The Voice of Small Business

Charles S. Owens, State Director
National Federation of Independent Business
115 W. Allegan / Suite 310
Lansing, MI 48933
(517) 485-3409

Testimony in Support of House Bills 4240, 4326, 4573 and 4500 Regulatory Reform Proposal Before the House Regulatory Reform Commerce Wednesday, May 18, 2011

My name is Charlie Owens and I am the State Director for the National Federation of Independent Business, an advocate for Michigan small businesses owners and we are here today to support the Regulatory Reform package of bills: HB 4240, 4326, 4573 and 4500.

As we move forward on the important mission of creating more and better jobs for the citizens of Michigan, we must consider the impact of our regulatory policy on the overall business climate for our state.

The business climate of a state is not a single issue or item but an overall blend of important elements that, together, determine whether there is an environment that encourages economic development, business growth and expansion and - as a consequence - job creation. Those elements are Tax Climate, Labor Climate, Legal Climate, Financial Climate and Regulatory Climate.

The bills under consideration by the Committee today deal with the Regulatory Climate element of our overall business climate. Small business is particularly impacted by the cost of compliance with regulations. According to the 2010 Small Business Administration report "The Impact of Regulatory Costs on Small Firms":

"In the face of yet higher costs of federal regulations, the research shows that small businesses continue to bear a disproportionate share of the federal regulatory burden… More specifically, the total cost of federal regulations has increased to $1.75 trillion, while the updated cost per employee for firms with fewer than 20 employees is now $10,585 (a 36 percent difference between the costs incurred by small firms when compared with their larger counterparts)."[1]

While this report references federal regulations, the inference to state regulations is no less relevant. We make it a point to call the Committee's attention to this report and its' conclusions because it

also an accepted fact that small business in Michigan has been, and will continue to be, the primary source of new job creation for our state.

Therefore, it is fitting these bills attempt to address that disproportionate cost by making much needed changes to Michigan's Administrative Procedures Act to allow more accountability and flexibility for small business.

The important changes included in these bills are:

- Restricting the promulgation of rules to be no stricter than an existing federal rule unless allowed by statute.
- Limiting the ability of agencies to create "rules" via internal memorandums, guidelines, or standards that avoid both the legislative and administrative process.
- Requiring state agencies to determine the impact of rules on small business and make appropriate accommodations including exemptions.
- Clarifying the role of the ORR (Office of Regulatory Reinvention) in the rule making process.
- Allowing for a cause of action for parties that are aggrieved by agency abuse of the rule making process.
- Requiring a review as to the need and effectiveness of existing rules.

These changes will do much to move Michigan's business climate forward and position our state competitively for many years to come.

We ask the Committee to support these bills.

Attachments:

[1] 2010 SBA Report - "The Impact of Regulatory Costs on Small Firms" can be downloaded at: www.sba.gov/advo/research/rs371tot.pdf

SBA Office of Advocacy
www.sba.gov/advo

Small Business Research Summary

Advocacy: the voice of small business in government

September 2010 No. 371

The Impact of Regulatory Costs on Small Firms

by Nicole V. Crain and W. Mark Crain, Lafayette College, Easton, PA, 18042. 2010
81 pages. Under contract SBAHQ-08-M-0466.

Regulations are needed to provide the rules and structure for societies to properly function. This research, while mindful of this important fact, focuses on the costs imposed by federal regulations; it thus updates and verifies the finding of disproportionality in the burden imposed by federal regulations on small business. Previous research by the Office of Advocacy has established that regulatory and paperwork costs were found to be more onerous for small firms than larger firms.

Overall Findings

In the face of yet higher costs of federal regulations, the research shows that small businesses continue to bear a disproportionate share of the federal regulatory burden. The findings are consistent with those in Hopkins (1995), Crain and Hopkins (2001), and Crain (2005).

The research finds that the total costs of federal regulations have further increased from the level established in the 2005 study, as have the costs per employee. More specifically, the total cost of federal regulations has increased to $1.75 trillion, while the updated cost per employee for firms with fewer than 20 employees is now $10,585 (a 36 percent difference between the costs incurred by small firms when compared with their larger counterparts).

A caveat is necessary at this point. This current iteration of the study uses an index for the calculation of the economic regulations estimate that is wider and more encompassing than that previously used. While different from the previous index, it provides the study with a fuller estimate, thus partially remedying previous underestimates. More specifically, the Regulatory Quality Index from the World Bank used in this study has more observations and also has continuous data from 1998 to 2008. The OECD index used in the previous study (2005) was more limited in scope and had observations every five years. A significant increase in the new estimate is due to the new, more encompassing methodology. To obtain an idea of how much of the increase in the estimate of economic regulations was due to the new methodology, the authors ran the new index on the 2005 data, in effect re-estimating the 2005 model using the new index. The economic regulations increased from $727 billion to $1.172 trillion, a $445 billion increase.

Annual Cost of Federal Regulations by Firm Size

Type of Regulation	Cost per Employee for All Firms	Cost per Employee for Firms with:		
		Fewer than 20 Employees	20–499 Employees	500 or More Employees
All Federal Regulation	$8,086	$10,585	$7,454	$7,755
Economic	5,153	4,120	4,750	5,835
Environmental	1,523	4,101	1,294	883
Tax Compliance	800	1,584	760	517
Occupational Safety and Health and Homeland Security	610	781	650	520

Source: *The Impact of Regulatory Costs on Small Firms,* by Nicole Crain and Mark Crain, 2010. U.S. Small Business Administration, Office of Advocacy (**www.sba.gov/advo/research/rs371tot.pdf**).

This report was developed under a contract with the Small Business Administration, Office of Advocacy, and contains information and analysis that was reviewed and edited by officials of the Office of Advocacy. However, the final conclusions of the report do not necessarily reflect the views of the Office of Advocacy.

While the true costs of federal regulation have yet to be calculated, Advocacy research has repeatedly and consistently attempted to uncover an estimate of the burden in general, and the impact it has on small businesses, in particular. This current iteration of the research advances the scope, and attempts to make a dent in previous underestimates.

Highlights

- Environmental regulations appear to be the main cost drivers in determining the severity of the disproportionate impact on small firms. Compliance with environmental regulations costs 364 percent more in small firms than in large firms. The cost of tax compliance is 206 percent higher in small firms than the cost in large firms.
- The disproportionality of the burden borne by small firms, identified in previous Advocacy studies, is further validated in this instance. On a per-employee basis, it costs about $2,830 more for small firms to comply than their larger counterparts. This straight difference translates into 36 percent. When compared with the 2005 study reflecting the new methodology, the disproportionality rate is lower. The current study basically finds that while there still is disproportionality borne by small business, there is slightly less disproportionality in the underlying distribution.
- This report details the distribution of regulatory costs for five major sectors of the U.S. economy: manufacturing, trade (wholesale and retail), services, health care, and other (a residual category containing all enterprises not included in the other four). The sector-specific findings reveal that the disproportionate cost burden on small firms is particularly stark for the manufacturing sector. The "other" category also deserves mention here as the disproportionality between small and large is stark. The compliance cost per employee for small manufacturers is more than double the compliance cost for medium-sized and large firms (110 percent and 125 percent, respectively). In the service sector, regulatory costs differ little between small businesses and larger firms. The distribution of the regulatory burden across firm sizes in the other major business sectors falls somewhere between these two cases.

Scope and Methodology

The report divides federal regulations into four categories: economic, environmental, tax compliance, OSHHS (occupational safety and health, and homeland security). The estimate of economic regulations is obtained by regressing the Regulatory Quality Index on gross domestic product per capita, and includes labor market economic regulations that were included in the workplace regulation column in previous reports. Second, gaps in the baseline are filled with Office of Management and Budget (OMB) estimates. The costs of workplace regulations are based on the updated estimates from the study by Joseph Johnson (2005). Homeland security cost estimates are based on OMB reports, as are environmental regulations estimates. Tax compliance costs, finally, are based on the 2005 report from the Tax Foundation. The allocation of costs across employment classes was made possible by use of Census data published by the Office of Advocacy.

This report was peer reviewed consistent with the Office of Advocacy's data quality guidelines. More information on this process can be obtained by contacting the director of economic research at **advocacy@sba.gov** or (202) 205-6533.

Ordering Information

Research from the Office of Advocacy is online at **www.sba.gov/advo/research.** The url of the report is **www.sba.gov/advo/research/rs371tot.pdf.** Copies are available for purchase from:

National Technical Information Service
5285 Port Royal Road
Springfield, VA 22161
(800) 553-6847 or (703) 605-6000
TDD: (703) 487-4639
www.ntis.gov
Order number: Pending

For email delivery of Advocacy's newsletter, press, regulatory news, and research, visit **http://web.sba.gov/list**. For RSS feeds, visit **www.sba.gov/advo/rsslibrary.html.**

Hopkins, Thomas D., 1995. *Profiles of Regulatory Costs.* U.S. Small Business Administration, Office of Advocacy. **www.sba.gov/advo/research/rs1995hoptot.pdf.**

Crain, W. Mark, and Thomas D. Hopkins, 2001. *The Impact of Regulatory Costs on Small Firms.* U.S. Small Business Administration, Office of Advocacy, **www.sba.gov/advo/research/rs207 tot.pdf.**

W. Mark Crain, 2005. *The Impact of Regulatory Costs on Small Firms.* U.S. Small Business Administration, Office of Advocacy, **www.sba.gov/advo/research/rs264tot.pdf.**

Johnson, Joseph M., 2005. "A Review and Synthesis of the Cost of Workplace Regulations," in *Cross-Border Human Resources, Labor and Employment Issues.*