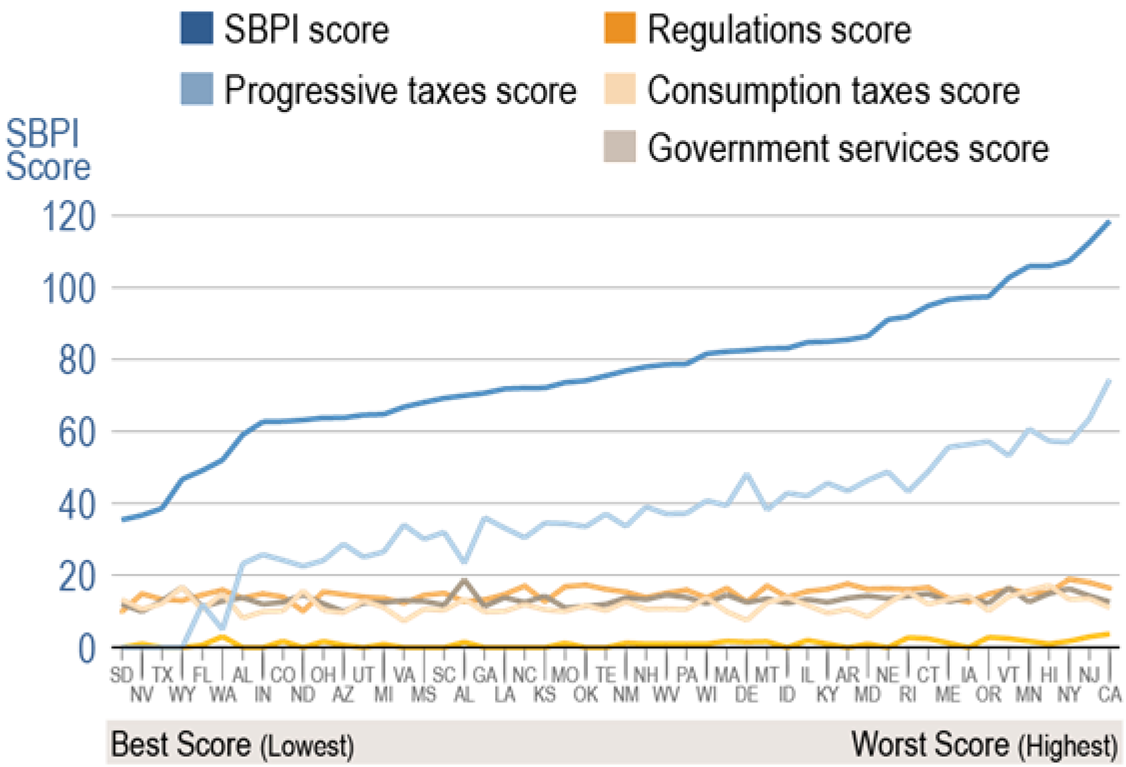
What Drives the SBPI?

The Small Business Policy Index (SBPI) is largely a measure of how much a state taxes or regulates business, and completely disregards the services a state offers businesses. While the index purports to be a measure of how well state government supports small businesses and entrepreneurship, the authors apparently believe that there are in fact no government programs or policies that are supportive as the index consists of 42 measures that are described as “government-imposed or government-related costs impacting small businesses and entrepreneurs.” Infrastructure (other than roads), the education system, small business development centers or entrepreneurship programs at public universities, technology transfer or business extension programs, business-university partnerships, small business incubators, state venture capital funding—none of these state-funded activities is included in the SBPI.

So what really drives the index? That is, which measures have the most influence on whether a state ranks high or low? When we grouped the measures by type, we found 15 dealing with progressive taxation, nine with other taxes (sales, excise, property), three with labor policies, eight with the size of government, and seven with government regulations and other factors. Comparing how each of these groups stacks the states up alongside the SBPI, we find that the 15 variables measuring the progressivity of taxes really drive the overall index. The remaining 27 measures are little more than random noise.

The figure below demonstrates our finding. The 50 states are arranged along the horizontal axis from the best state on the left (South Dakota, with the lowest overall SBPI score) to the worst on the right, with the highest score. The vertical axis shows the number of points awarded for the variables in each of the five groups we created. It is clear that four sets of variables show no tendency to rise along with the total score; the best states rate about the same on these measures as the worst states. The only thing that makes a difference, and that causes some states to rank high and others low in the overall SBPI, is a state’s score on tax progressivity. The result is that the SBPI rates states with regressive taxes high and states with progressive taxes low.

Small Business Policy Index Driven by State Scores on Progressive Taxes



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