<u>Encouraging Entrepreneurship in Delaware</u>

In a recent report ("Moving Delaware Out of the Economic Doldrums by David Stevenson), the Caesar Rodney Institute presented comprehensive data showing that since the 2007 recession Delaware's economy has been lagging the majority of states.

Beginning from 2007 Delaware has ranked 43rd in per capita real GDP growth and 45th in personal income growth. Median household income has dropped and the unemployment rate has risen. High industrial electric and natural gas rates have contributed to the loss of half the energy intense manufacturing in Delaware.

Actions that can readily stop this slide are obvious: public education reform, repeal of the Gross Receipts Tax, passage of a Right to Work Law, restructure of the Prevailing Wage law, and ending Delaware's participation in the Regional Greenhouse Gas Initiative.

Less obvious, but as important, is the restoration of the conditions that encourage entrepreneurship in Delaware.

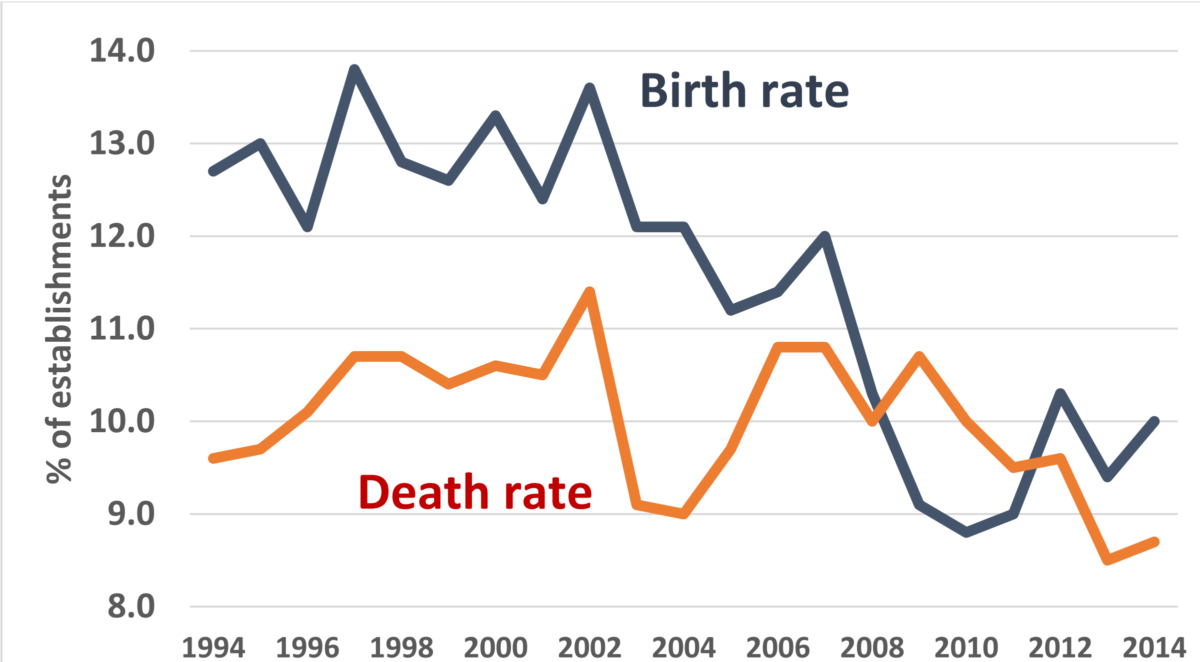
TRENDS IN ENTREPRENEURSHIP

Economists label the birth and death of business establishments in a geographic area "creative destruction." The birth of new establishments allows new technologies to be introduced to the economy and for the economy to adapt to changing tastes and preferences. The death of establishments permits the economy to shed itself of businesses which are no longer productive or whose goods and services are no longer in demand.

The chart below shows annual establishment births and deaths in Delaware as a percent of total business establishments. Two things jump out from the chart.

First, following the 2007 recession, the death rate of establishments in Delaware exceeded the birth rate for four years. The net effect was that the total number of business establishments in Delaware fell.

Second, over time, the birth rate of establishments in Delaware has dropped substantially. New establishments on an annual basis have gone from almost 14% of all establishments down to 10%. By retarding the process of "creative destruction", this drop in the formation of new business establishments causes a drag on Delaware economic growth.



Is this drop-in business establishment start-ups due to unavoidable macro-economic conditions, or have state officials enacted and enforced policies that discourage entrepreneurship in Delaware?

STEPS FOR REVIVAL

The widespread sketch of an entrepreneur's personality traits sounds like this: brilliant, hair-on-fire iconoclast with a game changing idea for a product or service. The most important trait is that business builders don't have job security in their top five life priorities, maybe not at all. They are motivated by desire "to make a difference', fame, fortune and impatient to get going.

So, what do these business starters need? A location to start the business, start-up capital for employees and equipment, and the government to get out of the way. They also want the location to be safe from crime and near to good public-school systems.

For start-up tech businesses, business incubators are a great place to start a business: low or no cost facility for 3-10 employees, common services and conference rooms, secure buildings and like-minded residents in the facility. Whether put together by university and public/private partnerships business incubators work well and provide a resource for start-up businesses.

For out of state entrepreneurs and venture capital firms thinking about location of their companies in Delaware the state has many plusses that other states don't have: upwards of 50 million people within 100 miles, international airport in 25 minutes, interstate highways, nice climate, reasonable access to Philadelphia, Baltimore/DC and Atlantic beaches.

The show-stopper for many lookers are the public schools that statewide boast the third highest spending per pupil in the country and academic performance in the bottom 20% of all states. Reversing this situation is entirely within the state's power to change…it just takes the political will to do so.

The other glaring fact that Wilmington shows up in surveys in recent years as in the top ten cites in the U.S. in per-capita murder rate. The number one job of government: keep residents safe. Whatever it takes, this situation must be righted as once a city gets a crime reputation as Wilmington does, it is very hard to reverse.

On the plus side, Delaware recently passed the Angel Investor Tax credit law that enables the state to return up to 25% of new investments in technology companies to its investors via income tax credits. This is very competitive with New Jersey with its Angel tax credit at 10% and Maryland at 50% tax credit for qualifying tech companies. Maryland is highly focused on biotech and medical tech companies. The law as written is somewhat unclear as to the availability of the tax credit to out of state investors but that is a must. New Jersey handles that by out of state investors filing for a refund.

Low interest rate loans that are forgivable over time if the company meets new employment goals are another tool that Delaware has and as far as it goes is competitive with neighboring states.

A highly successful program in some states is allowing qualified tech companies to "sell" their tax losses each year to a profitable tax-paying company of that state. Simple example: Delaware tech company has $2 million in losses; it "sells" its tax loss to a profitable Delaware taxpayer. At say a 6.5% corporate tax rate that means the profitable company can "save" $130,000 in taxes. In this case the tech company will get the $130,000 back minus a broker charge of usually less that 7%. Delaware should seriously consider implementing such a program.

The Delaware Department of State has the responsibility to conduct these incentive programs. It is not enough to post the programs on its website. The DOS must be proactive in communicating its programs widely. For example, when asked the question: what technologies would you think Delaware has an advantage over other states or a generally recognized high level of competence academically and in industry?

Knowledgeable folks answer: chemical engineering, chemistry including polymers of all sorts, plant genetics, agricultural and financial analytics. The Delaware incentive programs should be communicated to VC firms everywhere and overseas, trade publications of those industries, alumni associations of tech universities and so on.

Finally, what can we do for the non-tech geniuses who have the entrepreneurial drive but not the resources? Engineering consulting firms of all types, civil, electrical, mechanical are high paying jobs. Various jobs in dentistry are high paying. Many other careers are not necessarily high tech but are high paying. Answer: don't restrict the state programs exclusively to tech.

To the extent possible, remove or lower the state licensing requirements for as many license jobs as we can. Hairdressers probably don't need 15 months of schooling at a cost of $15,000 or more. The flush of new retirees in southern Delaware have to wait 4-6 months to get a “new patient” appoint at a primary care dentist because state licensing restricts the number of new dentists to the number of existing dentists that retire or move away. Lots of other examples. It takes political will to extinguish these rent-seeking anti-competitive regulations that have taken root over the years.

For the protections that both trade unions and craft unions enjoy, the state should insist on job training/journeyman programs.

The overall goal is to set a business climate that attracts the formation of new business and keeps our children from having to go out of state to get a good paying job.

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