncertainty about the future are important to future growth. From a federal policy perspective, there are three key areas of uncertainty in 2014:

- the deliberations surrounding raising the debt ceiling;
- reforming entitlements, taxes or both; and
- potential changes to monetary policy.

In February 2014, the debt limit for federal borrowing will expire and Congress must once again consider raising the nation's debt ceiling. While the approaching deadline may tempt some lawmakers to try to leverage significant changes to the budget, most agree that using the debt limit as a bargaining chip has significant unintended consequences. Allowing the federal government to go beyond that date and default on our nation's debt is not acceptable to financial markets or the public at large, and certainly would harm the economic environment for small businesses.

Beyond just raising the debt limit, some lawmakers may begin to seriously address later in 2014 the core component of rising federal debt—the growth of federal entitlements. At the same time, they could include reform of the federal tax system as part of the deliberations. Beyond the uncertainty associated with the timing of these decisions, the method chosen and the extent of reform to both entitlements and taxes could have



Source: National Small Business Association 2013 Mid-Year Economic Report.

important implications for small businesses.

The rising federal debt problem is real and growing. According to CBO, the debt-to-GDP ratio is projected to exceed 100 percent in the next 25 years, meaning that our nation's debt will exceed the value of our annual output. However, the last few years of budget cuts have focused on discretionary spending, which represents only one-third of our federal budget and is determined through the annual appropriations process. In fact, discretionary spending is at historical lows compared to GDP. The main source of the debt in the next two decades is what is called mandatory spending—outlays that are not subject to the annual budget process but are instead automatically obligated each year based on previously enacted laws that set eligibility and benefit levels for each program. A majority of small businesses identified reform of entitlement spending as their favored means of deficit reduction (Figure 2).

Most mandatory spending is for entitlement programs such as Social Security and Medicare. A combination of the aging of the population and rising health care costs is expected to accelerate the growth in these programs as well as the nation's federal debt over the

coming decades. According to the Congressional Budget Office, in order to bring the debt-to-GDP ratio back to historical levels, the federal government will have to reduce spending by \$4 trillion over the next decade (as compared to the \$1 trillion target under the current budget agreement). Achieving this goal would require significant increases in taxes, significant cuts in benefits or services, or both.

From a small business perspective, changes to the Social Security or Medicare payroll tax rates—or even changes to the taxable wage base to determine payroll tax liabilities—would adversely affect their profitability in the near term. In addition, since most physicians operate as small businesses, continued reductions in provider payment rates to offset Medicare's rising costs will also adversely affect their ability to grow and survive. Finally, if tax reform is discussed, the approach adopted must take into account the specific considerations of small businesses. Advocacy recently published research on the tax preferences most important to small business (*Measuring the Benefit of Federal Tax Expenditures Used by Small Business*, www.sba.gov/advocacy/7540/756313).

Continued on page 8.



In December, Chief Counsel for Advocacy Winslow Sargeant was a panelist at The Atlantic Small Business Forum, sponsored by The Atlantic magazine. Also participating were Nina Vaca from Pinnacle Technical Resources, Rob Cohn of TheAtlantic.com, and Rob Hilson from Bank of America. A video of the panel, “Small Business Savvy: Strategies for Growth and Success,” is online at <http://events.theatlantic.com/small-business-forum/2013>.

Small Business Research *from page 1.*

likely to hire their first employee. Moreover, wholesale trade, transportation, manufacturing, and professional industries are more likely to hire employees compared to other industry sectors. And finally, entrepreneurial training may lead firms to hire their first employee. With this valuable information, policymakers will be able to tailor legislation and focus on the best avenues for job creation.

The full report is available on the Office of Advocacy website at www.sba.gov/advocacy/7540/772191.

Economic Challenges in 2014

from page 7.

The third area of uncertainty is monetary policy. Many of the sectors doing well in 2013 were interest-sensitive industries like durable goods (e.g., automobiles) and housing. These sectors have benefited from the Federal Reserve’s large-scale purchase of government securities (a policy known

as “quantitative easing”) which has kept interest rates at historical lows. Since quantitative easing was always intended to be a short-term stimulus in the wake of the financial crisis, there is some degree of uncertainty about when the Federal Reserve will start “tapering” back on government security purchases and how long this process will take. Most important to small businesses is the question of how tapering

will affect interest rates and their ability to access capital in 2014. Statements by outgoing Federal Reserve Chairman Ben Bernanke indicated that 2014 would be a crucial year for tapering, and this will be a key issue for the newly confirmed Federal Reserve Chairman, Janet Yellen. Planning for these decisions will pose a critical challenge for small businesses in 2014.