THE LAWYER'S ROLE IN HELPING CLOSE THE MINORITY-WHITE GAP IN BUSINESS OWNERSHIP ["MINORITY BUSINESS DEVELOPMENT" OR "MBD"]

FIRST HOUR FOURTH CLASS, 4A & 4B, BRIEF REVIEW OF THE ASSIGNED READINGS RELATING PRINCIPALLY TO THE IMPACT OF COVID ON BUSINESSES, INCLUDING THE PAYCHECK PROTECTION PROGRAM (PPP) UNDER THE CARES ACT

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Class 4A&B, No. 1-7, IMPACT OF COVID ON BUSINESS ACITIVTY, FROM PROFESSOR FAIRLIE, NBER WORKING PAPER, JULY 2020:

- The number of active business owners in the United States plummeted by 3.3 million or 22 percent over the crucial window from February to April 2020.
- The drop in active business owners was the largest on record, and losses to business activity were felt across nearly all industries.
- Whites experienced a 17 percent drop.
- African- American businesses were hit especially hard experiencing a 41 percent drop in business activity.
- Latinx business owner activity fell by 32 percent, and
- Asian business owner activity dropped by 26 percent.
- For comparison, from the start to end of the Great Recession the number of active business owners [experienced] only a 5 percent reduction.

Class 4A&B, No. 1-7, INFORMATION ON THE Paycheck Protection Program (PPP)

- The CARES Act adopted the Paycheck Protection Program (PPP), the purpose of which is to facilitate lending to certain small businesses. There have been two authorizations: First Draw Loans, and Second Draw Loans
- Under the PPP, the Small Business Administration (SBA) through the Federal Reserve Board makes loans to banks and other financial institutions, which in turn make loans to eligible small businesses.
- Thus, banks and other financial institutions act as conduits through which loans from the Fed are passed on as loans to qualifying small businesses.
- In certain cases, the borrower's obligation to repay the PPP loan can be forgiven, which in effect converts the loan into a grant.

Class 4A&B, No. 1-7, INFORMATION ON THE Paycheck Protection Program (PPP)

- There Can be **Full Forgiveness of PPP Loans:**
  - PPP Loans made to eligible borrowers qualify for full loan forgiveness if during the 8- to 24-week covered period following loan disbursement:
    - Employee and compensation levels are maintained;
    - The loan proceeds are spent on payroll costs and other eligible expenses; and
    - At least 60 percent of the proceeds are spent on payroll costs.

Class 4A&B, No. 1-7, INFORMATION ON THE Paycheck Protection Program (PPP)

- Loan terms. In general, borrowers may receive a loan amount of up to 2.5X the average monthly payroll costs in the one year prior to the loan or the calendar year. No loan can be greater than $2 million.
- New entities may receive loans of up to 2.5X the sum of average monthly payroll costs.
- Entities in the Accommodation and Food Services industries may receive loans of up to 3.5X average monthly payroll costs.
- Fees are waived for both borrowers and lenders to encourage participation.
- For loans of not more than $150,000, the entity may submit a certification attesting that the entity meets the revenue loss requirements on or before the date the entity submits their loan forgiveness application.

Class 4A&B, No. 1-7, INFORMATION ON THE Paycheck Protection Program (PPP)

- A Jan 2021 NBER paper by Prof Fairlie addresses the following question:
- Is there evidence that the unprecedented federal government response to help small businesses – the $659 billion Paycheck Protection Program (PPP) and the related $220 billion COVID-19 Economic Injury Disaster Loans (EIDL) – which had a stated goal of helping disadvantaged groups, was disbursed evenly to minority communities?
- In answering this question, he concludes: [See next page]

Class 4A&B, No. 1-7, INFORMATION ON THE Paycheck Protection Program (PPP)

In answering the previous question, Professor Fairlie concludes:

- We generally find a slightly positive relationship between PPP loan receipt per business and the minority share of the population or businesses,
- [However] funds flowed to minority communities later than to communities with lower minority shares.
- Focusing on PPP loan amount per employee we find a negative relationship with minority share of the population.
- Economic Injury Disaster Loans (EIDL) (which are designed to provide economic relief to businesses that are currently experiencing a temporary loss of revenue due to COVID-19) in both number and amounts, were provided positively to minority communities. We find a strong positive relationship in the receipt of these loans and advances by the minority share of the population.

Class 4A&B, No. 1-7, INFORMATION ON THE Paycheck Protection Program (PPP)

The New York Times reports that the National Community Reinvestment Coalition found that:

- White bank customers were told more frequently than Black customers that they would qualify for a loan.
- Male customers who were either Black or white were told they would qualify for loans more frequently than female customers who fell into either category.
- Not a single Black female customer was encouraged to apply for a loan by having an employee assure her she would qualify.
- Black customers were also offered different products. In one case, a white customer was offered not just a P.P.P. loan but also a $100,000 business line of credit. The Black customer who visited the same bank and presented the same overall borrower profile was not offered the additional line of credit.

Class 4A&B, No. 8, INTERVIEW WITH THOMAS PEKETTY, NEW YORK MAGAZINE, APRIL 27, 2021

- PEKETTY IS AUTHOR OF (1) CAPITAL IN THE TWENTY-FIRST CENTURY, AND (2) CAPITAL AND IDEOLOGY, WHERE HE FOCUSES ON INEQUALITY
- PEKETTY WAS FIRST INTRODUCED IN CLASS 2 OF THIS COURSE; THE FOLLOWING ARE SOME OF HIS RECENT OBSERVATIONS ON INEQUALITY
- **Question: We've heard about Denmark covering75% of unemployed workers' salaries. When you look around the spectrum of responses, from the American response to the French, British, or Danish response, who is doing the best there?**
  Peketty's Answer: Well, it's difficult to say. But certainly the U.S. is probably doing the worst.

Class 4A&B, No. 8, INTERVIEW WITH THOMAS PEKETTY, NEW YORK MAGAZINE, APRIL 27, 2021

- **<u>Question</u>: In your new book, you call your preferred approach to these issues "participatory socialism." [The approach involves progressive taxation of wealth and capital endowments for all citizens.] What would a participatory socialist response to this crisis be?**
- <u>Peketty's Answer</u>: Less inequality and more access to economic opportunities, economic participation, economic power, and participation in decision-making.
- The bottom 50 percent of the population in the U.S. owns less than 2 percent of total wealth. It used to be 3 or 4 percent 20 years ago; now it's less than 2 percent. It's always been very small, in any case, but it's not going in the right direction.
- This has all sorts of bad consequences in terms of how you can plan your own life. These consequences are particularly clear at a time when you don't have a job and basically when you have no wealth. You need to accept any job. . . . So the question is: Is 2 percent of total wealth for the bottom 50 percent the best we can do? Or is it possible to think of another economic system, keeping the good aspects of the current system, but trying to do better? [Continued]

Class 4A&B, No. 8, INTERVIEW WITH THOMAS PEKETTY, NEW YORK MAGAZINE, APRIL 27, 2021

- **<u>Question</u>: In your new book, you call your preferred approach to these issues "participatory socialism." [The approach involves progressive taxation of wealth and capital endowments for all citizens.] What would a participatory socialist response to this crisis be? [Continuing from previous page]**
- <u>Peketty's Answer [Progressive Wealth Taxation]</u>: The very basic idea of participatory socialism is to say, "Well, look, if we want to improve that, one way is to have a more progressive tax system.
- So lower tax on people who are trying to access properties. People who have a lot of debt should pay less taxes. And people who are not in debt should pay more taxes." [Continued]

Class 4A&B, No. 8, INTERVIEW WITH THOMAS PEKETTY, NEW YORK MAGAZINE, APRIL 27, 2021

- **<u>Question</u>: In your new book, you call your preferred approach to these issues "participatory socialism." [The approach involves progressive taxation of wealth and capital endowments for all citizens.] What would a participatory socialist response to this crisis be? [Continuing from previous page]**
- <u>Peketty's Answer [Progressive Wealth Taxation]</u>: ** *
- What I'm proposing under the label of participatory socialism is to use the proceeds from this progressive tax to finance something.
- The people who now receive zero inheritance, who are basically the bottom 60 percent of population, will receive €120,000 or $150,000. In order to pay for that, people who now receive $1 million in inheritance would receive $600,000 or $650,000.
- So you will still have a lot of inequality between children — and if you want my opinion, I think we could go further than that — but this already will make a huge difference because this could put everybody roughly at the median wealth.
- Basically, it's an extension of what has been done in terms of progressive taxation.

Class 4A&B, No. 8, PROFESSOR THOMPSON'S REACTION TO THE PEKETTY INTERVIEW, IN THE NEW YORK MAGAZINE, APRIL 27, 2021

- **A HYPO BY PROF THOMPSON ILLUSTRATING (1) THE IMPACT OF ECONOMIC INEQUALITY, AND (2) THE NEED FOR BOTH (a) A PROGRESSIVE INCOME TAX, AND (b) A PROGRESSIVE WEALTH TAX TO REVERSE GROWING INEQUALITY, DRAFT FEB 1, 2021**
- Assume that there are two people in Country X: Capitalist, and Entrepreneur.
- Capitalist has $100M, which is the only money in Country X.
- Entrepreneur has a great idea for building and selling a Widget, which will costs $100M in payments to third parties who are not in Country X, and Entrepreneur expects to sell the Widget to someone outside of Country X for $108M.
- Entrepreneur approaches Capitalist for a $100M loan, which Capitalist, after reviewing Entrepreneur's business plan, makes to Entrepreneur.
- Entrepreneur uses the loan efficiently and builds the Widget for a costs of $100M, which is paid to workers and providers of materials who are outside of Country X.
- Entrepreneur then sells the Widget for $108M to Purchaser, who is located outside of Country X. [Continued]

Class 4A&B, No. 8, INTERVIEW WITH THOMAS PEKETTY, NEW YORK MAGAZINE, APRIL 27, 2021

- **[Professor Thompson's Hypo Continuing from the Previous Slide]**
- Entrepreneur uses the $108M from the sale to pay to Capitalist the principal of the loan, which is $100M, plus the $5M in interest. Consequently, Entrepreneur has $3M left over, which is his profit, or the growth in the economy.
- Note that Entrepreneur has done well for herself because she has gone from having zero wealth before the transaction to $3M in wealth after the transaction. So, it is a positive transaction from the perspective of Entrepreneur. Also, it is a positive transaction from the perspective of Capitalist.
- From the perspective of the whole economy of Country X, when the dust settles before any taxes or consumption, Capitalist has grown his capital to $105M, and Entrepreneur has grown her capital by the $3M earnings.
- Thus, the return of capital (r) of $5M has exceeded the earnings of Entrepreneur or growth (e) in the economy of $3M. [Continued]

Class 4A&B, No. 8, INTERVIEW WITH THOMAS PEKETTY, NEW YORK MAGAZINE, APRIL 27, 2021

- **[Professor Thompson's Hypo Continuing from the Previous Slide]**
- As long as in repeat transactions the 5% return of the Capitalist exceeds the Entrepreneur's profit, which is the growth in the economy, the Entrepreneur can never catch up in wealth, and there will be a growing inequality in wealth.
- It should be noted the growing inequality in wealth could be slowed by a significantly progressive income tax that taxed the Capitalist's interest of $5M at a higher rate than the tax on the Entrepreneur's $3M of earnings. And, the growing inequality could easily be reversed by a small wealth tax of, for example, 2% of wealth above a certain limit, such as $10M of wealth.
- As a general matter, assuming that (1) the benefit from the expenditures of the tax revenues was realized proportionately by Capitalist and Entrepreneur, and (2) both Capitalist and Entrepreneur saved all of their after-tax earnings, to reverse the growing inequality in wealth, the combined income and wealth taxes on Capitalist would have to be greater than the after-tax earnings of Entrepreneur. In such case, in time, Entrepreneur's capital would grow to the same size of the capital of Capitalist. [Continued]

Class 4A&B, No. 8, INTERVIEW WITH THOMAS PEKETTY, NEW YORK MAGAZINE, APRIL 27, 2021

- **[Professor Thompson's Hypo Continuing from the Previous Slide]**
- This hypo shows the importance of wealth taxes in addressing the inequality in Country X. The job cannot be done with progressive income taxes only.
- **Sam's comment:** The most important thing the hypo says to me is that in order to get serious about inequality in the US, it is absolutely necessary to make the Federal Estate and Gift taxes, which are wealth taxes, much more robust and less susceptible to abuse. Even though I am a tax lawyer and strong supporter of a progressive income tax, only after thinking about this inequality problem have I appreciated the necessity for an effective Federal Estate and Gift tax to help close the wealth gap.

Class 4A&B, No. 9-13, TESTIMONY IN U.S. HOUSE RE SMALL BUSINESS AND COVID, FEB 4, 2021

- INTRODUCTION: On Feb 4, 2021, Hearings were held before the Small Business Committee of the U.S. House or Representatives regarding: State of the Small Business Economy in the Era of COVID-19
- Testimony was given by
  - Robert Fairlie, Professor of Economics, U.C. Santa Cruz,
  - Karen Kerrigan, President, Small Business & Entrepreneurship Council
  - Steven Schoaps, Owner of a Small Two Screen Movie Theater
  - Sharon Pinder, President, Minority Supplier Development Council
- The following slides present some of the highlights of the testimony.

Class 4A&B, No. 9-13, TESTIMONY IN U.S. HOUSE RE SMALL BUSINESS AND COVID, FEB 4, 2021

- FAIRLIE TESTIMONY:
- The number of active business owners in the U.S. plummeted by 3.3 million or 22 percent over the crucial two-month window from February to April 2020. No other one-, two- or even 12-month window of time has ever shown such a large change in business activity. For comparison, from the start to the end of the Great Recession the number of active business owners dropped by only 5 percent.
- Recent Census Bureau surveys indicate that only 15-20 percent of small businesses have enough cash on hand to cover 3 months of operations. [Continued]

Class 4A&B, No. 9-13, TESTIMONY IN U.S. HOUSE RE SMALL BUSINESS AND COVID, FEB 4, 2021

- FAIRLIE TESTIMONY: [**Continuing from the Previous Slide]**
- [W]e found that funding from [the PPP and EDIL] programs both flowed to minority communities and away from minority communities.
- If anything we found a slightly positive relationship between PPP loan receipt per business and the minority share of the population.
- There is some evidence, however, that the first round of funds was disproportionately distributed to non-minority communities and the second round of funds was disproportionately distributed to minority communities.
- When focusing on PPP loan amounts per employee, however, we find a negative relationship with minority communities.
- In contrast, EIDL loans and advances, in both number and amounts, were provided to minority communities. [Continued]

Class 4A&B, No. 9-13, TESTIMONY IN U.S. HOUSE RE SMALL BUSINESS AND COVID, FEB 4, 2021

- FAIRLIE TESTIMONY: [**Continuing from the Previous Slide]**
- **Vulnerable Groups**. The losses . . . are especially alarming for two vulnerable groups, African-Americans and Latinx. Prior to the pandemic, business ownership as a share of the population and average revenues per business were already low for both groups.
- But, perhaps more importantly there is **a huge wealth gap**.
- Half of black families in the U.S. have less than $10,000 in total wealth and half of Latinx families have less than $25,000 in total wealth.
- White levels of wealth are 7 to 18 times higher.
- Many minority business owners will simply not have the financial resources to weather prolonged closures. [Continued]

Class 4A&B, No. 9-13, TESTIMONY IN U.S. HOUSE RE SMALL BUSINESS AND COVID, FEB 4, 2021

- FAIRLIE TESTIMONY: [**Continuing from the Previous Slide]**
- In closing, we need to reverse the negative impacts of the pandemic on minority-owned businesses.
- These losses are problematic for broader racial inequality because of the importance of small businesses for local job creation, economic advancement, and longer-term wealth gaps.
- Losses from the pandemic are also very costly to total U.S. productivity as minority-owned businesses represent the fastest growing segment of the business population.
- Finally, we will lose the vibrant downtowns with diverse restaurants and shops that truly make America great.

Class 4A&B, No. 9-13, TESTIMONY IN U.S. HOUSE RE SMALL BUSINESS AND COVID, FEB 4, 2021

- KERRIGAN TESTIMONY:
- Unfortunately, according to **Opportunity Insights Economic Tracker** (a project of Harvard University, Brown University and the Bill & Melinda Gates Foundation), as of December 31, 2020, the number of small businesses [openings] **decreased nearly 30%** compared to January 2020.
- An average of 74.6% of small businesses requested a PPP loan from the start of the program in March 2020, and 73.6% reported receiving a PPP loan.
- An average of 25.9% of small businesses requested EIDL assistance, and 23.4% report receiving a loan.
- At this point in time, 17.1% report that they requested SBA loan assistance and 11.8% received that assistance.

Class 4A&B, No. 9-13, TESTIMONY IN U.S. HOUSE RE SMALL BUSINESS AND COVID, FEB 4, 2021

- SCHOAPS' TESTIMONY:
- The pandemic has basically wiped out our business.
- 75% of movie theatres will be insolvent before Spring unless they receive financial aid.
- 95% have experienced revenue losses greater than 70%.
- Nationwide, 63% of jobs in theaters have been lost do furlough or permanent layoff.

Class 4A&B, No. 9-13, TESTIMONY IN U.S. HOUSE RE SMALL BUSINESS AND COVID, FEB 4, 2021

- PINDER'S TESTIMONY:
- We've all heard that when America catches a cold, minorities catch pneumonia. Well, it's now worst. America has COVID-19 and both minorities and their businesses are dying at dramatic rates. Just like many minority individuals have pre-existing health conditions, most minority businesses have faced pre-existing discriminatory conditions that show up in access to capital, opportunities, mentorship, and technical training.
- The COVID-19 crisis is affecting small businesses across the board. There are 1.1 million minority-owned employing more than 6.3 million people, generate more than $1.8 trillion in revenue annually. Women own nearly 300,000 of them, employing 2.4 million workers. [Continued]

Class 4A&B, No. 9-13, TESTIMONY IN U.S. HOUSE RE SMALL BUSINESS AND COVID, FEB 4, 2021

- PINDER'S TESTIMONY [**Continuing from the Previous Slide]**
- COVID-19 disproportionately affects minority-owned small businesses for two critical reasons:
  - They tend to face underlying issues (business co-morbidities) that make it harder to run and scale successfully, and
  - They are more likely to be concentrated in the service and health industries most affected by the pandemic.
- Rick Wade, from the US Chamber of Commerce, commented on CNN, "racial equality is a national imperative and a matter of American competitiveness."
- THE END