

**Testimony of**

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**U.S. House of Representatives  
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Subcommittee on Commercial and Administrative Law**

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Improvements to the Regulatory Flexibility Act**

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Mr. Chairman and Members of the Committee, I am pleased to present this testimony on legislation that is needed to improve the Regulatory Flexibility Act so that small business can benefit from regulatory relief.<sup>1</sup> My name is Tom Sullivan. I am an attorney with the law firm of Nelson Mullins Riley & Scarborough, LLP and I run the Small Business Coalition for Regulatory Relief.<sup>2</sup> This testimony is not being presented on behalf of any specific clients. Rather, my advice to the Committee today is drawn from my two decades of work on small business regulatory issues.

My first job in Washington was with the U.S. Environmental Protection Agency (EPA). I served under both Administrator Bill Reilly and Administrator Carol Browner. After learning about regulatory policy development from within government, I joined the Washington office of the National Federation of Independent Business (NFIB). My crowning achievement at NFIB was the successful effort to prevent small businesses from being sued under the Superfund law just because they sent household garbage to their local landfill. That was the story of Barbara Williams of Gettysburg, Pennsylvania who I was honored to be with when President Bush signed the small business superfund bill on January 11, 2002.<sup>3</sup> Later that month, I was unanimously confirmed to head the Office of Advocacy at the U.S. Small Business Administration (SBA). The Office of Advocacy is responsible for overseeing the Regulatory Flexibility Act.<sup>4</sup> I served as Chief Counsel for Advocacy until October 2008.

### **The need for small business protections in the federal rulemaking system**

There are three basic reasons for the Regulatory Flexibility Act.

- one-size-fits-all federal mandates do not work when applied to small business; and
- small business faces higher costs per employee to comply with federal regulation; and
- small business is critically important to the American economy.

As I will explain, the Regulatory Flexibility Act has not worked as well as it could to address the underlying regulatory challenges faces by small businesses. That is why I support efforts to improve the law's effectiveness through legislation.

### **Prevention of one-size-fits-all federal mandates**

Many times federal regulations that may work for large corporations simply do not work for small firms. I remember working with Brian Landon on the ergonomics regulation when it was being developed in the late 1990's. Brian owned and operated a carwash in Canton,

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<sup>1</sup> *Regulatory Flexibility Act*, Pub. L. No. 96-354, 94 Stat. 1164 (1980), amended by the Small Business Regulatory Enforcement Fairness Act of 1996, Pub. L. No. 104-121, 110 Stat. 857 (1996) (codified as amended at 5 U.S.C. §§ 601-612), also amended by § 1100 G of the Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, 124 Stat. 2112 (July 21, 2010).

<sup>2</sup> See <http://www.SBCRR.com>.

<sup>3</sup> *Small Business Liability Relief and Brownfields Revitalization Act*, Pub. L. No. 107-118, 115 stat. 2356 (2002).

<sup>4</sup> See <http://www.sba.gov/advocacy>.

Pennsylvania. Parts of the ergonomics regulation distinguished between the employees who worked on equipment and employees who were in charge of paperwork and back room operations. As is the case in many small businesses, Brian did all the jobs. And, his most trusted employees also performed multiple tasks, some clerical and some operational. The ergonomics regulation spelled out duties for the equipment maintenance employees that were very different from those responsibilities for the employees in charge of paperwork. Brian continually asked the Occupational Safety and Health Administration (OSHA) for help to figure out which classification would apply to him – and never really got an answer. Sometimes we forget that our country has millions of small enterprises that are at various stages of automation. For instance, when there is a new labeling requirement, a tendency is to naively think that compliance with a regulation mandating changes to labels can be accomplished with little effort through a computer program. The Regulatory Flexibility Act is supposed to force federal regulators to think about how a small operation would actually comply, realizing that it may not be as simple as entering information into a computer.

### **The disproportionate impact federal regulations have on small business**

Research published in September by Nicole Crain and W. Mark Crain of Lafayette College updates three previous studies on the impact of federal regulations on small business.<sup>5</sup> The report is entitled, “*The Impact of Regulatory Costs on Small Firms,*” and it provides a look at the regulatory burden in 2008. The total cost of complying with federal regulations was over \$1.75 trillion. The burden amounts to a cost of \$15,586 per household which is more than 1 ½ times what households pay for medical care. Most alarming, is the fact that in the four years studied, the cost of complying with federal regulations rose faster than the per-household cost of medical care.

The Crain study found that small businesses shoulder costs that are 36% more than their larger business competitors. Firms with fewer than 20 employees pay \$10,585 per employee per year and firms with 500 or more employees pay \$7,755 per employee to comply with federal regulations. The cost difference is most severe when looking at compliance with environmental regulations, with the smallest firms paying 4 times the amount per employee than the largest businesses.

The research provides data for a common sense reality in a small business owner’s world. Small businesses generally do not have vice presidents for safety and health to figure out OSHA rules. They do not have accounting departments to navigate changes to the tax code. Even if small businesses hire accountants to prepare their taxes, the owners take hours sweating the details because it is their signature on the IRS forms. Nor do small firms usually employ environmental engineers to track all the greenhouse gas regulations issued by the EPA. The task of figuring out volumes of federal requirements often falls on the small business owners themselves, taking

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<sup>5</sup> Nicole V. Crain and W. Mark Crain, *The Impact of Regulatory Costs on Small Firms*, written for the Office of Advocacy, U.S. Small Business Administration (September 2010), available at <http://www.sba.gov/advocacy/853/2016>.

more time for them than it would for regulatory experts. Since time is money - it costs the small businesses more.

The intention of the Regulatory Flexibility Act is to bring small entities directly into an advisory role with agencies so that final regulations reflect an accurate understanding of how compliance can cost small firms more.

### **The importance of small business to the U.S. economy**

Recent figures show there are more than 27.3 million small businesses in the United States.<sup>6</sup> They represent over 99% of the employer firms in the United States, employ half of the private sector employees, and produce 13 times more patents per employee than large research & development firms.<sup>7</sup> Of particular importance is the job-creation aspect of entrepreneurship. Small firms accounted for 65% of the 15 million net new jobs created between 1993 and 2009. Data show that since the 1970's small businesses hire two out of every three jobs and the Ewing Marion Kauffman Foundation likes to point out that in the last 30 years, literally all net job creation in the United States took place in firms less than five years old.<sup>8</sup>

### **History of the Regulatory Flexibility Act**

One of the top five recommendations from the 1980 White House Conference on Small Business was for a law requiring regulatory impact analysis and a regular review of regulations. That recommendation became reality when President Jimmy Carter signed the Regulatory Flexibility Act into law on September 19, 1980. The Regulatory Flexibility Act directed all agencies that use notice and comment rulemaking to publicly disclose the impact of their regulatory actions on small entities and to consider less burdensome alternatives if a proposal was likely to impose a significant impact. The law authorized SBA's Chief Counsel for Advocacy to appear as amicus curiae in Regulatory Flexibility Act challenges to rulemakings and it required SBA's Office of Advocacy to report annually on agencies' compliance with the Regulatory Flexibility Act.

In 1996, Congress considered changes to the Regulatory Flexibility Act; much like this Committee is doing now. Again, there was a White House Conference – and that conference's top recommendation was to strengthen the Regulatory Flexibility Act by directing small business participation in rulemakings and to allow for judicial review of agency compliance. President Clinton signed the Small Business Regulatory Enforcement Fairness Act (SBREFA) in March of 1996.<sup>9</sup> Those amendments to the Regulatory Flexibility Act established formal procedures for

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<sup>6</sup> Office of Advocacy, U.S. Small Business Administration, *Frequently Asked Questions* (January 2011), available at <http://www.sba.gov/advocacy/7495>.

<sup>7</sup> *Id.*

<sup>8</sup> John Haltiwanger, *Business Dynamics Statistics Briefing: Jobs Created from Business Startups in the United States*, Ewing Marion Kauffman Foundation (January 2009), available at: <http://www.kauffman.org/research-and-policy/bds-jobs-created.aspx>.

<sup>9</sup> *Small Business Regulatory Enforcement Fairness Act of 1996*, Pub. L. No. 104-121, 110 Stat. 857 (1996).

the EPA and for OSHA to receive input from small entities prior to the agencies proposing rules.<sup>10</sup>

In August of 2002, President Bush signed Executive Order 13272, *Proper Consideration of Small Entities in Agency Rulemaking*.<sup>11</sup> The Executive Order directed SBA's Office of Advocacy to train regulatory agencies on how to comply with the RFA and further instructed agencies to consider the Office of Advocacy's comments on proposed rules. The Small Business Jobs Act signed five months ago codified the Executive Order's requirements for agencies to respond to the Office of Advocacy's comments in final rules.<sup>12</sup>

There was one recent additional amendment to the Regulatory Flexibility Act. An amendment authored by Senators Olympia Snowe and Mark Pryor was adopted as part of the Dodd-Frank financial regulatory reform law. That amendment requires the newly created Consumer Financial Protection Bureau (CFPB) to conduct a small business panel process when issuing rules, the same requirement that EPA and OSHA already follow.<sup>13</sup>

### **What is required by the Regulatory Flexibility Act**

The basic spirit of the RFA is for government agencies to analyze the effects of their regulatory actions on small entities and for those agencies to consider alternatives that would allow agencies to achieve their regulatory objectives without unduly burdening small entities.

The RFA covers all agencies that issue rules subject to the Administrative Procedure Act (APA). The RFA requires agencies to publish an initial regulatory flexibility analysis (IRFA) unless the promulgating agency certifies that the rule will not have a significant impact on a substantial number of small entities.<sup>14</sup> The IRFA is supposed to be a transparent small business impact analysis that includes discussion of alternatives that can accomplish the stated objectives of the rule while minimizing impact on small entities. In the case of EPA, OSHA, and the CFPB, a small business advocacy review panel aids the agency's analysis and discussion of alternatives. This transparent analysis and exchange of information with small entities is published with the agency's proposed rule, educating stakeholders who participate in the notice and comment process.

The availability of an IRFA allows for a more informed notice and comment process that can guide an agency's formulation of its final rule. Under the RFA, an agency's final rule must

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<sup>10</sup> See, 5 U.S.C. §609.

<sup>11</sup> Executive Order 13272, *Proper Consideration of Small Entities in Agency Rulemaking*, 67 Fed. Reg. 53461 (August 16, 2002).

<sup>12</sup> *Small Business Jobs Act of 2010*, Pub. L. No. 111-240, §1601 (September 27, 2010).

<sup>13</sup> *Dodd-Frank Wall Street Reform and Consumer Protection Act*, Pub. L. No. 111-203, §1100G (July 21, 2010).

<sup>14</sup> See, 5 U.S.C. §605(b).

contain a final regulatory flexibility analysis (FRFA) if it published an IRFA with its proposal. The FRFA is basically a public response to issues raised in the IRFA.

### **Regulatory Flexibility Act in practice**

The Office of Advocacy at the U.S. Small Business Administration monitors implementation of the Regulatory Flexibility Act. A full accounting of how agencies are complying with the Act is published annually.<sup>15</sup> Also, a comprehensive history of the office's work has been published twice to aid with political transitions (Jere Glover published a background paper covering 1994-2000 and the office published a background paper covering 2001-2008 under my signature).<sup>16</sup>

From 2001-2008, the Office of Advocacy reviewed approximately 1,300 regulatory proposals every year. In those 7-years, the Office of Advocacy issued 300 public comment letters to 60 agencies (averaging 38 per year). Most of the comment letters are critical of agencies, but offer constructive suggestions on how agencies can tailor their approaches to achieve the desired regulatory outcome while minimizing the burden on small businesses. Even though the back and forth between the Office of Advocacy and regulatory agencies produces cost-savings, enhancements to the Regulatory Flexibility Act will make outcomes more consistent government wide and will reduce the tendency of some agencies to ignore the requirements of the Act.

### **Improvements to the Regulatory Flexibility Act are needed**

There are gaps in the law that need to be fixed and now is the time to do it. Small businesses continue to struggle as our economy tries to recover and they need to have their voices heard when government is considering piling more federal mandates on them. If you have any doubt about the fear small businesses have of the federal regulatory state, just consider these daunting statistics: In the last 2-years, the federal government issued 132 economically significant regulations (defined as having impacts of \$100 million or more per year).<sup>17</sup> Compare this against the average of 66 major rules per year with the average of 48 per year under President Bush and the average of 47 per year under President Clinton. Rulemakings are not slowing down either. There are 181 more regulations underway now than last year, representing a 5 % increase in activity. According to plans issued recently by regulatory agencies, there is a 20% increase in economically significant regulations under development.<sup>18</sup>

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<sup>15</sup> See, Office of Advocacy annual reports on the Regulatory Flexibility Act, available at <http://archive.sba.gov/advo/laws/flex/>.

<sup>16</sup> See, Background Paper on the Office of Advocacy 1994-2000, available at [http://archive.sba.gov/advo/advo\\_backgr00.html](http://archive.sba.gov/advo/advo_backgr00.html) <http://archive.sba.gov/advo/about.html>.  
See, Background Paper on the Office of Advocacy 2001-2008, available at <http://archive.sba.gov/advo/backgr08.pdf>.

<sup>17</sup> Susan Dudley, *President Obama's Executive Order: Improving Regulation and Regulatory Review*, Regulatory Policy Commentary, The George Washington University Regulatory Studies Center (January 18, 2011). Available at [http://www.regulatorystudies.gwu.edu/images/commentary/20110118\\_reg\\_eo.pdf](http://www.regulatorystudies.gwu.edu/images/commentary/20110118_reg_eo.pdf).

<sup>18</sup> *Id.*

### **Require Agencies to publish more complete impact analysis**

With the exception of the Consumer Financial Protection Bureau (CFPB), the Regulatory Flexibility Act requires agencies to analyze the *direct* impact a rule will have on small entities. Unfortunately, limiting the analysis to direct impacts does not accurately portray how small entities are affected by a new federal rule. For instance, when greenhouse gas regulations impose a direct cost on an electric utility, EPA should make public how its proposal will likely affect the cost of electricity for small businesses. I believe that the rulemaking process is short changed by not including discussion of such obvious impacts.

The notice and comment rulemaking process benefits from informed stakeholders who participate and offer constructive suggestions for how agencies can achieve their regulatory objectives. Analysis of how a regulatory proposal will impact energy costs, transportation costs, jobs and employment costs, and other reasonably foreseeable costs would go far in educating stakeholders so they can offer constructive solutions to regulatory agencies.

### **All agencies should utilize small business advocacy review panels**

As of now, the Regulatory Flexibility Act requires that EPA, OSHA, and the CFPB convene small business advocacy review panels to solicit input from small entities. The report that contains small business input is published with proposed rules. The panel process was created under the Small Business Regulatory Enforcement Fairness Act (SBREFA), so I refer to them as “SBREFA Panels” for the remainder of this testimony. SBREFA panels have proved instrumental in helping EPA and OSHA come up with regulatory solutions that minimize burden on small entities. When I was Chief Counsel for Advocacy, I did not think that the Regulatory Flexibility Act needed to be amended to force every regulatory agency to utilize SBREFA. I thought that agencies could do a good enough job soliciting input from small businesses on their own. Now I realize that some agencies will resist formally soliciting help from small entities prior to issuing proposed rules. Requiring the CFPB to have SBREFA panels made sense and that is why it passed into law. The same logic applies across the board to all federal agencies and that is why SBREFA panels should become the norm, not the exception.

### **SBA’s Office of Advocacy should clarify definitions in the Regulatory Flexibility Act**

Disputes over whether an agency’s proposed rule will “significantly economic impact on a substantial number of small entities” have limited the effectiveness of the Regulatory Flexibility Act. Legislation under consideration by this Committee addresses this problem by giving the Office of Advocacy rulemaking authority. Rules that better define how agencies are to properly consider small business impacts will benefit the process in two ways. First, it will minimize the confusion over whether agencies are properly considering small business impact. Second, rulemaking authority will confirm the primacy of the Chief Counsel for Advocacy when courts ultimately render opinions on the Regulatory Flexibility Act.

**Section 610 (periodic review of regulations) should be improved**

Section 610 of the Regulatory Flexibility Act requires agencies to review rules within 10 years of their publication.<sup>19</sup> It only makes sense that if the federal government expects business owners to know what rules are on the books, the agencies themselves have a duty to make sure rules are not out-of-date or duplicative of newer requirements. Unfortunately, the look back section of the Regulatory Flexibility Act has not resulted in significant regulatory reform that benefits small business. Michael See, an attorney who worked at the Office of Advocacy, wrote a law review article that has in its title, “willful blindness: federal agencies’ failure to comply with the Regulatory Flexibility Act’s periodic review requirement.”<sup>20</sup> As you would guess from its title, Mr. See’s research paints a dismal picture of agency compliance with Section 610. Mr. See’s observations are supported by Government Accountability Office (GAO) reports issued in 1994, 1997, and 1999 and a report issued by the Congressional Research Service (CRS) issued in 2005.<sup>21</sup> The legislation being considered by this Committee will bolster the effectiveness of Section 610 by broadening the number of rules that agencies will review, requiring transparency of the reviews by reporting annually to Congress and to the Chief Counsel for Advocacy, and by better defining the process through rulemaking by the Office of Advocacy.

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<sup>19</sup> 5 U.S.C. § 610.

<sup>20</sup> Michael See, *Willful Blindness: Federal Agencies’ Failure to Comply With the Regulatory Flexibility Act’s Periodic Review Requirement – And Current Proposals to Invigorate the Act*, 33 Fordham Urb. L.J. 1199 (2006) available at [http://archive.sba.gov/advo/laws/rfa\\_610review06.pdf](http://archive.sba.gov/advo/laws/rfa_610review06.pdf)

<sup>21</sup> See, U.S. Government Accountability Office, *Regulatory Flexibility Act: Status of Agencies’ Compliance* (1994), available at <http://archive.gao.gov/t2pbat3/151400.pdf>

See, U.S. Government Accountability Office, *Regulatory Reform: Agencies’ Efforts to Eliminate and Revise Rules Yield Mixed Results* (1997), available at <http://www.gao.gov/archive/1998/gg98003.pdf>

See, U.S. Government Accountability Office, *Regulatory Flexibility Act: Agencies’ Interpretations of Review Requirements Vary* (1999), available at <http://www.gao.gov/archive/1999/gg99055.pdf>

See, Curtis Copeland, Congressional Research Service, *Reexamining Rules: Section 610 of the Regulatory Flexibility Act* (2005), available at [http://assets.opencrs.com/rpts/RL32801\\_20050311.pdf](http://assets.opencrs.com/rpts/RL32801_20050311.pdf)

### **Small business regulatory relief beyond the context of the Regulatory Flexibility Act**

There are additional ways for Congress to reform the regulatory process to benefit small business. One reform that I would urge this Committee to look at in this Congress is to force agencies to waive penalties for first time non-harmful paperwork violations. I have never met a small business owner who was trying to be successful based on deliberately thwarting government regulators. I have talked with many small employers who are terrified they may be doing something wrong and the last person they would call for advice is someone at a government agency. Despite several efforts by government to move away from “gotcha” towards an attitude of “help ya,” there still is a perception that federal regulators will fine a business even when the mistake is an innocent paperwork violation that did not result in any real harm. Small businesses should be rewarded for trying to comply and if their efforts result in a harmless paperwork error, enforcement officials should be required to waive that violation.

Another reform is to insert greater accountability into the regulatory process. Legislation that is already under consideration by this Committee, the Regulations from the Executive In Need of Scrutiny Act (REINS) accomplishes this goal.

### **Conclusion**

I strongly support the legislation being considered by this Committee to amend the Regulatory Flexibility Act. The legislation will help focus regulatory agencies on the need to remove regulatory barriers and create an environment where small businesses can grow and create jobs.