

Small Business Boards: A Proposal to Raise Productivity and Wages in All 50 States and the District of Columbia

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Low profit margins keep many small businesses from investing in productivity-enhancing technology, which in turn holds down wages. To break that cycle, there should be a federal program that helps them reap economies of scale and scope by collaborating in areas such as R&D, investment, marketing, and health insurance purchases.

KEY TAKEAWAYS

- To escape the low-wage/low-productivity equilibrium, small firms can either be replaced through acquisitions or market loss, which is unlikely—especially given current antitrust fervor—or modernize, which will require collective action.
- To facilitate collective action, the Small Business Administration should operate a Small Business Board program that provides matching grants for states to launch pilot projects in the least-productive, lowest-paying, non-traded service sectors.
- Projects could focus on joint technology sharing; R&D collaboration; production technology modernization; marketing; vocational training; health insurance and retirement plans; and more.
- To raise productivity and wages in many of the least-healthy sectors of the U.S. economy, this proposed Small Business Board (SBB) program can apply approaches that have already succeeded in the past in American agriculture.

INTRODUCTION

The crisis of pay in the United States is also a crisis of productivity. Low-paying jobs tend to be concentrated in non-exportable, domestic service sectors such as hospitality, nursing care, retail, restaurants, and construction.¹ These sectors are dominated by small local firms in markets in which intense competition incentivizes employers to pay the lowest possible wages and provide few if any benefits. An alternative would be for these companies to develop innovative technology and new business models in order to boost firm productivity, thereby permitting both higher profits and higher wages and benefits for workers. But their low profit margins prevent many small businesses from investing in productivity-enhancing technology. The result is these sectors, which account for large numbers of firms and workers in the American economy, being trapped in a low-wage/low-productivity equilibrium, from which none by itself can escape.

To break this low-wage/low-productivity equilibrium in the most technologically laggard and poorest-paying sectors, there are two options. One is the replacement—through acquisitions or market-share loss—of many small firms with larger firms that can exercise at least some market power, enjoy economies of scale, and recycle higher net revenues into research and development (R&D), capital deepening, and higher wages.² But this might not happen on its own, in part because small business now receives significant incentives and protections that enable them to keep their existing market share even though they are generally less productive.³ In addition, America’s political culture, unlike those of some other nations, would prevent the government from either incentivizing or ordering the merger of small and inefficient firms—a policy that would be demonized by many in the progressive antitrust movement, which seeks to break up big, efficient firms.

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The other option is to allow firms to remain small or medium-sized, while at the same time helping them to reap at least some economies of scale and scope in areas such as R&D, investment, marketing, and the purchase of health insurance for workers by means of collaboration among most or all the firms in their sector. To prevent free riding, government must not only allow, but in some cases mandate, limited collaboration among numerous small and medium-sized firms for legitimate purposes. In other words, to maximize economic benefits for firms, workers, and the economy overall, some collective action is needed. As economist Paul Romer noted, “The lesson from economic growth is that collective action is very important and that everything, including institutions, can always be improved.”⁴

To that end, we propose creating a new Small Business Board (SBB) program, which would be operated by the Small Business Administration to increase productivity and raise wages in small firms. In return for matching grants from the federal government combined with state funding, each of the 50 states and the District of Columbia would be encouraged to create industry-wide SBBs, beginning with pilot projects in the least-productive and lowest-paying non-traded local service sectors. If at least half of the firms in the sector voluntarily agreed to a program, the state government, in partnership with the federal government, would help structure such a program and support joint inter-firm activities. In these cases, all the firms licensed to do business in a

particular sector in the state, while competing in other areas, would be required to participate in the program. Depending on the sector, this might involve joint technology sharing; collaboration in R&D; production technology modernization; targeted investments to improve productivity of individual firms; marketing; minimal wage, benefit, and working-condition standards; vocational training; and health insurance and defined-contribution retirement plans for all workers.

The proposed SBB program is modeled on existing federal programs with records of success going back over a century. In the Agricultural Marketing Agreement Act of 1937, Congress allowed procedures for establishing arrangements called “marketing orders,” to be overseen by the Department of Agriculture. Congress also authorized the creation of the agricultural extension service and more recently a Manufacturing Extension Program (MEP) run by the National Institute of Standards and Technology (NIST). The federal government has supported technology research consortiums, such as Sematech, which were provided with exemptions from antitrust law with the passage of the 1984 Cooperative Research and Development Act, the SBA’s small business investment company (SBIC) program, and the combination of federal matching grants and state funding for joint federal-state programs such as Medicare. The Prescription Drug User Fee Act (PDUFA) raised the fees drug companies pay to the Food and Drug Administration (FDA) to enable the agency to hire additional review personnel.⁵

All that is needed in order to raise productivity and wages in many of the least-healthy sectors of the American economy is to apply the same approaches that have already succeeded elsewhere.

COVID-19 HAS EXPOSED THE POOR HEALTH OF MANY SMALL BUSINESSES

The economic disruption associated with the COVID-19 pandemic and associated lockdowns and travel bans have hit some sectors of the economy far worse than others. The greatest suffering has been in sectors with both low productivity and low wages, such as hospitality, leisure, personal services, and brick-and-mortar retail. The sectors that have suffered the most are laggard sectors—laggard, that is, in moving from old-fashioned, labor-intensive and low-wage business models to innovative, capital-intensive, technology- and skills-based ways of providing goods and services. Upgrading these backward industries into high-wage, technology-intensive sectors must be a priority for bipartisan public policy in the aftermath of the COVID-19 pandemic.

Data from the Bureau of Labor Statistics in December 2020 provides confirmation of the disparity in economic impact. In the leisure and hospitality supersector, unemployment was 16.7 percent (with jobs declining 21 percent last year) and in “other services” 7.4 percent, compared with 4.3 percent in manufacturing and 6.1 percent in business and professional services. Not only was pandemic-induced unemployment higher in leisure and hospitality, but wages, benefits, union representation, and the number of hours worked per week were also lower.

Apart from mass unemployment, all those sectoral disparities preceded the COVID-19 pandemic and will reassert themselves in the future, unless something is done to ameliorate them. The U.S. economy since 1990 has added 20 million low-quality private sector jobs, compared with only 12 million high-quality jobs, according to the Job Quality Index.⁶ The difference is reflected in both hours worked and wages. Americans trapped in low-quality jobs work on average only 30 hours a week, compared with 38 hours for those in high-quality jobs. The federal minimum wage

of just \$7.25 per hour, which has not increased since 2009, while inflation has grown 21 percent, contributes to the problem.

Long before the pandemic, it was clear that many firms in the laggard sectors of retail, leisure, hospitality, and personal services were privatizing their profits while socializing their overhead costs—by paying such low wages that many of their workers could survive only with the help of food stamps, the earned income tax credit (EITC), and other aid charged to taxpayers. For example, 52 percent of fast-food workers have at least one family member relying on a public assistance program. And as we pointed out in our book *Big Is Beautiful: Debunking the Myth of Small Business*, the largest share of these workers are employed by small businesses. Indeed, a 2007 study by the Urban Institute found, “Low-income workers are disproportionately likely to work in smaller firms.”⁷

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During the Great Depression, President Roosevelt declared, “It is my conviction that the South presents right now the Nation’s No. 1 economic problem.”⁸ Low-productivity, low-wage sectors may be our country’s biggest economic problem today. Just as the impoverished rural South was brought up to the standards of the industrialized North by government-sponsored electrification, the minimum wage, and farm programs, the sectors that are currently dragging down U.S. wages and productivity need to be transformed with federal policy in cooperation with the states.

Rescuing good and bad firms alike during the initial stage of the pandemic made sense. But in the years and decades ahead, American taxpayer support should be limited to businesses that pay and treat their employees well and seek to increase profits, wages, and output at the same time by adopting innovative technologies, such as self-service technology, and high-performance labor practices. Firms whose business models rely on low-wage labor (and no benefits) shifting fixed costs to workers, or paying so little that their employees have to use welfare services deserve to go extinct. This will make it easier for the small and large firms that want to do right by their workers to do so.

Productivity and wages in laggard sectors can be raised in two ways. One way is to allow many small firms to be replaced by bigger firms that pay higher wages, enjoy scale economy efficiencies, and use more technology.

The other method—which does not require small firms to be absorbed into big businesses—uses public policy to help small business owners who are willing to take the high road. In partnership with state and local governments, small businesses can collaborate with each other in areas that benefit from scale, such as training and R&D, while competing with each other in the marketplace and retaining their own identities. Upgrading all the small firms in a sector on equal terms would be a win-win proposal that benefits industries, workers, consumers, and taxpayers alike.

THE PROBLEM: LOW PRODUCTIVITY AND LOW WAGES

Economists often divide the national, or local, economy into two sectors: traded and non-traded. The traded sector produces goods or services that can be sold abroad as well as at home. **Most**

manufacturing, agriculture, mining, entertainment, and software firms are traded. In the absence of foreign trade barriers, in theory, the market for traded goods and services can be all consumers in the world. Enormous markets allow firms to reap increasing returns from scale and scope, which by boosting productivity allow them to raise output, profits, and, usually, wages for their workers, all at the same time. Thanks to this win-win dynamic, most countries and almost all state and local economic development agencies seek to maximize the size of their traded sectors in the hope that they will be siphons sucking in revenue from growing numbers of consumers abroad as well as at home, driving job creation through the multiplier effect.

But more sectors are non-traded—and they employ a large share of workers. For example, although their inputs may be abroad, most houses and other buildings are constructed locally. Restaurants, nursing homes, day care centers, social services, and many other industries also belong to the non-traded domestic sector.

Given the comparatively intense competition in most traded industries, including with low-wage nations, one might think that wages for non-college-educated workers in these sectors would be lower than economy-wide wages. But because of the ability to use technology and gain economies of scale, the average salary for non-college-educated workers in traded industries is \$42,632, which is 38 percent more than in non-traded industries. And the gap between these sectors and the rest of the economy is increasing. For example, in 2008, traded-sector salaries were 35 percent larger than non-traded salaries.⁹

Technology can and is changing the relative ratio of traded to non-traded sectors. For example, before the rise of the Internet, most banking, insurance, retail, and travel services were non-traded, with consumers going to their local bank, insurance agent, retailer, and travel agent. Now, because of the Internet, much of this commerce can be traded, including across national borders, to achieve significant economies of scale. Even sectors that are inherently non-traded, such as real estate brokerage and taxis, are now partially traded, as international companies such as Uber, Lyft, and Redfin provide some of these services remotely through electronic means. This shift has in many cases resulted in the creation of more higher-wage jobs. For example, with the rise of e-commerce and companies such as Amazon with enormous economies of scale and intensive automation, the number of stock clerk and order jobs increased by 19 percent from 2010 to 2019, compared with an increase in retail sales jobs of just 1 percent. And in 2019, wages in the former sector were 19 percent higher than in retail, and mean nominal wages for stock clerk and order jobs increased 25 percent over this period, compared with just 1 percent in retail.¹⁰

High productivity is a necessary, though not sufficient, condition for higher wages. While wages are determined to some extent by the relative bargaining powers of employers and workers, firms' productivity imposes an upper limit on what employers are capable of paying, even if their workers are unionized or they share profits generously with employees through non-wage compensation.

If you remember your freshman year Microeconomics class, you'll probably recall graphs of supply and demand curves intersecting. Usually, it was a picture showing something like the price at which farmers would sell their wheat and the price that buyers would be willing to pay. In this ideal universe visualized by neoclassical economists, there is only one point at which supply and demand are in equilibrium, and the job of government is to not get in the way of the

market attaining it. At any particular time in this idyllic world, there should be only one price of wheat such that the market “clears,” meaning that all who want to buy and sell at that price are able to do so. If government subsidizes or taxes wheat, the market will not efficiently allocate wheat production.

Policy can help move economies to this higher-level equilibrium if it spurs workers to get more skills, and firms to use more skills, by investing in advanced technologies and high-performance work organizations.

But in fact, when we move to the economy-wide level, there can be multiple equilibriums in an economy, with some better than others. And markets acting on their own may actually pick the inferior ones, with society suffering as a result. Research by economist Elvio Accinelli and colleagues has shown that there is strategic complementarity between the percentage of high-skill workers and high-value-added, innovative firms in an economy.¹¹ They found that economies can be in perfect neoclassical equilibrium at either a high level of innovation and high skills or a “poverty trap” of low skills and underinvestment in innovation. In other words, if there are not enough skilled workers, firms will not adopt the advanced technology that leads to higher productivity because their workers don’t have the necessary skills—and if firms don’t adopt advanced technologies, workers won’t seek out the skills needed to use them. Hence, economies can settle into a poverty trap. This trap can be avoided when the number of innovative firms in an economy exceeds a threshold level while the number of skilled workers also increases. As such, policy can help move economies to this higher-level equilibrium if it spurs workers to get more skills, and firms to use more skills, by investing in advanced technologies and high-performance work organizations.

Unfortunately, from a firm perspective, the low-wage, low-investment path can be quite profitable. As Susan Helper and Ryan Noonan found in a study for the U.S. Department of Commerce, there is more than one “production recipe” firms can and do take to be profitable.¹² The “high road” recipe involves greater use of capital equipment, more reliance on skilled workers and their knowledge, and greater focus on innovation. The low road, which can be just as if not more profitable for firms, but less “profitable” for society and the firms’ workers, is the “recipe that involves minimizing capital expenditures, hiring less-skilled, low-wage workers, and producing commodity goods and services. Helper and Ryan found that these practices are highly correlated with firms adopting one being more likely to adopt others. For example, there is a positive 0.7 correlation between payroll per employee and value added per employee (in other words, firms that pay their workers more have higher productivity), and a 0.6 correlation between payroll and capital expenditures (firms that pay their workers invest more in capital goods).

In summary, the U.S. economy has fallen into a trap: too many low-wage, low-skill jobs and too little investment by companies in new machinery and high-performance work organizations. Getting out of this trap will require a wide range of policies, including better programs to boost worker skills. But one policy change that would move us in the right direction is a higher minimum wage. As such, advocates need to champion the minimum wage as a core element of a robust U.S. economic and productivity-growth policy. Doing so will help gain support for this needed reform.

While policymakers should encourage the broader and deeper digitalization of such sectors as health care, higher education, legal services, and others—so more sectors can gain needed economies of scale—for some sectors, that will be difficult to achieve. It makes sense, then, to combine efforts to raise a sector’s wages with efforts to raise productivity in a single program—and it makes political sense. It is pointless to force nursing homes to pay their workers more when they cannot afford to invest in labor-saving technology that would enable them to provide the same or better care with fewer, better-paid workers. The only result would be bankruptcy or increased costs for already financially strapped families.

If all the firms in a low-wage, low-productivity non-traded sector were to cooperate for purposes such as R&D and technology diffusion, then all firms might break out of the low-wage/low-productivity trap together. But in competitive markets with many small firms, the collective action problems are insuperable. Rationally, each firm should wait for the others to make the first move; and each firm would benefit from free riding on the collaborative efforts of the rest, which would benefit not just that specific firm but indirectly the entire sector. For example, in a given industry, one firm would benefit if all the other firms within that region invested in upgrading the skills of their workers, because it could then just hire those trained workers itself. But it is somewhat economically irrational for any one firm to do this on its own because the investments would also benefit their competitors.

This paralysis preventing firms from engaging in select collaboration with others that would make all of them better off makes it necessary for government, as an outside broker, to intervene to arrange the participation of all firms in a few joint efforts, while ensuring both the independence of each firm and competition among all the firms on most fronts.

WHY POLICY SHOULD BE STATE BASED AND SECTOR SPECIFIC

To shatter low-wage equilibriums in technologically laggard, labor-intensive non-traded sectors—such as restaurant work, nursing home care, and home health aides and construction—and catalyze productivity growth and higher wages, we propose the creation of a new dual federal-state institution: the Small Business Board (SBB). The sectoral boards in each state would be limited to non-traded service industries, not traded sectors such as manufacturing, whose challenges and structure are different.

Because the focus would be on the non-traded sector, it makes sense to create sectoral boards at the state level, rather than the national level. Traded industries such as manufacturing can be located anywhere, and the location decisions of many firms are highly sensitive to local wages, along with local taxes and regulations. This can create a “race to the bottom,” not only among states or provinces in a federal nation-state, but also among countries in the world economy.

A race to the bottom is not a problem with most or all non-traded service and goods industries. Most non-traded industries such as retail, nursing, and construction are found in every state, if not every county and city. An aerospace supplier may move from one state to another, but if a janitorial company pulled out of a state because wages were too high, there would still be plenty of janitorial companies in that state because the demand would remain strong.

Fifty state sectoral wage boards, plus one for the District of Columbia, would also allow flexibility in areas such as wages and training. While a higher basic federal minimum wage is a good idea,

the cost of living varies so dramatically between different parts of the U.S. that a poverty wage in California might be a living wage in Montana.¹³

It also makes sense to give employers and representatives of workers in different sectors the freedom to negotiate laws regarding hours and other regulations related to working conditions that are appropriate for that industry, even if they would not be for others. A one-size-fits-all policy for all occupations and industries does not make sense. For example, industries such as film have a very different occupational and work structure than such industries as nursing homes.

The need for industry-appropriate regulations was recognized during the First New Deal of 1933–1935, when the National Industrial Recovery Act (NIRA) sought to establish industry-specific codes for wages and benefits and pensions. Only after the Supreme Court ruled that the NIRA was unconstitutional (not on the merits but for the technical reason that it was allegedly an excessive delegation of power by Congress to the president) did the federal government turn to one-size-fits-all programs such as Social Security, the federal minimum wage, and standardized wages and hours laws in subsequent legislation. In European countries with strong traditions of management-labor bargaining, both firms and organized labor have preferred to negotiate wages and standards over having the government set them for all sectors.

Box 1: Lessons from Germany for American Small Businesses

Germany's success in manufacturing exports for the global market is often attributed to its *Mittelstand* (middle estate), which refers to its medium-sized enterprises. Rather than compete with large corporations, these companies, often family-owned over several generations, specialize in providing high-quality goods in niche markets.

Mittelstand firms are helped by industry-wide and nation-wide institutions that help them achieve strengths they could not achieve on their own. One example is Germany's famed vocational training and apprenticeship system, which is funded chiefly by firms.

Product and process R&D too expensive for individual small and medium-sized businesses to undertake on their own is sometimes carried out by the Fraunhofer Society, a nonprofit research organization with 72 institutes specialized in sectors of applied science, as distinct from basic science. Fraunhofer institutes do contract work for small firms in particular fields, helping them with innovation and technical challenges.

The German model of shared vocational training and research support for small businesses has attracted American attention. Fraunhofer USA, founded in 1994, has seven centers in the United States, working with firms, regional economic development agencies, and universities through its TechBridge and State Alliance programs. U.S. and German companies including BMW have collaborated in vocational education programs in Florida, North Carolina, Michigan, Wisconsin, and Georgia. Similar training initiatives and research contracts could be organized by sectoral SBBs.

In summary, it makes as much sense to set up different organizations to establish and oversee standards and support systems for small businesses in nursing as it does for those in

construction. And in cases in which existing federal regulations permit state variations or higher state standards to override a federal minimum standard, it makes sense that regulations and aid to, for example, nursing businesses should take different forms in North Dakota than in Florida—thereby reflecting the differences in local conditions.

SMALL BUSINESS BOARDS: WHAT THEY WOULD DO AND HOW THEY WOULD WORK

In each state, small business boards would be organized to promote collaboration among small and medium-sized firms in particular sectors for two purposes. The first objective would be to enable them to pool their resources and exploit increasing returns to scale in areas such as R&D, production testbeds, and other shared resources, and purchasing health insurance and contracting with 401k plans. The second objective would be to negotiate minimum wages (above the increased federal minimum wage), hours, and benefits in particular standards. This would put a floor on wages and benefits in that sector, thereby preventing a race to the bottom, although not preventing firms from offering higher wages and benefits, if they choose.

The federal government would offer to approximately match state funding for each of the sector-wide small business boards created by a state. The federal contribution might vary somewhat in the interest of equity among rich and poor states and initially should be larger than the state match until programs have been established and have a track record. A model for this kind of “cooperative federalism” can be found in Medicaid. On average, the federal government pays for two-thirds and states pay for one-third of Medicaid programs.¹⁴

In addition to the two streams of federal and state funding, small business boards should be funded to some degree by small assessments on member firms, on the condition that a majority of firms in a sector choose to vote to establish a state SBB.¹⁵ Here, the model is the agricultural marketing system of commodity boards for specific crops such as peanuts and potatoes, which is overseen by the U.S. Department of Agriculture (USDA). Some states also have their own programs. For example, the California Pistachio Research board is a cooperative effort authorized by a grower referendum and operating under the oversight of the California Department of Food and Agriculture. Firms pay small assessments used to fund research on pistachio propagation, production, harvesting, handling, and preparation for the market.¹⁶

The SBA should oversee the creation and operation of a state-based small business board system, in the same way USDA organizes and supervises agricultural marketing boards. The advantages of SBA are the many tools it has at its disposal and its long history of working closely with small and medium-sized firms.

Each SBB would preside over programs to benefit the small and medium-sized firms in a sector, as well as large firms that might be included, on a case-by-case basis. These could include shared R&D, technology extension services, sectoral adjustment finance, marketing boards, vocational training, wages, shared benefits (including defined-contribution retirement plans and health insurance). These are illustrative, as individual sector boards might identify other shared services and programs particular to their state and industry.

Let’s examine the possible programs that would be supervised by a proposed state-based SBB in detail.

Shared R&D

Unlike large firms with ample retained earnings, many small firms find it difficult or impossible to engage in either product or process R&D. While sometimes suppliers conduct R&D regarding equipment, in many cases, the focus is not on the actual product or service offered (e.g., construction firms could come together to support R&D on tools and other construction processes).

Joint Cybersecurity Efforts

Many small firms lack the resources (financial and expertise) to adequately secure their IT systems from attacks and threats. Each SSB could provide shared services on how to best ensure cybersecurity of the firms in the industry.¹⁷

Technology Extension Service

Each SBB would maintain a modest professional technology extension service, modeled on the agricultural extension service and NIST's Manufacturing Extension Partnership. Like these models, the sectoral technology extension service would share productivity-enhancing innovations and practices resulting from product and process R&D with all of firms in the sector in a particular state and help firms implement these practices.

Sectoral Adjustment Finance

After learning from the technology extension service or other sources about productivity-enhancing equipment or reorganization, many small firms may have trouble accessing loans to upgrade themselves. SBA could help with various kinds of adjustment finance, including grants, loans, and the chartering of small business investment companies (SBICs) that specialize in helping to modernize firms in particular sectors. Congress could charge SBA with prioritizing loans in the 7a and other SBA loan programs for firms that are part of state sectoral boards.

NIST's Manufacturing Extension Partnership

The Manufacturing Extension Partnership (MEP), run by the National Institute of Standards and Technology, is modeled after the long-standing agricultural extension service operated by the Department of Agriculture to provide technical assistance to the nation's farmers. The MEP program operates 51 centers in all 50 states and Puerto Rico, and is staffed by over 1,400 advisors at 375 service locations. NIST provides half the funding for centers, with state governments and companies making up the remainder.

The idea behind MEP is that small manufacturers play a critical role in the U.S. economy, either as suppliers to larger firms that compete internationally or as providers of final products that can be sold around the world, but that all too often they lack the resources needed to effectively modernize and adopt the latest technology. As such, the program, staffed by former manufacturing engineers and technicians, helps small manufacturing will help centered on five critical areas: technology acceleration, supplier development, sustainability, workforce development, and continuous improvement. The idea is not to substitute for other help they can get, such as from consultants, but to help companies that otherwise not be able to obtain help.

MEP delivers a significant return on investment for U.S. taxpayers. In FY 2020, MEP helped manufacturers achieve \$13 billion in sales, \$2.7 billion in cost savings, \$4.9 billion in new client investments, and helped to create or retain 105,000 U.S. manufacturing jobs.¹⁸

Vocational Training

Collective-action problems have always bedeviled vocational training in the United States. Firms are wary of training workers at their own expense for fear the workers will then quit and work for rivals. The proliferation of non-compete agreements even among low-wage occupations is a cure that is worse than the disease—not to mention they violate antitrust rules. The solution is a version of the German model in which firms in an industry pool the costs of vocational training of apprentices and employees.

In the United States, some states and sub-state regions have established sector-based regional training alliances. While the regional Workforce Investment Boards, established by the Workforce Investment Act of 1998, were an attempt to increase the influence of the private sector over the federally funded workforce investment system, in fact, the system generally does a poor job of engaging deeply with employers in skills development, particularly at the operational level. All too often their agenda is not determined by employer demand but by service providers' interests. Moreover, employers are often reluctant to invest in training their workers for fear their competitors in the same or similar industry in their region will lure those workers away after they have been trained. As such, this is a collective-action problem government could help solve, in part by encouraging firms to establish industry-led regional skills alliances as part of an SBB. In addition to being funded by company dues (and government matching grants) companies would agree to train their own workers and hire new workers in the program. For example, a manufacturing skills partnership established by the Virginia Manufacturers Association works with community colleges to expand credentialing for key manufacturing occupations. Each state SBB would consult with member firms and organize vocational education programs, including partnerships with community colleges and universities, that are tailored to the needs of the member firms.

Defined Contribution Retirement Plan and Health Care

Many small firms cannot afford either traditional defined benefit pensions or defined contribution plans such as 401ks and IRAs. Each SBB would organize a common defined contribution plan shared by all the firms in the sector. The pooling of retirement assets would give the small and medium-sized firms in the sector more bargaining power in negotiating costs with retirement investment firms than individual firms would have on their own.

As in the case of the sectoral minimum wage, the shared defined contribution plan would be a default. Individual firms could opt out, but only if they wished to make more-generous arrangements for their employees.

In addition, allowing all the firms in the sector to negotiate as a unit when contracting for health insurance for their employees would enable them to exercise a certain degree of buying power to obtain discounts from insurers and medical providers; discounts large employers already get. Individual firms would be allowed to opt out only if they chose to offer more-generous health plans to their workers.

Wage Board

Wage boards are more than a century old in Australia, Britain, Canada, the United States, and elsewhere. They were created to address inadequate wages and benefits in so-called “sweated trades” such as home-based sewing, in which dispersed production and sometimes part-time workers made traditional unionization impractical. The same conditions characterize many modern low-wage, labor-intensive, low-productivity industries. As an alternative to both a race to the bottom in wages and benefits among low-margin firms and attempts to unionize a sector one

firm at a time, a wage board can set minimum wages and standards for all the firms in a sector.¹⁹

A few states have had wage board statutes for generations. New York recently convened a wage board to deal with wages and working conditions in the fast-food industry.²⁰ It works by having the state secretary of Labor convene a wage board panel of three members, which then holds hearings and receives testimony from interested parties, including workers and firms.

By convening sectoral wage boards, state governments would bring together representatives of industry and labor in those sectors, as well as government and sometimes consumers. The representatives of workers on state wage boards need not be traditional unions, which are quite limited in the American private sector, where only a little more than 6 percent of workers are unionized. One method might be to require each firm to organize a works council, which would not engage in collective bargaining itself, but organize elections for worker representatives to the wage board in a specific sector. The candidates to represent worker interests could be labor unions, but they might also be major or minor political parties or nonprofits or other groups or individuals.

The representatives of labor and management from many small firms elected to sectoral wage boards would be tasked to reach a consensus on sector-specific wages and other matters. If they could not agree, the state executive branch would break the deadlock and issue regulations directly, subject to override by the state legislature.

The wages and benefits set by the sectoral wage boards under the supervision of a sector-wide SBB in a particular state would specifically be the minimums. The wage boards would rule out a destructive race to the bottom in sectors by firms competing with each other to pay their workers less and less. But individual firms could be more generous if they chose to offer higher wages and better benefits to lure away employees from their rivals in the same sector. This “race to the top” among small firms in non-traded sectors would encourage both productivity growth and the equitable sharing of the gains from higher profits.

What of concerns that either higher wages and benefits or higher productivity would mean fewer jobs? When opponents of a higher minimum wage or more benefits argue that they will lead to job loss, what they really mean is job loss at particular firms, not fewer overall jobs in the U.S. economy. To accurately assess overall employment impacts, whether from robots or a higher price for labor, we need to look at second-order impacts. In the case of the minimum wage, an employer may or may not hire the same number of workers, but if they hired fewer because of higher labor costs, then it’s important to recognize that the remaining workers would now earn more. These workers wouldn’t bury their extra earnings under the mattress; nor would they be likely to save much of them given that they’d have so little money to begin with. Rather, they’d spend that income on additional consumption: needed health care, repairing their car or buying one that works, subscribing to broadband, or even buying a bit more food so their kids don’t go to bed hungry. This increased spending creates demand, which leads other firms to create jobs, offsetting any jobs lost in the firms paying the now higher minimum wage.

Both small business owners and their employees, then, could benefit from higher wages and higher productivity. Small firms could produce the same output in the form of goods or services with fewer workers—or in some cases, more output with the same number of workers. Those who keep working for the upgraded firm would enjoy higher wages made possible by their higher productivity. And workers who have lost their jobs because of technological upgrades could find new jobs in other sectors at the same or higher wages—in part because of higher consumption spending by better-paid workers in the sectors wherein they were formerly employed.

A COMPLEMENTARY NATIONAL MODEL FOR TRADED-SECTOR FIRMS

A similar model should be adopted at the national level for firms of all sizes in traded sectors that sell and locate across state lines and throughout the world. In this case, it could be based on the aforementioned innovative 1994 proposal by economist Paul Romer for the establishment of self-organizing industry investment boards.²¹

Romer highlighted the importance of collective action for some and the risk of free riders making collective action difficult. A case in point is workforce training, where it might be rational for all the firms in an industry to invest collectively in a workforce training program, but because of free riders, the effort never gets made, as everyone seeks to benefit without paying.

Under this proposal, a particular industry could petition the U.S. Secretary of Commerce to hold a hearing to certify that the proposal for collective action addresses a genuine public need. If the department agrees that it does, it would oversee an election in which all producers in a particular sector would vote to levy a small tax on sales. “If a large enough fraction of the industry (measured as a fraction of total sales, as a fraction of the total number of firms, or some combination of the two) votes in favor of this initiative, a tax backed by the full force of law would be imposed on the entire industry.”²² The revenues would not go to government, but to industry-determined areas of expenditures, such as precompetitive research that would benefit the entire industry, or precompetitive shared production facilities. Ideally, Congress would allow the “industry tax levies” to qualify for firms’ R&D expenditures under an ideally expanded R&D tax credit.²³

Some industries already engage in similar action. As mentioned, such activities are common in agriculture. The cable TV and broadband industry also does this, funding the nonprofit CableLabs to help the industry with new technology and standards.²⁴

CONCLUSION

Too many economists see competition as the only legitimate form of interaction among businesses, with anything else being seen as anticompetitive collusion. But as FDR once stated, “Competition has been shown to be useful up to a certain point and no further, but cooperation, which is the thing we must strive for today, begins where competition leaves off.”²⁵ If we are to effectively address one of the nation’s most pressing problems today—the employment of tens of millions of Americans in small, low-productivity, low-wage firms—it is time for the federal government to help these firms work cooperatively to get out of their current low-wage, low-technology trap.

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