



WRITTEN STATEMENT

**BEFORE THE HOUSE COMMITTEE ON WAYS AND MEANS TAX POLICY
SUBCOMMITTEE**

HEARING ON

**“TAX REFORM AND SMALL BUSINESSES: GROWING OUR ECONOMY AND
CREATING JOBS”**

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Small Business Majority

Chairman Buchanan, Ranking Member Doggett and fellow Members of the Committee,

Thank you for inviting me to speak with you today about the new tax law and its impact on America's small businesses.

I was a long-time small business owner prior to founding Small Business Majority 12 years ago. For 13 years, I was the founder and CEO of ACI Interactive, an award-winning interactive communications company, and earlier I was the chief operating officer of a pioneering multimedia business. Following my many years of experience running small businesses, I founded Small Business Majority to create a national organization to serve as a leading advocate for America's entrepreneurs.

Small Business Majority's mission is to empower America's entrepreneurs to build a thriving and inclusive economy. We actively engage small business owners and policymakers in support of public policy solutions, and deliver information and resources to entrepreneurs that promote small business growth and drive a strong, job-creating economy. Our extensive scientific opinion polling, focus groups and economic research help us educate and inform policymakers, the media and other stakeholders about key issues impacting small businesses and freelancers, including access to capital, taxes, healthcare, retirement and critical workforce issues.

Small Business Majority has a network of 58,000 small business owners across the country, with nine offices in Washington, D.C. and seven states. We work closely with our network and with more than 1,000 local business groups to create a strong small business voice in Washington and state capitals, and deliver critical education and resources to America's job-creating entrepreneurs. Through our Entrepreneurship Program, we offer free education, tools and events to small business owners and aspiring entrepreneurs about access to responsible lending options, retirement, healthcare, wealth building tactics and more.

Through our daily interaction with small business owners and self-employed entrepreneurs we know that small businesses are not just the backbone of the American economy; we are its foundation. America's 30 million small businesses represent 99% of all employer firms and account for half of

our nation's jobs and economic output, and their creativity spurs innovation in all sectors of the economy. According to the U.S. Small Business Administration, small businesses have created two out of three new private-sector jobs since the Great Recession.¹ Private-sector job creation at small- and medium-sized businesses has outpaced the rate of large-size companies for every month of 2017, per ADP's National Employment Report.²

Despite this undeniable importance to our economic success, small businesses are consistently left behind during national policy debates. Our nation's tax system has historically benefited the wealthiest Americans and large multinational corporations at the expense of small business owners. Small Business Majority's polling found 7 in 10 small business owners believe their business is harmed when big corporations use loopholes to avoid taxes, and 85% feel the tax code unfairly benefits large corporations over small businesses.³

The newly enacted Tax Cuts and Jobs Act has done nothing to address this disparity. Indeed, we believe the law will hurt small businesses and the economy because (1) it will increase the deficit by \$1.5 trillion without giving most small business owners a significant tax break, (2) it adds more complexity and confusion and (3) fails to address corporate tax loopholes that give large businesses an unfair advantage. I will address these three issues in turn during my remarks.

The new law's tax breaks are skewed towards large corporations and a handful of wealthy pass-through entities, not Main Street small businesses

The real winners of the new tax law are large corporations and wealthy individuals, not Main Street small businesses. A priority of this legislation was to slash corporate tax rates from 35% to 21% even though only 5% of small businesses pay corporate taxes.⁴ Adding \$1.5 trillion to the deficit at a time of economic prosperity will do nothing to help small businesses, and it certainly doesn't level the playing field. It should be noted that our polling found 85% of small businesses want large corporations and wealthy Americans to pay their fair share of taxes.

Additionally, the law's treatment of pass-through entities gives the bulk of the benefit to the wealthiest business owners, rather than Main Street. New data from the Joint Committee on Taxation (JCT) reveals a whopping 44% of the new pass-through deduction (\$17.4 billion) will benefit approximately 200,000 individuals making \$1 million or more.⁵ In 2024, this will increase to \$31.6 billion.

According to the JCT report, the majority of the 2018 tax reduction benefit overall will go to the top 2.3% of pass-through firms, and by 2024 that percentage drops to one percent.⁶ By our calculations, a business owner earning \$600,000 per year (after standard and personal deductions) will save 26 times that of an owner with \$75,000 in income, despite only earning eight times more.

According to the Small Business Administration, the median income for individuals self-employed at their own incorporated businesses was \$50,347 in 2016.⁷ This statistic is important to note because most small businesses are indeed very small enterprises that bring in a modest income. According to the Tax Policy Center, less than two percent (1.7%) of all pass-through businesses, with average

¹ Small Business Administration FAQs, June 2016, https://www.sba.gov/sites/default/files/advocacy/SB-FAQ-2016_WEB.pdf

² ADP National Employment Report, January-August 2017, <http://www.adpemploymentreport.com/>

³ Small Business Majority, "Small Business Owners Want Fair Tax System Over Tax Cuts," October 2017, <http://smallbusinessmajority.org/our-research/taxes-budget-economy/small-business-owners-want-fair-tax-system-over-tax-cuts>

⁴ Brookings Institution, "Nine facts about pass-through businesses," May 2017, <https://www.brookings.edu/research/9-facts-about-pass-through-businesses/>

⁵ Joint Committee on Taxation, "Tables Related to the Federal Tax System as in Effect 2017 through 2026," April 2018, <https://www.jct.gov/publications.html?func=startdown&id=5091>

⁶ Ibid.

⁷ Small Business Administration, 2018, <https://www.sba.gov/sites/default/files/advocacy/2018-Small-Business-Profiles-US.pdf>

profits of nearly three-quarters of a million dollars, account for the majority of all pass-through income. These enterprises reaping most of the benefits of the pass-through deduction are hardly your typical Main Street small business.⁸

In addition to not providing a real tax benefit, the law will in fact hurt small businesses by making health insurance more expensive and difficult to access. Not only did Congress fail to consider bipartisan legislation last year to bolster the marketplaces, the new tax law repealed the individual mandate, which is essential to ensuring robust participation and balanced risk pools. Small businesses consistently rank the cost of healthcare as one of their top concerns. By introducing more instability and uncertainty to the healthcare marketplaces, costs will increase for the millions of small business owners, solo entrepreneurs and small business employees who rely on the individual marketplaces for health coverage.

Tax cuts are too convoluted to benefit small businesses

The tax cuts are structured in a way that is convoluted and benefit those at the top far more than lower-income business owners, with the majority of benefits going to the wealthiest pass-through business entities. Small business owners who do see any benefit will not receive enough savings to grow or invest back in their businesses.

While corporations received large, permanent tax cuts across the board that will allow them to plan ahead for the future, the same cannot be said for most small businesses. Small business owners were given a temporary and complicated tax deduction that does nothing to streamline their taxes or help them invest back into their businesses. A recent report co-authored by Anne Zimmerman, a member of our national Small Business Council who owns a small public accounting firm in Ohio, found the 20% deduction on qualified business income is unlikely to generate enough savings for real small businesses to hire new employees, invest back into their businesses or make operational improvements.⁹ Additionally, recent polling from Businesses for Responsible Tax Reform found a majority of small businesses say they do not plan on hiring new employees or giving raises as a result of the new tax law, and they say the law favors large corporations over small firms.¹⁰

In addition to the temporary nature of this tax cut, the complexity and confusion surrounding the new deduction means that any savings will go towards tax professionals to help entrepreneurs navigate their taxes or towards dealing with increased administrative burdens. We frequently hear from our members how confusing they find the changes. Mike Brey, owner of a hobby-based retail store in Maryland, says friends in the small business space are all anxious for advice and clarification about how the new tax law will impact their businesses. Mike says he feels small business owners have been told “so many competing narratives.”

Other small business owners echo this feeling of confusion after looking online and finally turning to tax professionals for help. “After doing quite a bit of research regarding the tax law, I’m still confused as to what [the] new changes mean for me and my employees. I have yet to be able to find a single source with straightforward information,” says Annie Wadsworth, second-generation owner of a bagel shop in upstate New York.

David Arena, owner of a commercial real estate media business in Philadelphia, told us, “I think they missed an opportunity to simplify taxes for small businesses and potentially reduce the administrative costs of filing taxes. In addition, I don’t think they addressed tax issues that impact a small business’s ability to hire new employees. I think there needs to be more focus on incentivizing

⁸ Tax Policy Center, “Distribution of Business Income, by Statutory Marginal Tax Rate; Current Law, 2017,” March 2017, <https://www.taxpolicycenter.org/model-estimates/distribution-business-income-march-2017/distribution-business-income-statutory>

⁹ Businesses for Responsible Tax Reform, “The Tax Cuts and Jobs Act: Implications for Small Businesses,” May 2018, https://docs.wixstatic.com/ugd/4a8609_5ae6299d49534af6b27acb872d044e30.pdf

¹⁰ Businesses for Responsible Tax Reform, “Poll: Tax Law Won’t Help Small Businesses Grow,” March 2018, https://docs.wixstatic.com/ugd/4a8609_a801668b62ff4d9bacfe8b9fadacb995.pdf

small business to hire more employees with competitive wages and good benefits. As far as immediate benefits for me as an employer, I don't actually think this will help us very much when all is said and done."

Given these sentiments, it's not surprising that the National Small Business Association found in a recent survey of its members that a mere 7% say they think filing taxes will become easier under the new tax law, and 1 in 3 say they already spend more than 40 hours each year on federal taxes.¹¹ An additional 1 in 3 say businesses plan to, or are considering, switching from a pass-through entity to a C-Corporation as a result of the Tax Cuts and Jobs Act, with the majority saying the temporary nature of the small business tax cuts is an issue for their business.

Simply put, small business owners wanted a simplified and more streamlined tax system that would also help level the playing with large corporations, and they got the opposite.

The new tax law fails to address loopholes and exacerbates the risk that wealthy individuals will game the system

The enactment of a "territorial" corporate tax system in the new law creates an even more unequal playing field for small businesses because it allows a few multinational corporations to funnel their profits to the lowest-taxation foreign jurisdictions—a provision small firms are unable to take advantage of. Indeed, this loophole primarily benefits 30 large corporations at the expense of small businesses. According to the Congressional Budget Office, corporations will shift \$235 billion in profits annually under the new tax law.¹² To make matters worse, this provision sits on top of yet another loophole in the law allowing large multinational corporations to repatriate their past profits at a steeply discounted rate.

And, last but not least, the new tax code, with its large gap between top individual rates and top pass-through rates, only encourages wealthy individuals to game the system by simply declaring themselves pass-through business entities. While the new law exempts certain industries from accessing the pass-through rate, there is no way to guard against abuse of the new deduction and ensure that it does not further exacerbate the benefits to hedge fund managers, lobbyists, lawyers and investment bankers—rather than Main Street small businesses.

Conclusion

Small business owners feel that our tax system primarily benefits wealthy corporate interests at their expense. The facts support this assessment. America's hard-working entrepreneurs don't want special treatment; they simply want to compete on a level playing field.

This is why we need a tax code that benefits America's entrepreneurs who are focused on growing their enterprises and making payroll at the end of each month. We had a once-in-a-generation chance to make our tax code work better for small businesses, and we blew it.

Thank you for the opportunity to comment on this important issue for America's small business community. I would be happy to answer any questions.

¹¹ National Small Business Association, 2018 Small Business Taxation Survey, <http://nsba.biz/wp-content/uploads/2018/04/Tax-Survey-2018.pdf>

¹² Congressional Budget Office, "The Budget and Economic Outlook: 2018-2028," <https://www.cbo.gov/system/files/115th-congress-2017-2018/reports/53651-outlook.pdf>