Office of Advocacy

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Testimony of

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Created by Congress in 1976, The Office of Advocacy of the U.S. Small Business Administration (SBA) is an independent voice for small business within the federal government. The Chief Counsel for Advocacy, who is appointed by the President and confirmed by the U.S. Senate, directs the office. The Chief Counsel advances the views, concerns, and interests of small business before Congress, the White House, federal agencies, federal courts, and state policy makers. Issues are identified through economic research, policy analyses, and small business outreach. The Chief Counsel's efforts are supported by offices in Washington, D.C., and by Regional Advocates located across the United States. For more information on the Office of Advocacy, visit http://www.sba.gov/advo, or call (202) 205-6533.

Chairman Manzullo, Ranking Member Velázquez, Members of the Committee, good morning and thank you for the opportunity to appear before you today to discuss the Small Business Regulatory Enforcement Fairness Act (SBREFA).

First, let me tell you what an honor and privilege it is for me to have been appointed Chief Counsel for Advocacy by President Bush. Since my confirmation just over one month ago, I have had an incredible experience. I am grateful for the tremendous support I have had from Members of Congress; from Administrator Barreto; from the staff of the Office of Advocacy; from government leaders; and from our many small business organization and trade association friends.

Although I had worked with Advocacy on many issues while I was Regulatory Policy Counsel for the National Federation of Independent Business (NFIB), and more recently Executive Director of the NFIB Legal Foundation, as Chief Counsel I have a new appreciation for the talent and energy of Advocacy's staff. I want to give special thanks to my deputy, Susan Walthall, who is with me here today. Susan served as Acting Chief Counsel until my confirmation, and she did a great job in keeping the Office of Advocacy running smoothly during this transition period, in addition to helping me prepare for the challenges ahead.

Last October, the Office of Advocacy held a day-long symposium marking its 25th anniversary. The theme of this event was "Advocacy at 25: Looking Back, Looking Ahead" and we did just that. Although I had not yet had my confirmation vote, I attended as a "civilian" along with more than 200 other Advocacy stakeholders and small business advocates from the

government, academic and private sectors. In addition to working sessions organized around Advocacy's regulatory and economic research missions, there was an excellent presentation on an important new study released that day on the costs of regulatory compliance, and an address by Dr. John Graham, Administrator of OMB's Office of Information and Regulatory Affairs, with whom, I might add, we are working closely.

But perhaps my favorite session that day was a roundtable featuring all four of my confirmed predecessors, former Chief Counsels Milt Stewart, Frank Swain, Tom Kerester, and Jere Glover – all of whom I am proud to call my friends. As I begin my tenure as the fifth confirmed Chief Counsel for Advocacy, I must tell you that I am humbled, not only by their achievements, but also by the enormity of the challenges ahead of us.

I am committed to addressing these challenges with renewed energy. We are working now on a strategic plan for the future, and are aggressively seeking ways to fine-tune our activities and refocus our limited resources to get more bang for the buck, while at the same time maintaining the quality of Advocacy's work, continuity in our ongoing activities, and commitment to our core missions.

I commend the Committee for its review of SBREFA at this time. As we are both looking back and looking ahead, and renewing our commitment to serve America's small businesses, it is appropriate that we examine together how one of our most important legislative tools has been working after more than five years' experience, with a view towards possible fine-tuning and improvements.

The importance of SBREFA

SBREFA **has** made a difference – a big difference, both in opening the rulemaking process to greater scrutiny and participation by those it affects, and in achieving quantifiable reductions in the regulatory burden on small business. Perhaps even more important, SBREFA is helping change the regulatory culture in at least some government agencies, an outcome far more significant than individual rulemakings. We want regulators to think about the effects of their proposals **before** they act, and our experience has shown that SBREFA helps accomplish this goal.

SBREFA amended the 1980 Regulatory Flexibility Act (RFA) in several significant ways. **First**, it gave the courts jurisdiction to review agency compliance with the RFA, thus providing for the first time a legal mechanism to ensure agency compliance with the law. **Second**, SBREFA mandated that the Environmental Protection Agency (EPA) and the Occupational Safety and Health Administration (OSHA) convene "Small Business Advocacy Review Panels" to elicit information from small entities on rules expected to have a significant impact on them, and to do so **before** the regulations are published for public comment. This formalized for those two agencies a process to involve small entities early in the agencies' deliberations on the small business impacts of regulatory proposals, and it forced agencies to consider equally effective alternatives. **Third**, SBREFA reaffirmed the authority of the Chief Counsel for Advocacy to file *amicus curiae* (friend of the court) briefs in appeals brought by small entities seeking relief from agency final actions.

Each of these three SBREFA provisions has had its effect and has made a positive contribution to our efforts to control unnecessary regulation. The judicial review provision has been particularly important. Small businesses are increasingly seeking judicial review of agency compliance with the RFA and having some success. Several court decisions have remanded rules to agencies for failure to comply with the RFA. The potential for judicial review provides a significant incentive for agencies to do more in-depth small business impact analyses and to take other steps to strengthen their in-house regulatory development processes.

Similarly, Advocacy's authority to join in litigation against agencies charged with failure to comply with the RFA has given pause to those that in the past ignored that Act's requirements. This *amicus* authority, which we use sparingly, is one more powerful incentive for agencies to consider their actions carefully. Advocacy's first brief was filed in *Northwest Mining Assoc. v. Babbitt*. The court agreed with the issues raised by Advocacy and remanded the rule to the Department of Interior. In other instances, the mere threat of using our *amicus* authority has been sufficient for an agency to reconsider its position.

One measure of the effect that the judicial review and *amicus* authority provisions of SBREFA have had may be the newfound interest of regulatory agencies in RFA and SBREFA training, a phenomenon which, not surprisingly, blossomed after the *Northwest Mining* decision in 1998. Advocacy has developed materials for this purpose and conducted training sessions and individualized counseling for hundreds of regulatory development specialists, attorneys, program managers and high-level policy officials from agencies throughout government. Many of these agencies also now participate in Advocacy's informal industry roundtables, in which those

involved in developing regulations can meet, listen to, and learn from those who will be affected by their actions. It is difficult to quantify the effect that this early exchange of information has on mitigating the cost of regulation to small business, but we are convinced that it is real.

This brings me to a theme that I believe is of paramount importance – early intervention in the rule-making process. Important as the judicial review and *amicus* provisions of SBREFA are, it would be far preferable if we never had to use them at all. If agencies consistently honored their responsibilities under the RFA and actively involved small businesses at each step of the rule development process, there would be little need to go to court.

The review panel provisions of SBREFA, which now apply only to EPA and OSHA, promote this approach and provide a model for early intervention with a proven record of success. The panel process has confirmed that: (1) credible economic and scientific data, as well as sound analytical methods, are crucial to rational decision-making in solving regulatory problems; and (2) information provided by small businesses themselves on real-world impacts is invaluable in identifying equally effective regulatory alternatives. It is important to emphasize that although the regulations that result from panel deliberations are likely to be less burdensome to small business, public policy objectives need not be compromised.

Regulatory savings and SBREFA

Although EPA and OSHA are the only agencies now required to use the panel process, SBREFA is affecting all regulatory agencies. Agencies logically wish to avoid judicial

challenges to their rules and are taking greater care to comply with the RFA. But beyond this pain-avoidance incentive, we are beginning to see a genuine desire on the part of some agencies to listen to small business concerns and work with Advocacy to craft better rules. Regulations have been changed to minimize their impacts on small entities, and I would like to share with you just two examples: an important IRS rule on cost versus accrual accounting methods, and a Department of Transportation (DOT) rule on providing transportation services to individuals with disabilities.

Internal Revenue Service rule. The Internal Revenue Service recently announced a change allowing simplified tax filing for up to 500,000 additional small businesses beginning with tax year 2001 returns. IRS Notice 2001-76 allows certain small businesses with gross receipts of $10 million or less to use the cash method of accounting for income and expenses, instead of the costly and complicated inventory and accrual method. Until now, the IRS could impose the more stringent method, accrual accounting, on businesses with more than $1 million in receipts.

Under accrual accounting, a business generally reports income when it has a right to receive payment, and deducts expenses when it has a fixed and determinable liability for them. This obviously can become very complicated, requiring specialized accounting assistance. Further, it can create cash-flow problems for small businesses.

Allowing more small businesses to use the cash accounting method was one of the recommendations of the 1995 White House Conference on Small Business. The Office of

Advocacy and White House Conference delegates have been active in urging the IRS to make this change. Advocacy also supported congressional action on this issue in testimony before the Senate Committee on Finance last year, so we are very pleased that the IRS has been so responsive in this instance. Although this change will primarily be of benefit to small service providers – businesses in manufacturing, wholesaling, retailing and mining are generally excluded – we still welcome this provision, which helps so many small businesses.

Department of Transportation rule. Another example of how an agency's good-faith effort to comply with the RFA as amended by SBREFA has made a difference is the Department of Transportation's revision of a proposal to implement provisions of the Americans With Disabilities Act (ADA). DOT proposed a rule requiring that over-the-road buses be accessible to passengers with disabilities, and that companies using such buses (motor carriers, tour operators, etc.) provide accessible over-the-road service. Advocacy commented that the rule as proposed would have had a serious impact on the small bus industry, and that it would have caused small operators to reduce transportation available to the public as a whole – especially in rural areas. Advocacy proposed that a service-based alternative would provide better transportation to all passengers, including those with disabilities.

Advocacy then arranged a conference for DOT officials and small business representatives to discuss the various issues involved and alternatives to the proposed rule that could accomplish DOT's objective of providing service to the disabled, while not unduly burdening small motor carriers and precipitating unintended reductions in service to the general public. DOT agreed to review the costs projected by the small businesses. After careful study,

the agency then crafted an innovative approach that achieved its regulatory objective while striking a balance among competing public policy objectives. This approach was incorporated in DOT's final rule and included both an "on-call service" feature and a phase-in period.

DOT's final rule transitions the private bus industry to full service for passengers with disabilities, while in the near term maintaining service for passengers who rely on small bus companies for essential needs. In addition, the industry has estimated that the revisions made to DOT's original proposal resulted in savings of approximately $180 million. Advocacy commends DOT for its efforts to work with small business and our office in the spirit, as well as the letter, of the RFA to reach a solution to this difficult, but solvable problem.

These are but two examples of agencies adopting a common sense approach to regulation which has and will result in substantial savings to small business, one using a "tiered" approach and the other a phase-in linked to a unique, problem-specific solution. Advocacy's annual Regulatory Flexibility Act reports detail many more such examples.

We estimate that during fiscal years 1998 through 2001, modifications to federal regulatory proposals in response to RFA/SBREFA provisions, and consultation with Advocacy, resulted in cost savings totaling more than $16.4 billion, or more than $4.1 billion per year on average. Many of these savings have been counted only once, though in fact, had the underlying proposal been finalized without small business input, the resulting costs would have been recurring from year to year.

RFA/SBREFA compliance still needs improvement

I noted earlier that SBREFA is helping change the regulatory culture in at least some government agencies. It is important to note, however, that this cultural change is by no means uniform within or among regulatory agencies. One of the largest hurdles to be overcome remains agency resistance to the concept that regulatory alternatives that are less burdensome on small business may in fact be equally effective in achieving public policy objectives. Other agencies simply haven't "internalized' their RFA responsibilities and don't seem to view its requirements as germane to their mission.

As we reported in our 20th anniversary RFA report for FY 2000, a number of agencies consistently ignore the requirements of the RFA. Two regular offenders are the Federal Communications Commission (FCC) and the Centers for Medicare and Medicaid Services (CMS), formerly the Health Care Financing Administration.

FCC. FCC regulations have not included adequate discussion of potential small business impact. Its analyses frequently are of the cut-and-paste variety, offering no specific or relevant information pertaining to the substance of the rule. Vagueness in its notices is a problem.

For example, last November the FCC proposed major changes to the current intercarrier compensation regime, in which providers of phone services compensate each other for the origination and termination of calls that begin on each others' networks. First, from the information provided, Advocacy is not convinced that a complete restructuring is necessary. Additionally, the rulemaking itself lacks specifics. Instead, it makes broad inquiries to which a

response is requested. It is impossible to ascertain what the impact on small business is because of this vagueness. Advocacy recommended that the FCC recast this rulemaking as a "Notice of Inquiry" to gather information. The Commission could then use the comments received in response to its original Notice of Proposed Rulemaking to analyze the small business impacts in a regulatory flexibility analysis.

FCC has also failed to comply with Section 212 of SBREFA, which requires that agencies publish compliance guides for small business to help those regulated better understand the rules which these agencies promulgate, a subject to which I will return shortly.

CMS. Turning now to CMS. An advisory committee on regulatory reform has been formed at the Department of Health and Human Services to identify overly burdensome Medicare regulations promulgated by that agency. This is a positive development, but frankly, a number of these overly burdensome regulations would not be on the books today if CMS had complied with the RFA.

For example, in the case of the Medicare reimbursement methodology for portable x-ray providers, CMS has ignored Advocacy's comments and recommendations since 1998. Advocacy commented on the proposed rule, indicating that the overall reduction in Medicare reimbursement for portable x-ray services amounted to as much as 54 percent in some cases, and that the agency had not prepared an adequate analysis of the impact on small entities. GAO also published a report in 1998 acknowledging (with some uncertainty) that portable x-ray providers may not be able to continue supplying services as a result of the reduced payments.

CMS published a final rule in this case which essentially ignored the comments of Advocacy and industry, so Advocacy submitted additional comments indicating that, under the RFA, the agency was required to address comments received in response to the initial regulatory flexibility analysis. Eventually, a transition period for implementation was allowed after a post-final rule discovery that a transition payment provision had been left out of the rule. This "fix" still did not address the overall issue of the need for an impact analysis. In December 2001, Advocacy was again forced to comment on a new payment regulation - this time a direct final rule, where the agency waived the Administrative Procedure Act requirement for a notice of proposed rulemaking. Once again, the agency failed to assess adequately the impact of the rule on small portable x-ray providers.

SBREFA Section 212 concerns

Before I conclude, I would like to offer a few remarks on Section 212 of SBREFA, which requires that agencies publish compliance guides to assist small entities in understanding rules for which final regulatory flexibility analyses (FRFAs) are required. This topic is timely because of a recently released GAO report entitled "Regulatory Reform: Compliance Guide Requirement Has Had Little Effect on Agency Practices." As the title suggests, GAO has found that agencies are not complying with Section 212, and I regret that this seems to be the case.

The problem is not restricted to the six agencies that were the subject of GAO's review. It is pervasive in other agencies as well. A particularly egregious example is the so-called "small entity compliance guide" published by the Federal Acquisition Regulation Council (FAR Council). In 1999, the FAR Council published in the *Federal Register* a list of all the previous

years' regulations with an asterisk beside those regulations containing a final regulatory flexibility analysis. In other words, the list itself was the compliance guide.

In yet another example, the FCC's Office of Communications Business Opportunities has created a web page to serve as a one-stop location for all of the agency's compliance guides. The agency claims that the site can be especially helpful to small businesses, and that it satisfies the requirements of Section 212 of SBREFA. Although the Small Business Compliance Guide list is of impressive length, with 285 entries, more than half do not address compliance questions at all. Of these 285 entries, 31 (or 11 percent) are consumer fact sheets aimed at consumers, 72 (or 25 percent) are news releases aimed at the media, and 43 (or 15 percent) are public notices with general information. The remaining 49 percent are links to issue pages, site maps, FAQ pages, and economic working papers. Some links are broken and lead nowhere. Few, if any, of the links on this site are devoted to small business issues. FCC's assertion that this website somehow satisfies its Section 212 obligations comports neither with the letter nor the spirit of SBREFA.

Frankly, I find it embarrassing that government agencies must be forced to publish guides to help small businesses comply with their rules. But recognizing that Section 212 is not working as intended, Advocacy wants to work with Congress and regulatory agencies to make sure that this problem is resolved. If additional legislation is needed to clarify the requirements of Section 212, then Advocacy would urge that consideration be given to the need for an oversight role. An annual report to this committee from each agency with respect to its compliance guide efforts might be productive. Also, further guidance from Congress on where and when the guides should be published and what they must include might help alleviate agency

confusion as to their responsibilities. Section 212 can hardly be called esoteric. What is really needed is a good faith effort to do the right thing.

Conclusion

In conclusion, I would like to refocus our discussion on why we have a SBREFA and an RFA, or why for that matter an Office of Advocacy – why do we go to all this trouble? Perhaps the best answer is the simplest – the bedrock importance of small business to our economy, both at the national and community levels.

These are the basic numbers, and though we small business advocates on both sides of the dais have heard similar statistics many times, I want to share with you the latest data we have. Small businesses:

- Represent more than 99 % of all employers;
- Employ 51% of private sector workers;
- Comprise nearly all of the self-employed, which are 7% of the workforce;
- Provide about 75% of net new jobs;
- Provide 52% of private sector output;
- Represent 96% of all exporters of goods;
- Obtain 33.3% of federal prime and subcontract dollars.

Small business is and has historically been our Nation's primary source of innovation, job creation, and productivity. It has led us out of recessions and economic downturns, offsetting job contraction by larger firms, and providing new goods and services. It has provided

tremendous economic empowerment opportunities for women and minority entrepreneurs. It plays an invaluable role in our defense industrial base. Small employers spend more than $1.5 trillion on their payroll.

All these are good reasons for us to work to ensure a healthy and competitive small business sector. Small business does not want preferential treatment – small business wants a level playing field. The cost of regulation is a good case in point. A recently released, Advocacy-sponsored study on this subject by W. Mark Crain and Thomas D. Hopkins disclosed that the cost of federal regulation to firms with fewer than 20 employees was almost $7,000 per employee, more than 50 percent higher than the per employee cost to businesses with 500 or more employees. This disproportionate burden is a huge impediment to small business realizing its full potential. Although small business has done a remarkable job in coping with this problem, it is tantalizing to think of what productive and innovative energies would be unleashed if we could reduce this burden.

That is why we are in business at Advocacy, and that is why the Congress wrote the Regulatory Flexibility Act and the Small Business Regulatory Enforcement Fairness Act – to help small businesses realize their full potential. Like the small businesses we serve, we must be flexible and innovative to respond to new challenges as they arise, but we must also keep focused on our core mission. I pledge the full cooperation and assistance of the Office of Advocacy in your deliberations on how best to accomplish this.

This concludes my prepared testimony. Thank you again for inviting me here today, and I am pleased to answer any questions you may have.