

Date of Hearing: April 20, 2010

ASSEMBLY COMMITTEE ON JOBS, ECONOMIC DEVELOPMENT AND THE
ECONOMY

V. Manuel Perez, Chair

AB 2692 (Tran) – As Introduced: February 19, 2010

SUBJECT: Small Business Regulatory Reform Commission

SUMMARY: Establishes the seven member Small Business Regulatory Reform Commission for the purpose of recommending regulatory reforms that encourage the development and expansion of small businesses. Specifically, this bill:

- 1) Establishes the Small Business Regulatory Reform Commission (Commission) consisting of seven members who serve at the pleasure of their appointing authority:
 - a) Four members appointed by the Governor;
 - b) Two members appointed by the Senate Rules Committee; and
 - c) One member appointed by the Assembly Speaker.
- 2) Authorizes members to receive per diem and be compensated for reasonable travel expenses to attend meetings.
- 3) Authorizes the Commission to recommend reforms to state regulations that will encourage the development and expansion of California small businesses, including, but not limited to, reforms that will decrease expenses incurred by small businesses that result from state regulations and encourage small businesses to hire employees and buy supplies and materials in state.
- 4) Requires recommendations be submitted in an annual report to the Governor and Legislature.
- 5) Sunsets the requirements of this bill on January 1, 2014.

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) Establishes the Office of the Small Business Advocate (OSBA), within the Governor's Office of Planning and Research, for the purpose of advocating for small businesses including responding to complaints from small businesses concerning the actions of state agencies and the operative effects of state laws and regulations.
- 3) Requires the OSBA to report to the Legislature, every two years, on the efforts of the state in assisting minority and other small business enterprises, and make recommendations on how to strengthen minority and other small business enterprises.
- 4) Finds and declares that there has been an unprecedented growth in the number of administrative regulations, in recent years and that correcting the problems requires the direct

involvement of the Legislature, as well as that of the executive branch of state government. Further, statute 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.

- 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 its impact 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.

Further, no regulation adopted after January 1, 1993 may apply to a business unless the state agency makes a finding that it is necessary for the health, safety or welfare of the people of the state.

- 6) Establishes the Office of Administrative Law (OAL) as the entity with purview of the state's regulatory process, however, OAL is not authorized to substitute its opinion relative to specific content over that of the state adopting agency. In submitting a regulation for OAL's review, the agency is required to provide, among other things, a description of reasonable alternatives to the regulation that would lessen any adverse impact on small business and the reason for rejecting those alternatives.
- 7) Defines, for the purpose of state regulations, that a small business means a business that is independently owned and operated, not dominant in its field of operation and has businesses activities in:
 - a) Agriculture with under \$1 million in gross receipts;
 - b) General construction with under \$9.5 million in gross receipts;
 - c) Special trade construction with under \$5 million in gross receipts;
 - d) Retail trade with under \$2 million in gross receipts;
 - e) Wholesale trade with under \$9.5 million in gross receipts;
 - f) Services with under \$2 million in gross receipts;
 - g) Transportation and warehousing with under \$1.5 million in gross receipts;

- h) Power transmission company generating and transmitting with less than 4.5 million kilowatt hours annually;
- i) A manufacturing enterprise with less than 250 employees; or
- j) A health care facility with less than 150 beds or \$1.5 million in annual gross receipts.

FISCAL EFFECT: Unknown

COMMENTS:

- 1) Author's purpose: Over the past 20 years, regulations have been created in California, often in a vacuum, without a proper prospective in how they impact and affect the business environment. This sometimes haphazard nature of regulation has led to unintended consequences and California being regularly rated as one of the worst states to create and do business.

Small businesses are permanently closing their doors every day in our state. This means that our communities are losing jobs and our economy is continuing to suffer. Many small businesses are closing because they cannot continue to meet the demands placed on them by the Legislature and regulations promulgated by California's departments and agencies.

If small businesses are closing up shop that means that we are losing more and more jobs every day. And these are jobs in our local communities. We must take action to address the root of the problem, the over regulation and taxation that paralyzes small businesses.

The Small Business Regulatory Reform Commission is established by AB 2692 and tasked with identifying and recommending reforms to state regulations that will encourage the development and expansion of small businesses in California. The Commission is authorized to perform its task until January 1, 2014 and will submit an annual report of its findings to the Legislature.

- 2) Small business studies: Due to their importance in the state economy, small business issues have been a particular focus of the Assembly Committee on Jobs, Economic Development and the Economy (JEDE) for the past several years. In March 2009, JEDE produced a state economic recovery strategy that included several key recommendations on the needs of small business, including helping small businesses meet their short term capital needs, the need for regulatory reforms, and workforce development programs that more directly link to the needs of businesses.

Later in the year, JEDE held a number of hearings specifically to receive testimony from small businesses and manufacturers about their economic recovery needs. During these hearings small business prioritized two areas: increasing access to capital and reducing the costs associated with doing business in California, including costs related to business permits, licenses and other areas of regulatory compliance.

There are two major sources of data on the cost of regulatory compliance on businesses, the federal Small Business Administration and the state OSBA. For the last 10 years, the federal Small Business Administration has conducted a peer reviewed study that analyzes the cost of

federal government regulations on different sizes of 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 impact of California regulations on small businesses was unknown until last year, when the study required by AB 2330 (Arambula), Chapter 232, Statutes of 2006, was published by the OSBA. Although state agencies have been required to consider the costs of adopted regulations on the California economy, in general, and on small business specifically, state agencies have historically failed to meaningfully undertake such an analysis, and instead, have indicated that the need for the regulation was an overriding state concern. This first state study found that total cost of regulations to the State of California was \$493 billion. Since small businesses constitute 99.2 % of all employer businesses in California and all of non-employer business, the regulatory cost, according to the report, is shouldered substantially by small business (averaging \$134,123.00 per small business in 2007).

AB 2330 also required that state agencies examine the cumulative impact of regulations. Due, in part, to the difficult economic times, state agencies have done a poor job in meeting this new requirement when developing and amending regulations.

- 3) Adoption of regulations in California: Existing law sets forth an extensive process for the development and adoption of regulations, including requiring the identification of potential adverse impacts of regulations on California businesses and individuals. Statute states that the purpose of the rulemaking process is to avoid the imposition of unreasonable and unnecessary regulations, reporting, recordkeeping, or compliance requirements. Businesses, however, have repeatedly testified before this policy committee that they believe that California's regulatory process is expensive, overly burdensome, and that compliance has not necessarily provided a better quality of life for people in the state.

One of the criticisms of the process has been that OAL has no real authority to ensure that the intent of the law is enforced because its oversight is limited to a procedural review. Legislative intent specifically states that neither the OAL nor the courts may substitute its "judgment for that of the rulemaking agency as expressed in the substantive content" of the regulation.

This means that while the rulemaking entity is required to consider the impact of a regulation on businesses and consider alternatives, the OAL may only check to be sure that an assessment has been done. Rulemaking agencies may even decline to consider alternatives and may limit their assessment of a regulation's impact to only information supplied by interested parties. AB 2692 would establish a new commission with the purpose of representing the interests of small businesses within the existing rulemaking process. Specifically, the commission would be charged with reviewing and determining areas where regulations should be changed in order to encourage small business development.

- 4) Federal model for regulatory reforms: In 1976, the federal government established the Office of Advocacy (Federal Office) within the Small Business Administration. The purpose of the new Federal Office is to "protect, strengthen and effectively represent the nation's small businesses within the federal government's legislative and rule-making processes."

Among its duties, the Federal Office reviews federal regulations and makes recommendations on how to reduce the burden on small firms and maximize the benefits small businesses can receive from the federal government. In 2009, the Federal Office issued 39 letters to federal agencies, each posted on the Federal Office website and accompanied by a fact sheet summarizing advocacy's letter. The letters covered a range of rulemaking including, but not limited to:

- a) The Truth in Lending Proposed Rule, the US Treasury;
- b) Stream Buffer Zone and Related Rules, Department of the Interior, Office of Surface Mining Reclamation and Enforcement; and
- c) Proposed Rule on Mandatory Reporting of Greenhouse Gases, Environmental Protection Agency.

Having a specific government entity responsible for the review and comment on federal regulations is particularly useful because the Federal Office can provide more detailed comments and make specific and technical recommendations to assist the rulemaking entity to modify a rule to lessen its impact on small businesses, without necessarily reducing its policy objective.

While California has an OSBA, the state advocate does not currently have the staff, or the directed statutory mission, to formally comment on pending state regulations. AB 2692 would establish a new state commission to review regulations but is silent as to whether the commission will engage during the rulemaking process or after.

- 5) Existing small business boards and commissions: There are a number of formal and informal small business boards and advisory committees. Many of the entities focus on a single aspect of small business development, such as state procurement issues. The entity that has the broadest scope is the California Small Business Board (Board). The Board is administered through the Business, Transportation and Housing Agency and was originally established to help guide the development of the California Small Business Loan Guarantee Program.

Today, however, the Board has the broader purpose of also advising the Governor and the Legislature on issues and programs affecting California's small business community including innovation and economic expansion, export financing, state procurement, technical assistance and access to business capital issues. The author may wish to consider an alternative to establishing a new commission by expanding the scope of this existing Board.

- 6) Structure of the proposed Commission: AB 2692 proposes the establishment of Small Business Regulatory Reform Commission however the bill provides very little detail as to how it will operate, including such things as who will staff the commission, how meetings will be convened, and its relationship to the OSBA and the broader small business community. The author and/or Committee may wish to address some of these operational elements through amendments.

Another area that may need to be addressed is the proposed Commission's relationship in the overall regulation process including how it and the other state agencies will interact. Due to the Commission's potentially sensitive oversight responsibilities, it may be necessary to

require that state agencies respond and cooperate with the Commission as it implements its mission. In considering its mission, there may be a need to clarify whether the Commission is engaged in commenting on regulations that are in the process of being developed or just reviewing the impact of existing regulations.

Beyond the structure and purpose of the Commission, Members may wish to add more specificity as to the structure and content of its recommendations. Without sufficient technical detail, the Commission's annual reports may not provide the guidance necessary for the Governor and Legislature to take action, or at a minimum pursue their own oversight of regulations.

- 7) Economic Recovery and Regulatory Reforms: The Legislature is currently considering five economic recovery packages, including initiatives prepared by the Assembly Committee on Jobs, Economic Development and the Economy (JEDE), the Governor's Office, the Senate Democratic Caucus, the Assembly Moderate Democratic Caucus, and the Senate and the Assembly Republican Caucuses.

In general, these initiatives are designed around four themes: tax reforms, tort reforms, regulatory reforms, and programs and services to support business and workforce development. In March 2010, the Legislature passed and the Governor signed approximately \$400 million in tax incentives to support job creation in the clean-tech and construction industries. Limited action has been taken on the other proposals, including proposals related to improving the state's regulatory processes.

There are, however, an extensive list of bills related to regulatory reforms. In general, these bills take two basic approaches. One set of bills recommends methods for streamlining and fast tracking existing state requirements. The other set of bills proposes changes in how regulations are developed and/or approved. Below is a preliminary list of pending regulatory reform legislation.

Bills that propose a fast-track or streamlined approach include, but are not limited to:

- a) AB 978 (V. Manuel Pérez and Logue) - Streamlined State Licensing: This bill requires the State Chief Information Officer (CIO), in collaboration with other relevant agencies, to develop an online master application for businesses to file for state permits and licenses. This bill will provide guidance to a \$30 million information technology project, which has been approved in a prior budget year. Status: The bill is pending in Senate Committee on Governmental Organization.
- b) AB 2231(V. Manuel Perez) - Renewable Energy Action Team: This bill requires the California Energy Commission (CEC) to convene the Renewable Energy Action Team for the purpose of developing the Desert Renewable Energy Conservation Plan. Members of the team would include representatives from the CEC, the Department of Fish and Game, and the Natural Resources Agency. The bill would require the CEC also to request the United States Fish and Wildlife Service and the United States Department of the Interior Bureau of Land Management to also participate in the team. Status: The bill is pending before Assembly Committee on Natural Resources.

- c) SB 959(Ducheny) - Expedited Permit Review: This bill requires Office of Planning and Research (OPR) to implement an expedited permit process whereby interested applicants for development projects could submit projects to OPR and OPR would assist the applicant in identifying which permits would be required and providing a copy of each of the required permit applications. Status: The bill is pending in the Senate Committee on Local Government.

- d) SB 1351(Wright) – Require Commercially Available Technology: This bill requires an agency that adopts a regulation that requires the use of a new or emerging technology or equipment in order to achieve the identified purpose of the regulation to post, as specified, upon the effective date of the regulation, that the required technology or equipment is commercially available or will be commercially available prior to the effective date of the regulation. This bill would, if the required technology or equipment is not commercially available on the effective date of a regulation, prohibit an agency from enforcing a violation of the regulation until at least 6 months after the technology. Status: Pending in the Senate Environmental Quality Committee.

Bills that propose improvements to how regulations are developed and approved include, but are not limited to:

- a) AB 1949(Logue) - Regulations: Five-year Review: This bill requires specified state agencies to review and report to OAL on regulations that it adopts five years after adoption. The bill would require that the review and report include 10 specified factors, including a summary of the written criticisms of the regulation received by the agency within the immediately preceding five years and the estimated economic, small business, and consumer impact of the regulation. Status: The bill failed passage in the Assembly Committee on Business, Professions and Consumer Protection and reconsideration was granted.

- b) AB 2196 (Smyth) – Small Business Advocate's Report on Regulations: This bill requires the Office of the Small Business Advocate to commission a study on the 10 costliest regulations on California small businesses. The study is required to be prepared by October 2011. Status: The bill is pending before the Assembly Committee on Jobs, Economic Development and the Economy (JEDE).

- c) AB 2529 (Fuentes) – State Auditor Cost Benefit Analysis: This bill requires the State Auditor to conduct a specified cost benefit analysis of regulations. If a proposed regulation is approved that has an annual statewide economic cost of more than \$10 million or that the benefits of the regulation do not equal or exceed the costs of the regulation, the State Auditor is required to notify the Legislature and specified legislative committees are then required to conduct a public hearing to review the regulation. Status: The bill is pending in the Assembly Committee on Business, Professions and Consumer Protection (BPCP).

- d) AB 2603(Gaines) – Regulation Reductions: This bill enacts the California Smart Regulation Act, which requires, on or before July 1, 2011, that each state agency determine how many regulations it imposes and, on or before December 31, 2012, to reduce the total number of regulations it has identified by 33%. The bill would also require, until December 31, 2021, that any new regulation proposed by an agency also

- eliminate another regulation. Status: The bill is pending in the Assembly Committee on BPCP.
- e) AB 2692 (Tran) – Small Business Reforms: This bill establishes the seven member Small Business Regulatory Reform Commission for the purpose of recommending regulatory reforms that encourage the development and expansion of small businesses. Status: The bill is pending in JEDE.
 - f) SB 356 (Wright) - Impact of Regulations on Small Businesses: This bill requires an agency considering the adoption of a regulation to consult with those persons and businesses potentially affected and would delete the condition that the agency only involve those parties if the proposal is large or complex. Status: Pending in Assembly Business and Professions Committee.
 - g) SB 942(Dutton) - State Auditor: Analysis of Regulations: This bill establishes new requirements in the rulemaking process under the Administrative Procedure Act (APA) to: 1) require state agencies that are proposing a regulatory action to submit more detailed information regarding the costs of the proposed action, as specified, and (2) enhance the authority of the OAL in reviewing the cost estimates of proposed regulatory actions, as specified. Also, SB 942 requires agencies to catalog and review its existing regulations and to report its findings to the Legislature. Status: The bill is pending in the Senate Committee on Appropriations.
 - h) SB 954(Harman) - Joint Committee to Determine Economic Impact: This bill enacts the Jobs Protection Act, which would rename the Joint Committee on Boards, Commissions, and Consumer Protection as the Joint Committee on Boards, Commissions, and Consumer or Business Protection, and would create a new legislative procedure for determining the economic impact of specified pending legislation. The bill would require the joint committee to move a bill estimated to generate a fiscal impact of \$10,000 or more on small business, as defined, or \$50,000 or more on any other business, to the suspense file of the joint committee for further consideration, subject to specified procedural requirements. Status: The bill is pending in Senate Committee on Rules.
 - i) SB 960(Dutton) State Air Resources Board: regulations: Office of Administrative Law: This bill requires the State Air Resources Board to submit a major regulation, as defined, to the OAL for the purpose of having an analysis prepared as to the costs and benefits of the regulation and whether the regulation is technologically feasible. Status: The bill failed passage in Senate Committee on Environmental Quality.
- 8) California's small business economy: California's dominance in many economic areas is based, in part, on the significant role small businesses play in the state's \$1.8 trillion economy. Businesses with fewer than 100 employees comprise nearly 98% of all businesses, and are responsible for employing more than 37% of all workers in the state.

Among other advantages, small- and medium-sized businesses are crucial to the state's international competitiveness and are an important means for dispersing the positive economic impacts of trade within the California economy. Of the over 52,000 companies that exported goods from California in 2006, 95% were small- and medium-sized enterprises

(SME) with fewer than 500 employees. These SMEs generated nearly half (44%) of California's exports in 2006. Nationally, SMEs generated only 29% of total exports.

Historically, small businesses have functioned as economic engines, especially in challenging economic times. During the nation's economic downturn from 1999 to 2003, businesses with less than five employees created 318,183 new jobs or 77% of all employment growth, while larger businesses with more than 50 employees lost over 444,000 jobs. From 2000 to 2001, microenterprises created 62,731 jobs in the state, accounting for nearly 64% of all new employment growth. Unfortunately during the current recession, Equifax is reporting that small business have been especially hard hit, with small business bankruptcies up 81% for the 12 months ending September 2009, as compared to the same period in the previous year. Nationally, bankruptcy filings were up 44%.

REGISTERED SUPPORT / OPPOSITION:

Support

None received

Opposition

None received

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