This report contains findings and recommendations of a project to identify problems in California's policies and in the administration of its laws regarding small businesses and to examine alternative solutions to those problems. Part 1 consists of the findings of five statewide Task Forces that concentrated on these aspects of operating a small business in California: access to capital; taxation, regulation, and assistance; education, training, and technical assistance; commercial and industrial revitalization; and nontraditional small business. In part 2 is a set of recommended actions, selected and refined by an ad hoc State review panel from recommendations prepared by the Task Forces. Part 3 summarizes research findings about California small businesses. The research described here includes a study of small business's role in employment growth, California case studies, problems and prospects of nontraditional small business, literature summary and bibliography of urban small business development, and benefits and costs of extended supported work projects. Appendixes include complete lists of recommendations from each of the five Task Forces and listing of Task Force members. (YLB)
SMALL BUSINESS POLICY FOR CALIFORNIA

REPORT OF THE
URBAN SMALL BUSINESS EMPLOYMENT PROJECT

This Report was funded by the California Employment Development Department under the federal Comprehensive Employment and Training Act (Award #S000-2732).
I am pleased to share with you the attached report, Small Business Policy for California. This report, funded through the Governor's Special Grant under the federal Comprehensive Employment and Training Act, contains the findings and recommendations of the California Urban Small Business Employment Project. The recommendations were derived from five task forces, composed of representatives of small businesses, professional, public and governmental entities.

Report findings emphasize the key role small businesses play in technological and product innovation, creation of new jobs, and California's overall economic vitality. They further provide specific recommendations designed to foster growth of new and existing small businesses.

Some of the findings and recommendations could ultimately impact directly upon not only small businesses but also many agencies, departments, committees, boards, councils and interest groups in California.

It is our hope that this report will be informative to you and will serve as a catalyst for future cooperative efforts in examining the range of factors which affect the creation and expansion of small businesses in California. A principal interest of the Employment Development Department (EDD) in the report focuses on the job generation potential of small businesses. Hence, this Department is available to assist other entities in exploring the recommendations of this independent project, particularly as they relate to employment generation. Please forward any comments to EDD's Planning and Policy Development Office (916/322-2198).

DOUGLAS X. PATINO
Director
SMALL BUSINESS POLICY FOR CALIFORNIA
REPORT OF THE
URBAN SMALL BUSINESS EMPLOYMENT PROJECT
LLOYD C. LEE, PROJECT COORDINATOR

TABLE OF CONTENTS

EXECUTIVE SUMMARY ........................................ iii
INTRODUCTION ................................................. 1
PART I: TASK FORCE FINDINGS ................................... 3
  1. Access to Capital ........................................ 6
  2. Taxation, Regulation and Assistance ................. 25
  3. Education, Training and Technical Assistance ... 37
  4. Commercial and Industrial Revitalization ........ 48
  5. Non-Traditional Small Business .................. 60
PART II: PRINCIPAL RECOMMENDATIONS OF PROJECT .... 75
PART III: SUMMARIES OF SMALL BUSINESS RESEARCH ... 85
APPENDICES
Appendix 1: Complete List of Task Force Recommendations
A. Access to Capital ........................................ 102
B. Taxation, Regulation and Assistance ............... 104
C. Education, Training and Technical Assistance ... 107
D. Commercial and Industrial Revitalization ........ 111
E. Non-Traditional Small Business ................. 113
Appendix 2: Task Force Members ......................... 115
Appendix 3: Project Research Reports ................ Vol. 2
EXECUTIVE SUMMARY

Ninety-five percent of the businesses in California have fewer than 50 employees. They provide 45% of all of the private jobs in the State. The State's rate of employment depends significantly on the creation and expansion of small firms. Fifty-six percent of the State's net gain of employment between 1976 and 1979 came from firms with fewer than 20 employees.

There are significant adverse factors which diminish the ability of Californians to start new businesses and to expand existing ones. These adverse factors operate especially strongly in urban areas and can be characterized generally as follows:

- lack of concise objectives to guide State agencies and local governments in creating a "good climate" for small businesses formation and growth;
- failure to maximize the economic benefits of State business assistance;
- existence of government-sanctioned economic discrimination against small businesses.

Although the Project recommends several short-term improvements, fundamental improvement in small business capacity to stimulate job creation and generate revenue can be expected only through initiatives with relatively long time horizons. Research indicates that most net new employment is created by firms during the first two years of existence, and that only a small proportion of new firms (13%) are strong generators of employment.

These findings imply that State efforts to assist employment growth should be (a) to encourage formation of those businesses which are most likely to expand and (b) to provide resources which encourage expansion. In addition to modest direct expenditures for small business needs, such efforts should include tax and regulatory changes,
coordination of educational and business development initiatives, creation of investment intermediaries, and creation of a set of business development policy objectives for use by the agencies and governmental units, both State and local which currently affect small businesses.

Specifically, the project's recommendations include:

- authorizing indirect investments by pension funds in small business.
- changes in bank regulation and in training of bank loan officers.
- making the corporate net income tax progressive.
- authorizing small business net operating loss carry forwards.
- funding small business development centers at State University campuses.
- reforms in State procurement procedures.
- including entrepreneurship education into public instruction programs.
- using enterprise zone designations to target incentives to urban small businesses.
- requiring disclosure of small business lending information by financial institutions.
- facilitating incorporation and operation of cooperatives and employee-owned businesses.
- developing supported work small businesses to provide jobs for hard core unemployed persons.

State and local governments have a special interest in preserving small businesses which act as stabilizing elements in economically fragile neighborhood economies. The public costs of business failure or desertion in terms of community deterioration are very high. The State's special interest in expansion of small businesses is also clear. Such expansion is the most efficient source of employment generation and economic growth. Policy initiatives directed toward community preservation and job creation should have high priority.
INTRODUCTION

This Report contains the findings and recommendations of the California Urban Small Business Employment Project. The Project's recommendations are intended to provide practical ways to improve the financial, regulatory and physical environments in which California small businesses operate and, in particular, to encourage their ability to create new jobs. The Project was created in January 1980 under concurrent sponsorship of the Employment Development Department, the Governor's Office of Planning and Research and the Office of Economic and Business Development. The Project was composed of citizen members from the State's urban areas, representing different small business, professional, public and governmental interests.

During the 13 months of its activities, the Project examined, on behalf of small businesses, the State's role in financial markets, its educational and training policies, its approach to urban revitalization, its tax policy and its view of innovative business forms. The Project identified problems in the State's policies and in the administration of its laws and examined alternative solutions to those problems.

The Report is in three parts. Part I consists of the findings of five statewide Task Forces which concentrated on different aspects of operating a small business in California. Part II is a set of recommended actions, selected and refined by an ad hoc State review panel from recommendations prepared by the Task Forces. The reviewers included staff representatives from the Employment Development Department, the Office of Planning and Research, the Department of Economic and Business Development, the Department of Industrial Relations and both houses of the Legislature. Part III summarizes research findings about California small businesses. Significant research focused on creation of state policy towards small businesses is apparently unique, and the work commissioned by the Project resulted in novel conclusions. The complete reports of the research teams are in Appendix 3 to this Report.
Three major concerns provoked recurrent discussions by participants in the Project. First, effective programs to assist small business to innovate, to create employment and to stimulate growth must be conducted within an integrated policy framework. To do this, there must be concise and specific objectives which can guide different State agencies and local governments. There is no single initiative which is the key to encouraging small business success. Rather, the cumulative effect of many governmental decisions creates or destroys a "good business climate". Without policy guidance, such decisions can result in contradictory results.

Second, public resources intended to aid small businesses must be targeted effectively. When the State directly intervenes by providing small business assistance, it should focus on maximizing the economic payoff. While this appears self-evident, it is politically tempting to spread eligibility for help to include the widest possible range of recipients or activities, often at the expense of effectiveness. Additional research is needed in order to provide a rational basis for decisions to target public resources for job creation purposes.

Third, there are multiple instances of unintended governmental economic discrimination against small businesses which the State can and should correct. Instances of discrimination include the corporate net income tax, regulation of capital markets and banks, State procurement policy and employee training programs.

The authors of this Report echo the following observations of the United States Senate Select Committee on Small Business:

Each generation must rediscover and translate traditional institutions into terms that are meaningful. Unless we do a better job with the values of the smaller participants in our free private enterprise system, small business will not be continued, preserved, or encouraged in the future . . . . [T]he Small Business Committee is deeply concerned that we may lose these enterprises and their manifold economic and social benefits to the quality of American life in the years to come.

*Small Business and the Quality of American Life, Senate Select Committee on Small Business, Washington, 1977.*
PART I

TASK FORCE FINDINGS

OVERVIEW

Each of the Project's five Task Forces found that the economy of California is a remarkably robust and bewilderingly diverse one. It depends both upon very large corporations and upon hundreds of thousands of small businesses which, in the aggregate, employ almost half of the private workforce of the State. The California economy has benefited from the migration of people and enterprises, large and small, from the Northeast and Midwest and from the abundant natural resources of this State. Nonetheless, the Task Forces were unanimous in also finding that small businesses, and especially those located in some of the State's densely populated urban areas, face a series of problems which prevent them from reaching their full economic potential.

Existing small businesses in urban areas face undue difficulty in expanding and often in maintaining or perpetuating themselves. In many urban communities, it is increasingly difficult for anyone to seek or be able to start a small business. Moreover, while the overall number of small businesses continues to increase, the share of the market captured by small businesses shrinks. The Task Forces found that, although there were special difficulties involved in operating a business in an urban area, most of the needs of small businesses transcended their location. However, small businesses play a key, and often overlooked, role in all urban revitalization programs. As a result initiatives focused on small businesses are particularly important when formulating policy which is intended to bring employment and services to economically-disadvantaged urban populations.

The five Task Forces identified three generic issues which cut across the specific areas of interest of the Task Forces. These issues were:

1. Economic disincentives resulting from public policy which reduce the likelihood of small business creation or expansion.
2. Private sector market failures which reduce the access of small businesses to needed economic resources and information.

3. Discrimination against small businesses sanctioned by force of law, administrative decision or by concepts of public policy.

In order to create an economy in which the propensity to invest and to create productive enterprise is maximized, significant reforms or innovations are required in each of these areas. While some of the detailed findings of the Task Forces, set forth in the individual Task Force Discussion Summaries below, may be addressed by short term recommendations, the Task Forces were quite clear in their belief that the long run capability of small businesses to stimulate jobs and create revenue can only be improved by more fundamental and long range undertakings. Many such long range initiatives appear to result in unacceptable short term expenditures or revenue losses, which cannot be matched with precision against their expected long term benefits. Nonetheless, without such initiatives, even an economy as strong as that of the State of California will find its most creative and volatile sector, small businesses, to be increasingly unable to create the employment, income, goods and services required in the years ahead.

Defining "Small Business". In reaching their findings, the Task Forces used a somewhat flexible definition of "small business." It is clear that no single definition of small business is adequate for all policy formulation purposes. Business size can be measured by assets, employment, revenues, or wages and salaries. Each of these indicators provides a different measure and has different uses. What constitutes a business as small, using any given indicator tends to vary widely, depending on the uses to which the definition is put. Traditionally, different industries have defined relative size differently. The issue is further complicated by the existence of hybrid forms of business, like franchises, which display characteristics of both small and very large businesses.

The basic guideline adopted by each Task Force was to class all firms employing 50 or fewer persons as small businesses. Of all firms in California, 94.5% have fewer than 50 employees. The Task Forces were free to elaborate on this definition. The Capital Access Task Force indicated that it believed that somewhat larger businesses, including those with significant growth potential should also
be considered "small" because of their inability to gain access to public capital markets. The Taxation, Regulation and Assistance Task Force suggested annual revenue limits of $1 million for non-manufacturers, $2 million for manufacturers and $3 million for construction firms as a definition of "small."
Inability to obtain appropriate investment and operating capital is one of the obstacles to small business creation and growth most persistently cited by owners of small businesses. Paradoxically, however, there seems to be no crisis apparent with regard to small business financing, except in times of peak interest rates. Small businesses continue to open their doors; most existing businesses continue in operation; and California banks point with pride to the number of loans made to small businesses. Why then do small business owners complain about insufficient access to capital?

The answer to that question involves analysis of the uses and sources of small business financing.

A. CAPITAL USES AND SOURCES

Small business uses for capital can be broadly classified into the following categories:

1. Pre-start up and start-up expenses, including research and development, product and prototype development, market research, and organizational expenses;

2. Working capital, including inventory, work in process and receivables financing;

3. Equipment financing; and

4. Real estate financing.

The relative proportions of funds used for these categories vary from business to business as a result of differing products, age of the business, size, and other
factors. For example, young, growing small businesses have needs for capital which are disproportionately large, but it is just such businesses which are able to provide the major increases in employment.

Businesses satisfy their capital requirements from the following sources:

1. Equity financing, including funds from entrepreneurs' personal savings, external investors, and retained earnings;
2. Non-equity venture capital, including convertible debt, debt with warrants or "carve-out" debt;
3. Normal debt, which can be subordinated, unsecured, or secured; and be short-term, medium-term, long-term, continuous or revolving;
4. Leases, both of real property and of equipment; or
5. Miscellaneous, including factoring and franchising.

The Task Force examined the sources of capital in detail and concluded that capital scarcity in certain key situations discouraged creation of small businesses, retarded the growth of others and made still others unnecessarily vulnerable to adverse changes in the economy.

B. CAPITAL GAPS

As it sought answers to the question posed above, the Capital Access Task Force identified several key gaps in the availability of capital for smaller enterprises. These gaps include:

1. Start-up and "second round" capital, both equity and non-equity, especially for technology-based businesses;
2. Medium-term (2 to 5 year maturities) loans or lines of credit for existing firms;
3. Long-term secured loans for land, plant expansion and equipment; and
4. Long-term mixed equity and debt packages.
There are fewer problems with regard to other types of capital. Obtaining short term bank loans for working capital is not overly difficult for most existing small businesses; likewise, many small businesses are able to get short term credit arranged through equipment manufacturers or suppliers. However, another potential gap, capital for business creation by low income persons, poses special problems of accumulating initial equity, and should be considered to be a separate issue which requires a comprehensive, programmatic response.

Start-up and Second Round Financing. The first of the gaps identified by the Task Force results from changes in the business environment which have altered both the extent of small business capital needs and the availability of key components of the mix of financing. The cost of entering industries with high growth potential has increased drastically. Once, several individuals with technical expertise could begin a viable semiconductor business with less than $250,000. Recent industry estimates indicate that, because of needs for increasingly sophisticated equipment, a similar business today would require $2 to 3 million for start up. Initial capital needs of this size puts a start up beyond the limits of the savings of most individuals and mandates outside investors. Likewise, there has been a qualitative change in the ability of high growth businesses to obtain capital to sustain growth rates of 40% to 100% per year, which are typical and necessary for a technology-based firm. Despite highly publicized recent public financing of genetic engineering firms, second round financing for high growth firms is rare. When even glamorous, technology-based businesses have difficulty obtaining appropriate capital, less spectacular, but growing and solid firms find the task almost impossible.

One of the most widely described and decried developments of the last 15 years in the capital market has been the gradual extinction of public equity financing for small and medium-sized businesses. This trend has been accompanied by the demise of the majority of small, regional brokerage houses, which provided the entree into the public equity markets and functioned as market-makers for the securities of small firms. Concomitantly, the expense of selling securities publicly has skyrocketed. The disappearance of the public equity market for smaller businesses has two related, pernicious effects. First, those businesses are forced to rely ever more exclusively on retained earnings and debt capital for expansion purposes. Secondly, because prospective investors realize that their opportunities to resell securities of a smaller
business at a profit in the public market are relatively slim, they are less likely to purchase the securities in the first place. Both Federal and State securities regulation have contributed to the difficulty and complexity of raising private equity capital. The Task Force found that the State can undo regulatory roadblocks without jeopardizing the public.

Medium-Term Debt Financing. Obtaining medium-term loans is a problem for most small businesses, even allowing for the SBA's loan guarantee program. Federal and state banking regulation and the highly concentrated banking market in California have combined to cause significant aversion to loan loss risks by the State's banks. This risk aversion particularly affects small businesses, even when they are willing to pay higher interest rates to compensate for higher risks. In addition to unjustified institutionalized risk aversion, bank lending officers in branch banks often lack expertise and motivation to make significant numbers of small business loans.

Long-Term Secured Loans. Long-term financing for business improvements is readily available to large companies from insurance companies or the public debt market. However, small businesses are usually unable to tap these sources. The loans which small businesses seek are often too small, or too long-term, or beyond the area of lending expertise of potential lending institutions. Again, SBA-sponsored institutions have made only a small dent in this neglected market. While SBA Section 502 Local Development Companies and California Business and Industrial Development Companies ("BIDCOs") are promising initiatives directed at this problem, the capital and the guaranteed authority available to them are severely limited. If the bonds to be issued under the newly created California Industrial Development Financing Act can be primarily used to finance businesses at the smaller end of the allowable size spectrum, the Act could be a major contribution to easing the gap in long-term finance.

Business Purchase Financing. As a result of the final gap identified by the Task Force, small businesses are too often wound up, even though successful, because appropriate long-term financing for replacement of a partner or for prospective new owners cannot be arranged. Mixed equity/debt financing for these and other business continuation or expansion purposes should be more freely available.

Data on Capital Access. Financial data clearly indicate a massive shift in the ability of small businesses to gain access both to equity capital and, possibly more importantly, to middle-term and long-term
Comparing the years 1972 through 1976 with the earlier period of 1958 through 1971, indicates that manufacturing corporations with less than $1 million increased their dependence on internally-generated funds from about 30% of annual financing to nearly 50%. Similarly, the same small businesses doubled their use of bank loans in excess of one year of maturity, while their use of other long-term liabilities, principally bonds and leasing agreements, decreased from 17% to about 2%. This shift indicates a drastic decrease in the average maturity of financing, because bank loans typically have a much shorter period of maturity than the other sources of financing.* The credit needs of non-manufacturing small businesses are at least as severe as those of manufacturing businesses, which are able to accumulate greater stocks of assets suitable for collateral.

In order to analyze appropriately the needs of small businesses for different types of credit, it is important to differentiate among small businesses by size. Nationwide surveys taken between 1973 and 1976 indicate that the smallest and the largest small businesses view unavailability of credit as a significantly more important barrier than do middle-sized small businesses.** The smallest are businesses with less than $50,000 in annual sales and the largest are those with annual sales of more than $350,000. A possible explanation for this fact is suggested by Osborne and Bradford, in a report prepared for the California Assembly Office of Research in 1977.*** They concluded that larger businesses need credit to expand, while the smallest businesses need credit to survive. Middle-sized small enterprises tend to stay within a limited size range.

The Task Force emphatically believes that many existing small businesses are unnecessarily under-capitalized because of unavailability of middle-term and long-term debt. The resultant reliance upon internally-generated funds for expansion hinders their growth and their capacity for employment generation.

The Role of Policy in Addressing Capital Gaps.

The Task Force recognizes that there are a number of overall economic conditions which impact upon small businesses which the State of California can do little to remedy directly. High interest rates, low savings rates, a depressed equity market for most small issues, inflation, and government-induced changes in the capital market have contributed to small businesses' financing problems. At the other end of the spectrum, patterns of implicit private and public credit allocation have resulted in uneven opportunity for small businesses to locate and expand on a neighborhood-by-neighborhood basis. Businesses in suburban areas have a better chance to obtain business capital than those in some urban areas. This sort of "allocation" results in part because of the increasing reliance of small businesses on funds from family, friends and associates. Dependence on this source makes entrepreneurial success much more dependent on the economic class of the entrepreneur than his or her merit. Another cause of implicit "allocation" is the tendency of whatever institutionally-derived risk capital does exist to flow primarily to small businesses in high technology industries, which tend to be located in relatively affluent semi-suburban areas. The Task Force concluded that the State should and could do more to make capital resources more available to small businesses in a more equitable fashion.

The Capital Access Task Force devoted most of its attention to:

(a) evaluating the need and potential for using public policy to increase sources of financing to fill the capital gaps it identified;

(b) examining the difficulties faced by the banking system in meeting small business capital needs;

(c) examining certain issues of State tax policy and small business needs for management assistance, to the extent that those issues affect the ability of small business to gain access to capital.

The Task Force left to the Taxation, Regulation and Assistance Task Force the detailed analysis and recommendations with regard to tax policy which affect the capacity of small businesses to generate capital internally.
Although the State of California can have little effect on overall macro-economic problems, there are a series of initiatives which the State could either encourage, or undertake on its own, to ameliorate the capital and credit difficulties faced by small businesses. These initiatives fall into three major categories:

A. Small but significant reforms in the regulation of state-regulated financial institutions, licensing additional independent banks and aggressive negotiation with leaders of the lending community to establish greater participation in opportunities available in small business lending.

B. Introduction of new instruments and techniques to permit small businesses to borrow at more favorable interest rates, for terms that are longer than currently available.

C. Creation of a package of regulatory and tax changes to make equity investment in California small businesses much more desirable than is currently the case.

The Task Force's recommendations (Appendix 1, pages 102-103) are directed toward creating initiatives in these areas. The remainder of this Discussion Summary examines the performance of institutional sources of small business capital and sets forth the findings on which the Task Force's recommendations are based.

C. PRIVATE SOURCES OF SMALL BUSINESS CAPITAL

Commercial Banks. Small businesses rely on banks as the single most important institutional source of small business finance. Banks provide small businesses with general short-term credit, secured loans and, along with specialized private lenders, inventory and receivables financing. Small business reliance on banks has increased markedly in the past 10 years. Evidence also suggests that, during this period, the average maturity of loans from institutional sources, including banks, has been dramatically reduced. At the same time, the availability of both long-term debt from other sources and of risk equity capital has been significantly reduced. This reduction places additional pressure on small businesses to utilize short-term bank lending as though it were risk capital. Standing squarely in the face of this development is a history of bank regulation and banking...
practice which encourages banks to avoid business risks, even when accompanied by commensurately higher rates of overall return. The Task Force was particularly concerned about the effects of risk aversion by institutional lenders. One Task Force member summarized research results on this issue in a paper as follows:

It was found that a majority of California's major bank senior officers defined the market for bank loans as the "no risk" market and did not believe in gradations of risk, even if accompanied by similar or even better ratios of return.

Put in simple numbers, banks generally believed that a loan portfolio with a 12% face interest return and 0.5% loss rate was acceptable, yielding an 11.5% return before expenses. Banks did not believe that a 14% face return with a 1.5% loss rate yielding a 12.5% net return before expenses was an acceptable business practice.*

Because of risk aversion, many small businesses, which as a class are perceived almost universally to be higher risk borrowers, find it difficult to obtain debt capital at any cost. This difficulty is especially true of term loans with maturities in excess of two years. Risk aversion is prevalent in older urban areas where the banking community is more consumer oriented and where business risks are believed to be higher.

Rather than attempting to combat such credit policy, both Federal and State banking regulation tends to reinforce it. Typically, banks are very highly leveraged, and in order to protect depositors, both the Federal and State governments have adopted extremely conservative standards of bank regulation. The most obvious example of this regulatory orientation is the tendency of bank examiners to "classify" loans to small businesses without regard to the borrower's actual credit worthiness. Classification means that a loan is deemed so insecure that it may not be counted as a part of the banks' assets for purposes of calculating reserve requirements.

One major Federal small business program has focused on this issue. The Small Business Act of 1958 guarantees 90% of the principal of bank loans made to small businesses. That program, however, has not been able to alleviate risk over some issues fully because both banks.

and small businesses perceive the additional costs of transaction and red tape to be excessive, and because the guarantee authority under the program is limited. Nonetheless, over $2.4 billion in SBA guaranteed §7(a) loans were made during fiscal year 1980.

The Task Force formulated five recommendations intended to reduce the incidence of risk aversion in small business lending. They are intended to complement Federal efforts.

The Task Force concluded that the degree of concentration in the banking market in California is a factor in the availability of finance for small businesses. Large banks tend to concentrate their commercial lending efforts on larger customers because the transaction costs of making such loans and the risk factors both tend to be low. The extensive branch networks of the larger banks in California have not resulted in a strongly positive response to small business lending demand. Branch bank loan officers often have a conservative approach to small business loans. In part this conservatism results from the method the banks use for evaluating the performance of branch bank managers and loan officers. Such evaluations tend to focus on the number of defaulted loans attributable to the branch, rather than to lending profitability. Branch bankers too frequently are not adequately trained to evaluate small business loan applications, and the high turnover of branch bank lending officers tends to make it difficult to maintain long-term borrower relationships which would support higher rates of loan approvals. Many branch bankers advance through their bank’s administrative system as head tellers and operation managers rather than through the bank’s lending system. Officers with this training often manage a branch with high teller activity, usually in urban communities. Such an officer too often lacks long-term commitment to commercial lending and, as a result, urban small business lending needs are likely to be de-emphasized.

In order to meet the needs of many small businesses for more accessible short and medium-term lending, banks should be encouraged to develop alternative systems of evaluating small business lending applications. Newly established small businesses are rarely able to project current net earnings, and many expect to generate profits no sooner than several years after start-up. Yet banks consistently tend to evaluate requests for loans during a business’s incubation stage on a yearly performance basis without regard to growth potential and future profitability. This short range approach to lending is a deterrent to adequate capitalization of new and growing businesses. Lending based on growth potential is clearly
needed. Such alternative lending criteria are used as a matter of course in some foreign countries, including Japan.

It appears that small and newer banks tend to provide proportionately better financing services to small businesses than larger banks. Creation of additional banks could help small businesses in many communities. However, in too many instances, small banks cannot generate sufficient savings activity and deposits to meet the loan demands of local small businesses. This is a particularly acute problem in economically depressed areas where savers tend to be older people who have been customers of a large bank for many years. Increasing the liquidity of small and new banks could be an important aspect of a strategy to improve the availability of financing for small businesses.

The need for adequate data concerning small business lending is a very important issue. There is very little information concerning business lending patterns, broken down by size of business and location of lender. While the Federal Community Reinvestment Act requires some small business loan information disclosure, most banks aggregate their commercial loans in their reports, making it difficult to determine actual performance by area. Without such data, it is impossible to determine how well a bank has performed as a small business lender. A statewide bank may make a significant cluster of small business loans through a single branch to particularly attractive borrowers, such as highly successful electronic businesses, while at the same time ignoring all other small business loan demand. Such a cluster of loans might not reflect as significant a commitment to small business lending as might otherwise appear. As a result, there is a need to supplement the disclosure requirements of the Federal Community Reinvestment Act in order to require bank branches to disclose their small business lending activities within their immediate neighborhoods.

Other Institutional Lenders. In addition to banks, there are a number of other institutional capital sources theoretically available to small businesses. In actuality, however, most small businesses receive no capital from non-bank, private institutional sources.

When non-bank credit is obtained, it often is from suppliers. Businesses interviewed by the Project's research team indicated that suppliers' credit was important to them, although it was limited in versatility. Credit extended by suppliers is almost always short-term and usually secured by a lien on the items purchased. Equipment financing often involves leasing rather than sales.
Businesses in some industries tend to use specialized lenders for equipment, receivables, or inventory financing. The specialized lenders include commercial finance companies and industrial loan companies, which are state-regulated financial institutions which provide a variety of relatively high-cost business credit services. The maturity of loans issuable by industrial loan companies is limited, in general, to seven years or less. Industrial loan companies are a relatively insignificant aspect of the small business capital market.

Savings and loan associations are primarily known as sources of home mortgage loans. Nonetheless, they are also permitted to lend funds based on the security of real property other than residential property. Federally chartered associations may invest up to 25% of their assets in commercial real estate loans, commercial paper and corporate debt securities. State chartered associations are likewise permitted to make commercial real property loans for terms of up to twenty years. Because of the massive size of the savings and loan industry in California, any comprehensive attempt to stimulate increased lending to small businesses must include them as an integral component, despite the fact that commercial and industrial lending has historically been a minor aspect of their activities.

Life insurance companies are major sources of capital for larger businesses, primarily for placement of longer term debt securities, sometimes with equity participation. However, financing from insurance companies is relatively unavailable to small businesses. Most insurance debt placements are of substantial size, in order to reduce transaction costs, and are generally beyond the scale of the needs of small businesses. Moreover, legal restrictions on the portfolios of insurance companies restrict their ability to invest in small businesses to a substantial degree. Finally, insurance companies lack the "retail network" of branches and lending officers that banks tend to possess, making them less accessible to borrowers. Despite the unfavorable attributes of the insurance industry as a source of capital for small businesses, the size of the financial resources which they control gives insurance companies interesting potential for involvement in small business lending programs. However, any such small business lending program necessarily must include creation of new intermediary institutions to perform the marketing and credit analysis functions which insurance companies are currently ill-equipped to undertake. Another possible tactic is the assembly of a sufficiently attractive package of State and Federal incentives to induce existing
fiscal intermediaries, such as brokerage houses, to package small business loans in formats which are more accessible and acceptable to insurance company investors. An example of this latter approach is the combination of Small Business Administration guarantees and California Pollution Control Financing Agency tax-exempt bond issues. The bonds are industrial revenue bonds backed by a guarantee of the SBA. They typically provide financing for 10 or more small businesses under a single issue. Packaged in this way, the bonds are an attractive investment for both institutional and individual investors, when priced at the market rate for AAA tax-exempt issues.

Institutional Sources of Equity Capital. The problems faced by small business in tapping the public market for equity securities were described above. Even greater problems exist in attempting to sell equity securities to private and public pension funds. The pension funds constitute the largest institutional source of investment capital in the nation, but because of legal restrictions on investments and lack of appropriate financial intermediaries, their capital is unavailable to small business. The investment policies of private funds are constrained by the Employees Retirement Investment Security Act, which has resulted in increasing the concentration of fund managers on the debt securities and stocks of the largest and most stable corporations. State statutes mandate the same result for all but a very small proportion of the assets of public pension funds.

Despite traditional reliance by the funds on long-term corporate bonds and mortgages, market conditions have forced the funds increasingly into stocks and, more recently and in very modest amounts, into venture capital. This movement could provide the basis for significantly increasing the flow of private capital to smaller businesses if appropriate intermediary institutions can be found or established to create and manage small business investment portfolios. The Task Force believes both the BIDCO program and existing SBICs offer good starting places for such a program.

D. PUBLIC SOURCES OF SMALL BUSINESS CAPITAL

Small Business Administration

The major Federal response to small business needs for capital has been through the Small Business Administration, which operates a large general purpose loan guarantee program and a large number of small special purpose direct and guaranteed loan programs for eligible small businesses.
Section 7(a) Loans. In fiscal year 1979, the SBA guaranteed $2.58 billion in small business loans and made direct loans of $229 million. In fiscal year 1980, the corresponding figures were $2.38 million in guaranteed loans and $83.5 million in direct loans. It is worthwhile to note that these nationwide dollar amounts for Small Business Administration lending represented in 1980 a total of 16,360 loans to small businesses. This number should be compared with the over 400,000 small businesses in the State of California which employ one or more people in addition to their owners.

The Small Business Administration's direct and guaranteed loan program, Section 7(a), is by far its most important undertaking in the capital markets. Nonetheless, in addition to the fact that a relatively limited number of loans are available, SBA guarantees and direct loans have not been efficient in gaining access for small businesses to new sources of capital. The SBA has become increasingly concerned with collateralizing its exposure in the same way that a private bank would. Because of this trend, the main advantage to most businesses of a SBA loan is to gain a slightly lower interest rate and a slightly longer term for the loan than would be the case if the business collateral had been used for a purely private loan. In addition, SBA loans typically require business entrepreneurs to risk all of their personal assets, in addition to all of the business's assets, in support of the loan. By requiring such pledges of personal property, the SBA guarantee becomes most attractive to people who own stable businesses or to those who have little in the way of personal assets to lose if the business fails. This policy, therefore, is no incentive, and perhaps is a disincentive, for people who own property who might consider starting a new business. Small business owners are almost uniformly negative with regard to the "red tape" generated by the SBA loan approval policy. The SBA requires secondary evaluation of all SBA loans by a SBA loan officer, an unnecessary and expensive step which tends to shift responsibility for making the loan from the bank to the Government. Finally, the SBA provides assistance only to businesses which fall within its size standards. Because of the rapid erosion of the capital market for any business less than a very substantial size, there is a gap for businesses larger than the SBA size standards but not so large as to be able to gain access to significant bank lines of credit or private placements from insurance companies.
Small Business Investment Companies. The Small Business Administration licenses and regulates Small Business Investment Companies ("SBICs"), which are privately capitalized and managed financial institutions. SBICs are chartered to provide equity capital and long-term loans with maturities of at least five years to small businesses. They also are authorized to provide management assistance to the companies they finance.

Although an SBIC can purchase equity securities of a small business, it is prohibited, in most cases, from owning more than 50% of the voting securities. SBICs are able to guarantee loans made by lending institutions to businesses in which the SBICs have invested. SBICs are means of funneling public funds to private businesses through the medium of long-term loans by the government to each SBIC. After an SBIC is qualified, and is licensed, the SBA will lend up to $3.00 of Federal money to match every $1.00 of private money invested in the SBIC. Funds lent to the SBIC by the SBA carry a one-half percent surcharge over the government cost of capital. The surcharge covers operating expenses and is used to create a loss reserve.

So far there have been no serious losses and there is a substantial surplus in the loss reserve. The SBIC program is currently of substantial size, with over $650 million in financing to small business outstanding as of the end of fiscal year 1980. At that time, there were 439 SBICs, including 110 so-called Section 301(d) licensees. Section 301(d) licensees are SBICs which have been provided with additional financing incentives which lower their operating costs but which must direct their financings towards businesses owned and operated by individuals who are economically or socially disadvantaged.

Although SBICs are an important resource for small businesses, they suffer from a number of faults designed into the program. The principal difficulty is their inability to provide "patient" or long-term, non-interest funds to growing business. SBICs must cover their overhead and the current interest costs on the debentures issued to the government. As a result, SBICs are biased in favor of low risk investments which pay an immediate return. Their investments typically take the form of convertible, interest bearing loans rather than straight equity investments. Despite this objection, SBICs remain an important addition to capital access for small businesses. However, the performance of SBICs could be improved by public investments which provided funds on which interest is deferred. Such investments in the SBICs would permit them to increase the flow of equity to growing small businesses.
State and Local Development Corporations. The State Development Corporation program, under Section 501 of the Small Business Investment Act is a potentially important source of capital for California small businesses. California is unique in allowing for the formation of any number of development corporations within the State under the licensing and regulatory authority of the State Banking Department. The regulated statute of the State Development Corporations, known in California as Business and Industrial Development Corporations or "BIOCOs", is particularly important, because it permits these institutions to be eligible for other government guarantee programs, including the SBA Section 7(a) program. Use of other guarantees is critical to a BIOCO because virtually no guarantees under Section 501 have been granted in recent years.

A BIOCO can be incorporated and owned by a wide variety of investors, including individuals, financial institutions, business corporations, public utilities, non-profit organizations, and governmental bodies. The opportunities for a BIOCO's financial operations are equally broad. It may lend money or otherwise extend credit, purchase securities directly or indirectly, or lease property to the businesses in the State of California. In addition, it may provide management and technical assistance and advice to California business firms.

Although the primary purpose of the State's BIOCO legislation was initially to permit the operation of State Development Corporations pursuant to Section 501 and to use Section 7(a) of the Small Business Act, BIOCOs are not limited to operations involving the Small Business Administration. They are authorized to provide financing assistance and management assistance to business firms, without regard to size standards, provided they are located within the State of California. One of the primary attractions of the flexibility available to BIOCOs is the ability to utilize their status as a licensed and regulated financial institution to obtain federal guarantees for up to 90% of the amount of the loan extended to a small business. After obtaining such a guarantee, a BIOCO may attempt to sell the guaranteed portion of the loan to other institutional investors and re-invest the proceeds from the sale of the guaranteed portion. In this way, the BIOCO, which originated the loan, can multiply its initial capital for lending into a much larger amount through the use of the Federal guarantee. This leverage is limited, of course, by the constraints, mentioned above, on the use of the Section 7(a) program, such as excessive reliance on
collateralization, high transaction costs and delays resulting from SBA loan approval policy, and loan size restrictions imposed by the SBA. Nonetheless, the ability to obtain Federal guarantees of BIDCO loans makes this type of small institution a potentially powerful source of capital for California businesses. The potential will not, however, be realized unless significant amounts of equity capital are invested in BIDCOs. During the first three years after adoption of the BIDCO legislation there has been no rush to incorporate and capitalize BIDCOs, although at the date of this report, two are in existence and others are planned. Having created this unique and potentially powerful institution by statute, the State of California should direct its attention to perfecting the institutional framework for the operation of BIDCOs and to encouraging their initiation and operation.

The SBA also administers programs of local development company loans for purchase of land, buildings, machinery and equipment. In fiscal year 1979, SBA direct and guaranteed development company loans totalled $79.7 million, and in 1980 totalled just $20 million. For fiscal year 1981, however, the SBA is authorized to provide a 100% guarantee of principal and interest on debentures issued by certain selected local development companies which have a full time professional staff, an active board of directors and professional management. The amount of each debenture guaranteed by the SBA cannot exceed one-half of the cost of each small business project. The remaining one-half must be obtained from non-Federal sources. For fiscal year 1981 this program will have a budgetary allocation of $100 million. This program is particularly well suited to local business revitalization programs.

Industrial Development Bond Financing. Until January 1, 1981 California had no State wide authorization of tax-exempt industrial development bonds. Such bonds are a mainstay of the economic development efforts of many states. The passage of AB 74 on August 31, 1980 authorizes up to $200 million of small issuance bonds to assist private businesses. The Act authorizes within each city and county in California an Industrial Development Authority which can be activated by vote of City Council or Board of Supervisors. An authority can issue bonds, to be paid by revenues from the businesses assisted. The bonds may be used to finance industrial projects (manufacturing, assembling or processing) or certain energy related projects. The bonds are intended to be used for small projects, as defined in Section 103(b)(4) of the Internal Revenue Code, and as further limited by the need to fall within the two eligible categories. Commercial facilities, such as shopping centers, retail
stores, medical facilities, hotels, etc. are ineligible. There may, however, be aid for commercial businesses in the 1980 amendments to the Community Redevelopment Law (SB 99), which will permit financing commercial structures in a redevelopment project area.

The Industrial Development Financing Act sets up the California Industrial Development Financing Advisory Commission which will approve or disapprove the bonds. Criteria for approval include a finding that the public benefits (including increased employment or payables, reduction of prices or increase in quality of products or better utilization of materials or energy) exceed any detriments.

Revenue bonds could be an exciting new source of funds for California small business, but several large questions remain. Without some form of risk spreading or mortgage insurance, the bonds may not be saleable to the public. This would mean that bank and other institutional lenders might be the only purchasers, and then only for bonds backed by relatively large and stable businesses. In addition, the limit of $200,000,000 may quickly be reached if the bonds are used for relatively large projects. There is no certainty of expansion of the borrowing limit.

Revolving Loan Funds. Publicly-funded revolving loan funds, operated by local governments or community-based organizations, are another potentially significant source of loan capital for urban small businesses. This type of loan fund has been created both by the Economic Development Administration under Section IX of the Public Works and Economic Development Act and by some cities using the Urban Development Action Grant and Community Development Block Grant programs. More than 15 locally operated revolving loan funds utilizing EDA or UDAG monies have been started or authorized in the State of California. They range in size from approximately $300,000 to several million dollars in initial assets. The State of California has used a portion of funds it receives from EDA to provide backup technical assistance in creating and operating local revolving loan funds for small businesses. However, the amounts allocated to the State for these types of activities are relatively small when compared to EDA's large expenditures for public sector grants for infrastructure and capital improvements. There is great potential for combining these local funds with private capital sources, including banks and BIDCOs, in coordinated programs for small business financing programs.
Community Development Corporations. Finally, a small but potentially significant source of capital for urban small businesses is found in community development corporations. Community development corporations ("CDCs") are the result of a federal anti-poverty program initiated in the 1960's. CDCs are community-based non-profit corporations charged with facilitating economic revival of their neighborhoods utilizing a combination of public funding sources and private investments. Certain CDCs, approximately 40 nationwide, including several in California, receive more intensive funding to conduct institution-building and venture investment programs. Other, smaller CDCs have utilized foundation grants, EDA funds, Office of Minority Business Enterprise funds, and a variety of other sources of support to encourage creation and growth of small entrepreneurial businesses, as well as community-operated self-help undertakings. In certain low income communities, CDC financing may be the only alternative for small businesses to gain a foothold in the capital market.

Management and Technical Assistance. Throughout the discussions conducted by the Capital Access Task Force there was recurring recognition that small expanding businesses typically require some type of management and technical assistance in order both to obtain and, perhaps more importantly, to utilize effectively, additional needed capital. The need for financial, management and technical assistance for small businesses was voiced across the business spectrums, by owners and operators of private venture capital firms seeking investment opportunities as well as owners of small struggling neighborhood businesses. This need is clearly not being met by existing institutional sources of education and training, nor by private business consultants, nor by financial institutions with which small businesses may come in contact.

One result of recognition of the need for this service was embodied at the national level in the creation by the Office of Minority Business Enterprise, beginning in 1972, of a large number of Business Development Organizations ("BDOs"). BDOs were essentially community-based organizations funded to hire professional staff to assist potential minority entrepreneurs. There were problems in finding qualified staff for such projects because there was little prior formalized business assistance for any class of small business. Few small businesses had believed that they could afford to pay professional costs for such a service. The people who worked in such organizations were generally new to such work. BDOs primarily packaged loan applications for SBA guaranteed
loans. Once financed, either through SBA Section 7(a) loans or from a Section 301(o) SBIC, the financed businesses were usually on their own, without continuing management and technical assistance. Such assistance was theoretically available from a separate group of OMBE-funded organizations called Business Resource Centers. Unfortunately, the businesses helped by BDOs rarely were helped by BRCS. Moreover, BDOs did not have ongoing responsibility for the long term successes of the businesses they assisted with financial packaging.* The contractors with responsibility to provide management and technical assistance (the BRCS) also had no long term financial commitment to the businesses. As one commentator has said, "Few business problems are of a nature that they can be solved by one-shot consulting assignment, and the program did not tie together the long-term commitment to success, the capacity and financing to support technical assistance, and the 'gut level' commitment to the success of the business matched with a financial investment in the business. No government programs more clearly point out the needed close relationship between all of the elements of business assistance than the minority enterprise program." **

Whatever initiatives eventually undertaken by the State in the field of financial technical assistance to small businesses must be designed to link immediate services to longer term commitments to the health of the businesses served. The Task Force on Education, Training and Technical Assistance suggests (pp. 43-46) that Small Business Development Centers attached to public educational institutions are a viable, tested way to deliver financial technical assistance.


** Hansen, Op. cit., p. 64
Government intervention in the private conduct of business is a pervasive fact of modern American life. These interventions take the form of an enormously complicated system of taxation conducted by local, State and Federal taxing authorities, the operations of civil judiciary, which adjudicates and enforces legal rights among private litigants, hundreds of legislatively authorized regulatory bodies for the purpose of promoting safety and the protection of the public, public contracting and procurement to provide for the needs of the government for goods and services, public works such as roads and ports, and finally, a host of governmental assistance programs which provide incentives and resources to private businesses. Small businesses have a strong interest in each of these areas, but often have been unable to participate effectively in decisions which affect them.

Historically, much lip service has been paid to the desirability of encouraging and maintaining the strongest possible small business sector in the national economy. However, public intervention in private markets has too often resulted in taxes, regulations and assistance programs which are primarily addressed to the actions or needs of larger businesses. The effect of this orientation, at both the Federal and State levels, has been to impose disproportionately large burdens on the owners and prospective owners of small businesses who seek to comply with governmental rules or to gain access to the benefits in the tax code, or from public procurement. These burdens make it more difficult to start a new business or to expand an existing one, and are particularly onerous when compared with the ability of larger businesses to comply or gain access to benefits. To the extent that small businesses are inhibited in their formation and growth, private employment is also
hindered, because small businesses generate disproportionately large numbers of new jobs. A big business orientation is particularly inappropriate, because the net contribution of large businesses to employment generation in the private market has been negligible in most parts of the country, and modest in California.

A. TAXATION ISSUES FOR SMALL BUSINESSES

The level and complexity of State and local taxation affect decisions to initiate, locate or expand businesses. These effects are caused not only by business taxes, e.g., corporate net income, sales taxes, payroll taxes, and business property taxes, but also by personal income and estate taxes as well. The costs of tax compliance also affect small business performance. In addition to preparing and filing returns and paying the taxes, many businesses are, in effect, agents of the State in collecting sales tax and payroll taxes. A typical small business operates in a highly competitive environment; profit margins are relatively low. Small firms are disproportionately affected by the costs of tax compliance because they have fewer sales over which to spread the costs of analyzing their obligations, collecting the tax, preparing forms and the like. However, from a public policy standpoint, the most important concern is that the current tax system discriminates in favor of large businesses because it does not permit small businesses to retain or accumulate the optimal amount of capital necessary for current operating needs and for expansion.

1. Corporate Net Income Tax. California is one of 46 states that imposes a net income tax on corporations. Business corporations in California, with certain exceptions, are subject to a franchise tax of 9.6% measured on net income, or $200.00, whichever is greater. Banks and financial institutions pay a corporate net income tax of 11.6% on income. Nationally, California has the second highest tax rate on corporations' net income of all states. In 1976-77 California derived $10.67 of revenue per $1,000 of personal income from corporate net income taxes. This was prior to the increase in the corporate net income tax which was correlated with repeal of the inventory tax. Only the state of Michigan had a higher rate. California's rate was 59.8% higher than the national average.

Because California's corporate net income tax rates are relatively high, they have a significant effect on business behavior and expectations and, even after giving effect to their deductibility under Federal income taxes, are a significant factor in the ability of small businesses to retain capital. The effect on capital formation and
retention is accentuated because the tax is a flat rate rather than progressive, and because of certain, significant differences between the treatment of corporate net income by Federal and California tax laws.

The Task Force was dismayed to discover that the effective State tax rate, after the computation of Federal taxable income, is 50% higher for businesses whose net income was less than $25,000 than it is for businesses whose income is over $100,000. This regressive taxation reduces the ability of small businesses to retain earnings. This retards business growth because the most important source of small business investment capital is retained earnings. The State is disproportionately taxing the major source of capital for small business expansion.

Among the deviations from Federal tax law which disproportionately affect California small businesses are the following:

1. California corporations cannot deduct operating losses incurred in one year, from net operating income in other years.
2. California lacks an analogue of the Subchapter S provisions in Federal law which permit direct pass through of earnings and losses to a limited number of shareholders.
3. Under State law, California corporations pay the same rate of tax on capital gains as they do on ordinary income.

Of these three items, the inability to deduct losses accrued in prior years from current income is the most important aspect of State taxation which discriminates against small, and particularly new small businesses. If a business incurs losses during its first three years of operation and is thereafter profitable, California corporate net income tax will be assessed in the fourth year even though the losses in prior years exceed the current year's gains. This means that, taken as a whole, the four-year period would result in a net loss, on top of which the business would have a tax liability. The tax liability reduces the availability of funds for expansion, just when the business becomes profitable. This is a strong disincentive to business formation and, in particular, to small business growth.

The unavailability of a Subchapter S analogue means that small business start up losses cannot be offset against the other income of investors. This inhibits the ability of small businesses to attract equity investors.
Currently, California corporations pay the same rates on capital gains as they do on other types of income. Reduction of rates on capital gains for certain types of businesses, or on certain types of assets, or both, might result in a substantial incentive to purchase new plant and equipment. This issue needs additional exploration and research, but provides an interesting option for public policy.

2. Personal Taxation. As expressed above, there is an intimate relationship between the ability of small businesses to attract or generate capital and the taxation of individuals. While the principal source of small business capital is retained earnings, the two principal sources of start-up capital are entrepreneurs' savings and investments by family, friends and associates. The attractiveness of an investment from either of these two sources depends in large measure upon the perception of gain to be realized upon the success of the business. At the Federal level, capital gains taxation rates increased from 25% in 1969 to 49% until 1978 when Congress reduced the ceiling to 28%. Not only did equity underwritings of small businesses dwindle to almost nothing during that period, but the attractiveness of private investments from savings and by family, friends and associates of a business owner also dwindled markedly. Although rates are now reduced, in order to attract capital from outside of a small business, further reform is necessary. While the bulk of taxation on capital gains is at the Federal level, State income tax rates are not inconsiderable. A State policy to encourage capital formation in small businesses should include attention to mechanisms to defer or forgive taxation on capital gains of individuals which are re-invested in small businesses or which are derived from the sale of interests in small businesses. Providing a deferral of capital gains tax on gains from passive investments which are invested in small businesses is a particularly promising way to spur productive, job producing investing.

3. Payroll Taxes. There has been a tremendous increase in the payroll tax burden borne by businesses in the past 15 years. Most of the increase can be attributed to the increase in social security rates and the tax base on which social security taxes are calculated. The 1980 maximum cost for social security taxes is 4.24 times the 1970 level. Allowing for inflation, this is still a doubling of the social security tax rate.

Payroll taxation, however, is an area in which it appears that the State can do little to alleviate the direct, financial burdens of small businesses. The State's collection of unemployment insurance, workers' compensation
and state disability insurance is not typically a major portion of the tax burden of small businesses. However, with regard to administration of taxation the State could do much to provide a more equitable procedure for appeals of administrative decisions affecting individual small businesses. It may be perceived as being costly for a small business owner to attempt to appeal an unemployment claim or an adverse ruling regarding workers' compensation. Commendably, the State has made a concerted effort to reduce the paperwork associated with filing and paying payroll taxes. This effort should be continued and reevaluated periodically. Some small businesses suffer from what they consider to be excessively high workers' compensation premiums. Re-examination of the effects of workers' compensation on small businesses which operate in hazardous industries may be warranted.

4. Local Taxation. Following the adoption of Proposition 13, numerous California cities hastily adopted major increases in local business fees and taxes. Some of these taxes had previously been considered merely "nuisance taxes", but after the increases they became substantial drains on the income of small businesses. Typically, cities with relatively depressed economic activity imposed the greatest number of these types of taxes. Such taxes are in the end counterproductive to a healthy local economy, because they tend to drive out otherwise viable small businesses, especially the very smallest small businesses. As a matter of public policy, the State government should investigate in detail the options available to alleviate the burden of such disproportionately high local business taxes in depressed urban areas and neighborhoods.

B. IMPACT OF STATE REGULATION ON SMALL BUSINESSES

Governmental regulation is a substantial problem for many small businesses. The problem was illustrated by a hypothetical example by James D. McKevit, Washington Counsel for the National Federation of Independent Business in hearings before the U.S. House Subcommittee on Special Small Business Problems in 1979:

You are a small businessman with 25 employees. As such you are not only general manager but function as sales manager, personnel manager and so on. You typically have a 60-hour work week. In addition to operating your business, you are expected to identify all federal regulations affecting your business from the more than 70,000 pages of the Federal Register printed annually, as well as state and local regulations, read and understand them, recognizing that the regulation
per se is the only arbiter of compliance, and then absorb the cost, with the knowledge that your per unit costs is greater than for larger competitors.

The degree of regulation imposed upon a small business by State and local authorities is primarily determined by the type of business operated. Many types of businesses require either a State or local license, or both, in order to begin operation. Such licenses include both competency-based licensing, such as for contractors or cosmetologists, those involving public safety and convenience, such as for emergency transportation services, or licenses such as those to control alcoholic beverages, undertaken to protect the safety, welfare, health and morals of the people of the State. Some of the less obvious forms of regulation affecting small businesses include local zoning ordinances and zoning bodies, local building codes and building inspections, State securities laws affecting the ability of businesses to issue securities, and a host of industry-specific regulatory bodies including the State Banking Department, the Department of Insurance, the Department of Real Estate, the Bureau of Automotive Repair, etc. Finally, several State regulatory agencies have broad ranging jurisdictions affecting many types of businesses. These include the Air Resources Board, the California Coastal Commission, the Division of Occupational Safety and Health, and the Division of Labor Standards Enforcement, among others.

Perhaps the most pernicious type of regulation is creation of entry barriers which unnecessarily inhibit formation of businesses. Such regulation takes the form of licensing requirements calling for overly stringent skill training, or health, labor or building codes which require excessive capital investments to begin operations. The effect of regulatory entry barriers cannot be detected by interviews with existing business owners, but declines in the number of family operated "mom and pop" operations, especially in low-income areas, can be evidence of the existence of legally sanctioned barriers to business ownership.

The Task Force realized the impracticality of attempting to examine the effect of each of the State's authorized regulatory agencies or commissions as they affected small businesses. In many cases, to the knowledge of Task Force members, these agencies and commissions are cognizant of and responsive to the needs of small businesses. However, Task Force members felt, based upon their experience, that the State had not done nearly enough to design many of its regulatory programs in ways which, while maximizing the
benefits to the public, minimized adverse consequences to small businesses. The needs which were identified as being particularly important to achieve this result are as follows:

1. Evaluation of regulations and administrative procedures promulgated by State regulatory bodies on a cost-benefit analysis basis, with explicit attention paid to costs imposed on small businesses and on potential new small businesses.

2. An expedited remedy and appeal processes for small businesses affected by agency determinations to avoid crippling losses of management time to small businesses.

3. In each case in which there is a potential for adverse consequences to a small business, a low-cost, non-judicial administrative remedy and appeal process.

4. A much more intensive and extensive form of notice giving and hearing procedure, in order to permit realistic opportunities for small businesses to comment upon and participate in the formulation of regulatory programs which will directly affect them.

5. In order to offset the disorganized nature of most industries primarily composed of small businesses, appointment within each major regulatory organization of a small business advocate to bring the point of view of the small business constituency to the attention of policy makers.

6. A central State clearinghouse for regulatory information collected from businesses to avoid time consuming duplication of information gathering.

7. Industry-by-industry checklists of regulatory compliance obligations, and a central data source for businesses seeking such information.

C. NON-REGULATORY REMEDIES

The need of small businesses to gain access to appropriate forms of redress is not limited to the regulatory arena. Small businesses also suffer from progressively greater inability to enforce private claims without excessive delay and legal costs. Many attorneys suggest to their small business clients that it is uneconomical to pursue business claims for amounts of less than $5,000 to $10,000. As a result, many commercial claims in excess of the
jurisdictional limit of the State's Small Claims Courts are abandoned by small businesses as uncollectible. This, in effect, is a denial of due process of law. Most formalized arbitration proceedings, even when they can be included in contractual arrangements, are almost as time consuming and expensive as judicial proceedings. There is a need for a more efficient business claims system for small businesses.

Moreover, reform of the effects on small businesses of the expansion of the doctrine of products liability is long overdue. Without adding to the protection of the public from unsafe products, the current state of the law needlessly endangers the survival of many small retailers and wholesalers.

D. STATE ASSISTANCE FOR SMALL BUSINESS

The State of California has recognized for a number of years the desirability of public policy initiatives to assist small businesses. Typically, these initiatives have been based upon awareness of the importance of the small business sector to the economy of the State in general, and the finding that increased small business opportunities, particularly for minority and economically disadvantaged persons, are a way to promote the health, safety and social welfare of all the citizens of the State. Beginning in 1968, the Legislature enacted six programs which were intended to extend the capabilities of the Federal Small Business Administration and Office of Minority Business Enterprise efforts. These programs are as follows:

2. The Management and Technical Assistance Program for contracts with consultants to provide loan preparation and advice to small businesses operating in disadvantaged areas.
3. A State pooled-investment program to place surplus deposits in small banks.
4. A procurement and contract program creating the Office of Small Business in the Department of General Services.
5. A contract payment program requiring government contractors to pay all subcontractors within 10 days of State payment.
6. The Business and Industrial Development Corporation ("BIDCO") Act which authorizes small business lending institutions which are licensed and regulated by the State Department of Banking.

1. Financial and Technical Assistance. The State's small business and minority business programs have suffered from a variety of problems during the 12 years of their existence. A study prepared for the Assembly Office of Research in 1977 analyzed the State small business programs and concluded that, "Our investigation of state activities in the small and minority business area indicates some duplication of effort, poor coordination and insufficient use of federal programs."

Assistance to small businesses, particularly in the area of management training, was not directed toward a specific group of businesses or business types, but rather was haphazard in application and therefore was likely to miss those firms most suited for such assistance. A particular criticism of the management assistance offered to small business was that State agency personnel and outside consultants were not properly trained to assist small business and "provided the wrong type of managerial problem-solving capability." The inability of the consultants to provide practical solutions to immediate problems was a major fault. Overemphasis on loan packaging was singled out for comment.

Participating corporations seem to be primarily interested in assuring that State funds be available to back up loans made to firms which do not qualify for conventional loans. Large banks dominate the program, and as a result there is a lack of awareness about the program among potential participants in the financial community. The key obstacles to the success of loan programs are: lack of coordination, poor definition of goals and clients to be served, and little incentive to provide increased flows of capital for the small business assistance programs.

The Task Force also found that lack of ability to target assistance to businesses which potentially were significant contributors to the economy reduced the effectiveness of the State programs.

---


** Ibid.
The California BIDCO program (described more fully in the Capital Access Discussion Summary), authorizes incorporation of financial institutions, capitalized with private investments, which can lend to and invest in small businesses, and obtain Federal, including SBA, guarantees of their loans. Currently, there are three California BIDCOs licensed and operating. BIDCOs are a promising, but not yet flourishing, attempt to combine loan capital, equity investment and management and technical assistance for small businesses. It appears that additional legislative honing of the BIDCO concept may be necessary in order to make them fully viable financial institutions.

Effective on January 1, 1981, Senate Bill 16 by Senator Roberti established the State Assistance Fund for Energy, Business and Industrial Development Corporations (SAFE-BIDCO) to provide financial assistance in the form of direct loans to small businesses established in the alternative energy industry and to small businesses seeking to convert to alternative systems. The SAFE-BIDCO is not expected to become operational until after June 1981.

2. Contract and Procurement Assistance. The Small Business Office in the State and Consumer Services Agency was established by the Small Business Procurement and Contract Act of 1973. The purpose of the office is to identify not only commodities and services which can be most effectively supplied by small businesses, but also the potential small business suppliers. In recent years, the Small Business Office has acted as an advocate within the State government for small business needs and concerns with regard to State procurement. The Small Business Office has faced continuing difficulties with regard to:

- coordinating with Federal procurement programs;
- obtaining significant participation of eligible businesses;
- determining the eligibility of potential contractors.

Much of the work of the Small Business Office is based upon the preference which the State grants to small businesses in bidding on State contracts and procurements. The State's preference allows a small business to bid 5% higher than a competing large business in order to obtain a contract. However, because of the relatively small number of small business contractors bidding for State contracts, the 5% preference is not as widely used as might be imagined. In addition to this problem, small businesses are leery of the difficulties in obtaining prompt payment from the State.
Small Business Office indicates that slow payment is a major problem in obtaining small business participation in its program. It has little or no authority to speed such payments from the multitude of independent contracting agencies, offices and departments, nor does it have a revolving fund from which to make advances. The Small Business Office recently has become a more effective advocate for small businesses, but it does not yet have sufficient authority or staff to create major impact upon State procurement.

There are a number of options available to the State to improve the performance of existing programs directed at small businesses. Some steps in making these improvements have already been taken. As described above, the Small Business Office has made improvements in its ability to impact upon State procurement, although not nearly to the extent that is desirable. Similarly, the loan and management and technical assistance and loan programs have been rapidly changed following legislation in both 1977 and 1979 to rationalize the operations of what was formerly entitled the California Job Corporation Program. These programs are operated by the Office of Small Business Development in the Department of Economic and Business Development, assisted by a statewide advisory panel.

The desirability of having two separate offices to undertake significant and related small business activities is open to serious question. The visibility and impact of small business initiatives could be improved by a coordinated or unified effort. Such an effort should include a much expanded rate of small business advocacy, similar to that of the Federal Office of Small Business Advocacy in the Small Business Administration. State level coordination with the programs of the Small Business Administration is a logical, but unattained objective. In particular, the opportunity to support and participate in the SBA’s highly successful Small Business Development Center program should be actively pursued. Two successful SBDC pilot programs operated at California university campuses were allowed to expire in 1980 because of lack of availability of State funds to match the SBA’s contribution. The Task Force believes that this lack of coordination is unjustifiable.

NOTE: Subsequent discussion with the involved agencies have revealed the following:

The Office of Small Business Development has initiated a number of proposals for joint projects with the Federal Small Business Administration to develop basic resource information for persons entering or established in business. It has recently submitted a proposal to the
Small Business Administration to revive the Small Business Development Center Program through the California State University system.

Though the desirability of having two separate offices to undertake significant and related small business activities is a debatable question, it can be argued that the functions of the two small business offices are different. The General Services' office is limited to administering the 5 Percent Small Business Preference Act which can be best performed as part of the agency with overall responsibility for State procurement. On the other hand, it can be argued that the visibility and impact of small business initiatives could be improved by a coordinated or unified effort.
EDUCATION, TRAINING AND TECHNICAL ASSISTANCE TASK FORCE

DISCUSSION SUMMARY

A. Introduction .......................................................... 37
B. Education and the Small Business Sector -- Findings and Analysis ................. 38
C. Training and Human Resource Needs of Small Business -- Findings and Analysis .... 40
D. Technical Assistance -- Findings and Analysis ....................................... 44
E. Conclusions .............................................................. 46

A. INTRODUCTION

The Education, Training and Technical Assistance Task Force had three major areas of concern. These were:

- the effectiveness of the educational system in aiding the development of urban small business in California;
- the role of employment and training programs, particularly those serving the unemployed and disadvantaged, in enabling workers to obtain jobs in small businesses and in meeting the skill requirements of such firms;
- the adequacy of technical information and management assistance available to small business owners and managers.

For each of these areas of concern, the Task Force examined and evaluated needs and requirements, the extent of existing resources and services, potential gaps and problems, and feasible improvements and changes. Although the Task Force focused primarily on California as it undertook this analysis, it also looked at experiences in a number of other states where innovative education, training or technical assistance programs relevant to the small business sector have been introduced. The following sections detail the key points which emerged from the Task Force's analysis.
B. EDUCATION AND THE SMALL BUSINESS SECTOR — FINDINGS AND ANALYSIS

The State’s educational system has a crucial role to play in aiding the development of the small business sector. First, educational institutions are important in educating and preparing existing and potential entrepreneurs. Second, these institutions also educate and prepare the future employees of small businesses. In addition to these two functions the educational system conducts a range of other activities as it serves a diverse student body and meets many different kinds of educational, career, and employment needs. Nonetheless, the small business education functions are important, for they are fundamental in maintaining the long-term health of small business in the State.

Unfortunately, the Task Force found that, in general, the State’s educational institutions are not fully meeting small business educational and employment needs, nor are they adequately serving the needs of entrepreneurs. Overall, the deficiencies found by the Task Force could be classified into two broad categories. First, students are not exposed at either the secondary or post-secondary levels, to the principles of self-employment and the techniques of owning and operating a business. This omission probably reduces the number of potential entrepreneurs with the capacity to establish their own businesses and almost certainly results in business entrants who are ill-prepared to meet the challenges of operating even a simple business.

Second, the Task Force found that specific business education programs for existing entrepreneurs are inadequately developed. Insufficient management and business skills are often major factors in small business failures yet, paradoxically, small business owners and managers rarely have the time to devote to the traditional educational programs. It ought to be possible to provide short, focused, and "non-academic" courses and workshops which would fill this gap and provide much needed information and skills to aspiring, as well as existing entrepreneurs. Such programs would also release the resources of one-on-one technical assistance providers to concentrate more on individual and immediate small business problems. So far, however, these kinds of programs have not been fully developed within the State.

The Task Force reached these overall conclusions after looking at the performance of the educational system’s major component parts, including the secondary schools, adult evening schools, regional occupational centers, community colleges, and the four-year and graduate institutions, as follows:
I. Secondary Schools. The Task Force found that the State's public secondary schools devoted very little attention to either economic or business principles underlying the operation of small businesses or to the practical aspects of working in or owning a small business. The Task Force was particularly concerned about the inadequate treatment of the basics of entrepreneurial and management activity within the vocational education system, despite the increasing attention such programs have given to work experience and work-site education. One reflection of this problem is the fact that within the vocational education system, only the marketing and distributive education curriculum (out of eight vocational education curricula) included specific elements on business ownership and management. The marketing and distributive education curriculum is available only to approximately 4% of the secondary vocational education students in the State.

2. Adult Evening Schools and Regional Occupational Centers and Programs. Specialized skill training is available to adults and out-of-school youths through three public education programs: Adult Evening Schools, Regional Occupational Centers, and Regional Occupation Programs, all administered by the State Department of Education. Adult Evening Schools receive funds from the State and from Federal vocational education legislation to conduct regular secondary education classes. The Regional Occupational Centers and Programs, which are supported by local taxes and State funds, offer a more flexible curriculum than standard secondary programs. While both the adult schools and the ROC/ROPs provide courses in management-related subject matter areas, neither system provides comprehensive attention nor significant numbers of courses which are intended to infuse entrepreneurial concepts. However, a small exception must be made in respect to adult education's business distributive education program.

3. Community Colleges. Community colleges offer courses of instruction to prepare persons either for four-year institutions or for commercial, industrial, agricultural and other vocations. There are 107 public community colleges in the State of California, many of which offer diversified business and management instructional opportunities. Community colleges are ideally situated to educate populations which are not traditionally served, including special short courses, without academic entrance requirements.

Despite the availability of general business-oriented courses and a flexible program structure, community colleges have not been able to provide specific courses of preparation for those interested in becoming business owners or operators. There are several reasons for this. First, on many campuses, entrepreneurship education has assumed a very minor role within
the general category of business supervision and management. Second, the non-credit type of courses most amenable to teaching entrepreneurship and business ownership and management subject matter receive secondary priority from those institutions which seek to enhance their "academic" standing. Third, as one of the fall outs from Proposition 13, community colleges find it increasingly difficult to hire part-time instructors with current knowledge and experience in specific small business subject matters. The most effective entrepreneurship education programs involve a balanced mix of theory and current practical experience. Finally, despite the potential flexibility of the community colleges, insufficient attention has been paid to developing the kind of scheduling and competency-based teaching which will encourage the participation of existing business owners in entrepreneurship and business ownership curricula.

4. Four Year and Graduate Institutions. The campuses of the State University and the University of California conduct, in differing ways, undergraduate economics and business courses of study and graduate-level degree programs in business administration. They also carry out a variety of non-degree teaching and research activities focused on business creation or development. Despite the extent of the resources available within the four-year institutions, educational offerings intended to provide specific training for potential entrepreneurs and existing business owners tend to be available only on an ad-hoc basis rather than being well-coordinated and consistent.

C. TRAINING AND HUMAN RESOURCE NEEDS OF SMALL BUSINESS — FINDINGS AND ANALYSIS

The Task Force examined the resources for, and the training needs of, small businesses and small business employers. These needs, the Task Force found, have often been overlooked and, as a consequence, the resources which have been provided have not always been adequate. In part, this situation has developed because most job training carried out for small business needs occurs informally as a result of on-the-job training conducted by business owners or other employees. This training method, while usually effective, can impose disproportionate costs on small businesses because there are few economies of scale. In addition, where the training in a small business is done by the owner, this may divert time away from other managerial duties.

The Task Force felt that it might be feasible to increase the efficiency and effectiveness of this informal on-the-job training process through efforts which helped small business
operators increase their own skills in employee training and supervision. Such efforts could form part of the increased technical assistance and educational activities recommended by the Task Force. These efforts could also address a related problem which was identified by one of the Urban Small Business Employment Project's research reports -- the problem of hiring the right person for the job. This problem seems to arise not where there is a lack of suitably qualified and trained applicants for a job, but because small business owners at times find it hard to gauge workers' skills before hiring.* To the extent that technical assistance and educational programs can enhance the ability of small business managers in assessing workers' skills and making hiring decisions, then this problem might be eased, although clearly what can usefully be done is limited and must recognize that many small business operators do have sufficient experience and skill in hiring.

In addition to informal training, the Task Force also looked at more formal kinds of training, focusing particularly on provision in the public sector. The Task Force recognized that an extremely broad range of programs is offered by private sector institutions, which include training for hundreds of career choices. Often such schools are major recipients of federal vocational education funding. Some of the private vocational and career schools also provide management training for graduates who expect to create their own small businesses. Entrepreneurship and management skills training is also available from some trade associations and membership groups, as well as from private seminar and workshop providers. Trade unions also have a role, particularly in the operation of apprenticeship programs. However, while the importance of these private-sector providers was realized, the Task Force was unable to come to specific findings as to whether these providers met urban small business needs.

In the public sector, the Task Force looked at the effectiveness of the State's main employment and training programs in meeting small business employer and employee needs, as well as looking at innovative programs in other states. Public-sector employment and training efforts are particularly important when informal on-the-job training is insufficient or where there is a shortage of particular labor skills. In addition, these programs have crucial roles in helping unemployed and disadvantaged workers access jobs (particularly good jobs) in the small business sector, in

contributing to the overall revitalization of depressed urban areas and their small business sectors, and in aiding non-traditional small businesses, such as cooperatives and neighborhood-based self-help businesses. To the extent that the lack of workers with particular skills or the unavailability of appropriate custom training and formal on-the-job training programs constrains the hiring of replacement or additional workers in small businesses, then these firms, the otherwise potential employee(s), the locality, and the State as a whole suffer.

Among the models of good employment and training programs considered by the Task Force were those operated in Nebraska, Oklahoma, Wisconsin, South Carolina and Minnesota. These states offer (or have offered) custom-designed training to meet the unique needs of particular businesses. In Nebraska, for example, the Nebraska Industrial Start-Up Training Program not only provides training to unemployed persons but also is available to upgrade existing labor force skills to meet the needs of each industry. That program offers assistance with advertising, screening, testing and interviewing of prospective employees as well as development of training curricula, materials and time schedules. The Minnesota New Jobs Program also provided similar custom training, while South Carolina continues to do so through its network of Technical Education Centers. The Task Force noted that there is a tendency in such custom training programs to focus on medium-sized to large firms (as evidenced by studies of the Minnesota and South Carolina programs). Nonetheless, it seems feasible that California could learn from these other experiences and adapt the models to small business needs.

The nearest California equivalent to the custom-designed training programs of other states is the California Worksite Education and Training Act. The Task Force considered this program a potentially important vehicle for training workers to meet small business needs. The Task Force also found that the State's Targeted Jobs Tax Credit was not a major factor in job creation or expansion decisions by small businesses. Furthermore, there was clear agreement that the federally-funded Comprehensive Employment and Training Act, a portion of which is administered by the State, was much more available to large businesses than small ones -- partly because of the amount of disclosure and red tape that a business must undergo in order to participate and partly because prime sponsors have not pursued small business needs.

The Task Force was split with regard to the desirability of closer coordination between CETA training and small businesses. Some Task Force members argued that placing CETA participants with relatively low skill levels in a small
business was often ill-conceived in terms of the business's needs, especially for new businesses. Others felt that participation by small businesses in a well-designed CETA program provided both human resources and welcome contributions to the cash flow of the businesses. There was consensus with regard to the fact that the level of resources in the CETA program available for small business needs was relatively insignificant in terms of the overall demand for employment. Nonetheless, it was felt that more could be done, even within these limited resources, in identifying and meeting small business needs. The resources available through Title VII (Private Sector Initiative Program) of CETA as well as those of the State's 4% discretionary funds have, perhaps, the greatest potential in demonstrating how small business needs could be met, but so far this potential has not been fully realized.

A final problem noted by the Task Force was that of labor market information. Although most new jobs are located in small businesses, only a proportion of small businesses grow or have the capacity to do so. These businesses need careful identification. More sensitive and finely tuned labor-market information systems and procedures would help in this identification process and could provide increased information on the training needs of small businesses. This information could be compiled through more sophisticated sampling even though many small firms find it difficult to predict their precise labor requirements for any great length of time into the future.

Overall, the Task Force recognized that it is more difficult for employment and training providers to meet small business needs as opposed to those of medium-sized and larger employers, because the providers have their own economies of scale. For example, in tailoring formal on-the-job training programs which might result in one or two placements per firm, overhead costs no doubt increase. This is unavoidable since most small employers cannot absorb more new workers at one time. Over the longer term, however, working with small employers could well have significant impacts in terms of job retention and business expansion and more than justify the additional costs. Moreover, innovative ways to reduce extra costs could be developed, such as initiating a brokerage system which would bring two or more small companies with similar needs together in order to get a cost-effective program going. This kind of coordination and cooperation can be encouraged by institutional means, through tax incentives, or in conjunction with the planning of training and vocational programs.
D. TECHNICAL ASSISTANCE -- FINDINGS AND ANALYSIS

Technical assistance is an ongoing need for many small businesses. It is especially important for new businesses and for businesses operated by minorities and women. The Task Force thus looked at the extent, quality, comprehensiveness, cost, and accessibility of technical assistance in both the public and private sectors.

The Task Force recognized that most technical assistance for small business is provided through the private sector by business and management consultants and by professionals such as lawyers and accountants. These private sector business professionals provide highly specialized services at relatively high cost. The Task Force, and especially the small business owners serving on the Task Force, were of the opinion that the essential ongoing professional services of law and accounting were fairly accessible to most urban small businesses, but that there is a significant gap with regard to general business consultation, including finance, accounting, marketing, management and personnel. Moreover, where these services exist, small businesses often cannot afford to contract with consultants, and then only when business problems reach crisis proportions.

In the public sector, the Task Force noted the contribution of a number of technical assistance initiatives. From the Federal level, the Small Business Administration (SBA) operates a variety of programs. These include the SCORE/ACE programs in which either active or retired executives provide consultation to small business owners; direct technical assistance from Small Business Administration personnel on packaging procurement assistance and loan guarantee applications; and one-on-one technical assistance through Small Business Development Centers (SBDCs); although none of these centers are currently operating in the State of California.

Two pilot SBDCs were jointly funded by the Small Business Administration and the Economic Development Administration in 1978 and 1979. These programs were undertaken at the Center for Business and Economic Development, California State University, Chico and at the California State Polytechnic University in Pomona. Each of these programs conducted well-attended workshops, clinics and conferences providing ongoing training and technical assistance for small business owners. The Task Force found these programs to be highly effective means of reaching a small business constituency which normally does not have available to it ongoing training and technical assistance opportunities. Unfortunately, these
programs were terminated in Fiscal Year 1980-81 because California did not have an appropriate State plan to administer the program. States are required to share half of the cost of SBDCs with the Federal government, so there is a financial issue involved. Nonetheless, the Task Force found the SBDC program to be productive and strongly urged the State to take steps necessary to re-institute and expand the program within California.

In addition to SBA efforts, the Department of Commerce's Federal Office of Minority Business Development (now the Minority Business Development Agency) has funded significant numbers of business development organizations and business development centers to provide technical assistance to businesses owned by minority persons. A small number of these organizations has also provided training to small business owners in addition to their primary focus on financial packaging services. There are 14 BDO/BDCs in California.

From within the State, the Department of Business and Economic Development's Office of Small Business Development on occasion has provided one-on-one problem-solving services, on a referral basis from other branches of the government. The State Small Business Office, in the State and Consumer Services Agency, also provides small businesses with assistance in obtaining State procurement contracts. In addition, a number of community-based organizations, as well as many local governments, play a significant and positive role in providing technical assistance to small businesses.

Although a variety of technical assistance provision exists, the Task Force identified some gaps and problems. More work needs to be done in identifying and developing appropriate, cost-effective small business technical assistance delivery mechanisms. Here, the Task Force felt that the SBDC model was a good one which could be extended. The Task Force also looked at models developed by other states, particularly the Massachusetts Business Information Centers (BIC) program. These centers used CETA resources to provide small business planning and technical assistance services at a local, decentralized level. One problem illustrated by the BIC program, however, was that of ensuring funding stability. Although the program was effective, it has largely terminated as CETA funds have been withdrawn.

In improving technical assistance services, the Task Force concluded that efforts should be better focused on those businesses unable to obtain appropriate private help, on developing better screening techniques in order to concentrate resources on those businesses with the greatest
viability or potential, and on ensuring that programs are localized and accessible. At the same time, the Task Force saw a need to develop and support business skill banks, management assistance centers, and local small business service cooperatives. There also is a particular need to help enhance the technical-assistance activities of community-based organizations, such as community development corporations, which are attempting to revitalize businesses in more depressed areas.

In addition to one-on-one specific technical assistance (on problems like loan packaging, cash-flow problems, or business plans, etc.), the Task Force identified a need to improve the dissemination of more general technical material, such as timely and accurate information on production, management, marketing, administration, financial control, and industry-specific marketing and production data.

E. CONCLUSIONS

The encouragement of the small business sector as a means of achieving structural changes in employment generation and overall economic growth is a particularly attractive and feasible public policy undertaking. However, the success of such a strategy depends to an important extent on resolving current deficiencies in the way the educational system prepares future small business managers and workers, how potential entrepreneurs acquire and improve their skills, the way workers are trained, and how ongoing technical assistance is provided. The Task Force found that these gaps could be significantly narrowed and it identified a range of appropriate models and ideas to help do this. These are embodied in the Task Force's recommendations.

It often seems to be the case, unfortunately, that while problems of the kind noted by the Task Force in the relationship of education, training, and technical assistance with the small business sector are widely recognized, recommendations to help narrow these problems tend not to be always acted upon. There are several reasons for this. First, training, technical assistance, and, in particular, education do not usually produce immediate impacts (although there are important exceptions). Rather, the effects of such efforts often take time to come to fruition, and are frequently qualitative rather than quantitative and easily measurable. Second, the institutional arrangements for the delivery of education, employment and training and technical assistance services are complex with many different providers, numerous funding sources, and non-centralized systems of decision making. Especially in the educational
sector, this relative autonomy is deep-seated (and, in general, very valuable). But this fragmentation and tendency to pursue well-established programs makes change and even coordination difficult.

Third, the business sector itself often takes a short-term perspective and, particularly for small businesses, is subject to continuous day-to-day financial pressures. It is thus hard for individual businesses to adopt the longer-term perspective that the problems of education, training, and technical assistance require. This is reflected in the business agenda which seems to prefer, for example, immediate tax-reductions rather than longer-term, tax-expending education, training, and technical assistance provisions. Those businesses which are able to take a longer-term view are usually larger ones, and as a result public efforts are often focused on such businesses because it is easier to identify and meet their needs. The public role, given these realities, is to take that longer-term approach, not just for large firms, but for the needs of the smaller business sector too.

Finally, there are, of course, resource issues. The Task Force recognizes that this is an era of limited financial resources at all levels of government. Nonetheless, it feels that the problems of small business education, training and technical assistance are important enough and have been overlooked enough to justify additional resources. In part, this may mean developing new resources. But it is also true that there are already sufficient resources within the system to carry out many of the actions the Task Force recommends, providing the necessary priority is forthcoming. The Task Force also accepts that up to now resources have often been lacking in a qualitative sense — the provision of small business education, training, and technical assistance is a relatively new concern and issues abound about how this provision can best be provided. This is why the Task Force has, in many of its recommendations, suggested processes which will encourage innovation, research, and experimentation.

The Task Force recognizes that it is unlikely that all of its recommendations will be accepted and acted upon. In a sense, this is less important than that a process of debate and discussion will have been initiated about small business education, training and technical assistance needs and how these should be met. The Task Force would hope that this discussion will involve small businesses, as well as other constituencies. But the Task Force also would re-emphasize that discussion in itself is not enough; this area of concern has for too long been overlooked and it is now appropriate and important that out of this discussion concrete actions and improvements should follow.
Small businesses are essential components of any urban revitalization strategy. Revitalization of older business areas contributes powerfully to the overall health of an entire urban area, and does so at a fraction of the cost and dislocation of classic, demolish and rebuild redevelopment. Urban communities in California will reap increasing rewards from soundly conceived State support of commercial and industrial revitalization which focuses on the primary economic generator of new jobs, small business.

Compared to much of the rest of the United States, California's economy is young, vigorous and less prone to the devastation of industrial recession than are older sections of the country. California's economy has been described as the first "post industrial economy" because more than half of its workers are employed in service rather than agricultural and industrial positions. Nonetheless, within the last decade California has come to share some of the economic ills associated with a maturing economy. Large, aging industrial plants have been shut down. Whole industries, such as San Francisco's formerly flourishing job shop printing industry, have closed or moved away. Older commercial centers have become dispirited, with unattractive and outmoded physical facilities, resulting in an inability to compete with suburban shopping malls. Major urban manufacturing areas, with buildings primarily constructed during World War II and shortly thereafter, are proving to be undesirable locations for the new, emerging, technology-based enterprises of the 1980's. Inner city work forces find it increasingly expensive and impractical, because of the vastly increased cost of energy, to commute to suburban and rural areas which have attracted growth industries in the recent past.
All of the factors mentioned above make it apparent that to preserve the strength of the California economy and to avoid the type of dislocations experienced by states in the upper Midwest and Northeast, the State of California must increase its efforts to renew the attractiveness of its urban areas to both manufacturing and service industries and to revitalize neighborhood commercial areas.

A. DEFINITIONS OF REVITALIZATION

Neighborhood commercial revitalization can be defined as the physical upgrading of, and financial investment in, selected retail areas of older business districts of inner cities, involving rehabilitation of existing buildings, construction of new, "in fill" commercial facilities, and construction of more sophisticated public improvements. Industrial revitalization means combining existing infrastructure and labor supplies with new resources needed to stimulate the growth of existing businesses and, equally importantly to foster the creation of new, growth-oriented small businesses.

There are a variety of reasons why a revitalization strategy should also be a small business strategy. First, attracting large manufacturing or other industrial operations to older urban areas is, in most cases, a hopeless undertaking. Such businesses are free to direct their capital to those locations which offer the lowest costs and greatest financial incentives. Often these locations are in rural areas or in foreign countries. On the other hand, small businesses are located primarily as a result of the residences of their founders and owners. They are often highly dependent upon specialized and skilled labor forces found in urban areas. Likewise, small businesses tend to serve a more limited geographic area and need, more than large, multinational businesses, a concentrated and accessible local market.

The relationship of neighborhood commercial revitalization to small businesses is also clear. Almost all neighborhood businesses are by definition small businesses, usually locally owned and operated. While exceptions to this generalization can be found, e.g., financial institutions, major supermarkets, and franchises, neighborhood merchants and providers of services are for the most part stereotypical small businesses. These small businesses perform the vital function of facilitating the flow of money within communities rather than channeling it to corporate headquarters, and thus help the communities to realize the maximum benefit of local resources. Despite California's strong general economy, there
are too many localities where small businesses have given up and where boarded store fronts or underused industrial buildings stand as stark reminders that the State is not immune from the urban ills of other regions.

B. RESOURCES FOR REVITALIZATION

Economically distressed cities and communities are not in a position to prevent and reverse a process of decline unaided. The very conditions which characterize a sagging local economy reduce the availability of local resources to provide the services required to make it attractive to private reinvestment in the long-run. When compared to the resources of local government, individuals and small businesses are much less able to affect the business climate in which they operate. A variety of potential resources for revitalization, however, exists at the Federal and State level. But these resources often remain largely illusory for many communities. The difficulties of capturing outside resources can be immense, particularly for smaller cities, and the applicability of such resources to the special needs of the small business community is often extremely limited.

California has some outstanding examples of both commercial and industrial revitalization. Large older factory sites in Los Angeles have been converted to industrial parks for small businesses. The China Basin development in San Francisco promises to provide long term benefits. However, these should be viewed as just straws in the wind of what must be done in order to protect the jobs and stability of our urban areas. The remarkable set of conditions which permit Ghirardelli Square to be a continuing commercial success do not exist in many of our low income urban areas. If strategies to promote economic adjustment and to prevent business flight are to be effective on a more widespread basis, they must be implemented widely, and soon, so that decline does not advance to the near inoperable stage which exists in many Eastern cities.

C. APPROPRIATE ROLES FOR STATE GOVERNMENT

The most important assistance the State can provide in the process of local commercial or industrial revitalization is to provide the resources necessary for comprehensive, effective coordination of existing Federal resources, State services and private investment capital to maximize the development of small business in declined areas. This approach represents the major conclusion of the Task Force. Emphasizing small business development is essential in order to generate the jobs and income on which self-sustaining local economic growth
depend. The growth process involves both public and private inputs, and coordination between the sectors must take place. Where this partnership has broken down, the State should, "prime the pump", if available private sector and Federal resources are to be utilized most effectively at the local level.

This Task Force's principal objective has been to make concrete what is meant by the ambiguous phrase "a public-private partnership." The emphasis on coordination echoes certain pilot initiatives undertaken at the Federal level which have begun to coordinate economic development programs, including those administered by the Departments of Housing and Urban Development, Small Business Administration, and the Economic Development Administration. There are existing, tested models of revitalization coordination even at this early stage of Federal activity. However, to make a significant impact upon the California economy, the State government must replicate, expand and refine techniques already developed. The State can fulfill the critical role of revitalization facilitator through well-targeted financial incentives, development of non-service developmental strategies for local government, and, most importantly, well-designed coordinated technical assistance to local communities and businesses. Much of the governmental structure to implement this role is already in place in California. The task is to focus and coordinate the efforts of the relevant State agencies, including the Department of Transportation, the Employment Development Department, the Department of Housing and Community Development and the Department of Economic and Business Development, upon integrating the needs of small businesses with local developmental activities.

The recommendations presented by this Task Force (set forth in full in Appendix 1) are directed toward this task. The remainder of this Summary describes, first, what we believe to be a model process for support of local commercial revitalization and then a preferred direction for State policy for industrial revitalization activities. Within each of those sections, a summary of resources is presented together with analyses of the barriers which tend to prevent or undermine their utilization in many distressed urban areas.

D. THE NEIGHBORHOOD COMMERCIAL REVITALIZATION PROCESS

Revitalizing a neighborhood commercial area involves a series of activities and events resulting in a functioning local partnership in which each of the partners has defined responsibilities, and from which the partners expect to profit
in one way or another. The participants in such a partnership are a neighborhood-based organization, merchants and property owners, residents, private lenders, and local government. At the beginning of a revitalization process, the merchants and property owners typically see the surrounding residential areas as unstable and changing and feel that they have no control over events which occur outside of their particular business. Residents are unorganized and typically fail to perceive the extent of decline, viewing the commercial area's deterioration as "natural." Lenders, including banks and savings and loans, may understand and be sympathetic to the needs of the small merchants, but typically fail to understand the confusing welter of city and federal programs and mechanisms designed to stimulate private reinvestment.

Most commercial revitalization projects undertaken in this country have been initiated by city governments. A majority of city staff assigned to commercial reinvestment projects bring a public planning background with them. The staff members typically have limited experience in retailing, merchandising and marketing or other small business skills. An intermediary to coordinate public planners and businesses is required. As a result a key, and often essential, participant in a neighborhood commercial revitalization project is the community-based organization. The neighborhood-based organization is able to work in close coordination with the businesses and to supplement their skills with business planners and other specialists. In a recent publication, the National Council for Urban Economic Development stated flatly that, "Neighborhood commercial revitalization projects should only proceed in those neighborhoods which have an organized neighborhood group."*

Despite the recognition that there are a series of functions that can best be undertaken by a community or neighborhood-based organization, far too often well-intentioned organizing efforts have resulted merely in the creation of a constituent group which has formal authority to "sign off" on the approval of a city-prepared public works plan. Without a professional staff capable of coordinating the public resources, and drawing in the private resources, the conducting of a successful reinvestment program is

exceptionally difficult. The neighborhood organization must be prepared to play the central role in the revitalization process and to perform, at a minimum, the following functions:

- Provide central liaison to all other groups involved in the process.
- Serve as the focus for community information regarding process and for generating and sustaining local support.
- Represent and mediate between merchant and resident groups throughout the planning process.
- Provide staff capacity for planning criticism and commercial area management upon completion of the physical aspects of the process.

The neighborhood organization must, in short, embody a working partnership among the other key actors and result in a primarily private sector approach to commercial revitalization. It is too much to expect this approach to simply "emerge" from the local small business community. To achieve this objective requires professional staffing capability at the neighborhood level. Such capability typically arises not as the first, but as one of the later stages of an organizing process which involves bringing together functional committees with membership from each of the partners. These functional groups must include local merchants, lenders, residents; and city officials. If each of the groups decides to support and participate in a revitalization program a group of interrelated responsibilities must be assigned. These responsibilities include:

- identifying expansion and new business opportunities;
- determining structure and organization of the revitalization organization;
- fund raising;
- creating a physical and environmental design;
- conducting public liaison on issues such as zoning, land use, taxes and public services.

The actual object of all commercial revitalization activity is to increase the ability of a neighborhood commercial area to attract additional private investment and consumer spending.
After careful assessment of existing physical and environmental conditions, creation of an inventory of commercial facilities and assets, assessment of business trends and market conditions, and projections of the market potential, a revitalization program is in a position to create a revitalization plan to which all of the represented participants in the process must agree. It is only after developmental goals and objectives are described and quantified and site-specific revitalization projects identified that the number and types of staff necessary to carry out the program can be finalized and the amounts of public and private investment financing necessary for achievement of the goals determined with finality. The responsibility of each of the participating partners for fiscal contributions should be identifiable, based upon risk/reward calculations conducted by each partner separately.

The process outlined above is obviously an idealized one, although it is based upon a series of successful revitalization projects conducted in a number of cities. For purposes of policy creation at the State level, it has several important implications. First, enormous amounts of time and effort can be uselessly expended on planning and program development initiatives to which no one, in the final analysis, is willing to agree. Unless the cooperative network of private and public actors has been organized prior to the planning process the revitalization effort as a whole in any particular neighborhood is likely to collapse. Second, the revitalization process is complex, and during the early stages can benefit from technical support prior to commitment from each of the partners. Third, after obtaining commitments, use of standard sources of investment incentives, technical assistance grants, loan guarantees and public capital improvements to achieve program goals begins to be feasible. The State's participation in this process should be limited to those functions, which cannot with any degree of ease be conducted with existing resources. Those areas and functions may be summarized as follows:

- providing staff or funding for staff to conduct initial contacts and meetings to determine the feasibility of bringing key actors into a working partnership;
- providing independent facilitation of the development of a joint preliminary development agreement between the essential partners;
- providing funding to pay the costs of organizing independent committees of merchants and residents who will participate in the revitalization process;
providing seed capital to initiate locally-operated fund raising and resource coordination activities, both public and private.

With these resources, an ad hoc local institution can be created and provided with staff and technical support. This institution, through functional committees with membership from each of the partners, is responsible for designing a program which reflects the market potential of the area and is consistent with community goals. Thereafter, having identified goals and created a revitalization plan and program, necessary resources can be assembled on a phased basis. The resources must be coordinated by a professional staff which will be responsible for providing technical assistance to merchants in the areas of financing, operations and marketing; conducting new business development; coordinating private investment in physical structures; coordinating public improvements; and directing the overall marketing plan of the area.

The model described above is capable of almost infinite variations; it is a long term developmental process that requires commitment and financing from sources that in many places have had difficulty in working effectively together at the neighborhood level. Coordination and harmonization of the motives, objectives and principles of the city, merchants, banks, and community residents-at-large require commitment of resources that will not result in the creation of any tangible results immediately.

Typically, the coordinative function has been undertaken by publicly-sponsored corporations and nonprofit community development organizations, as well as outside interveners such as the National Development Council or the National Neighborhood Reinvestment Corporation. Despite recent increases in the availability of funding for early stage coordinative activities, conducting such activities in many localities is still based on volunteer activities or woefully underfunded personnel. The resources currently available to conduct early stage coordination include the following: Community Development Block Grants, Office of Neighborhood Development grants to neighborhood organizations, the pilot Neighborhood Business Revitalization Program which coordinates federal resources and trains city personnel, and the Commercial Reinvestment Task Force of the National Neighborhood Reinvestment Corporation (conducts only two pilot projects nationwide). It is these programs which have spurred the creation of revitalization models, which are now available for replication in other locations. However, use of these models will depend upon the availability of early coordination funding. The need for such funding, especially that directed toward organizing associations of small merchants, should be addressed by a coordinated, interagency State level approach to urban revitalization.
In addition to the need for early stage coordinative funding support for neighborhood commercial revitalization, the Task Force also identified a need to provide training to city personnel in the areas of public grantsmanship, financial packaging, business marketing assistance and neighborhood liaison, in order to permit more effective participation by the city in a neighborhood partnership which has comprehensive revitalization goals. Without such training, city personnel, because of their background in capital improvements planning tend to focus primarily on infrastructure development and physical construction to the detriment of the other dynamic components of the revitalization process. Finally, the Task Force unanimously believes that commercial revitalization should be coordinated with comprehensive programs for neighborhood housing revitalization. There are twin pitfalls to be avoided. First, the two programs often compete for scarce city resources. This competition leads to acrimonious debate which retards the completion of either type of revitalization. The other pitfall which should be avoided is creation of commercial revitalization projects which result in overly-rapid gentrification of neighborhoods, involving significant displacement and relocation of lower income residents. State level planning and financial assistance should be directed at and conditioned upon a satisfactory plan for integrating neighborhood commercial with neighborhood housing revitalization.

E. INDUSTRIAL REVITALIZATION OPTIONS

The process of industrial revitalization is not nearly as well defined nor explored as neighborhood commercial revitalization. Enough successful examples of industrial revitalization exist to indicate its exciting potential. Recycling older industrial structures is clearly one aspect of the process, but so is creation of industrial miniparks following the demolition of outmoded factories.

Industrial revitalization is a local, project-centered activity which is conducted by public, quasi-public or private developers. Public developers include agencies of local government and, possibly, local or regional authorities. Quasi-public developers include publicly-sponsored corporations and nonprofit community development corporations. While industrial revitalization is an essentially local undertaking, State programs, policy and statutes have proven to be the underlying bases on which successfully operated industrial revitalization projects in many locations nationwide have proceeded.
"Comprehensiveness" is much over-used to describe the industrial development activities of most cities, yet from a business point of view, it is often critical to investment or expansion plans. However, most so-called "one stop" city industrial development offices really mean that businesses seeking to expand or relocate must go to one source for land, another source for financing, and another source for assistance with city permits, regulations and other matters. It is a particularly complicated, tiring and frustrating undertaking for small business owners who seek to relocate or expand. When the additional difficulties of modernizing and upgrading older areas to meet current needs are considered, the desire of so many small businesses to flee to suburban areas can be understood. State policy and programs are vitally important in the creation of comprehensive local revitalization programs. Several examples can be cited.

Smaller industrial businesses find it difficult to obtain access to appropriately-sized locations in urban areas. Very small manufacturing businesses often cannot find locations small enough to meet their financial constraints while remaining appropriate for manufacturing activities. Growing businesses are often unable to find economical ways to expand physically in their current urban locations. Each of these problems is compounded in densely urban settings, such as the City of San Francisco, by competing demands for land to be developed for residential and office uses. In any comprehensive urban industrial revitalization program there is a need to include a specific orientation to small business location and subdivision services in order to make available land and space in units small enough to suit smaller businesses. Likewise, there is a need to include a mechanism to provide expanding small businesses with additional urban facilities at overall costs which are comparable to those of relocation at suburban and rural sites. The Task Force believes that urban industrial land banking programs, even at relatively modest initial levels, can make significant differences in the ability of a revitalization program to meet locational needs of small businesses.

In the past, urban areas have served as incubators of beginning businesses because of the accessibility of specialized markets and labor and the availability of relatively low cost space and transportation. This incubator function is a special strength of urban areas, and every revitalization program should include a component devoted to the special problems of working with newly-formed small businesses. The need for this component is based upon the fact that the lack of flexible urban facilities, the costs of security, less efficient transportation caused by urban congestion and the difficulty and expense of commuting from suburban areas have reduced the attractiveness of urban areas.
as a site for beginning a small business. Changing these factors clearly calls for a comprehensive approach in which the resources of the local, State and Federal government are molded together. The need for comprehensiveness is further buttressed by the widely shared finding that small business owners and potential small business entrepreneurs are most likely to locate their businesses in areas where the overall quality of life, beyond that of the "business environment", is attractive and personally satisfying. Often the desire for quality of life attributes in a business location outweighs purely cost-based analysis.

Local governments have two basic approaches available to them in assisting a revitalization process, service and non-service initiatives. Service expenditures can include not merely typical municipal services such as police, fire and sanitation, but also capital improvement programs and locally-authorized bonds, loans or grants. Non-service approaches include use of regulatory, tax or administrative powers to assist local businesses. Such non-service approaches can also include organizing functions or advocacy roles for state or regional policy changes needed to further the revitalization process. A recent study pointed out:

Local governments have a variety of strategies open to them to assist small neighborhood businesses. But they are not yet systematically taking advantage of all of the opportunities they have, especially in the non-service area.*

City governments have found it difficult to coordinate categorical grants programs, locally-funded capital improvements, service improvements, business regulation and tax policy. In some places, this coordinative function has been undertaken by community organizations which negotiate with governments at all levels and interface with small businesses. In deteriorated neighborhoods, the role of community-based organizations can be quite broad, emphasizing financial investment and technical assistance (using community development block grants, Community Services Administration funds, or the SBA 502 program). Where local government revitalization programs are rudimentary, community-based organizations often conduct the major portion of comprehensive economic planning for deteriorated neighborhoods and districts.

Although the State's resources are relatively limited, it can draw upon a variety of funding sources to support early planning activities by local governments and community-based organizations which assist local governments, resource identification for revitalization projects, interim funding for project development while major funds are tied up, and other coordinative activities. It is this role that is most crucial in creating the credibility on the public side of any proposed public-private partnership. The next most crucial initiative which the State should undertake to facilitate industrial revitalization is to assist, through legislation, local governments to consolidate project development activities, including land acquisition, building and capital equipment financing and detailed information services in a single, local organization which is accessible and immediately responsible to small businesses. This initiative requires State action:

- to expand the recently enacted Industrial Revenue Bond Act to permit local authorities to prepare financing packages to meet a range of financing needs of participating small businesses in a speedy fashion;
- to integrate work force training programs with facility and acquisitions; and
- to encourage both State and local capital expenditures to be integrated with the needs of affected businesses.

Several models for this type of arrangement exist, most particularly in the states of Pennsylvania, South Carolina and Oklahoma. By coordinating this approach at the state level, wasteful tax expenditures at the local level can be minimized through the application of uniform minimum standards of feasibility and impact.
The Non-Traditional Small Business Task Force formulated and answered the following four questions:

- Can non-traditional business ownership and management increase worker satisfaction and productivity?
- Do non-traditional businesses provide a way to create or retain productive industry and jobs?
- Can non-traditional small businesses generate significant new employment in urban areas and among hard-to-employ populations?
- Can and should the State government facilitate the formation and growth of non-traditional small businesses?

The Task Force answered each question with a strong affirmative, as detailed in Section C of this Summary.

The members of the Non-Traditional Small Business Task Force were drawn from private businesses, community corporations, educational institutions and State government. All of the Task Force members have extensive experience in working with non-investor-owned businesses. This summary relies heavily on the experience and personal knowledge of the members of the Task Force.

| A. Identifying Non-Traditional Small Businesses | 61 |
| B. Functions of Non-Traditional Small Businesses | 63 |
| C. Workplace Oriented Enterprises | 65 |
| D. Developmental, Service and Training Functions of Non-Traditional Businesses | 66 |
| E. Needs of Non-Traditional Small Businesses | 68 |
| F. Resources and Support for Non-Traditional Small Businesses | 73 |
The Task Force was assisted by research undertaken at the University of California, Los Angeles by Urban Innovations Group, the practice arm of the School of Architecture and Urban Planning. The research surveyed the literature and data concerning non-traditional businesses and described a cross section of small California firms which in one way or another are non-traditional. See the summary of the research at pages 90-92, infra.

A. IDENTIFYING NON-TRADITIONAL SMALL BUSINESSES

In the United States most goods and services are produced by businesses, large and small, which are investor-owned and are managed by or on behalf of their owners. Increasingly, however, Americans have experimented with business firms which are structured and which operate very differently from most investor-owned firms. The success of large-scale agricultural cooperatives in providing benefits for farmers has spurred interest in more modest sized non investor-owned firms. Businesses owned by employees, by non-profit associations or by customers can have objectives that differ from most investor-owned businesses, while still retaining a place in the private economy. Their objectives in addition to creating income for their participants, have included neighborhood development, creation of more satisfying jobs, preservation of existing businesses and employment of hard core unemployed persons. Such businesses are hardly a new phenomenon in American history, but at no other time has the potential for widespread operation of non-traditional business been as great as it is today.

Non-traditional small businesses must be distinguished both from traditionally-organized and operated businesses and from charities. A private activity is a charity if it redistributes money or goods and services without generating sufficient revenues from those it serves to cover its costs. Many charities, including some hospitals and relief organizations, are very sizeable economic organizations, producing substantial revenues and employment. Such charities depend on public and private donations for their survival. However, if a firm produces a recognizable good or service, provides employment and generates sustaining revenue from its sales it should be classed as a business. In most, but not all cases, business activities are also conducted for profit.

* See, Appendix 3, "Non-Traditional Small Business in California: Problems and Prospects."
A business may be non-traditional as a result of its legal structure, its work processes, its objectives or its products and services.

**Non-Traditional Legal Structures.** Businesses which are organized on a membership basis are clearly non-traditional. Membership businesses include cooperatives and collectives. Likewise, businesses which are owned and/or controlled by employees, either directly or through trusts or other mechanisms, are non-traditional. Consumer cooperatives, owned and operated for the benefit of customer members, are the most visible urban cooperatives, but businesses with worker members also exist.

**Non-Traditional Work Processes.** Thousands of otherwise traditional businesses have institutionalized management participation by workers in the businesses. These arrangements vary from complete worker democracy in which employees elect managers and officers, to Scanlon Plan shop floor participation programs designed to increase efficiency.

**Non-Traditional Business Objectives.** Businesses have been created and operated to provide communities with jobs, to act as sources of profits for reinvestment in developmental activities, or to conduct needed on the job training. These objectives typically are foreign to investor-owned businesses.

**Non-Traditional Products or Services.** While any genuinely new product or service is in a sense non-traditional, certain new approaches to meeting public economic and social needs through business activities are an alternative to traditional financing assistance or tax incentives. Firms which combine sales of services or products to the private market with explicit contractual commitments to governmental bodies to also provide development, training or employment services are non-traditional businesses. Such businesses may be organized as either for profit or not for profit firms, and can include among their services hiring hard-to-employ persons on either a limited term basis or, as in the case of sheltered work or supported work programs, on a permanent basis.

The Task Force was unable to determine the size of the State's non-traditional small business sector. Based on the research conducted by Urban Innovations Group, it is clear that data concerning the number of non-traditional
businesses is scarce, but that there are certainly several thousand firms in the State which meet the criteria set forth above.

B. FUNCTIONS OF NON-TRADITIONAL SMALL BUSINESSES

If organizing businesses in new and creative ways serves merely to permit a small group of eccentrics to indulge in testing economic theories, there is no need for the State to interest itself in their activities. However, there is far more involved. Non-traditional businesses show great promise for alleviating a number of otherwise intractable economic problems.

The Task Force found that it could answer each of the first three questions posed at the beginning of this discussion summary in the affirmative.

1. Can non-traditional business ownership and management increase worker satisfaction and productivity?

Answer: Yes.

There has been national concern about studies and observations which document widespread instances of lack of worker involvement in work activities and lack of commitment to workplace performance. The causes have been identified as depersonalized workplaces, lack of incentives to produce and widespread changes in the work ethic. The Task Force found that democratically operated workplaces, both investor-owned and employee-owned, improve worker involvement in operations. Likewise, employee ownership of businesses has generally resulted in improved productivity.

2. Do non-traditional businesses provide a way to create or retain productive industry and jobs?

Answer: Yes.

Beginning with the introduction of tax incentives for employee stock-ownership plans, employee ownership has provided a way to preserve businesses that would otherwise have closed and to finance expansion of other businesses. Employee ownership situations offer great promise for small business, if a routinized, inexpensive pattern of ownership and control can be worked out. Cooperatively or community-owned businesses have been successful in breaking the ground for purely investor-owned business in depressed inner-city areas by demonstrating locational feasibility and positive workforce characteristics.
3. Can non-traditional small businesses generate significant new employment in urban areas and among hard-to-employ populations?

Answer: Yes.

Businesses which grow out of neighborhood organizations have proved to be significant and productive employers in low-income communities. Community development corporations and other organizations have sponsored or operated locally important businesses. Supported work businesses provide needed goods and services and provide jobs for former AFDC recipients, ex-addicts and ex-offenders, all at a cost less than existing systems of income transfer and institutionalization.

The Task Force analyzed the contribution of non-traditional businesses toward the solution of the issues presented above. The case studies conducted by the Urban Innovations Group revealed two general classifications of non-traditional businesses:

Workplace Oriented Enterprises: businesses which engage in private production of goods and services while operating with employee ownership or management; and

Neighborhood Economic Enterprises: businesses which mix private production with social aims, including community development, occupational training, developing cooperative relationships or providing services to special populations.

Businesses of the first type are usually organized around issues of workplace characteristics or job preservation. They often embody a strong commitment by their organizers to non-hierarchical decision making or a general ideology of cooperation or anti-exploitation of workers and customers. Businesses of the second type tend to be last-ditch private responses to failures of the private market to provide suitable employment opportunities, economic environments or services.

Workplace oriented enterprises often are designed to improve workplace satisfaction, productivity and job continuity, while those of the second type are often the only viable mechanism to deliver quasi-public services and conduct developmental activities in low-income areas. At
times the distinctions become blurred, as in the case of creation of a neighborhood corporation to purchase and operate a plant otherwise slated to close.

C. WORKPLACE ORIENTED ENTERPRISES

Many non-traditional small businesses are based on the notion that for certain types of businesses, usually those which are labor intensive, there are institutional advantages which make employee ownership an attractive alternative to investor ownership or which can best be achieved through democratically managed workplaces.

Job Security. Investor-owned businesses in cyclical industries tend to respond to slow periods with layoffs. Employee-owned businesses tend, on the other hand, to cut wages or hours. This approach maintains equity among workers and avoids layoffs. Decisions regarding continuation of a business are also affected positively, because an employee-owned business will be kept going even if profits are low. The primary income of worker-owners remains wages, and so long as wages can be paid, the return on invested capital is of lesser importance in determining issues of business continuation.

Business Ownership as a Financial Incentive. Where workers are also owners and managers, they are motivated to achieve higher levels of productivity and workmanship as a result of direct financial incentives in the form of higher distributions of earnings. Workplace disputes tend to be negotiated to resolution more often than they result in confrontation. (This is not always the case, as the recent strike at worker-owned South Bend Lathe Co. indicated.)

Workplace Flexibility. There is a tendency toward increases in worker discretion, innovation and self-improvement at the workplace in employee-owned and operated businesses. Self-organization of the work situation by workers contributes to competitiveness of non-traditional businesses through increases in worker productivity. This conclusion has been documented in studies of the worker-owned plywood cooperatives in the Northwest and the Volvo automobile plants in Sweden.
0. DEVELOPMENTAL, SERVICE AND TRAINING FUNCTIONS OF NON-TRADITIONAL BUSINESSES

The second group of non-traditional business we identified are neighborhood economic enterprises. They tend to value service to a community equally with maximizing earnings. They may be formally organized as for profit corporations, non-profits or cooperatives. Most are small scale, self-help enterprises that started with private funds, including foundation grants and often have used government programs for a portion of their support. The report prepared by UCLA Urban Innovations Group (Appendix 3) describes several neighborhood economic enterprises in detail. See, for example, the studies of TELACU, Spanish Speaking Unity Council, Peralta Services Corp., and Western Communities Industries.

The melding of business and community goals is particularly well illustrated by Western Communities Industries, which is a for profit corporation owned by a Community Action Agency in Fresno. It manufactures and sells insulation on the private market, but its corporate goals include job creation and providing supplies for low income weatherization activities. It was established with financial assistance from a Federal agency, but it is wholly self-supporting. Its gainful activities strengthen the service capacity of its parent organization and reduce its costs while creating beneficial economic and sociological impacts on its low income community.

Forms of Neighborhood Economic Enterprises. A neighborhood economic enterprise evolves from a business opportunity, the neighborhood needs and the expertise of the founders. The following examples are intended to illustrate the diversity of such businesses:

1. Privately-owned firms with formal public responsibilities: These are businesses which are operated in a manner intended to yield both profits to their owners and benefits in the form of capital investment, training, financial contributions or public services to a specific public community. An important example of this type of business is the South Shore National Bank of Chicago, described more fully in Appendix 3. South Shore Bank is a privately-owned neighborhood development bank which, while seeking profits, has as its primary goal "developing the neighborhood for the benefit of the residents."* The

Bank has operated as a small, but profitable, full service commercial bank focusing on the savings and credit needs of its neighborhood, while its affiliates have undertaken real estate rehabilitative services, technical assistance to other businesses and other developmental projects.

2. **Consumer cooperatives**: Cooperatives are businesses that are owned and controlled by the people with whom they do business. While there are some large California consumer cooperatives, such as the Consumers Cooperative of Berkeley, most are small enterprises that operate from a single location. Co-ops operate in virtually every area of the economy, but they are most frequently found in the food business. An important subgroup of cooperatives are credit unions, especially community development credit unions, which are based on affinity bonds between residents of a particular community.

3. **Non-profit or community-owned small businesses**: Neighborhood organizations have begun in the past 10 years to go beyond advocacy roles and to plan, promote, finance and, often, to operate and own small businesses which generate employment, income and needed goods and services. At times, the "business" conducted by a neighborhood organization which provides services may have only one "customer", either the State or Federal government. Activities of this sort include a variety of health care services, senior transportation services, day care centers and training facilities. Community Action Agencies have proved adept at conducting such businesses, which, although conducted by non-profit entities, are very comparable to more traditional professional businesses conducted by, for example, health care firms which receive a major portion of their income from government reimbursements. Such businesses often provide double social utility because they not only deliver a service needed in the marketplace, they also provide training for otherwise unemployable persons.

Community development corporations and community investment trusts in low income neighborhoods have taken the next step and have begun to use a mixture of public and private financing to invest in businesses which benefit the neighborhood, but which can otherwise be indistinguishable from other small businesses. A drug store, or coffee shop which provides enough traffic on a block to discourage muggings is an example. Businesses created and owned in this manner address a number of public policy issues while remaining private enterprises.
4. Supported Work Businesses: Of all the conclusions to come from the Task Force's discussion, perhaps the most controversial is that significant State resources should be devoted to providing operating revenues to "supported work" businesses. A supported work business is organized for the purpose of employing hard-to-employ groups as well as for producing goods and services. A supported work business depends on both sales of its goods and services and on revenues from the government for the employment services which the business offers. Many supported work businesses employ hard-to-employ persons for limited periods and act as a transition to unsupported employment. Others offer permanent employment to those unlikely to find other jobs. The attraction of supported work businesses from a public policy viewpoint is that there are significantly greater benefits than costs as a result of providing a job to a person through this type of business than to maintain the same person on public assistance without a job.

The Urban Innovations Group included two supported work businesses in its study, and concluded that they were effective mechanisms to reach hard-core unemployed persons. Follow-up analysis done at the University of California, Berkeley has detailed the cost-benefit effectiveness of supported work businesses. The conclusion of that work is that supported work demonstrations in 14 sites have been successful and cost effective for two target populations: (1) female recipients of Aid to Families with Dependent Children and (2) former drug addicts. Projects with recently released ex-offenders were marginally cost effective, with strong indications of success.

E. NEEDS OF NON-TRADITIONAL SMALL BUSINESSES

Can and should the State government facilitate the formation and growth of non-traditional small businesses?

Answer: Yes, it can and should.

As it has in other areas, the State should work to create the conditions for business growth when the effects of that growth will benefit all Californians. There are a series of needs which should be addressed to spur the growth of non-traditional businesses.

* See Appendix 3, "Benefits and Costs of Extended Supported Work."
The needs of non-traditional small businesses are similar to those of other small businesses. However, because of differences in structure or objectives, definition of the needs tends to be more complex, and the resources to meet those needs are more difficult to come by. A significant factor which we identified as affecting many aspects of conducting a non-traditional small business is that such businesses are often isolated from sources of information concerning business issues. Such isolation results in part from the fact that they are pioneering new undertakings and in part from the fact that the entrepreneurs who establish non-traditional businesses often are from backgrounds which were devoted to attempts, to achieve public policy objectives rather than work in a small business environment. Entrepreneurs of non-traditional business tend to lack contacts with knowledgeable people in their industry or in business generally.

Training and Technical Assistance Needs. The Task Force identified emotional commitment to quality products and organizational objectives by entrepreneurs and workers in non-traditional businesses as a key positive element in their growth. This commitment is particularly evident in workplace-oriented businesses. However, product commitment must be augmented with training in both traditional and non-traditional management skills if these businesses are to become a significant part of the economy. The report of the Task Force on Education, Training and Technical Assistance, above, pages 39 to 42, details needs for traditional business training. What, then, are the special needs of non-traditional businesses?

Historically, each new line of business has necessitated development of corollary expertise in production management and professional techniques applicable to that particular line. A similar, although more extensive, development is needed regarding the following types of issues confronting non-traditional businesses:

- defining operational practices and limits for participatory workplaces;
- definition of legal rights and responsibilities of employee-owners;
- creation of efficient legal structures for production cooperatives, community-owned and worker-owned businesses;
integration of management techniques with the participation of employees and customers; and
creation of financial and non-financial reporting systems which permit evaluation of progress toward non-traditional goals.

For non-traditionals to prosper in a major way, an infrastructure of knowledgeable consultants, attorneys, accountants and other business service providers is necessary. This need has several components:

1. Both types of non-traditional small businesses have needs for training in basic business skills, e.g., management and supervision, accounting, and marketing, plus they need training in management of unique organizational structures, issues of community involvement, staffing patterns, and financing.

2. Non-traditional small businesses, especially neighborhood economic enterprises, need training in government contracting and grant procurement so they will be able to make informed decisions about building their businesses with the aid of Federal or State programs.

3. Both types of non-traditional small businesses need specialized legal and accounting services.

4. Non-traditional small businesses need technical marketing assistance, including market research and identification, as well as help with communication of the commitment of non-traditional businesses to product quality.

Regulation and Legislation Needs. Although the Task Force discussed aspects of regulation and legislation only briefly, the needs which were identified have important implications for non-traditional small businesses. The State's "stamp of approval" on legal structures, methods of operation, financial recordkeeping and entry and exit of employees would allow for a less costly and frustrating process of formation and growth for non-traditional small businesses.

Some observers dispute that there are significant legal barriers hindering incorporation and operation of the various types of employee-owned and operated businesses. They point to the fact that the Business Corporation Law is extremely flexible with regard to capitalization and management structures, and that producer and worker cooperatives may be incorporated under
the Cooperative Corporation Law. However, attorneys and other professionals are unfamiliar with the alternatives which already exist in the law. In addition, a confusing, difficult and expensive series of steps faces any group which wishes to organize an employee-owned business having the attributes of continuity of control by employees and the ability to sell memberships or shares. As one example, the California Securities Law provides no expedited or exempt procedure for securities of consumer and producer cooperatives although such an exemption exists for agricultural co-ops. Likewise, there is no set of State-issued recommendations and instructions for incorporation of such corporations as there is for stock business corporations.

1. There is a need for legislation to facilitate incorporation and operation of workplace oriented enterprises, including producer cooperatives and employee-owned businesses.

2. There is a need for the State's regulatory agencies to evaluate more sympathetically various non-traditional business operations. This is especially important, for example, in the area of rules for financial recordkeeping for reimbursement programs and State contracts which currently hinder non-traditional business's ability to obtain financing.

Networking and Information Sharing Needs. The need for developing small business support organizations or networks was mentioned by several of the task forces. This need is particularly crucial for non-traditional small businesses. Such organizations could assist newcomers in identification of viable structures and procedures, provide a forum for sharing mutual problems and solutions, and act as representatives in traditional business, political and social arenas.

Non-traditional small businesses are hindered by the public's stereotyped impressions of their activities and business attitudes. These stereotypes limit creation and growth of non-traditional small businesses. One of the reasons non-traditional small businesses continue to be labelled as disjointed, high-risk and under-productive is that they have not engaged in a systematic and thorough effort to educate the traditional business community, government and the general public to the contrary. Effective public education would de-mystify non-traditional small business activities, emphasize their contributions to their communities, and also attract new business opportunities and employees.
1. There is a need for networking and information sharing among non-traditional small businesses with regard to:

(a) business structures (formal and informal);
(b) operating procedures; and
(c) specific products and services.

2. There is a need for a statewide non-traditional small business organization to conduct public education with regard to:

(a) the costs and benefits of non-traditional businesses as revealed by social accounting techniques; and
(b) the contribution of non-traditional business to employment and productivity.

3. There is a need to identify the social, business and political contacts which could facilitate non-traditional small businesses' access to traditional business networks and organizations and reduce problems of denial of "business civil rights."

Financing Needs. Many non-traditional small businesses have been excluded from transactions with the financial community. For example, an organization cannot get a loan or a contract through the SBA if it is a non-profit corporation, no matter how business-like its operations are. Non-agricultural cooperatives were "unbankable" before the Consumer Coop Bank was created. Lenders tend not to distinguish between unconventionality and risk. The Task Force felt strongly that non-traditional small businesses had major needs in the finance area.

1. There is a need to institutionalize credit evaluation criteria to correspond with the finances of non-traditional businesses. Such criteria would help financial institutions to understand financial records of non-profits, cooperatives and collectives and the applications for financing that they submit.

2. There is a need to change the regulatory climate for financial institutions in order to allow or encourage them to conduct business with small businesses in officially-encouraged programs of socially responsible lending.

3. There is a need to investigate how the Federal Community Reinvestment Act might be utilized and supplemented at the State level to make socially responsible lending and investment more attractive.
4. There is a need for soundly-based, non-traditional financial institutions to service various types of non-traditional small business.

5. In order to make private financing more available, there is a need to spread the risks on lending to non-traditional small businesses and perhaps create a secondary market for non-traditional small business obligations through new fiscal intermediaries.

F. RESOURCES AND SUPPORT FOR NON-TRADITIONAL SMALL BUSINESSES

There are striking differences in the sources of both initial capital and operating revenues between workplace oriented businesses and neighborhood economic enterprises. Personal savings and loans from friends and family are the primary sources of initial capital for workplace oriented ventures, just as they are for more traditional businesses. Revenues are derived from sales of goods and services on the open market, often in established, highly competitive fields, food stores, packaging, printing, medical services and construction. After a period of operation, several of the businesses interviewed had obtained short-term loans from banks and also had obtained credit from suppliers. Long-term debt is more difficult to obtain.

On the other hand, neighborhood economic ventures, especially those organized as cooperatives and non-profit corporations have used donated funds to start operations and have had difficulty in obtaining loans from banks, even after successful operations. Both short- and long-term debt is extremely hard to obtain. Government contracts provide the source of much of the operating revenues for many neighborhood economic ventures. These contracts can include direct fee for service transactions, reimbursements for services or "grants" in exchange for specified activities. All of these revenue sources are difficult to translate into a basis for private loans for facilities, equipment or working capital. Neighborhood entrepreneurs are rarely able to use CETA training revenue, for example, as the basis for a loan. To the extent that neighborhood enterprises also generate revenue from sales to the public, they are also able to seek loan capital, if but usually only if, their corporate structure appears conventional.

Public sources of capital for neighborhood economic ventures are important. Neighborhood development grants of
various sorts, from HUD and EDA, administrative funds from the Community Services Administration and CETA demonstration contracts all have assisted the growth of such ventures. Continued progress for neighborhood economic ventures depends on combining such donations and contracts with a removal of the legal and operational road blocks which we have described above.

Non-financial resources for the businesses we have described are available from a variety of sources, many of which are organizations which are relatively new and not well established. Efforts to establish statewide or regional information clearinghouses and support networks are in their infancy. While users of such organizations can and should be expected to bear the costs of their services in the long run, short-term public support toward their establishment may be warranted. The basis for providing such support should be the benefits to the public as a whole from the existence of a sector of non-traditional businesses.

Our recommendations to achieve the changes necessary to enhance the viability of both types of non-traditional small businesses are set forth in Appendix 1.
PART II

PRINCIPAL RECOMMENDATIONS OF THE

URBAN SMALL BUSINESS EMPLOYMENT PROJECT

The principal recommendations of the Urban Small Business Employment Project were developed by an ad hoc State review panel from the complete set of recommendations submitted by the Project's Task Forces (see Appendix 1). The reviewers represented the staffs of the Employment Development Department, the Office of Planning and Research, the Department of Economic and Business Development, the Department of Industrial Relations, the Senate Select Committee on Small Business, the Assembly Labor Committee, Senator Bill Greene and Assemblywoman Maxine Waters.

The reviewers developed their recommendations based on the following criteria:

1. Reduction of governmental role in private business.

2. Avoidance of new State expenditures or loss of revenue.

3. Encouragement of local or private initiatives as alternatives to governmental action.

4. Promotion of governmental efficiency and optimal use of existing resources.

5. Targeting to promote small business growth.

6. Political feasibility - broad legislative acceptability.

Adoption and implementation of these Principal Recommendations would, in the opinion of the review panel, significantly better the environment and prospects for small businesses in California. The text of each Principal Recommendation and a brief comment are set forth below.
A. CAPITAL ACCESS RECOMMENDATIONS

Principal Recommendation 1:
Explore the potential for prudent investment of
public pension fund assets in support of smaller
businesses through small business investment pools,
mortgage pools, long term leasing of real estate and
other debt and equity participation intermediaries.

Implementation of this recommendation could dramatically
increase the potential supply of capital available to small
businesses. The effects range from a richer larger venture
capital industry to expanded ability to market the guaranteed
portion of Small Business Administration loans. Full
implementation could require legislation to broaden the
investment authority of the trustees of the public investment
funds. The Governor's Public Investment Task Force is
preparing detailed proposals to encourage small business
investments by public pension funds.

Principal Recommendation 2:
The Superintendent of Banking should
administratively determine that a bank loan to a
small business should be "classified" by examiners
and charged against the bank's reserves if the loan
is adequately collateralized and not in default, and
should encourage federal banking officials to follow
suit.

"Classification" of a loan by a bank examiner acts as a
charge against the capital of a bank and reduces its lending
capacity. The Capital Access Task Force found that bankers
believe that small business loans are likely to be classified
even if they are in no danger of default. Adoption of this
recommendation and dissemination of information regarding its
adoption would encourage bank lending to small businesses at
no cost to the State.

Principal Recommendation 3:
Institute small business lending and investment
internships to train, season and place small
business financial officers in urban lending
institutions in order to provide special attention
to the needs of minority- and women-owned small
businesses.

The need for highly skilled small business loan officers in
urban financial institutions was strongly expressed by the
Capital Access Task Force, and supported by the reviewing panel. This recommendation addresses that need directly. The panel recommended that the role of the State be limited, however, to sponsorship and coordination of an internship program, with the major resources, i.e., salaries and training costs, to be supplied by participating private financial institutions and institutions of higher education.

B. TAXATION, REGULATION AND ASSISTANCE RECOMMENDATIONS

Principal Recommendation 4: The State should adopt a progressive state corporate net income tax to eliminate the current inadvertent statutory impact favoring large businesses which results from a higher effective State tax rate on small businesses, after computation of federal taxable income.

Because Federal corporation taxes are now progressive, California's flat 9.6% corporate net income tax results in an unequal State tax burden. This burden is heaviest on small businesses which most depend on retained earnings as a source of expansion capital. By reducing the statutory State tax rate to 6.7% for businesses with net income under $25,000 and raising it, in steps, to 10% for businesses with net incomes over $100,000, the effective State tax rate could be equalized at 5.68% for businesses of all sizes. This change would result in no net loss of revenue to the State, while increasing the availability of capital for reinvestment in smaller businesses.

Principal Recommendation 5: The Bank and Corporation Tax Law should be amended to permit a corporation to carry forward for seven years up to $10,000 in net operating losses per year for each of the first four years after commencement of business.

A bill (A.B. 2012) permitting businesses to carry forward net operating losses was passed by both houses of the Legislature in the 1980 term, but was vetoed by the Governor because of technical, drafting inconsistencies and because of the significant impact on State revenues. The review panel modified the Task Force's Recommendation on this subject, based on a belief that a bill with limited deductions, available only to new businesses would achieve the primary goal of making it more attractive to start a business while standing a better chance of enactment.
Principal Recommendation 6:
The State should appropriate or administratively allocate funds sufficient to match federal Small Business Administration funds earmarked to California for the purpose of creating small business development centers attached to State University campuses and administered in conjunction with the Office of Small Business Development.

The Small Business Development Center program has been widely acclaimed as an effective and useful way to strengthen small business management skills. Pilot programs in California bear out these comments. The State should make full use of the 50% matching funds offered by the SBA to activate this program. The Office of Small Business Development has attempted to reallocate existing funds in a way which will satisfy the SBA requirements, but funds specifically designated for the program should be found.

Principal Recommendation 7:
Because small businesses are more affected than large businesses by delays in payment for goods and services, the State should speed payment to suppliers, especially small businesses, and, to encourage this result, all State agencies should be required to pay interest at the prime rate on all accounts which remain unpaid 45 days from the date of invoice, payable from the budget of the accounting entity which placed the order.

The review panel supported this method of providing a budgetary incentive for speedier payment of State obligations. In addition, the panel supported proposals to permit and encourage the State's agencies to obtain prompt payment discounts from suppliers.

Principal Recommendation 8:
In order to enable small businesses to compete in state procurement on a more equal basis with large businesses, the State should eliminate the reference vendor procedure from its procurement operations for all products and services.

The basis for use of the reference vendor procedure (mandatory notification of a specified seller, usually a large business, of State procurements for any of a specified list of products) will be reduced by the publication of the State Register, which will notify a larger number of potential vendors of forthcoming contracts.
Principal Recommendation 9:
The State should forego taxation of capital gains resulting from investments in job producing small businesses, if the period for which the investment is held exceeds five years.

The reviewing panel preferred this formulation of a capital gains initiative to that proposed by the Task Force (compare Recommendation 4, page 104, Appendix 1) because the incentive effects would be focused more sharply on job producing small businesses at less cost to the State.

C. EDUCATION, TRAINING AND TECHNICAL ASSISTANCE

Principal Recommendation 10:
A. The Department of Education should encourage secondary school systems to provide their students with a basic classroom orientation to ownership, operation and management of small businesses as part of the standard curriculum, and to include such orientation in career and vocational counseling.

B. The State's Department of Education should urge school districts which operate work experience programs to increase the relative number of students placed in small businesses as compared to larger businesses.

C. Vocational education students at the secondary level who have entrepreneurial expectations should be offered expanded opportunity to participate as trainees in businesses which provide goods and services to the public and which are sponsored by secondary schools and/or community colleges, community-based organizations or Junior Achievement programs.

The review panel noted that this set of recommendations was directed principally at local school districts. Nevertheless, the State's leadership in providing direction and information could materially assist in attaining local decisions to implement business ownership education options. The panel modified part C of the Task Force recommendation to emphasize its support of the operation of school-sponsored youth enterprises.
Principal Recommendation II:
A. Each post-secondary educational institution which conducts vocational education programs, including Regional Occupation Centers/Programs, community colleges and adult education systems, should offer entrepreneurship skills education and link entrepreneurial education to specific vocational skills when appropriate.

B. Post-secondary institutions should provide vocational education students with the opportunity to observe and to practice entrepreneurial skills through structured contact with self-employed people in the community.

C. Post-secondary education institutions should include small business owners as mandatory participants in their vocational advisory council structure.

D. As part of each course of instruction which graduates significant numbers of potential business owners, post-secondary educational institutions should provide small business management training which reflects the specific needs of the particular industry.

E. Post-secondary education institutions should seek to coordinate small business/entrepreneurial education with opportunities for students seeking to go into business to obtain specific technical assistance and to obtain preferential consideration for loans from participating lending institutions.

F. Entrepreneurial and business skills programs should be extended into apprenticeship training and professional school curricula (e.g., engineering, medicine, etc.)

The review panel viewed this set of recommendations as the most important of the educational recommendations because of the potential over time for significantly changing the level of skills with which business owners begin operations. Little, if any, legislation would be required to implement these recommendations. However, a strong state-level effort to spur the local innovations would be required. State level activities might include:

informational services directed at statewide and local educational systems, jointly conducted by the Department of Education, Employment Development
Department and Economic and Business Development, detailing the needs for and benefits of business ownership education;

creation of model program materials;

facilitation of demonstration entrepreneurial education programs through incentive grants;

coordination with business groups to increase business involvement at the local level.

The reviewers supported an entrepreneurship educational strategy using a competency-based approach, conducted in settings that are fully commensurate with the time and locational needs of potential entrepreneurs, who are often employed full time.

Principal Recommendation 12:
The State should conduct an interdepartmental study to determine (a) the extent to which research on entrepreneurial and small business is conducted by public educational institutions in the State, the location of such research and the subjects covered in order to provide a basis for coordinating small business research, and (b) the feasibility of providing, on a coordinated statewide basis, entrepreneurship and small business research, curricula design and data to institutions conducting instruction in small business subjects.

D. COMMERCIAL AND INDUSTRIAL REVITALIZATION

Principal Recommendation 13:
Although the separate responsibilities of existing offices may be consistent with conduct of an urban revitalization strategy, the State should designate, authorize and fund a single office to coordinate the implementation of State revitalization policy, involving informational, capital and human resource programs, because lack of such a specifically authorized and funded coordinative function will result in a fragmented and ineffectual approach to urban revitalization.

This recommendation could be initially implemented by an ongoing interdepartmental team, in a manner similar to that suggested by the Ad Hoc Task Force on Plant Closures in its December 1980 Report: Such a team would be responsible for
marshalling and coordinating available resources to maximize the effectiveness of local revitalization activities. This ongoing interdepartmental effort could include plant closure responsibilities as well as responses to less dramatic needs of declining areas.

Principal Recommendation 14:
The State should enact a program to designate certain small neighborhood commercial areas or urban industrial areas which meet both local and State economic criteria, as "enterprise zones" for the purpose of providing a targeting mechanism for State financial incentives and technical assistance programs.

Although initially split regarding the concept of enterprise zones, the review panel supports this recommendation on the premise that designation of such zones by local governments, under guidelines established at the State level, would permit more efficient use of State resources for revitalization. Designation of enterprise zones would be a targeting device for State programs, especially if the responsibilities of the interdepartmental team suggested under Recommendation 13, above, were linked to the designations. Any initiative to establish an enterprise zone program should be carefully and selectively coordinated with Federal enterprise zone initiatives.

Principal Recommendation 15:
To the extent permitted by federal law, the State should require disclosure of small business lending information in excess of that required by the Federal Community Reinvestment Act to help to ensure that adequate responsibility is taken by the State's financial institutions for commercial and industrial revitalization.

At little or no cost to lending institutions, who already assemble, but do not disseminate information on the location and amounts of small business loans, this information could be made available to determine if lending shortfalls and the potential for more aggressive lending exist. Such information would be particularly appropriate for discussion when institutions seek to merge or extend branching and for consideration of applications to form new banks.
Principal Recommendation 16:
The State Industrial Development Financing Advisory Commission should be authorized and directed to create policy guidelines for local bond authorities which, if followed, would result in integrating local industrial revenue bond programs with other aspects of small business revitalization policy and programs.

The new Industrial Revenue Bond Act (A.B. 74) created authority for city and county governments to issue industrial revenue bonds, subject to approval by the State Bond Commission, provided certain standards of public benefit are met. The review panel recommended that one of the major criteria for evaluating public benefit be the extent of integration of a proposed bond with industrial revitalization objectives. It also recommended that as part of the coordinated State approach to revitalization issues, the State should make available bond packaging assistance to local bond authorities which are engaged in revitalization programs.

E. NON-TRADITIONAL SMALL BUSINESSES

Principal Recommendation 17:
The Legislature should commission a study of statutes affecting the incorporation and operation of cooperative and employee-owned businesses and, based on such study, amend the relevant statutes to encourage growth of such businesses.

Representatives of employee-owned and managed businesses reported difficulties in adapting the Corporation Law and the Securities Act to the special needs of their businesses. Lack of organizational models and statutorily sanctioned modes of operation have proved to be significant deterrents to formation of viable non-traditional businesses.

Principal Recommendation 18:
Because partially subsidized employment by non-traditional small businesses has demonstrated potential to bring otherwise intractably unemployed persons into the labor force, reduce the net expense of transfer payment support, e.g., welfare, and provide employees with marketable skills, the State should encourage creation of such businesses through appropriate financial and technical support and through development of a program to identify and to utilize welfare and other transfer payment savings to underwrite ongoing partial-wage reimbursement for employees of such businesses.
This recommendation is based on research undertaken by the UCLA Urban Innovations Group which described operations of supported work small businesses. The concept is supported by a report summarizing the costs and benefits of supported work projects included in Appendix 3. Supported work businesses offer a way to provide both income and job skills, reduce the level of expected criminal activity of unemployed groups, and provide a realistic transition to private sector employment for hard core unemployed persons at a cost which is less than the long term cost of welfare and other transfer payments, which merely provide sustenance.
PART III

SUMMARIES OF SMALL BUSINESS RESEARCH

In order to provide a sound informational basis for its recommendations, the Project sponsored a series of research surveys, case studies and analyses. The results of these research efforts are summarized in this Part III.

The research was comprised of the following components:

Review and analysis of data on small business, especially data compiled by the California Employment Development Department, emphasizing identification of firms and sectors responsible for creation of new employment.

A limited scale survey of firms in the San Francisco Bay Area designed to elicit the experiences of small business formation and growth, the problems encountered and the responses to problems.

Analysis and case studies of California small businesses which are non-investor owned, which demonstrate novel means of management, or which have non-traditional business goals.

A survey of scholarly and popular literature on major topics concerning or affecting the small business sector of the economy.

Follow-up research on businesses operated as supported work programs for hard-to-employ populations was also commissioned, based on the findings of the Non-Traditional Small Business Task Force. A summary of that paper is also included.
SMALL BUSINESS AND EMPLOYMENT GROWTH IN CALIFORNIA

Institute of Urban and Regional Development
University of California, Berkeley.

A healthy economy should meet people's legitimate aspirations to work in stable and rewarding jobs. Maintaining existing employment and creating opportunities for new entrants to the labor market are therefore among the highest public priorities of public policy. Federal, State, and local governments all attempt to support employment generation in various ways. These diverse efforts range from macroeconomic policy at the Federal level to subsidies by local governments intended to attract new businesses.

Up to quite recently, the central focus of employment generation policy has been the large business. Whether implicitly or explicitly, economic policy has emphasized large firms, which have grown in relative importance and now dominate the national economy. The work of David Birch, however, challenges accepted ideas in an important respect, namely, job generation. His analysis of a very large data set compiled by Dun & Bradstreet suggests that small firms are responsible for a disproportionate amount of all new employment that is created. According to Birch, firms with twenty or fewer employees accounted for 66% of net employment growth between 1969 and 1976.

If Birch is correct—and he has been challenged—these findings are profoundly important. Policies designed to support job generation take on new forms when their primary target is the small firm. In macroeconomic policy, the consequences of monetary anti-inflation measures that work primarily through restrictions on credit and capital availability fall heavily on the critical element for long-term economic dynamics in the economy. At State and local levels, the questions of whether to attempt to attract large businesses or to stimulate local innovation takes on new meaning. How to support job generation in small business is certainly not clear.

This study is a preliminary attempt to find out how and where employment is generated. It uses a completely different data source from that employed by Birch, and therefore is a partial test of his findings.

The research utilized data from the California State Employment Development Department (EDD). These data allow us to track the employment record of every firm in the State that participated in the unemployment insurance system between 1975 and 1979. Thus, we can see specifically where employment was created or lost. The limited time and money available for the study, however, and problems with the huge data set (some 750,000 forms, in all) make this a preliminary analysis. Most of our work has been done on a sample of 25,071 firms over the period 1975 through 1979 drawn randomly from the complete data set. For this reason, and because of limitations in the data themselves, the study findings should be regarded with caution.

The data themselves do not always distinguish between new firms and transfers of ownership. Nonetheless, several important findings emerge:

1. Small business plays a major role in the State's economy
   - Half of all the State's businesses employ less than four employees.
   - Ninety-eight percent of the State's businesses have less than 100 employees.
   - Over one-half of total employment occurs in businesses with less than 100 employees.

2. Small business, defined as 100 employees or less, includes virtually all businesses.
   - Policies and programs directed toward small business without further distinction will apply to virtually every firm in the State.
   - Policies and programs for specific purposes will be expensive and not cost-effective if they are broadly inclusive, while their real targets comprise only a small fraction of small businesses.

3. Small businesses appear to be major generators of new employment in the State.
   - Sample data from EDD support David Birch's contention that small businesses create much of the net new employment.
   - Over the 1976-1979 period, sample firms with less than twenty employees accounted for 56% of net employment added.
Among manufacturing firms, somewhat larger businesses are major job generators. About 43% of net added jobs in the manufacturing sector occurred in firms of less than 100 employees.

Firms entering the sample for the first time contributed more added employment than those in existence throughout the period. Small firms were predominant employment generators in both groups.

Although small businesses dominate job generation, much of the actual creation of jobs is concentrated in relatively few firms and over short time periods.

In a sample cohort of entering firms, most of the added employment was created in the first two years.

Among a group of very small (zero to nine employees) entering firms, most subsequent employment growth was concentrated in about 13% that grew rapidly. Twice as many gross new jobs as net were needed to offset job losses as firms disappeared.

Study of the employment dynamics in a cohort of firms of varying initial sizes that entered the EDD records in a given quarter expands our understanding of the complexity of job generation. While small firms are revealed as strongly dominating the creation of new jobs, their impact is uneven in time and concentrated within the cohort of firms. Most net new employment in the cohort sample was created early — within the first two years. Most net new employment was concentrated in the 13% of firms that grew relatively rapidly.

Much more analysis is needed to test these preliminary conclusions. If they are correct, the implications for policy are disturbing. Small business constitutes the overwhelming majority of all businesses. Yet, only a very small proportion of small businesses appear to be strong net employment generators, and those only for relatively short periods. Measures aimed at all businesses are likely to be extremely costly. By definition, only a small proportion of such expense will reach the firms that actually grow.

Cost-effective policies should target firms that are probable growth sources. But these are the hardest to identify, since they are most similar to those that also have the highest probability of failure. Measures to sustain and encourage the formation and growth of small businesses are clearly in the State's economic and social interest. However, without some means of focusing resources on potentially successful firms, the cost may be unacceptable.
The World of Small Business:
A Summary of California Case Studies

Institute of Urban and Regional Development
University of California, Berkeley

A research group surveyed 28 small businesses in the Bay Area. Although other surveys of small businesses have been done, apparently none had focused on California. The interview questions were structured to gain both qualitative and quantitative information on a range of topics, including the business environment, entrepreneurship, finance capital, labor, location and physical facilities, other private sector costs, and the effects of public sector taxation and regulation.

The study looked at a small number of small firms across economic sectors rather than attempt a comprehensive and statistically verifiable analysis. See attached table of firm characteristics. The principal findings are as follows:

1. The business environment of the sampled firms was quite turbulent, subject to seasonal, cyclical, spatial, and sectoral fluctuations of substantial magnitude. Particularly damaging were setbacks associated with rising costs, recession-related declines in sales, and market saturation at later stages of the product cycle. Many of the small businesses operated in markets dominated by large firms or depended on a few major suppliers or customers. These firms were quite vulnerable to changes in the business behavior of such larger firms. The strategies most often used by the small firms to deal with business environment and competitive problems included branching, product or service diversification and product differentiation.

2. All of the entrepreneurs in the study were white males. Almost all of them had gained experience in the same product line—through families, friends, or previous jobs in management, sales, engineering, or production—before beginning or buying into their current operation. A majority of the firms were closely-held corporations. The attitude of the entrepreneurs toward continued growth varied from consciously choosing to remain small to pursuing vigorous expansion plans. Innovativeness emerged mainly in product diversification and not in changes in production techniques.
3. **Finance capital posed a major problem for the firms.** Entrepreneurs with advanced business education tended to be more aggressive about expansion and knowledgeable about contemporary business practice. Overwhelmingly, those interviewed cited the difficulties in procuring short and long-term finance as the major internal factor hampering expansion, frustrating their ability to ride out cyclical, seasonal, and sectoral changes. Personal resources provided the sole or major source of initial capitalization. Only those firms with special connections or saleable assets seemed able to secure bank credit. Supplier credit was used by one-third of the businesses with varying degrees of satisfaction. Cash flow problems were severe for over two-thirds of the businesses in the sample. Scarcity of longer-term finance and dependence on retained earnings lead small businesses to be undercapitalized on the whole.

4. Neither shortages of skilled and unskilled labor, nor turnover rates posed major problems for the majority of the firms. A surprisingly high incidence of skilled jobs and full-time work characterized the sample. Occupational segregation by race was apparent in at least half the cases, while segregation by sex was even higher. Wage levels were not generally below five dollars an hour and were not frequently cited as a deterrent to employment expansion. Unions were present in less than one-third of the firms. Only firms in the manufacturing sector expressed strong opposition to unionization.

5. The firms had located in the Bay Area because their entrepreneurs live here, although quite a few had changed their business location within the area. Market access, adequate space, and access to transportation links appeared to be the most important determinants of present locations. Over two-thirds of the firms leased their space. No clear advantages emerged to buying over leasing across the sample—many firms in both categories were hard-hit by the current level of land and building prices.

6. Other factors mentioned by certain firms as problems included materials, insurance, and security. However, neither taxation nor regulation seemed to be particularly onerous for the firms in the sample. Although a number of firms complained about a single regulation, or an aspect of a particular tax (often this was the paperwork involved rather than the money amount), it was generally found that tax and regulatory problems caused considerably less difficulties than business environment or capital access issues.
NON-TRADITIONAL SMALL BUSINESS IN CALIFORNIA:
Problems and Prospects
Urban Innovations Group,
School of Architecture and Urban Planning
University of California, Los Angeles

As part of the California Urban Small Business Project, the Urban Innovations Group undertook a six-month study of non-traditional small business in California. For purposes of the study, "non-traditional" referred to a variety of different enterprises that have grown in number in recent years -- consumer and producer cooperatives, collectives, neighborhood-based enterprises, buying clubs, worker-owned businesses, community development corporations, and non-profit workshops. Generally, an enterprise was considered non-traditional if it exhibited one or more of three characteristics: 1) direct ownership of the firm's assets by workers or consumers, 2) participation by workers or consumers in the management of the enterprise, and 3) an explicit commitment to hiring and training people who have encountered discrimination and other difficulties in the labor market -- minorities, women, youth, elderly, the handicapped, ex-offenders, etc.

The study had three main objectives. First, it sought to describe the status of non-traditional small business (NTSB) in California, presenting some general statistical information gathered from a variety of sources. Second, by conducting 14 case studies, it aimed to illustrate the major difficulties encountered by NTSB in such areas as organization and management, finance, employment and training. Third, on the basis of findings from the case studies as well as a brief review of activities in other states, it sought to recommend policies for consideration in California to support NTSB and expand its employment potential.

In considering the findings, one should bear in mind that they are not based on a statistically valid survey. Data are presently inadequate for such a survey, and consequently, the study's findings should be viewed cautiously.
Major findings are as follows:

1. It is difficult to determine how many non-traditional small businesses currently operate in California. There are no centralized sources of data that distinguish ownership or management arrangements in such a way that worker-owned or worker-managed firms can be readily identified. From a variety of sources, the study calculated an estimate of the minimum number of different types of NTSBs operating in the State. This calculation included 155 consumer co-ops, 337 co-op credit unions, 47 collectives and worker-owned enterprises, 45 buying clubs, and 56 community development corporations. Unaccounted for is a substantial number of non-profit organizations that are concerned with hiring and training hard-to-employ people.

2. NTSBs operate in most of the same sectors as conventional small businesses, including light manufacturing and construction. Generally the businesses interviewed displayed a clear understanding of their products and how to market them. Most, rather than suffering from inadequate demand, were concerned about how to expand to meet demand. Primary factors inhibiting expansion were concerns about the effects of growth on worker-ownership and participation and inability to obtain long-term financing.

3. Except for those enterprises formally organized as consumer cooperatives, the legal provisions for worker-ownership were nebulous and often very informal. California presently has no straightforward procedures for incorporating as a worker-owned corporation or producer cooperative. Consequently, the legal claims of worker-owners on the assets and profits of their businesses are ambiguous and possibly in jeopardy.

4. All of the NTSBs interviewed recounted a turbulent history of developing workable systems of democratic management. Almost all were poorly informed about various approaches and possible problems.

5. Among those NTSBs that had adopted conventional corporate structures and therefore could exhibit the appearance of a conventional firm, financial problems closely resembled those of small business generally -- limited access to short-term working capital from institutional lenders, almost no access to long-term debt or equity capital other than from personal savings and friends, and minor though annoying problems with obtaining credit from suppliers. Among NTSBs that depart more formally or openly from conventional ownership arrangements, financial problems are more severe. For such firms, assistance from institutional
lenders is very difficult to obtain. Similarly, non-profit organizations experience serious difficulties in obtaining both short-term and long-term capital. Their problems are further compounded by the fact that future income from government grants and contracts is not assignable as collateral for loans.

6. Among NTSBs that are wholly self-supporting from the sale of goods and services and that differ from conventional firms only in terms of ownership and management arrangements, there is no evidence that they are employing greater numbers of minorities or other hard-to-employ people. Women, however, do appear to figure more prominently as owners and managers in NTSB. Among more socially-oriented NTSBs that have explicit objectives for hiring and training the hard-to-employ, the record with minorities, the handicapped, ex-offenders, and others is much better -- indeed one might say impressive. Most successful among those interviewed are two "supported work" programs that integrated training with work experience in producing goods and services that generated income for the organizations.

7. A striking feature of many NTSBs is their isolation from other NTSBs and from any agency or institution that might offer technical assistance with beginning and operating worker-owned and worker-managed businesses. One explanation for this isolation is that there are currently few sources of technical assistance sensitive to the unique objectives and concerns of NTSB. Even the business development offices of CDCs are poorly informed about alternatives and remain suspicious of cooperatives and other arrangements for worker-ownership and participation.

8. A few other states -- Massachusetts, Michigan, and Wisconsin -- have begun efforts to support NTSB, providing investment capital and technical assistance. However, to date these are modest efforts and, in at least one instance, subject to considerable political bickering. Perhaps two of the most interesting models for community development and support for NTSB are provided by the Southshore Bank in Chicago and the Department of Cooperatives and Co-op Development in Saskatchewan, Canada.
URBAN SMALL BUSINESS DEVELOPMENT REPORT: A Literature Summary and Bibliography

Graduate School of Administration
University of California, Riverside

The survey covered Federal and California State government publications, private studies funded by the government, and periodicals. After developing appropriate key words and phrases, the search was conducted using various indexes both manually and in conjunction with the on-campus Computer Literature Search Service at the University of California, Riverside.

California State publications dealing with small business are far less extensive than Federal materials. Although traditional small business problems, such as taxation, over-regulation, excess paperwork are covered, there is a lack of systematic study of social and economic impacts of government policy on small business in specific geographic areas. Such information could have a positive impact on job creation.

Nature of the California Economy

California's economy has been called the world's most advanced industrial economy and has sometimes been characterized as "post industrial". California's economy is heavily service oriented with over half of its people employed in the service industries.

Small business in California plays a very important part and possibly is even at the forefront of California's technologically-oriented industries. This is evidenced by the fact that California has a greater proportion of small firms in these high technology industries than the nation as a whole.

The make-up of small business in California is similar to the United States when compared on the basis of the number of firms in each industry, employee size-class, and the number of persons employed within that size of firms. However, when looking at California's three largest SMSA's one sees that the economics of these SMSA's differ based on the percentage of employees in selected industries from one SMSA to the next. Generally, San Diego and San Francisco-Oakland SMSA's are more service oriented while the Los Angeles-Long Beach SMSA tends to be more manufacturing oriented.
Access to Capital

Small businesses, like all businesses, have two outside sources of capital, debt financing and equity financing. However, the availability of both of these sources has decreased to the point that small firms must rely heavily on retained earnings for any capital expansion.

In general, the reasons for small business problems in gaining access to capital are as follows:

1. A public policy that tilts sharply toward encouraging consumption and discouraging savings and investment.
2. Savings have gravitated toward larger institutions that are less likely to invest those savings in smaller and new businesses.
3. Well-intentioned efforts to protect investors which inadvertently places small businesses at a disadvantage in competing for available funds.
4. Attrition and concentration in the network of financial institutions and firms that have served our economic needs well by mobilizing capital.

There have been numerous recommendations to alleviate the capital problems of small business. There is a general consensus that a reduction or deferral of capital gains taxes would be an effective way of providing the incentives to attract investment in the small business sector.

Taxation

Generally the current taxing system impacts on the small business in the following ways:

1. It discriminates in favor of big business because it does not permit small business to retain or accumulate the capital necessary for its operating and expansion needs.
2. It creates a bias against small business because of the difficulties encountered in understanding and complying with its complexities.
3. It lacks incentives to attract private investment capital to the small business sector.
4. It increases the difficulties encountered by the operator of a small business in developing some sort of retirement security.

5. It imposes inequitable estate tax burdens on the family of a deceased small business operator.

6. It discourages small business independence because it penalizes the sale of a business to independent operators but encourages mergers with larger enterprises.

In response to increasing demands for tax relief for small business, Congress, in 1979, enacted a new corporate income tax which contains a graduated tax rate on net income levels under $100,000. Although this is a step in the right direction, more reform is needed, especially regarding capital gains taxes.

The State of California imposes a flat 9.6% tax rate on corporate net income. However, since state corporate income taxes are deductible for purposes of computing Federal taxable income, the effective California tax rate is actually "regressive" in nature. It produces a bias in favor of the large business.

**Government Regulations as a Barrier to the Growth of Small Business**

Government regulation is an important small business problem. Only inflation and taxes are cited more often by small firms as their single most important problem. Moreover, regulation affecting small business is on the increase. In the past ten years, the budgetary expenditures for the 56 agencies having major regulatory functions increased 500 percent. Often the small firms may have to comply with similar regulation from more than one agency or may be subject to contradictory regulation.

Regulation has proven to be disproportionately burdensome to small firms. This is partially due to the uniformity with which regulations are applied to both large and small business, but small business has less volume over which to spread regulatory costs.

Moreover, regulation poses three problems for small firms that are less likely to confront large firms. They are: (1) discovering regulation, (2) understanding regulation, and (3) absorbing regulatory costs on single products or small volume. The basic difficulty is for small business to comply with regulation aimed primarily at big business without the resources available to big business.
A number of approaches have been developed to lessen the burden of regulation on small business with varying results. Much of this has been in the form of exemptions or two-tier regulation for small firms. Whatever the approach used there is still considerable work to be done to free small business from excessive regulation and equalize its burden relative to larger firms.

**Paperwork**

Government places excessive burdens on business firms through its increasing requirements for information. Moreover, the burden falls heaviest on small firms which have less staff and income to absorb the cost. The rate of growth in paperwork has steadily increased over the years. Much of this recent growth in paperwork is attributable to a lack of effective controls. Even where controls exist, considerable paperwork falls outside these controls. For example, more than 50% of the forms completed by the typical small firm and two-thirds of the reporting hours are not controlled.

The most significant aspect of paperwork for the small businessman is its cost. Although government controls on the growth of paperwork have not seemed to work, the Counsel of Advocacy of the SBA has, after considerable research, developed a number of new strategies to control paperwork's burden on small business.

**Competition**

Over the years, the means of production have become increasingly concentrated in the hands of relatively fewer large firms, and as a result these large companies dominate the market place. About 2,000 companies are now responsible for fifty percent of all private production. This affects small business in one of two ways: either they become absorbed through merger, or they face competitive stress to deal with the larger resources and brand identification of large firms. The evidence suggests that once the small firm is absorbed, it becomes less innovative, less efficient, less effective and less profitable. Moreover, studies have shown that the resulting absentee owners show less concern for the health of the local community than the original small business entrepreneur.

In addition, some of the literature points out that public sector competition threatens small business survival as much as any unfair competition in the private sector.

The consensus, however, is that much work needs to be done to protect the competitive equality of small business.
Inflation

Small businessmen list inflation as the number one problem facing them today. Evidence indicates that the impacts of inflation are greater on the small firm than on larger ones. The inflationary spiral pushes the costs of materials, supplies, and wages ever upward. Unlike large firms, the competitive position in which small firms find themselves does not allow these costs to be fully passed on to their customers. This reduces the small business's already marginal financial position. Big businesses, on the other hand, are able to pass on increasing costs due to inflation in their prices and thus strengthen their financial position and dollar market share.

The government's attempts to cure inflation have also had a negative effect on small business by raising interest rates and drying up needed sources of capital. It is obvious that lessening the impact of inflation on small business requires attention to the market position of small business.

Job Generation

Small business is the major force in creating jobs in the U.S. Over one-half of all private sector jobs exist in firms with less than 100 employees and most new jobs are created by small firms. Studies at MIT have determined that about 80 percent of all new jobs are created in establishments four years old or younger. When an establishment is over four years old, it does less in the way of new job creation. Also, of all new jobs, 50 percent are created by independent, unaffiliated entrepreneurs.

Given the impact of small business on job creation, the question becomes: how do we encourage small business to create jobs? It has been argued that the most cost effective means is through small business guaranteed loan programs, such as those administered through the SBA. Figures show that the approximate cost per job through SBA loan programs is $1,300 while the cost per job through the CETA program is $8,300.

The SBA cites five reasons why stimulation of the private sector by loan programs is superior to public sector employment.

1. The stimulus involves loan funds which are repaid -- not grants which are budget outlays with no direct payback.
2. Jobs created through the private sector are more permanent than public sector jobs.

3. The impact on the budget is minimal since only the repurchase reserve (15%) appears initially as an outlay.

4. Small business is more labor intensive than big business.

5. SBA programs represent a direct injection into the economic mainstream.

Innovation

Innovation is an essential ingredient for creating jobs, controlling inflation, and for economic and social growth. Small businesses make a disproportionately large contribution to innovation. Over one-half of the scientific and technological innovations that have taken place in this century have come from small businesses. The importance of small, innovative, high technology firms cannot be over-emphasized. Studies at MIT have revealed that high technology firms increased employment at a rate of 40 percent between 1969 and 1974, that is four times the national population growth.

A study by the federal government Office of Management and Budget revealed the following findings regarding small business and innovation:

1. Firms with less than 500 employees accounted for almost one-half of the major U.S. innovations during 1953-1972.

2. The ratio of innovations to sales is about one-third greater in firms with less than 1,000 employees than those with over 1,000 employees.

3. Firms of less than 1,000 employees have a ratio of innovations to R&D employment which is approximately four times greater than firms with over 1,000 employees.

4. The cost per R&D scientist and engineer is almost twice as great in firms of over 1,000 employees versus those with less than 1,000 employees.

Managerial Effectiveness

Whenever the problems of small business are discussed, one point that is frequently heard is that small firms suffer
from managerial deficiencies. This belief, that managerial deficiencies exist in small business, is prevalent in the Federal government as evidenced by the Small Business Administration's managerial assistance programs.

However, there are some facts that indicate that the majority of small firms may actually be better managed than large firms. Tax return data for all corporations show that earnings on assets, including executive compensation, decrease at logarithmic rate with increasing size in every industry and size class. This may be attributable to higher managerial effectiveness and lower organizational costs among smaller firms.

In surveys of small business problems, it is found that small businessmen rarely cite a need for managerial assistance. Rather, they cite other problems facing them, such as unfair competition, taxation, government regulations and paperwork, and lack of access to capital.

**Urban Small Business Development**

The need for business development in urban areas is becoming more apparent if the decay of our urban areas is to be reversed. In response to this need, the Federal government has implemented the nation's first "Urban Policy". This policy puts a special emphasis on economic development in central cities through the joint efforts of numerous federal agencies in cooperation with private sector.

An example of a program that has resulted from the new urban policy is the development project being undertaken in the City of Long Beach, California. This program is intended to transform downtown Long Beach through the influx of nearly $700 million in investment funds by 1985.

In the past, government development policies were instituted on a very broad basis at a macro level. The new urban policy represents a step in the direction of implementing a more regional and specific industry development.

In the future, attempts to stimulate economic development and create jobs need to be focused on those industries that have the greatest potential for growth in areas of high unemployment. Government efforts should be directed at enlisting the resources to the private sector, especially small business because small business has the greatest capacity for job creation.
BENEFITS AND COSTS OF EXTENDED SUPPORTED WORK*

Supported work projects are businesses which produce goods or services for the public while providing either a transitional or long-term work experience geared to hard-core unemployed persons. A portion of the expenses of supported work businesses is publicly subsidized. The results of a national experiment at 15 sites involving over 10,000 persons indicate that supported work businesses are a cost-effective tool to integrate certain groups of hard-core unemployed persons into the private labor force.

The experiment used four target populations: (1) female long-term recipients of Aid to Families with Dependent Children ("AFDC"), (2) recently released ex-offenders; (3) former drug addicts; and (4) young high school dropouts, half of whom have criminal records. The experiment included both a target group and a control group. The costs used in the analysis were local supported-work program costs, central administrative costs, foregone earnings, and child care costs. The benefits were the value of program output, increased post-program earnings, reduced welfare, education, employment program and drug treatment program costs; and reduced criminal activities.

For the AFDC and former drug addict target groups clearly positive cost benefit ratios emerged. For ex-offender groups costs appeared to roughly match measured benefits and for the youth groups costs exceeded benefits, largely because of increased criminal activity of participants.

By producing and selling goods and services, supported work businesses may compete with non-subsidized businesses. The potential for subsidized firms to displace existing, unsubsidized firms and workers is small in light of the potential size of the supported worker population. Such displacement can be further minimized by careful analysis of appropriate business sectors and labor force characteristics. Supported work businesses appear to be more equitable and less likely to cause displacement than either direct or indirect, i.e., tax credit, wage subsidies for hiring hard core unemployed persons. Displacement should not be a deterrent, if it is considered in planning operating projects.

*Prepared by students at the Graduate School of Public Policy, University of California, Berkeley.*
APPENDIX 1:

LIST OF TASK FORCE RECOMMENDATIONS
RECOMMENDATIONS OF
CAPITAL ACCESS TASK FORCE

1. Authorize and encourage the public pension funds in the State to invest indirectly in smaller businesses through small business investment pools, mortgage pools, long term leasing of real estate and other debt and equity participation intermediaries.

2. Establish an umbrella agency (a) to coordinate the development finance undertakings of the State, including oversight and certification of local industrial revenue bonds, (b) to establish operational objectives for business finance programs and (c) to review and report on progress in achieving improved access to capital for small businesses.

3. Conform significant aspects of California's corporate net income tax with federal income taxation, including provision for investment tax credits, Subchapter S corporations and net operating loss carry forwards.

4. Create a user-financed, self-supporting industrial and commercial mortgage insurance agency available only to small businesses.

5. The Superintendent of Banks should actively seek to expand the number of independently owned and operated commercial banks in California based in part on consideration of the needs and convenience of small businesses for local sources of credit.

6. Require all banks in the State to disclose and to post annually the numbers and total dollar volume of commercial loans to or for small businesses on a branch-by-branch basis.

7. The Superintendent of Banking should administratively determine that no bank loan to a small business should be "classified" by examiners and charged against the bank's reserves if the loan is adequately collateralized and not in default, and should encourage federal banking officials to follow suit.
8. The Superintendent of Banking should officially encourage State banks to create, on a pilot, voluntary basis, portfolios of higher risk-higher return loans to small business borrowers.

9. Permit and encourage public retirement funds to purchase the guaranteed portion of loans to California businesses which are guaranteed by the Small Business Administration.

9. Support efforts by the State's public education institutions to link entrepreneurial training programs with lending preferences by private lending institutions for program graduates.

10. Institute small business lending and investment internships to train, season and place small business financial officers in urban lending institutions in order to provide special attention to the needs of minority- and women-owned small businesses.

11. Encourage the creation of employee stock ownership plans for the purposes of business continuation or expansion, and investigate and evaluate the establishment of a self-supporting finance agency to facilitate funding of employee stock ownership trusts.

12. Amend California Securities Law Sections 25102 E, F and H to facilitate private offerings of common stock to a limited number of individuals without registration and to permit sales of such stock in exchange for a wider array of assets.
RECOMMENDATIONS OF
TAXATION, REGULATION AND ASSISTANCE TASK FORCE

Taxation of Small Businesses

1. The State should adopt a progressive State corporate net income tax to eliminate the current bias in favor of large businesses which results from a higher effective State tax rate on small businesses after computing Federal taxable income.

2. The State should amend the Bank and Corporation Tax Law to permit a deduction in succeeding years for corporate net operating losses up to a maximum of $50,000 per year for seven years in order to remove the disincentive effects of the current tax law which inhibits investment in new small businesses which are likely to incur losses following their start-ups.

3. The State should institute a deferral of capital gains taxation on gains which are realized and which are reinvested within six months in qualifying small businesses.

4. Small businesses, as measured by their total assets, should be permitted to deduct from their California taxable income the costs of investment in plant, machinery and equipment immediately, rather than depreciating them over the estimated life of the investment, in order to aid such companies to self-finance their expansion.

5. The State should amend the Banking and Corporation Tax Law to create an analogue to the Federal Subchapter S election for small business investors.

State Regulation and Assistance

6. The Governor should designate a Small Business Advocate within the administrative branch of the State government having the expertise to represent small business, through oral and written representations, to agencies in formulating and administering regulations in ways which would take into account legitimate needs of small businesses.
The State should institute a small business research and information service, affiliated with one or more public higher education institutions, to assemble, update and disseminate data on Federal, State and local procurement opportunities for California small businesses; provide analysis and localized information with regard to export opportunities in foreign markets, especially in Mexico; and act as a clearinghouse and library for small business information to be disseminated by the Office of Business and Economic Development and its affiliates.

The State should appropriate funds sufficient to match Federal Small Business Administration funds allocated to California for the purpose of creating small business development centers attached to State University campuses and administered in conjunction with the Office of Small Business Development.

The State should institute a small business purchasing program, applying to all purchasing agencies, whereby purchases of certain goods and services, as determined by the Secretary of the State and Consumer Services Agency, shall be made only from small businesses.

Because small businesses are more affected than large businesses by delays in payments for goods and services, the State should speed payment to suppliers, especially small businesses, and, to encourage this result, all State agencies should be required to pay interest at the prime rate on all accounts which remain unpaid 45 days from the date of invoice, payable from the budget of the accounting entity which placed the order.

In order to eliminate one aspect of bias against small business in State procurement, the State should eliminate the reference vendor procedure from its procurement operations for all products and services.

The State should re-examine the need for performance bonds with regard to all procurement, including both products and construction, for which the contract price is $50,000 or less, and eliminate bonding requirements where such bonds are not absolutely essential for the protection of the fiscal integrity of the State.

The Office of Administrative Law should be directed to (a) evaluate both proposed and existing regulations and administrative procedures to determine the costs imposed on small businesses and their deterrent effects on the creation of new businesses and (b) recommend ways to minimize such costs and deterrent effects.
The State should seek to expand the availability and utilization of binding non-judicial remedies for commercial disputes.
RECOMMENDATIONS OF
EDUCATION, TRAINING AND TECHNICAL ASSISTANCE TASK FORCE

1. Post Secondary Entrepreneurship Education

A. All post secondary educational institutions (including community colleges and adult education centers) which conduct vocational education programs should offer courses to teach entrepreneurship skills and link entrepreneurial education to vocational programs when appropriate.

B. Post secondary education institutions should provide vocational education students with the opportunity to observe and to practice entrepreneurial skills through structured contact with self-employed people in the community.

C. Post secondary education institutions should include small business owners as a mandatory element of their advisory council structure to aid in creating vocational education programs.

D. For fields of study which have high rates of self-employment, post secondary educational institutions should provide small business management skills training which reflects the specific needs of the particular industry.

E. Small business/entrepreneurial education for students at post secondary education institutions should be articulated with programs providing specific technical assistance to students seeking to go into business and with structured consultation with participating local lending institutions.

F. Entrepreneurial and business skills programs should be extended as elective elements into apprenticeship training and professional school curricula (e.g., engineering, medicine, etc.).

2. Secondary Education -- Orientation to Small Business

A. The State Department of Education should encourage and assist local districts to provide their secondary
school students with a basic orientation to ownership, operation and management of small businesses in the classroom as part of the standard curriculum, and to reinforce that orientation through vocational and career counseling.

B. The State's Department of Education should assist school districts which operate work experience programs to increase the number of students placed in small entrepreneurial businesses.

C. Students in vocational education who have entrepreneurial expectations should be offered expanded opportunity to participate in school-sponsored business projects which actively operate a business, especially projects conducted jointly with community colleges, community-based organizations or Junior Achievement.

3. Small Business Educational Support

A. The State should undertake to determine, through a cooperative interdepartmental study, the extent to which entrepreneurial and small business research and technical resources are currently available at public educational institutions.

B. Existing entrepreneurship and small business research and development activities should be coordinated in order to provide curricula design, course content and small business information on a statewide basis to secondary schools, community colleges, continuing education programs and the State universities.

C. Research and development of technical resources for entrepreneurial and small business issues should be undertaken in conjunction with operation of small business development centers which would provide in the field training and technical assistance services to small businesses.

4. Small Business Development Services

A. The State, in cooperation with the higher education systems, should marshall and coordinate Federal and State research, training and technical assistance funds to establish local offices and regional centers to provide ongoing information dissemination and consultation to small businesses; such facilities should be based on the
successful demonstration project conducted at the California State University of Chico.*

B. The State should coordinate the operation of at least five regional small business development centers by local agents in economically and geographically diverse areas of the State.

C. Each regional small business development center should include a council composed of representatives of small business owners, local governments, community-based organizations, community colleges or State universities as appropriate, to encourage accountability, accessibility and flexibility of the services provided by or through the regional centers.

5. Linking Manpower and Training Programs with Small Businesses

A. By means of planning assistance, one-shot coordination grants and eligibility for State tax credits the State should actively promote linkages between local employment training programs and local reindustrialization efforts for the purpose of providing individuals who are specifically screened, trained and tested for jobs in specific smaller businesses (custom-trained labor force) as an incentive to business expansion.

B. The State, through the Employment Development Department, should subsidize costs of on-the-job training of distressed area residents which cannot be reimbursed to small businesses by CETA (High Support OJT).

C. The State should authorize and direct an interdepartmental project to provide periodic survey data on local labor supplies, migration patterns, skills assessment, and labor force training needs in categories reflecting small business needs.

D. The State, possibly through an amended Worksite Education and Training Act, should support local capability to directly contact smaller employers and provide technical assistance to employers regarding workforce utilization as a way to encourage participation in employment and training efforts.

*The Task Force emphasized that regular, pre-emergency contacts between extension agents and small business owners fosters small business stability and growth, and that a recognizable, standardized, statewide nomenclature for all extension offices is essential.
E. CETA reimbursement to small employers must be made more quickly to encourage small business participation.

F. Federal and State contracting and procurement should be coordinated with Federal on-the-job training programs to permit small businesses to participate in OJT without disallowance of necessary training-related costs.

G. The State should determine by research the extent to which customized labor force training for expanding businesses is self-supporting in terms of increased tax revenues from both business and personal taxes and savings from lower transfer payment costs (i.e., unemployment insurance, welfare).
RECOMMENDATIONS OF

COMMERCIAL AND INDUSTRIAL REVITALIZATION TASK FORCE

The Basis of Economic Revitalization

1. The primary strategy of the State with regard to revitalizing economically declining commercial and industrial areas should be to encourage localities to address quality of life issues comprehensively as the necessary precondition for the success of efforts to induce investment in new and expanding small business ventures in those areas.

Governmental Coordination -- The State's Role

2. The primary function of the State's revitalization activities should be to assist locally operated programs to integrate effectively and to use most efficiently the private sector and Federal sources which are available.

3. Although responsibilities of existing State offices may, in the aggregate, be consistent with revitalization strategy, the State should designate, authorize and fund a single office to coordinate the implementation of State revitalization policy, involving informational, capital and human resource programs, because lack of such a specifically authorized and funded coordinative function will result in a fragmented and ineffectual program.

4. The State should use coordinating grants and technical assistance to encourage local governments to integrate portion of their manpower/human resource training programs into economic development efforts which are directed at the specific needs of individual firms.

5. The State should enact a program to designate certain small neighborhood commercial areas or urban industrial areas which meet both local and State economic criteria, as "enterprise zones" for the purpose of providing a targeting mechanism for State financial incentives and technical assistance programs.

6. The California Office of Local Economic Development ("OLEO") should be provided with sufficient additional funds to provide comprehensive technical assistance services including grantsmanship, loan packaging,
long range planning and analysis, development of cooperative investment and lending relationships and other support services, to cities with designated enterprise zones and to businesses located within the zones in order to create a working revitalization program.

7. Because of the fundamental importance of active participation of associations representing merchants or industrial firms in distressed areas in the revitalization process, state assistance should be provided to localities to organize and assist such associations to become partners in local revitalization projects.

Reinvestment

8. Designation of an enterprise zone should entitle local governments, businesses, and business investors to the following financial and service programs in addition to those provided by OLED:

(a) The State's portion of the sales tax should be rebated to businesses located in enterprise zones for a specified term of years;

(b) A tax credit on personal income should be available to persons investing in businesses located in enterprise zones.

(c) First preference to loan guarantees from the State's loan loss reserve fund should be given to enterprise zone businesses.

9. The State should explore the potential for joint or coordinated activities with the Neighborhood Reinvestment Corporation in order to involve private sector financial institutions in planning and implementing commercial revitalization.

10. To the extent permitted by Federal law, the State should require disclosure of lending information in excess of that required by the Federal Community Reinvestment Act to help to ensure that adequate responsibility is taken by the State's financial institutions for commercial and industrial revitalization.
RECOMMENDATIONS OF
NON-TRADITIONAL SMALL BUSINESS TASK FORCE

1. The Legislature should initiate a comprehensive study of the effects of State corporation and securities laws on cooperative and worker-owned businesses and thereafter should amend the Corporations Code in accordance with the conclusions of the study to facilitate easier incorporation and operation of such businesses.

2. The Office of Small Business Development should employ a specialist in the area of employee ownership and cooperative workplaces to provide information services to businesses and employee groups regarding organizational alternatives and the role of State corporation and securities laws.

3. Because private small businesses which are organized for the purpose of revitalizing urban neighborhoods or employing hard-to-employ local residents, as well as for producing goods and services, have proved to be effective mechanisms to achieve public economic goals, the State's development planning and programs should (a) expand the role assigned to such businesses in policy implementation, (b) support the activities of such businesses through public procurement and capital expenditures, and (c) raise the priority given to such businesses in obtaining publicly funded developmental assistance.

4. Because publicly-funded private financing institutions, including banks, savings and loans and insurance companies, as well as widely-used public sources of financing, including the Small Business Administration do not adequately service the needs of non-traditional small businesses such as cooperative corporations, non-profit corporations, worker-owned businesses and businesses with substantial citizen participation, the State should authorize creation of a mixed public/private financial institution and give it powers to make and guarantee loans to non-traditional small business, provide equity capital to certain classes of non-traditional small businesses and provide financial technical assistance in leveraging private capital to support the development of non-traditional small businesses.
5. State policies promoting employment for hard-to-employ populations such as AFDC recipients and ex-offenders, should concentrate on developing supported work enterprises in which participants receive skill training and are also employed in production of goods and services that produce income for the enterprises.

6. The State should authorize and institutionalize secure and ongoing reimbursement, not exceeding 50% of the minimum wage, of the wage costs of supported work small business enterprises which provide employment to individuals who have chronic difficulty in securing private, unsubsidized employment.

7. The State, in collaboration with the Federal government, should develop an experimental "investment transfer" program in which welfare costs and other transfer payments saved as a result of subsidized employment are used to underwrite ongoing wage reimbursement programs for hard-to-employ populations in private supported work enterprises.

8. The State should seek to retain existing jobs in small businesses through technical assistance to employee groups attempting to purchase the firms for which they work.

9. A goal of State policy should be establishment or expansion of freestanding institutions which will provide capacity building services and technical support to new economic activity, including, but not limited to employee-owned small businesses, cooperatives, individual entrepreneurs and groups involved in local public/private business partnerships.

10. The State should establish a permanent interagency program which, in cooperation with local governments and community organizations would be directed to define and publicize to communities throughout the State opportunities to undertake social entrepreneurship initiatives such as local self-help businesses and non-traditional enterprise development.
APPENDIX 2:

LIST OF TASK FORCE MEMBERS
TASK FORCE MEMBERS

1. Access to Capital

MICHAEL A. KADENACY, Task Force Chairman. Senior Partner, Kadenacy, Menke & Albing, Attorneys, Los Angeles. Also Vice-Chair, Advisory Board to the Senate Select Committee on Small Business Enterprises; General Counsel for the Latin American Civic Association and Judge Pro Tem: Small Claims Court.

RON CARRIGAN, Director, South Central Economic Research & Development Associates, Los Angeles, an organization providing business and loan packaging assistance, industrial and commercial development coordination and revitalization activities.

DEREK C. DUNLOP, Senior Vice President, 1st State Bank of Encino. Also, Director of Encino Chamber of Commerce; Chairman, Southern California Finance Committee, Advisory Board to Senate Select Committee on Small Business.

DAVID DURHAM, Durham and Associates, San Francisco, financial consultants to small businesses.

DEREK HANSEN, President, Hansen & Associates, Inc., San Francisco, providing consulting services to government agencies on financing programs for energy, small business and economic development.

JOHN HARRINGTON, Political Coordinator, SEIU, Oakland. Also President, California Alternative Investment Task Force and Chairman, Governor's Public Investments Task Force. Former Member of Sacramento City Employees Investment Board and State Senate Select Committee on Investments.

HAP KLOPP, President, The North Face, Inc., Berkeley. Also Chairman, DAP Division of American Apparel Manufacturers Association and Guest Lecturer, Stanford University Graduate School of Business.

LAWRENCE LITVAK, Community Economics, Inc., Oakland; a non-profit consulting firm. Consultant to state and local governments on issues of financing economic development. Author of Innovations in Development Finance. Currently working on several efforts to channel more pension fund money into local development-enhancing investments.
DON MARVIN, District Director, Small Business Administration, San Francisco. Also participates in various business seminars and heads California Small Business Advisory Council.

DEAN J. MISCZYNSKI, Director of Policy and Planning Governor's Office of Planning and Research, State of California. Responsible for research and policy and proposal development, especially for urban, fiscal and development issues.

CLARENCE J. PENDLETON, Jr., President, San Diego Urban League, Inc.

THOMAS QUEEN, President, Cal Regional Small Business Development Corporation, San Francisco, a firm which guarantees loans for small businesses, minority and disadvantaged.

ANN SANTIAGO, Executive Vice President, Builders Mutual Surety, Los Angeles, an insurance company primarily involved in bonding small and minority contractors.

MICHAEL B. TEITZ, Professor of City and Regional Planning, University of California, Berkeley. Research project director.

JOHN TILLAPAUGH, Associate, Kidder, Peabody & Co., San Francisco, financial advisors. Currently involved in the Small Business Administration's guarantor program for pollution control projects.

LEONARD WEIL, President, Manufacturers Bank, Los Angeles.

Resource people:

JOHN CRETOL, Employment Development Planner, Employment Development Department, State of California. Assistant for planning and coordination of urban and rural job development; staff to EDD Economic Development Task Force; responsible for coordinating EDD job creation policy and procedures for development.

JAY JONES, Boalt Hall School of Law, University of California, Berkeley.
2. Taxation, Regulation and Assistance

GORDON BIZAR, Task Force Chairman. President, National Independent Business Alliance, Santa Monica. Also, owner of a metal fabricated parts manufacturing company and president of a publicly held financial service organization.

MARK AOAMS, Governor's Office of Planning and Research, State of California.

GEORGE BEAUBIEN, Executive Director, Mayor's Office of Small Business Assistance, Los Angeles. Assists small and minority businesses with City procurement and provides information regarding City contracts and contract awards. Also, Procurement Project Director for Small and Minority Businesses for 1984 Olympics and MBOA Executive Commissioner.

JULIAN CAMACHO, Assistant Secretary, State and Consumer Services Agency, State of California.

ARTHUR R. DANSBY, President, Bi-Plex Corporation, Los Angeles. Also, President, Black Business Association; member of the Private Industry Council, Los Angeles and the Black/Jewish Economic Coalition of Los Angeles.

ALLAN DESIN, Director of Research and Statistics, Franchise Tax Board, State of California.

STAHRL EDMUNOS, Dean, Graduate School of Administration, University of California, Riverside. Research interests include small business and regional economic development.

JOSEPH FLORES, President, Sacramento Community Development Corporation, Inc. Also, Executive Director, California Mexican American Chamber of Commerce and President, Sacramento Chamber of Commerce.

STAFFORD W. KEEGIN, Attorney, National Economic Development and Law Center, Berkeley.

H. JACK KOUJAKIAN, marketing consultant specializing in services to small businesses, San Francisco.

BARBARA A. NIXON, State Coordinator, Century Freeway Project, Department of Business and Transportation, State of California.
Resource People:

JIM CURTIS, Chief, Urban Development Unit, State CETA Office, Employment Development Department, State of California.

JIM EXUM, Director, Small Business Office, State of California.

AMY K. GLASMEIER, Institute of Urban and Regional Development, University of California, Berkeley.

3. Education, Training and Technical Assistance

ALICIA MADRID, Task Force Chairwoman, Executive Director, California Federation for Technology and Resources, Sacramento, which provides technical assistance in economic development, planning and marketing studies, loan packaging and management and organization development assistance to small businesses.

HELEN M. BALLOU, Director of Continuing Education, Napa College. Program responsibility for community education throughout district.


FRANK W. CASTINE, Retired, former Director, Manpower Programs, Los Angeles Unified School District.

PATRICIA A. COLEMAN, Chief of Program Development, Private Industry Council of Sacramento, Inc. Member of Industry Education Council of Sacramento and Sacramento Area Commerce and Trade Organization.

MARY CORNELL, Founder and President, Cornell Company, Sunnyvale, printing company.

JAMES H. CRANDALL, Coordinator, State Department of Vocational Education, State of California.

RICHARD DAVIS, Director, Center for Business and Economic Research, California State University at Chico, which conducts business feasibility studies, economic impact studies, market research and opinion surveys.
RICHARD GOEBEL, Director of Business Services, Center for Community Services, Santa Rosa. CCE is an Economic Development project providing managerial and technical assistance to small business with primary emphasis in financing.

RAYMOND R. HOLLAND, Assistant Director, Mayor's Office of Employment and Training, San Francisco. Also, legal counsel and chief of program planning and evaluation of CETA programs in San Francisco.

MAURICE S. KANE, Century Freeway Coordinator, Employment Development Department, State of California, coordinating employment and training activities dealing with small businesses.

JEFF MATHIEU, Community Development Analyst, City Of Long Beach.

LINDA MCKINNEY, Acting Director, Governor's Office for Citizen Initiative and Voluntary Action, State of California. Involved with various State level non-profit corporations and voluntary sector organizations.

JIM NICHOLSON, Special Consultant, Employment Development Department and State Department of Education, State of California. Consultant liaison between EDO and SOE to improve coordination and cooperation between the departments with special emphasis on influencing vocational education to be responsive to the job market.

BARBARA SULLIVAN, Assistant to the Chancellor, California Community Colleges, State of California. Vice President, Education Division, United Federation of Small Business.

JOHN G. TAYLOR, President, Tayko Industries, Sacramento, manufacturer of rebuilt diesel equipment.

Resource People:

JIM CURTIS, Chief, Urban Development Unit, State CETA Office, Employment Development Department, State of California.

PHILIP SHAPIRA, Institute of Urban and Regional Development, University of California, Berkeley.
4. Commercial and Industrial Revitalization

RICHARD BEYER, Task Force Chairman, Executive Vice President, Pittsburg Economic and Housing Development Corporation.

WALTER COHEN, Economic Development Coordinator, Emeryville Redevelopment Agency. Responsible for economic development activities in redevelopment project areas. Executive Director, Emeryville Economic Development Fund; member of CALED and CUED.

EARL COOPER II, Deputy Executive Director, Los Angeles Economic Development Corporation, engaged in economic development in the City of Los Angeles for small and minority firms.

A. EDWARD EVANS, Director of Economic Development, City of La Habra. Executive Director, La Habra Local Development Co., Inc.; Economic Development Administrator, LOC Consortium of Orange County Cities.


CHANNING O. JOHNSON, President, Economic Resources Corporation, Lynwood.

R.D. LOTTIE, JR., President, Pacific Coast Regional Urban Small Business Development Corporation, Los Angeles, a non-profit corporation funded by the State of California to assist small businesses in becoming successful members of the California business community.

VALERIE POPE LUDWIG, President, San Bernardino Westside Community Development Corporation engaged in industrial park and residential/commercial planned unit developments, operation of a vocational school and CETA, Manpower Programs, and solar energy/alternative energy development projects.

WILFRED L. MARSHALL, Economic Development Representative, Economic Development Administration, specializing in commercial revitalization, industrial expansion and economic development.

WES MCDANIEL, Executive Director, San Bernardino Associated Governments, coordinating planning and financial programming for county and cities in areas of population, employment, highways, transit,
airports, and air quality. Formerly City Manager, City Planning Director and Redevelopment Agency Board Member.

Resource People:

ROBERT MARR, Office of Planning and Policy Development, Employment Development Department, State of California.

KAY REYNOLDS, Deputy Director, Office of Local Economic Development, State of California.

DOUGLAS SWENSSON, Institute of Urban and Regional Development, University of California, Berkeley.

5. Non-Traditional Small Business

ROY ESCARCEGA, Task Force Chairman, Senior Vice President Urban Development Division, The East Los Angeles Community Union (TELACU), administering community development corporations' human service programs.

PETER ABRAHAMS, past Executive Director, National Training Institute for Community Economic Development, Palo Alto, an organization funded to provide training to Title VII-funded community development corporations throughout the United States.


HAL BROWN, Senior Analyst, Governor's Office of Planning and Research, State of California.

MICHAEL CLOSSON, Co-Director, New Ways to Work, Palo Alto. Founder of the Work Creation Project of New Ways to Work which provides start-up assistance to people initiating small businesses and community service organizations, with special emphasis on non-traditional enterprises.

AL OILUOIVICO, Consultant, META-WORK, Santa Cruz, an organization providing pre-loan technical assistance to inner city cooperatives in Watts, Tenderloin District, West Oakland, and East Palo Alto. Presently under contract with State Department of Consumer Affairs specializing in co-op development.
KAREN HIXSON, President, Karen Hixson and Associates, Los Angeles, a consulting firm specializing in small and disadvantaged business development, urban business and economic development and research.

GARY HOACHLANDER, Lecturer; University of California, Los Angeles; Research Director, University of California, Berkeley, teaching public finance, urban economics and policy evaluation. Directs studies for National Institute of Education on financing of vocational education.

ELEANOR HOSKINS, Executive Director, Career Planning Center, Inc., Los Angeles, a private non-profit organization. Also member of Los Angeles County PIC; California Advisory Council on Vocational Education. Consultant to organizations on issues related to women and work.

TYBIE KIRTMAN, Business Manager, Santa Barbara News and Review, a cooperative weekly newspaper. Also senior partner, Bols Bookkeeping Service and Admissions Committee member National Association of Alternative Newsweeklies.

DAVID OLSEN, President, New School for Democratic Management, San Francisco.

OSCAR G. PEREZ, Deputy Director and Director for Economic Development, Spanish Speaking Unity Council, Oakland, a Title VII-funded community development corporation.

Resource Person:

RUSS HART, Urban Development Unit, Employment Development Department, State of California.

Project Staff:

LOYD C. LEE, Project Coordinator
Attorney at law, National Economic Development and Law Center.

BARBARA BROWN, Assistant.

KAREN MOUNDAY, Assistant.