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REGULATORY FLEXIBILITY ACT

Clarification of Key Terms Still Needed

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Mr. Chairman and Members of the Committee:

I am pleased to be here today to discuss the implementation of the Regulatory Flexibility Act of 1980 (RFA), as amended, and the Small Business Regulatory Enforcement Fairness Act of 1996 (SBREFA).[1] As you requested, I will discuss our work on the implementation of these two statutes in recent years.

The RFA requires federal agencies to examine the impact of their proposed and final rules on "small entities" (small businesses, small governmental jurisdictions, and small organizations) and to solicit the ideas and comments of such entities for this purpose. Specifically, whenever agencies are required to publish a notice of proposed rulemaking, the RFA requires agencies to prepare an initial and a final regulatory flexibility analysis. However, the act also states that those analytical requirements do not apply if the head of the agency certifies that the rule will not have a "significant economic impact on a substantial number of small entities," or what I will—for the sake of brevity—term a "significant impact." SBREFA was enacted to strengthen the RFA's protections for small entities, and some of the act's requirements are built on this "significant impact" determination. For example, one provision of SBREFA requires that before publishing a proposed rule that may have a significant impact, the Environmental Protection Agency (EPA) and the Occupational Safety and Health Administration must convene a small business advocacy review panel for the draft rule, and collect the advice and recommendations of representatives of affected small entities about the potential impact of the draft rule.[2]

[1]The RFA is codified at 5 U.S.C. §601-612 and took effect on January 1, 1981.

[2]This provision of SBREFA is codified at 5 U.S.C. §609 and took effect on June 29, 1996.

We have reviewed the implementation of the RFA and SBREFA several times during recent years, with topics ranging from specific provisions in each statute to the overall implementation of the RFA. Although both of these reform initiatives have clearly affected how federal agencies regulate, we believe that their full promise has not been realized. To achieve that promise, Congress may need to clarify what it expects the agencies to do with regard to the statutes' requirements. In particular, Congress may need to clearly delineate—or have some other organization delineate—what is meant by the terms "significant economic impact" and "substantial number of small entities." The RFA does not define what Congress meant by these terms and does not give any entity the authority or responsibility to define them governmentwide. As a result, agencies have had to construct their own definitions, and those definitions vary. Over the past decade, we have recommended several times that Congress provide greater clarity with regard to these terms, but to date Congress has not acted on our recommendations.[3]

The questions that remain unanswered are numerous and varied. For example, does Congress believe that the economic impact of a rule should be measured in terms of compliance costs as a percentage of businesses' annual revenues or the percentage of work hours available to the firms? If so, is 3 percent (or 1 percent) of revenues or work hours an appropriate definition of "significant?" Should agencies take into account the cumulative impact of their rules on small entities, even within a particular program area? Should agencies count the impact of the underlying statutes when determining whether their rules have a significant impact? What should be considered a "rule" for purposes of the requirement in the RFA that the agencies review rules with a significant impact within 10 years of their promulgation? Should agencies review rules that had a significant impact *at the time they were originally published*, or only those that *currently* have that effect? Should agencies conduct regulatory flexibility analyses for rules that have a positive economic impact on small entities, or only for rules with a negative impact?

These questions are not simply matters of administrative conjecture within the agencies. They lie at the heart of the RFA and SBREFA, and the

[3]Last year, legislation was introduced in the Senate (S. 849, the Agency Accountability Act of 2001) that would, in part, require the Chief Counsel for Advocacy of the Small Business Administration to promulgate regulations to define the terms "significant economic impact" and "substantial number of small entities."

answers to the questions can have a substantive effect on the amount of regulatory relief provided through those statutes. Because Congress did not answer these questions when the statutes were enacted, agencies have had to develop their own answers—and those answers differ. If Congress does not like the answers that the agencies have developed, it needs to either amend the underlying statutes and provide what it believes are the correct answers or give some other entity the authority to issue guidance on these issues.

EPA's Use of RFA Discretion

The implications of the current lack of clarity with regard to the term "significant impact" and the discretion that agencies have to define it were clearly illustrated in a report that we prepared for the Senate Committee on Small Business 2 years ago.[4] One part of our report focused on a proposed rule that EPA published in August 1999 that would, upon implementation, lower certain reporting thresholds for lead and lead compounds under the Toxics Release Inventory program from as high as 25,000 pounds to 10 pounds.[5] At the time, EPA said that the total cost of the rule in the first year of implementation would be about $116 million. The agency estimated that approximately 5,600 small businesses would be affected by the rule, and that the first-year costs of the rule for each of these small businesses would be from $5,200 to $7,500. However, EPA certified that the rule would not have a significant impact, and therefore did not trigger certain analytical and procedural requirements in the RFA.

EPA' determination that the proposed lead rule would not have a significant impact on small entities was not unique. Its four major program offices certified about 78 percent of the substantive proposed rules that they published in the 2 ½ years before SBREFA took effect in 1996, but certified 96 percent of the proposed rules published in the 2 ½ years after the act's implementation. In fact, two of the program offices—the Office of Prevention, Pesticides and Toxic Substances and the Office of Solid

[4]U.S. General Accounting Office, *Regulatory Flexibility Act: Implementation in EPA Program Offices and Proposed Lead Rule*, GAO/GGD-00-193 (Washington, D.C.: Sept. 20, 2000).

[5]The proposed lead rule was published at 64 Fed. Reg. 42222 (1999). Toxics Release Inventory reporting is required by section 313 of the Emergency Planning and Community Right-to-Know Act of 1986 (EPCRA) (42 U.S.C. §11023). Reporting is also required under the Pollution Prevention Act of 1990 (42 U.S.C. §13106), which added reporting requirements to EPCRA's reporting requirements in 1991.

Waste—certified *all 47* of their proposed rules in this post-SBREFA period as not having a significant impact. The Office of Air and Radiation certified 97 percent of its proposed rules during this period, and the Office of Water certified 88 percent. EPA officials told us that the increased rate of certification after SBREFA's implementation was caused by a change in the agency's RFA guidance on what constituted a significant impact. Prior to SBREFA, EPA's policy was to prepare a regulatory flexibility analysis for any rule that the agency expected to have any impact on any small entities. The officials said that this guidance was changed because the SBREFA requirement to convene an advocacy review panel for any proposed rule that was not certified made the continuation of the agency's more inclusive RFA policy too costly and impractical. In other words, EPA indicated that SBREFA—the statute that Congress enacted to strengthen the RFA—caused the agency to use the discretion permitted in the RFA and conduct *fewer* regulatory flexibility analyses.

EPA's current guidance on how the RFA should be implemented includes numerical guidelines that establish what appears to be a high threshold for what constitutes a significant impact. Under those guidelines, an EPA rule could theoretically impose $10,000 in compliance costs on 10,000 small businesses, but the guidelines indicate that the agency can presume that the rule does not trigger the requirements of the RFA as long as those costs do not represent at least 1 percent of the affected businesses' annual revenues. The guidance does not take into account the profit margins of the businesses involved or the cumulative impact of the agency's rules on small businesses—even within a particular subject area like the Toxics Release Inventory.

Previous Reports on the RFA and SBREFA

We have issued several other reports in recent years on the implementation of the RFA and SBREFA that, in combination, illustrate both the promise and the problems associated with the statutes. For example, in 1991, we examined the implementation of the RFA with regard to small governments and concluded that each of the four federal agencies that we reviewed had a different interpretation of key RFA provisions.[6] We said that the act allowed agencies to interpret when they believed their proposed regulations affected small government, and recommended that Congress

[6]U.S. General Accounting Office, *Regulatory Flexibility Act: Inherent Weaknesses May Limit Its Usefulness for Small Governments*, GAO/HRD-91-61 (Washington, D.C.: Jan. 11, 1991).

consider amending the RFA to require the Small Business Administration (SBA) to develop criteria regarding whether and how to conduct the required analyses.

In 1994, we examined 12 years of annual reports prepared by the SBA Chief Counsel for Advocacy and said the reports indicated variable compliance with the RFA—a conclusion that the Office of Advocacy also reached in its 20-year report on the RFA.[7] SBA repeatedly characterized some agencies as satisfying the act's requirements, but other agencies were consistently viewed as recalcitrant. Other agencies' performance reportedly varied over time or varied by subagency. We said that one reason for agencies' lack of compliance with the RFA's requirements was that the act did not expressly authorize SBA to interpret key provisions in the statute and did not require SBA to develop criteria for agencies to follow in reviewing their rules. We said that if Congress wanted to strengthen the implementation of the RFA, it should consider amending the act to (1) provide SBA with authority and responsibility to interpret the RFA's provisions and (2) require SBA, in consultation with the Office of Management and Budget (OMB), to develop criteria as to whether and how federal agencies should conduct RFA analyses.

In our 1998 report on the implementation of the small business advocacy review panel requirements in SBREFA, we said that the lack of clarity regarding whether EPA should have convened panels for two of its proposed rules was traceable to the lack of agreed-upon governmentwide criteria as to whether a rule has a significant impact.[8] Nevertheless, we said that the panels that had been convened were generally well received by both the agencies and the small business representatives. We also said that if Congress wished to clarify and strengthen the implementation of the RFA and SBREFA, it should consider (1) providing SBA or another entity with clearer authority and responsibility to interpret the RFA's provisions and (2) requiring SBA or some other entity to develop criteria defining a "significant economic impact on a substantial number of small entities."

[7]U.S. General Accounting Office, *Regulatory Flexibility Act: Status of Agencies' Compliance*, GAO/GGD-94-105 (Washington, D.C.: Apr. 27, 1994). The Office of Advocacy's report is entitled *20 Years of the Regulatory Flexibility Act: Rulemaking in a Dynamic Economy* (Washington, D.C.: 2000).

[8]U.S. General Accounting Office, *Regulatory Reform: Implementation of the Small Business Advocacy Review Panel Requirements*, GAO/GGD-98-36 (Washington, D.C.: Mar. 18, 1998).

In 1999, we noted a similar lack of clarity regarding the RFA's requirement that agencies review their existing rules that have a significant impact within 10 years of their promulgation.[9] We said that if Congress is concerned that this section of the RFA has been subject to varying interpretations, it may wish to clarify those provisions. We also recommended that OMB take certain actions to improve the administration of these review requirements, some of which have been implemented.

Last year we issued two reports on the implementation of SBREFA. One report examined section 223 of the act, which required federal agencies to establish a policy for the reduction and/or waiver of civil penalties on small entities.[10] All of the agencies' penalty relief policies that we reviewed were within the discretion that Congress provided, but the policies varied considerably. Some of the policies covered only a portion of the agencies' civil penalty enforcement actions, and some provided small entities with no greater penalty relief than large entities. The agencies also varied in how key terms such as "small entities" and "penalty reduction" were defined. We said that if Congress wanted to strengthen section 223 of SBREFA it should amend the act to require that agencies' policies cover all of the agencies civil penalty enforcement actions and provide small entities with more penalty relief than other similarly situated entities. Also, to facilitate congressional oversight, we suggested that Congress require agencies to maintain data on their civil penalty relief efforts.[11]

The other report that we issued on SBREFA last year examined the requirement in section 212 that agencies publish small entity compliance guides for any rule that requires a final regulatory flexibility analysis under the RFA.[12] We concluded that section 212 did not have much of an impact on the agencies that we examined, and its implementation also varied across and sometimes within the agencies. Some of the section's

[9]U.S. General Accounting Office, *Regulatory Flexibility Act: Agencies' Interpretations of Review Requirements Vary*, GAO/GGD-99-55 (Washington, D.C.: Apr. 2, 1999).

[10]U.S. General Accounting Office, *Regulatory Reform: Implementation of Selected Agencies' Civil Penalty Relief Policies for Small Entities*, GAO-01-280 (Washington, D.C.: Feb. 20, 2001).

[11]Last year, legislation was introduced in the Senate (S. 1271, the Small Business Paperwork Relief Act of 2001) that would, in part, require agencies to report information on civil penalty relief to certain congressional committees.

[12]*Regulatory Reform: Compliance Guide Requirement Has Had Little Effect on Agency Practices*, GAO-02-172 (Washington, D.C.: Dec. 28, 2001).

ineffectiveness and inconsistency is traceable to the definitional problems in the RFA that I discussed previously. Therefore, if an agency concluded that a rule imposing thousands of dollars of costs on thousands of small entities did not trigger the requirements of the RFA, section 212 did not require the agency to prepare a compliance guide. Other problems were traceable to the discretion provided in section 212 itself. Under the statute, agencies can designate a previously published document as its small entity compliance guide, or develop and publish a guide with no input from small entities years after the rule takes effect. We again recommended that Congress take action to clarify what constitutes a "significant economic impact" and a "substantial number of small entities," and also suggested changes to section 212 to make its implementation more consistent and effective.

Two years ago we convened a meeting at GAO on the rule review provision of the RFA, focusing on why the required reviews were not being conducted. Attending that meeting were representatives from 12 agencies that appeared to issue rules with an impact on small entities, representatives from relevant oversight organizations (e.g., OMB and SBA's Office of Advocacy), and congressional staff from the House and Senate committees on small business. The meeting revealed significant differences of opinion regarding key terms in the statute. For example, some agencies did not consider their rules to have a significant impact because they believed the underlying statutes, not the agency-developed regulations, caused the effect on small entities. There was also confusion regarding whether the agencies were supposed to review rules that *had* a significant impact on small entities at the time the rules were first published in the *Federal Register* or those that *currently have* such an impact. It was not even clear what should be considered a "rule" under the RFA's rule review requirements—the entire section of the *Code of Federal Regulations* that was affected by the rule, or just the part of the existing rule that was being amended. By the end of the meeting it was clear that, as one congressional staff member said, "determining compliance with (the RFA) is less obvious than we believed before."

Mr. Chairman, this concludes my prepared statement. I would be happy to respond to any questions.

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