A Review of State and Local Policies on Small Business in Region VI

by

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STATE AND LOCAL POLICIES ON SMALL BUSINESS IN REGION SIX

INTRODUCTION

Many public policies affecting business are restrictive in nature; they are designed to promote competition and consumer welfare by restricting the growth of very large firms. One major exception to this restrictive aspect of the government-business interface is the promotion of small business. Various federal, state, and local policies have as their purpose an improvement in the ability of small firms to grow into effective competitors for the larger firms. The major effort in this regard is made through the federal Small Business Administration. Yet state and local governments also have programs designed to enhance the growth and robustness of small scale enterprises in their jurisdictions.

There is, for example, little evidence of a "no growth" attitude on the part of state and local government officials in Region Six. On the contrary, all five states and the many cities in the region appear to be "pro-business," in the sense of actively encouraging new businesses to locate and existing businesses to grow in their respective jurisdictions. However, the states and local governments differ in their willingness to aid business development, more specifically small business development. In no case can it be said that any evidence of anti-small business attitude or behavior was found on the part of any government agency. Variability in the willingness of various government agencies below the federal level actively to promote small business is probably the result of the visibility of the Small Business Administration. Some
state and local administrators may simply believe that the federal effort is adequate.

The first part of this chapter will present a general discussion of the nature of business assistance by public and private agencies in Region Six. Since most local governments do nothing specifically to assist small business growth and development, much of this section of the paper is devoted to the effort of the private assistance agencies such as local Chambers of Commerce. Following this, a review of the small business policies of the five states in the region (Texas, Louisiana, Oklahoma, Arkansas, and New Mexico) will be presented. Because Texas is the most active promoter of small business, its programs and policies are treated at greater length. Information was gathered from each state in a uniform manner to assure neutrality; on this basis, the state of Texas ranked above the others in the region. The existing programs and policies reviewed in preceding sections will then be evaluated and critiqued. A final section will present a theoretical basis for alternative policies that state and local government policymakers can consider in assisting the formation and development of small enterprises in their jurisdictions.

I. Non-Federal Assistance

All states and every city of significant size, including many cities with populations in the 10,000 person range, provide general informational service to prospective businesses. Information packages are available which, in varying degrees, explain the advantages of placing a business in a particular location.

A state office, usually called an industrial commission, provides
general information about transportation, power, natural resources, labor force, labor training programs, tax advantages, construction, quality of life, and various market information. More specific assistance is provided upon request. Existing businesses can receive varying amounts of assistance from such state agencies. Such assistance is available to all interested parties, so that small businesses receive assistance as a matter of course. However, there are usually no specific programs designed to meet the special needs of small businesses, and it is logical to assume that potentially large plant operations will be given the most attention by state commissions.

City governments supply general information explaining the advantages of business location in their city. Industrial parks, typically the most concrete form of assistance given, are of use only to certain types of operations. As will be discussed below, more useful information about a particular city, and sometimes the only information about a city, is provided by the local Chamber of Commerce. Cities generally provide no special assistance for small businesses.

At the local level, excepting assistance from the Small Business Administration, the most useful services provided for small businesses are by businesses themselves, typically through the local Chamber of Commerce. Some of these programs will be considered here because although the Chambers are private organizations, they have a quasi-official status in most cities and frequently have good contacts with local officials. San Antonio and Dallas have two of the most active programs of assistance to small businesses of the major cities in Region Six.

The Small Business Council in the Chamber of Commerce in San Antonio was formed in January 1979 to give small businesses help in solving internal
and external problems. The Communications Task Force works to improve communication among small businesses and promote recognition of their needs. It surveys member needs and communicates these at the local and national level. The Governmental Affairs Task Force is designed to influence government policy on all levels, partly by keeping in contact with appointed and elected officials, and also by communicating support for particular issues to various levels of government.

The Special Programs and Services Task Force maintains a file of small business information, provides counseling, devises cost-saving programs, and organizes meetings and seminars. For example, in May 1979, it sponsored a seminar on Financing Opportunities for Small Businesses, with talks by a banker, an attorney, and a CPA. The Mobilization Task Force promotes membership and support, and motivates member participation in Small Business Council activities.

The Small Business Member/Services Committee of the Dallas Chamber of Commerce was organized in February 1978. It operates much like the Small Business Council in San Antonio. The Dallas Committee notes that "most small businesses face problems of a financial, operations, legislative and regulatory nature on a scale unknown to past entrepreneurs."

To help business cope with such problems, the Committee holds seminars and workshops. In the second half of 1978 these included sessions on time management, employment discrimination, retirement planning, and reducing business insurance costs. Information relevant to small business interests is collected by the Committee. The Legislative Affairs Subcommittee monitors proposed legislation at all levels of government that may affect small business. Small business support for, or opposition to, legislation is mobilized as needed.
Other cities have less active programs, although the Chamber of Commerce usually has some information available. In Shreveport, the Chamber publishes a Small Business Guide that provides some information about regulatory requirements and the availability of certain services. As in other cities, the Chamber sponsors the Service Corps of Retired Executives (SCORE). Affiliated with the Small Business Administration, SCORE is a volunteer program that provides free management assistance to small businessmen and to those contemplating going into business. Individual counseling is available as well as occasional workshops.

Evident from this survey is a general lack of active assistance by local government to small business development. Activities are limited to various information services provided by local jurisdictions to the market in general. Most of this may be classified as mere "boosterism": communities are interested in attracting business to the area as a source of tax revenues and jobs. While laudable goals, these are not specifically aimed at enhancing the prospects of small businesses which offer beneficial competition to their larger rivals. Some policies toward small business at the state government level do enhance these prospects.

II. State Policy Regarding Small Business

The states of Region Six differ widely in their promotion of the interests of small business. As will be discussed below in more detail, government policy toward small business may either actively promote the interests of small firms vis-à-vis their larger competitors, or may be merely neutral or nondiscriminatory. Two of the states in Region Six (Texas and Louisiana) combine the positive and neutral approaches, and Arkansas may be moving toward a similar combined approach. New Mexico
and Arkansas have been essentially neutral, while Oklahoma does little more than avoid being discriminatory against small business.

A. Texas

All states in Region Six have industril development commissions to promote business immigration; but usually these commissions do not explicitly direct state resources toward small business. This is not so in Texas where: "It is the policy of this state to ensure economic competition by assisting small business entities to the greatest possible extent." This policy is executed by the Small Business Act of 1975. By this Act, Texas has taken more concrete action to assist small business than any other state in the region.

Small business is defined, for the purpose of assistance, as any for-profit enterprise, independently owned and operated, having fewer than 100 employees, or less than $1 million annual gross receipts. In Texas, the legislature has directed that each state agency "award ten percent of all purchases of articles, supplies, commodities, materials, services, or contracts for services to small business." This is the fundamental manifestation of active small business promotion in the state. However, an Advisory Council on Small Business also exists; it is composed of nine members, at least six of whom are owners of small businesses. Members are appointed by the Governor with the consent of the Senate—three at a time—for staggered six year terms. The Advisory Council provides assistance, guidance, and expertise to the Industrial Commission, the State's all purpose business development agency. The Industrial Commission has primary responsibility for the administration of the provisions of the Small Business Act.
To help small businesses take advantage of the directive ordering at least ten percent of all state contracts to go to small businesses, the Industrial Commission provides advice and counsel to qualified enterprises, especially on how to bid on State supply requirements. The State Board of Control was also directed to help in this regard. The Commission also provides technical and managerial assistance to small businesses on sound management practices. To expand its ability in this regard, the Commission cooperates with public and private associations of all types to help make available better information concerning the management, financing, and operation of small business.

The Industrial Commission and Board of Control promote state supply requirements for small businesses by maintaining a master list of qualified small businesses, by helping to determine how small business productive capacity can be used most effectively, and by encouraging contractors to let subcontracts to small businesses. All state agencies are charged with assisting the Industrial Commission in this endeavor by including small businesses on master bid lists, informing small businesses of state procurement opportunities, waiving bond requirements when possible, and monitoring the effectiveness of the Act in improving the ability of small businesses to do business with the State. A report on such activities is provided annually by the Industrial Commission.

In fiscal year 1978, 29.5 percent or $439 million of State procurements were from small business. The State collects the information from each State agency and institution, breaking the information about small business contracts into different categories. In
open market, contract and delegated purchases through the Board of Control, 32.2 percent ($136 million) of the State procurements were from small business. Procurements in spot and emergency purchases from small business were 23.1 percent (Re8 million) of the total. The highest percentage in any category was in architectural and engineering contract awards, where 70.4 percent ($12.1 million) of the expenditures were with small business. Consultant contracts were similarly high, 53.2 percent ($9.6 million) for small business. The single largest category was construction contracts, where 28.2 percent ($242.4 million) went to small business. Since this information is reported by each state institution, annual comparisons can be made and goals for further procurements from small business set.

B. Louisiana

In 1977 Louisiana passed the Small Business Procurement Act. It is similar to the legislation passed in Texas in 1975. In the context of the Louisiana law, small business means a Louisiana for-profit business not dominant in its field of operation or an affiliate of a business in its field of operation. A business is deemed dominant in its field if it is a manufacturing enterprise with over 100 employees and has received over $15 million in gross receipts in the past three fiscal years. A nonmanufacturing business is dominant if it employs more than 25 persons and has had receipts of over $3 million in the preceding three fiscal years.

A business is also dominant in its field of operation, hence not a small business, if it is an affiliate or subsidiary of a dominant
business. It qualifies for this status if it is at least 20 percent owned by partners, officers, directors, majority shareholders, or their equivalent in a business dominant in that field. Any business is considered dominant if it exercises controlling or major influence in its field. Such determination can be made by number of employees, volume of business, financial resources, and other criteria indicating market power.

Small businesses that qualify are eligible to be a part of the group of businesses that will be awarded up to ten percent of the value of total state procurement of goods and services, excluding construction, each year. The commissioner of the Division of Administration divides State procurements into contract award units of such size that bids from small business will be competitive. Although all goods and services are to be divided so that small businesses are competitive, small businesses are not to be discouraged from bidding for contracts not broken into small units. Before giving contracts to small businesses, the commissioner is to make the determination that the business bidding can deliver as needed. If no small businesses receive contracts for some portion of the State's procurements, additional procurements of equal value in other areas will be set aside for small businesses. To date, this program is not as active as the one in Texas.

This legislation also established the Louisiana office of minority business enterprise within the Division of Administration. This office actively promotes the existence of the set aside procurement program for small businesses. It will help to locate small businesses able to fulfill contracts if not enough apply. Managerial
and financial assistance programs may be developed as needed in conjunction with other State agencies assisting small business development.

Ten percent of the value of procurements designated for set aside awards to small business are to be awarded to businesses owned and operated by socially or economically disadvantaged persons. These are persons previously deprived of the opportunity to develop and maintain a competitive business because of cultural, social, or economic circumstances or background or physical location. If ten percent of the small business procurements cannot be awarded to such businesses, they will be awarded to other small businesses.

C. Arkansas

Effective July 1, 1979, Arkansas established a Small Business Assistance Division within the Department of Economic Development. The primary role of this small office is to serve as a matchmaker, helping small business by referring inquiries to the best financial and managerial sources the Small Business Assistance Division knows of. The office is not large enough to provide much direct assistance, so it serves an information specialization function.

The office also promotes small business interests by writing position papers for the legislature, to provide it with guidance in legislation that would assist small business. The Division is suggesting a small business procurement act, like those in Texas and Louisiana. It is also recommending that the state treasurer place state money in banks that will earmark some of their loanable
funds for small business venture capital. To assist the availability of venture capital, the Division is urging that the state bond guarantee program, which has over $2 million in reserve, be used to direct more funds to small business.

D. New Mexico

The State of New Mexico has no specific programs to aid small business. The State purchasing agency does give a ten percent price preference for products produced by local firms owned by New Mexico residents. This does serve to aid some small businesses, giving New Mexico businesses an edge over out-of-state competitors. Like other states, New Mexico's Commerce and Industry Department gives assistance to all businesses. A considerable portion of the available regular programs do aid small business.

In 1975 the Development Credit Corporation Act was passed. It was designed, in part, to encourage new small industries and expansion of existing industries by establishing credit for certain applicants who may not otherwise qualify for private or government credit. One million dollars was appropriated for the fund, but it has never been used. Rather than loan the money directly, the State has tried to tie its money to private funds. Private sources have not been interested in the venture, so that nothing has been done to date. Apparently the program may be scrapped.

E. Oklahoma

The State of Oklahoma has no programs or legislation for small business assistance.
III. Evaluation and Suggestions

There are so many variables affecting the growth and creation of small businesses, it is probably impossible to assess the net effect of state and local laws and policies as they effect small business. However, a logical distinction can be drawn between laws or policies which serve to discriminate against small enterprises and those which serve to assist. Many laws are neutral in their effect on businesses of all sizes; others serve to help or harm businesses of certain sizes.

Policymakers must decide if the policy of a government is to be non-discriminatory in its relations with business, i.e., make laws as neutral in impact as possible, or if steps will be taken to aid certain businesses. In an economic sense, this means: will the government act so as to be neutral with respect to competition in the private sector or will the government act to assist small firms in competing in the private sector (assuming that actively discriminating against small firms is not acceptable)?

For a government to be neutral or favorable with respect to small businesses in the competitive environment, there needs to be a review of sources of discrimination against small businesses. Tax laws and other important laws which impact on small business have been reviewed in other parts of this study. An example of state laws that serves inadvertently to discriminate against small businesses are state securities regulations (blue sky laws).

Blue sky laws not only serve the same function as federal security laws, to provide certain information to the public about securities offered for sale, but they also serve as a barrier to entry for small enterprises. By use of the state merit regulations, state security commissioners have
life or death power; they can set the terms of proposed security offerings or to refuse to allow a security offering to be sold in the state at all. The costs of registration serve as a regressive tax on new business formation, because similar costs must be incurred by entrepreneurs whether the offering of new securities is for one million dollars or one hundred million dollars. Besides the proportionally higher cost incurred by small security offerors, state merit regulators generally impose higher standards on small offerings than they do on offerings from large firms, so that small firm offerings are frequently killed. State security commissioners will be more suspicious of an offering of securities in a local hardware store than in General Motors.

The effect of state securities laws has been to impede the entry of new firms into operation. Generally, securities offerings are not a realistic way for small businesses to obtain funds, due to the costly and restrictive nature of the state regulations. This places small firms at a competitive disadvantage in capital formation, requiring entrepreneurs to obtain debt (loans) rather than equity (stock), or to sell their idea to an existing large firm not faced with the capital constraints of the small firm.

If securities laws and other laws which serve to discriminate against small business can be eliminated or modified, then state laws could be said to be neutral with respect to small business. Lawmakers could then decide whether the free market produces neutrality in competitive ability with respect to size, or whether certain market failures exist that could be corrected to provide competitive equality.

For example, one problem small businesses may encounter in establishing themselves in a market is due to the common knowledge that most small
businesses have short lives. Assume that you wanted to have an underground sprinkler system placed in your yard. Assume that the standard guarantee for such systems is ten years. You have the choice of having the job done by a small local sprinkler company or a large national sprinkler company. Even if the small company offers a lower price, and even if you think the quality is the same, you may choose the large company to do the job, because you are more certain that it will be around for ten years to fulfill the warranty on the sprinkler. Common knowledge about their short lives may restrict small businesses to short term and service markets, reducing their ability to deal in long term contracts and many durable goods.

The state could play a role in allowing small businesses to compete effectively in the market for long term contract business by helping to assure the fulfillment of these risky contracts. For instance, it could help band together the small sprinkler system producers, so that their association could guarantee the fulfillment of the warranty, should the firm that did the work initially fail in business.

The states which have procurement acts may help to serve this function—they are helping to guarantee that small businesses can have long term contracts to fill orders for certain goods. This may increase the confidence that private buyers have in these firms. If small businesses have long term contracts to guarantee a certain level of business, the contracts themselves help to assure the survival of the firm, which in turn aids its ability to compete for other long term supply contracts.

The sprinkler system example illustrates how the state might act to help small businesses overcome natural market barriers in their competition with larger firms. Such policies would attempt to make firms
competitive by overcoming market barriers that serve to discriminate against certain types of firms. In such efforts the government would be attempting to be neutral, that is, allow all firms to compete effectively without subsidizing a class of businesses. Such active promotion of small business may seem positive rather than neutral, but it is not. Where the problems of small business are the result of private market failures, it takes active intervention to promote an even footing among large and small enterprises.

State laws could also serve to discriminate actively in favor of small businesses. State procurement acts which resulted in state purchases from small businesses at higher prices than from larger businesses would constitute a subsidy. Such a policy has the virtue of protecting a small enterprise only while it is small. When growth is achieved, the subsidy disappears for any particular firm.

While procurement programs in Texas and Louisiana do not appear to give any such subsidy, the price preference given in New Mexico to New Mexico firms is a subsidy. The Texas and Louisiana laws have easily met the quota set by the legislature for purchases, so the primary function they have served is to make buyers and sellers more aware of the desirability of increased competition from small businesses. Larger firms may have scale economies in dealing with large buyers like state governments. It would simplify the job of the buyer if a few sellers could supply most of the goods required. By the procurement act, all state agency buyers are forced to consider the range of sellers available, which has undoubtedly improved the competitive ability of small businesses. The information value of the law is one of its primary contributions. The law in New Mexico acts as a tax on New Mexico residents,
making them pay extra for goods produced in the state purchased for State use. The desirability of such a policy is obviously for the legislature to decide.

Differentiating between subsidies to small businesses and programs which serve to improve competition by removing barriers faced by small businesses is difficult. For instance, the Small Business Assistance Division in Arkansas helps provide managerial and financial information to small firms. Large firms do not need such information because they have specialists within the firm who know what is needed or know where to get the information. Small businesses, on the other hand, cannot afford to have such staff specialists and are at a disadvantage in their ability to obtain expert information and service. The state, by providing expert information and advice to small businesses, does not give small firms something unobtainable by large businesses but rather enables them to operate with the advantage of the best advice available. Insofar as the advice is free, there is a subsidy; but it is the knowledge of what to do that is really more important than the information itself, so that the law is neutral in this respect.

IV. Conclusion

It is easy to discern from the nature of this chapter that state and local governments do not have much in the way of policies regarding small business. States vary in how much they do regarding small business even more than do local units of government, which generally do nothing in particular for small business. This does not imply bias or callousness on the part of the governments. Many programs are designed to aid all businesses, so that no special effort for small business is believed necessary.
Generally it is most logical to assume that policies regarding small business would be at the state rather than the local level. Although local governments could adopt procurement programs similar to those used in two of the five states in Region Six, most programs would have to be designed at the state level. With the exception of large cities like Houston and Dallas, it is doubtful that local governments can afford to have special small business programs. In any event, from the perspective of the citizens of a state, it is most desirable that small business competition be enhanced statewide, not on a piecemeal local basis.

One very important factor ignored throughout this discussion has been the role of the federal government. Because of the Small Business Administration, it is clear that lower levels of government assume, and rightly so in some instances, that small business assistance is a part of the federal domain. There is little reason to duplicate federal efforts or to begin a state program if there is hope that the federal government will establish and pay for desired programs. Unless the relative positions and responsibilities of the governments are clarified, there is little reason to expect state or local governments to invest in more activities beneficial to small business than they already have.