

United States House of Representatives

Committee on Financial Services

“Promoting Economic Recovery and Job Creation: The Road Forward”

January 26, 2011

Eric Hoffman – Written Testimony

I want to begin by thanking Chairman Bachus and the members of the Committee on Financial Services for the invitation to speak today. I have had the privilege to work at our family business, Hoffman Media, LLC (or “Hoffman Media”), and be a part of the incredible growth story; and as I strategize about both our company’s continued growth, as well as small business growth throughout the United States, I am concerned by recent changes in financial regulation, healthcare and taxes. In this testimony I will share with you the history of Hoffman Media, concerns I have on The Volcker Rule and long-term negative effects on small business and job growth, and concerns of future burdens caused by healthcare reform and higher taxes. Overall I am concerned that the significant changes we are seeing will hurt our future ability to grow as uncertainty is the worst head wind we face.

Overview of Hoffman Media:

Hoffman Media was founded in 1998 by my mother, Phyllis Hoffman who currently serves as Chairman & CEO. After successfully working for five years at a large publicly-traded publishing company (through the acquisition of her first start-up company), Phyllis left in 1998 to start Hoffman Media. She formed the company by acquiring two magazines, and financed the start-up by mortgaging her house (true sign of an entrepreneur). From 1998 – 2003 the company ran on an extremely tight budget whereby all operating profits were reinvested in the business to fund continued growth through launching of new magazine brands. In 2003, Hoffman Media had approximately 20 employees and generated revenues of approximately \$4,000,000 annually. It was during this period that Phyllis decided in order to properly fund growth and scale the company, both through organic growth and acquisition, that Hoffman Media would need to raise capital (since Hoffman Media was not producing net income it prevented the company from accessing traditional commercial lending from a bank). After 24 months of meeting with private equity firms, Hoffman Media successfully raised \$5,000,000 from BIA Digital Partners and Frontier Capital. This capital raise allowed Hoffman Media to complete a strategic acquisition of a complementary business, Martha Pullen Co., and fund additional marketing and hiring needs. From the period of 2004 – 2010, Hoffman Media was able to grow revenues from approximately \$10,000,000 to \$40,000,000, while also growing employee count from approximately 20 to 135.

The capital raised from BIA Digital Partners is worth explaining further. BIA Digital Partners provided mezzanine debt with warrant coverage to Hoffman Media, which Hoffman Media successfully paid back in 2009. The outcome was a win for all parties involved in that BIA Digital Partners (including their LPs) achieved a healthy rate of return on the investment, and Hoffman Media was able to properly fund the growth strategy. As a result, Hoffman Media's economic impact has grown dramatically, having created jobs, and generating substantial sales tax at the state and local level while also producing taxable income. This growth would not have been possible without the financial support of BIA Digital Partners (and their LP investments).

The Volcker Rule and Long-term Negative Effects on Small Business and Job Growth:

Highlighting BIA Digital Partner's investment in Hoffman Media is important because it is my understanding roughly half of the firm's LPs are some of the greatest and largest banks in North America. It is my opinion that the restrictions being proposed on banking entities abilities to own or invest in private equity funds will have long-term negative implications for small business and job growth, and had BIA Digital Partners not had banks as LPs, Hoffman Media would not have secured the same level of funding (structure, commitment size, etc.).

The Volcker Rule's hedge fund and private equity fund investment restrictions generally prohibit a banking entity from acquiring or retaining any equity, partnership, or other ownership interest in, or sponsoring a private equity fund (other than perhaps 3% or less of Tier 1 capital). I fear this could lead to a substantial decrease in the funding support of private equity firms, especially those firms covering the lower middle market (companies similar to Hoffman Media in 2004). My concern is that there will be a small amount of capital, if any, available to invest in lower middle market private equity funds. Instead it will all be allocated to the larger buyout firms (examples: The Blackstone Group, KKR, The Carlyle Group, TPG, Apollo Management, etc.) because of the total economics related to those relationships with those firms (investment banking advisory fees related to M&A, equity and debt capital raising, leverage buyout financing, etc.). While Hoffman Media has demonstrated credit worthiness and strong growth, it is highly unlikely we will gain the coverage from the larger financial institutions (other than commercial lending), however, unlike most larger buyout transactions, Hoffman Media has created real value (job growth, revenue and sales tax growth, etc.) not generated through financial engineering and the use of high amounts of leverage.

As EVP & COO of Hoffman Media, I have had the opportunity to speak at BIA Digital Partners' annual LP meeting, where I have been able to present the company performance as well as network with some of

the leading banks in North America. This opportunity eventually allowed Hoffman Media to seek traditional bank lending and repay BIA Digital Partners' debt they provided the company.

Small business is where sustainable economic growth will come from. It is companies like Hoffman Media that take risks, seek funding, and grow out of the dreams and passions of an entrepreneur. As a representative for small businesses across this country it is our desire to see as few hurdles as possible for small business to grow and seek growth capital. The Volcker Rule is one more hurdle that will slow down this economic recovery. Financial institutions should always be focused on maximizing shareholder value, and if they choose to allocate capital to private equity funds, both large and small, in order to generate profits and future business development, they should be able to do so without restriction or limitation from the government.

I've been at ground zero and seen this work, and I urge members of the committee to please limit the impact the Volcker Rule has on the funding of small business.

Future Burdens Caused By Healthcare Reform and Higher Taxes:

It is with great concern I also address the healthcare reform and the risk of higher taxes. Hoffman Media currently has 135 employees, of which, a large majority are using benefits provided through the company. Just in the past 12 months our health insurance costs have risen 8% (far lower than the rate of other small businesses in our area) and are expected to increase again soon. In an environment where unemployment is over 9%, housing foreclosures are higher than ever, it is already incredibly hard to run a successful business, but with extremely large increases in employee benefit expenses, it makes it even harder. If this trend continues, whereby operating expenses grow at a faster rate than revenue growth, our country will continue to see the jobless level remain high. This creates a disincentive towards companies hiring, rewarding employees with raises, or even keeping the current level of headcount you have, rather, it creates a real bottom line need to cut other costs, which ultimately leads to a weaker long-term outlook. With the new healthcare laws, and the future requirements for everyone to be offered insurance, I am deeply concerned that this will put undue pressure on businesses, especially small businesses. There are additional compliance and regulatory costs, estimated increases in health insurance costs, and unjust penalties proposed, all of which negatively impact this country's ability to create jobs and generate real GDP growth.

In addition to healthcare changes, I have great concern over the future of tax rates, both individual and corporate rates. Increasing tax rates will negatively impact Hoffman Media, and other companies just like us. Tax increases directly diminish our after tax free cash flow and after tax margins, thus reducing the amount of money available for reinvestment. I know how difficult it is to operate in a tough

economic environment like we are in now, so effectively decreasing margins is one more disincentive to hire, give raises, or keep our current headcount. In addition, companies like Hoffman Media who are faced with the need to pay down loans are further impacted by tax rate increases since principal payments on debt are not tax deductible, only the interest expense. Hoffman Media has cut its debt level in half over the past 24 months, and had our tax rate been higher we would not have been able to do so as it would have effectively cost us more to pay down the same level of principle. Going forward we will be faced with tougher challenges as business operators and employers, where the costs of being successful and generating profits are higher.

I urge members of the committee to please review these points. I do not speak alone. Millions of small business operators in this country feel the burden ahead. An economic recovery and job recovery are very possible if we reduce the hurdles of higher taxes and higher healthcare costs. We need an environment that encourages risk taking and entrepreneurs to follow their dreams, and unfortunately I do not see this ahead.


Closing:

In conclusion, I believe the story of Hoffman Media's growth performance and path to growth capital is one of several thousand examples throughout the United States. It is a success story, for our business, for our investors, for banks, and for our country. My hope is that complicated law and regulation, such as The Volcker Rule and healthcare reform, do not negatively impact our economy, the entrepreneurial spirit of this country, and the access to capital for small businesses, but I am afraid that currently they will. Please reduce the impact the Volcker Rule has on our financial institutions. Please do not raise taxes on anyone, or any corporation, in fact, lower the taxes and reduce the hurdles put in place by our government. And finally, limit the healthcare reform so businesses like Hoffman Media are not faced with ever increasing costs and increased regulatory oversight...it is bad for business and our economy.

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“TRUTH IN TESTIMONY” DISCLOSURE FORM

Clause 2(g) of rule XI of the Rules of the House of Representatives and the Rules of the Committee on Financial Services require the disclosure of the following information. A copy of this form should be attached to your written testimony.

1. Name: Eric Wayne Hoffman	2. Organization or organizations you are representing: Hoffman Media, LLC
3. Business Address and telephone number: <div style="background-color: black; width: 400px; height: 40px; margin: 10px auto;"></div>	
4. Have <u>you</u> received any Federal grants or contracts (including any subgrants and subcontracts) since October 1, 2008 related to the subject on which you have been invited to testify? <input type="checkbox"/> Yes <input checked="" type="checkbox"/> No	5. Have any of the <u>organizations you are representing</u> received any Federal grants or contracts (including any subgrants and subcontracts) since October 1, 2008 related to the subject on which you have been invited to testify? <input type="checkbox"/> Yes <input checked="" type="checkbox"/> No
6. If you answered .yes. to either item 4 or 5, please list the source and amount of each grant or contract, and indicate whether the recipient of such grant was you or the organization(s) you are representing. You may list additional grants or contracts on additional sheets. <div style="height: 150px;"></div>	
7. Signature: <div style="text-align: center; margin-top: 20px;"></div>	

Please attach a copy of this form to your written testimony.