

U.S. Securities and Exchange Commission

T W E N T Y - S E V E N T H A N N U A L

SEC Government-Business
Forum on
Small Business
Capital Formation



FINAL REPORT

Capital formation is a term used in national accounts statistics and macroeconomics. It basically refers to the net additions to the (physical) capital stock in an accounting period, or, to the value of the increase of the capital stock; though it may occasionally also refer to the total stock of capital formed. Thus, in UNSNA, capital formation equals fixed capital investment, the increase in the value of inventories held, plus (net) lending to foreign countries, during an accounting period. Capital is said to be "formed" when savings are used for investment purposes, often investment in production.

What is Capital Formation?

A term that is commonly employed in the study of macroeconomics, capital formation has to do with additions to the capital stock in a given accounting period. It was heralded by some financial analysts as an essential aspect of the financial picture of a country. Understanding the

CAPITAL FORMATION creation or expansion, through savings, of capital or of producer's goods—buildings, machinery, equipment that produce other goods and services, the result being economic expansion.

capital formation

Definition

The transfer of savings from households and governments to the business sector, resulting in increased output and economic expansion.

capital formation

The creation of productive assets that expand an economy's capacity to produce goods and services. Private savings facilitates capital formation by allowing resources to be diverted to corporate investment rather than individual consumption.

November 20, 2008
Washington, DC

2008 Annual SEC Government-Business Forum
on Small Business Capital Formation

FINAL REPORT

Published April 2009

The SEC hosts the annual Government-Business Forum on Small Business Capital Formation, but does not seek to endorse or modify any of the Forum's recommendations. The recommendations are solely the responsibility of the Forum participants from outside the SEC, who were responsible for developing them. The recommendations do not necessarily reflect the views of the SEC, its Commissioners or any of the SEC's staff members.

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SUMMARY OF PROCEEDINGS

Background

As mandated by the Small Business Investment Incentive Act of 1980, the U.S. Securities and Exchange Commission hosts an annual forum that focuses on the capital formation concerns of small business.¹ Called the “SEC Government-Business Forum on Small Business Capital Formation,” this gathering has assembled every year since 1982. A major purpose of the forum is to provide a platform for small business to highlight perceived unnecessary impediments in the capital-raising process and address whether they can be eliminated or reduced. Each forum seeks to develop recommendations for government and private action to improve the environment for small business capital formation, consistent with other public policy goals, including investor protection. Prior forums have published numerous recommendations in the areas of securities and financial services regulation, taxation and state and federal assistance, many of which have been implemented.

The 2008 forum, the 27th, convened at the SEC’s headquarters at 100 F Street, N.E., Washington, D.C., on Thursday, November 20, 2008.

Planning and Organization

Consistent with the Commission’s statutory mandate in the Small Business Investment Incentive Act of 1980, the Commission’s Office of Small Business Policy, Division of Corporation Finance, invited other federal and state government agencies and leading small business and professional organizations concerned with capital formation to participate in planning the 2008 forum. The individuals who participated in planning the forum, and their professional affiliations, are listed on pages 3 through 5.

The planning group recommended that this year’s forum be held in Washington, D.C. and that it remain focused on securities regulation and taxation, as has been the case in recent years. The members of the planning group also assisted in preparing the agenda and in recruiting speakers and moderators.

Participants

The SEC’s Office of Small Business Policy worked with members of the planning group to identify participants for the 2008 forum. Invitations were sent to participants in previous forums and to members of various business and professional organizations concerned with small business capital formation. The SEC issued two press releases to inform the public about the time, date and location of the forum. The press releases publicized the fact that the forum would be webcast live over the Internet.

¹ The SEC is required to conduct the forum annually and to prepare this report under 15 U.S.C. 80c-1 (codifying section 503 of Pub. L. No. 96-477, 94 Stat. 2275).

Approximately 100 participants attended this year's forum in person, including 33 roundtable panelists, moderators and SEC staff. The video webcast of the forum received 945 hits on the day of the forum, indicating that many individuals participated by watching or listening over the Internet. The archived video webcast of the forum received an additional 481 hits through January 31, 2009. During the forum, roundtable panelists responded to questions not only from participants in attendance, but also from webcast viewers using the Twitter online networking and micro-blogging system.

Proceedings

The agenda for the 2008 forum is reprinted starting at page 6. The forum began with opening remarks from SEC Chairman Christopher Cox, which are reproduced starting on page 10. Chairman Cox's remarks were followed by two morning roundtable discussions and an afternoon roundtable discussion. The roundtable topics included small business capital formation and the current credit crisis, regulatory initiatives to facilitate small business capital formation, and intermediaries assisting small businesses with raising capital and merger-and-acquisition activities.

The afternoon proceedings also included breakout group meetings open to all forum participants in attendance. Four breakout groups met, one on securities offerings by private companies, another on securities regulation of smaller public companies, a third on private placement and M&A brokers, and the last on tax issues affecting small businesses.

The discussions of the four breakout groups resulted in draft recommendations on federal securities and tax law topics. The moderators of the four breakout groups presented their draft recommendations at a final assembly of all the forum participants as the last matter of business on November 20. The assembly discussed and approved all the draft recommendations.

After November 20, the four breakout group moderators worked with the members of their breakout groups and compiled, edited and prioritized the recommendations of each of their respective breakout groups. A final list of 22 securities law recommendations and 15 tax law recommendations based on the discussions in these breakout groups and the final assembly is presented beginning on page 13.

Records of Proceedings

Video recordings of Chairman Cox's opening remarks at the 2008 forum and of the roundtable sessions of the forum are available for viewing on the SEC's web site at <http://www.connectlive.com/events/secgovtbusinessforum112008/>.

A transcript of the morning sessions, afternoon roundtable discussion, breakout group meeting on private placement and M&A brokers, and closing session is available in the official Record of Proceedings of the forum, which can be found on the SEC's web site at <http://www.sec.gov/info/smallbus/sbforumtrans-112008.pdf>.

PLANNING GROUP

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AGENDA

2008 SEC Government-Business Forum
on Small Business Capital Formation
Washington, D.C.
November 20, 2008

9:00 a.m. Call to Order
Gerald J. Laporte, Chief, Office of Small Business Policy
SEC Division of Corporation Finance

Opening Remarks
SEC Chairman Christopher Cox

9:15 a.m. Roundtable Panel on Small Business Capital Formation and the Current Credit Crisis

Moderators:

Karen Kerrigan, President & CEO, Small Business & Entrepreneurship Council, Oakton, Virginia

Chad Moutray, Ph.D., Chief Economist & Director of Economic Research, Office of Advocacy, U.S. Small Business Administration, Washington, D.C.

Panelists:

David A. Bochnowski, Chairman and Chief Executive Officer, Peoples Bank SB, NorthWest Indiana Bancorp, Munster, Indiana

Tom W. Burke, Senior Vice President, National Program Director/Compliance Manager, SBA Lending, Wells Fargo & Company, Minneapolis, Minnesota

Daniel M. Covitz, Ph.D., Assistant Director, Division of Research and Statistics, Chief, Capital Markets Section, Board of Governors of the Federal Reserve System, Washington, D.C.

Kenneth R. Pelowski, Founder and Managing Partner, Pinnacle Ventures, Palo Alto, California

Ned Pollock, Deputy Comptroller for Credit and Market Risk, Office of the Comptroller of the Currency, U.S. Department of the Treasury, Washington, D.C.

Andrew J. Sherman, Partner, Dickstein Shapiro LLP, Washington, D.C.

Eric R. Zarnikow, Associate Administrator, Office of Capital Access, U.S. Small Business Administration, Washington, D.C.

10:45 a.m. Break

11:00 a.m. Roundtable Panel on Current Issues in Securities Regulation for Smaller Companies

Moderators:

Gerald J. Laporte, Chief, Office of Small Business Policy, SEC Division of Corporation Finance, Washington, D.C.

Steven E. Bochner, Partner, Wilson Sonsini Goodrich & Rosati, Palo Alto, California

Panelists:

David A. Bochnowski, Chairman and Chief Executive Officer, Peoples Bank SB, NorthWest Indiana Bancorp, Munster, Indiana

Brian V. Breheny, Deputy Director, SEC Division of Corporation Finance, Washington, D.C.

Aaron M. Gurewitz, Head of Equity Capital Markets, Roth Capital Partners, LLC, Newport Beach, California

John D. Hogoboom, Partner, Lowenstein Sandler PC, Roseland, New Jersey

Kara B. Jenny, Chief Financial Officer, Bluefly, Inc., New York, New York

William D. Lutz, Ph.D., J.D., Director, SEC 21st Century Disclosure Initiative, Washington, D.C.

E. Rogers Novak, Jr., General Partner, Novak Biddle Venture Partners, Bethesda, Maryland

1:00 p.m. Lunch Break

2:15 p.m. Reassembly to Divide into Breakout Groups to Develop Recommendations

2:30 p.m. Private Placement and M&A Brokers Panel and Breakout Group Discussion

Moderators:

Brian A. Bussey, Assistant Chief Counsel, Office of Chief Counsel, SEC Division of Trading and Markets, Washington, D.C.

Gregory C. Yadley, Partner, Shumaker, Loop & Kendrick, LLP, Tampa, Florida

Panelists:

Faith Colish, Counsel, Carter Ledyard & Milburn, New York, New York

Denise Voigt Crawford, Securities Commissioner, Texas State Securities Board, Austin, Texas

Kristina Fausti, Special Counsel, Office of Chief Counsel, SEC Division of Trading and Markets, Washington, D.C.

Shane B. Hansen, Partner, Warner Norcross & Judd LLP, Grand Rapids, Michigan

Mike Ribet, Principal, Focus Capital Advisors, Downers Grove, Illinois

Dennis Roberts, Senior Managing Director, The McLean Group, McLean, Virginia

Private Securities Offerings Breakout Group

Moderator: Brian T. Borders

Securities Regulation of Smaller Public Companies Breakout Group

Moderator: John D. Hogoboom

Tax Breakout Group

Moderator: Dillon J. Taylor

3:30 p.m. Break

3:45 p.m. Continuation of Breakout Group Discussions

4:45 p.m. Plenary Session to Develop Next Steps

Moderators:

Gregory C. Yadley, Partner, Shumaker, Loop & Kendrick, LLP,
Tampa, Florida

Gerald J. Laporte, Chief, Office of Small Business Policy, SEC
Division of Corporation Finance, Washington, D.C.

5:30 p.m. Networking Reception

**TRANSCRIPT OF
OPENING REMARKS OF
CHAIRMAN CHRISTOPHER COX**

SEC Government-Business Forum on Small Business Capital Formation

November 20, 2008

Thank you Gerry [Laporte], very much, for that very generous introduction

This is a splendid panel that we've assembled here this morning. I am delighted to join with Gerry in greeting all of you and welcoming you to what, as he noted, is the 27th Annual Forum on Small Business Capital Formation here at the SEC. It's something that each year we take very, very seriously. We think it's very important, and in fact, our devotion to small business capital formation imbues a great deal of the work that goes on in all of the divisions and offices here at the Securities and Exchange Commission.

I think Gerry also mentioned that, in addition to those of us who are right here in the auditorium, we've got people participating on the Web. We've got people participating on the Web with us through Twitter, and, if you are one of those, I encourage you to submit your questions by e-mail, and we'll try to get to as many of those as we can. The SEC's mission, very formally, is to protect investors, to maintain orderly markets, and to promote capital formation. It's that third leg of our mission that calls us together here today. The economic crisis has centered on a lot of the largest players in the financial world, Fannie and Freddie, AIG, Lehman, WaMu, and now the big three carmakers. The big players are getting a great deal of attention, but this crisis is affecting the entire economy, including small business. I don't need to tell you how rapid and severe the impact of recent events has been. For at least the past two decades, small businesses, which are 99% of all businesses, have bailed us out of every recession, and we are looking to small business to fulfill that role once more.

You have generated between two-thirds and three-quarters of all net new jobs, year-end and year-out, and that is, in relation to your overall size, your relative size, truly over-performing. In 2001, which was probably the most extreme example of this, following the burst of the dot com bubble, small business generated 100% of net new jobs in the United States of America. Backed up with statistics such as that, small business is the engine of growth in America, and America, as always, is counting on you. While the credit crunch is making it difficult for small businesses to get loans for inventory, operations and expansion, your customers at the same time are also feeling the pinch, and yet even today, according to the Small Business Administration with whom we are delighted to be partnering in this event, small firms employ about half of all private sector workers.

You are responsible for 45% of total U.S. payroll, and you've generated, as I said, the lion's share of net new jobs in the United States with that fraction of total resources.

Our success as a country, and as an economy, is therefore inextricably tied to the success of small business, and that's why we here at the SEC are dedicated to ensuring that small businesses continue to have access to capital. If we expect to exit this downturn and re-energize our economy's growth as quickly as possible, we've got to smooth the way for the men and women who are continuing to work, sweat, and take risks and make payroll every week, every month, and every year. While the fashion lately seems to be robbing Peter to pay Paul, we thought it was high time someone started listening to Peter for a change. We're delighted you could all be here. We recognize the financial burden on small business from government is even more serious than it is for larger companies. The smaller the business, the more true that is. Firms with fewer than 20 employees spend 45% more per employee on complying with federal regulations.

We've been reminded once again of the important role that regulation plays in protecting investors and in ensuring a level playing field, and that's particularly important for small business. But that in no way means that the burden of regulation should be allowed to fall disproportionately on small business. So as lawmakers and regulators look to reform the system over the coming months, we've got to ensure that we do everything possible to support the growth and the capital formation of small business.

At the SEC, we've recently taken a number of steps to make it easier for small businesses to comply with SEC regulations. Since June of last year, we've revised the eligibility requirements for primary securities offerings on Forms S-3 and F-3. We've enacted smaller reporting company regulatory relief and simplification. We've revised Rules 144 and 145 with the same objective in mind. We've exempted compensatory employee stock options from registration under Section 12(g) of the '34 Act, and we've offered relief and tailored guidance for smaller companies regarding management's report on internal controls.

As you know, our partners at the SBA have also taken steps to improve small businesses' access to capital. Some of their work includes an interim final rule earlier this month that allows new SBA loans to be made with an alternative base interest rate—the one-month LIBOR rate, in addition to the prime rate, which was previously allowed. That's helping to address the recent disparity between those two rates.

Of course, there's much more that needs to be done; and I know that you all here have a lot of ideas, and we want to hear them, and we want to get to business on them right away. So we're going to turn to that immediately. The morning's agenda features two roundtable panels. The first, on small business capital formation and the current credit crisis, will be moderated by Karen Kerrigan, the President and CEO of the Small Business and Entrepreneurship Council in Oakton, Virginia, and Chad Moutray, the Chief Economist and Director of Economic Research at the Office of Advocacy in the U.S. Small Business Administration. They are going to lead seven distinguished panelists in what promises to be an extraordinarily timely discussion.

The second panel will be at 11 o'clock devoted to current issues in securities regulation for smaller companies. That will be moderated by our own Gerry Laporte,

who is of course Chief of the SEC Office of Small Business Policy in the Division of Corporation Finance, and co-moderated by Steve Bochner, partner at Wilson, Sonsini, Goodrich & Rosati in Palo Alto, California. They will lead another seven distinguished panelists, including our own Bill Lutz, who directs the SEC's 21st Century Disclosure Initiative.

After lunch, we'll reassemble at 2:15 and divide into another panel discussion and breakout groups to develop recommendations. The moderators will include Brian Bussey, Assistant Chief Counsel in the SEC's Division of Trading and Markets, and Greg Yadley, who is a partner at Shumaker, Loop & Kendrick in Tampa, Florida. Then, we'll break at 3:30, following which we will continue discussions until our 4:30 plenary session to develop next steps.

Then, with our work done for the day, I invite you all to join us for a networking reception at B. Smith's Restaurant in Union Station. I would like to thank, anticipatorily, the moderators and all the panelists, as well as everyone who has traveled here, to take part in today's proceedings; and, I'd also like to express my appreciation to the staff of the Division of Corporation Finance for being able to bring together such an impressive cast for today's production. So thank you to all of you.

RECOMMENDATIONS²

Set forth below are the recommendations of the 2008 Government-Business Forum on Small Business Capital Formation. The recommendations of three different securities regulation breakout groups are followed by the recommendations of a single tax issues breakout group. These recommendations were developed in the breakout groups on the afternoon of November 20, 2008. After that date, the breakout group moderators worked with their respective breakout group members to compile, edit and prioritize their recommendations. The recommendations have been prioritized only within each breakout group category.

Recommendations of Securities Regulation Breakout Groups

The three securities regulation breakout groups developed the following 22 securities law recommendations.

Private Placement and M&A Broker-Dealer Breakout Group

In his Opening Remarks to the 2007 forum, Chairman Cox acknowledged the critical importance of small business to the U.S. economy:

- “Small firms represent . . . 99.7% of all the employer firms in the United States. They employ half of the entire labor force in the private sector.
- “Of all the net new jobs created in our country, small business generated between 60 percent and 80 percent in every year during the last decade.
- “[S]mall business makes up 97 percent of all identified exporters. It produces over 28 percent of the nation’s entire export value.
- “[S]mall business employs over 40 percent of all the high-tech workers in the United States.”

In this light, we urge the Commission to implement general recommendation No. 1, and, without further delay, to take the three specific actions in recommendations Nos. 2 through 4:

1. U.S. small business owners are poised to transfer an estimated \$10 trillion worth of business assets in preparation for their retirements. To facilitate these transfers and to assist small business owners in continuing their leading role in job creation,

² The SEC hosts the annual Government-Business Forum on Small Business Capital Formation, but does not seek to endorse or modify any of the forum’s recommendations. The recommendations are solely the responsibility of the forum participants from outside the SEC, who were responsible for developing them. The recommendations do not necessarily reflect the views of the SEC, its Commissioners or any of the SEC’s staff members.

- exports, and technology innovation, we implore the Commission to implement the recommendation of its own Advisory Committee on Smaller Public Companies³ and adopt rules as recommended by the American Bar Association in its “Report and Recommendations of the Task Force on Private Placement Broker-Dealers,” dated June 20, 2005.⁴
2. Allow “private placement brokers” to raise capital through private placements of issuers’ securities with one or more “accredited investors” in amounts per issuer of up to 10 percent of the investor’s net worth (excluding his or her primary residence), with full written disclosure of the broker’s compensation, and in aggregate amounts of up to \$20 million per issuer, periodically adjusted for inflation.
 3. Provide an exemption from the definitions of “broker” and “dealer” for “finders”; recommend to FINRA the adoption of a rule to permit broker-dealer fee-sharing with finders; and coordinate the implementation of these actions with the states.
 4. Take the lead in adopting rules, in coordination with the states, to create a limited federal registration exemption and simplified system of state registration and regulation for merger-and-acquisitions and business brokers who act as intermediaries and advisors in the purchase and sale of existing businesses, and adopt a “small business sale” exemption from federal broker-dealer registration by codifying the SEC staff’s no-action letter *Country Business, Inc.* (Nov. 8, 2006).

Securities Offerings by Private Companies Breakout Group

5. Adopt the Commission’s proposed new Rule 507 of Regulation D establishing a new exemption permitting limited advertising.⁵ Reduce the integration period following the closing of a Rule 507-exempt offering from 90 days (as proposed) to 30 days before a subsequent Rule 506 offering can be undertaken.
6. Adopt Recommendation No. IV.P.5 of the Final Report of the Commission’s Advisory Committee on Smaller Public Companies, dated April 23, 2006, which reads as follows:

³ The Final Report of the SEC Advisory Committee on Smaller Public Companies, dated April 23, 2006, is available on the SEC website at <http://www.sec.gov/info/smallbus/acspc/acspc-finalreport.pdf>.

⁴ Task Force on Private Placement Broker-Dealers, ABA Section of Business Law, *Report and Recommendations of the Task Force on Private Placement Broker-Dealers*, 60 Bus. Lawyer 959-1028 (May 2005), available at http://www.abanet.org/buslaw/tbl/tblonline/2005_060_03/home.shtml#1.

⁵ The Commission proposed Rule 507 in *Revisions of Limited Offering Exemptions in Regulation D*, Release No. 33-8828 (Aug. 3, 2007) [72 FR 45116 (Aug. 10, 2007)]. An adopting release has not yet been acted upon.

Adopt a new private offering exemption from the registration requirements of the Securities Act that does not prohibit general solicitation and advertising for transactions with purchasers who do not need all the protections of the Securities Act's registration requirements. Additionally, relax prohibitions against general solicitation and advertising found in Rule 502(c) under the Securities Act to parallel the "test the waters" model of Rule 254 under that Act.⁶

In regard to the Regulation D proposal, expand upon this concept to accomplish the foregoing recommendation, including giving further consideration to the type of communications that should be permitted in light of the increasing use of the Internet, and whether accredited investors should be allowed to invest in these exempt offerings.

7. Exclude accredited investors, large accredited investors and qualified institutional buyers from the 500 shareholders of record calculation in Section 12(g) under the Securities Exchange Act of 1934 for purposes of becoming a public company.⁷ Investors already determined not to require the protections of registration under the Securities Act should not be included in determining the Section 12(g) threshold necessary for triggering periodic reporting and other obligations under the Securities Exchange Act of 1934, particularly in light of the increasing time period required before a company can achieve a public offering in today's environment.
8. Consider extending Rule 144A beyond qualified institutional buyers. For example, establish a new Rule 144A-type exemption limited to trading among purchasers who do not need the protections of Securities Act registration to provide liquidity for privately placed securities.
9. Shorten the integration safe harbor in Regulation D from six months to 90 days, and consider further the Advisory Committee's recommendation to shorten such period to 30 days.
10. Add the proposed \$750,000 investment-based test as an alternative means of qualifying as an "accredited investor," as defined in Rule 501 of Regulation D, as set forth in the Regulation D proposal.

⁶ Final Report of the SEC Advisory Committee on Smaller Public Companies, note 3 above, at 72.

⁷ The term "accredited investor" is defined in 17 CFR 230.501(a) of Regulation D; the term "large accredited investor" was proposed in the Regulation D proposing release, referred to in note 5 above; and the term "qualified institutional buyer" is defined in 17 CFR 230.144A(a)(1).

Securities Regulation of Smaller Public Companies Breakout Group

11. Eliminate the listed company requirement to determine eligibility status for smaller public companies in General Instruction I.B.6(c) of Form S-3 and General Instruction I.B.5(c) of Form F-3.
12. Eliminate the one-third of market capitalization limit for primary offerings by smaller public companies in General Instruction I.B.6(a) of Form S-3 and General Instruction I.B.5(a) of Form F-3.
13. Permit forward incorporation by reference for all Form S-1 registration statements.
14. Increase the threshold for Section 12(g) registration in Rule 12g-1 from \$10 million to \$100 million.
15. Amend Item 308 of Regulation S-K to exempt all public companies with assets of less than \$100 million from the requirement to provide an attestation report of a registered public accounting firm, as required by Section 404(b) of the Sarbanes-Oxley Act of 2002 (“SOX”).
16. Provide relief to smaller banks and bank holding companies by increasing the Section 12(g) registration thresholds for those entities.
17. Consider all facts and circumstances, without undue reliance on the number of shares being registered, in determining whether Rule 415 offerings are properly characterized as true secondary offerings, or are really primary offerings by selling shareholders who are effectively acting as underwriters selling on behalf of an issuer.
18. Rather than suspend or eliminate “mark-to-market” accounting, provide better guidance on the “other than temporary impairment” criteria that recognizes that even temporary impairments can last longer than 12 to 15 months.
19. Implement the rulemaking proposal on Rule 144(i) requested in the recently submitted petition for rulemaking letter by Feldman Weinstein & Smith *et al.*, dated Oct. 1, 2008.
20. Amend the Instruction to Item 308 of Regulation S-K to apply the one-year grace period for compliance with Section 404 of SOX to reverse merger registrants.
21. Amend or interpret Rule 144(d)(3)(i) so that holders can tack payment-in-kind (PIK) interest back to the date the underlying security is acquired as is currently the case for PIK dividends.

22. Expand the Commission's 21st Century Disclosure Initiative for the disclosure requirements for registrant information to add selected market information, such as ownership information reported by institutional investment managers as filed on Form 13F, the amount of securities registered, aggregate short interest and other relevant market measures.

Recommendations of Tax Issues Breakout Group

The tax issues breakout group developed the following 15 recommendations.

1. Simplify the qualified home office deduction by providing a limited, optional standard home office business deductions. Fifty-three percent of America's small businesses are home-based. The requirements to qualify for and calculate the deduction are confusing for taxpayers and do not account for changes in technology that affect the way business is conducted. Consequently, many at-home workers do not take advantage of the home office business deduction. The Internal Revenue Service National Taxpayer Advocate supports simplification of the home office business deduction.⁸
2. Modernize the "use rules" for a "qualified home office" to permit 20 percent de minimis personal activity in a home office, similar to the personal use that normally occurs in other business and governmental office environments.
3. Remove cell phones and personal computers costing less than \$2,000 from the "listed property" record keeping and reporting requirements of Section 280F of the Internal Revenue Code ("Code"). Since 1986, significant reductions in the initial cost and ongoing expense for these technologies, including common use of "unlimited cell use plans," has effectively eliminated any real marginal cost for non-business use. The record keeping requirements needed to actually comply with the listed property regulations are now unrealistically burdensome on business users, and are commonly ignored, which sets a bad precedent for tax compliance.
4. Modernize the Code Section 280F(a)(1) depreciation limitation on "luxury" automobiles and light trucks to reflect the current average cost of vehicles necessary for normal business use. The inflation adjustment formula specified in the original legislation was flawed by its limitation to basic automobiles like those that existed in 1980s, without allowance for the safety and fuel economy features mandated on current vehicles. This resulted in only a 20% increase in the limit since 1986 even though the general inflation increase during that period was over 90%. The current law limits the cost recovery for a new vehicle over the normal

⁸ See "Legislative Recommendations," Vol. 1, Section Two, National Taxpayer Advocate 2007 Annual Report to Congress, available at http://www.irs.gov/pub/irs-utl/arc_2007_vol_1_legislativerec.pdf.

5-year depreciation period to only \$15,000. The average new car price in 2006 was \$28,450.

5. Equalize the tax deductibility of group health insurance costs for the 21 million “self employed” small businesses that report their business income on IRS Schedule C or F or partnership Schedule K-1. These small entrepreneurs are prohibited from deducting group health insurance premiums as a business expense by Code Section 162(l)(4), and, as a result, pay an extra 15.5% self-employment tax on the cost of their group health insurance premium costs. With many states and the federal government moving toward mandatory health insurance requirements, this tax inequity should be corrected.
6. Equalize the alternative minimum tax (“AMT”) exemption on business income for businesses that report income on a personal tax return with the \$7.5 million, 3-year average gross income exemption that is now given to C corporation business entities, if the reporting individual materially participates in the business. The reporting of business income by S corporations and other entities that report “pass-through” income on the personal return, even when it has to be re-invested back into the business, results in a phase out of the personal AMT exemption, causing the AMT to be assessed at much lower income levels. This results in an inequitable AMT tax impact on the business income that would not apply to a small C corporation business under the same circumstances.
7. Increase the deductible percentage for business meal expenses to 100 percent for small businesses. Small businesses usually do not have tax deductible, on site, conference rooms and client entertainment facilities that are often available to larger businesses. Personal meetings with existing or potential customers at a restaurant are one of the primary methods of client development for small businesses. Limitations could be put on the gross income size of business and the maximum per person amount that would qualify for 100 percent deduction.
8. Permanently reform the estate tax prior to 2010 to provide a unified gift and estate tax exemption of \$5 million per person, indexed for inflation, with a re-valuation of the tax basis of non-cash assets at time of death, and portability of any credit remainder to a spouse. The variation in exemption levels resulting from prior legislation has made estate planning difficult for businesses and individuals. A failure to re-value inherited assets at the time of death, as will occur in 2010 under current law, can create a major capital gains tax burden for descendants, and significant tax determination problems for tax preparers and the IRS.
9. Make permanent the current \$250,000 Code Section 179 small business expensing provisions to stimulate business investment in new equipment and technologies. Small businesses often pay high interest rates to purchase new equipment in order to grow their business and create new jobs. The ability to recover the cost of a limited amount of new investment in the year of purchase,

- rather than over a long depreciation period, can be a critical factor in helping a small business survive and grow.
10. Until there is a consistent and uniform definition of “contingent tax liabilities,” suspend the application to non-public companies of FASB Interpretation No. 48 “Accounting for Uncertainty in Income Taxes – an interpretation of FASB Statement No. 109.”
 11. Congress should set reasonable and equitable standards for state taxation of non-resident businesses. As state governments have experienced revenue shortages, state legislatures have created expanded non-resident business activity taxes that they are trying to impose on national Internet or mail order businesses with no physical nexus in their state. If this is allowed to continue, small businesses could potentially have to calculate and pay one or more taxes in all 50 states. Because many of these state taxes allow credits for taxes paid in other states, they do not create significant net new revenue for all the states combined, but would create a major accounting, tax preparation and potential tax penalty cost for small businesses who are not prepared to deal with this level of complexity.
 12. Whenever Congress requires tax returns or information returns to be filed electronically, Congress should include a provision to allow paper filing or a 10-day automatic “correction period” extension without penalty when a business is unable to file properly an electronic return due to IRS technology or operating limitations.
 13. Congress should enact a tax credit option for direct investment in a qualified small business to encourage investment in small businesses. Code Section 1202 provides a reduction in the capital gain recognized on the sale of stock in a successful qualified small business, but the current lower capital gains rates and AMT impacts have greatly reduced its incentive value. Code Section 1244 also allows taking an ordinary loss on a stock investment in an unsuccessful small business, but neither provision provides any immediate tax incentive at the time of the investment to offset the much higher risk of loss and lack of market liquidity on an investment in small business stock.
 14. Congress should raise the capitalization limit for captive business insurance companies from \$600,000 to \$6 million because of the higher risk limits they need to cover in today’s higher risk environment.
 15. Congress should provide greater economic stimulus for small business job creation and investment by providing a \$100 billion stimulus allocation to the Small Business Administration to be used for increasing SBA loan guarantee amounts and reducing loan fees.

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