

Statement for the Record

by

Coalition to Promote Independent Entrepreneurs



**Hearing Series on Tax Reform:  
Growing Our Economy and Creating Jobs**

before the

Committee on Ways and Means  
U.S. House of Representatives

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Entrepreneurs  
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The Coalition to Promote Independent Entrepreneurs (the “Coalition”) respectfully submits this Statement for the Record concerning a May 16, 2018, hearing before the U.S. House of Representatives Committee on Ways and Means titled *Hearing Series on Tax Reform: Growing Our Economy and Creating Jobs*.

The Coalition consists of organizations, companies and individuals dedicated to informing the public and elected representatives about the importance of an individual’s right to work as a self-employed individual, and to defending the right of self-employed individuals and their respective clients to do business with each other. We appreciate the opportunity to submit this statement setting forth our views on how we believe the *Tax Cuts and Jobs Act* (P.L. 115-97) will help grow the economy and create jobs by encouraging independent entrepreneurship.

The Coalition’s Statement focuses on only one aspect of the *Tax Cuts and Jobs Act*, namely the newly enacted section 199A of the Internal Revenue Code of 1986, as amended (the “Code”). While, acknowledging the difficulty in evaluating the impact of tax reform so soon, Chairman Brady observed that “we are on the first batter in the first inning of tax reform,” we believe it highly likely that Code section 199A will be of immense value in encouraging independent entrepreneurship. For the reasons set forth below, increased independent entrepreneurship is expected to lead to higher levels of economic growth and efficiency and a more engaged and satisfied workforce. We applaud the Congress, especially this Committee, and President Trump for enacting this new provision.

## **I. New Code Section 199A Will Encourage Independent Entrepreneurship**

New Code section 199A creates a new tax deduction – of up to 20% – for pass-through entities, which include certain independent contractors. This new tax deduction offers an important new financial incentive for individuals to pursue or continue pursuing their entrepreneurial aspirations.

The new tax deduction is available to an individual taxpayer for “qualifying business income” from certain pass-through business activities, including business income from a sole proprietorship. Because independent contractors operate sole proprietorships, they are eligible to claim the deduction. The new deduction could provide qualifying independent contractors with significant tax savings.<sup>1</sup>

The deduction, among other things, helps mitigate the financial consequences of the disparate treatment of independent contractors relative to employees for purposes of Social Security and Medicare contributions. Independent contractors are required to pay 100 percent of their Social Security and Medicare contributions, in the form of Self Employment Contributions

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<sup>1</sup> For a typical independent contractor whose taxable income for the tax year does not exceed the threshold amount, currently defined as \$157,500 per year or \$315,000 if filing a joint tax return, the Code section 199A deduction, subject to certain exceptions, would be the lesser of: (i) 20 percent of the taxpayer’s qualified business income amount or (ii) 20 percent of the taxpayer’s taxable income. For an analysis of the Code section 199A deduction as it applies to independent contractors see Russell A. Hollrah & Patrick A. Hollrah, *New Passthrough Deduction Creates Tax Benefit for Self-Employed*, TAX NOTES, Feb. 2018, at 1051-55.

Act (“SECA”)<sup>2</sup> contributions, while employees pay 50 percent, in the form of Federal Insurance Contributions Act (“FICA”) contributions<sup>3</sup> (through employer withholding)<sup>4</sup> with the remaining 50 percent being paid by their employer.<sup>5</sup> Since the new Code section 199A deduction is available to independent contractors, but not employees, the deduction can help mitigate the financial consequences of this difference.

Even when considered without regard to any other tax provision, the new Code section 199A deduction could provide a powerful incentive for individuals to pursue self-employment, as it will encourage individuals to take the risk associated with individual entrepreneurship by permitting self-employed individuals to retain a greater portion of the income they earn.

## **II. Policies Encouraging Independent Entrepreneurship Can Increase Economic Growth and Efficiency**

The individuals who offer their services as independent entrepreneurs are critical contributors to market flexibility, business efficiency and economic growth. The Coalition submits that the government should encourage and support this sector. Code section 199A is an exemplary example of how government can incentivize individuals to pursue their entrepreneurial dreams and thereby strengthen our nation’s economy.

### **A. Independent Entrepreneurship Fosters Economic Growth**

By encouraging independent entrepreneurship, new Code section 199A should lead to increased economic growth by expanding the formation of new businesses and creating new job opportunities, while increasing labor-force participation and reducing unemployment.

A 2010 study<sup>6</sup> on independent contractors found that independent entrepreneurship increases economic growth and efficiency.<sup>7</sup> The study identified a strong correlation between independent contracting, entrepreneurship, and small business formation.<sup>8</sup> To be sure, it found that “of the 10.3 million independent contractors identified in the 2005 CAWA survey, nearly 2.4 million had one or more paid employees.”<sup>9</sup> Furthermore, the study concluded that independent contracting “provides a first-step on the ladder to starting a small business, and creating jobs for others.”<sup>10</sup>

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<sup>2</sup> Code section 1401.

<sup>3</sup> Code section 3101.

<sup>4</sup> Code section 3102.

<sup>5</sup> Code section 3111.

<sup>6</sup> Jeffrey A. Eisenach, *The Role of Independent Contractors in the U.S. Economy*, at 30-40 (Dec. 2010) (“Eisenach Study”), <https://iccoalition.org/wp-content/uploads/2014/07/Role-of-Independent-Contractors-December-2010-Final.pdf>.

<sup>7</sup> *Id.* at 30-40.

<sup>8</sup> *Id.* at 36.

<sup>9</sup> *Id.* at 36.

<sup>10</sup> *Id.* at 42.

Individual entrepreneurship also offers a gateway out of unemployment or underemployment. A McKinsey Global Institute study<sup>11</sup> concluded that independent work<sup>12</sup> may help the unemployed by providing “a critical bridge to keep earning income while they search for new jobs.”<sup>13</sup>

Several recent studies analyzing independent-contractor relationships quantified their economic impact. A 2017 study<sup>14</sup> found that “independent contractors played a large role in the economic recovery.”<sup>15</sup> The study indicates that between 2010 and 2014, independent contractors grew by 11.1 percent (2.1 million workers) and represented 29.2 percent of all jobs added during that time period.”<sup>16</sup> The new businesses created by these 2.1 million workers generated nearly \$192 billion in revenue from 2009 to 2014.<sup>17</sup> In the ridesharing industry, alone, the study found that the independent-contractor opportunities attributable to ridesharing companies (e.g., Uber and Lyft) generated an additional \$573 million in revenue during 2014.<sup>18</sup>

Another 2017 study<sup>19</sup> shows that independent entrepreneurship is often as lucrative, if not more lucrative, than full-time employment. Specifically, the study found that 72% of freelance workers<sup>20</sup> reported earning the same or more income than when working as an employee,<sup>21</sup> and 57.3 million entrepreneurs earned \$1.4 trillion from freelancing during 2017.<sup>22</sup>

The many documented positive economic effects of independent entrepreneurs demonstrate the wisdom of government policies, such as new Code section 199A, that incentivize independent entrepreneurship.

## **B. Independent Entrepreneurship Contributes to Economic Efficiency**

The above-referenced 2010 independent contractor study<sup>23</sup> also found that independent-contractor relationships increase economic efficiency. These relationships facilitate workforce flexibility and efficient contracting by permitting contracting companies to engage independent contractors as needed instead of being forced to hire full-time employees who may be over or

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<sup>11</sup> *Independent Work: Choice, Necessity, and the Gig Economy*, MCKINSEY GLOBAL INSTITUTE (Oct. 2016) (“McKinsey Study”).

<sup>12</sup> The McKinsey Study defines “independent work” to include: the self-employed, independent contractors, freelancers, some small business owners, and many temporary workers, including those who get short-term assignments through staffing agencies. *Id.* at 20.

<sup>13</sup> *Id.* at 14.

<sup>14</sup> Ben Gitis et al., *The Gig Economy: Research and Policy Implications of Regional Economic, and Demographic Trends*, American Action Forum & Aspen Institute’s Future of Work Initiative (Jan. 10, 2017).

<sup>15</sup> *Id.* at 8.

<sup>16</sup> *Id.* at 8.

<sup>17</sup> *Id.* at 18.

<sup>18</sup> *Id.* at 20.

<sup>19</sup> *Freelancing in America: 2017*, Edelman Intelligence (Commissioned by Upwork and Freelancers Union) (Sept. 2017).

<sup>20</sup> Freelance workers include independent contractors and other contingent workers. *Id.* at 3.

<sup>21</sup> *Id.* at 43.

<sup>22</sup> *Id.* at 15, 41.

<sup>23</sup> See above note 6.

underutilized depending on business demand.<sup>24</sup> The study explained that labor force flexibility is correlated with economic growth and job creation, while less flexibility leads to slower growth and higher unemployment.<sup>25</sup>

Independent entrepreneurs also benefit from the economic efficiencies attributable to their status, as exemplified by their ability to work for a variety of different clients,<sup>26</sup> and to “enter, exit, or participate partially in the labor force as they choose.”<sup>27</sup> Similarly, the McKinsey Global Institute study found that independent work “enables people to specialize in doing what they do best and what makes them feel engaged. Engagement typically has the effect of increasing productivity ....”<sup>28</sup>

The foregoing data suggest that the incentive that Code section 199A provides toward independent entrepreneurship can be expected to lead to increased economic efficiency and higher levels of worker productivity.

### **III. Independent Entrepreneurs Are a More Engaged and Satisfied Workforce**

Recent research found that independent entrepreneurs possess highly desirable characteristics that can lead to higher levels of performance and individual satisfaction.

A recent study drawn from psychology and sociology and based on data collected on nearly 5,000 individuals in the United Kingdom, the United States, Australia and New Zealand who work in a wide variety of vocations including health, finance and education, found that self-employed individuals reported significantly higher levels of “job engagement” than organizational employees.<sup>29</sup>

Self-employed respondents were also found to value “challenging” aspects of work more than organizational employees, which contributes to their higher levels of job engagement.<sup>30</sup> In this context, the authors explain that job features that “challenge” an individual include financial and organizational responsibility, competition with others, demanding tasks, difficult decision-making, and the requirement for innovation, personal independence and autonomy.<sup>31</sup>

The characteristics the study found to be associated with the self-employed, such as working at a high energy level, valuing challenging aspects of work, and overall feeling more engaged with their work, generally have the effect of increasing productivity.<sup>32</sup>

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<sup>24</sup> Eisenach Study at 31-31.

<sup>25</sup> *Id.* at 39.

<sup>26</sup> *Id.* at 31.

<sup>27</sup> *Id.* at 39.

<sup>28</sup> McKinsey Study at 14.

<sup>29</sup> Peter Warr & Ilke Inceoglu, *Work orientations, well-being and job content of self-employed and employed professionals*, WORK, EMPLOYMENT AND SOCIETY, 8 (Aug. 2017).

<sup>30</sup> *Id.* at 12.

<sup>31</sup> *Id.* at 5.

<sup>32</sup> See above note 28.

Many studies have found that most independent entrepreneurs prefer independent work relative to traditional employment. One recent study<sup>33</sup> found that in 2017, 63% of freelancers started freelancing by choice, an increase of 10% since 2014.<sup>34</sup> Moreover, 50% of respondents said there is no amount of money which would incentivize them to stop freelancing and instead work at a traditional job.<sup>35</sup> What might be surprising to some, the McKinsey Global Institute study found that one in six people in a traditional job would like to become an independent earner;<sup>36</sup> and for every one independent worker who would prefer traditional employment, two traditional employees would prefer to move in the opposite direction.<sup>37</sup>

By encouraging independent entrepreneurship, Code section 199A will benefit not only the economy but also the individuals who engage in more satisfying entrepreneurial endeavors.

#### **IV. Conclusion**

The Coalition is supportive of Congressional actions that promote and encourage independent entrepreneurship, such as new Code section 199A. Such actions increase economic opportunity and growth and create an incentive for individuals to pursue a path that will enable them to become more engaged and satisfied with their work. For these reasons, we believe the *Tax Cuts and Jobs Act* will help grow the American economy, create new jobs and allow more individuals and their families to pursue the American dream. The Committee's leadership in this important area is commendable.

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<sup>33</sup> *Freelancing in America: 2017*, Edelman Intelligence (Commissioned by Upwork and Freelancers Union) (Sept. 2017).

<sup>34</sup> *Id.* at 25.

<sup>35</sup> *Id.* at 29.

<sup>36</sup> McKinsey Study at 7.

<sup>37</sup> *Id.*