



National Audit Office

# Supporting Small Business

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## EXECUTIVE SUMMARY



**1** The latest data, from 2003<sup>1</sup>, showed that of the 3.5 million businesses in England all but 5,400 were either small (with fewer than 50 employees) or medium-sized (with 50 to 249 employees).<sup>2</sup> Small and medium-sized businesses are found in all sectors of the economy, account for half of all business turnover and employ 57 per cent of England's private sector workforce. The needs of small businesses are many and varied and in 2000, the Department of Trade and Industry (the Department), established the Small Business Service (SBS) with the vision to make the United Kingdom the best place in the world to start and grow a business.

**2** An analysis commissioned by SBS reported that in 2003-04 the Government spent £2.6 billion in supporting small businesses.<sup>3</sup> A variety of departments, agencies and local bodies were involved: less than 15 per cent of the total was spent by SBS.

**3** Since its inception SBS has moved away from being a deliverer of services to influencing key Government policies and actions supporting potential entrepreneurs and small businesses. In particular SBS facilitated the development of, and is overseeing implementation of, the Government Action Plan for Small Business issued in January 2004, which flowed from the 2002 policy paper *Small Business and Government – the Way Forward*. SBS's expenditure for 2005-06 was £213 million. Its staffing was planned to reduce to 218 staff by 1 April 2006 and it achieved 190. This report examines SBS's performance management framework and its performance against its key targets. The report presents four aspects of its work in more detail – SBS's role in: influencing Government regulations and policies; facilitating small business access to finance; helping to join up services across Government; and providing advice and support to small business. Together these aspects of SBS's work represent 90 per cent of its expenditure.

**4** *The Way Forward* set out three aims central to the Government's vision for the small business sector. In turn SBS is responsible for an enterprise Public Service Agreement (PSA) objective which contains three targets for achievement by 2008. SBS has focused on the Government's enterprise policy which comprises seven strategic themes. The activities which flow from these themes encompass a wide variety of different programmes which are the formal responsibility of a number of different accounting officers across Government.

#### The Government's aims:

Many more people, regardless of their background, having the desire, skills and opportunity to start a successful business.

Everyone with the ambition to grow their business being helped and supported.

A supportive business environment with all small businesses finding it easy to respond to Government and access its services.

**PSA objective:** To build an enterprise society in which businesses of all sizes thrive and achieve their full potential.

**Targets:** Increase in the number of people considering going into business;

Improve the overall productivity of small firms; and

More enterprise in disadvantaged communities.

#### The seven strategic themes:

Build an enterprise culture.

Encourage a more dynamic start-up market.

Build the capability for small business growth.

Improve access to finance for small businesses.

Encourage more enterprise in disadvantaged communities and under-represented groups.

Improve small businesses' experience of Government services.

Develop better regulation and policy.

#### Four workstreams:

Building the Business Link brand.

Developing the [www.businesslink.gov.uk](http://www.businesslink.gov.uk) portal.

Progressing the strategic alignment of government funding.

Overseeing the introduction of common commencement dates for new regulations.

<sup>1</sup> This is the latest date which provides specific information for England as opposed to the United Kingdom.

<sup>2</sup> For the purposes of this report the term small business refers to small and medium-sized businesses.

<sup>3</sup> *Mapping of Government Services for Small Businesses*, PACEC, 2005.

5 While the Small Business Service is responsible for achieving the PSA objective, not all of the actions undertaken to support the objective are its responsibility. Its task is to encourage other government departments and agencies to deliver the Government Action Plan, and so help the Government achieve its PSA objective.

6 In 2002, Government established a high level working group chaired by SBS, and comprising senior officials from the main departments contributing to the Action Plan, to improve the coherence and effectiveness of small business policy across Government. Since 2004, the group has concentrated on taking forward four workstreams. The group's current focus is the simplification of business support programmes.

7 The better targeting of support for business was a theme of Sir Peter Gershon's 2004 report *Releasing resources to the frontline*.<sup>4</sup> The report called for government interventions in the private sector to be both efficient and effective. Sir Peter's recommendations on this and other issues were accepted by the Government and are being implemented through an Efficiency Programme designed to secure £21.5 billion of annual efficiency gains by March 2008. SBS has reduced its staff by over 300 since March 2004. This figure includes both efficiency savings and the transfer of functions. An example of the latter was the loss of about 130 posts when responsibility for running the Business Link network was transferred to the Regional Development Agencies.

8 *The Way Forward* and the Government Action Plan were welcomed by the small business community, as they brought together for the first time a cross-government view of support for the small business sector. But there are difficulties in managing these arrangements:

- **Complexity.** The small business sector is a complex policy area which requires several complementary activities to work together to achieve success. SBS considers that given these complexities it has achieved a great deal in developing a cross-Government policy for small businesses and a cross-Government Action Plan where before there was

none. There remain, however, a number of different expressions of the Government's intentions for small businesses as demonstrated by the Government's aims for the small business sector; the PSA objective and three targets; the seven strategic themes and the high level group's four workstreams. In addition the most recent cross-cutting review of Government expenditure on small business identified 15 Government Departments with 265 programmes aimed at small businesses. SBS is now leading work at both a national and regional level to reduce and simplify business support programmes in England. The Budget in March 2006, announced the Government's intention that the number of national, regional and local support programmes should be reduced from over 3,000 to 100. In addition to the complexity of the sector, factors external to Government affect the performance of the small business sector. These circumstances make planning a cost-effective package of interventions problematic.

- **Lack of precision and alignment in the performance measurement framework.** The complexity of the small business sector means that it can be difficult to link the Government's aims, the PSA objective and targets and the strategic themes. For example, some of the seven strategic themes overlap, and several themes contribute to each of the targets – making it difficult to assess which of the themes are having an effect on performance against those targets.
- **Monitoring.** SBS records in a database performance against the measures of success which were listed in the Action Plan, including the PSA targets. A few of these measures are published in the Department's Annual Report. At task level, SBS monitors progress with all the tasks which fall to it under the Action Plan. SBS does not, however, routinely collate progress on tasks outlined in the Action Plan which are the responsibility of other parts of Government. This means that SBS is not able regularly to assess and publish overall progress against the Action Plan, as originally intended.

4 *Releasing resources to the front line: Independent Review of Public Sector Efficiency*, Sir Peter Gershon, CBE, July 2004.

- **Evaluation.** Government interventions represent only one set of factors that influence small business performance. Periodic evaluation studies can help isolate the impact of government interventions. Three SBS evaluations of its major established programmes have used econometric techniques to produce estimates of net impact. A further two such evaluations pre-dated the existence of SBS. More evaluations, including an economic impact study of Business Link Operators, are in progress. But none of these evaluations has to date evaluated the impact of SBS as a whole or by reference to its strategic themes, or interpreted its or Government's contribution to higher level targets and aims.
  - **Coherence with the needs of small business.** Our survey of 12 business representative groups identified the areas they regarded as top priority for Government action. We found that there is a direct correspondence between the top two business priorities and the strategic themes. Other business priorities, for example, for a more favourable tax regime and a more skilled workforce also feature within the strategic themes but are expressed differently. In turn, the Government has objectives for greater enterprise and diversity which the business groups we consulted did not place among their top priorities.
- Top business needs:**

  - Better regulation
  - Better access to finance
  - More effective business support
  - Less government bureaucracy
  - Clear communication and information from government
  - A favourable tax regime
  - A more skilled workforce
- 9 We examined the work that Government has undertaken to date under the two top business priorities of better regulation and improving small business access to finance:
    - **Better regulation and policy.** International surveys indicate that the United Kingdom is relatively lightly regulated, compared with many other countries, but that regulation places a disproportionate burden on small businesses. We examined how successfully SBS had influenced nine regulations (all but one introduced in 2003 and 2004) and two policies (from 2002 and 2003). In five of the 11 cases SBS had contributed fully to the development of the policy or regulation. In the others, SBS's involvement was more limited often because the other Department did not consult SBS in a timely manner. SBS have not systematically measured the effect of their contribution to developing new regulations or on the potential to reduce burdens further. But in one case, where SBS took forward the adoption of common commencement dates for new regulations, the Department estimated a reduction of burdens on business of around £20 million annually. Across the entire range of policy, funding and regulation activity, the Gershon Review highlighted the need for the Government to 'secure high levels of public benefit at the least cost to both businesses and to government itself.'<sup>5</sup> The Government is taking forward broader plans to assess the overall scale of burdens imposed on small businesses, and ways to reduce them. Procurement exemplifies SBS's work on developing policy, where Government is looking to improve small business access to Government contracts, including developing a web portal that will facilitate access to lower value Government contracts.

5 *Releasing resources to the front line: Independent Review of Public Sector Efficiency*, July 2004, page 38.

- **Improving access to finance.** SBS has estimated that around 150,000 (3.4 per cent) of established small businesses each year have difficulty raising the finance they need, although up to 60 per cent of these businesses subsequently obtain finance through the market. The Government has taken a number of steps in this area to stimulate the existing financial markets in the United Kingdom. On debt finance, in 2005-06, the Government supported 5,800 firms through the long-running Small Firms Loan Guarantee. Reviews have shown that the scheme continues to provide valuable support for small businesses – particularly those without the collateral to attract commercial lending – and can also provide some wider economic benefits. But they also show that the scheme has high default rates and engenders high levels of displacement. SBS considers that high default rates can demonstrate that the scheme is encouraging lending at levels of risk that lenders would not normally consider and that high levels of displacement can enable more efficient and productive businesses to enter the economy. We observe that the scheme’s objectives envisage assistance to viable businesses and question the extent of the evidence of extra benefits commensurate with the increased risk, or of assisted businesses being more productive than those they displace.
  - In its 2003 report *Bridging the Finance Gap*, Government identified a gap in the equity funding of small businesses particularly for amounts between £250,000 and £2 million.<sup>6</sup> The report estimated that between 9,000 and 18,000 firms would be suitable for such equity investments each year and that existing sources of equity financed between 3,000 and 6,000 firms. By the end of December 2005, Government backed equity finance schemes had invested £215 million in 558 businesses. These schemes have a number of objectives including demonstrating to potential investors that commercial returns can be made by funds that provide investment to fill the equity gap.
- 10** We also examined the work SBS has undertaken to improve Government’s understanding of small business issues and its ability to influence the rest of Government. In addition, we reviewed SBS’s work in managing the Business Link network, and introducing and overseeing the businesslink.gov web portal.
- **Joined-up services.** Small business issues rarely feature in top-level or supporting targets for Government Departments. In 2004, we surveyed officials in 25 Departments who deal with small businesses about their views of SBS. 15 respondents thought SBS was well placed to set the agenda for small business but 14 thought SBS was not communicating its role and purpose clearly. 17 respondents thought that SBS’s work had benefited their organisation and that SBS was a reliable source of objective information. We followed up these views in December 2005 and found some improvement to the ratings for communication and expertise but a less favourable view of SBS’s ability to set the Government’s agenda. Of the 12 business representative groups we surveyed, 11 agreed that SBS understands the small business environment and the issues facing small business owners and that, since 2000 when SBS was established, Government’s understanding of small businesses has improved. A quarter of these bodies cited the limited influence of SBS over government departments as a barrier to successful implementation of the Government Action Plan.

6 *Bridging the Finance Gap: next steps in improving access to growth capital for small businesses*, HM Treasury, December 2003.

- **Advisory services.** Government provides support to small businesses in many forms. We looked at two mechanisms operated or overseen by SBS – the Business Link network of 42 operators which provide advice to small businesses across England, and the businesslink.gov web portal. Business Link operators assisted more than 492,000 existing businesses in 2004-05, a penetration rate of businesses of over 14 per cent, a figure which had more than doubled since 2001-02. In 2004-05, Business Link also helped 172,000 pre-starts; that is people considering starting a business. To enable performance management by Business Link area, SBS sets and reports targets for penetration rates based on the Inter-Departmental Business Register, which includes businesses in all parts of the economy but not all very small businesses, and also include pre-starts in their calculation. On this basis Business Link achieved a penetration rate of 37 per cent in 2004-05. Customer satisfaction rates with Business Link have also increased, rising from 74 per cent in 2000-01 to 90 per cent in 2004-05. From 1 April 2005, the Business Link network has been managed by the Regional Development Agencies. The web portal, still managed by SBS, has also proved a success: website hits are 20 per cent ahead of target, it won a United Nations award in 2005 for the best e-content application for business in the United Kingdom and attracted 5.6 million unique visitors in the 12 months to 31 March 2006.
- 11 On value for money:**
- In light of the Efficiency Programme's emphasis on releasing funds for front-line services and the set of zero-based budget reviews to be included in the 2007 Comprehensive Spending Review,<sup>7</sup> public bodies not directly involved in the delivery of public services need, more than ever, to demonstrate their effectiveness.
  - Government spends over £2.6 billion in providing support to small businesses. While SBS has evaluated a number of individual programmes it is not able to establish the overall impact of either its or wider Government activity on small businesses. It has acknowledged this problem and has recently commissioned consultants to review the quality of evaluative evidence on business support across Government, with the aim of moving towards a common set of performance indicators and evaluation techniques which will improve its ability to make judgements about the relative cost-effectiveness of departmental initiatives.
- In 2005-06, SBS spent £151 million providing direct support by facilitating access to finance (£110 million) and Phoenix Fund activities (£41 million), £8 million providing part-funding for consultancy support to small businesses to promote management best practice, and spent £35 million in supporting Business Link and joining up Government services primarily through funding for the businesslink.gov website. Most of the associated schemes or projects show progress against their specific objectives. Under SBS's tenure the Business Link network has, with constant levels of funding, improved the quality and volume of services provided – and so is clearly better value now than in 2000. Similarly, the web portal project has enjoyed higher volumes than expected and has been widely welcomed. On access to finance, evaluations of the Small Firm Loan Guarantee demonstrate the numbers of businesses that have been supported but also show high levels of default and economic displacement. These factors limit the cost-effectiveness of the scheme against its objectives. Possible wider effects on productivity have not been evidenced and need closer examination if they are to be the basis for judging scheme success.
  - Aside from the £151 million spent on direct business support, SBS also spent in 2005-06, £7 million to promote various forms of enterprise, £2 million on policy development and influencing and on research and evaluation, and £10 million on their own administration costs. In some areas, monitoring of results is not well-developed: for example there is no system to assess the impact of SBS's small business expertise on the development of regulations. And there are as yet no systematic measures of the added value SBS produces as an influencing organisation. SBS will in part address this issue through its plan to undertake further surveys of the views of government departments and agencies drawing upon an existing survey undertaken by the NAO for this report.

7 HM Treasury, Budget 2006, March 2006.

## Recommendations

Our recommendations are consistent with the Gershon proposals and fall into two groups:

### Recommendations to reduce complexity, facilitate evaluation and improve reporting of progress

**a** The current performance measurement framework could be simplified and given added force by:

- reviewing the PSA objective and targets to ensure that they best represent the Government's objectives for the small business sector and promote the desired changes;
- simplifying and aligning better the Government's vision, aims, PSA objective and targets and strategic themes; and
- ensuring that the way progress is measured reflects, as far as possible, the impact of Government's actions rather than the impact of external factors.

**b** SBS should consider improving its programme of evaluations by:

- ensuring that its evaluations of individual schemes link back to the Government's overall objectives for the small business sector and, where appropriate, to the PSA targets, as well as assessing progress against the scheme's objectives; and
- pulling together scheme evaluations and other evidence in Government-wide evaluations of performance against major Government small business aims and targets, to estimate the overall impact of Government actions.

**c** SBS has improved the evidence base designed to support its actions but evidence on the cost-effectiveness of some of the instruments it employs is incomplete. More comprehensive information would increase confidence that the package of activities proposed is cost-effective and it would help resource activities economically towards defined targets.

**d** The Government Action Plan has achieved some co-ordination between departments, but needs to be developed further to encourage more joint working across Government by:

- specifying more precisely the contributions expected of each government department;
- incorporating specific commitments from government departments on the actions they are undertaking and the resources they have committed to small business issues, in the way that Delivery Plans outline progress towards PSA targets; and
- ensuring that the monitoring and reporting arrangements for the Government Action Plan that were promised in the Plan are established. This could draw upon the scorecard approach used by SBS to report its own contributions.

**e** The Government should examine whether SBS has the ability and the appropriate level of authority to influence the other government departments with an interest in promoting enterprise, to ensure that a more dynamic small business sector is established.

### Recommendations to improve business support programmes

**f** In March 2005, the Government announced a series of actions to measure, and ultimately reduce, the volume of regulation faced by business. The actions include a programme of administrative burden reductions, and a consolidation of regulatory and inspection bodies. As part of this process SBS should identify those areas of Government regulation which most impose burdens on small businesses, explore with the departments concerned how they will use regulation simplification plans to reduce those burdens, and make sure that cuts in burdens for small businesses are targeted within the overall regulatory reform programme.

**g** SBS should track any reductions in burdens, or increase in benefits, that its involvement in the development of regulations has stimulated, and use that information to help target its resources and demonstrate to departments the value of its regulatory expertise.

**h** The Government should develop measures to track the adoption of procurement practices by public bodies that offer appropriate access to public contracts, and to check that small businesses are aware of procurement opportunities.

**i** The *Bridging the Finance Gap* review estimated the size and nature of a number of gaps in the finance market, which a variety of interventions – some old, some new – now aim to address. Viewed at the micro level, a scheme like the Small Firms Loan Guarantee has been a lifeline to many small businesses who would not be the success they are today without its help. At the macro level the scheme has had a higher default rate than commercial lending and similar schemes in other countries, and has displaced non-assisted businesses. These might be indicators of positive impact but might be cause to question the value for money of the scheme. There are now a large number of schemes to help finance small businesses, each with its own objectives and indicators. SBS in conjunction with the Treasury, should review the evidence on the impact of the schemes as a group against the key estimates of beneficial change identified in *Bridging the Finance Gap*. They should clearly state their expectations of progress against those key estimates to help judge whether the package of finance schemes is providing value for money.

**j** SBS, working with the Regional Development Agencies, should improve the cost-effectiveness of Business Link Operator monitoring by:

- moving to a single, national survey of customer satisfaction;
- explaining clearly the methodology they have adopted for reporting the penetration rates achieved by Business Link Operators in public documents; and
- reviewing, as planned, the first year's estimates of the value added by Business Link to understand the variations in performance between Business Link Operators, and so helping raise overall performance.