State and local barriers to entrepreneurship

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State and local governments lure businesses with incentive packages. Yet these governments impose rules stifling entrepreneurs starting new businesses, forgetting that Amazon, offered multi-billion dollar deals for its HQ2, started out of **Jeff Bezos's** garage.

A new Cato Institute study, "Entrepreneurs and Regulations" by **Chris Edwards**, details the state and local government burdens on startups. Elected officials should carefully weigh these policies' benefits against the burdens. The administration of many rules can be significantly improved.

How do regulations harm small businesses? First, many compliance burdens occur at startup. While every added employee or business location involves compliance, many licenses, permits, and inspections must be obtained before opening. One study found that regulatory costs per employee were 29 percent higher for small versus large businesses.

Startups also employ more lower-wage workers: weekly earnings at small firms were half the average for the largest firms. Increases in minimum wages and mandated employee benefits hit small businesses harder.

Large businesses have more political influence and can reduce the burden of new regulations on themselves or obtain exemptions to rules. Businesses that do not yet exist cannot influence regulation.

Startups have very tight margins and cannot afford extra costs. Entrepreneurs typically invest their life savings, borrow from friends and family, and earn little initially. One study found that half of tech company founders made less than $6 an hour during the first year.

Alcohol licenses illustrate another type of burden. Eighteen states limit the number of alcohol permits; the existing permits can be sold, with prices often exceeding $250,000. Chain restaurants can more easily afford this cost than a chef opening her first restaurant.

"Entrepreneurs and Regulations" offers a new measure of state policy burdens, called the Entrepreneurial Regulatory Barriers Index. The index includes 13 measures across four areas: small business owners' perceptions of the burden of regulations, occupational licensing, entry barriers (like Certificate of Need laws), and policy-created costs.

The best states for startups are Georgia, South Dakota, and North Dakota; California, New Jersey, and Connecticut are the worst. Alabama ranks 29th, a little lower than in other small business policy indexes. The Pacific Research Institute and Small Business and Entrepreneurship Council rank Alabama 15th and 11th, respectively. Alabama's climate for startups is not horrible but could be better.

Local governments may impose even greater burdens, as Mr. Edwards details. Consider the sheer number of rules. In New York City, small businesses are subject to 6,000 regulations, while 15 city agencies issue over 250 licenses and permits. Delays are common. Honolulu is supposed to issue small commercial building permits in 14 days but takes on average over 150.

Entrepreneurs often must pay rent while waiting for approvals. In addition to delay is uncertainty, which economic research consistently shows reduces business investment. Many city offices offer no way to track the progress of applications, so entrepreneurs cannot know when or if permission to open will be granted.

Government rules, frequently zoning laws, hamper home-based businesses. Zoning historically kept businesses and industry out of residential areas. Yet, the internet allows businesses to be run unobtrusively from home, keeping costs low while entrepreneurs explore the potential for their product or service. Complaints by neighbors typically trigger zoning enforcement, highlighting the often unpredictable impact of rules on new businesses.

The Alabama legislature helped home-based businesses this year with a "cottage foods" bill. The law lifts a cap on the value of annual sales, increases the range of foods people can make at home and allows internet sales. Alabamians can now more fully participate in America's cottage food boom.

State and local governments might have to sustain business over the next several years. The Biden administration is clearly very pro-regulation. As Mr. Edwards writes, "whatever happens in Washington, state and local governments can do much to improve the entrepreneurial climate by repealing low-value and harmful regulations." Regulatory reform can help grow Alabama's economy.