

The British Entrepreneur

How startups can put Britain back in
business

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Edited by Allan Nixon

ONWARD ▶

About Onward

Onward's mission is to develop bold and practical ideas to boost economic opportunity, build national resilience, and strengthen communities across all parts of the United Kingdom.

We are not affiliated to any party but believe in mainstream conservatism. Our vision is to address the needs of the whole country: young and old, urban and rural, for all communities across the UK – particularly places that have too often felt neglected or ignored by Westminster.

We believe in an optimistic conservatism that is truly national – one that recognises the value of markets, supported by a streamlined state that is active not absent. We are unapologetic about standing up to vested interests, putting power closer to people, and supporting the hardworking and aspirational.

Thanks

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Executive summary



Britain was once the most entrepreneurial country in the world. The Industrial Revolution fused innovation and enterprise and transformed the country. It was all made possible by risk-taking individuals like Matthew Boulton and James Watt - two engineers from Birmingham - who capitalised on new technologies such as the steam engine, transforming manufacturing and industry for decades to come.

The UK has retained some entrepreneurial prowess, but that infectious culture of enterprise has steadily faded. And in its place lies a deep aversion towards risk and a knotted web of regulation. This contrasts to countries like the United States, where the aspirational 'American dream' pushes the desire of small business owners for growth and expansion. In Britain, aspiring entrepreneurs often believe they are destined to fail.

This is worrying because Britain urgently needs more entrepreneurship. But it isn't just any kind of entrepreneurship, Britain needs growth-oriented startups. Too many British businesses are small and staying that way. Over the last two decades, the share of small businesses within the business population has remained static. And over the last five years alone, the share of high growth businesses has fallen by 13%. At present, just under 1% of the business population generates over 11% of the country's productivity.

Decisions around growth for most British businesses are often about simple steps like hiring the first employee or finding enough funding to open a high street shop front. Leveraging entrepreneurship for growth needs a sharp focus on the different types of businesses struggling to grow and the differing challenges each of them face. High street bakeries and AI tech startups, for example, need very different forms of support to grow.

With potential tax hikes on businesses on the horizon, the Labour Government risks quelling Britain's entrepreneurial spirit even further. The Conservative Party must reclaim being the natural home for British businesses. It has long championed an economic environment where enterprise can thrive with the right kind of government support. But the centre right must renew its focus to meet the needs of contemporary businesses. The British Entrepreneur makes the case for renewing entrepreneurship and sets out exactly how it can be done.

What is holding back entrepreneurial Britain?

There are five main barriers to entrepreneurship in Britain:

1. **High costs.** A bundle of costs currently pose a disproportionately large burden on businesses. The UK has the highest VAT threshold in the world, charging 20% at the £90,000 turnover level. Nearly 26,000 businesses are intentionally staying below the threshold to avoid a higher VAT bill. Business rates are imposing large

costs especially among medium-sized businesses in high-value locations. Although there are exceptions, the average business pays 14p for every £1 of tax paid towards rates. The fixed cost of business rates, coupled with its administrative complexity, make it challenging to navigate.

Off-payroll working regulations (or IR35 rules) are unfairly taxing freelancers and contract labour. Although introduced to reduce tax fraud, IR35 has produced poor outcomes. Since its introduction the tax bill for freelancers has increased by £1.5 billion, leaving 35% of freelancers out of work altogether. Ambiguous IR35 guidelines also mean that court verdicts from a handful of high-profile cases have become the basis for HMRC to update its self-employment determinant criteria.

2. **Access to finance.** British entrepreneurs are uniquely under-reliant on external finance. Debt finance is hard to access. The UK has one of the highest SME loan rejection rates in the OECD of 45%, driven by an increased reticence to lend to smaller businesses among major commercial banks - plus an internal aversion to debt among small businesses. Equity finance is the reserve of the few, with less than 5% of British businesses use any amount of equity funding.
3. **Challenging economic climate.** A collection of external shocks - from the pandemic to high energy prices resulting from the Russian invasion of Ukraine - means that entrepreneurs have a negative outlook of the economy. Interest rates for SMEs are the highest they have been for a decade, and over half of all trading businesses reported no change to their turnover in the last year.
4. **Fear of failure.** British entrepreneurs tend to be uniquely risk averse. Just five UK universities rank among the top 100 for producing successful entrepreneurs, compared to ten from California alone. The fear of failure rate in the UK is 20% higher than the global median and the US. This is driven largely by concerns around loss of money, but also by fears of reputational damage. Among growing businesses, the top driver of a fear of failure was the impact it would have on their future job prospects.
5. **Bureaucracy.** Excessive bureaucracy costs the UK nearly £40 billion in lost productivity. Particularly bad is its poor infrastructural support for businesses, ranking in the bottom five globally on measures like planning and transport that support entrepreneurship. HMRC inefficiencies have also negatively affected entrepreneurship. During the pandemic, over a million self-employed individuals were left with no financial support because of HMRC failing to hold adequate information about the nature of their employment.

Who exactly is the British entrepreneur?

Polling from JL Partners and analysis by Onward has identified a pipeline of entrepreneurial talent - examining the entrepreneurial ambitions among the general population, and growth ambitions among current entrepreneurs.

The general population

1. **On the bench** - Less than a third of this group said they were likely to start their own business. They are older, lower-skilled and on low incomes. They tend to view salaried employment as a source of stability, even at the cost of being employed in low-wage roles. Targeting this group to become entrepreneurs is unlikely to be successful.
2. **On the fence** - Between a third and two-thirds of this group are in favour of starting a business. They are younger, on average incomes, in middle management positions and most worried about startup and everyday costs. They are likely to be in the early stages of developing their businesses and view entrepreneurship as the best occupational stepping ladder in the industries they work in.
3. **On the brink** - This group is on the cusp of starting a business. They are more likely to be male, younger, and in high-skilled senior occupations with higher degree educational qualifications. They are most confident that their experience will aid their entrepreneurial goals. And unlike those on the fence, this group reports difficulty finding funding as the primary barrier to setting up a business.

The entrepreneurial population

4. **Sole operators** - The group is least interested in growing their business. They are predominantly sole traders, male, older, and are only educated to the GCSE level. They are too preoccupied with everyday business management to consider growing, and think high administrative costs are holding them back. Unlike other entrepreneurs, this group rarely seeks external finance and nearly half are not concerned about their business failing.
5. **The contemplators** - This group of entrepreneurs actively want to grow their business, but are held back by a set of practical concerns. They are younger, run mid-sized businesses, and struggle to access private funding. High costs and a perception that their business is not successful enough to grow is holding the contemplators back from growth. They are the most afraid of failure compared to other types of entrepreneurs.

6. **The growers** - This group of entrepreneurs are growing their businesses. They are overwhelmingly male, younger, have the highest share of those with university degrees, and run private limited companies. Concerns that growth comes at the cost of profitability persist even among the growers. Nearly a quarter (24%) of this group think they would be more profitable in their current state, and 26% feel that high admin costs are choking their growth plans. And their fear of failure is more reputational than economic - more growers worry that a failed business would impact their future jobs.
7. **The executives** - This group has grown their business to its maximum potential. They are more likely to be male, highly skilled and working in London and the South East. They typically run businesses employing over 55 people and have the highest share of businesses with over 250 staff. Their primary concerns are the state of the economy. There is an active role for public policy to target this group and investigate whether the growth ceiling that the executives perceive is artificial. Over a third turn over less than £1 million each year.

Recapturing entrepreneurial Britain

The state does not offer all the solutions for private enterprise - nor should it. But there is a clear role to help turn the aspiring entrepreneur into a real one and help businesses struggling to grow to reach their full potential.

But not all entrepreneurs require the same support. The Conservatives in opposition must win back support from those keen to start a business and those keen to expand, identified as those “on the brink” and those contemplating and currently growing.

To address the cost burden:

1.1 The VAT threshold should be lowered significantly and replaced with a tapered rate. The flat rate of 20% at the £90,000 level should be replaced with a tapered rate that increases in turnover. Increasing the threshold neither solves the issue, and costs nearly £50 million for every £1,000 increase in the threshold. Only a lowered threshold will eliminate the cliffedge and allow businesses to grow. And a tapered rate will mean that the smallest businesses see the lowest VAT rate.

1.2 Business rates should be reformed to make them fairer and more efficient. In the short-term, introducing temporary reductions for expanding business, abolishing the downwards transition, and introducing high street rental auctions would reduce the cost burden on small businesses. In the long-term business rates could either reflect commercial land value or be made conditional on business turnover.

1.3 HMRC should simplify its self-employment determination criteria and institute an IR35 ceiling. HMRC should simplify its existing Check Employment Status for Tax (CEST) rules to run simple and straightforward tests to verify an individual's employment status. On releasing the amount of potential tax at stake in IR35 litigation cases, it could be made the case that only self-employed individuals earning over (for example £50,271 - the higher rate tax threshold) needs to have their contracted company determine their IR35 status.

To improve access to finance:

2.1. A new wave of commercial bank backed Community Development Finance Institutions (CDFIs) should be introduced. CDFIs are regional financial intermediaries aimed at providing additional capital to businesses that have been rejected from mainstream lenders. CDFIs could increase SME funding received by between £1.5-£1.7 billion, with an additional 50-60k of businesses getting more funding. This should be accompanied by a collaborative fund pooling together government and private capital, and a long-term enforcement plan to involve commercial banks in capitalising CDFIs.

2.2 The British Business Bank should transform its funding finder tools.

Company registration should be made conditional on businesses entering their top options for finance based on the British Business Bank's '3-Step Funding Finder Tool.' The Bank could go further and launch an interactive digital networking platform to match entrepreneurs and funders, modelled on of Singapore's 'Startup SG.'

To help aspiring entrepreneurs take risks:

3.1 Introduce 'Business Startup Relief' (BSR) to incentivise greater entrepreneurship. A "Business Startup Relief" would provide those that have paid a fixed amount in tax through PAYE with a tax refund to help establish their new company. Modelled off the Irish Start-Up Relief for Entrepreneurs (SURE), and the Dutch system of 'entrepreneurs allowance,' this relief would allow aspiring entrepreneurs to claim a share of their new investment as a tax refund to help reduce their upfront costs to setting up a business.

To tackle red tape

4.1 Councils and mayoralities should create expedited planning processes to help businesses secure new premises. A "Fastrack Business Planning Initiative" (FBPI) could prioritise applications from businesses seeking to expand or establish new premises.

Table of recommendations

Problem	Solution
1. High costs to setting up and growing a business	1.1 The VAT threshold should be lowered significantly, and a tapered VAT rate should replace the flat 20% rate 1.2 Business rates should be reformed to avoid penalising high street businesses 1.3 HMRC should simplify its self-employment determination criteria and institute an IR35 ceiling
2. Poor access to finance	2.1 Introduce a new wave of commercial bank-backed Community Development Finance Institutions (CDFIs) 2.2 The British Business Bank should transform its funding finder tools
3. High fear of failure	3 Introduce 'Business Startup Relief' (BSR) to reduce upfront costs for aspiring entrepreneurs.
4. Bureaucracy	4 Councils and mayoralities should create expedited planning processes to aid business growth

Entrepreneurship for growth

Why entrepreneurship matters



Unleashing entrepreneurship is vital to overcoming sluggish growth and stagnant productivity. Entrepreneurs contribute to growth primarily by greater innovation and productivity and they do so in two key ways.

First, they introduce new products, services, and processes to the market. Challenger banks like Revolut, Monzo, and Starling introduced a flush of new banking services like all-purpose mobile banking apps, virtual cards, and peer to peer payments. The success of these new products revolutionised the UK fintech industry, which received more equity deals from 2020-22 than any other sector.¹ Business innovation was ultimately responsible for over half (51%) of labour productivity from 2000-2008.²

Second, entrepreneurs trigger innovation in incumbent businesses by spurring competition. Following the success of challenger banks, incumbent institutions like JP Morgan began to offer similar perks and launched a credit builder card 'Chase Freedom Rise' for individuals with limited credit history.³ In sectors where incumbent firms are already technologically advanced, the productivity benefits from innovation induced by the entry of a new firm are estimated to be nearly double that from what new firms might directly contribute.⁴

Entrepreneurship will only go on to grow in importance. James Wise, venture capitalist and author of the book *the Startup Century*, argues that the unprecedented speed of diffusion of new technologies presents a unique opportunity for entrepreneurship to unlock productivity.⁵ A 2021 study that surveyed business experts found that entrepreneurship is expected to have a much larger role in the future of work by 2030 given the increasing speed of product and service innovation and new forms of collaborative entrepreneurship needed to solve the nation's most complicated challenges.⁶

But not just any form of entrepreneurship is needed – the UK needs growth-oriented entrepreneurship.

Entrepreneurship drives growth so far as the businesses being created are productive – creating new products, services, processes, and driving competition. A small group of highly productive businesses in the UK representing just 0.7% of the business population (32,000 businesses) are responsible for over 11% of UK GVA (£268 billion).⁷ It is the creation of growth-oriented and highly productive businesses that makes greater entrepreneurship a worthwhile pursuit for government.

Despite successive governments pledging to “back British businesses” and form “a new partnership with business,” policies to encourage entrepreneurship have failed to focus on growth. A 2024 NAO report that identified 39 reliefs for business investment, 29 of which cost nearly £17 billion, concluded that there was not enough evidence to understand if they were encouraging growth.⁸ A review of 'Entrepreneur's Relief' – that reduced the amount of capital gains paid by entrepreneurs when they sold their firms – found that while the scheme was

widely used, there was not enough evidence to determine whether the reliefs succeeded in creating successful businesses.⁹

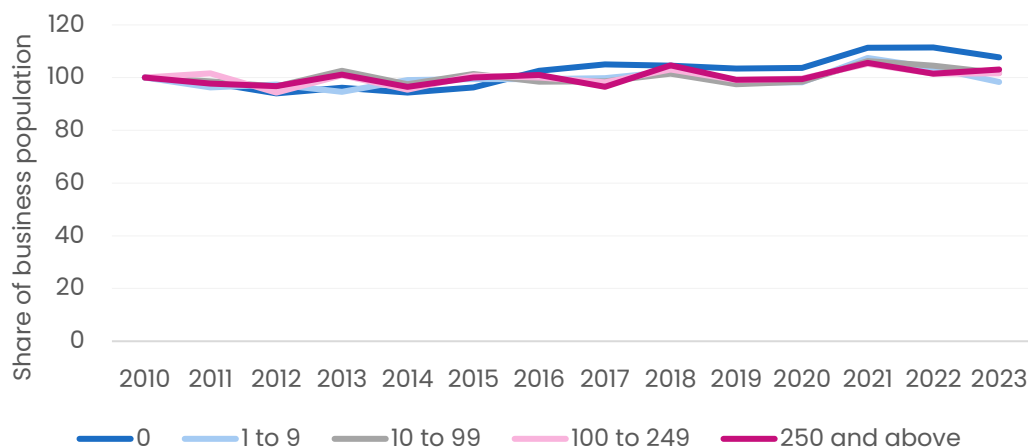
The Government's limited efforts to encourage growth-oriented entrepreneurship are endemic of a broader issue: entrepreneurship in the UK is insufficiently growth-minded. Two factors drive this: the UK produces many new firms, but they struggle to scale, and the pandemic saw a significant decline in business creation.

Failing to scale

The majority of British businesses are small and staying small. While the majority of their businesses in most countries are SMEs., this share is particularly high in the UK. In an average OECD country, 70-80% of businesses are small or medium sized, but in the UK this share is as high as 99.9%.¹⁰ The share of micro and small businesses has remained relatively unchanged over the last decade, and there has been no growth in the share of large businesses either.

Figure 1: SMEs as a share of the business population, 2010-23 (Index 2010=100)

Source: ONS Business Demography

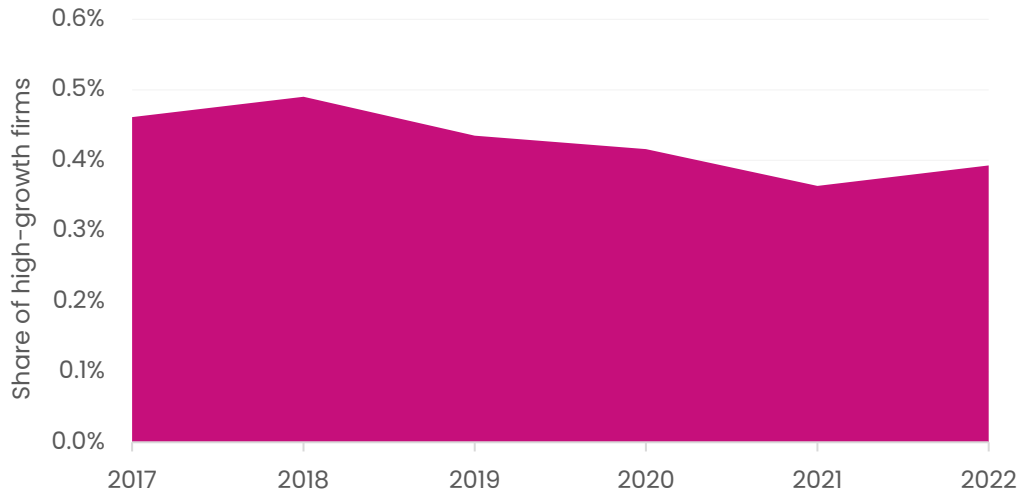


And British businesses have been growing less over the past decade. In 2012, the share of businesses growing in employment terms was 20%; whereas in 2022, it fell to just 12% – a decline in growth of 40%.¹¹ Businesses of all sizes have been growing less. The Enterprise Research Centre found that in 2019, just 2% of UK businesses had reached over £1 million turnover in three years, and just under 8% of £1-2 million turnover businesses grew to £3 million over a three year period.¹²

The UK's share of 'scale-ups' is also in decline. In 2022, scale-ups made up just 0.39% of all businesses in the UK, down from 0.46% in 2017, resulting in a 13% decline or a loss of over 1,600 high growth businesses.¹³

Figure 2: Scale-ups as a share of all active businesses, 2017-22

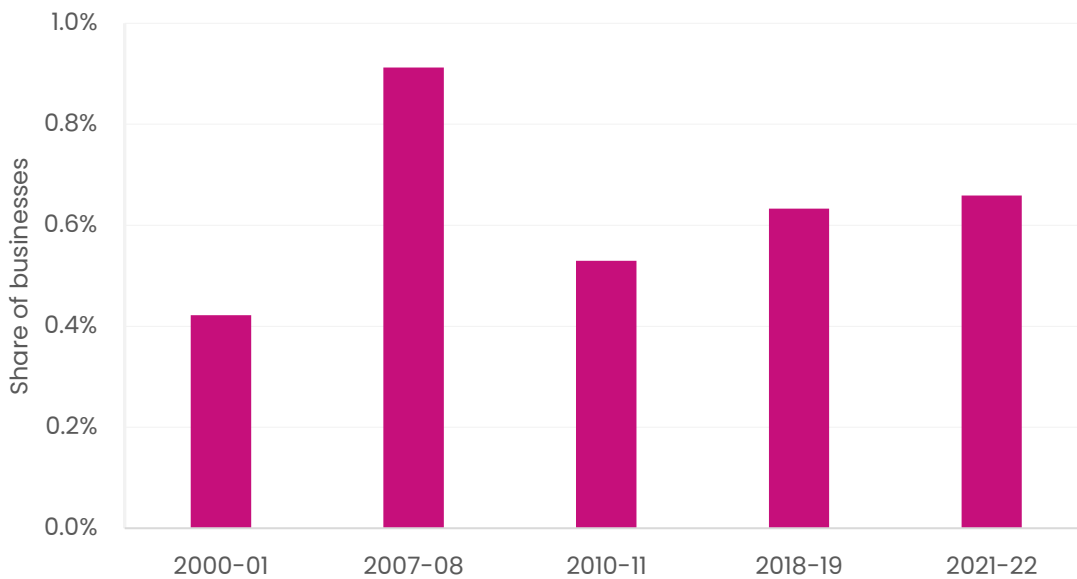
Source: ONS Business Demography



But turnover and employee growth alone are not sufficient to explain business growth. Evidence suggests business turnover and job creation are poor determinants of productivity.¹⁴ Instead the turnover a business generates for every employee it hires ('turnover per employee') is key. The businesses that increase their turnover per employee at a faster rate than their employment are the drivers of UK productivity.¹⁵

Figure 3: Productivity heroes as a share of all business, 2000-22

Source: Enterprise Research Centre



Yet these “productivity heroes” are few in number and heavily concentrated in some places and sectors. In 2021-22, they represented just over 0.6% (around 36,000 firms) of all businesses, while being responsible for 11% of UK Gross Value Added (GVA). They are sectorally concentrated: nearly two-thirds are found in just two sectors – business and professional services and wholesale and retail, shown in Figure 4 below. They are geographically concentrated too: over a third are located in London and the South East (37%), with Northern Ireland and the North East home to just 1.2% and 2.8% respectively.

Figure 4: Productivity heroes by sector

Source: Enterprise Research Centre

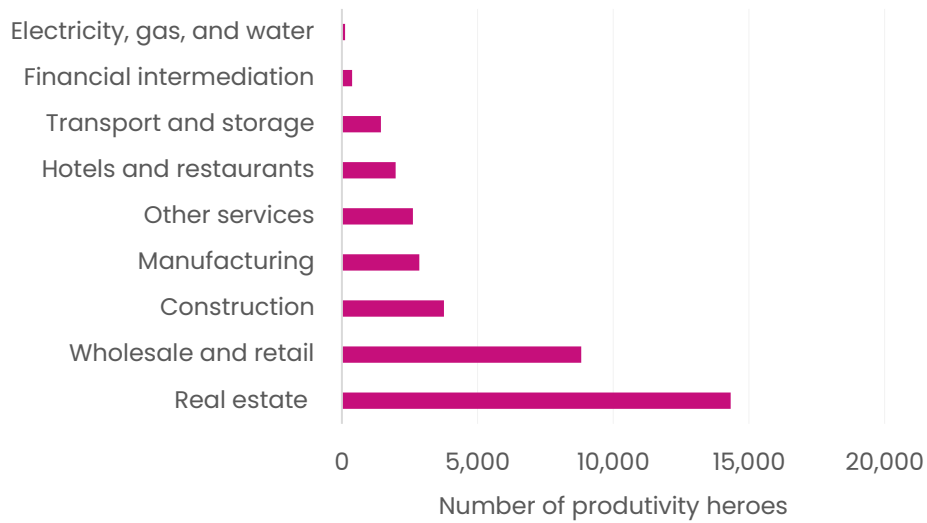
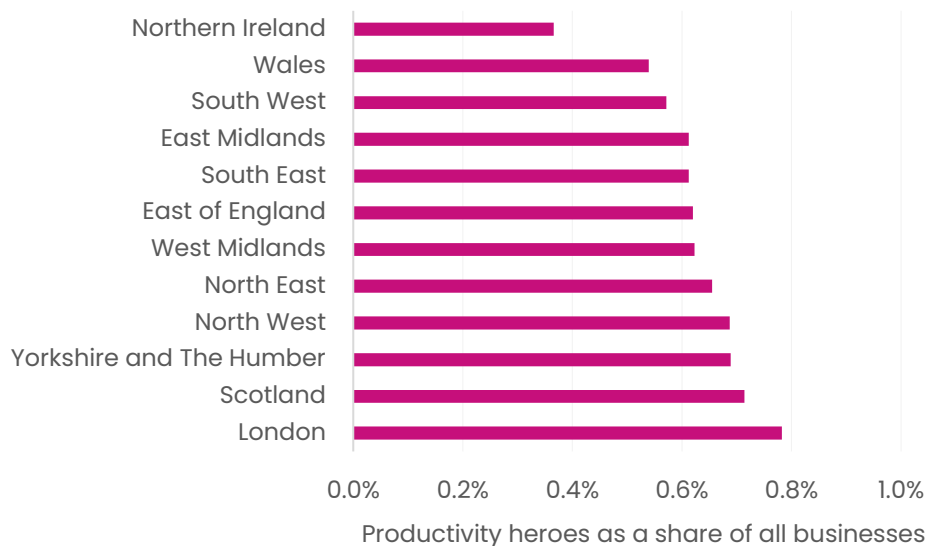


Figure 5: Productivity heroes by region

Source: Enterprise Research Centre, Onward analysis



Reflecting this national trend of low growth, polling by Onward and JL Partners found that a large share of entrepreneurs were uninterested in growth altogether. Over a fifth of entrepreneurs said they were uninterested in growing their businesses, and when coupled with those who feel they have already maximised their growth potential, the share goes up to nearly 40%.

The UK suffers from a ‘growth intention’ gap.¹⁶ Entrepreneurial leadership and the intention to grow a business is a stronger predictor of economic growth in the UK compared to business birth rates or self-employment rates.¹⁷ Encouraging more businesses to become scale-ups and productivity heroes will be essential to realise the economic gains from entrepreneurship.

Entrepreneurship has not recovered since the pandemic

Until the Covid pandemic, entrepreneurship had been steadily increasing. Self-employment rates increased by a quarter in the decade up to 2020 and the business population expanded by a third. But the pandemic saw a marked decline in business creation that is yet to be reversed. There are currently 425,000 fewer businesses and 734,000 fewer self-employed individuals than in 2020.

Figure 6: Count of all private businesses in the UK, 2010–23¹⁸

Source: DBT business population estimates, 2023¹⁹

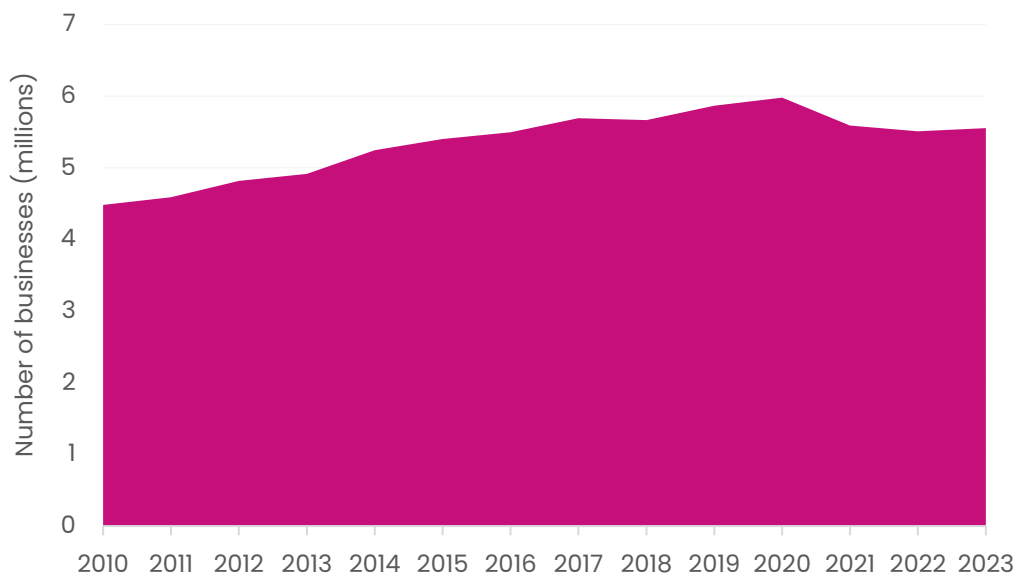
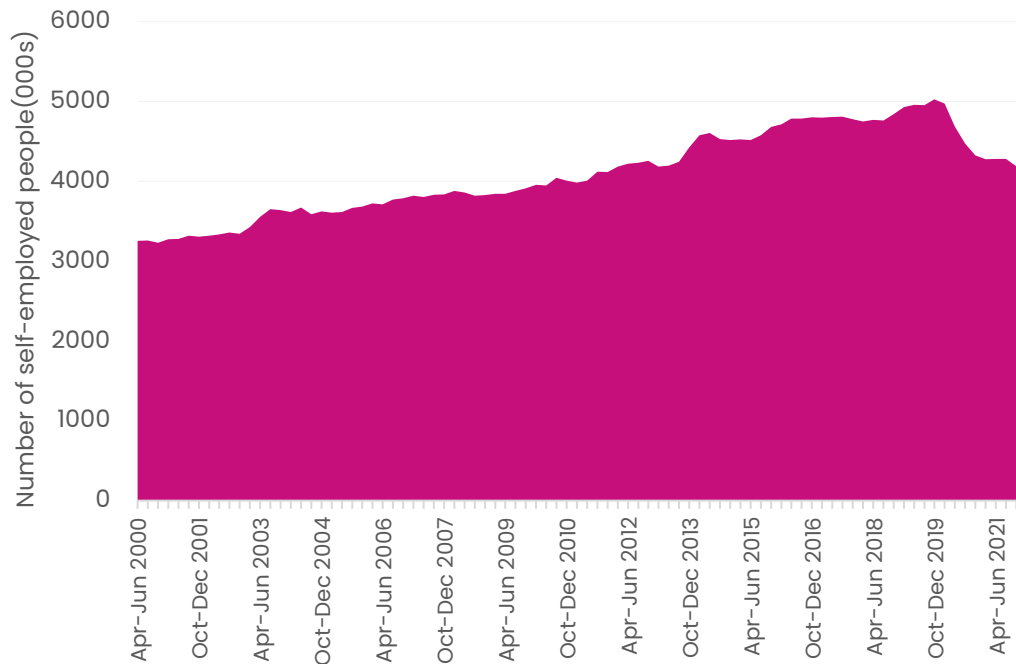


Figure 7: Number of self-employed individuals, March 2000 – March 2022

Source: ONS, *Understanding changes in self-employment statistic*



The decline in entrepreneurship has been driven by one type of business - sole traders. Sole traders are responsible for 95% of the post-pandemic decline in businesses. But the number of private companies that were set up during the pandemic actually increased by 6%.²⁰ Bank of England analysis shows that this was mostly driven by online retail and gig economy businesses born during the pandemic. However many of these businesses have since dissolved.²¹

The decline in self-employment has been from groups with high potential to set up high growth businesses. Those in managerial and professional positions, the highest skill levels, saw a 31% decline (370,000 fewer individuals) in self-employment - the largest decline among all occupation levels from 2020-22.²²

Figure 8: Business population decline from 2020–23, by business type, region, and industry

Source: DBT Business statistics, Onward analysis

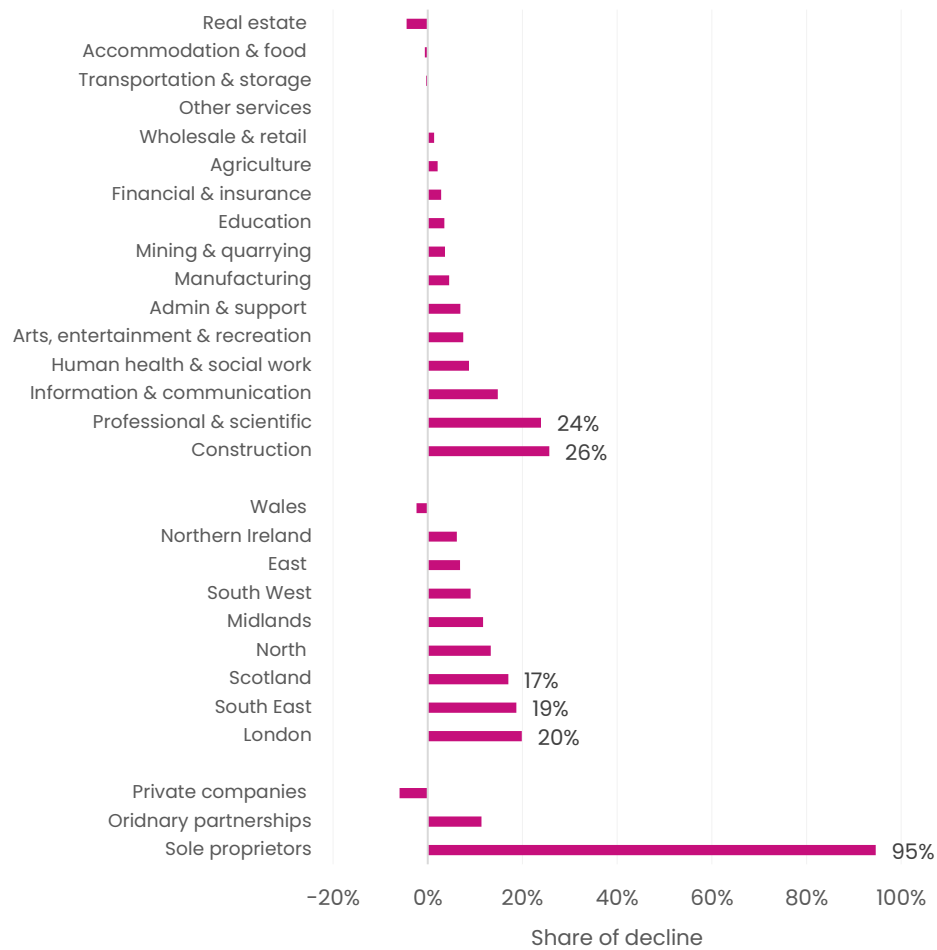
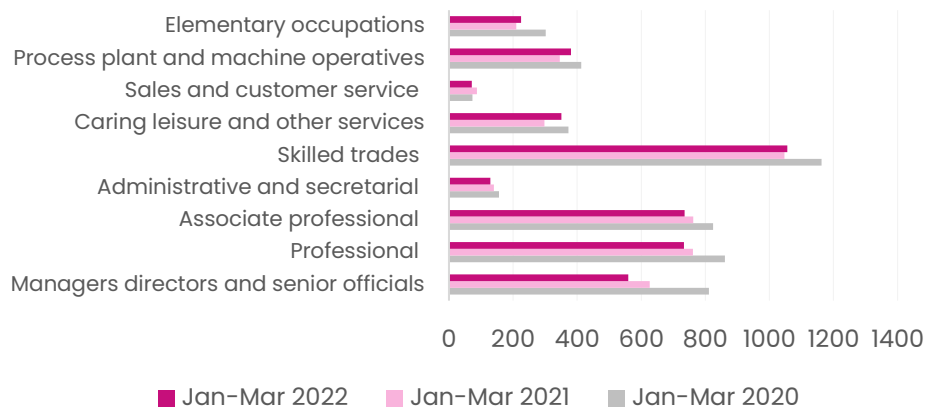


Figure 9: Self-employed individuals aged 16 and above, Jan–March 2020 – 2022, by occupation level

Source: ONS data, Understanding changes to self-employment



Business undercurrents

What is holding back
entrepreneurial Britain?



To drive growth, the Government must focus on promoting growth-oriented entrepreneurship. There are five main challenges to business ownership and growth, explained by original polling by Onward and JL Partners:

1. High costs
2. Poor access to funding
3. Challenging economic environment
4. Low appetite for risk
5. Excessive bureaucracy

Figure 10: Challenges to starting a business, ranked as minor (6-9) and major (1-4) among the general public and entrepreneurs

Source: Onward-JL polling, April 2024

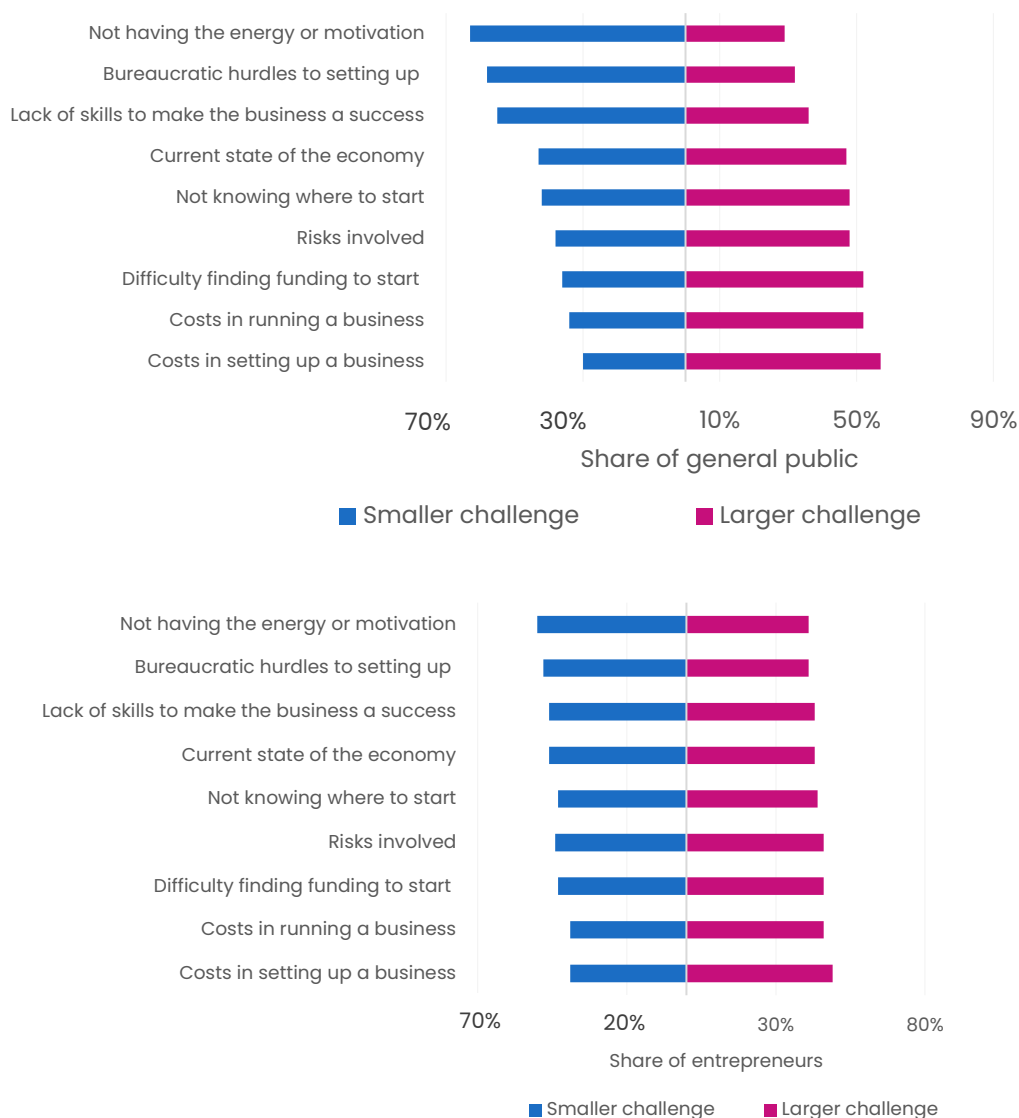
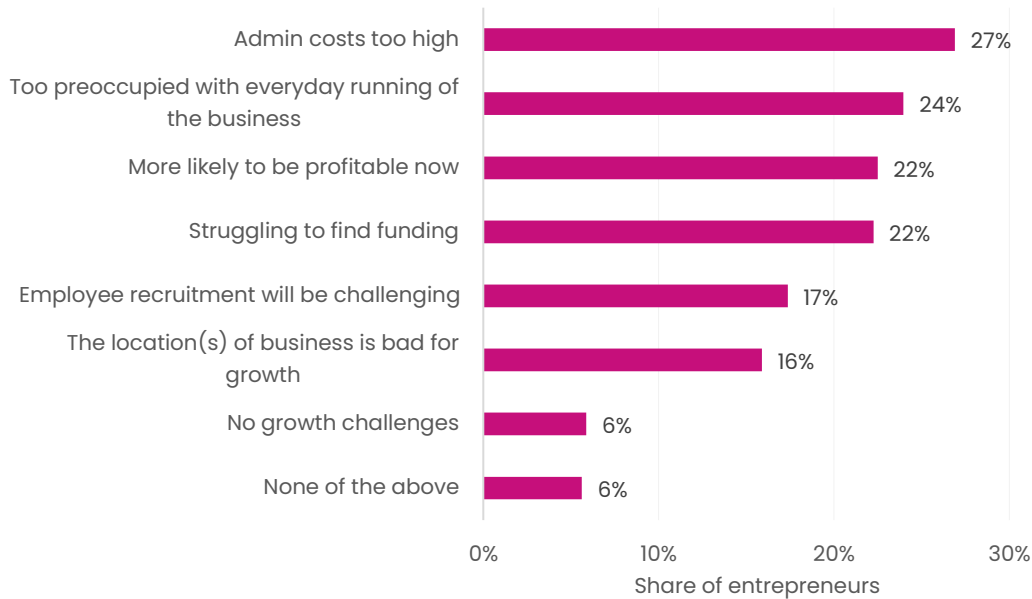


Figure 11: Challenges faced by entrepreneurs in growing their business

Source: Onward-JL polling, April 2024



High costs

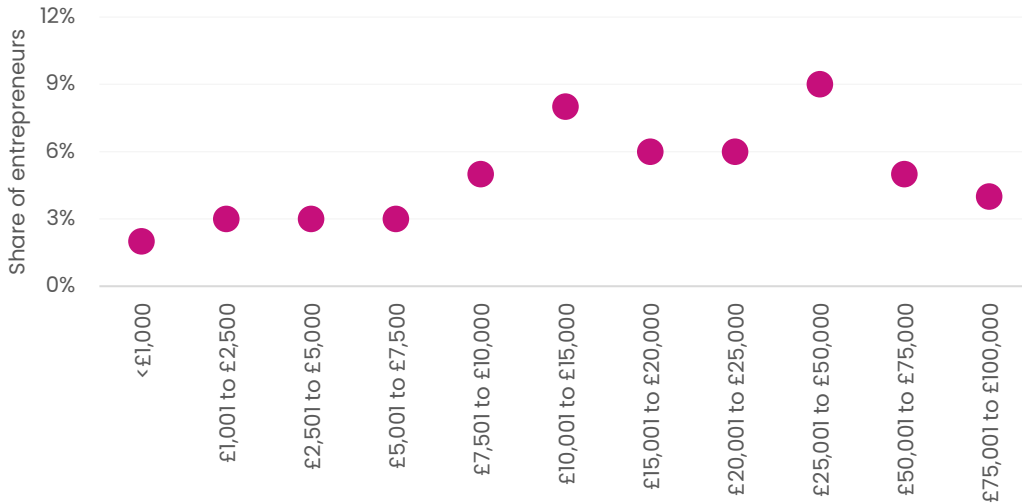
The most pressing concern for both non-entrepreneurs and existing entrepreneurs was practical – the costs involved in setting up and running a business. These included startup costs such as professional fees and licences, and everyday costs like wages and rent for premises. More than half of the general population and 48% of entrepreneurs think that costs are the biggest impediment to starting a business.

The cost burdens are understandably higher for some groups compared to others. But some entrepreneurs feel that costs affect them more. The smaller the business, the more likely they were to report costs as their biggest challenge. Businesses with an annual turnover of less than £250,000 were 11 times more likely than businesses with an annual turnover of over £1 million and above to report costs as their top challenge.²³

However, aspiring entrepreneurs tend to overestimate startup costs. Polling from the Entrepreneur's Network found that aspiring entrepreneurs overestimated startup costs by a multiple of seven. They perceived startup costs to be approximately £35,000, when the average business startup cost is around just £5,000.²⁴

Figure 12: Estimated average startup costs

Source: The Entrepreneur’s Network and American Express polling, February 2024²⁵



The costs for a small business saw a major hike in the first half of 2022, shown in Figure 13 below. These costs were most keenly felt by brick-and-mortar shops and freelancers. Throughout 2022, shops faced a cost burden approximately five times higher than in 2021 and previous years.²⁶ A higher cost burden on high street shops and freelancers are a likely result of burdensome taxes like business rates and IR35, both of which are explored in greater detail later in this chapter.

Figure 13: Small Business Price Index (SBPI)²⁷ by type of small business, 2008q1–2022q3

Source: Enterprise Research Centre²⁸



Onward’s polling of current and aspiring entrepreneurs shows that high costs are the largest barrier to business growth. Two of the top three challenges identified had to do with high costs. Over a quarter (27%) of entrepreneurs felt that administrative costs were too high, and a further 22% thought that they would be more profitable in their current state.

External costs are weighing down on small businesses and holding them back from pursuing greater growth. What are some of these costs?²⁹

Value Added Tax (VAT)

VAT is dampening business growth. The UK has the highest VAT threshold in the world, charging 20% VAT for businesses with a turnover of £90,000 and above.

The high VAT threshold is disincentivising growth for businesses whose turnover is approaching the threshold. Analysis from the Tax Policy Associates shows the dramatic drop off in the number of registered companies, sole traders and partnerships around the VAT threshold.³⁰ They estimate that approximately 26,000 businesses are intentionally staying below the threshold to avoid the 20% VAT bill, and HMRC’s own evaluation found that 20% of businesses were doing so.³¹ And notably, over half the decline after the threshold can be seen among sole traders, shown in Fig 15 below.

Figure 14: VAT threshold in OECD countries 2021, in USD and at purchasing parity power³²

Source: Tax Policy Associates

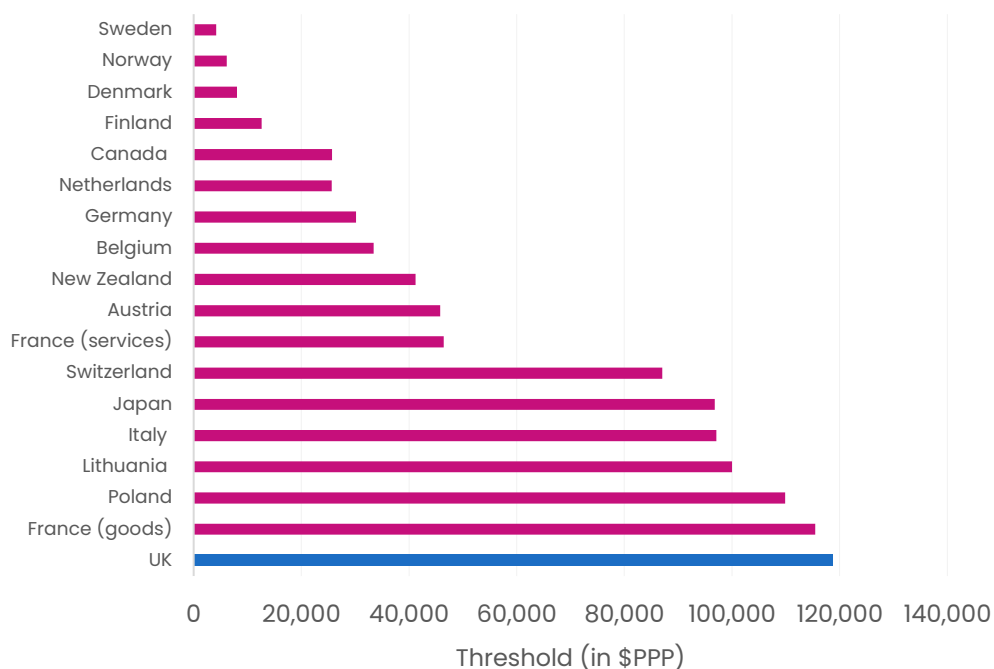
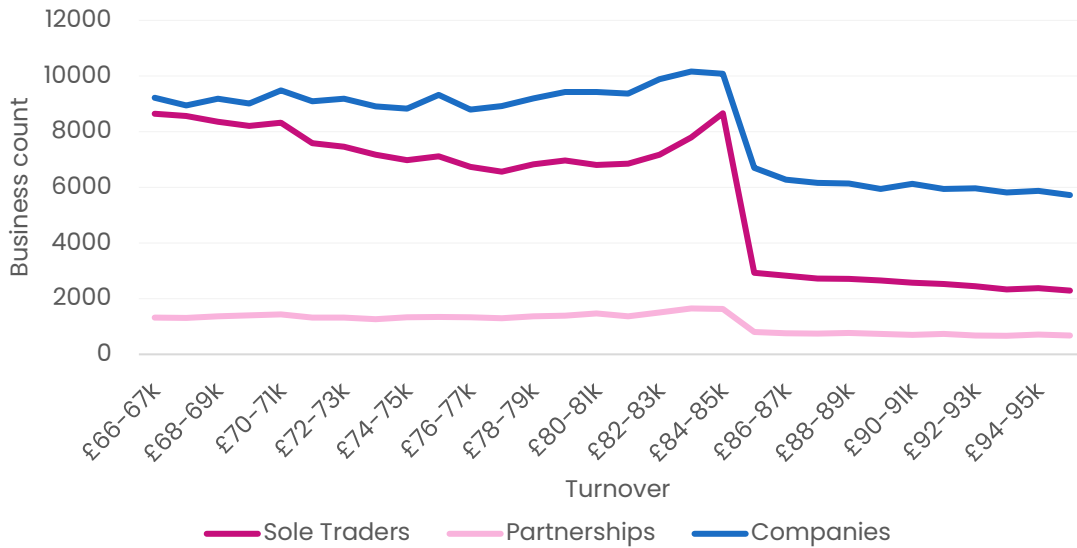


Figure 15: Number of businesses by turnover band and business type, around the registration threshold, 2018-19

Source: Tax Policy Associates



Businesses report concerns that going beyond the threshold would negatively affect their profitability and competitiveness. Of those restricting their turnover, 47% admitted to closing their business or stopping advertising, and 21% were reducing or turning down extra work. Overall, 78% said they could not afford to increase prices to cover the additional VAT costs.³³

Focus group participants were unhappy with the current VAT structure. Jill, an entrepreneur in the hospitality sector said, “VAT bills can be a real killer in your early days of running your business.”

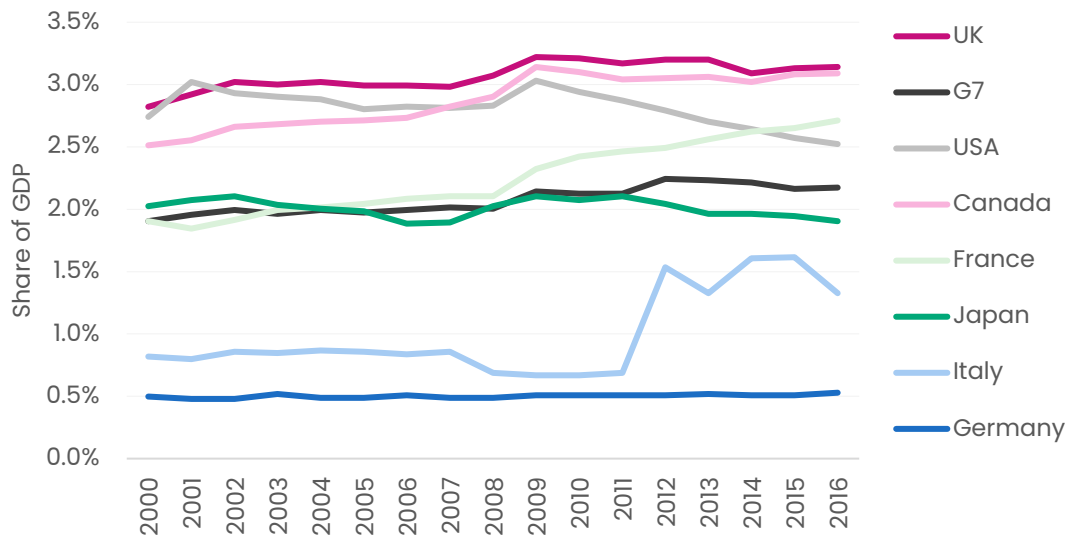
Business rates

Business rates are damaging the high street. While there are significant exceptions for small businesses and businesses located in certain parts of the country, 14p for every £1 of tax paid by an average business goes towards business rates.³⁴ Small or medium sized businesses that are not exempt and those in higher value locations are likely paying even higher rates.³⁵

The UK is uniquely reliant on immovable property taxes compared to other G7 countries. Business rates make up over 3% of the UK GDP, a share that is 45% higher than the G7 average (2.2%).³⁶ And its reliance on business rates has only been increasing over time, compared to countries like the USA and Japan which have seen marked decrease in their reliance on property tax revenues. A high business rate burden makes the UK a less competitive destination for high street investment.

Figure 16: Recurrent taxes on immovable property as a % of GDP, 2000-16

Source: CBI³⁷



The retail sector is especially adversely affected by business rates. In the years leading up to the closure of Selfridges on Oxford Street, business rates for the unit increased from £10.9 million to £17.5 million, a substantial increase in their operational costs.³⁸ The retail sector contributes a quarter of all business rates receipts – nearly £7 billion in 2022-23.

Business rates also disproportionately affect deprived areas in the UK. Analysis from WPI Strategy found that in 2019-20, the business rates burden³⁹ was highest in the North and Midlands. Leigh, in Manchester has a burden seven times higher than Tunbridge Wells. The 50 constituencies with the highest business rate burden pay £54 million more in business rates than the 50 constituencies with the lowest business rates burden.⁴⁰

The fixed cost and administrative complexity of business rates make them burdensome for high street businesses. First, the rates are not tied to a firm's revenue, but rather the rateable value of their commercial property. This negatively impacts those businesses in their early years of operation and running on tight margins.⁴¹ Second, it is not just the amount of business rates, but its administrative complexity that makes it challenging for businesses to navigate. Rates are frequently revised (now set to be revised every three years instead of five), with multiple exceptions and reductions based on size and location, all of which small businesses struggle to keep up with.

Paul, a small construction business owner said, "Taxes are normally based on how much profits you make. But business rates you pay regardless. That is what wipes out businesses."

IR35 or off payroll working regulations

Box 1: What is IR35?

IR35 is a set of tax regulations that determine the tax status of an individual based on whether they are contract labour (i.e. self-employed) or salaried payroll employees.

It was introduced to ensure that self-employed individuals who were effectively serving as employees did not pay less tax. Revisions in 2017 and 2021 transferred the onus of determining an individual's IR35 status from the contractor to the employer to tackle the estimated £440 million in evaded tax.⁴²

Today, if an employer places an individual within the IR35 status, they are treated as a payroll employee and see their take-home pay taxed at the source. They pay in tax up to 30p for every £1 of their take-home pay, forgoing the lower rates of tax that self-employed individuals pay.⁴³

It is more tax-efficient for both freelancers and companies that hire them to have them operate as self-employed individuals rather than salaried employees. Self-employed individuals typically pay less tax than those on the payroll. And companies that hire freelancers also pay less in tax in hiring them as they are not required then to make National Insurance contributions on their behalf.

Introduced to reduce tax fraud, IR35 had poor outcomes. Instead of absorbing the responsibility of determining an individual's IR35 status, several companies have simply placed blanket bans on hiring contract labour. Since the introduction of IR35, 28% of UK businesses have reduced the amount of contract labour they use.⁴⁴

IR35 has priced out freelance and contract labour. The tax bill for freelancers and contract labour increased by £1.5 billion since the introduction of the rules, and in 2021-22 alone, those that were placed within IR35 rules saw their taxes increase by approximately £9,800 compared to those that remained self-employed. 35% of freelancers even stopped their freelance work altogether.⁴⁵ A 2024 evaluation by the Public Accounts Committee found that "HMRC's approach to serious abuse is not deterring criminal activity sufficiently, while at the same time its approach to tackling IR35 is deterring legitimate economic activity."⁴⁶

IR35 guidelines are also ambiguous, meaning that in many cases an individual's self-employment status has to be determined by the courts. A handful of high-profile IR35 cases have become the basis on which HMRC has been updating its guidance on determining an individual's tax status.⁴⁷ Reliance on common law for status determination, where judgements have created a patchwork of complexity, is clearly insufficient.

Funding is hard to access

Funding turns entrepreneurial aspirations into reality. But 52% of the public and 46% of entrepreneurs surveyed perceived difficulty in finding the funding they needed for their business plans. Both groups ranked funding challenges as the second biggest impediment to business ownership, after high costs (Fig 10 above). And nearly a quarter of entrepreneurs cited a lack of funding as a barrier to growing their business (Fig 11 above).

SMEs struggling to secure finance is inevitable, but British businesses find it harder than many others. The Global Entrepreneurship Monitor ranked British businesses' access to finance for entrepreneurship less than sufficient, lagging behind its European counterparts like France, Switzerland and Netherlands, and significantly worse than Middle Eastern countries like Saudi Arabia and the UAE.

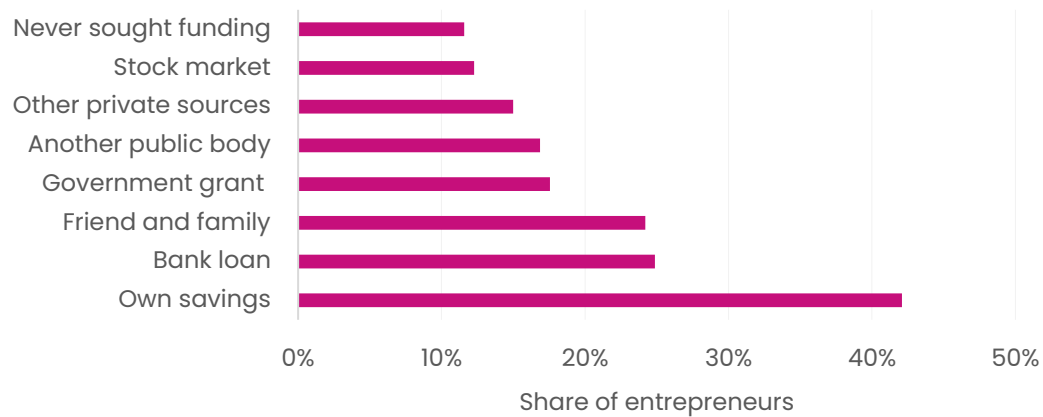
Figure 17: International comparison of ease of accessing finance (debt and equity), 2023

Source: Global Entrepreneurship monitor data



Figure 18: Share of entrepreneurs accessing each type of finance

Source: Onward-JL polling, April 2024



External finance is important because it positively correlates with faster business growth.⁴⁸ This is particularly the case for innovation-oriented growth. Nearly two-thirds (65%) of businesses creating new products and services had accessed external finance, compared to just 58% of businesses that did not innovate.⁴⁹

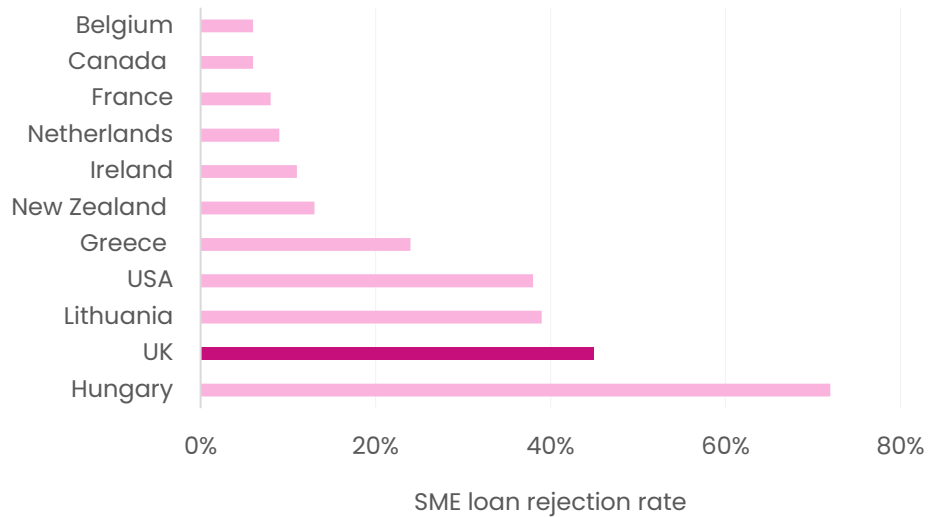
Inadequate finance is therefore stifling growth. In 2022, four in ten small businesses reported being unable to invest in their firms due to a lack of financing options, up from just over one in ten in April 2021.⁵⁰ A 2023 Censuswide survey found that 29% of SMEs had delayed major investments due to insufficient funding with over a fifth delaying investing in new technology or hiring new staff. One in ten ultimately ceased operating due to lack of funding.⁵¹ The challenges in accessing each type of finance is discussed in turn below.

Debt financing is hard to access

The UK has some of the highest SME loan rejection rates in the OECD. In 2022, nearly half of all SMEs (45%) saw their loan applications rejected, lower than only Hungary in the OECD (73%). Other OECD countries like the United States (37%), France (9%), Canada (7%), and Belgium (7%) see much lower rejection rates.

Figure 19: SME loan rejection rates, 2022

Source: OECD, *Financing SMEs and Entrepreneurs*, 2024⁵²



A range of demand and supply-side factors have made debt financing harder to access for SMEs.

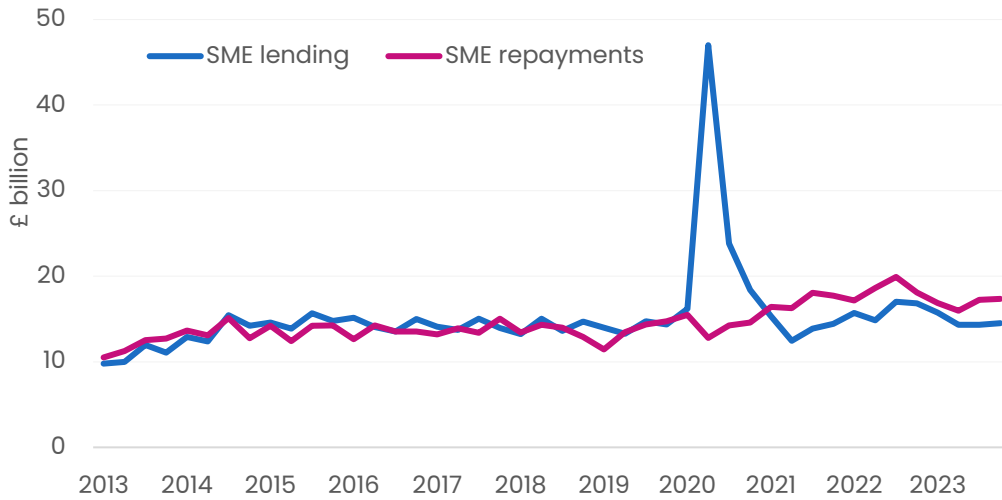
SME demand for debt financing has fallen because business owners want to run down their debt and have a cultural preference to have less debt. The Government ran several loan schemes during the pandemic, including the popular Bounce Back Loan Scheme (BBL) which saw businesses draw nearly £46.6 billion between May 2020 and June 2022.⁵³ But businesses are now focusing their efforts to paying back pandemic debt, with nearly three-quarters of SMEs admitting to wanting to bring down their debt level. An even higher share of SMEs (77%) said they would rather accept a slower growth rate than take on debt to grow faster.⁵⁴

An aversion to debt was also borne out in the focus groups. Simon, an entrepreneur in the digital automotive industry said, “I know it’s a bit oldy worldly, but I’ve always a thought a business should fund its own growth. I thought I should bring in an investor, but I don’t want someone breathing down my neck. The only scenario where I might take money from an investor is if they say here’s a hundred grand, no strings attached.”

The SME preference to bring down debt levels is borne out in the data. Figure 20 shows how SME loan repayment has now outpaced gross lending.

Figure 20: Yearly flows of gross lending and repayments by SMEs, 2013–23

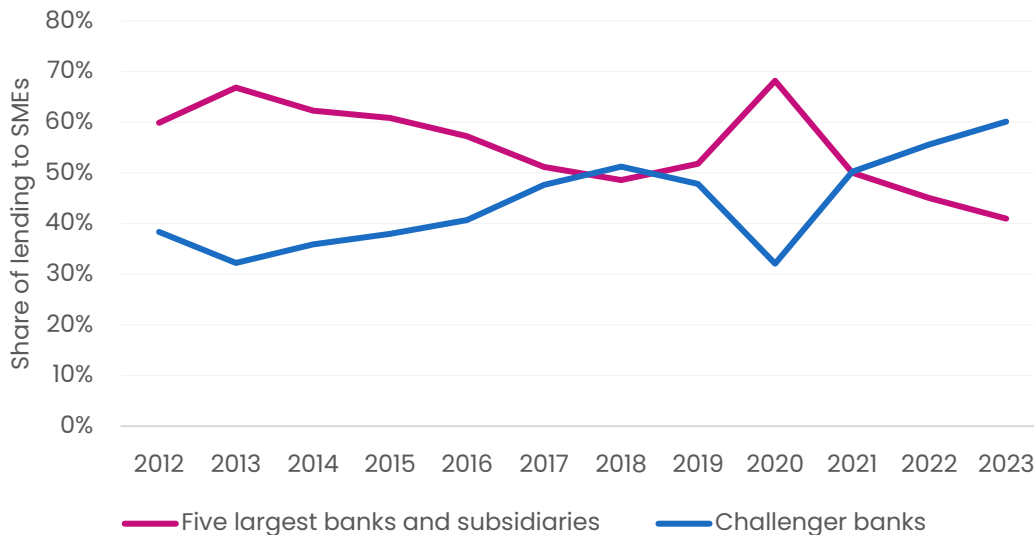
Source: Bank of England Finance and Investment Decisions Survey



Suppliers of finance have also become more risk-averse. Since the financial crisis, big banks have become more reticent lenders. From 2012 to 2023, the five largest commercial banks lending to SMEs have declined by 50%, while smaller, newly established ‘challenger banks’ like Revolut and Monzo have seen their SME lending increase by 50%.⁵⁵ The decline in SME funding from major banks is estimated to have left a funding gap of almost £95 billion between 2015 and 2022.⁵⁶

Figure 21: Share of total gross bank lending to small businesses by type of bank

Source: British Business Bank, Bank of England analysis⁵⁷



A driving force behind the reticence of major banks has been regulation on capital requirements for SME lending called the Basel III regulations.⁵⁸ These regulations were introduced after the global financial crisis imposed minimum capital requirements to reduce the risk of bank runs and to protect their depositors.

Introduction of Basel III meant that banks had to increase their minimum capital requirements from 2% under Basel II to approximately 10.5% of risk-weighted assets.⁵⁹

The UK's Prudential Regulation Authority (PRA) is now phasing out the SME leniency factor in Basel III (renamed as Basel 3.1) between 2025 and 2029. This is estimated to further damage SME financing, reducing the supply of funds to SMEs by £44 billion and increasing the cost of borrowing for SMEs by 1–1.5%.⁶⁰

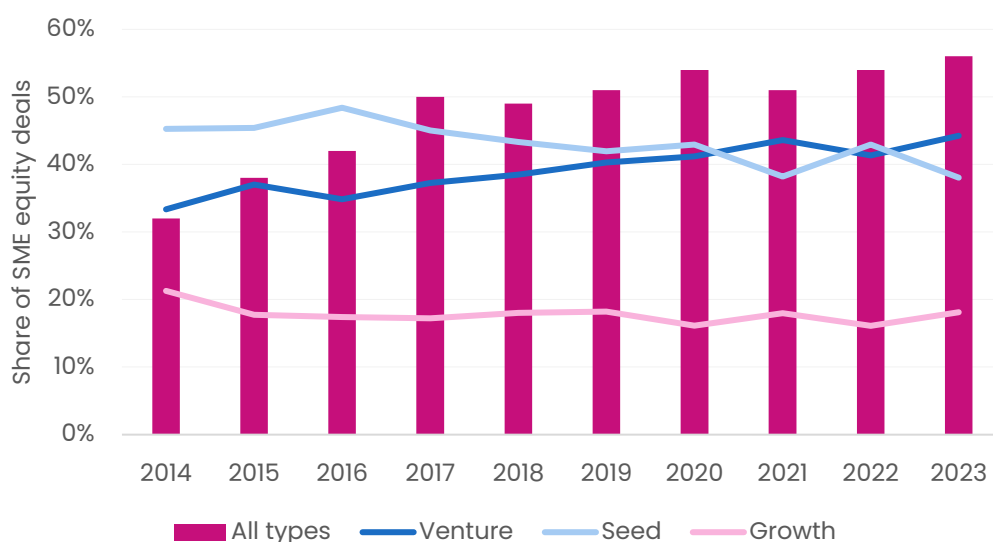
But it is not just risky businesses – established, high-growth businesses are struggling to raise funding too. Evidence from Community Development Finance Institutions (CDFIs) in the UK highlight this. The loans issued by CDFIs to SMEs that have been rejected by mainstream banks see a 90% repayment rate.

Equity finance is the reserve of the few

Equity finance is the least accessed form of small business financing. While the share of small businesses taking up equity deals has been increasing over the last decade, less than 5% of businesses use any amount of equity funding.⁶¹

Figure 22: Equity deals made to SMEs, as a share of all equity deals issued, 2014–2023

Source: British Business Bank SME Finance Monitor^{62,63}



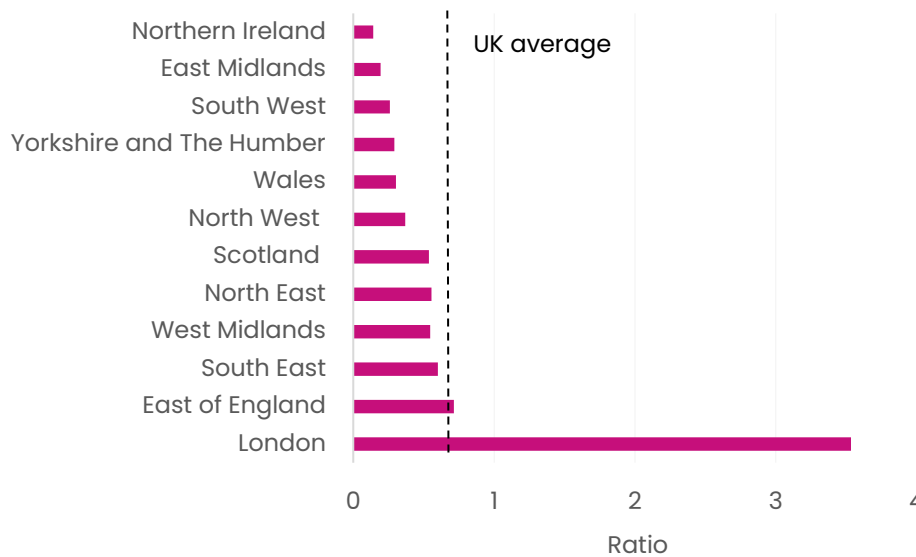
While the UK is a celebrated hub for venture capital (VC), its VC ecosystem falls short in two ways. First, later stage VC in the UK, often geared towards business growth, lags behind the US. VC investment as a share of GDP in the US is 1.4 times higher than in the UK.

Second, UK venture capital does not venture far enough. 80% of venture capital investment goes towards the ‘Golden Triangle’ of Oxford, Cambridge, and London. This is understandable as these regions both have a larger share of SMEs and a more hospitable environment for SME growth. But even after adjusting for SME

population, London still remains far ahead of other regions, receiving over thrice the volume of equity deals compared to Northern Ireland and the East Midlands. Detailed econometric analysis also reveals that the probability of businesses getting equity funding outside is up to 50% lower in nearly all regions outside London.⁶⁴

Figure 23: SME equity deals and value by region and nation, 2020

Source: BEIS Research Paper, 2020⁶⁵



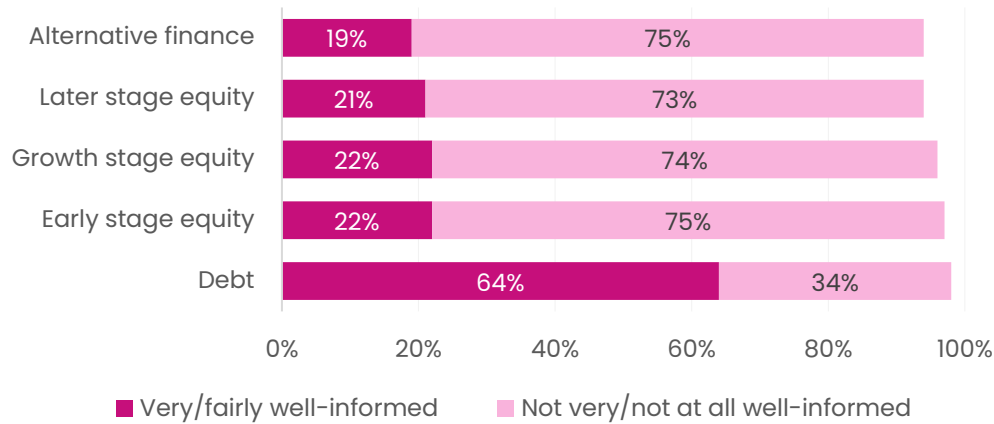
SMEs are not accessing more equity for three reasons. First, entrepreneurs are worried about losing ownership over their business. Polling by the Entrepreneurs Network found that the ‘desire to be your own boss’ and the ‘freedom to do what I want’ were the leading motivations among aspiring entrepreneurs to set up their own businesses.⁶⁶ And equity finance is viewed as a form of funding that sees entrepreneurs lose control over their business.

In a focus group, Paul, a small construction business owner said, “I’ve already got it to the level I dreamed it would be at. And I don’t want to go to that next level where other managers tell me how to do my job. It is just too much.”

Second, there is widespread lack of awareness about equity finance as a viable source of funding. Nearly three-quarters of SMEs reported that they were either not very or not at all well-informed about different forms of equity funding - nearly double the level of those who reported being poorly informed about debt finance.

Figure 24: SME awareness of different types of financing

Source: BBB Small Business Finance Monitor



Finally, the uneven distribution of equity deals is a symptom of the UK's regional wealth imbalances. The frequency of equity deals decreases as the distance between the investor and the headquarters of the business they are investing in increases. Given the concentration of investors in London, over half (52%) of investors in the capital only fund businesses in their home region.⁶⁷

Businesses don't know where and how to find funding

Accessibility challenges are made worse by the fact that the majority of SMEs do not know where to find finance. The British Business Bank found that in 2023, only 60% of UK smaller businesses reported knowing where to obtain information on finance options. In 2016, this figure was 65%.⁶⁸

Extremely poor levels of awareness of the British Business Bank symbolises the challenge of SMEs not knowing where to find funding. Just 22% of SMEs reported knowing the bank existed.⁶⁹

Businesses that have had expert training are much more successful in finding suitable financing. Alumni of the Goldman Sachs 10,000 Small Business programme are more successful in their applications for external finance. Whereas 40% of alumni, who were trained in funding by leading experts on the programme, were successful in utilising external finance in a 12 month period, only 27% of their high-potential peers did so.⁷⁰ Those without an insight into or understanding of their options are less able to access finance.

The Bank of England survey highlights a correlation between businesses' perceptions of their investments and access to finance. Of those who said they felt they had invested too little, 29% believed their application would be unsuccessful. Those that said they had invested appropriately were less negative regarding their access to finance.⁷¹

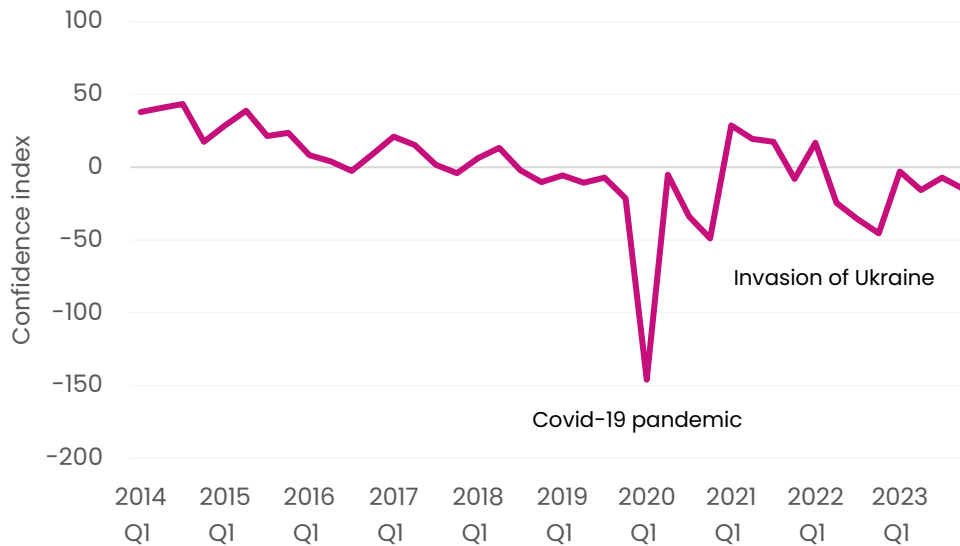
Challenging economic environment

The wider population and the entrepreneurial community overwhelmingly feel that the current state of the economy does not support entrepreneurship. With the economic slowdown since 2020 and the impact on living costs following the war in Ukraine, it is hardly surprising that over half those surveyed (52%) believe the dire state of the economy was a significant barrier to setting up a new venture.

Other polls also show an overarching negative economic outlook among SMEs. The Federation of Small Business's 'Confidence Index' indicates negative confidence in the country's economic environment since 2022 and during the early parts of the Covid-19 pandemic. Recovery to 2014 levels would require a 143% increase in confidence levels.

Figure 25: Small business confidence index

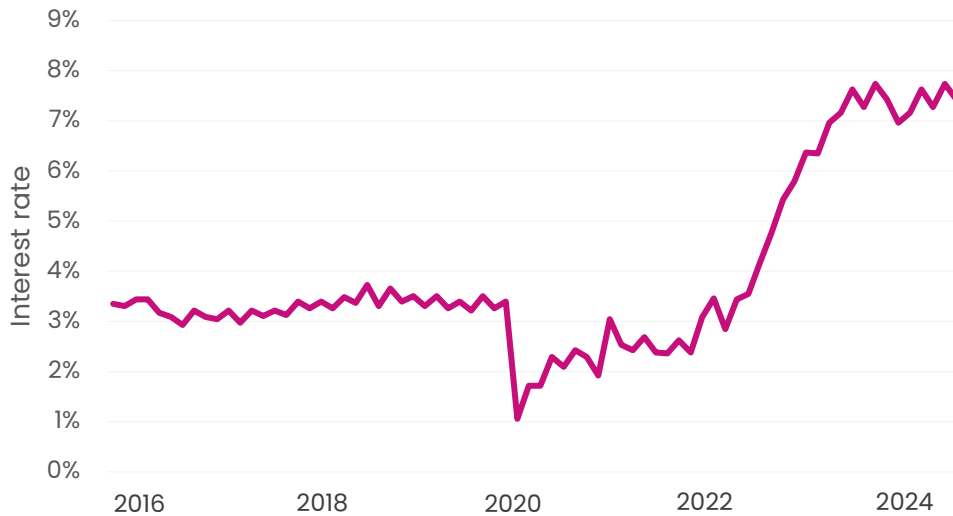
Source: Federation of Small Business



Their fears are corroborated by the evidence on the impact of the economic environment on SMEs. Interest rates for SMEs are the highest they've been in the last decade. Interest rates on new business lending was 7.5% in December 2023, over double the 3.2% rate charged on average in 2016.⁷²

Figure 26: Effective interest rates for new businesses, 2016–2023

Source: British Business Bank, Bank of England⁷³

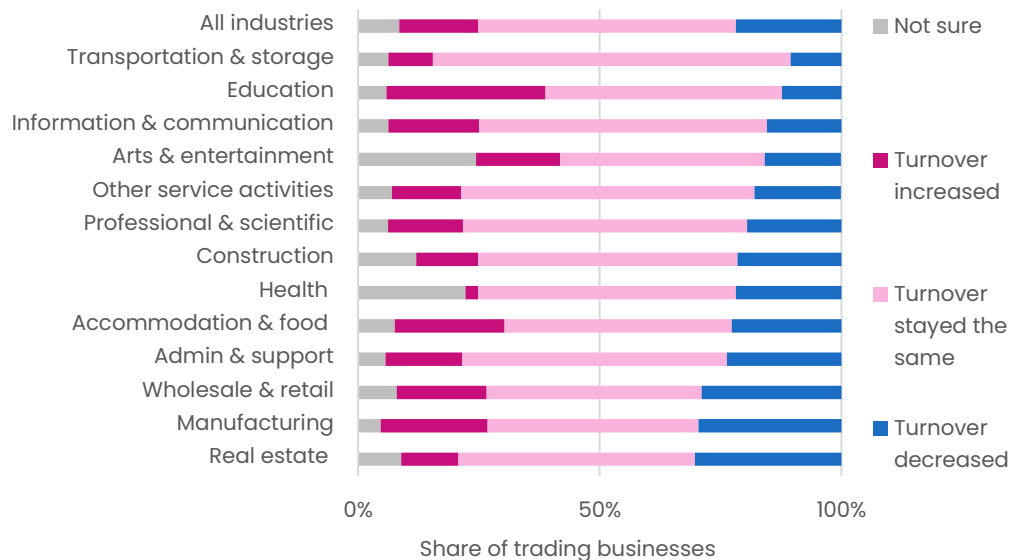


More than 1 in 6 businesses (17%) also reported that their business performance had fallen from 2023-24 - especially in sectors like accommodation and food services and manufacturing.

Over half of all trading businesses reported no change to their turnover. Nearly 22% of businesses reported a decrease - the highest decreases noted in sectors like real estate, manufacturing, and wholesale and retail. This compares to just 16% of businesses that reported an increase in their turnover - notably in sectors like education and hospitality.

Figure 27: Reported changes in performance, by industry, March 2023–24

Source: ONS BICS Survey



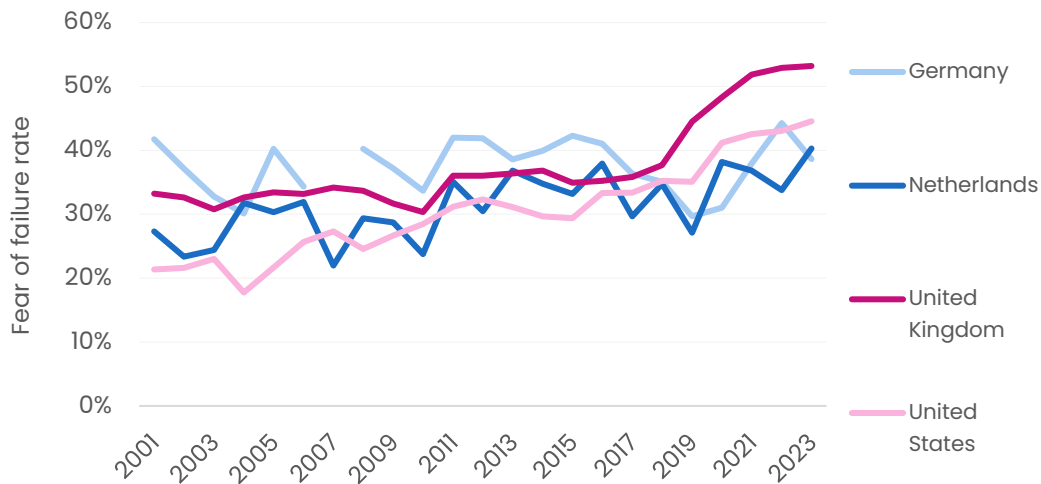
Despite a gradually recovering economy, businesses do not feel optimistic about the future. Nearly half of all businesses expect their business performance to stay the same over the next year, with even fewer (21%) expecting their performance to improve.

Low appetite for risk

British entrepreneurs are unusually risk averse and becoming more so with time. The fear of failure rate in the UK is 20% higher than the world median and the US. As of 2023, over half (53%) of the British working population were held back from starting their own businesses by a fear of failure, compared to 45% in the US, 40% in Netherland, and 39% in Germany, shown in Figure 29 below.

Figure 28: Fear of failure rate⁷⁴ across different countries, 2001-23

Source: GEM Adult Population Survey



The most risk-averse entrepreneurs in the UK are more likely to be older and run small-mid sized businesses. Businesses with an annual turnover of between £250-999,000 were almost six times more likely than those earning less than £250k and five times more likely than those with a turnover of £25 million and above to say to be unduly risk-averse.⁷⁵

Similarly, those businesses with between one and ten employees also reported being the most risk-averse - even more than sole traders and large businesses employing over 250 businesses. A survey conducted by the Federation of Small Businesses (FSB) in 2022 revealed that 65% of micro business owners are willing to take significant risks to grow their business, compared to only 40% of mid-sized business leaders.

Evidence from the Bank of England also shows it is medium sized businesses are most financially risk averse. Medium-sized businesses were found to prioritise debt repayment and cautious investment strategies, reflecting their risk averse preferences. Specifically, around 77% of surveyed businesses preferred slower growth to avoid borrowing, indicating a reluctance to take on debt despite potential growth opportunities.⁷⁶ Their conservative financial behaviour becomes even more pronounced in periods of economic uncertainty, reinforcing their over-reliance on internal funds.⁷⁷

Overall, mid-sized businesses are more likely to prioritise maintaining their market position and protecting existing assets, whereas micro businesses, which typically have fewer resources, may pursue riskier strategies in hopes of rapid growth or breakthrough success.

Regardless of size, the aversion to risk is driven largely by economic concerns. Onward polling found that the top three underlying risk factors for entrepreneurs were all economic: the current state of the economy (27%), impact on future job prospects (22%), and a loss of money (22%).

Figure 29: Drivers of a fear of failure among entrepreneurs

Source: Onward-JL polling



But even the economic risk concerns are underpinned by a deeper cultural preference for low risk in the UK. Tom Blomfield, entrepreneur and founder of the multimillion dollar online bank Monzo commented:

“There’s a pessimism in the UK that often makes people believe they’re destined to fail before they start. That it’s wrong to even think about being different. Our smartest, most technical young people aspire to work for big companies with prestigious brands, rather than take a risk and start something of their own.”⁷⁸

University graduates in the UK are shying away from entrepreneurship compared to the US. Just five UK universities rank among the top 100 for producing successful entrepreneurs, compared to ten from the state of California alone.⁷⁹

Table 1: Number of entrepreneurs, number of companies founded, and amount of capital raised by university of undergraduate education

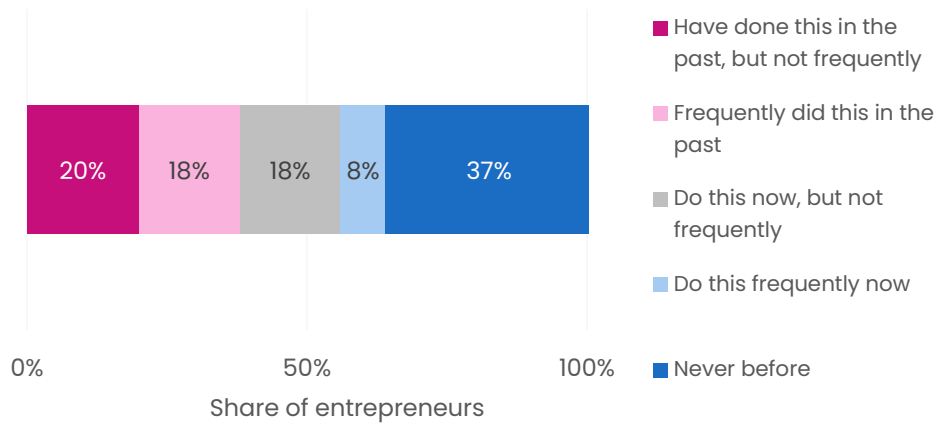
Source: Pitchbook data, 2023⁸⁰

Rank	University	Number of founders	Companies founded	Capital raised
1	Stanford University	1435	1297	\$73.5 billion
2	University of California, Berkeley	1433	1305	\$47.5 billion
3	Harvard University	1205	1086	\$51.8 billion
4	University of Pennsylvania	1083	993	\$34 billion
5	MIT	1079	959	\$46 billion
7	Tel Aviv University	825	692	\$26.3 billion
11	Yale University	638	594	\$24 billion
30	Tsinghua University	443	418	\$28.4 billion
46	Indian Institute of Technology, Madras	301	266	\$14.2 billion
50	University of Oxford	286	275	\$8.4 billion
61	University of Cambridge	262	253	\$8.2 billion
79	London School of Economics	216	210	\$4.8 billion
87	University of London	190	185	\$5.6 billion
100	Imperial College London	162	152	\$3.5 billion

But there is an emerging trend of ‘side hustles’ that is derisking entrepreneurship. The average person no longer has just a single job. While they may have a primary source of income, most Britons have a portfolio of jobs. This includes smaller revenue streams like freelance work, selling products online or at a flea market. Onward polling found that almost two-thirds (63%) of entrepreneurs reported having some kind of side hustle, with a quarter (26%) reporting currently operating such a venture.

Figure 30: Frequency of engaging in side hustles among entrepreneurs

Source: Onward JL polling, April 2024



Side hustles equip aspiring entrepreneurs with the skills to set up something more permanent. 46% of small business owners reported that their side hustles helped them to quit their jobs and start their own businesses.⁸¹ They also derisk the transition into full-time entrepreneurship by providing supplemental income. A 2018 BEIS survey found that 65% of side hustlers said gig work was less than 5% of their total income, and only 9% earned more than 90% total income through the gig economy.⁸²

Bureaucracy

While entrepreneurs did not rank bureaucracy as one of the top barriers to business ownership and growth, many felt it was dampening everyday business operations.

The evidence makes clear that British businesses face significant bureaucratic challenges. The Federation for Small Business estimates that small business owners spend over 33 hours per month on administrative tasks, representing almost a quarter of their working hours.⁸³ And a worrying two-thirds of businesses say that excessive red tape is preventing them from focussing on their core business functions.⁸⁴

The most notable bureaucratic hurdle for business stem from poor infrastructural support for businesses. Businesses find the planning system cumbersome to navigate to secure new premises and expand their operations.

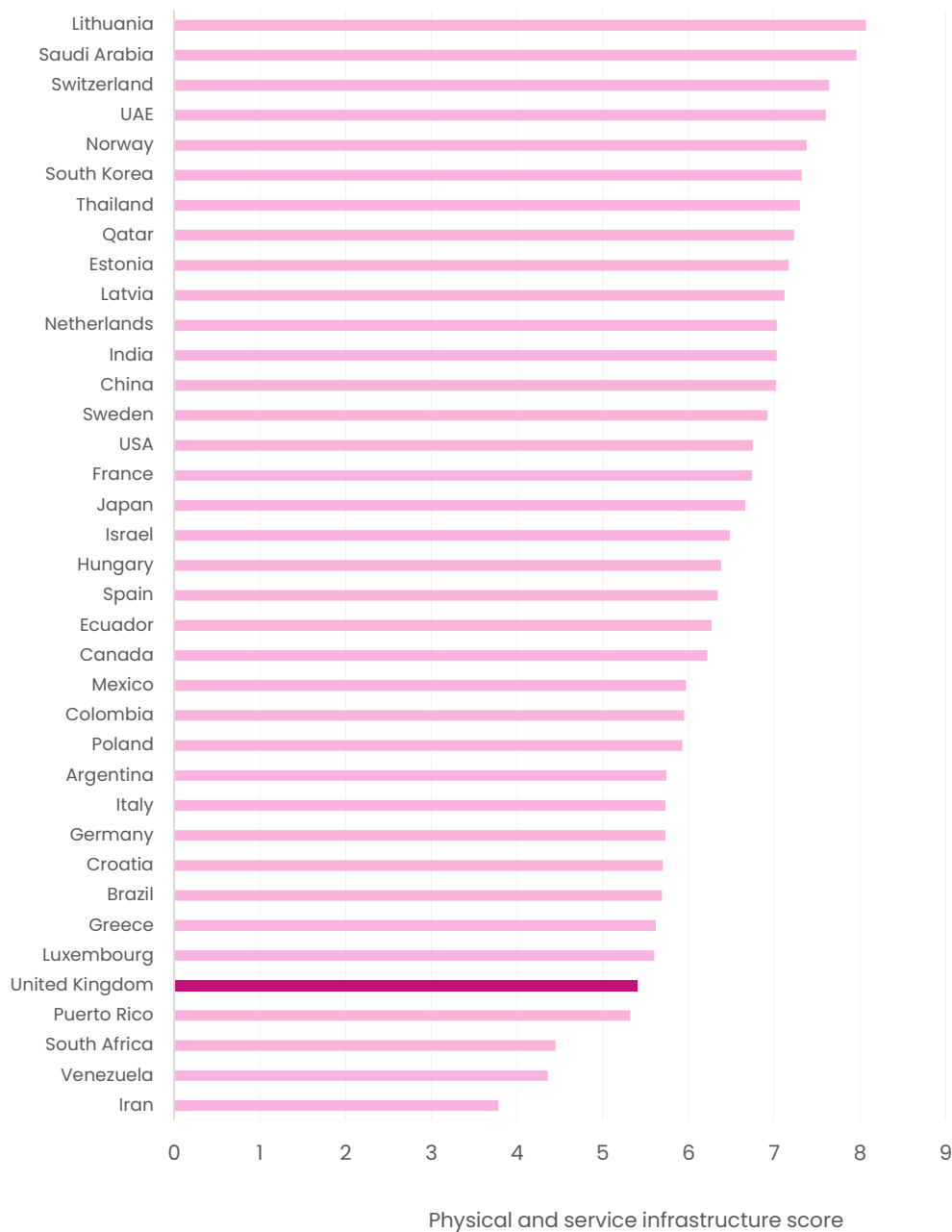
Elliott, a founder of a wellness clinic commented in focus groups about the delays he experienced: *“When we were expanding to our new clinic, the council investigated the work we were doing and took six to eight weeks to complete the investigation. And it took us another two months to implement what they wanted done, and I was left paying rent on two sites for a longer time than I would have liked*

to, and this all increased the cost of my expansion by about 40%. That was quite tough.”

An international comparison of the extent to which physical and service infrastructure supports entrepreneurship ranked the UK the worst among all Western countries.⁸⁵ It performed 30% worse than Norway and 23% worse than the Netherlands.

Figure 31: International comparison of physical and service infrastructure to support entrepreneurship, 2023

Source: Global Entrepreneurship Monitor



HMRC's own review of its interactions with small businesses found that only 35% of SMEs thought the department was efficient and didn't waste taxpayer money.⁸⁶

Focus group participants had negative views of HMRC's handling of SMEs. Jill, an entrepreneur in the hospitality industry said, "A lot of these checks are just time wasting. We had HMRC come down to do a review and it took a whole day. They were checking us for minimum wage standards - that shouldn't have had to take a whole day, and you know you are paying them minimum wage because you can't hire them if you don't. I lost a full day of work." Amy, an operations entrepreneur said, "If you need to get a hold of HMRC on the phone, it takes ages." In 2023, taxpayers spent the equivalent of 798 years on hold waiting to speak to a HMRC call operative.⁸⁷

HMRC bureaucracy handicapping entrepreneurship was most pronounced during the pandemic when a large number of entrepreneurs and freelancers were left with minimal financial support. An independent inquiry by the Public Accounts Committee found that nearly 1.1 million entrepreneurs had been excluded from covid-19 grants like the SEISS, including 0.7 million limited company directors and 0.4 million freelancers.⁸⁸ The error was found to be a result of HMRC failing to hold adequate information and data regarding the nature of self-employment of these individuals.

Excessive bureaucracy is bad for business because it dampens productivity. In 2017, the UK lost approximately £40 billion in GVA to administration, the highest of all countries surveyed barring the United States. This was a result of businesses losing nearly 6% of their time to administration, compared to less than 5% in Australia and the United States, and less than 4% in Germany, shown in Table 2 below.

Table 2: Comparison of economic losses from time spent on administration

Source: SAGE and Plum Consulting data, 2017⁸⁹

Country	Share of time lost to administration	Implied loss in productivity (£ billion)
United Kingdom	5.6%	39.9
France	7.7%	37.8
Ireland	3.5%	1.9
Australia	4.9%	16.2
Canada	6.5%	10.3
Singapore	5.5%	5.8
United States	4.9%	261.5
Germany	3.7%	24.3

The pipeline of entrepreneurial talent

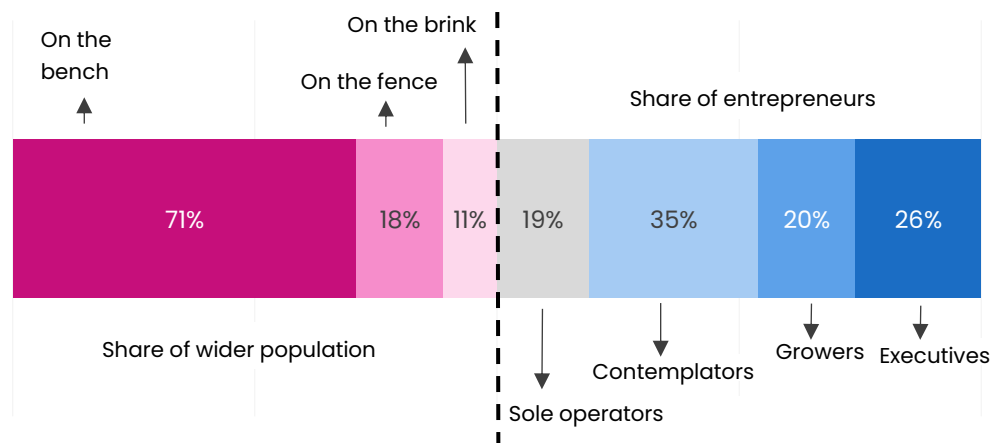
Who are Britain's current and
aspiring entrepreneurs?



The challenges facing Britain’s entrepreneurs are multifaceted and vary by characteristics of the business and entrepreneur. To understand how to support Britain’s entrepreneurs and potential future entrepreneurs, understanding Britain’s current and aspiring entrepreneurs and their unique challenges is crucial. They can be grouped into seven distinct categories (Figure 32).

Figure 32: Pipeline of entrepreneurs: aspiring to current

Source: JL polling, Onward analysis, April 2024



The pink colours show non-entrepreneurs, grouped based on their likelihood of starting a business. Grey and blue segments show current entrepreneurs based on their growth aspirations. Each of these groups have been explored in greater detail below.

The general public can be grouped into three categories based on their likelihood of starting a business:

Group 1: On the bench

This group is the least likely group to set up their own business, reporting less than a third likelihood of starting their own business. Majority in this cohort have never participated in any side-hustle activities (51%), and even fewer have owned a business in the past (8%).

This group is predominantly older, from lower socioeconomic backgrounds, and employed in low-income jobs. Over half (54%) of the group is aged 55 and above, and earn less than £30,000 annually. Just 2% of this group have an annual income greater than £100,000. Nearly half of this group report being unemployed. 64% of this group are either semi-skilled workers, casual workers, or pensioners.⁹⁰ They are also more likely to be a woman and have a male-female ratio of 9:11.

They tend to view salaried employment as a source of stability, even at the cost of being employed in a low-wage role. A total of 28% of the group think salaried employment is more attractive than business ownership, the highest level of agreement among all aspiring entrepreneurs. But this group also have the most constricted view of entrepreneurship. Two-thirds of this group think that entrepreneurs have to be inventors, whereas less than a third of the group think owning a shop makes someone an entrepreneur.

They also tend to feel that their current roles and sectors are not entrepreneurial. Majority report that the sector they work in, the skills they've picked up, or the occupational level they operate at benefit any future plans to start a business.

Entrepreneurship is not the chosen professional path for those on the bench. They are content in salaried employment and are likely to make better employees than entrepreneurs. Targeting public policy to encourage them to pursue entrepreneurship is unlikely to yield success - for them or the country as a whole.

Group 2: On the fence

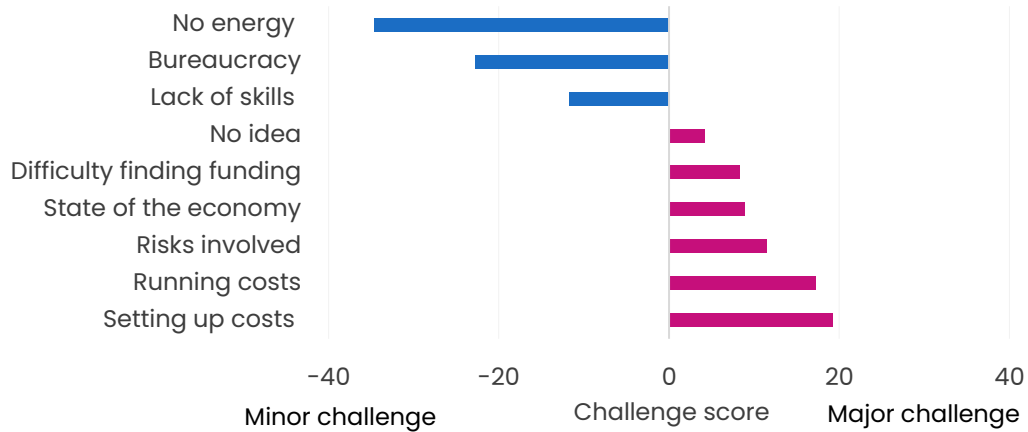
The on the fence group exhibit some level of interest in starting their own business, reporting between a third and two-thirds chance of starting their own business. Over a quarter of this group have owned a business in the past, and as many as 84% of them have at least once earned income from a side-hustle. In fact, over a third report currently being engaged in side projects other than their primary job.

This group is predominantly younger, earning an average income, and employed in middle managerial roles. Over half the group is less than 34 years old, earning an annual income of between £30-70k, and operating at either intermediate or middle management levels in their current jobs. This group has a near equal gender split - 52% are men and 48% are women.

When asked about the biggest challenges to starting their business, this group reported costs as their top concern. The costs of setting up a business is their top concern, followed by the everyday costs of running a business.

Figure 33: Challenge score⁹¹ for those on the fence

Source: JL polling, Onward analysis, April 2024

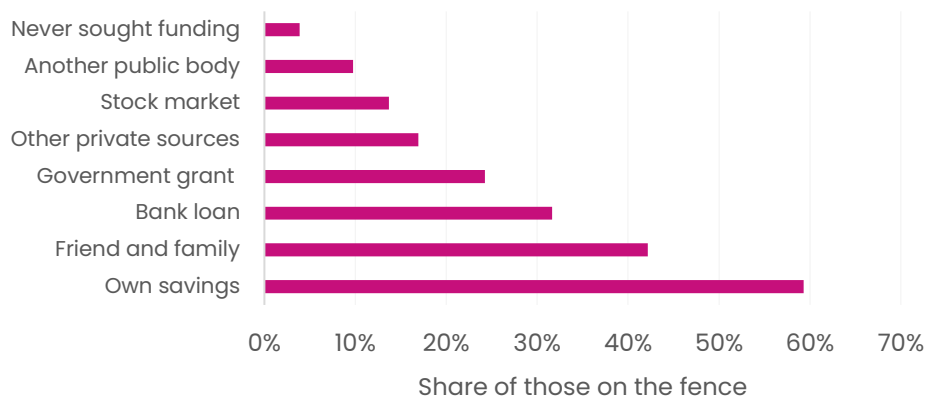


Unsurprisingly, costs were the largest concern for those on the lowest incomes. Those on the fence that earn an annual income of between £30-50,000 were three times as likely to report that costs were a roadblock to starting their own business compared to those on incomes less than £30,000 and between £50-70,000.

Cost pressures for this group are made worse by their over-reliance on their own savings to finance their business ideas. Nearly three times as many of those on the fence rely on their own savings compared to bank loans. And only 17% report having accessed other private sources like venture capital and investment funds.

Figure 34: Sources of funding accessed by those on the fence

Source: JL polling, Onward analysis, April 2024



Those on the fence are likely to be in their early stages of finding funding for their business plans. Their biggest funding challenges are in accessing private funding, where over six in ten struggle, and in taking the first steps to secure funding. 48% of this group say they have heard of different sources of funding but do not know

where to find them. Of those who reported struggling to access private funding, only 20% have attempted accessing funding from a private source.

This group is most likely to view entrepreneurship as the best occupational stepping ladder in the industries they work in. Nearly a third of those on the fence feel that entrepreneurship is the best way to progress in their respective industries. Compared to those on the bench, a much higher share of this group think the sector they work in and the skills they've picked up will benefit their entrepreneurial ambitions. And 40% of this group think they have an occupational advantage in starting a businesses - that their current occupation level will have a positive impact on their business leadership.

There is no clear policy that would encourage those on the fence to take the next step in their business journey. But they require support to take the next steps and realise their entrepreneurial ambitions. They are likely engaged in side hustles (but not frequently). The kinds of support they are likely to benefit from are more guidance and training that expose them to realities of pursuing entrepreneurship full-time.

Group 3: On the brink

Those “on the brink” report a two-thirds or higher likelihood of becoming an entrepreneur. Majority of this group has owned a business before, and an even larger share of them have engaged in a side hustle at some point in their lives. They are a highly entrepreneurial group - a third of this group are currently engaged in a side hustle.

Relative to other groups, those on the brink are most likely to be male, younger, in well paid senior roles with higher degree educational qualifications. 57% are male and less than 34 years old. They have the highest share of those educated to Level 4 and above (50%), and a quarter of this group have a university degree. Relative to those on the bench and on the fence, this group has the largest share of high income earners - 11% of this group earns over £100,000 annually, compared to just 4% among those on the fence and 2% among those on the bench. Over one in five of those on the brink are also senior managers or C-suite executives.

Economic comfort and security in their salaried roles means they might perceive greater risks to starting their own business. Fabian, an automotive manager and aspiring entrepreneur said in focus groups, *“Most successful startups have a steep starting curve. And that means that I have to accept that in the beginning especially it might be quite frustrating without much reward. And compared to my current salary as a manager, it is a tough choice.”*

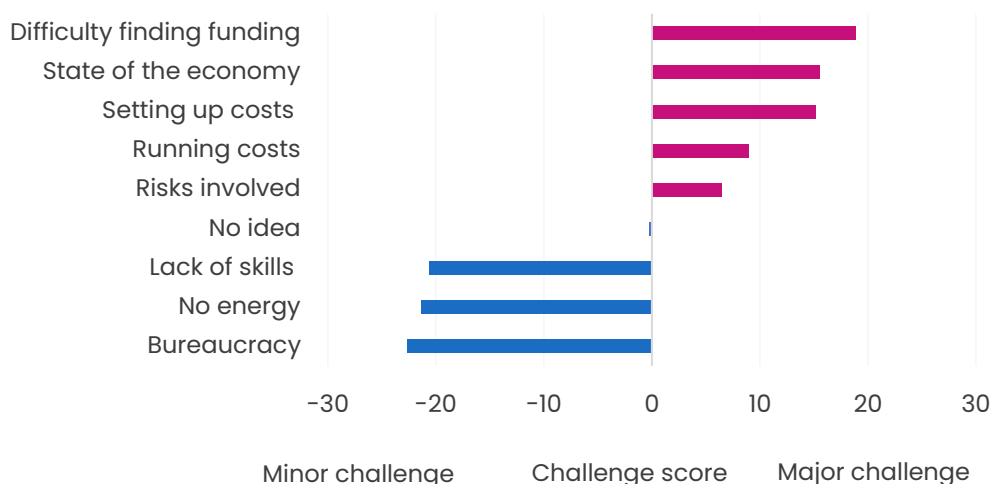
This group is most confident that their past experience will aid their entrepreneurial goals. They are confident in their skills to start a business - either in the sector they currently work in or a new sector altogether. And over half this group think that their relative seniority within their current roles will aid their entrepreneurialism.

Their confidence is rooted in evidence. Analysis from the former Department of Business, Energy, and Skills (DES) found that among the best performing businesses, 84% had managers with degrees, compared to just 54% of businesses that performed poorly.⁹²

Expert training is shown to help entrepreneurs find the right funding for their business, yet those with the best credentials still struggle to find funding. Those on the brink ranked difficulty finding funding as the top concern holding them back from starting their businesses.

Figure 35: Barriers to starting your own business among those on the brink

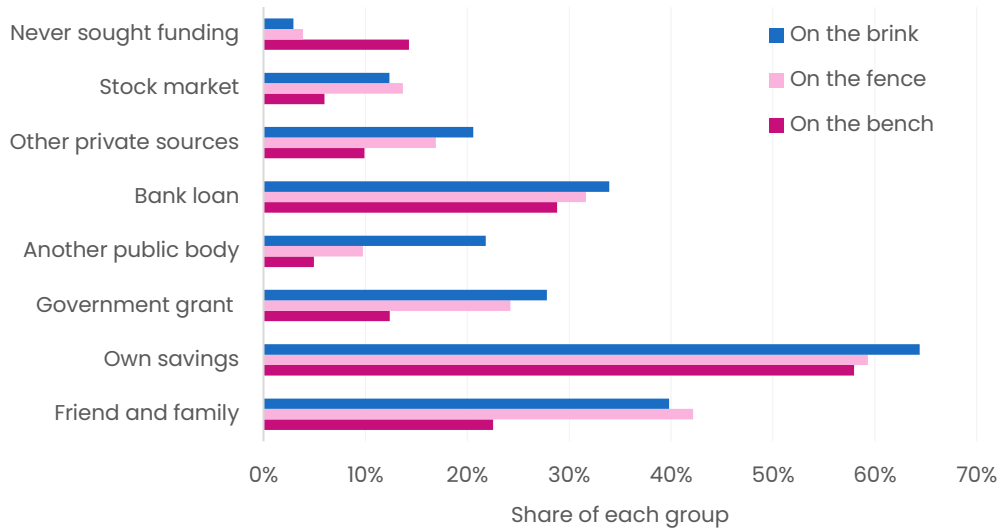
Source: JL polling, Onward analysis, April 2024



But unlike other groups, those on the brink have taken their first steps towards setting up their businesses. They have sought funding from a much wider variety of sources, including grants from organisations like the British Business Bank, and private sources like venture capital. But despite their broader reach of funding sources, over six in ten of this cohort find both government and private funding harder to access.

Figure 36: Sources of funding accessed by aspiring the general public, by likelihood of starting a business

Source: JL polling, Onward analysis, April 2024



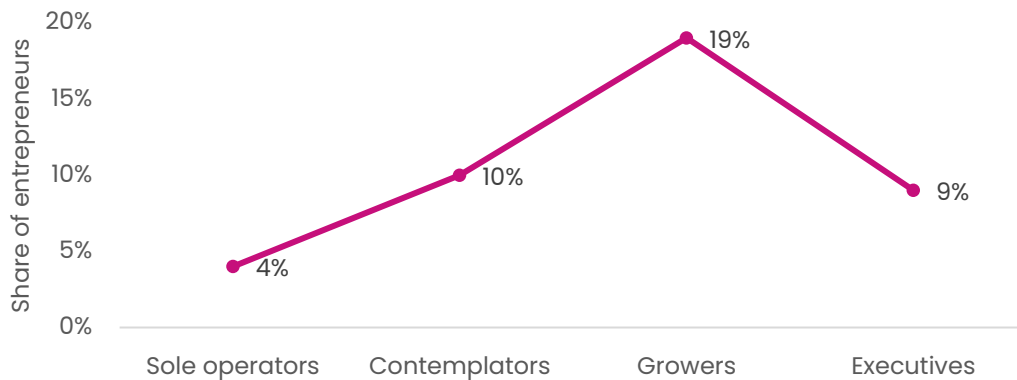
Current entrepreneurs be grouped into four based on their growth aspirations:

Group 4: The sole operator

“The sole operators” represent 19% of our sample and explicitly state they are uninterested in growth. They are content in their current state of self-employment - of all the groups of entrepreneurs, sole operators are least likely (just 4%) to report finding salaried employment more lucrative.

Figure 37: Share of entrepreneurs who find salaried employment more attractive than self-employment

Source: JL polling, Onward analysis, April 2024



This group is predominantly male and older. Of all the groups of entrepreneurs, sole operators have the highest share (16%) of entrepreneurs educated to just Level 1 and 2.

Sole traders (58%) make up the bulk of this group. Most of them run businesses that turn over less than £250,000 annually (62%) and employ a maximum of one employee (43%). They have limited experience running businesses - over 60% of this group have never owned a business before.

Having no legal distinction between the business and the entrepreneur makes daily business management burdensome on the entrepreneur. Most sole operators have to fill in Self-Assessment forms for which they are required to accurately calculate their income, expenses, and allowances. They also have to submit regular VAT returns which requires meticulous bookkeeping and keep track of different classes of National Insurance contributions. While these are standard business processes, sole operators, as their name suggests, rarely have dedicated business departments or employees to handle these functions.

The 2024 Conservative manifesto pledge to abolish National Insurance (NI) contributions for the self-employed was likely targeted at this group. Self-employed individuals typically pay 6% NI on basic rate incomes, and 2% on incomes higher than £50,270.⁹³

Unsurprisingly then, sole operators are too consumed by daily business tasks to think about growth. They report high admin costs and being too preoccupied running their businesses as the main reasons for both not pursuing growth as well as in running their business shown

Figure 38: Barriers to growth among sole operators

Source: JL polling, Onward analysis, April 2024

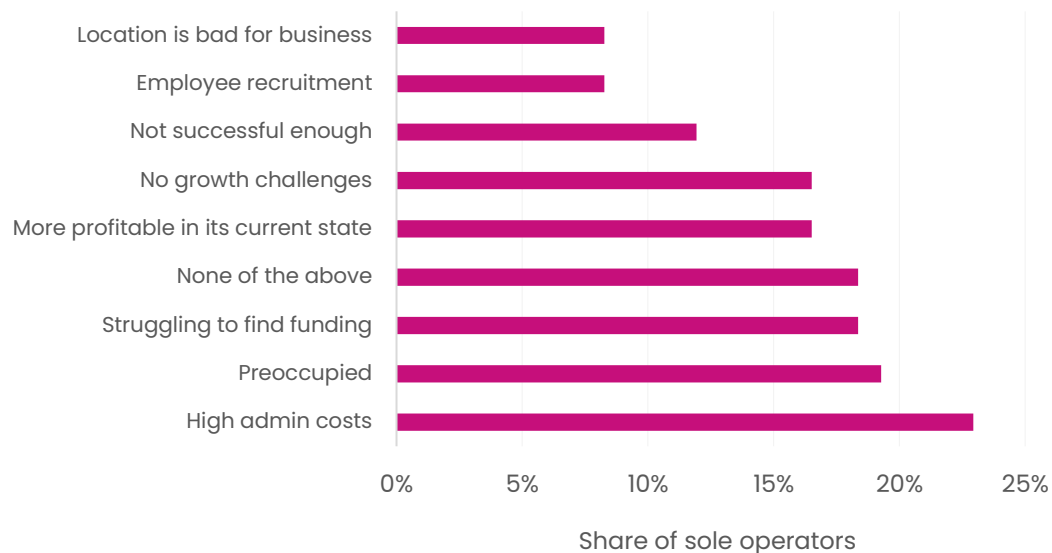
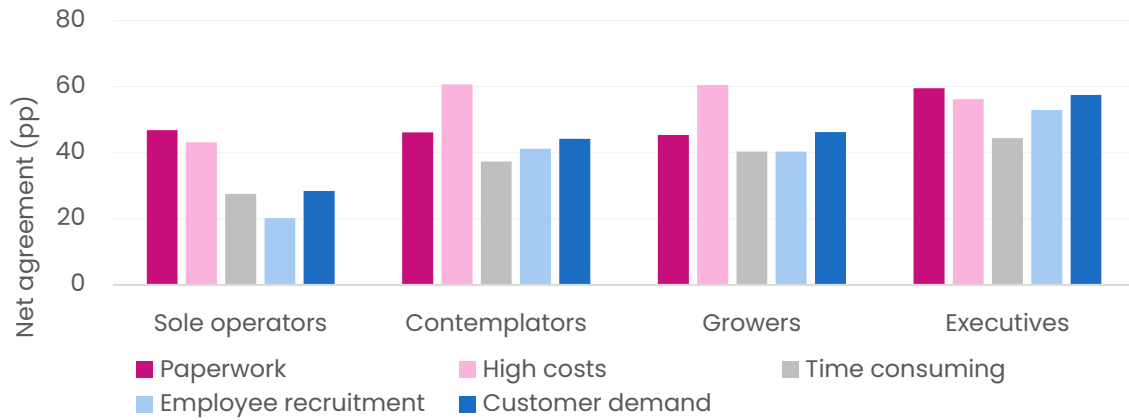


Figure 39: All entrepreneurs: Thinking of the process of setting up a business, which of the following statements do you agree with?

Source: JL polling, Onward analysis, April 2024

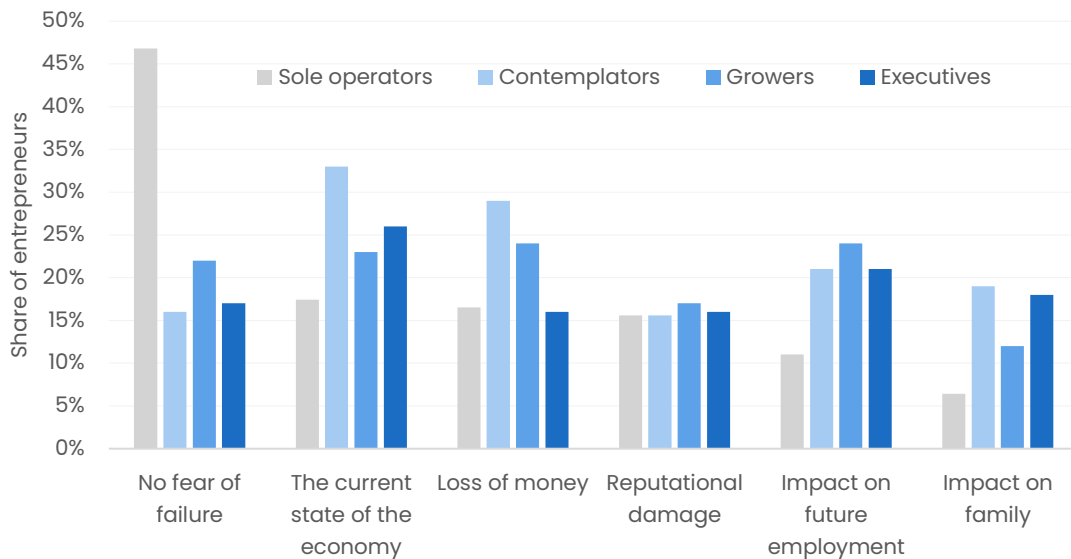


Sole operators rarely seek external finance and seem to be content with their current sources of funding. Nearly a third (31%) of this group have never sought external funding before, with half this group saying they relied on their own savings or funds from family and friends to finance their business. But on funding related challenges, they report the least dissatisfaction of all cohorts of entrepreneurs.

Unlike the rest of the business community, nearly half of this group are not worried about their business failing (46%). And on all drivers of a fear of the business failing, sole operators report less fear than other groups of entrepreneurs.

Figure 40: Drivers of a fear of failure, by type of entrepreneur

Source: JL polling, Onward analysis, April 2024



Group 5: The contemplators

The contemplators represent over a third (35%) of our sample, and are contemplating growing their business but are held back by a set of practical concerns.

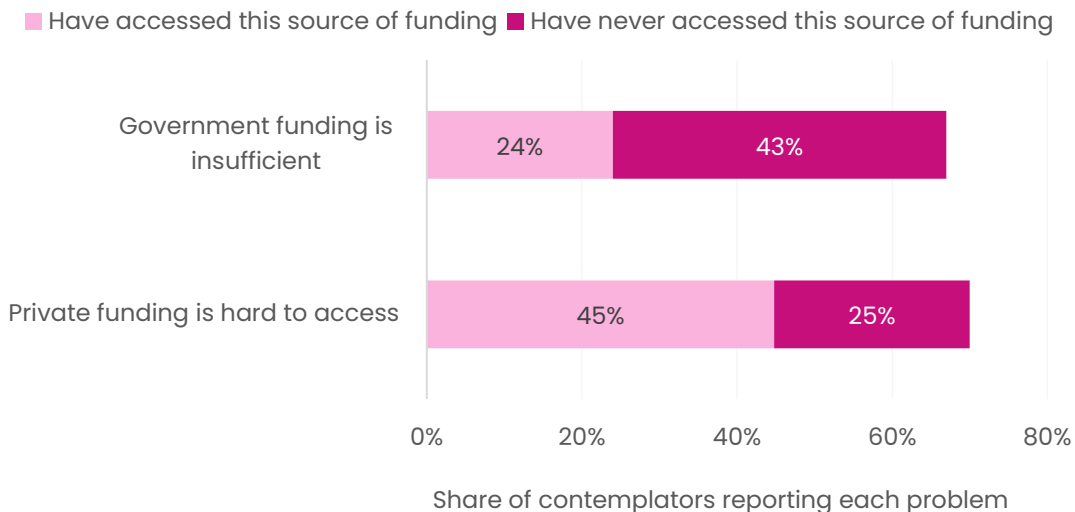
Typically, they are younger than other entrepreneurs and have the largest share of medium-sized businesses. Six in ten are aged 25-34, and represent a wider variety of businesses such as informal and limited liability partnerships and private and public limited companies compared to sole operators. Over a third (37%) of entrepreneurs in this group hire between 55 and 249 employees and 40% of the cohort turns over between £1 mill and £100 million each year.

Contemplators have raised funding for their business from a more diverse range of sources than sole operators. Majority (45%) relied on their own savings to set up/ or grow their business. But the share that relied on bank loans, other private sources like venture capital, and the stock market for startup and growth finance is double that of the sole operators.

However, a majority of this group report finding it very hard to access private and government funding. 70% of this group thinks that private funding is hard to access and 64% think that government funding is insufficient. But some of this concern is based on hearsay rather than experience. Of those who say that private funding is hard to access, over a third (36%) have never tried accessing funding from private sources before. And of those who say that government funding is insufficient, two-thirds (67%) have never tried accessing government funding before.

Figure 41: Concerns around access to funding vs share that have attempted accessing funding, by source of funds

Source: JL polling, Onward analysis, April 2024

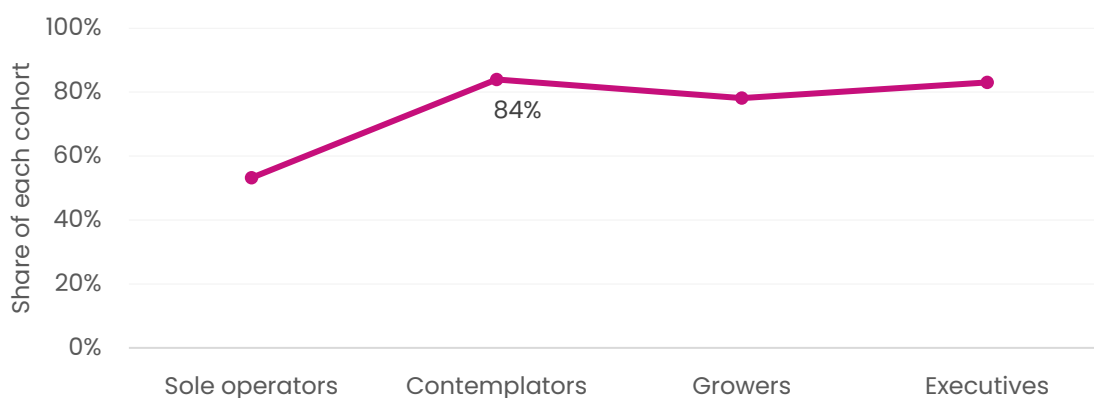


High costs are the top reason holding the contemplators back from greater growth. Nearly a third reported costs as the largest obstacle to growth, followed by a perception that they are not successful enough to grow (26%), and being too preoccupied with everyday running of the business (24%).

They are most afraid of failure relative to all other groups. 84% of contemplators reported a fear of failure, compared to just 53% of sole operators, shown in Figure 43 below. Driving their fear of failure is an overwhelming concern around the current state of the economy (32%) and losing money (either their own or an investor's) - 29%.

Figure 42: Share of each group reporting a fear of failure

Source: JL polling, Onward analysis, April 2024



Contemplators are worried about business concerns most visible to them, like high costs, harsh economic headwinds, and being time-poor from everyday management of the firm. But they also symbolise the nature of entrepreneurial fear in the UK - with an overwhelming majority reporting a fear of failure without having taken any significant steps towards growth. Breaking down immediate economic barriers would incentivise greater growth among these firms, but a broader cultural shift is likely to be needed to encourage them to achieve the scale of growth that a high growth firm possesses.

Group 6: The growers

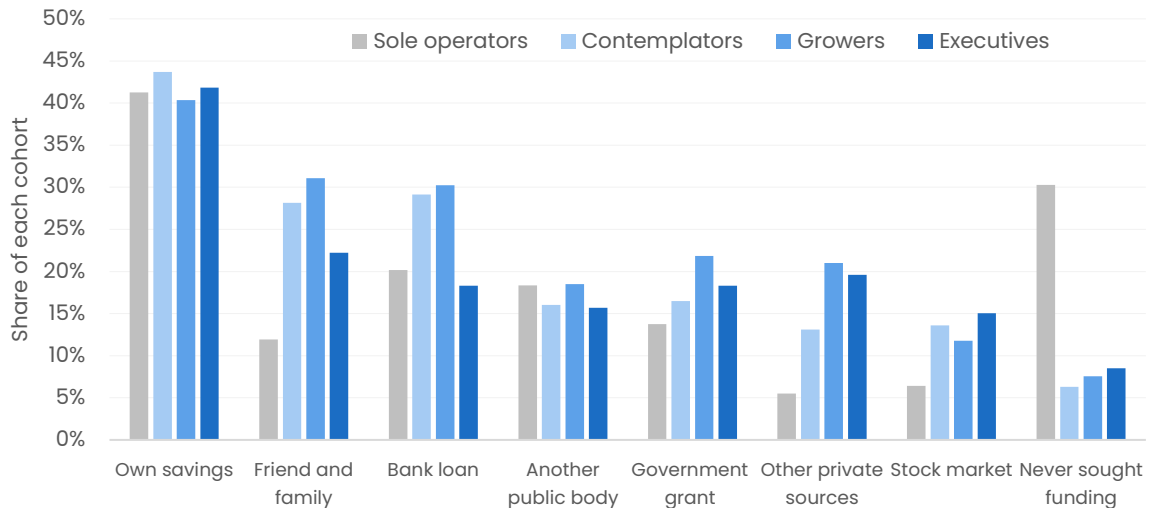
The growers represent 20% of the sample and are made up of those entrepreneurs who are currently growing their operations. They are overwhelmingly male (69%), young (two thirds are aged 25-44), and have the highest share of those educated to degree level.

Businesses in this group typically employ over 50 people and half have an annual revenue of over £25 million. Majority of growers are private limited companies, and this group sees the highest share of limited liability partnerships of all entrepreneurial groups. Unsurprisingly then, the growers attract funding from a

diverse set of sources, Relative to other groups, they have the largest share of funds raised from bank loans, other private sources like venture capital, and public body grants.

Figure 43: Sources of funding accessed, by group of entrepreneur

Source: JL polling, Onward analysis, April 2024



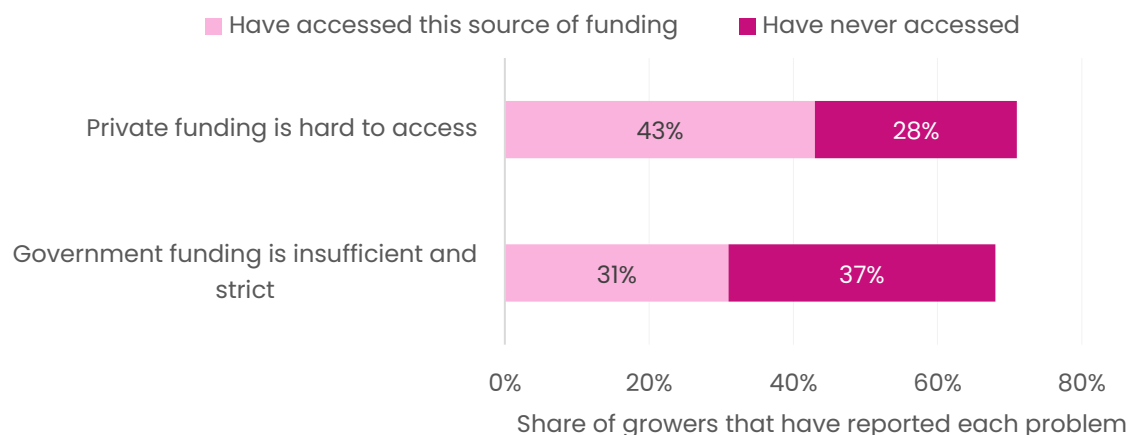
Even for those entrepreneurs who are currently pursuing growth, concerns that growth comes at the cost of profitability persist. Nearly a quarter (24%) of this group think they would be more profitable in their current state, and 26% feel that high admin costs are choking their growth plans. Of those who said that they think they would be more profitable in their current state, 44% have an annual turnover of between £10-24.9 mill, and 36% have a turnover of £100-499 million.

Similar to previous groups, the growers perceive great funding challenges without having attempted to access different funding sources. They report finding private funding hardest to access (71%) and government funding being both insufficient and strict (68%). Yet:

- Of those who say that access to private funding is hard, 40% have never tried accessing private funding
- Of those who say government funding is too strict, 54% have never tried accessing government funding

Figure 44: Share of growers reporting finding funding challenging vs having attempted accessing funding, by source of funding

Source: JL polling, Onward analysis, April 2024



Interestingly, this group’s fear of failure is more reputational than any other groups. Nearly a quarter (24%) reported concern that failure might impact their future job prospects. The growers are likely to have amassed a reputation via their business, and perhaps worry that a business failure would reflect poorly on their professional competencies. Suki, a foreign exchange business owner said in focus groups, “I always think about what will happen if I fail. I’ve got a good reputation in what I do now and what I’ve done in the past. But if I go into something and realise this isn’t exactly working out, then what is everyone who knows me going to think of me?”

This group should be a key target of public policy. It is worth investigating which sectors these entrepreneurs operate in to better understand how they can manage the tradeoff between profitability and growth. Policies that bring down their costs are likely to have a significant positive impact on the scale of their growth plans.

Group 7: The executives

The executives represent 26% of our sample and report that they have grown their businesses to its maximum potential. This group is dominated by men (75%) and almost half (48%) are aged 35-44, while also having the highest share of those aged 55-64 (15%). Nearly two-thirds of this group is highly skilled, working in London and the South East. Two thirds of this group (66%) have over 55 employees and over a fifth (21%) employ more than 250 staff.

Their primary concerns about expansion are the parlous state of the economy and worries that further expansion could be risky. Paul, a construction business owner said in focus groups, “I’ve already grown the company from three staff to 45, any more would be bad. I am already doing 60 hour weeks and I’m in my 50s. I make a

nice living out of this and the business is doing well. I just don't need the aggravation."

The majority (64%) of this group funded their business through their own savings or from friends and family, but this group also has a higher reliance on other sources of private capital like venture capital, angel investment, and the stock market compared to the average entrepreneur.

Looking at everyday business, the executives find excessive paperwork and the time-consuming nature of business operations are the two biggest barriers to business for this group.

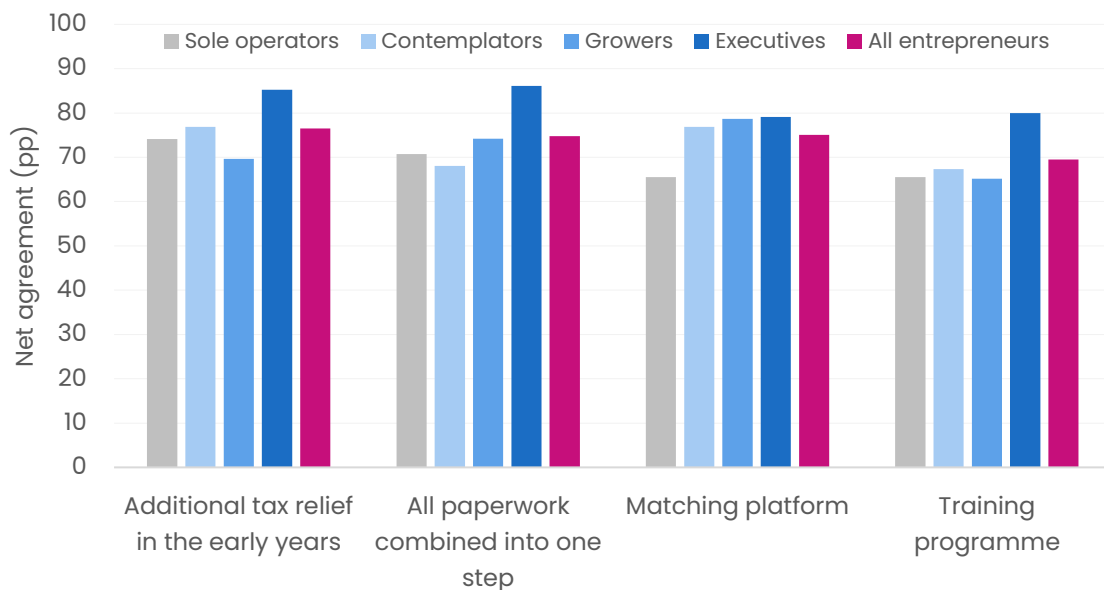
There is an active role for public policy to target this group, and that is to investigate the extent to which the growth ceiling that the executives perceive is artificial. Over a third of this group (37%) still turn over less than £1 million each year, and the same share employ less than 50 employees. This is the group that is closest to achieving 'mega growth' to become one of the UK's unicorns or decacorns.

What are each group's key asks?

Entrepreneurs report no clear preference for a single policy that would encourage greater business ownership. Additional tax relief in the early years marginally stand out as the most popular across all groups. And across the different entrepreneurial cohorts, the executives report the greatest agreement that the listed policies would encourage more business ownership.

Figure 45: Net agreement that each of the policy options would encourage greater business ownership

Source: JL polling, Onward analysis, April 2024



Recommendations

Recapturing entrepreneurial Britain



Reducing costs for businesses

Recommendation 1.1: The VAT threshold should be lowered significantly, and a tapered VAT rate should replace the flat 20% rate.

The VAT threshold in the UK is disincentivising business growth. But what is less clear is the best way to reform the VAT system. Organisations like the Federation for Small Business have long argued for a higher threshold - some suggesting it should be at £100,000.⁹⁴ Reform UK also pledged to increase the VAT threshold to £150,000.⁹⁵

But an increased threshold is unlikely to remove the cliff-edge and incentivise growth. Instead, it will only shift the point at which SMEs artificially control growth to the higher threshold, that too at an additional cost to the Government of £50 million for every £1,000 increase in the threshold.⁹⁶ Reform's pledge to increase the threshold to £150,000 would have costed approximately £3 billion.⁹⁷

The only way to reform VAT in a way that eliminates the cliff-edge altogether is to lower the threshold. This is likely to be politically challenging as it would impose an additional tax on businesses that are currently exempt. However, a tapered rate accompanied by the new digital VAT system can make the shift more politically palatable.

Analysis from Tax Policy Associates shows how this can be implemented. For example, if the threshold was lowered to £30,000, VAT could be charged at 1%,⁹⁸ increasing gradually in turnover till it reaches 20% at the £140,000 turnover level.⁹⁹ A tapered VAT rate was recommended for further investigation by the Office for Tax Simplification in 2019, but was not investigated any further.¹⁰⁰

Tapered VAT isn't without its own administrative burdens, but it remains the only way to encourage the long-term growth among businesses currently choked by the threshold. The digital VAT filing system implemented in 2022 means the returns will be calculated entirely digitally for businesses submitting their returns. However, it will make it harder for businesses to estimate the rate of VAT to charge, especially for those whose turnover changes within a single quarter. But this could be fixed by allowing for more frequent filing for those businesses for which this might be the case. The VAT filing system already makes exceptions for businesses that are better suited to monthly filing.

A lower VAT threshold with a tapered rate would impact Groups 4 and 5. Both groups see approximately two-thirds of their respective cohorts turn over less than £250,000 annually. For businesses under the current threshold of £90,000,

the proposed VAT regime would increase their cost burden. However, they would be paying VAT from a much earlier point in their tax journey, eliminating an abrupt change in tax codes. The impact on growth for this group is hard to estimate. Some might find the evened out VAT tax burden from an earlier stage easier to account for, while others might find the increased tax burden a dampener on growth.

The sole operators and contemplators that operate just below the VAT threshold of £90,000, and up to a turnover level of £140,000 are likely to benefit from the new VAT regime. They will see their VAT bills fall, as the 20% threshold is now reached only at the £140,000 mark. Specifically for Group 5s whose cost concerns are holding back growth, lower VAT rates could encourage them to take the first steps to grow their business.

Recommendation 1.2: Business rates should be reformed to avoid penalising high street businesses.

Business rates pose a clear disadvantage to brick and mortar businesses. While there are significant exemptions for businesses with properties valued less than £15,000, and some other criteria based on location and sector, for non-exempt small to medium sized businesses in areas with high property values, business rates are a major cost burden.

Simply adding a larger number of exemption criteria to business rates will only make the system more complex to navigate. In an Ipsos survey that asked individuals to rank their understanding of 11 different taxes, business rates (and corporation tax) stood out as the least understood.¹⁰¹

Any further cuts would also negatively impact local council revenues. Currently, most business rates accrue to the respective combined authorities the businesses are located in. Most combined authorities are part of the 100% retention pilot, while a few regions and non-mayoral combined authorities retain 50% of their business rates. At a time when council finances are stretched thin, it would be unwise to further constrain one of their primary revenue streams.

The current business rates regime should be transformed to make it a more progressive and efficient tax. This could involve a mix of some short and long-term measures.

In the short-term:

- **Introduce temporary reductions for expanding businesses.** Businesses that invest in new locations or expand existing properties could be offered a time-limited reduction based on the scale of their expansion. By

amending the upward transitional relief, growing businesses could be offered their former business rate bracket for two years.

- **Abolish the downwards transition.** This currently unfairly penalises businesses that have seen their property value fall but are not given the full tax reduction.
- **Introduce the ‘High Street Rental Auction’ system.** This would help tackle commercial vacancy and at the same time allow businesses seeking affordable rents access them. High street rental auctions for commercial property would target properties that have been vacant for over 12 months. It would require landlords, many of whom are institutional investors to conduct a public rent auction and let their units to one of the bids.¹⁰²

In the long-term, business rates should be reviewed as part of broader reform to business and property taxation. This could involve:

- **Replacing business rates with a commercial land value tax.** A commercial land value tax would be a more efficient and progressive tax compared to business rates. The supply of land is fixed, meaning that taxing it will not reduce the amount of it available in the market, compared to taxing property values which actively dissuades expansion. The replacement land value tax would have to be made cost-neutral so as to not strain local council revenues. Analysis from WPI Economics has found that a land value rate of 0.5% would generate the same amount of revenue as the current business rates system.¹⁰³
- **Replacing business rates with a turnover or profit-based tax.** This would tax businesses on their turnover rather than the value of the property. It could be modelled off the German “trade tax” or “Gewerbesteuer,” which uses the business’ operating profit as the tax base with local multipliers that reflect local economic conditions. The choice to base the tax on business profits or turnover should be based on which format will both impact local council revenues the least and reduce costs on businesses looking to grow.

Two new English devolution deals in practice means that a larger part of the country is now covered by mayoralities that should have a larger role to play in administering a tax to replace business rates. The replacement should operate on the principles identified by the Confederation of British Industry: that the tax should be predictable, stable, and simple.¹⁰⁴

A simpler and easier to use business rate replacement would have the strongest impact on the contemplators and growers for whom significant cost burdens are dampening their growth ambitions. Simpler business rates will see these groups

secure new premises and expand their operations to more locations across the country.

Recommendation 1.3: HMRC should simplify its self-employment determinant criteria and institute an IR35 ceiling.

Freelance and contract labour has been adversely affected by IR35. The Government should abolish these rules and shift the responsibility of determining an individual's tax status as a salaried employee or a freelancer back to the individuals themselves. The status quo that relies on court judgements is highly impractical.

There must, however, be provisions to ensure that individuals do not misuse the system to masquerade their salaried employment as self-employment to enjoy lower taxes. HMRC must simplify its existing Check Employment Status for Tax (CEST) rules to run simple and straightforward tests to verify an individual's employment. The model followed in New Zealand offers a promising alternative, where a freelance individual's tax status is determined by five simple criteria¹⁰⁵:

1. Control over the work
2. Own money at risk
3. Provision of major assets
4. Coverage of training costs
5. Accountability for work

HMRC should also release information regarding the amount of potential tax at stake in IR35 litigation cases. Based on these figures, it could be made the case that only self-employed individuals earning over (for example £50,271 - the higher rate tax threshold) needs to have their contracted company determine their IR35 status.

Simpler IR35 rules would benefit those aspiring entrepreneurs that are on the fence and on the brink. It will nudge them along into business ownership. These groups have the highest share of those presently engaged in a 'side hustle,' which is known to derisk entrepreneurship by providing supplemental income and the skills to pivot into full time entrepreneurship.

Improving access to finance for viable businesses

Recommendation 2.1: Introduce a new wave of commercial bank-backed Community Development Finance Institutions (CDFIs)

Market failures in SME finance are leaving viable small businesses choked of their funding. And the situation is only expected to get worse with the introduction of Basel 3.1 regulations that will further widen the SME finance gap by £44 billion.¹⁰⁶

It is often small businesses looking to loan less than £100,000 that are left with very limited support. This category of loans represents over 5% in value of all SME loans applied for.¹⁰⁷ And it is predominantly microbusinesses (99%) with less than 10 employees that apply for loans of this value, with the average microbusiness looking for loans of approximately £26,000. For this group of approximately 180-230,000 businesses alone, the unmet demand for finance stands at between £4-6 billion each year.¹⁰⁸

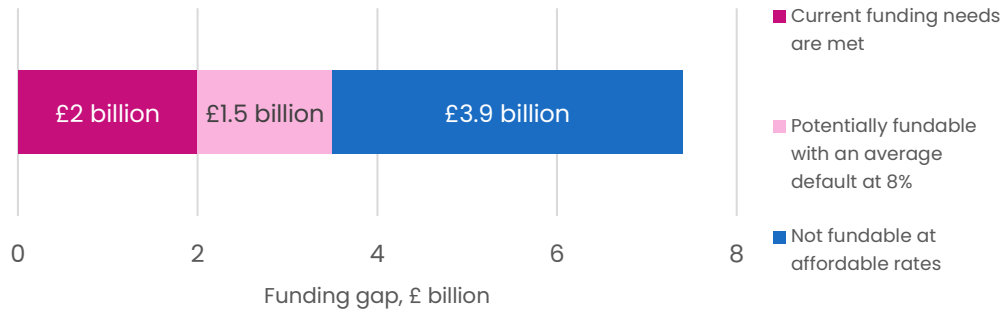
But not all these businesses will be creditworthy and risk-safe borrowers. There is a directly proportional relationship between the overall default rate in the market and the share of viable businesses that can be served. Credit modelling estimates find that between 33 -50% of viable businesses are underserved by mainstream finance at the industry average level of default of around 4%. Estimates from Responsible Finance identify between 70-140,000 viable and creditworthy SMEs that are being rejected from traditional lenders.¹⁰⁹

The American model of Community Development Finance Institutions poses a promising solution for British SMEs. CDFIs are financial intermediaries aimed at providing additional capital to businesses that have been rejected from mainstream lenders. They do not face the same market pressure failures that sees high street bank lending constrained by risk and shareholder and regulatory pressures and can issue loans at slightly higher default rates.

Reduced market pressure means that CDFIs can accept a higher default rate. A default rate of 8% is estimated to increase SME funding received by between £1.5-£1.7 billion, with an additional 50-60k of businesses getting more funding.¹¹⁰

Figure 46: Annual funding needs of SMEs of loans less than £100,000

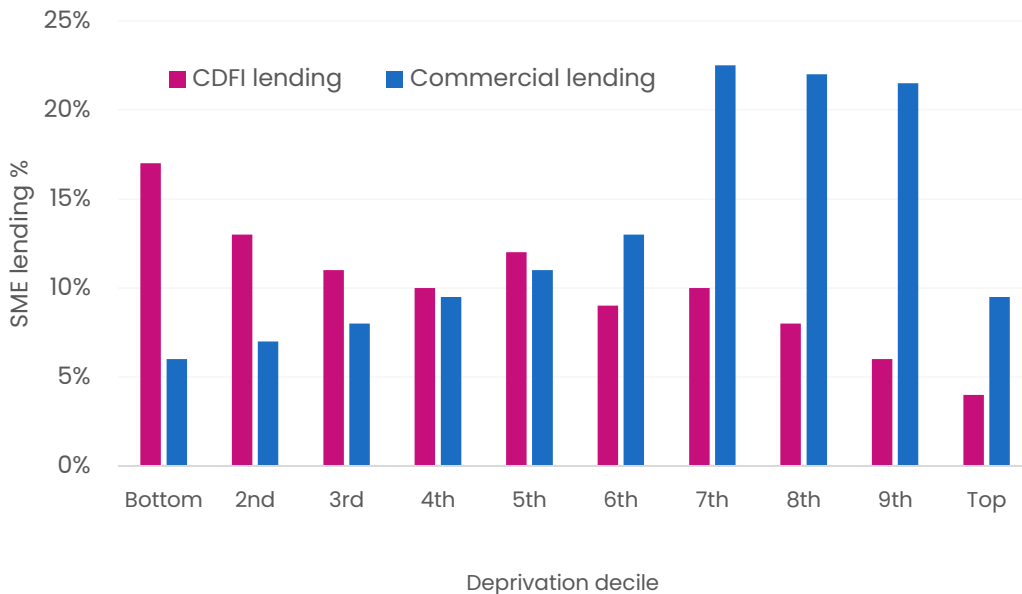
Source: Responsible Finance, 2022



Despite their unique ability to reach out to otherwise rejected SMEs and those predominantly in deprived areas (see Fig 48 below), CDFIs in the UK are highly undercapitalised. Of the £1.5-£1.7 billion, the network of 50 CDFIs in the UK have enough capital to only lend around £0.2 billion - just 12% of its potential.

Figure 47: Share of CDFI and commercial SME lending, by deprivation decile of recipient

Source: Responsible Finance, 2022



To make up for this gap in capital, a collaborative capital fund should be created. This fund would provide ‘first loss capital’¹¹¹ to CDFIs, in a manner that de-risks private banking involvement. If the Government contributed £200 million to distribute over five years, a 4:1 of private match ratio could attract at least £1 billion in new capital. And by funding only high-impact, CDFIs in the UK, the grants will incentivise scale, efficiency and innovation in the sector.¹¹²

But a collaborative fund alone is unlikely to meet the SME finance gap. American CDFIs see a higher rates of capitalisation because their commercial banks contribute to CDFIs. The Community Reinvestment Act (CRA) evaluates commercial banks based on whether they met the credit needs of the areas they operate in, especially in deprived neighbourhoods. In fact, major commercial banks in the US have found ways to successfully incorporate capital contributions to CDFIs into their operational cost models without renegeing on lending standards.¹¹³

Box 2: JP Morgan Chase CDFI programmes in the United States

Source: JP Morgan Chase press release, May 2022¹¹⁴

In 2021 alone, JP Morgan Chase contributed over \$500 million through CDFIs to serve businesses in America's most deprived neighbourhoods. The products they offered ranged from philanthropic donations and low-interest debt to capacity-building programmes, such as:

The Equitable Path Forward (EPF) Growth Fund, which provided \$40 million investment to issue flexible capital in the form of low unsecured working capital loans to small businesses in deprived neighbourhoods.

Service Corps, that matched employees in the bank with loan beneficiaries to share their business acumen and maximise impact.

The Financial Justice Fund, which saw the bank commit over \$20 million - a mixture of debt and philanthropic capital, carefully designed promote growth in underserved communities.

The UK should follow in the footsteps of the American Community Reinvestment Act (CRA) and have commercial banks capitalise local CDFIs. Not all parts of the American system will be relevant or replicable in the UK, but some key aspects should be considered. The CRA was introduced to ensure that marginalised neighbourhoods received ample investment. And key to its success was a highly effective enforcement plan - banks underwent 'CRA reviews' when applying to open new branches or undergo mergers and acquisitions.

New SME lending compliance criteria should be introduced for major UK commercial banks. The Prudential Regulation Authority's (PRA) plans to phase in Basel 3.1 regulations between 2026 and 2029 will further harm SME lending. Not only should the SME support factor that currently enables lending to SMEs be protected, but conditional on the success of the collaborative fund, the PRA could go a step further and introduce a SME lending compliance criteria for commercial banks. Like in the American case, this 'SME lending certificate' could be made a pre-requisite for mergers or opening new regional branches.

A new CDFI model is likely to encourage greater business growth among the sole operators and contemplators. These groups are most likely to currently seek out smaller value loans for growth. In the long-term, if CDFIs become an embedded feature in the UK banking network, it could also motivate those on the fence and on the brink to start a business, knowing they will have easier access to finance across the country.

Recommendation 2.2: The British Business Bank should transform its funding finder tools

Majority of small businesses in the UK simply do not know where to start looking for funding. As the types of finance for SMEs becomes increasingly diversified, with new sources like peer to peer lending and mezzanine finance gaining prominence, this issue is only likely to get worse.

But the British Business Bank already operates a very user-friendly and detailed funding finder tool. Their digital ‘3-Step Funding Finder Tool’¹¹⁵ asks small business six questions about the nature of the business, amount they are looking to raise, and asset base and profitability to provide them with a list of possible public, private, and hybrid funding sources they are eligible for. But significantly low levels of awareness of the British Business Bank among SMEs means too few of them are likely accessing this tool.

At the first instance, company registration should be made conditional on businesses entering their top options for finance after having used this tool. This would standardise exposure to the tool in ways that other dissemination channels like regional chambers of commerce and online advertising cannot achieve. The registration form for Companies House (in the case of incorporated businesses and limited liability partnerships) and tax registration with HMRC (for sole traders and informal business partnerships) should include a question asking founders to list their top options for finance using BBB’s funding finder tool. Simply signposting them to a website is less likely to see founders engage and use the tool.

The British Business Bank could go further and launch an interactive digital networking platform ‘Startup UK’ for entrepreneurs and funders alike. This could be modelled on the highly successful StartupSG in Singapore, that has user portals for SMEs to upload their business pitches and growth plans, and an array of funders list funding opportunities.¹¹⁶ Startup UK should have sectoral and regional breakdowns of financing, infrastructure, and mentorship opportunities available in the startup community. It could also run events, conferences, and other networking opportunities, and produce research and analysis that identifies gaps in the entrepreneurial landscape and shares best practices.

Those on the brink and sole operators are most likely to benefit from having more information about finding funding.

Managing risk in entrepreneurship

Recommendation 3: Introduce 'Business Startup Relief' (BSR) to reduce startup costs for aspiring entrepreneurs

Chapter 3 identified those on the brink as those most likely to go on to set up successful businesses. When asked what policies would encourage them to start a business, additional tax relief in the first year of running a business stood out as the most popular choice.

Encouraging growth-oriented entrepreneurship - the setting up of businesses that pursue growth - requires policies that target those with the greatest chance of setting up a fast growing business to do so. 'Opportunity entrepreneurs' - individuals that start a business to exploit a commercial opportunity - have been found to be more profitable than other types of entrepreneurs.

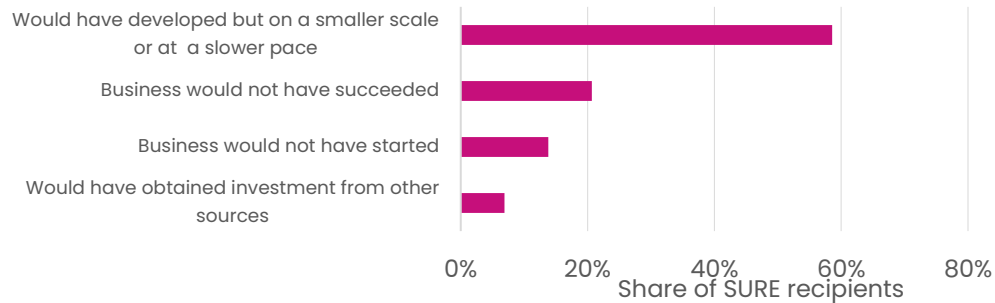
A 'Business Startup Relief' would provide aspiring entrepreneurs who have paid a certain amount of tax with an income tax refund if they invest their own funds into a new business. There are some international examples of how this might work in practice:

Box 3: Start-Up Relief for Entrepreneurs (SURE), Ireland and Entrepreneurs allowance, Netherlands.

'Start-Up Relief for Entrepreneurs (SURE)' in Ireland offers entrepreneurs an income tax refund up to 41% of new investment into their business. Nearly 91% of SURE users reported that it was vital to establishing their business, and 80% reported that it supplied them with finance that would otherwise not have been available.

Not only did SURE help businesses get set up, it also helped them grow. Over one in five SURE recipients report that their business would not have succeeded in the absence of SURE, and nearly 60% say they would not have grown as much or would have grown at a slower rate had their not been any SURE funding.¹¹⁷

Figure 48: Share of SURE recipients reporting access to finance in the absence of SURE. Source: Indecon analysis of Revenue data from Ireland, 2018



However, the complexity of the application process meant that SURE was not widely used. Just 80 individuals accessed SURE funding in 2016, amounting to just €23,750 per applicant or €1.9 million in total.

Entrepreneurs allowance in Netherlands is a package of different forms of tax reliefs and credits that can be deducted from profits so that businesses pay less tax. Collectively, business owners can deduct up to nearly 40% of their profits. One specific tax within this package, the ‘startersaftrek’ allows entrepreneurs to deduct a fixed sum of €2,123 from their annual gross profits a maximum of three times in a five-year period.¹¹⁸

While this tax relief has been beneficial for increasing the number of startups, its impact on sustaining and scaling these businesses has been limited. It has helped boost the number of new businesses, but only a small proportion of these companies evolve into larger, high-growth firms. This is sometimes referred to as the “Dutch entrepreneurship paradox,” where the country excels at encouraging startups but falls short in fostering scale-ups that contribute significantly to economic growth.¹¹⁹

The proposed ‘Business Startup Relief’ for British businesses could build on both the Dutch and Irish models. A tax refund from income tax paid in the previous years (the Irish model) would help aspiring entrepreneurs reduce their upfront costs compared to tax deductions from profits (the Dutch model). New firms take on average between one and two years to generate profit, so an immediate source of funds are likely to be more popular.

But the policy would have to be accompanied with a major awareness programme or be embedded into company registration processes to ensure widespread adoption. Like the Dutch model, BSR should be designed so that it is a one-time use relief.

BSR would allow PAYE taxpayers that have paid at least £11,112¹²⁰ in a tax in the last two years with a tax refund if they set up a new business. These aspiring entrepreneurs would then be able to claim a share of their investment into their new business as an income tax refund. The amount of refund will depend on the individual's gross pay, and could follow either a flat rate system where all individuals are eligible to claim the same share of their investment as an income tax refund, or a tiered system where higher investments receive higher refunds.

The relief would have to be capped at a maximum level. A £3.3 billion pot of funding (roughly 2% of the income tax paid by the top 10% of earners) could fund the BSR scheme. To ease pressures on the Treasury, the BSR could even be part-funded from the Business Asset Disposal Relief (BADR) scheme (formerly Entrepreneurs Relief), worth £1.5 billion each year.

Box 4: What is Entrepreneurs' Relief and Business Assets Disposal Relief (BADR)

Entrepreneurs' Relief (ER) was introduced in 2008 to incentivise entrepreneurship by reducing the capital gains tax rate on the sale of businesses. This relief allowed qualifying business owners to pay a lower rate of 10% on the profits from selling their business assets, up to a lifetime limit. The maximum amount for which ER could be claimed was £10 million, and its successor, 'Business Assets Disposal Relief' (BADR) lowered to £1 million.

While introduced to encourage entrepreneurship and reward risk-takers, few mechanisms were set in place to monitor the types of recipients of the scheme and whether the relief was generating value for money. Nearly £22 billion was spent on ER over a decade, and costs were ten times higher than the Treasury had budgeted.¹²¹

The current Government has proposed abolishing BADR,¹²² but the principle that underpins Entrepreneurs Relief and BADR is one that should be encouraged. Rewarding entrepreneurs for the risk they have taken will encourage more entrepreneurship in the country and drive economic growth. The £1.5 billion should be redirected towards the new and well-targeted business startup relief.

Those on the brink of starting their business are most likely to benefit from a Business Startup Relief programme. This groups sees the highest share of aspiring entrepreneurs reporting that high startup costs were the largest barrier to setting up a business. And they are also most likely to set up a business that goes on to become a high growth business.

Tackling bureaucracy

Recommendation 4: Councils and mayoralities should create expedited planning processes to help businesses secure new premises

An efficient planning system is essential to reducing bureaucratic delays that hold back business expansion and deter commercial investment.

Local councils should introduce a "Pre-Approval Scheme" for standardised business expansion plans. Applications under this scheme would by default be granted planning permissions if they met three simple criteria around economic benefits to the local area, site suitability (whether for commercial, retail, or industrial), and transport and infrastructure requirements. This could significantly reduce the need for lengthy reviews, allowing businesses to secure premises more quickly.

Mayoralties specifically could introduce a "Fastrack Business Planning Initiative" (FBPI), which expedites planning applications from businesses seeking to expand or establish new premises. This initiative could set reduced timeframes for decision-making on commercial planning applications. By setting strict deadlines for each stage of the approval process and implementing penalties for unnecessary delays, authorities can create a more business-friendly environment that encourages timely development.

Sole operators, contemplators and growers are most likely to benefit from expedited planning processes. These are the groups that are up against growth for whom delays and excessive bureaucracy amount to significant cost barriers.

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