

principles of Entrepreneurship

>>>> 18. The Importance of Government Policies

Entrepreneurial activity leads to economic growth and helps to reduce poverty, create a middle class, and foster stability. It is in the interest of all governments to implement policies to foster entrepreneurship and reap the benefits of its activity.

Thomas A. Garrett, a senior economist with the Federal Reserve Bank of St. Louis, says that government policies can be categorized as “active” or “passive” depending on whether they involve the government in determining which types of businesses are promoted. Active policies, such as targeted tax breaks, help specific forms of businesses, while passive policies help create an environment that is friendly to entrepreneurs without regard to specific firms.

Both active and passive policies are effective in promoting small business, Garrett says, but passive policies promote entrepreneurship most broadly. “It is this entrepreneurial-friendly environment that will allow any individual or business—regardless of size, location or mission—to expand and to thrive,” he says.

Among the most successful strategies for encouraging entrepreneurship and small business are changes in tax policy, regulatory policy, access to capital, and the legal protection of property rights.

Tax Policy: Governments use taxes to raise money. But taxes increase the cost of the activity taxed, discouraging it somewhat. Therefore, policymakers need to balance the goals of raising revenue and promoting entrepreneurship. Corporate tax rate reductions, tax credits for investment or education, and tax deductions for businesses are all proven methods for encouraging business growth.

Regulatory Policy: “The simpler and more expedited the regulatory process, the greater the likelihood of small business expansion,” says Steve Strauss, a lawyer and author, who specializes in entrepreneurship. Reducing the cost of compliance with government regulations is also helpful. Governments can, for example, provide one-stop service centers where entrepreneurs can find assistance and allow electronic filing and storage of forms.

Access to Capital: Starting a business takes money. There are required procedures and fees as well as the initial costs of the new enterprise itself. Therefore, the most important activity a government can undertake is to assist potential entrepreneurs with finding money for start-ups.

In the United States, the Small Business Administration (SBA) helps entrepreneurs get funds. The SBA is a federal agency whose main function is guaranteeing loans. Banks and other lenders that participate in SBA programs often relax strict loan requirements because the government has promised repayment if the borrower defaults. This policy makes many loans available for risky new businesses.

Legal Protection of Property Rights: Small business can thrive where there is respect for individual property rights and a legal system to protect those rights. Without property rights, there is little incentive to create or invest.

For entrepreneurship to flourish, the law needs to protect intellectual property. If innovations are not legally protected through patents, copyrights, and trademarks, entrepreneurs are unlikely to engage in the risks necessary to invent new products or new methods. According to the World Bank report, “Doing Business 2007: How to Reform,” new technologies are adopted more quickly when courts are efficient. “The reason is that most innovations take place in new businesses—which unlike large firms do not have the clout to resolve disputes outside the courts.”

Creating a Business Culture: Governments can also show that they value private enterprise by making it easier for individuals to learn business skills and by honoring entrepreneurs and small business owners. Policy makers can:

- Offer financial incentives for the creation of business incubators. These usually provide new businesses with an inexpensive space in which to get started and services – such as a copier and a fax machine – which most new businesses couldn’t otherwise afford. Often business incubators are associated with colleges, and professors offer their expertise.
- Make information available. In the United States, for example, the SBA has many offices, making publications widely accessible. Its “Small Business Answer Desk” (telephone: 800-827-5722) and its Web site (www.sba.gov) answer general business questions. Its online business tutorials are available to anyone with Internet access (<http://sba.gov/training/coursestake.html>).
- Enhance the status of entrepreneurs and businessmen in the society. Governments might create local or national award programs that honor entrepreneurs and call on business leaders to serve on relevant commissions or panels.