

January 13, 2005

Hand Delivery and E-mail

Mr. Gary M. Jackson
Assistant Administrator Office of
Size Standards
U.S. Small Business Administration
409 Third Street, SW, Mail Code 6500
Washington, DC 20416

RE: Advance Notice of Proposed Rulemaking: Small Business Selected Size Standards Issues; 69 Fed. Reg. 70197 (December 3, 2004).

Dear Mr. Jackson:

The Office of Advocacy submits this comment letter to the U.S. Small Business Administration's (SBA) Office of Size Standards in response to the above-referenced Advance Notice of Proposed Rulemaking (ANPRM). These comments represent the views of small entities shared with the Office of Advocacy pursuant to our procurement roundtable on April 4, 2004, and subsequent meetings held with, and letters received from, small businesses.

I. Advocacy Background

Congress established the Office of Advocacy (Advocacy) under Pub. L. 94-305 to represent the views of small business before Federal agencies and Congress. Advocacy is an independent office within the SBA, so the views expressed by Advocacy do not necessarily reflect the views of the SBA or of the Administration. Section 612 of the Regulatory Flexibility Act (RFA) requires Advocacy to monitor agency compliance with the RFA, as amended by the Small Business Regulatory Enforcement Fairness Act.¹ The RFA requires agencies to analyze the economic impact of proposed regulations when there is likely to be a significant economic impact on a substantial number of small entities, and to consider regulatory alternatives that will achieve the agency's goal while minimizing the burden on small entities.²

On August 13, 2002, President George W. Bush enhanced Advocacy's RFA mandate when he signed Executive Order 13272, which directs Federal agencies to implement

¹ Pub. L. No. 96-354, 94 Stat. 1164 (1980) (codified at 5 U.S.C. §§ 601-612) amended by Subtitle II of the Contract with America Advancement Act, Pub. L. No. 104-121, 110 Stat. 857 (1996). 5 U.S.C. § 612(a).

² See generally, Office of Advocacy, U.S. Small Business Administration, A Guide for Federal Agencies: How to Comply with the Regulatory Flexibility Act (2003).

policies protecting small entities when writing new rules and regulations.³ Executive Order 13272 instructs Advocacy to provide comment on draft rules to the agency that has proposed the rule, as well as to the Office of Information and Regulatory Affairs (OIRA) of the Office of Management and Budget.⁴ Executive Order 13272 also requires agencies to give every appropriate consideration to any comments provided by Advocacy. Under the Executive Order, the agency must include, in any explanation or discussion accompanying the final rule's publication in the *Federal Register*, the agency's response to written comments submitted by Advocacy on the proposed rule, unless the agency certifies that the public interest is not served by doing so.⁵

II. Proposed Revisions to the Size Standard Program and RFA Compliance

The Small Business Act requires SBA to establish distinct definitions by which businesses are deemed small and thus eligible to receive a variety of financial, procurement, and business development assistance as mandated by Congress. The regulations promulgated by the SBA, 13 Part 121 of the Code of Federal Regulations, implement the size standards program required by the Small Business Act. The SBA size standards regulations also define which businesses are small for RFA analysis purposes, unless after consultation with Advocacy and opportunity for public comment, the regulating agency establishes an alternate size standard for RFA analytical purposes.⁶

The Office of Advocacy recognizes the magnitude of the task before the SBA to revise its size standards program. We commend the SBA for its commitment to seek input from stakeholders before promulgating regulations to revise its size standards program as was urged in Advocacy's June 29, 2004, comment letter⁷ to SBA concerning its March 19, 2004, notice of proposed rulemaking (NPRM). Advocacy also applauds SBA for holding public meetings across the country to solicit further comment on the ANPRM.

In the March 2004 NPRM, SBA proposed to reduce the number of size standards and simplify the application of SBA's size standards to federal government programs. In general, SBA proposed to move from receipt-based size standards to a system that is mainly employee-based, but also defined a hybrid employee/receipt cap in particular cases. The proposed size standards range between 50 employees and 1,500 employees. Despite SBA's desire that the proposed changes have a neutral impact, there was concern in the small business community that the size standard changes would have the unintended consequence of penalizing some small entities that currently participate in federal programs. Small businesses advised Advocacy that the proposed rule could have had a negative impact on these small entities and lead to certain job loss. Some small businesses were concerned that adoption of the proposed size standards would have forced them to re-tool their businesses and reduce the size of their workforce in order to retain their small business designation. Advocacy urges SBA to consider the comments

³ Exec. Order No. 13272 § 1, 67 Fed. Reg. 53461 (Aug. 16, 2002).

⁴ E.O. 13272, at § 2(c).

⁵ *Id.* at § 3(c).

⁶ 5 U.S. C. § 601(3).

⁷ Advocacy's entire letter in response to these proposed regulations may be viewed at www.sba.gov/advo.

from small businesses carefully in order to overcome these barriers when it issues a new proposed size regulation.

A. SBA's RFA Analysis Must Better Analyze the Impact on Small Businesses

SBA's March 2004 proposed rule contained an initial regulatory flexibility analysis (IRFA) as was required by section 603 of the RFA. The IRFA noted that under the new size standards 35,200 new small businesses would become eligible for federal programs and that 34,100 would lose their small business designation resulting in a net gain of 1,100 small businesses. The projected gain in small businesses eligibility led the SBA to conclude that the rule's impact on small businesses would have a positive net effect. Advocacy is concerned that under this methodology the SBA has offset negative economic impacts on one group of small businesses by granting a benefit to another without adequate data and analysis. If the rule's benefits and costs were affecting the same small entities, then a net calculation may be appropriate; but if not, net impacts do not figure in the RFA calculation because it is not the same analysis that is required in a cost/benefit analysis.

The objective of the IRFA is to identify and analyze the economic impacts and consider less burdensome alternatives in a manner that enables the public to comment meaningfully on those impacts and the underlying proposed rule. This objective is consistent with the Small Business Act, 13 CFR Part 121.102, that states: "(a) SBA considers economic characteristics comprising the structure of an industry, including degree of competition, average firm size, start-up costs and entry barriers, and distribution of firms by size, and (b) as part of its review of a size standard, SBA will investigate if any concern at or below a particular standard would be dominant in the industry." Pursuant to section 603 of the RFA, Advocacy suggests that in the proposed rule the SBA should better analyze and discuss the magnitude of the impacts on any distinct groups of small businesses and consider alternatives that could further enhance the rule's benefits and reduce its costs. Comments submitted in response to the ANPRM and from SBA's national outreach hearings should help to ensure that the SBA has sufficient information to perform a more detailed small business impact analysis that takes into consideration, degree of competition, average firm size, start-up costs and entry barriers, and distribution of firms by size.

B. Impact of SBA Size Standards on the Regulations of other Federal Agencies⁸

SBA size standards establish the default small business size standards for the RFA and its application. The Regulatory Flexibility Act (RFA) requires agencies to consider the impacts of any proposed and final rule on small entities, including small businesses, small non-profit organizations and small governmental jurisdictions. Once an agency has made an initial determination that a proposed rule is likely to have a significant economic impact on a substantial number of small entities under the RFA, it must publish an IRFA

⁸ In the ANPRM, SBA seeks comment on the impact of SBA size standards on the regulations of other Federal agencies, 69 Fed. Reg. 70201 (December 3, 2004).

in its proposed rule so that the public may have an opportunity to comment on the potential economic impact of the rule on small entities.

As part of the RFA analysis agencies are required to utilize SBA's size standards. However, section 601(3) of the RFA states that an agency may establish an alternate definition of small business if they: 1) consult with the Office of Advocacy of the SBA, and 2) provide an opportunity for public comment by publication in the *Federal Register*. SBA's regulations further interpret section 601(3) of the RFA in Size Regulations 13 CFR 121.903(c), where an agency head may develop a size standard different from that established by SBA for the sole purpose of performing RFA analysis. Otherwise, regulations provide that an agency may do so only after written approval from the SBA Administrator.

In an attempt to comply with the analytical requirements of the RFA, agencies will often consider alternatives which provide small businesses with flexibilities or exemptions. However, SBA's current regulations potentially discourage agencies from adopting alternatives/exemptions that benefit small businesses because prior approval of the size standard from SBA's Administrator is required. The Small Business Act's requirement that agencies obtain approval of the size standard from the SBA Administrator when using an alternate size standard causes an unintended duplication of effort since Advocacy has already reviewed and approved the alternate size standard used for the purpose of providing regulatory relief to small entities. It is important to note that the alternate size standard approach proposed by Advocacy does not change the requirement that agencies should make their alternate size standards available to the public for notice and comment. Moreover, the change contemplated by Advocacy would not affect size standard determinations for other purposes such as eligibility for SBA programs.

Advocacy requests that the SBA consider adopting alternative measures to the SBA size standard approval process that will serve to provide agencies with an incentive to continue providing small businesses with regulatory flexibilities under the RFA. We recognize that the analysis which an agency performs under the RFA is similar to the review done by SBA's Office of Size Standards when approving an alternate size standard; i.e. the consideration of economic characteristics comprising the structure of an industry, degree of competition, average firm size, distribution of firms by size, as well as the objectives of the agency's proposed rule and the impact on the proposal on different size standard levels. It does not make sense, therefore, to require agencies to duplicate the analysis in order to accommodate size standard regulations and the Regulatory Flexibility Act. Advocacy invites comment on ways the size standard regulation can be improved, under this limited situation, to allow for an appreciation of an agency's rigorous analysis under the RFA as well as the detailed review of the agency's regulatory analysis by SBA's Office of Size Standards.

III. Conclusion

Advocacy is encouraged by SBA's desire to seek input from a broad sector of stakeholders across the country. We urge the SBA to collect sound economic data that will support changes to the existing size standards program and we ask that the proposed rule include a request for comment on streamlining the duplicative regulatory impact analysis requirements that agencies must follow under the Regulatory Flexibility Act and SBA size standard regulations.

We look forward to working with SBA to ensure that the proposed regulation addresses Advocacy's recommendations and enables the public to provide meaningful comments on potential small business impacts.

If you have any questions regarding this letter, please contact Major L. Clark, III in my office at (202) 205-7150.

Sincerely,

/s/

Thomas M. Sullivan
Chief Counsel for Advocacy

/s/

Major L. Clark, III
Assistant Chief Counsel for Procurement