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Resource Development Council for Alaska, Inc.

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May 4, 1983

Neil Phelps-Munson
Representative Joe Hayes
Pouch V
Juneau, Alaska 99811

Dear Neil:

Here is the backup information that you wanted for the economic development policy resolution. We certainly appreciate your help on this legislation and look forward to its passage.

I have enclosed two articles from a prominent business magazine that rates the 50 states on their business climates. In one, Alaska received a letter grade (D), and in the other a numerical rating (45th).

We feel that Alaska must raise these "grades" by demonstrating its commitment to economic development. A key symbol of state support for business development is legislative and gubernatorial support of an economic development policy such as we have submitted to your office.

This legislation is the RDC's top priority for the 1983 session. We have put many hours and the knowledge of many experts into its development and would certainly appreciate your support.

Thanks again,

Mike Abbott

Mike Abbott

State given 'D' grade for business

Alaska has received a grade of "D" on a report card from a Inc. magazine which analyzed the overall climate for small business in each of the 50 states.

While the state came in second in the energy costs category of the magazine's analysis, it did not rank among the top states in the other four categories, capital resources, small business commitment, labor or taxes.

A sixth factor, quality of life, also was recorded but the magazine editors said they considered it too subjective for overall ranking.

Inc., which is headquartered in Boston, Mass., said it researched more than 50 different components of small business life, including loan programs, wage rates and unemployment taxes, to determine state rankings within the six categories.

The magazine's editors said the survey findings were confirmed by statistics showing a direct correlation between high performance companies and high performance states: the greatest number of fast growing enterprises are found in the top ranked states.

No Alaska companies were listed on Inc.'s 1981 roster of the 200 fastest growing publicly owned small companies, which the magazine plans to publish in December.

In a letter to Gov. Jay Hammond and the Alaska Legislature, Inc. editor Milton D. Stewart, urged "your state and every state to treat this report as a baseline against which to measure future small business growth."

Each state was asked to appoint a technical correspondent to suggest ways to improve Inc.'s method of ranking them.

Stewart said the rankings "will become more meaningful . . . if we have the help of state specialists in achieving consensus."

Next year, he said, the magazine will rank states in terms of degree of improvement over this year's ranking as well as compare them with one another.

In its October issue, Inc. includes to other articles related to the ranking. Entrepreneur Jules Abend cautions that statistics do not determine where any individual company will local. Economist Robert Berney warns against using ostensible tax advantage in ranking states.

Inc. gives its criteria for "fastest growing companies," of which none were found in Alaska, as follows:

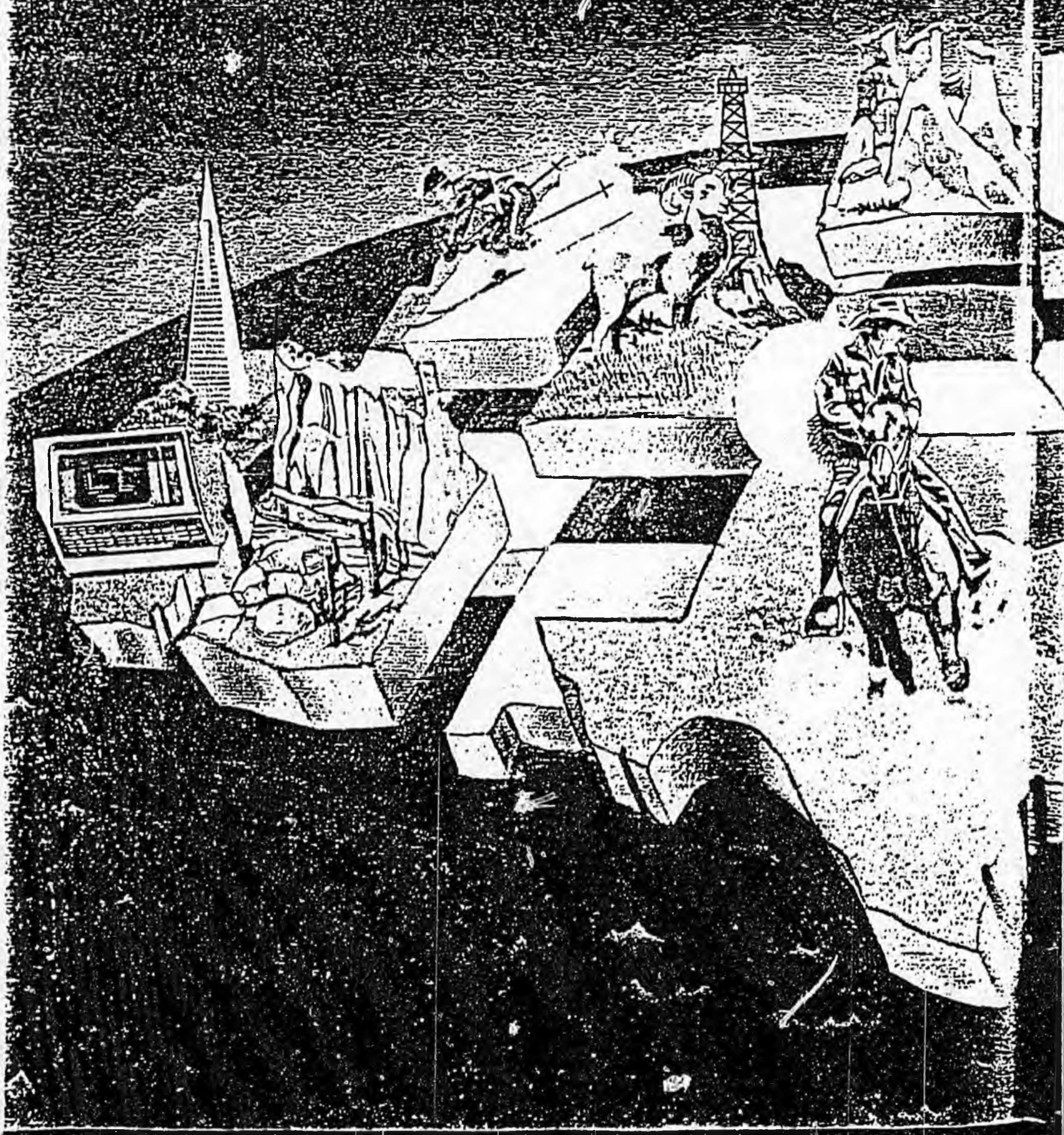
— The company must be an independent, publicly held corporation in manufacturing, mining or service industry.

— The company showed a sales/revenues history of at least five years, with an increase in its fiscal 1980 closing figures.

By Kuldarshan Padda

REPORT CARD ON THE STATES

Ten states are great homes for small companies; five states aren't



A small business- in which state has the *best* business climate, and you can bet he'll give his home state as the answer. At a different time, ask the same businessman which state has the *worst* business climate, and you can bet he'll give you his home state as the answer.

To bring some objectivity to the process of analyzing the business climate in each of the 50 states, INC researched over 50 factors in six areas of doing business: tax burdens, labor, capital resources, official commitment to small business, energy costs, and quality of life. We have ranked the top 10 states in each of the six areas. The rankings and an explanation of the factors involved in each ranking begin on page 92.

In addition, INC decided to give each state a report card based on the combi-

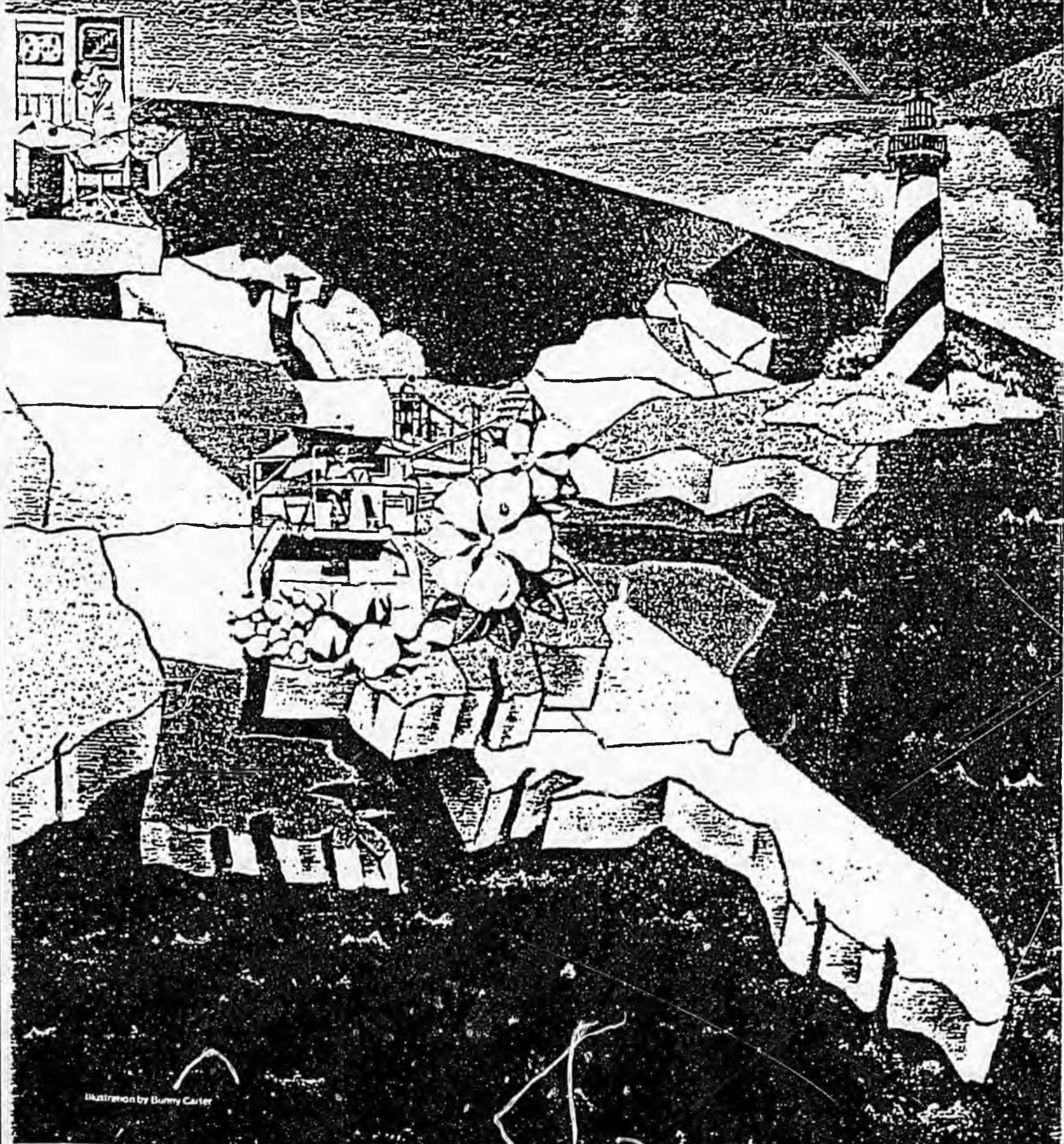


Illustration by Bunny Carter

nation of five of the individual rankings (excluding quality of life, which is so subjective). We've assigned each state a letter grade, from A through F, and published each report card in the table on pages 96 and 97. The results (10 A's, 18 B's, 11 C's, 6 D's, and 5 F's) are often surprising. You wouldn't think, for instance, of North Dakota and Idaho as states rating an A for small business climate. Both follow much the same formula for getting that grade: very high rates of small business activity (number of small companies per 1,000 population), excellent labor conditions, and light tax burdens. Both states share the same failings: weak official commitment to small business on state programs and limited capital available to home-state businesses. Idaho, in particular, gets good grades for its lower energy costs.

Minnesota has a fairly heavy tax burden, but gets an A for its efforts to attract high-technology companies. The state is one of the top five in its official sensitivity to the needs of small business, and offers a large pool of capital to its entrepreneurs. Colorado gets an A from its above-average labor climate, its light tax burden, and a positive ranking in the cost of energy.

Both Arizona and California get an A because of their governments' respective commitments to helping out small business. Beyond that similarity, the two states diverge: Arizona has a light tax burden, low energy costs, and a good labor situation, although it doesn't offer entrepreneurs much in the way of capital resources. California, on the other hand, has the second largest pool of venture capital, but is seriously weakened by high taxes and high labor costs.

While no state in the Northeast earned an A, four southern states came out tops: Texas, Mississippi, Alabama, and North Carolina. If any state could be pegged as Number 1 overall as a place to run a small company, Texas would be the one. (We wanted to avoid ranking the states' overall climates because the decision about where to do business is so complex that it grossly oversimplifies the problem to say that one state is the best place for all small businesses.) Texas made the top 10 in labor, taxes, and capital resources: more top rankings than any other state. Though Alabama is hurt by its labor climate, the

THE TOP 10 STATES IN SIX CATEGORIES

CAPITAL RESOURCES

1. New York
2. California
3. Massachusetts
4. Connecticut
5. Minnesota
6. Texas
7. Pennsylvania
8. Alabama
9. New Jersey
10. Mississippi

One of the biggest headaches every entrepreneur faces is the task of raising seed capital. And if his company not only survives but grows, he often must raise second and third phase financing as well. This ranking measures the availability of that money by gauging the looseness or tightness of investment capital in the 50 states. In which states do the money sources seem most willing to invest in young and growing companies?

Not surprisingly, the top 10 include most of the acknowledged money centers in this country. The only ones conspicuous in their absence are Illinois and Florida. Illinois's failure to make the top 10 list reflects an extremely low Small Business Investment Company activity and Industrial Revenue Bond issuance rate ($4 per capita vs. the national average of $40 per capita). Florida, which ranks No. 47, lacks a loan program tailored to small business and satisfactory IRB issuance. Florida is further hindered by a conservative banking community.

New York achieved the No. 1 position through an extremely aggressive banking community as well as a preponderance of venture capitalists and other investors willing to risk participation in startups and young companies. California also boasts an aggressive banking community, high SBIC activity, and, like New York, a large number of investors willing to take risks.

Massachusetts, Connecticut, and Minnesota all have aggressive banking communities and active SBIC programs. Connecticut, in fact, is the national leader in SBIC activity. Minnesota and Massachusetts possess very active IRB programs as well.

Pennsylvania and Alabama are hobbled by a lack of small business loan programs. But they both managed to make the top 10, the former by claiming the nation's most active IRB authority and the latter by registering the second most active SBIC program. Mississippi overcame the handicap of a cautious banking community to earn a top slot by promoting the second most active IRB authority along with a well-run SBIC program.

Anchoring the opposite end of the spectrum, West Virginia finds itself in the company of Nevada, Nebraska, Kansas, Alaska, and Hawaii. Geographically a rather diverse crew, these states can all be characterized as having average to nonexistent IRB sales and SBICs. All except Alaska are also the victims of banking communities that are recalcitrant when it comes to lending.

ENERGY COSTS

1. Hawaii
2. Alaska
3. Washington
4. Montana
5. Oregon
6. Wyoming
7. Idaho
8. Maine
9. Louisiana
10. Florida

Hawaii number one? A Sunbelt oil producer like Texas or Oklahoma would seem to be a more logical choice. How could an island that is forced to import all its fuels have the lowest energy costs? The answer lies in Hawaii's climate.

The formula used for calculating energy costs took into account the raw cost per Btu for electricity, heating oil, and natural gas. The formula calculated the percent use of oil and natural gas for heating and then constructed the total heating dollar by multiplying the percent use times the raw cost for each fuel. This figure was then plugged into a formula incorporating the number of heating days, while the price of electricity was factored into the number of cooling days. Also taken into account were the electricity costs involved in day-to-day operations, such as office lighting and running plant machinery.

Thus, despite some of the highest energy costs, Hawaii, with a climate tempered by ocean breezes, has no heating bills. Alaska, on the other hand, despite a large number of heating days, managed to score well due to no cooling bills and the availability of natural gas at one-third the national average cost. Limited cooling needs also earned Maine a position among the top 10.

Washington and Oregon ranked high, based on dirt-cheap electricity provided by abundant hydroelectric power. Montana and Idaho attribute their low energy bills to a combination of very cheap

A NOTE FROM THE EDITOR

INC.'s first Special Report on the states' small business climates must be read with care because it is a *first* report. We know from our experience with similar surveys that it takes two to three years of doing a particular report to find the best and most comprehensive ways of compiling them. We think this first report on the states gives as fair and accurate a picture of those factors analyzed as possible. We also know that each state can make a better case for its own achievements in its appeals to some particular kind of business or industry.

We will, however, engage in a continuing technical review of how to improve this report during the next year. We will talk with state officials, academic specialists, and small business leaders. And we will be particularly interested in our readers' response to the report, for which we've provided a postpaid card bound in at a page 91.

During the next months, we will also study what the executive and legislative branches of each state's government is doing to specifically improve its attractiveness to small businesses. We will select for special citation those states that haven taken the most promising steps for small business in certain areas: taxes, regulation, paperwork, capital, credit, procurement, data collection, management assistance, and others.

In 1980, the National Governor's Association adopted a resolution at their annual meeting in Denver, Colo., which signaled a higher priority for small business at the state level. In part it said: "From a state and local economic development standpoint, small businesses offer considerable potential for ensuring economic diversity, stability and long-term growth. The governors pledge their cooperation in working at both the state and national levels to encourage the growth and development of America's small business."

Since that conference, we've heard of some promising beginnings in what we think could be called the "50 State Small Business Sweepstakes," in which there are literally no losers.

—Milton D. Stewart, Editor

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electricity generated through hydro power and petroleum, as well as the availability of natural gas and heating oil at well below the national average cost. Wyoming, too, claims low electricity costs, through cheap coal. It also has natural gas at costs well below the national average.

At the bottom of the rankings are the Middle Atlantic and southern New England states. Spanning an arc from Virginia to Massachusetts, these states are beset by hefty heating and cooling costs, but lack the cheap energy available to western states lying at the same latitude.

SMALL BUSINESS COMMITMENT

1. California
2. New York
3. Minnesota
4. Massachusetts
5. Kentucky
6. Illinois
7. Wisconsin
8. Michigan
9. Connecticut
10. Ohio

Visit almost any state in the nation and you will hear the familiar complaint: "Our state government is one of the worst. The fellas in the state capital just don't care about small business." Same old belly-aching, you say? Not if you are talking with an entrepreneur from Nevada, Wyoming, or South Dakota. All three states rank among the bottom 10 in terms of budget policies and commitment to small business programs. South Dakota, in fact, is No. 50 in this respect.

INC. analyzed the level of support among state legislatures for small business, as well as their attitude toward expenditures and revenues in general. These factors (see table on page 96) were correlated in a computer model to generate a ranking of the 50 states based on their support of small business.

The top 10 found their niche through solid commitment to small business programs, such as procurement setasides, advisory offices, and significant legislative activity favoring smaller enterprises. It is essentially the strength of these programs rather than the presence of balanced budgets that propelled them to the head of the pack.

LABOR

1. North Dakota
2. South Carolina
3. North Carolina
4. Idaho
5. Florida
6. New Mexico
7. Utah
8. Texas
9. New Hampshire
10. Kansas

Armed with a labor force that is willing to work for one of the lowest wage rates in the country and that does not believe in striking, North Dakota tops the list in the labor category. The only Achilles' heel the state exhibits is a rather tight labor pool, with one of the lowest unemployment rates in the country.

The ranking took into account many factors including union strength, militancy, and recent success in recruiting; wage rates; and the ability to find skilled workers to fill both blue- and white-collar positions.

Taking second and third place are South Carolina and North Carolina. Their strength lies in the fact that their workers get paid the lowest and third lowest wage rates, respectively, in the country and are the least unionized work forces as well. In fact, the Carolinas are organized at a level that is less than half the national average, and incredibly this level has been decreasing in recent years. North Carolina's shortcoming is that it possesses a scarcity of skilled workers for blue-collar jobs, while South Carolina has a severe shortage of workers for white-collar positions. To compensate for these weaknesses, both states are funding two of the most extensive vocational programs in the country.

Idaho's major selling points are a low strike rate and the fact that it is undergoing one of the most rapid deunionization rates. Florida and New Mexico boast two of the lowest wage rates as well as a very low strike rate among two of the least unionized work forces in the 50 states. Florida also spends the highest amount per worker on vocational training programs.

Utah has a well-trained, nonunion work force, but it also has a high wage rate and the manpower is in a tight market marked by low unemployment. Texas and New Hampshire have low unionization levels. New Hampshire also has a low wage rate but suffers from a tight labor market and a poorly funded vocational program.

Among those ranked at the bottom of the list are Indiana, West Virginia, Hawaii, Missouri, state shows exceptional performance in capital resources. Mississippi is helped out by its capital resources, primarily distributed through Industrial Revenue Bonds. And North Carolina gets particularly good grades for its labor pool and a low tax burden.

The second tier of states, those that got a B, include most of the industrial states in the country. New York and Massachusetts, for example, have enormous pools of capital for small business people, but also suffer from high taxes and energy costs. Arkansas, on the other hand, offers the fifth-best tax structure and reasonable energy costs, but has little capital. And Maine has an above-average small business activity rate, inexpensive labor, and insignificant cooling costs, but its economy is one of the most depressed in the country.

Pennsylvania and Illinois both got C grades, surprisingly. Those Philadelphia banks help their state get a top-10 ranking in capital resources, but the state is hurt by high taxes, high energy costs, a poor labor picture, and an abysmal rate of small business activity. Illinois, on the other hand, has a surprisingly strong commitment to small business through government programs and a fair amount of capital, but is hurt by its labor and energy costs.

Iowa and Maryland are surprising states to get a D on small business climate. While Maryland has an awakening interest in small companies, particularly high-technology firms, it ranks in the bottom 10 for its tax burden and its energy costs. And Iowa scores well in its tax structure and its government support of small business, but is hurt by a tight labor supply and a shortage of venture capital.

The five states that earned a failing grade are, perhaps, most interesting of all 50. Hawaii is a great place to visit, but it's a tough place to run a business. It has the lowest energy costs in the country, but it's number 49 in taxes, number 48 in labor, and gets poor marks for capital resources and official support for small business. West Virginia's government is sensitive to small business, but the state ranks in the bottom five for labor, taxes, and capital resources, and has the lowest rate of small business activity in the country.

Delaware ranks in the bottom five in

Michigan, Pennsylvania, Ohio, and Oregon, where workers earn among the highest hourly wages in the nation and are unionized at two to four times the level of workers in the top 10 states. The union activity in these lowest ranked states is marked by militancy and memberships that are much more willing to pursue job actions to achieve their goals.

TAXES

1. Nebraska
2. Arizona
3. Texas
4. Indiana
5. Arkansas
6. New Hampshire
7. North Dakota
8. Missouri
9. South Dakota
10. Colorado

Tax rates, it can be argued, are the most important factor in any comparison of state business climates. However, it is often the presence of nontaxation or exemption from taxation that can be the critical element in a fledgling company's survival and growth. Unfortunately, the wide diversity of small business makes it impossible to quantify the exemptions (see table on page 96) offered by each state.

To quantify tax policies for a state-by-state ranking, INC. weighed the tax burden per capita, the recent trends in that burden, and the future trend based on state debt. The tax burden borne by small business was not used because timely and accurate data is not available. Unemployment related taxes, however, were incorporated to more closely approximate the cost of operating a business in each state in tax terms. Nebraska, for example, emerges as No. 1 due to strong performance in all categories but particularly because of a very low employer contribution rate to the state's unemployment compensation fund.

Arizona claims very low debt per capita, leading to the expectation of a low tax rate in the future. The state also has a wealthy unemployment compensation fund that promises low unemployment taxes in the future.

Texas has low debt per capita, but even more important is the absence of a corporate or personal income tax. The Lone Star State also has the lowest employer unemployment contribution rate.

Arkansas scores well in all categories and is especially notable for one of the lowest percentage increases in taxes from 1979 to 1980.

Claiming the lowest taxation rate in the country, New Hampshire has not only avoided taxing personal income but has also kept the lid on its unemployment contribution rate.

North Dakota has a low tax rate, a small debt, and its taxes rose the least in the nation from 1979-80.

Low tax burdens also earn Missouri, South Dakota, and Colorado top 10 rankings.

As expected, states like Massachusetts, New York, and Minnesota, with notoriously high tax rates, are standouts among the bottom 10 on the list, with Alaska earning the dubious distinction of worst case.

QUALITY OF LIFE

1. North Dakota
2. Iowa
3. South Dakota
4. Wyoming
5. Hawaii
6. Rhode Island
7. New Hampshire
8. Vermont
9. Montana
10. Florida

Could North Dakota rank first in quality of life? Where's California, that mecca of sunseekers and trendsetters? The answer lies in how the quality-of-life factors were tabulated. Unlike the other rankings, for which it was possible to create fairly accurate models that evaluated various factors on the basis of their importance to small business, the quality of life is something that is totally subjective. For example, how does one explain to the ski buff in Colorado that Florida's beaches contribute more to the quality of life than ski trails?

In fact, it is impossible to weight factors for differing lifestyles in the same scale. To establish some measure, however, INC's computer selected the states that were the best for the lifestyles they represent. The factors incorporated in the calculations ranged from cultural elements such as orchestras and opera, to quality of health care and education, recreational facilities, and the cost of living. The result is a list of 10 states that represent the best of their breed when personal preferences are considered.

North Dakota, for example, earns top billing on the basis of its crime rate (lowest in the nation), long life expectancy and lower cost of living. Ditto Iowa, New Hampshire, and Vermont. If your preference, however, is culture, health care and other factors associated with living near metropolitan areas, then Rhode Island, Massachusetts (No. 13), or New York (No. 14) are good bets. Sun, surf, and sand? Hawaii or Florida.

And what about California? Based on high cost of living, a tight housing market, and a high crime rate (second in the nation), the Bear Republic emerges as No. 32, just behind Minnesota and North Carolina and just ahead of Oregon and Pennsylvania in a ranking best left to humans.

STATE	INC. overall rating[1]	TAXES[2] Per capita	Unempl.	Exemptions[3]	CAPITAL RESOURCES SBIC index	IRB issues per capita	Gen. obl. bonds	State loans	Bank loans
Alabama	A	$ 493	2.6%	C. P. E. L. M. I. N. R	276.53	$ 66	NO	NO	15.5%
Alaska	D	3,541	4.8	E. N	23.78	0	YES	YES	19.7
Arizona	A	688	2.2	C. P. I	24.59	45	NO	NO	15.6
Arkansas	B	532	2.1	I. N	32.64	45	NO	NO	13.6
California	A	853	3.4	I	116.42	0	NO	YES	18.9
Colorado	A	538	1.3	C[8] P. E. N	106.92	15	NO	NO	17.8
Connecticut	C	591	2.6	P[9] M[10] I	388.04	31	YES	YES	17.9
Delaware	F	886	2.8	C. E[11] L. M. I. N	33.21	43	YES	YES	8.5
Florida	B	542	2.0	C. P[9] E[11] I[12] N	80.45	18	NO	NO	10.3
Georgia	B	533	1.9	L. I. N	45.32	31	NO	NO	14.2
Hawaii	F	1,091	2.8	E	40.18	NA	YES	YES	14.4
Idaho	A	542	2.1	I. N	217.11	NA	NO	NO	16.7
Illinois	C	630	3.3	L[13] M. I. N[14]	18.69	4	NO	YES	24.2
Indiana	B	499	1.6	L[15] M. I[16] N	27.31	72	NO	YES	12.1
Iowa	D	602	2.8	C[17] L[18] M[19] I[20]	8.19	45	NO	NO	11.8
Kansas	B	536	1.8	C[8] L[21] M[21] I[22] N[21]	20.85	45	NO	NO	13.0
Kentucky	B	608	2.2	L[23] M[23] I[23] N	49.45	22	NO	YES	13.2
Louisiana	C	595	3.3	C. L[24] M. N. R	116.36	8	NO	NO	16.8
Maine	B	564	3.1	I. N. R	42.10	34	NO	YES	17.5
Maryland	D	665	3.8	L[23] M. I. N. R[25]	39.34	32	NO	YES	13.0
Massachusetts	B	681	3.5	C. M. N. R	140.35	64	NO	YES	23.0
Michigan	D	643	4.1	C. P. L[26] M. I. N	27.17	30	NO	YES	14.5
Minnesota	A	789	2.3	C. P. E. L[27] M. I. N[28] R	106.98	99	NO	YES	17.6
Mississippi	A	578	2.1	P. L. M. I. N	133.64	100	NO	YES	12.5
Missouri	F	430	2.3	C. P. N	11.28	NA	NO	YES	14.5
Montana	B	554	2.9	C[29] L. I[30] N[31]	11.34	27	NO	YES	15.4
Nebraska	C	549	1.3	I	.00	19	NO	NO	12.6
Nevada	F	679	3.0	C[9] P[9] I[31]	32.20	NA	NO	NO	14.1
New Hampshire	B	302	1.8	P[9] M. I. N	214.68	62	NO	YES	14.7
New Jersey	D	560	3.7	L. M[19] I. N	87.56	79	YES	YES	14.2
New Mexico	B	746	2.1	M. I	248.59	6	NO	NO	18.0
New York	B	721	3.6	C[32] P[33] E[11] L. M[35] I. N. R	69.15	14	YES	NO	24.2
N. Carolina	A	574	2.1	I. N[35]	50.78	36	NO	NO	18.1
N. Dakota	A	566	2.5	C. E. L[36] M[34] I. R[25]	.00	60	YES	YES	14.5
Ohio	B	444	2.4	C. P. L. M. I. N	44.22	67	NO	YES	14.8
Oklahoma	B	614	1.6	L[21] M. I. N	106.01	96	NO	YES	16.7
Oregon	C	576	3.4	C. P. E[37] L[36] I. N	98.06	13	YES	YES	19.4
Pennsylvania	C	617	3.4	E. L. M[38] I[39] N. R	36.25	139	NO	NO	18.2
Rhode Island	D	593	2.9	L. M. I. N. R	24.44	67	NO	YES	20.3
S. Carolina	B	572	2.1	L. M. I. N. R	86.09	68	NO	NO	13.5
S. Dakota	B	393	1.3	C. P. E. L. I	201.01	24	NO	NO	13.4
Tennessee	B	431	1.8	P. L[23] M. I. N	22.58	56	YES	YES	14.5
Texas	A	505	.6	C[9] P. L[40] M	117.71	22	NO	YES	21.0
Utah	C	575	1.7	I	35.27	42	NO	NO	18.6
Vermont	C	540	3.3	L. M. I. N	212.24	49	NO	YES	13.6
Virginia	C	528	1.1	L. M[23]	64.72	57	NO	NO	13.7
Washington	C	743	3.3	C[9] P. E. L. M. I	126.98	0	NO	NO	25.1
W. Virginia	F	649	2.6	C. P. E. N	5.27	18	NO	NO	8.8
Wisconsin	B	713	3.2	C[41] M. I. N	58.94	42	NO	NO	14.8
Wyoming	C	862	1.3	C[9] P. E. I	68.35	88	NO	NO	17.0

LABOR			SUPPORT			
% Unempl.	% Union	Avg. hourly wage index	Procurement prog.	Assist. office	Advisory board	Legis. committee
7.1	19.2	85	10%	NO	NO	NO
9.2	26.2	147	NO	YES	NO	NO
5.1	13.8	99	YES	YES	NO	NO
6.2	15.0	77	NO	YES	NO	NO
6.2	23.7	104	YES	YES	YES	YES
4.8	15.2	102	NO	YES	YES	NO
5.1	21.9	98	15-25%	YES	NO	NO
8.0	21.7	100	NO	NO	NO	NO
6.0	11.7	79	NO	YES	YES	NO
5.1	13.6	77	YES	NO	YES	NO
6.3	32.1	94	NO	NO	NO	NO
5.7	14.3	100	NO	NO	NO	NO
5.5	31.5	112	YES	YES	NO	NO
5.4	29.3	118	YES	NO	NO	NO
4.1	19.2	118	NO	NO	NO	YES
3.4	12.8	100	10%	NO	NO	YES
5.6	22.4	99	YES	YES	YES	YES
6.7	16.0	103	10%	YES	NO	NO
7.2	18.3	84	NO	NO	NO	NO
5.9	21.0	101	YES	YES	NO	NO
5.5	24.4	90	5%	YES	NO	YES
7.8	34.6	133	YES	YES	NO	NO
4.2	24.4	104	20%	YES	NO	YES
5.8	12.4	72	YES	YES	NO	NO
4.5	30.0	98	NO	YES	NO	NO
5.1	24.1	115	YES	YES	YES	NO
3.2	15.3	100	NO	YES	NO	NO
5.1	22.9	104	NO	NO	NO	NO
3.1	13.3	80	NO	NO	NO	NO
6.9	23.0	101	NO	YES	NO	NO
6.6	12.1	78	NO	YES	NO	NO
7.1	39.2	99	YES	YES	YES	YES
4.8	6.5	72	YES	NO	YES	NO
3.7	14.7	89	NO	NO	YES	NO
5.9	29.5	121	NO	YES	YES	YES
3.4	13.5	99	NO	NO	NO	NO
6.8	23.1	117	NO	YES	NO	NO
6.9	34.2	105	YES	YES	YES	NO
6.6	27.1	77	NO	NO	YES	YES
5.0	6.7	74	NO	NO	NO	NO
3.5	10.3	89	NO	NO	NO	NO
5.3	17.7	81	NO	YES	YES	NO
4.2	11.0	95	10%	YES	YES	NO
4.3	13.0	95	NO	YES	NO	NO
5.1	17.5	85	NO	YES	NO	NO
4.7	12.7	83	NO	YES	NO	NO
6.8	33.1	129	YES	YES	NO	NO
6.7	36.8	110	NO	YES	YES	YES
4.5	27.8	112	YES	NO	YES	YES
2.8	14.9	97	NO	NO	NO	NO

FOOTNOTES

1. grade based on total points accumulated in 6 categories: taxes, capital, labor, small business support and energy
2. 1980 per capita data (Bureau of the Census); unempl. is % of total payroll employer pays in unemployment tax (U.S. Employment & Training Admin.)
3. Key: C-corporate income, P-personal income, E-excise, L-land, capital improvements, M-machinery, equip., I-manufacturer's inventory, N-new equip., sale/use tax, R-tax exemption to encourage R&D (Site Selection Handbook, Conway Publications Inc., Atlanta, Ga.)
4. 1980 Small Business Investment Company financing: 100 = balance between share of SBIC financing and state economic activity (Small Business Administration); Small issue Industrial Revenue Bonds (Congressional Budget Office); general obligation bonds (Conway Publications); 1980 state loans (Directory of State Small Business Programs, Office of Chief Counsel for Advocacy, SBA)
5. total commercial & industrial loans as % of total bank assets (FDIC)
6. 1980 unemployment rate, seasonally adjusted (U.S. Bureau of Labor Statistics); % unionization (Directory of National Unions and Employee Assns., BLS); average hourly wage & fringe benefits for selected manufacturing (U.S. Dept. of Labor)
7. state government's commitment to small business programs; % procurement indicates percent of state purchases awarded small business (SBA)
8. 10-yr. credit for new business based on job investment
9. state does not tax personal income; Nevada, Texas, Washington and Wyoming also do not tax corporate income.
10. equip. acquired after 1973 exempt from local prop. tax
11. does not levy excise tax
12. inventory items assessed at 10% of just valuation
13. available in Cook County
14. phased; fully exempt 1984
15. 10-yr. partial prop. tax abatement in urban areas.
16. finished goods destined out of state
17. 50% of federal tax paid
18. 5-yr. abatement on land & equip.
19. tangible property taxed at 1.3% of half its cost; tax repealed for equip. bought after 1-1-77
20. first $1[illegible],500 of assessed taxable value of pers. prop.
21. 10-yr. exemption on IRB-financed property
22. applies to goods stored in licensed warehouse, provided at least 35% of prior year sales were shipped out of state
23. local level only
24. capital improvements only
25. includes R&D equip.
26. local option in redevelopment areas
27. pollution equip. only.
28. detachable tools & equip. with useful life up to 1 yr.
29. 1% credit based on wages for first 3 yrs., to selected new industries
30. all inventories reduced to 4% of market value.
31. no sale/use tax.
32. up to 10-yr. credit under job incentive program
33. credit equal to 4% of qualified capital invested in new equip., facilities with useful life of 4 yrs. or more
34. personal property
35. 1% preferential rate on new equip., max. $60/article
36. new construction only
37. credits to manufacturers & processors for prop. taxes paid on goods in process
38. sale/use tax excluded on items used in industrial production & research.
39. tangible personal prop. excluded from local tax.
40. 7-yr. annexation of development exemption
41. credit for sales tax paid on energy

taxes and energy costs, and Missouri makes the top 10 for its taxes, but ranks in the bottom 20 in labor, energy costs, and capital resources. And, unless you run a gambling business, Nevada may be one of the hardest states to do business in: The state ranks in the bottom 20 in every category.

Missouri, in particular, demonstrates the difficulties in grading states on their relative business climates. INC. didn't consider transportation costs in its analysis, and that factor is one of Missouri's advantages. Its location in the hub of the country's transportation system is an extremely important factor for companies with heavy shipping requirements.

In order to compute rankings in six areas of doing business and to assign a grade to each of the 50 states, INC. programmed a computer to weigh and compare more than 50 factors, based on data from numerous sources. We weighted these factors to reflect their importance to small businesses in general. For example, the availability of venture capital is far more important to smaller enterprises than giant corporations, so INC. placed more emphasis on that factor in ranking the states for capital resources. Likewise, we de-emphasized the importance of unions in the work force, because they affect smaller businesses less relative to large ones.

In addition, INC. generalized the computer model to make sure that the results of our analysis would be meaningful to a wide range of small companies. Energy costs, though, were analyzed for a high-technology, light-manufacturing company. Therefore the energy rankings would be somewhat different if the costs had been calculated from the point of view of a retail or service business, and considerably different for a heavy industrial manufacturing business.

Generalizing factors for whole states was also a problem. Tax burdens, for instance, are not necessarily uniform throughout the whole state. Maryland and Michigan both have very high tax burdens, but some aggressive areas within both states offer substantial property-tax exemptions. And California presents a significant problem in analyzing energy costs, because the whole state spans East Coast latitudes ranging from Connecticut in the north to South Carolina in the south. The degree days required for both heating and cooling cover wide ranges between the northern and southern latitudes. In addition, California, Florida, and New York are difficult states for calculating statewide labor climates: In each, the unemployment rates are higher in the southern, urban areas than in the northern, rural areas.

Perhaps the most difficult obstacles to creating an objective and meaningful critique of the states' small business climates is the highly subjective nature of the decision about where to locate a business. Among people who study this sort of decision, the current thinking is that most start-up businesses are located where their founders live. If the entrepreneur does have the luxury of deciding where to locate, the decision is most often based on factors that affect his business directly: proximity to markets in the case of regional, distribution companies, for example. Or the decision is based purely on the owner's lifestyle.

But a state's business climate does become particularly important in the case of companies that, having reached the expansion stage, want to find a good location for a new plant or branch office. And, from the state government's point of view, the true measure of managing the business climate well comes from the performance of those small companies already in the state. Without successful small companies, no state can look for real growth.

This report was prepared by Kulbhushan Padda, an editorial intern and Harvard undergraduate, with the assistance of INC. senior editor Bradford W. Ketchum, Jr.

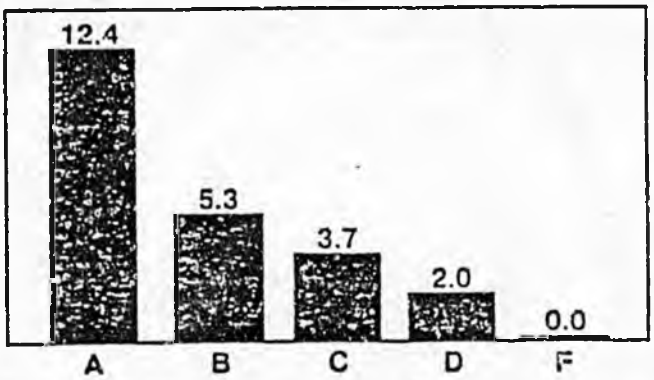
HIGH-PERFORMANCE COMPANIES LIVE IN HIGH-PERFORMANCE STATES

Not surprisingly, there is a direct correlation between the location of the country's fastest-growing, smaller companies and those states with the most positive climate for small business. When we matched up the location of the INC. 200 firms for the last three years and the states that earned an A in our analysis, we found that the top 20% of the states spawned 43% of the fast-growing companies.

From another angle, the relationship between business climate and the concentration of emerging companies becomes more clear. The average number of high-growth firms per state (adjusted) ranges from a high of 12.4 per A state to a low of 0 per F states.

We've adjusted the high-growth-companies-per-state formula to account for two anomalies: New Jersey and Missouri. New Jersey, a D state, has a high number of INC. 200 companies (19) for the last three years. But we discounted that because the business climate probably does less for emerging companies than the state's location in the bustling Northeast corridor. And Missouri is an anomaly: its one INC. 200 company, Billings, only recently moved there from Utah. Because most of the company's growth took place in Utah, we can't really give the credit to Missouri.

NUMBER OF INC. 200 COMPANIES (1979-81) PER STATE



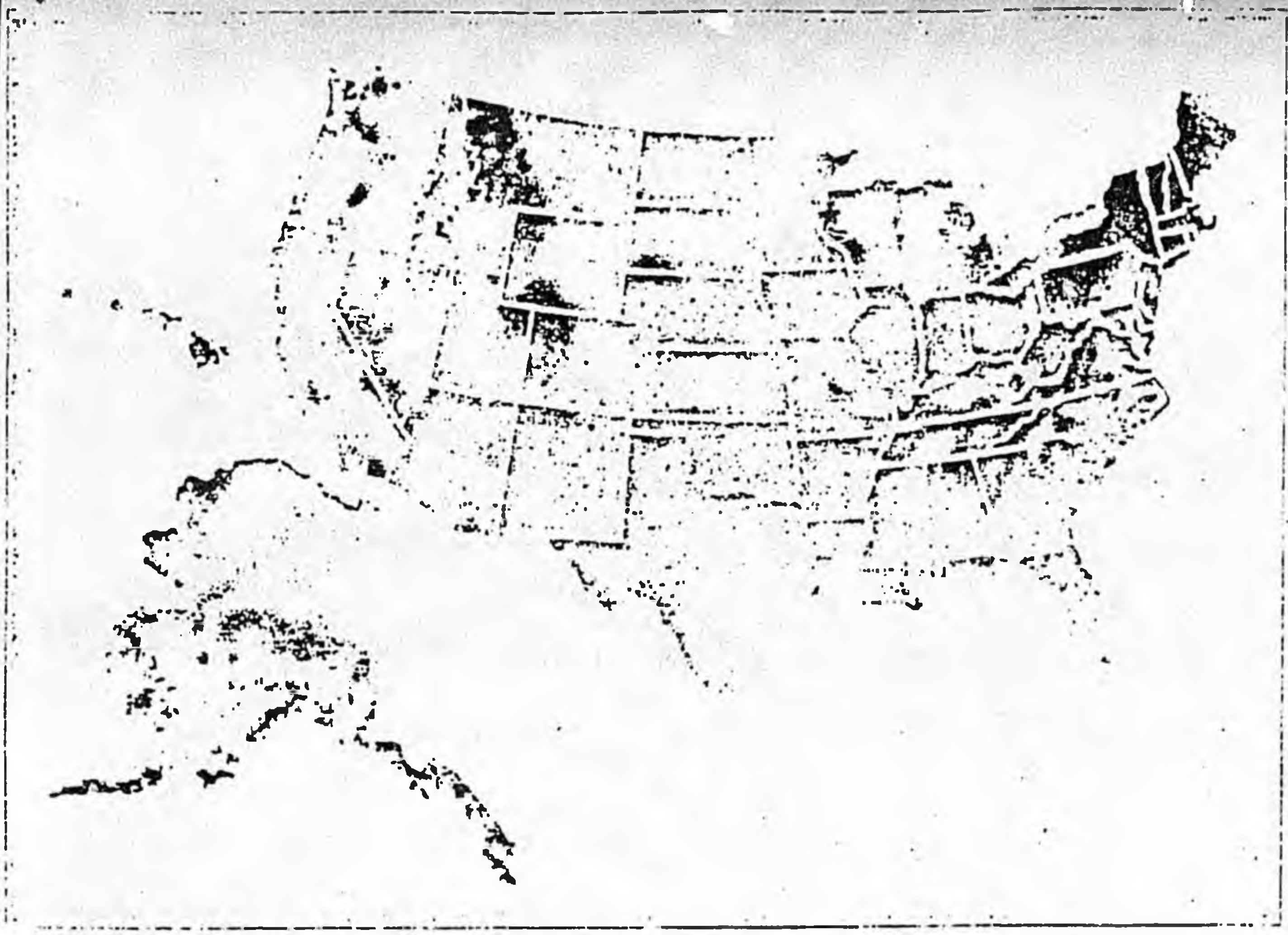
HOW ABOUT PUERTO RICO AND THE VIRGIN ISLANDS?

Puerto Rico may be the perfect choice for companies who have reached the expansion stage, and are now deciding where to locate that new manufacturing plant. Over 30 INC. 200 companies would agree, that's how many have chosen the Puerto Rico option. Agressively pursuing the manufacturing industry (especially in high technology), this tropical island has put together a package of incentives that is hard to beat. Highlights of this package include a complete exemption from U.S. corporate income taxes along with a 90% exemption from Puerto Rican corporate income and property taxes. Another important benefit of operating in Puerto Rico is its low labor costs: less than half of the U.S. average. One of the many interesting programs that Puerto Rico offers is its twin plant concept. This involves sub-assembly work in foreign islands, elsewhere in the Caribbean, at dirt-cheap labor costs. The parts are then shipped back to Puerto Rico (U.S. tariff laws do not require taxation on re-imported parts), and final assembly work done.

These advantages led Puerto Rico located plants to achieve a profit-to-sales ratio of 22.6% compared to 5.7% of their counterparts on the mainland.

The major drawbacks of locating on the island are high shipping costs and management problems because of cultural shock. The high shipping cost can be turned into an advantage if you are interested in servicing the booming economies of Venezuela and Mexico. The culture shock is not really a problem anymore because close to 90% of all industrial plants in Puerto Rico are run by managers who are natives. This means there really isn't a need to send your own vice-president down there.

The Virgin Islands is attempting to lure manufacturing companies with a package of tax incentives consisting of a 100% exemption on real-property and gross-receipts taxes along with a similar exemption from excise taxes on plant-construction expenses. There are also subsidies on federal and local income taxes. Perhaps the major attractions are relatively low labor and shipping costs. The low labor cost is gained from operating in a depressed economy like that of the Virgin Islands. And shipping costs less because the islands are exempt from the Jones Act and do not have to ship their goods to the mainland via expensive American-flagged shipping. The problems in doing business in the islands include high operating costs due to expensive land, utilities, and other such factors. You also have to have a large inventory, since it takes a while to have items shipped from the mainland.



A REPORT ON THE STATES

INC.'s second annual study rates 50 small business climates.

By Bruce G. Posner

If your company's history is anything like that of most small companies, where it is located—be it Palo Alto, Calif., or Portland, Maine—has nothing to do with any carefully drawn corporate plan. Instead, you put the business where you were raised, attended school, or simply wanted to live. Presumably, the area had much of what you wanted of the myriad things that influence "quality of life." Perhaps there was good skiing, music, or a major university within easy reach. Or you may have wanted to be near people in similar vocations, which may be why so many high-technology companies grew or are expanding in California's Silicon Valley and along Boston's Route 128.

Although state officials everywhere wish they could do more to spawn and keep growth oriented companies, all too often they find that it is hard enough to define the amenities that attract small businesspeople without trying to influence a decision to set up business. But apart from the intangibles in appraising a business climate, there are factors that are both more concrete and, to some extent, within a state's control.

As companies grow, for example, they may need long-term debt and equity, in addition to working capital. They may also need to hire employees who have specialized skills. A company's inability to find such fundamental resources when they are needed can greatly influence its success, and it can also dampen the growth of the economy within the state.

The purpose of INC.'s second report on the states is to compare some of the major, quantifiable aspects of the climate for small business, to help businesspeople and state officials understand better how to make improvements. In selecting the criteria for measuring the 50 states as homes for smaller companies, INC. interviewed economists, state development officials, venture capitalists, and small business executives. INC. also talked with special liaison people appointed by governors to gather information on small business support programs in every state.

The analysis focused on areas of broad concern to all small companies, rather than such factors as transportation and energy, important as these may be to some businesses. Since all small business operators have capital and labor needs and are affected by taxes, we looked at the impact of those three factors on small companies. Growth opportunities in a particular environment are also influenced—sometimes heavily—by external economic and business factors. These factors, therefore, are reflected through a number of criteria under the heading of business activity.

Finally, we examined each state for small business support programs initiated at the executive or legislative level. The mere existence of official support does not

RATING THE STATES BASED ON FIVE MAJOR FACTORS

Rank/state	CAPITAL RESOURCES				LABOR				TAXES
	Bank loans % assets	Comm./ind loans per capita	SBIC finan. per 1,000 pop.	State programs[1]	Avg. wkly. wage	% union	% H.S. grads.	Value added per worker (thou./yr.)	Per $1,000 personal income
Median	53.5%	$ 927	$0.8	–	$317	23%	68%	$43.6	$112
1. Texas	54.8%	$2,527	$3.9	DL	$328	11%	65%	$55.1	$ 98
2. California	64.7	1,468	3.2	DL,LG	339	27	74	48.0	122
3. Colorado	57.9	1,262	3.1	–	326	18	78	45.7	113
4. Florida	49.5	598	1.2	–	265	12	65	37.0	97
5. New Hampshire	63.2	588	1.8	LG	256	16	70	31.2	92
6. Kansas	48.4	1,082	1.4	–	325	15	73	44.0	100
7. Arizona	62.6	888	0.6	–	317	16	73	47.7	133
8. Oregon	58.8	1,112	1.8	DL	352	26	76	39.0	114
9. Oklahoma	52.8	1,921	1.2	DL	329	15	66	42.2	102
10. Washington	58.9	1,382	0.9	–	405	34	76	49.5	109
11. New Mexico	52.7	1,043	2.3	–	259	19	66	36.0	122
12. New York	54.4	4,164	2.2	DL,LG,BG	309	39	66	47.2	163
13. Kentucky	49.2	773	1.0	DL,BG	309	24	53	45.6	104
14. North Dakota	50.1	1,245	–	BG	271	17	68	52.6	102
15. Connecticut	59.7	857	5.1	DL,LG,VC	319	23	70	42.8	105
16. Virginia	60.0	718	0.9	–	270	15	64	36.0	102
17. Nevada	59.5	738	0.3	LG	325	24	76	51.0	105
18. Massachusetts	50.0	1,213	2.1	DL,BG,VC	280	25	72	40.0	139
19. Minnesota	54.5	1,430	2.7	DL	331	26	73	45.5	127
20. New Jersey	53.1	765	0.9	DL,LG,BG	322	26	66	47.4	117
21. Utah	56.5	838	0.1	–	308	18	80	40.4	125
22. Arkansas	52.1	946	0.2	BG	247	16	56	30.4	99
23. Georgia	52.8	683	1.0	–	255	15	59	33.3	108
24. Tennessee	51.9	908	0.5	–	268	19	55	33.7	94
25. Wyoming	53.4	1,54[illegible]	2.6	–	314	19	76	61.4	148
26. Mississippi	50.6	6[illegible]	0.8	LG	236	16	52	31.6	109
27. Montana	55.1	1,17[illegible]	1.2	–	370	29	73	47.9	130
28. Maryland	57.1	555	0.3	DL,LG,BG	335	23*	69	43.7	120
29. Missouri	47.4	1,112	0.1	BG	318	28	64	43.6	93
30. Ohio	50.4	757	0.6	DL,LG	390	31	68	46.6	94
31. Rhode Island	55.0	1,426	0.4	DL,LG,BG	240	28	62	28.4	119
32. Idaho	55.8	344	3.5	–	311	18	72	36.0	104
33. Illinois	58.7	2,841	0.7	DL	356	30	66	47.0	112
34. North Carolina	51.4	804	0.5	–	232	10	55	30.6	106
35. Wisconsin	55.8	853	0.6	DL	353	29	70	43.6	125
36. Michigan	54.3	909	0.7	DL	426	37	69	47.6	115
37. Pennsylvania	53.5	1,365	0.5	DL	325	35	65	38.5	116
38. Vermont	66.3	712	1.3	DL,LG	272	18	70	36.6	127
39. Hawaii	60.6	992	0.1	DL	290	28	73	45.1	148
40. Iowa	48.6	854	0.1	DL	379	22	72	51.0	111
41. South Dakota	67.5	1,039	1.5	–	296	15	69	36.6	106
42. Indiana	51.4	726	0.3	DL,LG,VC	376	30	67	43.5	88
43. Nebraska	50.6	965	0.2	–	324	18	74	46.7	111
44. Louisiana	52.2	1,231	1.6	DL,LG	362	16	58	64.9	116
45. Alaska	45.0	978	0.2	DL,BG,VC	457	34	80	54.2	368
46. Alabama	48.7	664	0.7	–	260	22	56	30.8	96
47. South Carolina	48.2	361	0.6	–	250	8	57	27.3	107
48. Maine	54.1	502	0.5	DL,LG	296	24	68	27.8	125
49. Delaware	46.3	551	–	–	333	25	70	49.4	116
50. West Virginia	49.8	499	0.1	DL,LG	347	34	53	43.5	112

1 DL-direct loans, LG-loan guarantees, BG-bond guarantees, VC-venture capital
2 AO-advisory office, OM-ombudsman, AC-advisory council, LC-legislative committee, SC-statewide conference, PS-procurement set-asides.
* Includes union membership in District of Columbia

STATE SUPPORT	BUSINESS ACTIVITY				
Small bus. assistance, (1971-80)	Pop. % change (1971-80)	Employmt. % gain (1971-80)	Pers. inc. % change (1971-80)	Business units per 1,000 pop.	INC.100 companies (1979-82)
-	11.5%	27.7%	45.4%	46	2
AO,OM,AC,LC,SC	27.1	67.8	77.4	47	27
AO,OM,AC,LC,SC	18.5	41.6	48.7	46	49
AO,OM,AC,SC	30.7	61.0	74.2	50	13
AO,OM,LC,SC,PS	43.4	65.9	77.1	55	10
AO,LC,SC,PS	24.6	47.9	56.7	46	2
AO,AC,LC,SC,PS	5.3	63.2	43.5	46	1
AO,OM,AC,SC,PS	53.3	79.7	88.7	49	3
AO,OM,AC,SC	26.5	46.5	64.3	51	4
AO,SC,PS	17.2	46.6	65.6	49	6
AO,LC,SC,PS	21.0	25.1	60.4	47	4
AO,OM,SC,PS	24.7	58.0	67.6	50	2
AO,OM,AC,LC,SC,PS	-3.3	0.6	9.1	46	31
AO,OM,AC,LC,SC,PS	13.7	41.8	44.4	40	1
AO,AC,LC,SC	5.6	50.5	45.5	54	-
AO,OM,PS	2.5	17.0	26.7	43	6
AO,OM,SC	11.8	39.6	50.3	39	5
AO,LC,SC	63.8	96.8	92.0	50	1
AO,OM,LC,SC	0.8	17.1	21.3	40	12
AO,OM,LC,SC	6.9	34.6	37.9	41	18
AO,OM,AC,LC,SC	2.7	17.2	22.2	44	16
AO,OM,AC,SC	37.9	32.6	70.3	48	1
AO,AC,SC,PS	18.5	38.9	60.3	45	0
AO,OM,AC,LC	17.8	37.8	49.7	45	6
AO,OM,AC,SC,PS	13.0	13.3	50.0	42	4
-	41.1	88.6	123.1	57	4
AO,OM,AC,LC,SC	12.9	34.4	50.0	44	1
AO,AC,SC,PS	13.3	42.4	42.3	56	-
AO,AC,LC,SC,PS	7.5	25.6	34.2	35	5
AO,OM,LC,SC,PS	5.1	18.5	31.9	44	1
AO,OM,AC,LC,SC	1.0	13.3	24.9	40	3
AO,AC,LC,SC,PS	-0.4	15.8	25.0	47	-
-	32.3	58.7	61.5	50	-
AO,OM,AC,LC,SC,PS	1.2	14.5	23.9	41	-
AO,AC,LC,SC	15.5	33.8	45.2	41	1
AO,OM,AC,LC,SC	6.5	27.1	36.5	40	3
AO,OM,AC,SC,PS	4.2	15.0	32.6	37	2
AO,OM,AC,SC,PS	0.2	8.6	24.9	42	6
AO,SC	15.0	35.1	29.4	54	-
AC,LC,SC	25.3	37.5	41.0	52	2
OM,AC,LC,PS	3.1	24.7	31.9	47	1
AC	3.8	36.0	30.4	50	-
OM,SC,PS	5.7	17.4	31.0	39	6
AO,OM,SC	5.3	30.7	34.4	49	-
AO	15.3	51.8	65.8	46	1
OM,SC	32.5	84.3	93.3	49	1
OM,SC,PS	12.9	34.4	50.9	41	2
AO,SC,PS	10.8	41.0	53.0	42	3
AO,OM,AC	13.2	26.3	38.9	49	-
AO,OM,AC,LC,PS	8.6	21.3	29.6	44	-
AO,OM,LC,SC,PS	11.8	25.1	49.1	43	-

Sources (by column, left to right): Federal Deposit Insurance Corp. (1,2); U.S. Small Business Administration (3); State development agencies (4); U.S. Department of Labor, Bureau of Labor Statistics (5,6); U.S. Department of Education (7); Bureau of Census, Census of Manufacturers (8); Tax Foundation (9); INC survey of 50 states (10); Bureau of the Census (11); Bureau of Labor Statistics (12); U.S. Department of Commerce, Bureau of Economic Analysis (13); Bureau of the Census, County Business Patterns (14); INC (15).

guarantee that significant numbers of small companies are being helped. However, support for innovative programs and a strong commitment to small business at high levels can be enormously useful. Through special programs, a state can leverage its existing capital and labor resources to the benefit of small businesses. State support can also soften the effects of a declining economy.

INC. ranked the 50 states in five categories. Each category—capital, labor, taxes, business activity, and state support—was weighted to reflect its relative importance to small companies. The scoring system was based on a scale of 100 points. Because most of the experts we spoke with considered capital resources and state support the two most critical factors, each was given 25 points. Taxes, while always an area of real concern, received only 10 points, the lowest weighting, since taxes rarely play more than a minor role in the investment decisions of small companies. Labor and business activity were each weighted at 20 points to reflect their broad significance to smaller companies. Calculated by this method, the overall scores range from 82 for Texas to 33 for West Virginia.

Texas achieved the top overall ranking with an unbeatable combination of strong capital resources, an effective labor force, and a low tax burden. But it was further aided by a high level of business activity within the state and official support for small business. California and Colorado, with higher tax rates than Texas, placed second and third, respectively, largely because of their strength in capital and labor. Each also received a very helpful boost from a robust economy.

Fourth-ranking Florida scored very favorably in labor, taxes, business activity, and small business support, but appeared in the bottom 10 for capital resources. For the other states scoring low in capital, such as West Virginia and Delaware, the impact on the overall ranking was often devastating. They did not compensate as well as Florida did with strengths in other areas.

West Virginia, for example, ranked 50th overall and scored weakly on labor and business activity and only average in taxes and small business support. Its ranking of 49th in capital resources—low lending activity compared with bank assets—compounds its weakness in other areas. Delaware, although somewhat stronger than West Virginia in labor and business activity, also suffers from its poor showing in capital. It ranks last in the capital category and 49th overall. In fact, four of the five lowest-ranking states on the summary table (West Virginia, Delaware, South Carolina, and Alabama) are the weakest four states for capital resources. The fifth state, Maine, ranks 48th overall and also suffers in terms of capital.

The influence of other categories, while important, proved less decisive in a state's ranking. Although 7 of the top 10 states had very favorable climates for labor—only Oregon, Oklahoma, and Washington did not—poor performers in labor (reflecting such factors as high levels of wages, low level of education, and the strong presence of organized labor) did not automatically suffer in the overall rankings. In fact, only three states scoring low in labor—Indiana, West Virginia, and Alabama—appeared in the bottom 10 overall. Other high wage and highly unionized states, such as Ohio, Illinois, Michigan, and Pennsylvania, ranked higher because of stronger showings in other areas.

At first glance, Indiana's rank of 42 seems surprisingly weak in relation to such midwestern neighbors as Illinois and Michigan. While none of these states ranks very favorably in terms of labor or business activity—measures by which Illinois ranks at the very bottom—Indiana distinguishes itself by having the lowest taxes (per $1,000 of personal income) in the nation, while Illinois and Michigan fall in the middle.

Nevertheless, Indiana parts company from Illinois and Michigan in small business support activities. Unlike Michigan, for example, Indiana has neither a small business assistance office nor a governor's advisory council on small business. It also lacks a legislative committee devoted to small business matters, as Illinois and 11 other states have had and as 9 states have now added. To Indiana's credit, though, its officials have recently shown an interest in bolstering small business capital resources through the state's new Corporation for Innovation Development (see page 100).

A careful examination of the accompanying table shows that even states that appear quite similar can differ dramatically. But the most useful discovery may be that each of the 50 states has its own set of strengths. The Midwest and the New England states, for instance, are clearly not seeing the same heady growth as Texas and California. But both regions can become vibrant areas for small companies.

Increasingly, states concerned about the future are examining their support programs as the most obvious way of upgrading their climate for small business. Delaware, for example, made notable strides in the past year when it created four support vehicles—an advisory council, a legislative committee, an assistance office, and a program requiring the state to purchase goods and services from small companies.

THE BEST OF SHOW

Capital: Activity at the money centers

1. California
2. Connecticut
3. New York
4. Texas
5. Massachusetts
6. Minnesota
7. Colorado
8. Illinois
9. Oklahoma
10. Wyoming

High interest rates, as the past couple of years have painfully shown, can be catastrophic for small companies, wherever they are. Generally, states can do very little to mitigate borrowing costs for small companies. Apart from the cost of funds, though, capital resources vary widely from state to state. What is more, the types of resources in place in the state and how they are being used can be critical if, like most companies, yours cannot meet all its capital needs. Therefore, capital resources, along with state support programs, receive our heaviest overall consideration in ranking the states' climate for small business.

To see how the states stack up in terms of capital resources for small business, INC. looked first at two sets of banking industry figures—total state commercial bank loans as a percentage of total assets, and commercial and industrial bank loans on a per capita basis. While these measures don't tell what types of businesses are getting the loans—or even whether all the funds are being lent within the state—they usually reflect the degree to which banks are using their asset bases for aggressive lending to meet the working capital needs of business.

INC. also analyzed the states for special capital programs, such as direct loans, loan guarantees, bond guarantees, and state-sponsored venture capital investing, in the belief that these can help bring capital other than working capital to small companies. Because most experts believe that even small-issue industrial revenue bonds tend to benefit large companies and their subsidiaries with solid credit histories, we didn't consider IRBs. Finally, INC. looked at small business investment company (SBIC) investments in the states on a per capita basis, as an indicator of the relative availability of venture capital.

California, with its aggressive banks and active SBICs, emerges as the state with the most extensive capital resources for small business, a distinction it certainly would have earned more easily had all sources of private venture capital been included. Next come Connecticut and New York, whose ranks reflect their active banks, SBICs, and the targeted capital programs in place. Oklahoma and Wyoming aren't usually thought of as states with substantial capital resources, but both benefit from high levels of SBIC investments and per capita commercial and industrial bank loans.

South Carolina, West Virginia, and Delaware emerge as the states where a lack of capital resources—or an unwillingness on the part of commercial banks to lend—poses hurdles for growing small businesses. For instance, commercial and industrial lending in these three states is anemic compared to that in the rest of the states. Low levels of banking activity within a state can, of course, stem from depressed loan demand in a slow economy, but conservative bankers seem to be at least as great a factor.

Labor: The Plains states set the pace

1. Wyoming
2. North Dakota
3. Nevada
4. Kansas
5. Nebraska
6. Arizona
7. Colorado
8. New Hampshire
9. Utah
10. South Dakota

When it comes to labor, the needs of different types of small businesses vary substantially. Most companies, of course, are interested in keeping labor costs down as much as possible. But few can afford to ignore requirements involving skill and concerns over productivity.

In examining labor markets within each state, INC. looked at comparative wage levels for manufacturing and at comparative levels of unionization, which can be a factor in high wages. But in addition to factors affecting the price of labor, INC. also compared the states by levels of productivity and by levels of education among workers.

For productivity, the question was how much each worker added to the value of manufactured goods. In education, the percentage of state residents over the age of 18 who have completed high school was considered, although companies needing highly skilled employees might consider the number of engineering graduates.

At the top of the chart for labor are Wyoming, North Dakota, Nevada, Kansas, and Nebraska. Among these high scorers, however, Kansas is the only state with low union activity. None of the 5 states ranks among the top 10 in terms of low wages. In all but North Dakota, however, 73% or more of their residents over the age of 18 hold high school degrees.

Poorest performers in the labor category are West Virginia, Illinois, Indiana, and Pennsylvania. They have work forces in which only 53% to 67% of the workers hold high school de-

Such programs can be extremely valuable for bringing awareness and help to small companies. But for states facing difficult economic times and declining industries, the future may require more specialized programs in the areas of capital resources, job training, and technical assistance—all aimed at broadening opportunities for small businesses.

In the past, several states targeted most of their initiatives at existing companies, through efforts such as technical assistance programs in connection with universities. But increasingly, some states—Pennsylvania, Georgia, and New York, for example—appear to be highlighting new companies as the important thrust in their economic development efforts. Each of these states is directing money into supporting technology-based start-ups, with technical universities playing key roles (see page 100). Notes Roger Vaughan, a consultant at the Council of State Planning Agencies in Washington, D.C., and former deputy planning director of New York: "States interested in distinguishing themselves will have to do a lot more in helping new businesses come about."

Just as important to the small business climates of many states, though, may be how well the capital and labor needs of growing companies can be met. A growing number of states are considering such measures as the revamping of investment guidelines on public employee pension funds and increasing the outlays for technical education. Through its new Technology Park Corp., for instance, Massachusetts is putting up $20 million for a center co-funded by industry in order to train engineers and other technical specialists in microelectronics.

Some experts are convinced that every state will need to help reshape its work force to accommodate businesses. During the next decade companies are going to need a great many technically competent workers for seemingly nontechnical jobs, according to a number of authorities on small business.

It may not be easy for public officials to think about helping small business in such ways, especially in the Midwest and the South, where the emphasis has long been on big companies and large manufacturing plants. "Politicians don't have to learn how to wave 1,000 jobs around," says Alexander Dingee, president of Venture Founders Corp., a Waltham, Mass., company specializing in assistance to start-up companies. "But it's a lot harder for them to make election-year claims about how they've helped small companies."

Bruce G. Posner is an associate editor at INC.

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grees, and all are heavily unionized in their major industries. In addition, wages for Illinois and Indiana workers average among the highest for manufacturing in the nation.

State support: Kentucky leads the bandwagon

1. Kentucky
2. New York
3. Illinois
4. California
5. Wisconsin
6. Ohio
7. Delaware
8. New Jersey
9. Mississippi
10. Kansas

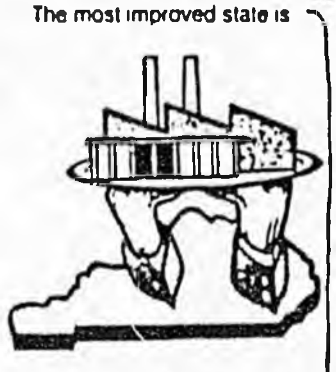
Official state recognition for small business won't make or break small companies very often, but it can give them a boost from time to time and help create a positive business climate. Programs that provide reliable information or technical assistance, for example, can save business operators both time and money.

INC. surveyed the 50 states to identify those that address the concerns of small companies through small business assistance offices, ombudsmen, statewide small business conferences, standing legislative committees, and governors' advisory councils. Nine states have created new legislative committees in the past year, bringing the number of legislatures with small business committees to 21. What is more, 13 governors have recently formed new advisory councils, bringing to 29 the number of states with that form of small business support.

The number of states committed to purchasing a specified portion of their goods and services from small businesses—usually 5% to 15%—has also increased substantially. Twenty-five states currently have procurement set-aside programs, 10 of which were established in the past year.

Kentucky, New York, and Illinois emerge at the top of the charts for official state support for small business. They are the only three states in the nation with a full array of the programs measured in INC.'s survey. But even more noteworthy is that, in the past year, 25 states have upgraded their small business support activities.

The most improved state is



Delaware, which installed four new components to its small business support: an assistance office, an advisory council, a legislative committee, and a procurement program. Almost as impressive is New Hampshire, which added three programs but still lacks an advisory council.

Among the other states demonstrating increased support are Mississippi, Kansas, Rhode Island, Maryland, and Missouri.

Taxes: Indiana takes the smallest bite

1. Indiana
2. New Hampshire
3. Missouri
4. Ohio
5. Tennessee
6. Alabama
7. Florida
8. Texas
9. Arkansas
10. Kansas

As unpleasant as taxes are to many small companies, their importance to a state's overall business climate is seldom on a par with such factors as capital and local resources. Nevertheless, the level of state and local taxes that businesses and individuals must pay tells something about whether it is possible to operate and grow in that state.

Since states tax businesses so differently—by income, payroll, or inventory, for example—and vary greatly in terms of tax credits allowed, state officials and tax experts agree that any direct comparisons are nearly impossible. Instead, INC. focused on the overall level of state and local taxes as related to each $1,000 of personal income—a measure that can be examined on a state-by-state basis. By this measure, Indiana's tax rate of $88 per $1,000 was the nation's lowest, followed by New Hampshire ($92), Missouri ($93), and Ohio and Tennessee (both with rates of $94).

The state with the highest tax was Alaska at $368, although in reality nearly all of the state's revenue is drawn from big energy companies. (In fact, most

Alaskans pay no state or local taxes.) New York, where individuals pay $163 per $1,000, was No. 2, although it has just enacted new rules for start-ups (see page 101). Following New York are Hawaii and Wyoming (both $148) and Massachusetts ($139).

Such tax burdens are comparatively stiff. But tax specialists and economists point out that high state taxes rarely influence a business decision about whether to start up or expand in a particular location—except in the unlikely event that other variables are equal. For one thing, higher taxes can mean better services and schools. "If you can sell 10 times as many widgets in New York as you can in Mississippi or Alabama, you don't mind paying those high taxes," says a national tax partner for a Big Eight accounting firm. "Taxes are usually just the tail," he says, "not the dog."

Bradford W. Ketchum Jr., a senior editor at INC., assisted in the preparation of this section. Anita Harris, a freelance writer, and Carol Holliday Blew, a business analyst, both based in Boston, assisted in research and data analysis.

BOOSTING SMALL BUSINESS

Overcoming an antibusiness bias

The idea of states cutting red tape for development permits and business licenses is nothing new, but Oregon has added some creative wrinkles to overcome a nagging antibusiness reputation.

Antigrowth sentiment was so strong in Oregon during the 1970s that then-governor Thomas McCall once quipped, "Come visit us, but for God's sake, don't stay!" That line was apparently

delivered in jest, but Oregon, reeling from the construction industry slump, which has shut down most of its lumber mills, is still working overtime to convince business that the state wants diversified growth and jobs.

Companies interested in doing business in Oregon were concerned about the need to obtain environmental and other permits, so the state decided to copy neighboring Washington and institute a "one-stop" center, where information on all requirements for permits could be obtained. "Oregon became the second state in the country to apply the one-stop concept," says Paul Haugland, manager of Oregon's Office of State Regulation Assistance. Haugland headed Washington's pioneer program and was hired away by Oregon, where he has carried the idea much further.

Last year, legislation was passed that, in effect, gives businesses a regulatory guarantee. "We'll look at your project and tell you every permit and license you're going to need," explains Haugland. "If it turns out that we slipped up and forgot one, it's on us. You don't have to get it."

So far, the office hasn't missed a permit, so the legal question of what would happen if someone sued to block a project because of a forgiven license has never been resolved. But no one questions the merits of allowing a business to find out about all its permits at once.

Any company planning to set up shop in Oregon now fills out just one 4½-page application. In 30 days, according to Haugland, his office will provide the guaranteed list of permits needed for the project. The office then acts as an advocate for the company in resolving any difficulties with state agencies.

Pension fund steps in

Late last year, Graydon Webb, president of G. D. Ritzy's Inc., wanted to expand his fledgling fast-food restaurant business, headquartered in Columbus, Ohio. Webb, a former vice-president for franchise sales at Wendy's International Inc., the highly successful hamburger chain, was eager to grow beyond his two outlets in the Columbus area, but doing it with a lot of debt would not be easy. Fortunately for Webb, he didn't have to. His company received a $2 million equity investment—and from a very unlikely source: the Public Employees Retirement System of Ohio (PERS).

In exchange for 40% of its stock, G. D. Ritzy's became the $6.5 billion PERS's first small company investment since the Ohio legislature liberalized investment guidelines earlier in 1981. PERS, like most of the nation's public employee funds, had previously been governed by statutes limiting investments to larger, publicly traded companies. Thus, most of its investments were in highly rated debt of big companies, some of which were based outside the state.

Under the new guidelines, the Ohio fund is now authorized to put 5% of its assets—or up to $325 million—into any partnership, proprietorship, or corporation that is either based in the state or has half of its assets or employees there. "Pension funds," says Robert McLaughlin, a PERS investment officer, "can step in to fill the financing gap to the benefit of the local economy and the performance of the fund." While it may take a while for PERS to find appropriate investments, in time it could put money into dozens of Ohio businesses and generate jobs there.

Other states seem to be following Ohio's lead in an effort to direct new capital into emerging companies. Neighboring Michigan, for example, badly scarred from the prolonged slump in the auto industry, recently adopted legislation permitting state pension funds to put up to 5% of its $6.7 billion State Employees' Fund in Michigan small companies and venture capital firms.

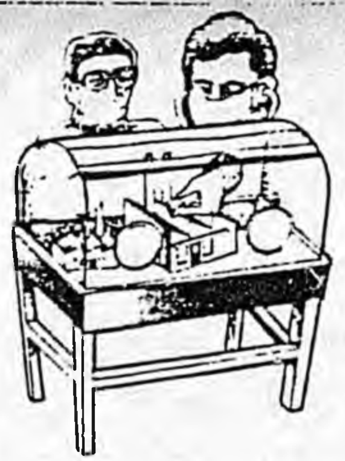
From ivory tower to marketplace

Pennsylvania was a pioneer in acknowledging the importance of technology transfer when it created the Pennsylvania Technical Assistance Program (PennTAP) in 1965. The program linked the state's small business community to existing academic resources. Now the state has begun to carry its role as business problem-solver one step further.

Later this year, a new state-supported program called the Ben Franklin Partnership will get under way with $1 million of state funds, to be matched by an equal amount of private money. Pennsylvania's idea is to further leverage university resources, which are already bringing technical assistance to small businesses, to assist entrepreneurs in product commercialization and applied research.

PennTAP, based at Pennsylvania State University, at University Park, has already earned its spurs with many smaller companies, in which lack of research facilities and personnel can make even a small technical problem loom very large. L. N. Rendall Harper Jr., president of American Micrographics Co. in Pittsburgh, for example, knew he was wasting lots of silver from the film plates he uses in his business but didn't know if it would be economical to recover it. PennTAP introduced him to Penn State researchers, who showed him how to reclaim the silver while complying with federal environmental rules.

Pennsylvania is not the only state with this type of incubator program. Georgia and Tennessee are among the others that



have built small business programs around their universities. The result, says Reuben Harris, director of the Center for Industrial Services at the University of Tennessee, is that "businesses can get the help they need, and ivory tower professors get real-world experience."

Pennsylvania's Ben Franklin Partnership will operate from regional centers around the state. But instead of dealing only with technical problems, as PennTAP does, it will develop ways to move new ideas from the laboratory to the marketplace. The state hopes the new program will help create growth in advanced technologies, such as robotics, biotechnology, and magnetics, as a means of offsetting declines in Pennsylvania's older industrial base.

A fresh approach to capital

No matter where an enterprise is based, finding equity capital for growth is often one of the toughest problems an entrepreneur faces. Private venture capitalists put money in few deals, and few states are willing to expose public funds to high risks. But even in the fiscally conservative Midwest, Indiana seems to have found a way to bring a new source of venture capital to the state's small companies.

Indiana's new Corporation for Innovation Development (CID), authorized last year by the legislature, will be capitalized by private investors, who get a credit—30% of their investment—against their state taxes. While granting tax credits means that Indiana will give up some revenue initially, Lieutenant Gov. John Mutz points out that the approach allows the state to "leverage additional private investment while leaving venture capital investment decisions to the private sector." If the enterprises are successful, they will pay taxes.

Indiana expects CID to draw at least $8 million of private funds, primarily from the state's commercial banks, insurance companies, utilities, and manufacturers. The corporation, which will eventually pay investors Indiana state tax-exempt dividends, could make its first investments by the end of the year. And while it is too soon to say where the money will actually go, Marion C. Dietrich, CID's president and chief executive officer of Cummins Engine Co. in Columbus, Ind., says CID is particularly interested in funding enterprises that are devising productivity improvement technologies to assist manufacturing industries, such as auto and steel.

By law, CID must put its money into Indiana start-ups and new federally licensed small business investment companies. Dietrich reports that the corporation also plans to participate in leveraged buy-outs.

In creating CID, Indiana joins Connecticut and Massachusetts, among a few other states, in developing programs to make more venture capital available. Since its establishment in 1972, the Connecticut Product Development Corp. (CPDC) has committed about $5.3 million to finance product development by 39 companies within the state. When these businesses bring products to market, CPDC claims a royalty, which in 1981 amounted to $219,000. Since 1979, meanwhile, the Massachusetts Technology Development Corp. (MTDC) has invested about $3.7 million in 16 businesses, helping, it says, to make available an additional $14 million in capital for the companies from private sources.

"Private venture capitalists aren't geared to high-risk investments," says Fred Schmid, president of Crystal Systems Inc., a Salem, Mass., company that recently struck out in its efforts to attract private equity investors. Crystal Systems produces industrial synthetic sapphire crystals, but it needed new capital to develop a silicon product for commercial photovoltaic applications. Although private venture capitalists kept saying no, MTDC agreed to lend Crystal Systems $250,000 for seven years, in the belief that a market will eventually develop for the product.

What is more, MTDC's loan enabled Crystal Systems to get a larger credit line from its bank and another $500,000 in long-term debt from another lender. "MTDC's investment showed confidence in the business at a critical time," Schmid says.

The enterprising states

While the Reagan Administration's controversial proposal to create urban enterprise zones in depressed areas is still being considered by Congress, a few states are taking matters into their own hands. Regardless of what finally happens in Washington, Connecticut has passed enabling legislation for its own brand of enterprise zones. This fall it will decide which of the state's economically depressed communities will be the new enterprise zones.

Other states, including Virginia and Kentucky, have their own enabling legislation, and still more are looking at enterprise zones to stimulate business and employment. Connecticut's programs, for example, will offer companies state and local property tax relief, as well as $1,000 grants for each job created. What seems to distinguish Connecticut's plan from those being developed elsewhere is its focus on small businesses.

Such an orientation wasn't accidental. "We're interested in overall development of the zones," says John J. Carson, Connecticut's commissioner of economic development, "so we're targeting small and medium-sized businesses."

Many have criticized the federal enterprise zone plan because it would primarily benefit large corporations that can use tax write-offs. Instead of stimulating new business, this might merely lead to shifts of corporate assets from one side of town to another. Such concern has led small business advocates to suggest that any tax credits be made refundable, to ensure that they are useful to new and small businesses needing cash flow more than tax benefits.

While Connecticut didn't opt for refundable credits, it did establish a new $1 million loan fund for small companies operating within the zones. The fund will lend a company up to 25% of its fixed or working capital, up to a maximum of $100,000 for manufacturing concerns and $50,000 for retailers. It will lend the money for seven years at one percentage point higher than the rate of the state's most recent general obligation bond offering.

Connecticut's enterprise zone legislation will also assist small companies with a unique job-voucher system designed to reduce the cost of finding qualified workers. The state labor department will determine which workers qualify for job credits either as zone residents or under the guidelines of the federal Comprehensive Employment Training Act (CETA). Those who do qualify turn vouchers over to the zone employer who hires them, says Carson, thus saving small companies the sometimes hefty cost of screening employees.

Going for growth in job training

Job-training programs may be coming of age with a new program in Arizona that targets funds for employment in such high-growth industries as electronics and aerospace. Arizona is taking an approach that is different from such states as North and South Carolina, Georgia, and Alabama, where job-training programs have been offered to almost any company willing to set up shop in the state—even when the jobs are in such declining domestic industries as textiles and furniture making. To minimize unemployment problems down the road, Arizona's Office of Economic Planning and Development tries to help only those employers that are apt to generate growth.

The state conducted a major study titled "Opportunities in Arizona for Suppliers of High Technology Manufacturers," which amounted to a series of market studies for a number of industries. Now Arizona can offer job-training subsidies of up to 50% of wages for six months to industries in the state showing the greatest growth potential.

"We're trying to avoid training people for dead-end jobs," says Alton Washington, the state's manpower program manager. He reports that in the program's first year of operation, 8,000 people have been or are being trained by new programs.

Early indications point to satisfaction on the part of the employers. Comtec Economation Inc., for instance, a maker of electronic quartz crystals, is using the program to train 200 employees in Flagstaff. "It took the state only eight weeks to accept our application for training assistance," says Dave Convery, general manager.

A shift in tax incentives

While most state legislatures seek ways to stimulate business through an array of tax incentives, New York has a sharper focus. Eager to spur development of new—particularly high-technology—companies, New York this year began exempting investors in new businesses from capital gains tax payments as long as their money is held in a company for at least six years.

The state has also granted its 6% investment tax credit and its new 10% research and development investment tax credit to new concerns. These measures are meant to provide willing investors and greater cash flow in the early years of a business.

Whether the policy will have its intended impact won't be apparent for some time. The first investment tax credit refunds won't come until next year, and the capital gains exemption won't come into play for four years, when a portion of it becomes available. But an intense lobbying effort by the National Federation of Independent Business to have both measures apply to all small companies suggests that at least some people believe these measures could be significant spurs to investment.

In September 1981, California dropped the capital gains tax on long-term investments in all small independent businesses—except those dealing in tangible assets, such as gems and collectibles. No concrete results are yet evident, but Michael Kieschnick,

director of California's Office of Economic Policy, says, "I've gotten hundreds of calls from lawyers and accountants." Kieschnick plans to conduct a survey this fall to see how the California exemption of capital gains for new small businesses has affected investment decisions.

David L. [illegible]dorff, a New York City-based freelance writer, assisted in the preparation of this section. Counsel for Community Development Inc., a Cambridge, Mass., consulting firm, contributed material.