

Congress of the United States

U.S. House of Representatives

Committee on Small Business

2361 Rayburn House Office Building

Washington, DC 20515-6315

To: Members, Subcommittee on Investigations, Oversight and Regulations
From: Committee Staff
Date: March 11, 2013
Re: Hearing: "Regulating the Regulators – Reducing Burdens on Small Business"

I. Introduction

On Thursday, March 14, 2013 at 10:00 am in Room 2360 of the Rayburn House Office Building, the Subcommittee on Investigations, Oversight and Regulations will meet for the purpose of receiving testimony on whether federal agencies are complying with the Regulatory Flexibility Act (RFA).¹ The RFA requires agencies to assess the economic impact of their regulations on small businesses,² and if the impact is significant, consider alternatives that are less burdensome. The hearing will examine whether federal agencies are complying with the RFA and reducing unnecessary regulatory burdens on small businesses.

II. RFA

On average, agencies publish between 3,000 to 4,000 final regulations every year on diverse subjects including, but not limited to: workplace safety; environmental protection; health care; energy conservation; and listing of endangered species. By virtue of their size and resources, small businesses are disproportionately burdened by the cost of regulations in comparison to their larger counterparts.

During the 1970s, more than 30 major statutes were enacted that established new federal agencies and provided powerful new regulatory authority. As the decade came to a close, small businesses were struggling to both run their businesses and comply with the growing number of complex federal regulatory requirements. Congress took note of the plight of small businesses in a series of hearings in the late 1970s from which two central themes emerged: 1) small businesses were underrepresented in the rulemaking process; and 2) small businesses were disproportionately burdened by one-size-fits-all regulations.³

¹ 5 U.S.C. §§ 601-12.

² The RFA uses the term "small entities," which includes small businesses, small not-for-profit organizations, and small governmental jurisdictions. See 5 U.S.C. § 601(6). For the sake of simplicity, this memorandum will use the term "small business."

³ Pineles, *The Small Business Regulatory Enforcement Fairness Act: New Options in Regulatory Relief*, 5 COMMLAW CONSPPECTUS 29, 29-30 (1997).

Given these concerns, Congress enacted the Paperwork Reduction Act⁴ and the RFA. Although the RFA is over 30 years old, federal agencies still fail to fully comply with its requirements.

A. Overview

The RFA applies to every proposed and final rule for which an agency must conduct notice and comment rulemaking as required by § 553 of the Administrative Procedure Act (APA)⁵ or any other law.⁶ Under the RFA, each federal agency must review its regulations to ensure that, while accomplishing its statutory mandate, the ability of small businesses to invent, produce and compete is not inhibited. Agencies are forced to identify and account for the potentially excessive costs and disproportionate impacts of regulations on small business.

B. RFA Analytical Requirements

The RFA requires an agency to complete a threshold analysis of the economic impact of a proposed or final rule. This is used by the agency to decide whether to prepare an initial regulatory flexibility analysis (IRFA) or certify the rule. If the agency determines that “the rule will not, if promulgated, have a significant economic impact on a substantial number of small entities,” then the agency head (or the person the agency head delegates) is entitled to certify to such a conclusion (the agency must provide the factual and legal basis for the RFA certification) and need not prepare an IRFA nor examine alternatives.⁷

An agency that determines a proposed or final rule will have a significant economic impact on a substantial number of small businesses is required to prepare either an IRFA or FRFA.⁸ Each regulatory flexibility analysis must contain the following: 1) a description of the reasons why action by the agency is being considered or taken; 2) a succinct statement of the objectives of, and legal basis for, the rule; 3) a description of and, when feasible, an estimate of, the number of small businesses to which the rule will apply; 4) a description of the projected reporting, recordkeeping and other compliance requirements of the rule, including an estimate of the classes of small businesses which will be subject to the requirement and the type of professional skills necessary for preparation of the recordkeeping or reporting requirement; 5) an identification, to the extent practicable, of all relevant federal rules which may duplicate, overlap, or conflict with the rule; and 6) alternatives to the rule that might reduce the economic impact on small businesses.⁹ The FRFA also must describe the steps an agency has taken to

⁴ The Paperwork Reduction Act is beyond the scope of this memorandum.

⁵ Exemptions from the notice and comment requirements of § 553 are found in 5 U.S.C. § 553(a) and (b).

⁶ For example, a provision of the Medicare Act, 42 U.S.C. § 1395hh, and a provision of the statutes relating to federal procurement policy, 41 U.S.C. § 1707, mandate that rules be issued by notice and comment rulemaking even though the rules are covered by exceptions in § 553(a)(1)-(2).

⁷ 5 U.S.C. § 605(b). A certification of the proposed rule does not mean that the agency is entitled to certify the final rule. Data obtained during the notice and comment process may force an agency to rethink its decision to certify. If sufficient information is submitted to the agency that demonstrates a significant economic impact on a substantial number of small businesses, then the agency is required to prepare a final regulatory flexibility analysis (FRFA).

⁸ An agency must prepare a regulatory flexibility analysis whether the rule will have a beneficial or negative effect. In a FRFA, the agency is only required to explain what steps it has taken to minimize the impacts on small business.

⁹ 5 U.S.C. § 603(a).

minimize the significant economic impact on small businesses and why each alternative that would lessen economic impact was rejected.¹⁰

The critical element of a regulatory flexibility analysis is consideration of alternatives. Alternatives contemplated by the authors of the RFA may include separate reporting requirements or compliance standards to take account of the limited resources of small businesses. The agency may ultimately develop a tiered regulation with different requirements for entities of different sizes or decide not to regulate small businesses because they only contribute to a small portion of a problem that the agency is trying to ameliorate.

Consideration of these alternatives does not require the adoption of any particular regulatory alternative. An agency may adopt a regulatory strategy that imposes substantial burdens on small businesses as long as the agency has complied with the RFA's analytical requirements.

C. Small Business Administration (SBA) Office of the Chief Counsel for Advocacy¹¹

Congress gave the Chief Counsel for Advocacy of the SBA (SBA Advocacy) the responsibility of monitoring agency compliance with the RFA. On an annual basis, the Chief Counsel for Advocacy is required to report to the President and the Committees on Small Business and the Judiciary of the United States Senate and House of Representatives on agency compliance with the RFA.¹² Pursuant to Executive Order 13,272,¹³ SBA Advocacy has published a RFA compliance guide for federal agencies.¹⁴ That same executive order also requires SBA Advocacy to provide compliance training to agency personnel.

D. Small Business Advocacy Review Panel (SBAR) Process¹⁵

The RFA contains affirmative outreach requirements for federal agencies to assure small businesses have had an opportunity to participate in the rulemaking process. This requires agencies to do more than simply publish a proposed rule in the Federal Register.¹⁶

¹⁰ *Id.* at § 604(a)(6).

¹¹ President Ford signed Pub. L. No. 94-305, 90 Stat. 668 (1976), codified at 15 U.S.C. §§ 634a-g, which established the Office of Advocacy within the SBA and vested management of the Office in the Chief Counsel for Advocacy, who was to be appointed by the President with the advice and consent of the Senate.

¹² SBA Advocacy complies with this requirement by issuing an annual report that discusses agency compliance with the RFA and comments it has filed with agencies concerning RFA compliance. Annual reports for Fiscal Years 2001 through 2012 are available on SBA Advocacy's website, <http://www.sba.gov/advocacy/823/4798>.

¹³ Exec. Order No. 13,272, 67 Fed. Reg. 53,461 (Aug. 16, 2002).

¹⁴ OFFICE OF THE CHIEF COUNSEL FOR ADVOCACY, UNITED STATES SMALL BUSINESS ADMINISTRATION, A GUIDE FOR GOVERNMENT AGENCIES: HOW TO COMPLY WITH THE REGULATORY FLEXIBILITY ACT (2012), available at http://www.sba.gov/sites/default/files/rfaguide_0512_0.pdf.

¹⁵ Some people call them SBREFA panels after the Small Business Regulatory Enforcement Fairness Act, which created the requirement for the Environmental Protection Agency (EPA) and the Occupational Safety and Health Administration (OSHA). Pub. L. No. 104-121, Title II, § 244, 110 Stat. 857, 867 (1996). The Consumer Financial Protection Bureau (CFPB) was added to the list of agencies in the Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, § 1100G, 124 Stat. 1376, 2112 (2010).

¹⁶ 5 U.S.C. § 609(a). The statute lists techniques that agencies should use, including, but not limited to: publishing the notice of proposed rulemaking in publications likely to be obtained by small businesses; conducting public

For three agencies, CFPB, EPA, and OSHA, the outreach requirements are even stronger.¹⁷ When any of these agencies are ready to issue a proposed rule for which they would have to prepare an IRFA, they are required to conduct a formal procedure prior to publication of the proposed rule in the Federal Register. Essentially, the agency obtains input from small businesses on the potential impact of the rule and alternatives that might abate its effects. The agency, in consultation with SBA Advocacy, identifies small businesses from the affected industries to serve as small entity representatives (SERs), and provides SERs with any draft of the proposed rule, analysis of the impacts on small businesses, and a description of any significant alternatives. The SERs then provide their assessment of the proposed rule, and its potential impacts on small businesses, to the SBAR panel. The SBAR panel, made up of federal employees,¹⁸ then prepares a report which the agency includes in the notice of proposed rulemaking.¹⁹

III. Compliance Issues with the RFA

As previously stated, the antecedent to the requirement to comply with the RFA is notice and comment rulemaking pursuant to the APA or another statute. Section 553 of the APA provides the basic framework governing the federal agency process for “notice and comment rulemaking.”²⁰

Section 553 also contains exemptions from the notice and comment rulemaking process for: 1) rules dealing with military and foreign affairs functions; 2) rules relating to agency management or personnel or to public property, loans, grants, benefits or contracts; 3) interpretative rules, policy statements, and procedural rules; or 4) rules for which an agency finds there is “good cause” to forgo the notice and comment process because it is impracticable, unnecessary, or contrary to the public interest.²¹ When agencies fail to undertake notice and comment rulemaking through inappropriate reliance on an exception to the APA’s notice and comment requirement, the agencies also are avoiding their obligation to consider impacts on small businesses as mandated by the RFA.

Even when agencies do conduct notice and comment rulemaking as required by § 553 of the APA, they sometimes give short shrift to the RFA’s requirements. For example, agencies certify rules as not having a significant economic impact on a substantial number of small businesses but fail to provide a factual basis as required. They also publish IRFAs and FRFAs that have significant flaws in the economic impact analyses or lack a discussion of significant alternatives that reduce impacts on small businesses. Sometimes agencies do not conduct the kind of affirmative outreach that is

hearings concerning the rule for small businesses and soliciting comments via the Internet; and adopting agency procedural rules to reduce the cost and complexity of participation in the rulemaking process. *Id.*

¹⁷ *Id.* at § 609(b)-(d).

¹⁸ The SBAR panel consists of an employee of SBA Advocacy, an employee of the Office of Management and Budget’s Office of Information and Regulatory Affairs, and an employee of the agency writing the rule.

¹⁹ The covered agency may respond to the report prior to publication of the proposed rule. The report and agency response must be placed in the public rulemaking record and summarized in the notice of proposed rulemaking.

²⁰ 5 U.S.C. § 553. The phrase “notice and comment rulemaking” comes from the requirements in § 553 that agencies must publish the notice of proposed rulemaking in the Federal Register, allow interested persons the opportunity to submit written comments, and publish the final rule not less than 30 days before its effective date. *Id.*

²¹ *Id.*

required under § 609 of the RFA and accordingly limit the opportunity for small businesses to provide adequate input in the rulemaking process. We address this seriatim.

A. Inadequate Support for Certification

The RFA provides no exception to the requirement that an agency either publish an IRFA or a certification statement with a factual basis. Too often agencies will certify a rule as not having a significant economic impact on a substantial number of small businesses but fail to include a factual basis for the certification. If an agency lacks the information needed to complete its threshold analysis of the proposed rule, the notice of proposed rulemaking will not provide adequate information upon which the regulated entities may comment. More importantly, it fails to alert small businesses that the proposed rule may be of consequence to them, thereby undermining the outreach requirements of § 609(a) of the RFA.

B. Regulatory Flexibility Analyses and Consideration of Alternatives

There are three key elements to an agency's compliance with the RFA's regulatory flexibility analyses requirements. They are: 1) identification of the affected small businesses; 2) estimate of the costs; and 3) development of less burdensome alternatives. Unfortunately, there are instances where agencies do not adequately identify the small businesses that will be affected by the rule and do not adequately estimate the costs associated with the rule. If an agency does not identify the costs and impacts of the rule on small business, the agency may lack the information it needs to develop significant alternatives that can accomplish the objectives of the rule while minimizing the costs on small business.²²

C. Affirmative Outreach Requirements

The RFA is an analytical process that builds upon the rulemaking process imposed upon agencies by the APA. Under the APA, agencies may not take actions that are "arbitrary, capricious, an abuse of discretion, or otherwise not in accordance with law."²³ In other words, this standard requires agencies to promulgate rational rules.²⁴ Creating rational rules requires the agency to: 1) understand the problem it seeks to solve; 2) craft potential solutions; 3) request public comment on those solutions; and 4) design a final rule that complies with all relevant statutory requirements.²⁵

Since 99.7 percent of employer firms are small businesses,²⁶ which consequently represent the majority of businesses most likely to be subject to any particular regulation, the RFA forces agencies to do outreach to small businesses during the rulemaking process. Notice and comment plays one part in the effort to obtain information from the regulated community. The outreach requirements of the RFA provide another. This outreach ensures that the agency will have considered the relevant factors, including the impact on small business. Ultimately, these

²² An agency need not examine every alternative or every alternative that significantly reduces adverse consequences or provides maximum benefit to small business. See *Associated Fisheries of Maine v. Daley*, 127 F.3d 104, 115 (1st Cir. 1997).

²³ 5 U.S.C. § 706(2)(A).

²⁴ Pineles, *supra* note 3, at 30.

²⁵ *Id.*

²⁶ http://www.sba.gov/sites/default/files/FAQ_Sept_2012.pdf.

affirmative outreach requirements should result in a dialogue between the regulator and the regulated entities that helps the regulator create a rule that solves the problem it seeks to solve without unduly burdening small businesses. Unfortunately, agencies often err on the side of doing minimal outreach unless there is a public outcry.

D. Regulatory Flexibility Agendas

Section 602 of the RFA requires federal agencies to publish a regulatory flexibility agenda in the Federal Register each April and October. In the regulatory flexibility agendas, agencies must identify rules that they expect to propose or promulgate which are likely to have a significant economic impact on a substantial number of small businesses. The regulatory flexibility agendas provide small businesses and their advocates with information about potential new regulatory burdens. Compliance with § 602 is the first step in ensuring that small businesses have the ability to provide adequate input in the rulemaking process and should be viewed as a necessary, but not sufficient, component of the RFA's outreach requirements.

The current Administration has recognized that publication of the semiannual regulatory agendas, and by extension the regulatory flexibility agendas, is "a key component of the regulatory planning mechanism" that was prescribed in Executive Order 12,866.²⁷ Nevertheless, the Fall 2011 regulatory flexibility agenda was published four months late, the Spring 2012 agenda was never published, and the Fall 2012 agenda was not published until January 8, 2013. Failure to publish regulatory flexibility agendas each April and October violates the RFA.

IV. Conclusion

The RFA was designed to improve the quality of the agency rulemaking process by requiring that impacts on small businesses are examined and alternatives that are less costly are considered. Although agency compliance has improved over the intervening years, agencies also have gone to considerable lengths to avoid complying with the RFA. Regulators must comply with the RFA to ensure that unnecessary burdens are reduced and small businesses are able to thrive in a challenging economy.

²⁷ Cass R. Sunstein, Administrator, Office of Information and Regulatory Affairs, Office of Management and Budget, Memorandum for Regulatory Policy Officers at Executive Departments and Agencies and Managing and Executive Directors of Certain Agencies and Commissions, re: Spring 2012 *Unified Agenda of Federal Regulatory and Deregulatory Actions*, at 1 (Mar. 12, 2012), available at <http://www.whitehouse.gov/sites/default/files/omb/assets/inforeg/agenda-data-call-and-guidelines-spring-2012.pdf>.