

Date of Hearing: April 21, 2015

ASSEMBLY COMMITTEE ON JOBS, ECONOMIC DEVELOPMENT, AND THE ECONOMY

Eduardo Garcia, Chair

AB 866 (Eduardo Garcia) – As Amended April 13, 2015

SUBJECT: Economic development: small business

SUMMARY: Expands the duties of the Small Business Advocate to include assisting state rulemaking agencies in identifying the aggregate number and size of business which may be affected by a proposed new or amended regulation. To the extent information is available, the SBA will also identify related small business stakeholder groups which the rulemaking agency may include when disseminating public information about the proposed new rule or amendment.

The bill also requires a state agency that develops a small business compliance guide in partnership with federal agency, under the federal Small Business Regulatory Fairness Act of 1996 (Public Law 104-121), to notify the Office of the Small Business Advocate within 45 days after the guide becomes available to the public. The notice is also required to include information on how a small business or nonprofit organization can obtain a copy of the guide.

EXISTING LAW:

- 1) Finds and declares that it is in the public interest to aid, counsel, assist, and protect the interests of small business concerns in order to maintain a healthy state economy.
- 2) Finds and declares that the complexity and lack of clarity in many regulations put small businesses, which do not have the resources to hire experts to assist them, at a distinct disadvantage.
- 3) Establishes the Governor's Office of Business and Economic Development (GO-Biz) to serve the Governor as the lead entity for economic strategy and the marketing of California on issues relating to business development, private sector investment, and economic growth. In meeting its mission, GO-Biz is authorized to make recommendations to the Governor and the Legislature regarding new state policies, programs, and actions, or amendments to existing programs, in order to advance statewide economic goals, respond to emerging economic problems, and to ensure that all state policies and programs conform to the adopted state economic and business development goals.
- 4) Establishes the Office of the Small Business Advocate to serve, among other things, as the principal advocate in the state on behalf of small businesses, including, but not limited to, advisory participation in the consideration of all legislation and administrative regulations that affect small businesses.
- 5) Establishes basic minimum procedural requirements for the adoption, amendment, or repeal of administrative regulations, including assessing the potential adverse impact of an action on California businesses and individuals with the purpose of avoiding the imposition of unreasonable and unnecessary regulations, reporting, recordkeeping, or compliance requirements. Among other requirements, an agency is required to:
 - a) Base decisions on adequate information;
 - b) Consider the impact of a proposed rule on an industry's ability to compete with businesses in other states; and

- c) Assess its impact on the creation or elimination of jobs and new and expanding businesses.

FISCAL EFFECT: Unknown

POLICY ISSUE FRAME:

Although the state has a vigorous public process that is designed to allow the rulemaking agency to fully consider the comments, suggestions, and economic impacts of proposed regulations on all business – especially small businesses – state agencies are often unable to clearly identify which types of businesses are potentially affected by a proposed rule and assess the cost and complexity of the proposed implementation model on varying size businesses. An intrinsic conflict to California's rulemaking process is that those businesses that may be most affected have the least ability to monitor the broad range of state rulemaking entities, recommend appropriate alternative implementation models or engage meaningfully in the often complex and highly technical rulemaking proceedings.

Given that nearly 3 million firms in California have no employees and 90% of firms with employees have less than 20, having implementation methods that are appropriate for small businesses in terms of time, money, and expertise are important state's economic growth.

Without an easy to access and respected source for their own data or a realistic method for small businesses to participate in the regulatory process, it is difficult for state agencies to adopt rules that are considerate of needs of small businesses while, still meeting the intended policy standards.

This measure proposes that the Small Business Advocate assist state agencies in their rule making process by providing reliable information on the number and size of businesses within the industry sector which could be impacted by the regulation. Further, the Small Business Advocate would assist the rulemaking agency in identifying key small business stakeholder groups, which should be included in the public dissemination of information.

The Comment section of the analysis explores these issues more fully and includes information on California small businesses, studies on the cost of regulations, legislative attempts to reform state rulemaking practices, small business advocacy, and summary of prior legislation.

COMMENTS:

- 1) **California's Small Business Economy:** Small businesses form the core of California's \$2.2 trillion economy. Research shows that net new job creation is strongest among businesses with less than 20 employees, that small businesses have historically led the state's local and regional economies out of recessions, and that these businesses are essential to the state's global competitiveness by meeting niche industry needs.

Businesses with no employees make up the single largest component of businesses in California, 2.9 million out of an estimated 3.6 million firms in 2012, representing over \$149 billion in revenues with the highest number of businesses in the professional, scientific, and technical services industry sector. As these non-employer businesses grow, they continue to serve as an important component of California's dynamic economy.

Excluding non-employer firms, businesses with less than 20 employees comprise nearly 90% of all businesses and employ approximately 18% of all workers. Businesses with less than 100 employees

represent 97% of all businesses and employ 36% of the workforce. These non-employer and small employer firms create jobs, generate taxes, and revitalize communities.

2011 Business Profile By Size (excludes non-employer firms)						
Area Description	Employment Size	Number of Firms	Percent of Firms	Employees	Percent of Jobs	Annual Payroll (\$1,000)
United States	Total	5,684,424		113,425,965		\$5,164,897,905
California	Total	689,568	12% of U.S. Firms	12,698,427	11% of all U.S. Jobs	\$663,570,657
United States	0-4	3,532,058	62% of U.S. Firms	5,857,662	5% of U.S. Jobs	\$230,422,086
California	0-4	429,139	62% of CA Firms	702,508	5.5% of CA Jobs	\$35,472,447
United States	<20	5,104,014	89.7% of U.S. Firms	20,250,874	17.8% of U.S. Jobs	\$732,759,369
California	<20	614,538	89.1% of CA Firms	2,386,296	18.7% of CA Jobs	\$99,417,066
United States	0-99	5,585,510	98.2% of U.S. Firms	39,130,875	34% of U.S. Jobs	1,478,844,420
California	0-99	672,360	97% of CA Firms	4,587,628	36.1% of CA Jobs	194,611,832
United States	<500	5,666,753	99.6% of U.S. Firms	54,998,312	48.4% of U.S. Jobs	\$2,169,353,973
California	<500	683,999	99.1% of CA Firms	6,331,871	49.8% of CA Jobs	\$280,857,823
United States	500+	17,671	0.3% of U.S. Firms	58,427,653	51.5% of U.S. Jobs	\$2,995,543,932
California	500+	5,569	0.8% of CA Firms	6,366,556	50.1% of CA Jobs	\$382,712,834

Source: U.S. Census <http://www.census.gov/econ/subs/index.html>

Reflective of their important role, the JEDE Committee Members regularly hear testimony regarding the challenges small businesses face in meeting the implementation requirements of state, local, and federal regulations. While opponents of regulatory reform accuse small businesses of trying to avert their responsibilities, businesses that have testified before the Committee have continually stated that their goal is to achieve a regulatory environment that encourages small business development, while still maintaining public health and safety standards. Consistent with these recommendations, AB 866 does not call for the lowering of any regulatory standard, and instead, proposes an expert source for small business data and stakeholder groups within the existing regulatory framework.

- 2) **Cost of Regulations on Business:** There are two major sources of data on the cost of regulatory compliance on businesses, the federal SBA and the Office of the Small Business Advocate (OSBA). For the last 10 years, the federal SBA has conducted a peer reviewed study that analyzes the cost of federal government regulations on different size businesses. This research shows that small

businesses continue to bear a disproportionate share of the federal regulatory burden. On a per employee basis, it costs about \$2,400, or 45% more, for small firms to comply with federal regulations than their larger counterparts.

The first study on the impact of California regulations on small businesses was released by the OSBA in 2009. This first in-the-nation study found that the total cost of regulations to small businesses averaged about \$134,000 per business in 2007. Of course, no one would advocate that there should be no regulations in the state. The report, however, importantly identifies that the cost of regulations can provide a significant cost to the everyday operations of California businesses and should therefore be a consideration among the state's economic development policies.

Regulatory costs are driven by a number of factors including multiple definitions of small business in state and federal law, the lack of e-commerce solutions to address outdated paperwork requirements, procurement requirements that favor larger size bidders, and the lack of technical assistance to alleviate such obstacles that inhibit small business success.

- 3) **Different Approaches to Regulatory Reform:** In general, the Legislature's engagement on regulatory reforms has taken two basic approaches. One set of policies have addressed specific regulatory challenges on a case-by-case basis. The other approach makes systemic change to the way in which rules are adopted, often adding a supplemental more targeted review pre- or post-adoption. Recommendations for systemic change have included:
- a) ***Dynamic Fiscal Analysis in Appropriations Committee:*** These bills required an analysis of bills before the Legislature on their impact on business and the economy. Currently, the Legislature's fiscal committee reviews focus on the bill's direct impact on state funds, and most specifically on the General Fund. The fiscal committee's analysis is not intended to include legislations' potential economic impact on the state.
 - b) ***Substantive Administrative Review:*** These bills shifted the review of the Office of Administrative Law from a procedural review of the regulation package to a substantive review of its impact on business and the economy, including the sufficiency of the assessment of alternatives. Alternatively, legislation has suggested that another state entity, such as the State Auditor or Legislative Analyst's Office, could be designated to undertake an expanded review of proposed regulations.
 - c) ***Enhanced Analysis of Alternatives:*** These bills required a more meaningful consideration of alternative implementation models, which could lower costs or reduce the implementation burden on small businesses.
 - d) ***Post Implementation Analysis:*** These bills required a review of a regulation's impact five-years after its implementation. Alternatively, legislation has been suggested that all regulations have a sunset date, which would allow for full review once the actual impacts could be identified.

Until now, the first approach has been the most successful, although by its nature it has had very limited overall impact on California's regulatory business climate. Due to their potential implementation costs, a majority of the bills advancing the systemic approach to regulatory reform have failed to move from the fiscal committees - as illustrated in the comment on related legislation.

The most significant systemic change in recent years was approved in SB 617 (Calderon), Chapter 496, Statutes of 2011, which required an enhanced economic impact analysis for regulations anticipated to have an impact of \$50 million or more. The SB 617 process follows the federal

regulatory model (described below), however, it should be noted that the state process is silent as to the assessment of costs based on size of business.

The Legislature heard several bills to refine the SB 617 process in 2013-14 session including AB 2723 (Medina), which would have required rulemaking entities to consider the specific impact of major regulations on sole proprietorships, and AB 1711 (Cooley) which moved up the economic impact assessment to the initial statement of reasons for all regulations. Ultimately, the Governor signed AB 1711 (Cooley), Chapter 779, Statutes of 2014 and vetoed AB 2723 (veto message below).

- 5) **Federal and State Small Business Advocacy:** In 1976, the federal government established the Federal Office of Advocacy (FOA) within the Small Business Administration for the purpose of protecting and effectively representing the nation's small businesses within the federal government's legislative and rule-making processes. A few years later, the Regulatory Flexibility Act of 1980 was enacted, which provided a specific process for assessing and mitigating the potential impact of federal regulations on small businesses. The federal process, which has been updated over the years, includes the annual publication of a regulatory agenda, an initial and final regulatory flexibility analysis, a mandatory periodic review of adopted rules, and direction for a possible judicial review of regulations. The FOA serves as the "watchdog" agency for the Federal Regulatory Flexibility Act.

In carrying out its duties, the FOA regularly reviews federal regulations and makes recommendations on how to reduce the burden on small firms and maximize small business participation within the federal government. In 2013, the FOA issued 19 letters to federal agencies requesting alternative implementation methods and encouraging better technical review of proposed regulations.

Another FOA activity is the convening of issue-specific Small Business Advocacy Review Panels. Utilizing the FOA as a facilitator has proven to be particularly useful in developing more detailed comments and making specific and technical recommendations to assist the rulemaking entity in modifying a rule to lessen its impact on small businesses, without reducing its policy objective.

Adopted over a series of years, California law currently has several but not all of the key elements of the federal model. As an example, existing state law sets forth an extensive process for the development and adoption of regulations, including requiring the identification of potential adverse impacts on small businesses and individuals, as well as the consideration of alternative.

The process, however, places the primary responsibility for developing alternative implementation methods on the impacted parties. As noted above, small businesses do not have the capacity in terms of time nor expertise to follow every rulemaking process that the state is undertaking in a given year, nor the expertise to offer alternatives.

While California has an Office of the Small Business Advocate, the state advocate does not currently have the staff to formally comment on pending state regulations. On a case-by-case basis, the Governor's Office of Business and Economic Development has been able to engage with other agencies on current and proposed regulatory proposals through its Office of Permit Assistance, but again, state statutory direction is permissive and not mandatory.

AB 866 addresses these issues by leveraging the expertise of the Small Business Advocate in providing good information on the size of businesses affected, which should impact the initial development of the implementation method by the rulemaking agency.

- 6) **Impact on Business Varies by Size:** Small businesses play differing roles within industry sectors. The bullets below show the top three industry sectors for California small businesses (employing 0-99 employees) by number of businesses:
- a) The real estate and rental and leasing sector had the highest percentage of small businesses in California, consisting of 98.1% of the firms in the sector.
 - b) The health care and social assistance sector had the second highest percentage of small businesses in California, consisting of 97.8% of the firms in the sector.
 - c) The professional, scientific, and technical services sector had the third highest percentage of small businesses in California, consisting of 97.7% of the firms in the sector.

Based on the number of employees, the top three industry sectors for California small businesses (employing 0-99 employees) are:

- a) The accommodation and food services sector, which had the highest number of workers employed by small businesses in California, with a total of 676,837 employees, consisting of 48% of employment in the sector.
- b) The health care and social assistance sector, which had the second highest number of workers employed by small businesses in California, with a total of 574,968 employees, consisting of 33% of employment in the sector.
- c) The professional, scientific, and technical services, which had the third highest number of workers employed by small businesses in California, with a total of 488,362 employees, consisting of 43% of employment in the sector.

Implementation of AB 866 would assist state rule making agencies in identifying more clearly the size of businesses impacted by a potential regulation.

- 7) **Related Legislation:** Below is a list of bills from the current and prior sessions.
- a) Current Session
 - i) **AB 19 (Chang) Review of State Regulations:** This bill requires the Governor's Office of Business and Economic Development, under the direction of the Small Business Advocate, to review all regulations affecting small businesses adopted on or after January 1, 2016, in order to determine whether the regulations need to be amended in order to become more effective, less burdensome, or to decrease the cost impact to affected sectors. Status: Scheduled to be heard on April 21, 2015, in the Assembly Committee on Jobs, Economic Development, and the Economy.
 - ii) **AB 419 (Kim) Compiling of State Regulations:** This bill requires the Governor's Office of Business and Economic Development (GO-Biz) to annually compile all regulations adopted by the state that affect small businesses and report this information to the Legislature, as specified. Status: Scheduled to be heard on April 21, 2015, in the Assembly Committee on Jobs, Economic Development, and the Economy.
 - iii) **AB 582 (Calderon) Professionals in Public Services Act of 2015:** This bill establishes the Professionals in Public Service Program, under the administrative oversight of the Board of Equalization (BOE), for the purpose of utilizing the expertise of private sector professionals to help make BOE practices more accessible to small businesses. Status: Scheduled to be heard

on April 21, 2015, in the Assembly Committee on Jobs, Economic Development and the Economy.

- iv) **AB 1286 (Mayes) Regulatory Review Council:** This bill establishes the California Regulatory Reform Council (Council) for the purpose of analyzing the holistic impact of all levels of state and local regulations on specific industries operating within the state. The Council's recommendations may be made to the Governor and the Legislature, as appropriate. Status: Scheduled to be heard on April 21, 2015, in the Assembly Committee on Jobs, Economic Development, and the Economy.

b) Prior Sessions

- i) **AB 393 (Cooley) GO-Biz Website:** This bill requires the Director of GO-Biz to ensure that the GO-Biz website contains information on the fee requirements and fee schedules of state agencies. Status: Signed by the Governor, Chapter 124, Statutes of 2013.
- ii) **AB 1098 (Quirk-Silva) Small Business Regulation Report:** As passed by JEDE, this bill would have directed the Office of the Small Business Advocate within GO-Biz to commission a study of the costs of state regulations on small businesses every five years. Amendments taken in the Senate deleted the content of the bill and added language relating to legal documents provided over the internet with Assemblymember Gray as the author. Status: Died in the Senate Committee on Rules, 2014.
- iii) **AB 1400 (Assembly Committee on Jobs, Economic Development, and the Economy) Export Document Certificates:** This bill modifies the state's Export Document Program to accept requests electronically, expedite approval of existing labels, and extend the term of the export labels from 180 days to 365 days, in order to alleviate backlog of exports of food, drug, and medical devices. Status: Signed by the Governor, Chapter 539, Statutes of 2013.
- iv) **AB 1711 (Cooley) Economic Impact Assessment:** This bill requires an economic impact assessment to be included in the Initial Statement of Reasons that a state agency submits to the Office of Administrative Law when adopting, amending, or repealing a non-major regulation. Status: Signed by the Governor, Chapter 779, Statutes of 2014.
- v) **AB 2723 (Medina) Small Businesses and Major Regulations:** This bill would have added statutory protections to ensure that the costs of major regulations on the state's smallest size businesses are considered when state agencies undertake their economic impact assessment for major regulations. Status: Vetoed by the Governor, 2014. The veto message reads: " This bill would require the economic analysis for major regulations to include a separate assessment of the impact on sole proprietorships and small businesses. I signed legislation in 2011 to require a comprehensive economic analysis of proposed major regulations. The analysis must assess whether, and to what extent, the proposed regulations will affect all California jobs and businesses. Agencies must also identify alternatives that would lessen any adverse impact on small businesses. I am not convinced that an additional layer of specificity based solely on the legal structure of a business would add value to the comprehensive economic analysis already required."
- vi) **SB 176 (Galgiani) Outreach on Administrative Procedures:** This bill would have amended the Administrative Procedure Act by requiring state agencies to make a reasonable effort to outreach and provide notice to affected entities when developing regulations. Statutes: Held on the Suspense File of the Assembly Committee on Appropriations, 2013.

- i) ***SB 560 (Wright) Small Business Regulations:*** This bill would have made a number of reforms to help small businesses grow encouraging more realistic regulations and a real assessment of the actual costs of regulations to the business community. The bill would have: (1) authorized a state agency to consult with “parties who would be subject to the proposed regulations” rather than “interested persons.” It also would have required the agency to notify in writing the Office of Small Business Advocate and the Department of Finance (DOF) if the agency does not, or is unable to, consult with parties subject to the regulation and reasons for not consulting the impacted businesses; (2) revised the economic impact assessment to include a small business economic impact statement as specified; (3) required the notice of proposed adoption, amendment, or repeal of a regulation to also include the small business impact statement and removes the requirement for an agency to make a specified statement in the notice of proposed adoption, amendment, or repeal of a regulation if the agency is not aware of any cost impacts that a representative private person or business would incur in compliance with the regulation, and instead required the agency to include a statement describing how a private person or business could comply with the proposed regulation without incurring a cost; (4) required Office of Administrative Law to also return any regulation to the adopting agency if the adopting agency has not provided the above cost estimate and small business economic statement; and (5) added restrictions for regulations relating to a new or emerging technology, as specified. Status: Held in the Senate Committee on Environmental Quality, 2012.
- vii) ***SB 617 (Calderon) State Government and Financial and Administrative Accountability:*** This bill revises the state Administrative Procedure Act to require each state agency adopting a major regulation to prepare an economic impact analysis and requires state agencies to implement ongoing monitoring of internal auditing and financial controls and other best practices in financial accounting. Status: Signed by the Governor, Chapter 496, Statutes of 2011.
- viii) ***SB 981 (Huff) Review of Prior Regulations:*** This bill would have required each state agency to review each regulation adopted prior to January 1, 2014, and to develop a report to the Legislature containing prescribed information. Among other information, the report would have included the regulations purpose, identification of impacted sectors, direct costs by sector, and an assessment as to whether the regulation needs updating. Status: Died in Senate Committee on Governmental Organization, 2014.
- ix) ***SB 1099 (Wright) Streamline Implementation of Regulations:*** This bill requires new regulations to become effective on one of four dates in any given year. This limitation is designed to create a regulatory environment that is more predictable. In addition, the bill requires regulations to be posted on the internet website in an easily identifiable location for a minimum of six months. Status: Signed by the Governor, Chapter 295, Statutes of 2012.

REGISTERED SUPPORT / OPPOSITION:

Support

Building Owners and Managers Association
 California Asian Pacific Chamber of Commerce
 California Business Properties Association
 California Chamber of Commerce
 California Manufacturers and Technology Association
 Industrial Environmental Association
 International Council of Shopping Centers

NAIOP – Commercial Real Estate Development Association
National Federation of Independent Business
USANA Health Sciences

Opposition

None received

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