Statement of
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before the

Committee on Small Business
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on

Regulatory Flexibility: Creating Jobs by Reducing Unnecessary Costs to Small Businesses

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Chairman Graves, Ranking Member Velazquez and Members of the Committee.

Thank you for inviting me to participate in this hearing on HR 527, the Regulatory Flexibility Improvements Act of 2011 and HR 585, the Small Business Size Flexibility Act. Millions of businesses are daily impacted by federal government regulations. My tenure in the Reagan Administration as SBA Chief Council for Advocacy and my experience in private law practice confirm that regulatory problems continue to be a major negative factor for small business.

I had the opportunity to participate in the original Congressional consideration of the Regulatory Flexibility Act (RFA), as legislative counsel to the National Federation of Independent Business (NFIB) in 1980. At that time there was broad support for the concept of regulatory reform. Several regulatory agencies with broad portfolios, including the Environmental Protection Agency, Occupational Safety and Health Administration, and the Federal Trade Commission, were zealously making and enforcing rules impacting small business, and small business was increasingly frustrated by these new and often unnecessary or excessively burdensome requirements.

The Regulatory Flexibility Act was, in 1980, one of several proposals which the Congress was considering which would require the government to reform itself, essentially by creating administrative and review screens through which regulations would have to pass. There were many in the Congress, and even in the Carter administration, who believed that getting some regulatory coordination and review outside the immediate agencies was essential to overall rational regulation. There were proposals for creating regulatory review panels and requirements which would apply cost benefit and other criteria.

Thirty years later, there is only one regulatory review statute that impacts all agencies, and that is the Regulatory Flexibility Act. The Congress did give statutory authorities to OMB's Office of Information and Regulatory Affairs, (OIRA), and every recent President has issued Executive Orders attempting to impose regulatory reform standards, which have included linking the review authority of OIRA to SBA Advocacy efforts at enforcement of Regulatory Flexibility.

It bears noting that we now may be in a similar time of concern and focus over regulatory technique. The advances of technology are enabling and challenging all of us to ensure that innovation and entrepreneurship are not stymied by regulation which is unnecessary or too slow. And that is a dilemma – because the regulatory process, especially in fields of science and advancing technology, is already too slow. Indeed the Food and Drug Administration last year initiated a program to advance "regulatory science" to keep up with the accelerated scientific developments in drugs and devices given critical public health needs. It is useful and important that the Congress drive regulators to do their jobs more carefully and more efficiently. With careful statutory changes in the Regulatory Flexibility Act and agencies committed to smart and informed regulation, the two goals are absolutely consistent.

The approach of the Regulatory Flexibility Act was simple and still wise – if agencies take a careful look at the impact their rules have on small business, it may be possible to alter those rules to be less burdensome without compromising the overall regulatory goal. The approach recognizes that agencies have programmatic regulatory responsibilities, and the RFA does not dictate any particular substantive result which would adjust those principles or mandates. However, it does require transparency and analysis – if regulations impact small business, there must be a public description of that impact and disclosure of the analyses. Only with that disclosure can interested businesses, the SBA, the OMB and any other observer offer meaningful comments and work with the agency to reach a more finely tuned less burdensome result.

That is the theory of Regulatory Flexibility. The results have not been so clear. In any regulatory review process, a balance must be struck between substantive regulatory goals and the review process. To be an effective statute for small business and for the jobs and investment they make, the RFA needs to be strengthened to restore the balance originally intended, but not achieved because of Statutory ambiguities and administrative and judicial decisions. With thirty years experience, the Congress should now, through HR 527, address the following core issues:

> Eliminate the ability of agencies to completely avoid addressing any "indirect" effects of regulatory proposals (Section 2 b of HR 527).
>
> Clarify the IRS obligation to analyze the impact of their legislative and interpretive rules, regardless of connection to an existing tax form. (Section 2 f)

Strengthen and clarify requirements for the Initial Regulatory Flexibility Analysis (IRFA) to require more detail and clearer attempts at assessing cumulative impact. (Section 3 a)

Authorize the SBA Chief Counsel to issue rules defining various RFA terms and processes to be used by Federal agencies (Section 4) and speak to such issues in an amicus filing (section 7 d). This would clarify some existing ambiguities as well as signal that courts should show deference to appropriate Chief Counsel views on the RFA.

Make the periodic review of RFA Section 610 more thorough, transparent and publicly available through internet dissemination. (Section 6)

The Regulatory Flexibility Act was a compromise in 1980 between small business interests who desperately wanted the government to somehow get a handle on small business regulation, and "pro-regulatory" interests who were concerned that businesses not have a tool to slow otherwise important health or safety regulation. During my tenure as SBA Chief Counsel for Advocacy, commenting in nearly 400 rulemakings, I observed examples of good intentions and compliance, but also regulatory situations in which agencies inappropriately avoided the RFA requirements. Such issues have been amply described by a series of GAO and Congressional Research Service reports, court decisions attempting to apply unclear statutory language, and less than aggressive compliance by regulatory agencies. Thirty years later the Congress must recalibrate several Regulatory Flexibility Act principles and terms for the reality of today's regulatory dynamics.

Eliminate the ability of agencies to completely avoid addressing any "indirect" effects of regulatory proposals (Section 2 b of HR 527).

There are obvious problems "at the front end," of the regulatory process, at the point at which agencies make a threshold decision as to which of their rules will undergo the analysis required by the Regulatory Flexibility Act. The temptation for mission-driven agencies to define away certain Regulatory Flexibility analytic requirements in order to finalize their rules is often irresistible. For example, the EPA regulates refrigerants under authority it maintains it has through the Clean Air Act to regulate greenhouse gases. EPA has imposed a cap and trade system for manufacturers of refrigerants, in order, over time, to drive down the use of such substances. Although lessening greenhouse gases is a laudable goal, what has resulted, not surprisingly is a cap and no trade system, in which the large firms which have been the historic producers of refrigerants have no incentive to share any product with smaller or new entrant

firms. The indirect result of this regulatory system has been to discourage innovation and competition by small firms in this field. The direct impact, less refrigerant contributing to greenhouse gases, is clear. The indirect impact, a heavy regulatory tax on innovative small business, could be avoided by alternative and more flexible regulatory approaches and analysis.

Clarify the IRS obligation to analyze the impact of their legislative and interpretive rules, regardless of connection to an existing tax form. (Section 2 f)

The Internal Revenue Service plainly considers its mission of administering the tax laws often to be beyond the Regulatory Flexibility Act requirements. Implementation of the laws through regulatory decisions often has a very direct impact on smaller firms. The IRS makes most tax regulation policies without the formal Administrative Procedures Act rulemaking process which normally triggers the Regulatory Flexibility Act. The Service and the Treasury Department have, made many arguments, almost theological in their complexity, as to why the IRS need not regularly perform analyses of the small business impacts of their decisions. Congress clearly has the right and the obligation to clarify the situation, and it attempted to do so in SBREFA. The IRS countered with an interpretation of the coverage of RFA which the Congress should clarify.

But the Congress should consider an additional approach to breaking this IRS regulatory analysis log jam. Anyone who has ever practiced before the IRS on regulatory issues knows that the IRS has, over the years, relied less and less on formal notice and comment regulations, and more on not only interpretive rules but other IRS-specific techniques such as private letter rulings, Technical Advice Memoranda and other means to achieve interpretations of the tax law without full notice and comment. With the complexity of the tax law, this trend may be inevitable, but it is not good for a public which needs to better understand the tax rules and how IRS makes decisions. It is beyond the scope of this legislation to completely address this important issue, but this bill should consider one small step in this direction. I recommend the bill call for establishment of a senior level group, with representatives from not only Treasury and IRS, but also the OMB and the small business community, possibly convened by the Administrative Conference of the US or other neutral party committed to action. The purpose of the group would be to get a grip on what can practically be done to extend IRS regulatory analysis to one or more categories of rules which have a direct impact on small firms, and be able to be

accomplished in our collective lifetimes. IRS should do more under the requirements of the existing RFA. But why not define what more can be done now, even if it involves not all interpretive rules or decisions, focusing on those with the greatest impact on small business.

Strengthen and clarify requirements for the Initial Regulatory Flexibility Analysis (IRFA) to require more detail and clearer attempts at assessing cumulative impact. (Section 3 a).

The current law requires a "succinct" description of the objectives of a rule. Agencies have slavishly followed this adjective. Analyses are inevitably succinct, and rarely attempt to look at a larger picture of cumulative regulatory impacts. In the past 30 years, the methodology and knowledge of measuring impact and alternative means has greatly advanced. Agencies can and often do more internal analysis now. Those analyses and their methodological and source basis should be referenced in the IRFA. The ability of economists and policy analysts to measure and quantify regulatory impact has advanced greatly, as has data availability and other tools which facilitate these analyses. What might have been a good guess years ago can be precisely analyzed today. Further, a specific regulatory action may simply be the latest iteration of a major regulatory scheme. Agencies should not use blinders, assessing narrowly a seemingly minor proposal which has a major impact because of its significance in a larger regulatory plan.

Authorize the SBA Chief Counsel to issue rules defining various RFA terms and processes to be used by Federal agencies (Section 4) and speak to such issues in an amicus filing (section 7 d). This would clarify some existing ambiguities as well as signal that courts should show deference to appropriate Chief Counsel views on the RFA.

The SBA Chief Counsel is not an expert on the substance of OSHA or Clean Air, but is an expert on the procedural requirements of small business regulatory analyses. GAO and other observers have confirmed what is common knowledge, that certain RFA terms are ambiguous or their meaning is subject to debate. If the Chief Counsel had authority to issue regulatory guidance on RFA procedures, that would provide some needed certainty, as well as establish the guidance as entitled in certain situations to judicial deference. The Council on Environmental Quality under the National Environmental Policy Act (NEPA) issues procedural regulations defining the process for performing analysis of the environmental effects of Federal actions. NEPA was very

much in the minds of the RFA sponsors in 1980 as a model for regulatory review. The SBA should be able to play a role for Regulatory Flexibility similar to the role CEQ plays for NEPA.

Make the periodic review of RFA Section 610 more thorough, transparent and publicly available through internet dissemination. (Section 6)

This welcome change might result in better performance under what is probably the least effective section of the RFA. As our government inexorably piles regulation on regulation, despite the best intentions of individual administrations, there must be some mechanism for reviewing cumulative impact and identifying exiting rules which should be rethought or set aside. Indeed, President Obama's Executive Order 13563 is aimed at exactly the same problem, requiring retroactive reviews of existing rules. This principle should be strengthened in statute.

HR 527 includes many other positive reforms of the process, including a further attempt to define the specific grounds under which the chief counsel, a Presidential appointee, may appear in court as an amicus commenting, inevitably negatively, on a regulatory action being taken by another agency led by a Presidential appointee. This is a tough needle to thread, but notwithstanding the traditional reluctance of the Department of Justice to tolerate any other Federal official in court outside their representation, the circumstances in which such an important step can be taken can be more constructively defined.

The need for many of these reforms is apparent after two decades of experience with a very important law. The success of the Regulatory Flexibility Act is a tribute to the Congress and to this Committee's continuing interest in small business regulatory reform, as well as the SBA Chief Counsel for Advocacy's monitoring efforts. It also reflects the effective interest of the OMB Office of Information and Regulatory Affairs and some agency leaders in the process of making good regulatory decisions. The proposed bills update and clarify key points in the RFA and will ensure the balance of regulatory decision is more fair for job-creating small business.