



WORK, ENTREPRENEURSHIP, AND OPPORTUNITY IN 21st CENTURY AMERICA

A Special Report From the

U.S. CHAMBER OF COMMERCE

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America's Entrepreneurial Workforce

This report documents a development in the U.S. economy that is both exciting and challenging—the rise of what we call America's entrepreneurial workforce.

Traditional employment remains strong in our economy, and more Americans work in these jobs than ever before. Yet participants in the entrepreneurial workforce have cast aside the traditional model of working for one employer, for one paycheck, and on a set schedule that never changes.

Responding to new economic, technological, and social conditions, millions of workers and companies are instead making alternative arrangements and are seeking different opportunities. These arrangements assume a variety of forms including flex time, telecommuting, independent contracting, working as a temp or on an on-call basis, home-based businesses, and starting a small business full time.

While some may be pushed into the ranks of this workforce due to employer cutbacks, the great majority appear to be willing—even enthusiastic—participants. They choose entrepreneurial work to maximize wealth potential, to better balance the responsibilities of work and family, or to improve career satisfaction.

Some segments of the entrepreneurial workforce have seen substantial growth, particularly independent contracting. There are now an estimated 10.3 million independent contractors in the United States, making up 7.4% of the workforce. Small business startups, especially those created by women and minority Americans, are also increasing at an impressive pace.

Workers and companies must be free to create and select from a wide range of business solutions and working arrangements to meet the demands of today's marketplace.

The growth of the entrepreneurial workforce has triggered some resistance from those with a vested interest in perpetuating the status quo. Some union leaders, trial lawyers, and disgruntled workers have launched attacks on independent contracting and other innovative work arrangements.

If successful, these attacks will hurt, not help, our workers and our economy. The better approach is to help Americans seize the economic opportunities created by our evolving and expanding marketplace. Governments need to adjust outmoded rules designed for an earlier economic era, ensuring that there is flexibility in our regulatory systems. Workers and companies must be free to create and select from a wide range of business solutions to meet the demands of today's highly competitive global economy.

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Entrepreneurial Workers— the Economic Backdrop

The reason why millions of Americans are empowered to participate in alternative work arrangements, start small businesses, or strike out on their own is because our economy is free, flexible, and resilient. It rewards those who work hard, take risks, create innovations, and embrace change. The rise of the entrepreneurial workforce is not borne from economic weakness but rather from impressive strength.

Even as the entrepreneurial workforce grows, traditional employment remains strong.

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Since the 2001 economic downturn, the U.S. economy has consistently registered 3.5% to 4.0% growth, with unemployment dropping to 4.7%—a far better performance than in most major developed economies. France and Germany, for example, have double-digit rates of unemployment, caused in large part by the inflexibility of their labor markets.

Consumer spending, which accounts for two-thirds of the economy, has remained solid. More than 2.1 million new jobs have been created between March 2005 and March 2006—and almost 5 million since August 2003. A strong housing market and record levels of home ownership have pushed household incomes to an all-time high.

Some features of traditional jobs are under strain—such as employer-sponsored health insurance and pensions. However, despite rising costs, companies maintain a strong commitment to a broad range of benefits, including health insurance, retirement plans, and paid time off. According to the *2005 Employee Benefits Study* by the United States Chamber of Commerce, employers allocated 40.2% of payroll expenses to employee benefits in 2004.

Yet the pace of change in a rapidly globalizing economy has also created uncertainties and anxieties for many Americans. The rising cost of energy and health care, uncertainty about private pensions, increasing international competition, corporate restructuring, and fears of terrorism have caused many citizens to be concerned about their personal and financial security.

While it is small comfort to the worker who is involuntarily displaced by economic change, such change is nothing new. In the U.S. economy, jobs begin and end, companies come and go, and industries rise and fall. This constant churning is not unusual as upward of 1 million Americans lose, change, or gain jobs in a single month. Globalization, advancing technologies, and worldwide competition have only accelerated this process, but this activity is all within normal ranges for our healthy, vibrant economy. Nevertheless, it is important that displaced workers receive adequate support and retraining. And it is critical that the American economy maintain the freedom and flexibility that workers and companies need to adapt and excel in an ever-changing, competitive environment.

Unfortunately, some laws that govern the workplace have failed to keep pace with new alternatives and realities. For example, wage and hour laws presume a fixed, traditional 40-hour work week, even when it is inconsistent with contemporary, mobile work locations and communication technologies. Going forward, regulators and policymakers must ensure that our free enterprise system and the labor market that powers it are freed of the impediments and rigidities that have severely stifled growth and progress in some European Union economies.

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Despite the obstacles, millions of Americans are already embracing entrepreneurship by running their own small businesses, through independent contracting, or direct selling.

These work arrangements have flourished in the midst of a relatively healthy economy and strong traditional employment. While some may be drawn to alternative arrangements because of job and benefit cutbacks, the reasons for the growth and popularity of entrepreneurial work relationships have more to do with the financial opportunity, schedule flexibility, and independence they offer.

Sizing Up the Entrepreneurial Workforce

It is difficult to precisely define and aggregate what we have termed “the entrepreneurial workforce.” Many Americans maintain both a regular job and run a small home-based business on the side. Others are in a standard employment relationship but perform professional tasks at home. Some are small business owners, but having incorporated their businesses, they are counted in government statistics as “employees.” Despite this imprecision, we can nonetheless identify major characteristics and categories that comprise the entrepreneurial workforce.

Alternatives Within Traditional Employment ...

- ★ More than 27 million full-time wage and salary workers have flexible schedules that allow them to vary the time they begin or end their workday. These workers make up 27.5% of the full-time wage and salary workforce, according to the Bureau of Labor Statistics (BLS) in a May 2004 report.
- ★ Nearly 20 million Americans—one in six workers—work from home at least once a week. Seventy percent of these telecommuters work for companies, government, or other employers while 30% are self-employed, according to the Economic Policy Foundation.
- ★ More than 17 million Americans are engaged in direct selling of products for companies like Avon and Amway, with many operating home-based businesses while maintaining their regular jobs, the Direct Selling Association reports.
- ★ Nearly 25 million Americans work less than full time—17% of the current workforce. Only a small percentage indicated that their part-time status was due to the inability to find full-time work, according to BLS.

Flexible Work Arrangements in the United States

- ★ 27 million workers have flexible schedules.
- ★ 20 million work from home at least once a week.
- ★ 17 million are engaged in direct selling of products.
- ★ Nearly 25 million choose to work less than full time.

Contingent and Alternative Employment ...

Our economy also supports groups of workers who fall outside traditional employment models and participate in contingent and alternative arrangements. In its survey *Contingent and Alternative Employment Arrangements, February 2005*, BLS reports that there were

- ★ 5.7 million contingent workers, accounting for 4.1% of total employment (contingent workers are those who do not expect their jobs to last or who describe their jobs as temporary),
- ★ 10.3 million independent contractors (7.4% of total employment),
- ★ 2.5 million on-call workers (1.8% of total employment),
- ★ 1.2 million temporary help agency workers (0.9% of total employment), and
- ★ 813,000 workers provided by contract firms (0.6% of total employment).

Contingent and Alternative Employment in the United States as of February 2005

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Small Business Owners and the Self-Employed ...

- ★ As of 2004, there were approximately 24.7 million businesses in the United States—and 99.7% were small businesses, according to the U.S. Small Business Administration (SBA).
- ★ SBA reports that small firms employ half of all private sector employees, pay 45% of the total U.S. private payroll, and have generated 60% to 80% of net new jobs annually over the last decade.
- ★ According to 2003 SBA data, 18.6 million small firms were without employees. And 53% were home-based businesses, underscoring the entrepreneurial structure of this vibrant sector of our economy.
- ★ There are more than 767,000 franchised businesses in the United States, according to the International Franchise Association.
- ★ In November 2005, 10.2 million Americans identified themselves as self-employed—7.2% of the employed workforce, according to BLS.

The Entrepreneurial Workforce—a Growth Model?

Government statistics measuring the self-employed indicate little overall change over the past 25 years. However, such calculations do not account for the growth of alternative work arrangements within the context of traditional employment, such as flexible schedules and telecommuting. The Congressional Research Service (CRS) reports, for example, that during the 1990s the proportion of full-time wage and salary workers with flexible schedules almost doubled.

Statistics alone cannot measure the impact of high-speed information technologies that enable growing numbers of Americans to work at home or away from the office or efficiently manage small consulting, freelance, and direct sales businesses on the side. Nor can these statistics delineate heightened entrepreneurial activity among certain segments of the population. A growing number of older workers and new mothers, for instance, are remaining in the workforce because of the

opportunities provided by flexible and part-time schedules as well as by independent contracting. According to the U.S. Census Bureau, there has also been exponential growth in small business ownership among women and minorities.

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Signs of change and growth in the ways that Americans work can be seen in the U.S. staffing industry and in the heavy use of offshore workers, according to the American Staffing Association. The staffing industry boasts 6,000 firms that employed 2.8 million workers in the third quarter

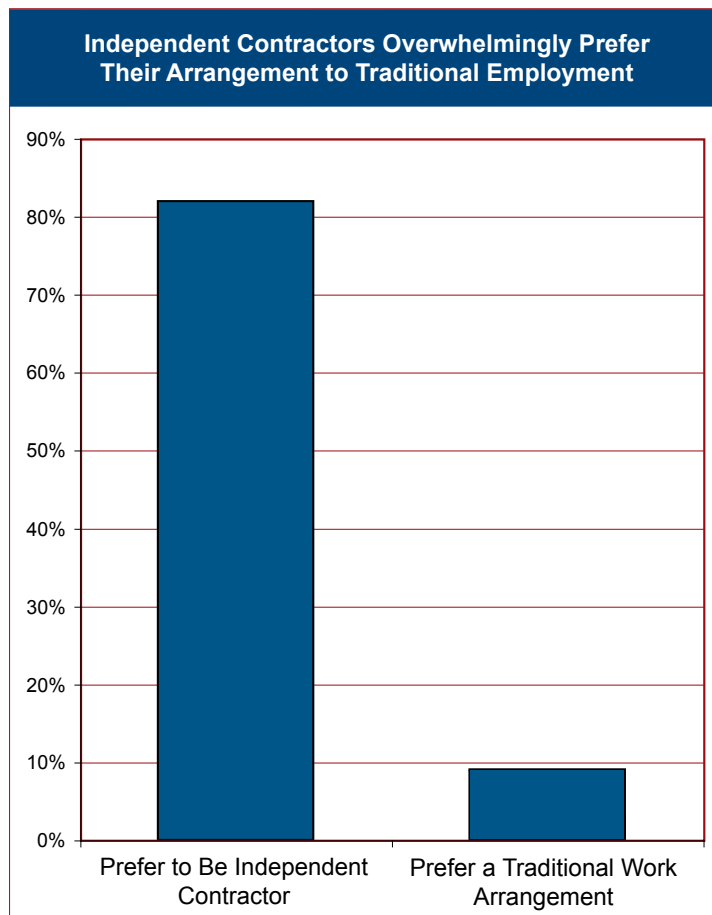
of 2005 (a 7.1% increase from the previous year) and reported 12 consecutive quarters of positive year-over-year growth. Additionally, U.S. firms engage the services of 900,000 offshore workers, a number that is expected to grow to 2.3 million by 2008.

Independent contractors are the largest segment of the entrepreneurial workforce and the one where government statistics show substantial, measurable growth. Approximately 10.3 million Americans are employed as independent contractors, representing 7.4% of all employed persons. This is up from 6.4% just five years ago, according to the BLS February 2005 survey.

BLS reports that median weekly earnings for independent contractors are \$719. Although BLS no longer calculates earnings for the traditional workforce precisely in this manner, it is interesting to note that in February 2006 mean hourly earnings in private industry stood at \$17.25 and mean weekly hours at 35.6. This amounts to \$614.10 for a week's earnings.

Moreover, independent contractors tend to be older, highly educated people who work in relatively high-paying management, business, and financial operations occupations. Six-figure incomes among these contractors are not uncommon. Further, BLS indicates that 82% of independent contractors prefer their arrangement to traditional employment, and less than 10% say that they would prefer a traditional work arrangement.

Whatever parameters are used to define and measure components of the entrepreneurial workforce, these workers are a significant and expanding force in our economy. And while the entrepreneurial workforce is growing and strengthening, the concept of a unionized workforce is weakening. The percentage of private sector workers in unions has dropped to 7.9%, the lowest rate in more than a century.

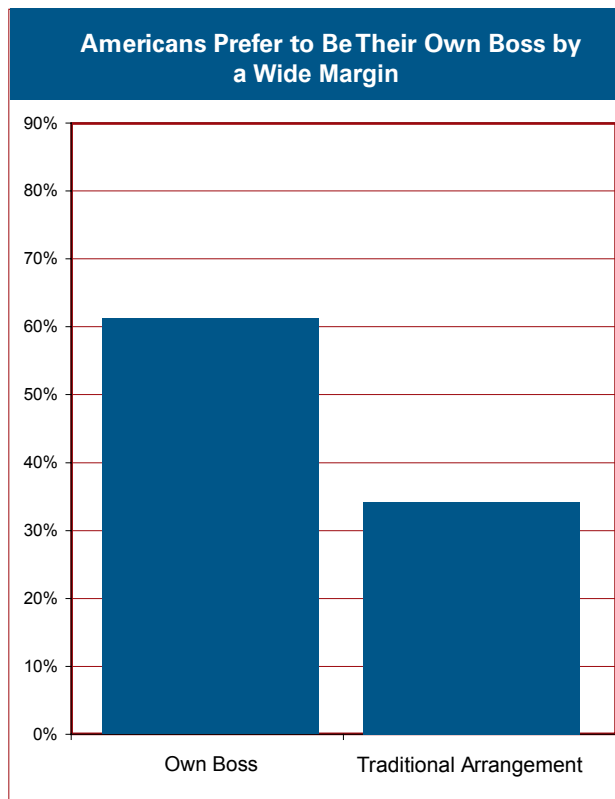


Source: BLS

Advantages and Challenges for the Entrepreneurial Workforce

Being a part of or engaging the services of America's entrepreneurial workforce carries distinct advantages for both workers and companies. For workers, there is the opportunity to be one's own boss, exerting greater control over time and daily activities; building equity and wealth in equipment, customer base, and good will; spending less time commuting, attending meetings, and participating in bureaucratic chores; and better balancing family and work life. Perhaps the biggest advantage for entrepreneurs is the opportunity to grow and expand their businesses as they choose, ensuring greater financial security for themselves and their families. The advantages are not lost on Americans who, in a 2005 EOS Gallup Europe survey, demonstrated an overwhelming preference (61% to 34%) to be their own boss.

For companies utilizing the entrepreneurial workforce, advantages include adjusting quickly to marketplace demands; moving nimbly into new lines of business; and paying more for skill and productivity and less for overhead by shedding the bureaucracy and management expenses associated with having too many full-time employees. The advantages can be especially attractive for small businesses.



Source: EOS Gallup Europe

However, entrepreneurial work is not for everyone. It comes with factors that some see as disadvantages. Some workers prefer the stability, security, and structured environment of traditional employment. Likewise, many companies find that full-time traditional employees are more engaged in the core mission, have a stronger commitment to the team, and are more imbued with the values and culture of the organization.

The good news is that those who prefer the traditional employment relationship, employees and companies alike, remain free to choose that relationship. The expansion and growth of the independent contractor and other models simply provide greater choice for those who prefer to work in an alternative arrangement.

The Question of Pay and Benefits ...

BLS statistics indicate that some groups of entrepreneurial workers—particularly independent contractors (the largest category recognized in government surveys)—earn more than the workforce as a whole. In contrast, because they are often younger and less educated, temporary and on-call workers earn less. The area where traditional employment offers the most advantages, though, is benefits. Traditional employers have become a primary source for most employees' health care and retirement benefits.

Even so, health coverage and pension benefits are widely available to entrepreneurial workers. Using 2001 data, the CRS estimates that 80.1% of workers provided by contract companies have health insurance coverage secured through their employers or on their own. Independent contractors came in second with 72.5%. In addition, 38.4% of independent contractors had established individual retirement accounts or Keogh plans.

Because many companies are finding recent double-digit price increases for benefits too much to bear, they are forced to pass on higher costs to employees, restructure coverage, or, in some cases, leave the benefits market altogether. As some traditional employers reduce coverage, it is likely that over time the benefits advantage enjoyed by traditional employees over entrepreneurial workers will diminish.

Many believe that the cost of benefits is pushing employers toward using more independent contractors. However, data compiled by the Employment Policy Foundation found that the desire to control benefit costs is typically one of the least important reasons why firms hire independent contractors. And a Conference Board survey cited by the foundation found that the two most frequently cited reasons for hiring contingent workers were “flexibility to meet demand fluc-

tuations” (81%) and to “acquire specific expertise” (48%). Only 12% mentioned “controlling benefit costs” as a reason. Despite suspicions of a business strategy to “fire” employees and bring them back as contractors, thus avoiding benefits and taxes, BLS data indicate that only about 8.5% of independent contractors reported that they had previously been an employee of their current clients.

Many of the common assumptions about contingent and alternative workers are challenged by the actual numbers. In reality, they are often paid more than their traditional employee counterparts, and most have access to health care and individual retirement plans.

Attacks on Entrepreneurial Work

Despite the advantages for millions of Americans, innovative workplace relationships have historically come under criticism and attack. As the most visible and rapidly growing segment of the entrepreneurial workforce, independent contracting is today the most frequent target of such attacks. These attacks seek to reclassify independent contractors as employees, returning them to the same employer-employee relationship that they rejected. If successful, such attacks could result in many people being forced back into traditional employment relationships and deprived of the opportunity to operate and grow their own small businesses in the industry of their choosing.

Despite the advantages for millions of Americans, innovative workplace relationships have historically come under criticism and attack.

The growth of independent contracting is not the only economic innovation that has come under attack by those with a fear of or vested interest in preventing change. Business and labor history are replete with examples of such resistance.

The franchising and direct selling industries were strongly challenged during their infancy. Today, these business models support the work of tens of millions of people worldwide. Since the mid-nineties, attempts to give more flexibility to employees in the form of flex time and comp time—driven by pressures on families—have been under attack by unions. Further, the growth of global sourcing has drawn numerous proposals to punish companies that choose to engage offshore workers. Anti-sourcing advocates ignore the fact that the U.S. insources more jobs than it outsources, enjoys a substantial trade surplus in services, and is continually urging other nations to open their markets and level the playing field for government contracts.

Current attacks on independent contracting can be seen as a continuation of a history of resistance to economic change and flexibility. Some opponents of independent contracting are exploiting a complex array of laws, regulations, court precedents, and tax agency rulings that can make the classification of workers as either employees or independent contractors open to varying judgments and interpretations.

Existing worker classification rules are complicated, confusing, and subjective. The employment relationship, including the definition of the terms “employer” and “employee,” is defined in a variety of ways (including some that conflict) under federal and state statutes.

In fact, many states have their own tests that tend to significantly broaden the employee classification, thereby restricting those who can be classified as independent contractors—even when they desire to work as a contractor. Many claims of wrongful classification originate before state authorities where preliminary judgments can be used as fodder for litigation and plaintiff organizing campaigns on the part of class action trial lawyers.

For companies and workers alike, it is important to understand whether a worker is classified as an “employee” or as an “independent contractor.” If a worker is an employee, the employer is obliged to withhold income tax, pay Social Security and Medicare taxes, and make available benefits offered to other employees. The worker is required to work according to the company’s schedule, likely have limited control over his or her individual financial opportunity, and not free to grow his or her business as desired.

Existing worker classification rules are complicated, confusing, and subjective.

Thus, significant consequences for the employer and worker flow directly from the classification of the worker as either an employee or independent contractor. These consequences can prevent both parties from operating and growing their respective businesses should they be impacted by an inconsistent ruling or attack from a trial lawyer.

While the promulgation of clear and simple classification criteria is worthy of support, this must be accomplished without harming those businesses that have operated successfully under the current law for more than two decades. Clearer classification guidelines—either statutory or regulatory—should include improved resolution of classification disputes and better training for IRS examiners.

Thus, the laws regarding classification of workers should honor principles of ownership and equity and be flexible enough to allow people the choice to work in alternative arrangements, as decided by them, not by the government.

Preserving the American Advantage

Entrepreneurship and the independence that come with owning a business and being one's own boss remain our country's distinct advantage. It explains our vibrancy, creativity, resiliency, and growth. Indeed, it helps explain why millions of people seek to immigrate to America every year.

Entrepreneurship is not an easy path, and it is not for everyone. But it is an exciting path, and where it thrives it will define successful economies in the 21st century. Entrepreneurial work arrangements, while not without challenges, offer many Americans their best opportunities to be successful participants and equity stakeholders in the economy of the future.

Small business entrepreneurs need flexibility, especially in the use of their own labor and access to others to succeed. Nearly all experts agree that labor market rigidity is a major contributor to double-digit rates of unemployment in France and Germany. Overregulation of small enterprises in those countries stifles entrepreneurship and innovation. Our country enjoys three times the growth and has less than half the unemployment precisely because we nurture the spirit of enterprise and embrace flexibility as a core economic value.

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This report shows that the employer-employee relationship is highly complicated and defies easy definition. Federal and state governments use a variety of definitions for employers, employees, independent contractors, the self-employed, and others under tax, labor, and employment laws.

These laws and rules must evolve and reflect the economic reality of our times—in a manner that does not harm companies operating successfully under current approaches. They must avoid shoehorning all workers into the definition of a traditional employee. This would have the effect of forcing many people out of their desired alternative work arrangement. As we have seen, millions of Americans are now pursuing alternative arrangements in their existing jobs or as independent entrepreneurs and do not want to perform their work as “employees.”

Employers, frustrated as they are with confusing regulations—and the readiness of some workers, unions, and lawyers to exploit that confusion—must faithfully apply all existing rules governing employment and staffing, while working with the U.S. Chamber and others to modernize those rules that hamper their success in a highly competitive environment.

Governments at all levels must shape laws and regulations that provide workers and businesses with maximum flexibility to meet the changes and realities of the 21st century economy and craft rules that help all succeed.

Note on Sources and Statistics

The most authoritative source for recent statistics on employment in the United States, including forms of contingent or alternative employment such as independent contracting, is the U.S. Department of Labor's Bureau of Labor Statistics. BLS's July 2005 release of its *Contingent and Alternative Employment Arrangements, February 2005* offers a particularly useful statistical profile that illustrates the growth of the independent contractor model as well as the pay, benefits, and satisfaction of most participants.



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