



Washington State Auditor's Office

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Performance Audit

Assessing Implementation of the Regulatory Fairness Act

December 27, 2016

Lawmakers recognize that small businesses are likely to bear a disproportionate share of regulatory costs and burdens, and that the failure to recognize differences in the scale and resources of regulated businesses can adversely affect competition in the marketplace, discourage innovation, and restrict employment opportunities. Washington's Legislature enacted the Regulatory Fairness Act (19.85 RCW) in 1982 to reduce the disproportionate impact of state administrative rules on small business.

However, we examined 331 rules affecting businesses proposed by regulatory agencies during 2014 and 2015, and found they did not always fully meet every requirement of the law. We found a number of opportunities, many of which are no- or low-cost, for increasing the likelihood that agencies complete all the requirements of the Regulatory Fairness Act when proposing rules. They include clarifying certain parts of the law, modifying the form that agencies use to propose rules, and giving all employees tasked with rule development access to tools and training about meeting the law's requirements.



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State Auditor’s Office contacts

State Auditor Troy Kelley

360-902-0370, Auditor@sao.wa.gov

Jan M. Jutte, CPA, CGFM – Deputy State Auditor

360-902-0360, Jan.Jutte@sao.wa.gov

Chuck Pfeil, CPA – Director of State & Performance Audit

360-902-0366, Chuck.Pfeil@sao.wa.gov

Deborah Stephens – Principal Performance Auditor

360-725-5565, Deborah.Stephens@sao.wa.gov

Lori Reimann Garretson – Senior Performance Auditor

360-725-5000, Lori.Garretson@sao.wa.gov

Corey Crowley-Hall – Performance Auditor

360-725-5380, Corey.Crowley-Hall@sao.wa.gov

To request public records

Public Records Officer

360-725-5617, PublicRecords@sao.wa.gov

Executive Summary

Lawmakers recognize that small businesses are likely to bear a disproportionate share of regulatory costs and burdens. If the state does not recognize differences in the scale and resources of regulated businesses, it risks reducing competition in the marketplace, discouraging innovation, and restricting employment opportunities. Washington's Legislature enacted the Regulatory Fairness Act (RFA) in 1982 to reduce the disproportionate impact of state administrative rules on small businesses. It requires state agencies to consider how their proposed rules will impact businesses and to mitigate the costs to small businesses that are disproportionately affected.

To assess implementation of the RFA, we reviewed 331 rules proposed by 16 state agencies that affected businesses and were published by the Office of the Code Reviser in 2014 and 2015. We conducted this performance audit to answer the following questions:

1. Did state agencies fulfill all Regulatory Fairness Act requirements when proposing rules?
2. Are there opportunities for the state to improve implementation of the Regulatory Fairness Act?

Our evaluation of proposed rules did not include a determination of how additional clarification, documentation or completion of requirements would ultimately affect the cost of any rule to small businesses.

We found agencies did not always provide clear, fully-supported, and complete information consistent with the complex requirements of the RFA. However, we identified a number of no- or low-cost opportunities to greatly improve the accuracy and transparency of agencies' proposed rule filings.

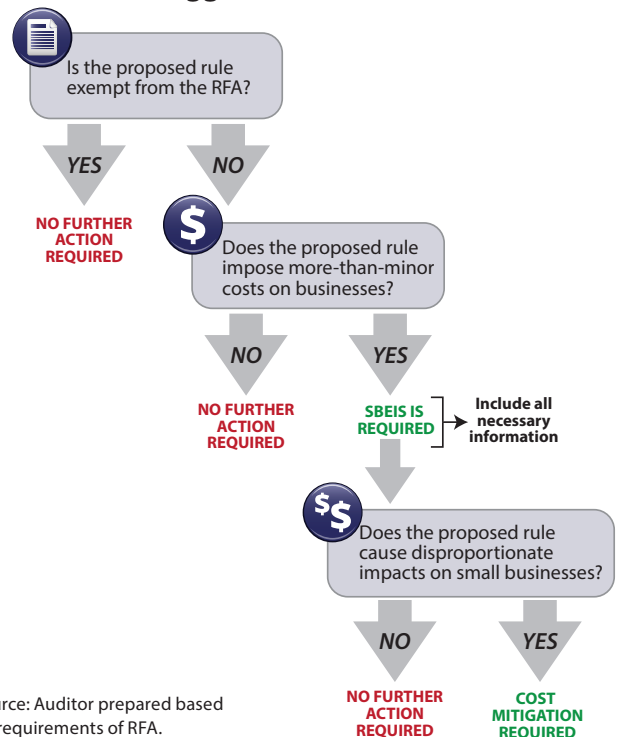
The RFA requires agencies to consider a number of cost comparisons and other business-related information

When proposing rules that affect businesses, agencies must first consider whether the rule is exempt from the RFA. Exemptions include rules that are expedited, are emergency rules, or are setting rates or fees.

For proposed rules that are not exempt from the law, agencies must analyze the costs to business to determine if they would exceed legally defined thresholds resulting in more-than-minor costs. If costs are more-than-minor, agencies must prepare a Small Business Economic Impact Statement (SBEIS). The SBEIS must demonstrate whether a proposed rule would impose a higher cost on small businesses relative to larger ones. For proposed rules that agencies determine will have a disproportionate impact on small businesses, agencies must mitigate those costs.

The process is illustrated in the graphic at right; the full list of necessary information is set out in Exhibit 7 on page 15 of this report.

Proposed rules imposing more-than-minor costs on businesses trigger an SBEIS



Source: Auditor prepared based on requirements of RFA.

Clarifying some sections of the law could help agencies better understand the requirements

Based on our evaluation of proposed rules, we found that agencies did not agree on the meaning of some important sections in the law, or had difficulty in understanding the requirements. Various types of proposed rules are exempt from the RFA; however, agencies that claimed their proposed rules were exempt from the law cited clear and allowable exemptions about half the time. Also, agencies did not interpret one of the exemptions defined in the Administrative Procedures Act consistently. In other cases, agencies did not understand which exemptions were allowable. A simple modification to the Code Reviser's proposed rulemaking form (CR-102) that provides a checklist of allowable exemptions could help to ensure agencies cite only allowable exemptions to the RFA in their proposed rules.

Some agencies believed they were exempt from completing an SBEIS when a proposed rule did not affect any small businesses. While the law does not explicitly identify this as a legal exemption, we concluded that the cost analysis required in an SBEIS serves no purpose when an agency can demonstrate that no small businesses would be affected.

In other cases, agencies concluded that a calculation of disproportionate costs was not necessary when only small businesses were affected. We concluded that a rule imposing costs on small business and no cost on large businesses should be considered to have a disproportionate impact on small businesses.

Agencies could improve proposed rule filings with statewide access to complete and accurate guidance

Because the RFA requires regulatory agencies to access extensive business-related information and complete a series of complex cost calculations, guidance and training are critical to ensuring agency employees have a clear understanding of the law, and are able to completely and accurately meet the law's requirements. In Washington, however, no entity provides guidance or training statewide. Some agencies told us they provide written materials to help employees complete the requirements of the RFA.

Of the 25 proposed rules that did include an SBEIS, only seven included all of the information required by law. In our evaluation of agencies' filings and the information required by the RFA, we found that agencies with written guidance prepared a better SBEIS than agencies with either no written guidance or guidance containing significant errors. Only three agencies provided materials that we concluded were both complete and accurate; the rest all contained various problems, including inaccuracies. Furthermore, not all agencies directed staff to retain relevant supporting documentation. We concluded the Department of Health's training materials and template could be useful to staff in other agencies.

Better access to accurate cost information may also help agencies meet the law's requirements

We found agency employees often had problems completing the various cost calculations required in the law. For example, only about half of the proposed rules that concluded the cost impacts on businesses would be less than minor included what we considered to be sufficient support. Agencies said they would like help in analyzing the data needed for their calculations. We found some industry payroll and revenue data online that could help agencies complete their minor-cost calculations. Access to tools, such as an Excel calculator we developed, could help staff with their analyses.

Business association members we interviewed suggested agencies could work with industry groups to reach and survey their members to gather information required in the analyses.

Agencies could improve their filings with support and oversight from a central entity

While the state does not have a single central authority to provide support or oversight for the RFA, such an entity could provide basic examples and templates as well as help in modeling various cost scenarios. Agencies themselves suggested that centralized coordination could allow them to share information and expertise within and across agencies – which in turn would help improve proposed rule filings.

Recommendations

To ensure agencies meet all requirements of the Regulatory Fairness Act, we recommend the Legislature:

1. Make the following clarifications in the Act:
 - a. A proposed rule is exempt from the Act if the proposing agency can demonstrate that it affects only businesses with more than 50 employees
 - b. A proposed rule that affects only small businesses inherently imposes disproportionate costs, and the proposing agency must consider all cost mitigation options defined in the Act
 - c. In the absence of sufficient data to calculate the disproportionate impacts, an agency whose rule imposes more-than-minor cost must mitigate the costs to small businesses, where legal and feasible, as defined in the Act
2. Require the Code Reviser to:
 - a. Modify the proposed rule form (CR-102) to include a checklist of allowable exemptions
 - b. Provide access to an SBEIS template that includes all required information
3. Assign a central entity to:
 - a. Collaborate with and provide support to state agency employees to help them meet the requirements of the law. Such support could include:
 - Providing online guidance and tools to help agency staff understand and complete the requirements
 - Providing access to available cost data
 - Facilitating sharing of information among agencies and between agencies and business associations
 - b. Hold agencies accountable for ensuring all proposed rules meet the requirements of the law

Introduction

Washington's small businesses play a vital role in the state's overall economy. As of 2015, businesses with fewer than 50 employees (a legal definition for small business in our state) account for 96 percent of Washington's businesses, and employ close to half (46 percent) of the state's private sector workers. The United States Small Business Administration (SBA) estimates that between 1993 and 2013, small businesses created 63 percent of all new jobs in the country.

The costs of meeting government regulations can strain small businesses, because they cannot easily spread the costs of compliance across their business or employ experts to help them navigate the regulatory landscape. According to the SBA, in its 2010 report titled *The Impact of Regulatory Costs on Small Firms*, businesses employing fewer than 20 employees bear the largest burden of federal regulations. The report estimated that their regulatory cost per employee was more than a third higher than the regulatory cost facing businesses with 500 or more employees.

SBA's report noted that many of the costs associated with regulatory compliance are "fixed costs," that is, they do not vary with the amount of production, such as many occupational safety and health requirements. Therefore, a firm with five employees incurs roughly the same expense as a firm with 500 employees. In large firms, these fixed costs of compliance are spread over a substantial revenue, output and employee base, which results in lower costs per unit of output as firm size increases. Small firms, with less revenue and output and fewer employees, are disproportionately affected. Overall, the report concludes, compliance costs place small businesses at a competitive disadvantage. Washington's Legislature has recognized that the disproportionate impacts of regulatory costs can reduce competition, innovation, and new employment opportunities, and can potentially threaten the survival of the businesses themselves.

To help ease the disproportionate impact of the state's administrative rules on small businesses, lawmakers in Washington state passed the Regulatory Fairness Act more than 30 years ago. The law, modeled after federal legislation that passed two years earlier, requires regulatory agencies to mitigate the costs, where legal and feasible, associated with new or modified rules when those costs would be disproportionately higher for small businesses.

Agencies meeting all requirements in the Regulatory Fairness Act consistently take the necessary steps to help small businesses and entrepreneurs thrive as the essential part of our state's economy that they are. This audit looked at agency implementation of the RFA, and examined whether the state has any opportunities to help improve agency implementation of its requirements.

We designed this audit to answer the following questions:

1. Did state agencies fulfill all Regulatory Fairness Act requirements when proposing rules?
2. Are there opportunities for the state to improve implementation of the Regulatory Fairness Act?

"Compliance costs" are the direct costs to businesses as they perform the various tasks associated with complying with government regulation.

Background

Lawmakers at both the federal and state level have recognized the importance of small businesses to the economy, and have adopted laws and executive orders requiring agencies to consider and mitigate the costs of their regulatory impacts, where legal and feasible.

Congress passed the federal Regulatory Flexibility Act in 1980 to help small businesses with the cost of regulation

At the federal level, Congress recognized the difficulty small businesses face in complying with regulatory requirements and adopted the Regulatory Flexibility Act in 1980. It requires that before agencies develop a regulatory rule, they must conduct an economic analysis of the impact of the proposed rule and consider the costs that the rule will impose upon small entities including businesses, small governments, and small nonprofits.

In 1996, Congress reinforced the 1980 law with passage of the Small Business Regulatory Enforcement Fairness Act, which added “teeth” to the Regulatory Flexibility Act. In addition to allowing for judicial review, it allowed businesses to challenge an agency’s compliance with the federal RFA and confirm or refute its cost assertions. The 1996 legislation required agencies to request and consider the input of small businesses as they developed new regulations.

President Bush’s Executive Order 13272 (signed in 2002) directed the Small Business Administration’s (SBA) Office of Advocacy to provide agencies with training and information on how to comply with the Regulatory Flexibility Act. President Obama’s Executive Order 13563, Improving Regulation and Regulatory Review (signed in 2011), strengthened the Act and underscored the importance of engaging with small businesses early in the regulatory process.

Washington responded in 1982 with the state’s Regulatory Fairness Act

Washington’s Legislature addressed regulatory flexibility in the Regulatory Fairness Act (RCW 19.85), quoted in the sidebar below. As with the federal law, it requires agencies to take the financial effects of proposed rules into account and calculate the costs to businesses. Agencies must prepare a Small Business Economic Impact Statement (SBEIS) for proposed rules under two circumstances: first, if the proposed rule will impose more-than-minor costs on businesses; or second, if requested to do so by the Joint Administrative Rules Review Committee.

The Legislature finds that administrative rules adopted by state agencies can have a disproportionate impact on the state’s small businesses because of the size of those businesses. This disproportionate impact reduces competition, innovation, employment, and new employment opportunities, and threatens the very existence of some small businesses. The Legislature therefore enacts the Regulatory Fairness Act with the intent of reducing the disproportionate impact of state administrative rules on small business.

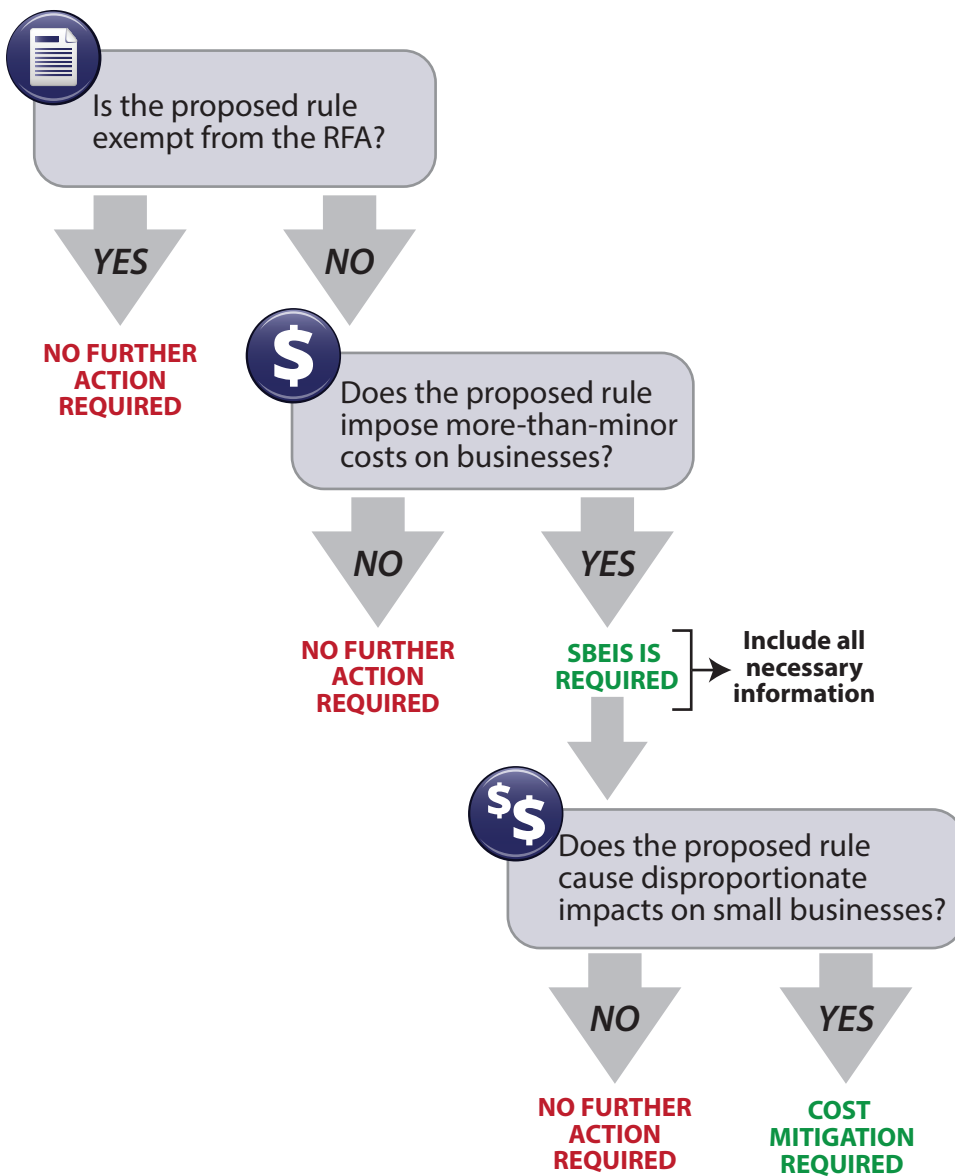
RCW 19.85

As an agency prepares to file a new or amended rule with the state’s Office of the Code Reviser, which it submits on a standardized form, it must determine whether a proposed rule is exempt from the RFA, and if not, whether it will impose more-than-minor costs on businesses. The Regulatory Fairness Act defines minor costs to businesses as costs of a proposed rule that exceed thresholds based on annual revenue or payroll, or for the Department of Social and Health Services, cost per client served.

When an agency determines that costs are more-than-minor, it must prepare an SBEIS in addition to the CR-102 form it submits to the Office of the Code Reviser. **Exhibit 1** summarizes the sequence of decisions required by the law to determine whether an SBEIS is required.

Exhibit 1 – When an agency determines its proposed rule imposes more-than-minor costs on businesses, it must complete an SBEIS

The full list of necessary information required by an SBEIS is set out in Exhibit 7



Source: Auditor prepared based on requirements of RFA.

As outlined in the law, the SBEIS must provide a description of all compliance costs, and must consider, based on input received, whether the proposed rule will cause lost sales or revenue. The SBEIS must also demonstrate whether the proposed rule will have a disproportionate cost impact on small businesses by comparing the cost of compliance for small business with the cost of compliance for the largest 10 percent of businesses required to comply. Based upon the extent of disproportionate impact on small business, agencies must consider, without limitation, a number of methods for reducing the impact, where legal and feasible, including reducing or eliminating substantive regulatory requirements, reducing the frequency of inspections, and delaying compliance.

The SBEIS must also provide a description of how the agency will involve, or has already involved, small business in the development of the rule, and a list of industries affected. The law states that an agency may survey a representative sample of affected businesses to collect information for the SBEIS, and should, whenever possible, appoint a committee to help accurately assess the costs of the proposed rule and the means to reduce the costs imposed on small business.

In 2007, the Legislature modified the requirements of the SBEIS to include the estimated number of jobs created or lost due to the impact of the rule.

A full list of requirements for a Small Business Economic Impact Statement is provided on page 15.

Two legislative offices play a role in administering the Regulatory Fairness Act

Two legislative offices, the Office of the Code Reviser and the Joint Administrative Rules Review Committee, play a role in administering the RFA.

The Code Reviser publishes the State Register and the Washington Administrative Code. Agencies adopting new rules or changing existing rules must file them with the Code Reviser for inclusion in the State Register as public notice of the rulemaking. The Code Reviser requires that filings follow a certain format, and may return documents (such as the CR-102 'Proposed rulemaking' form) if they have not been filled out correctly. Agencies required to file Small Business Economic Impact Statements must attach them when they submit the proposed rule.

The Joint Administrative Rules Review Committee (JARRC) of the Legislature is empowered to conduct selective reviews of agencies' SBEIS. The RFA also gives the Committee authority to require an agency to prepare an SBEIS. The Committee has required some agencies to correct or amend an SBEIS; however, it has been a rare occurrence, and conducted in response to citizen complaints.

Currently, neither of these offices is charged with conducting an independent review of proposed rule filings to determine whether the requirements outlined in the Regulatory Fairness Act have been met. Nor are they or any other known agency available to answer agency questions or provide help as agency employees attempt to comply with the law.

One duty of the Office of the Code Reviser is to publish rules of executive branch agencies (also called Washington's Administrative Code, or WACs) which are issued by authority of statutes (laws). The Regulatory Fairness Act applies to agencies filing those regulatory rules.

Scope & Methodology

To answer our audit questions, we conducted three primary activities.

1. Evaluated proposed rules affecting businesses

We identified all rules proposed by the 26 regulatory agencies in the 2014 and 2015 State Register, and narrowed the scope of the audit to the 16 agencies who proposed more than a few rules affecting businesses (listed in Appendix B). To evaluate our sample of proposed rules to ensure they met the requirements of the Regulatory Fairness Act (RFA), we grouped them by whether agencies filed them with a claim of an exemption from the RFA, a claim of imposing less-than-minor costs on businesses, or a claim of more-than-minor costs.

- We examined those rule filings that claimed an exemption to determine whether the exemption claimed was clearly identified and allowable by law. We did not examine whether a clearly identified and allowable exemption was applied correctly.
- To evaluate those proposed rules claiming impacts to businesses that were of less-than-minor costs, we asked agencies for their supporting documentation. We considered the claim fully supported if it included costs to businesses compared to one of the legal thresholds, provided a clear conclusion, and described a credible source of data. If the agency provided a qualitative analysis, we considered that analysis to be sufficient if it cited a credible source for the information and contained a clear explanation of how the agency reached its conclusions. We did not evaluate the accuracy of the calculations themselves.
- For those rule filings claiming more-than-minor cost impacts to businesses, which require the completion of a Small Business Economic Impact Statement (SBEIS), we reviewed the SBEIS to ensure they contained all information required by the RFA. We did not evaluate the quality or accuracy of the contents of the SBEIS.

Our evaluation of proposed rules did not include a determination of how additional clarification, documentation or completion of requirements would ultimately affect the cost of any rule to small businesses.

2. Reviewed available tools to help agencies meet the requirements of the RFA

We sent a questionnaire to the agencies in our audit asking them to describe how they ensure their employees meet the requirements of the law, and to provide any written guidance the agency made available to them. We reviewed the written guidance for completeness and accuracy, and reviewed any templates agencies provided. We also looked at guidance and tools available statewide and considered practices in other states that could be helpful to regulatory agencies in Washington.

3. Asked business associations and small businesses for their input

We met with eight associations that represent small businesses to discuss their experiences with agency rulemaking and the SBEIS process. Six of the associations represented various economic sectors; two represented a broad array of industries – Washington’s chapter of the National Federation of Independent Businesses and the Independent Business Association. The latter two forwarded to their members our questionnaire asking about their experiences and expectations regarding agency rulemaking and the Regulatory Fairness Act.

Audit performed to standards

We conducted this performance audit under the authority of state law (RCW 43.09.470), approved as Initiative 900 by Washington voters in 2005, and in accordance with Generally Accepted Government Auditing standards (December 2011 revision) issued by the U.S. Government Accountability Office. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives. See **Appendix A**, which addresses the I-900 areas covered in the audit. **Appendix B** contains more information about our methodology.

Next steps

Our performance audits of state programs and services are reviewed by the Joint Legislative Audit and Review Committee (JLARC) and/or by other legislative committees whose members wish to consider findings and recommendations on specific topics. Representatives of the State Auditor’s Office will review this audit with JLARC’s Initiative 900 Subcommittee in Olympia. The public will have the opportunity to comment at this hearing. Please check the JLARC website for the exact date, time, and location (www.leg.wa.gov/JLARC). The State Auditor’s Office conducts periodic follow-up evaluations to assess the status of recommendations and may conduct follow-up audits at its discretion.

Audit Results

Question 1: Did state agencies fulfill all Regulatory Fairness Act requirements when proposing rules?

Answer in brief: Partially. Agencies did not always provide clear, fully supported and complete information consistent with the Regulatory Fairness Act requirements in their original proposed rule filings.

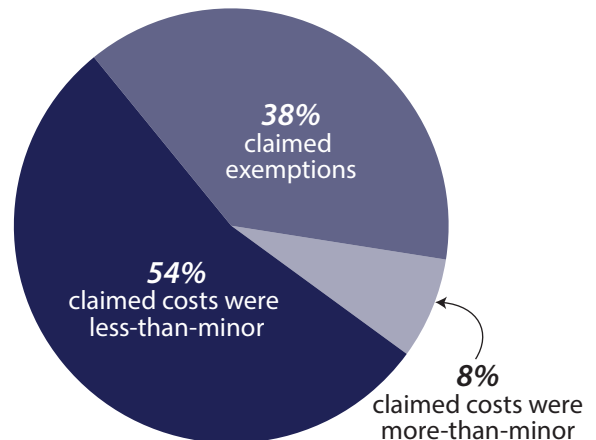
The Regulatory Fairness Act (RFA) requires agencies to consider the costs to businesses when proposing new or amended rules, and to mitigate those costs, where legal and feasible, when they disproportionately affect small businesses. We examined 331 proposed rules affecting businesses filed by state agencies in 2014 and 2015, and found that agencies provided clear, fully-supported, and complete information consistent with the law's requirements in their initial rule filings about half the time. For those filings that did not contain complete information, the degree of omission varied considerably. Some agencies, for example, omitted only one or two considerations (such as the consideration of potential lost sales or revenue of a proposed rule) from the law's many complex requirements.

Of the 331 proposed rules we reviewed, 38 percent claimed exemptions, another 54 percent claimed the rules imposed less-than-minor costs, and the remaining 8 percent claimed the rules imposed more-than-minor costs on businesses (see Exhibit 2).

When agencies said costs were less-than-minor, we asked them for clarification or supporting documentation or to explain the reasoning behind the rule filing as originally written. In some cases, they revised the information they provided in their original filings; in a few cases, they demonstrated logical reasons for their lack of complete documentation.

We found some agencies had difficulty correctly identifying allowable exemptions from the RFA, calculating whether rules would impose more-than-minor or less-than-minor costs to businesses, and properly completing all requirements of a Small Business Economic Impact Statement (SBEIS) when necessary.

Exhibit 2 – Of the 331 proposed rules we examined, only 8% claimed the rule imposed more-than-minor costs on business



Source: Auditor analysis of proposed rules.

Only about half the proposed rules claiming exemptions from the RFA cited clear and allowable exemptions

Agencies proposing new rules affecting businesses must first determine whether their filings meet any of the allowable exemptions from the RFA, summarized in Exhibit 3. Appendix C provides the precise language of the law for each exemption.

Exhibit 3 – A dozen laws or subsections address exemptions from the RFA

Rules are exempt if they	According to RCW
Are expedited rules	19.85.025(1) & (2) 34.05.353(3)
Are emergency rules	19.85.025(3) 34.05.310(4)(a)
Relate only to internal governmental operations	34.05.310(4)(b)
Adopt federal or state laws or regulations by reference without material change	34.05.310(4)(c)
Make typographical or clarifying changes without changing the effect	34.05.310(4)(d)
Have content explicitly dictated by statute	34.05.310(4)(e)
Set or adjust fees or rates according to legislative standards	34.05.310(4)(f)
Relate to the process of agency hearings or applying for a license or permit	34.05.310(4)(g)
Include a cost-benefit analysis with all requirements of an SBEIS	19.85.025(4)
Complete the pilot rule process	19.85.030(1)(a)(ii)
Are adopted by a referendum under the Agricultural Enabling Act	15.65.570(2)

Source: Revised Code of Washington, www.leg.wa.gov.

Agencies claimed exemptions in 127 out of 331 (38 percent) of the rules we examined. In those 127 filings, agencies cited clear and allowable exemptions only slightly more than half of the time (see Exhibit 4). In the remainder, some agencies claimed exempt status without citing a specific reference within the law while others provided no explanation to justify why they believed no SBEIS was necessary. When we asked for clarification, others changed their claim to another reason that an SBEIS was not required, such as less-than-minor cost to businesses, which is discussed in more detail below. One proposed rule claimed an exemption that had been removed from the law more than 20 years ago.

In 14 filings, agencies claimed exemptions from the RFA because the proposed rules did not affect small businesses. When asked, agencies gave us credible supporting documentation for most of the 14 filings to demonstrate the proposed rules only affected businesses with more than 50 employees. However, the RFA does not contain language to explicitly exempt agencies for this reason: it requires an SBEIS whenever the cost to businesses in the regulated industry is calculated as more-than-minor. This issue can lead agencies to perform time-consuming documentation and cost analysis for a rule that does not affect small businesses.

Detail of Exhibit 1 – Agency’s 1st decision point

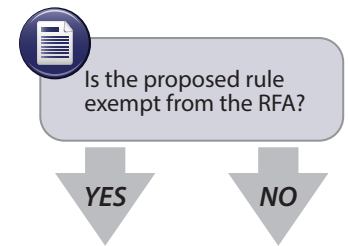
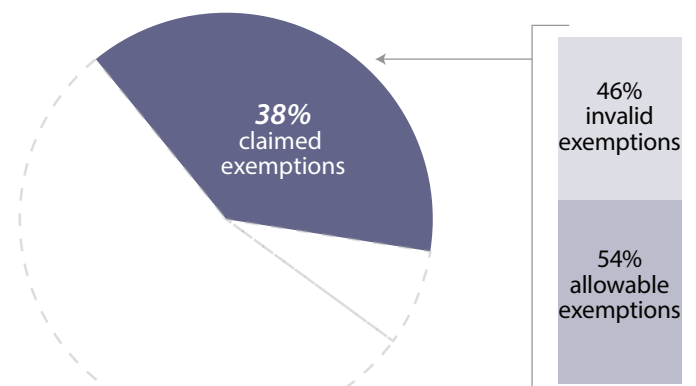


Exhibit 4 – Agencies applied allowable exemptions for half of the filings originally claiming exemptions



Source: Auditor analysis of proposed rules.

Agencies provided sufficient supporting documentation for half the filings that claimed less-than-minor cost impacts

Once agencies have established the proposed rule is not exempt from the RFA, they must determine whether the rule will impose more-than-minor costs for businesses. An agency must first estimate the costs of compliance for all businesses, then compare that cost to one of the three minor-cost thresholds identified by the law, illustrated in Exhibit 5. They are not currently required to include documentation supporting these calculations with the rule filing.

Detail of Exhibit 1 – Agency’s 2nd decision point

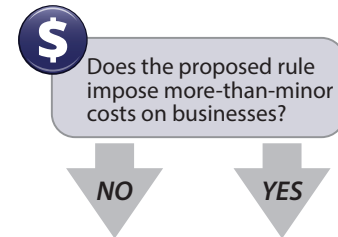


Exhibit 5 – Agencies must compare cost of compliance with legal thresholds to determine whether a rule will impose more-than-minor costs

Costs of compliance

- Equipment
- Supplies
- Labor
- Professional services
- Increased administrative costs
- Lost sales or revenue



Minor-cost thresholds

Most agencies use whichever is the greater:

- 0.3 percent of annual revenue
- \$100
- or
- 1 percent of annual payroll

DSHS only = \$50/client

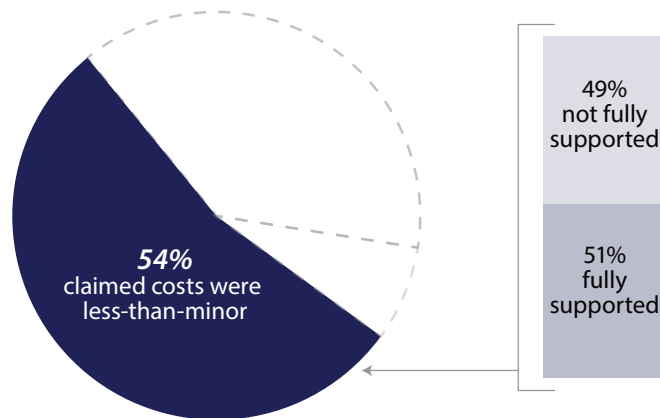
Source: Auditor prepared based on requirements of RFA.

To evaluate rule filings indicating a result of less-than-minor costs for businesses, we asked agencies for documentation of their calculations. While we did not test the accuracy of the specific calculations, we considered the claim fully supported if it included costs to businesses compared to one of the legal thresholds, provided a clear conclusion, and described a credible source of data. If the agency provided a qualitative analysis, we considered that analysis sufficient if it cited a credible source for the information and contained a clear explanation of how the agency reached its conclusions.

Of the 331 rules we evaluated, 179 (54 percent) stated the rule would impose less-than-minor costs to businesses. Agencies provided what we considered sufficient support for about half of the 179 proposed rules; the remainder we considered not fully supported, as shown in Exhibit 6. In a few cases, agencies changed the less-than-minor-cost assertion in the original filing to an exemption claim. Several agencies provided unquantified cost descriptions in the supporting documentation, such as cost impacts based on a one to four scale. Others told us they were unable to estimate the costs because they lacked the necessary data or access to economists.

In addition, the cost portions of the filings were provided in an array of different formats. Agencies filed many of their minor-cost claims, for example, in SBEIS formats. The inconsistent formats for these and other portions of the rule filings addressing the RFA’s requirements could make information confusing to readers, and business representatives in particular.

Exhibit 6 – Agencies provided full support for claims that costs were less-than-minor half the time



Source: Auditor analysis of proposed rules.

Less than a third of all SBEIS filed by agencies included all necessary information

Once an agency determines that a proposed rule will cause more-than-minor costs to businesses, it must complete an SBEIS. The requirements for an SBEIS are numerous and complex. A comprehensive list of requirements for the SBEIS is provided in **Exhibit 7**.

Detail of Exhibit 1 – Agency's action point

SBEIS IS REQUIRED } → **Include all necessary information**

Exhibit 7 – This information must appear in a complete Small Business Economic Impact Statement

Determine compliance costs

Briefly describe:

- Reporting, recordkeeping, and other compliance requirements of the proposed rule
- Kinds of professional services that a small business is likely to need to comply
- Costs of compliance for businesses required to comply, including costs of:
 - equipment
 - supplies
 - labor
 - professional services
 - increased administrative costs
- Whether compliance with the rule will cause businesses to lose sales or revenue

Provide other business information

Describe:

- How the agency will involve small businesses in the development of the rule
- Industries that will be required to comply with the rule
- An estimate of the number of jobs that will be created or lost as the result of compliance with the proposed rule

Determine disproportionate costs

Compare:

- Cost of compliance for small business
- Cost of compliance for the 10 percent of largest businesses required to comply

Basis of comparison, using one or more:

- Cost per employee
- Cost per hour of labor
- Cost per one hundred dollars of sales

Mitigate disproportionate costs, if determined to exist

Describe steps taken to reduce costs for small business if disproportionate impact exists, by:

- Reducing, modifying, or eliminating substantive regulatory requirements
- Simplifying, reducing, or eliminating recordkeeping and reporting requirements
- Reducing the frequency of inspections
- Delaying compliance timetables
- Reducing or modifying fine schedules for noncompliance
- Any other mitigation techniques suggested by small businesses or their representatives

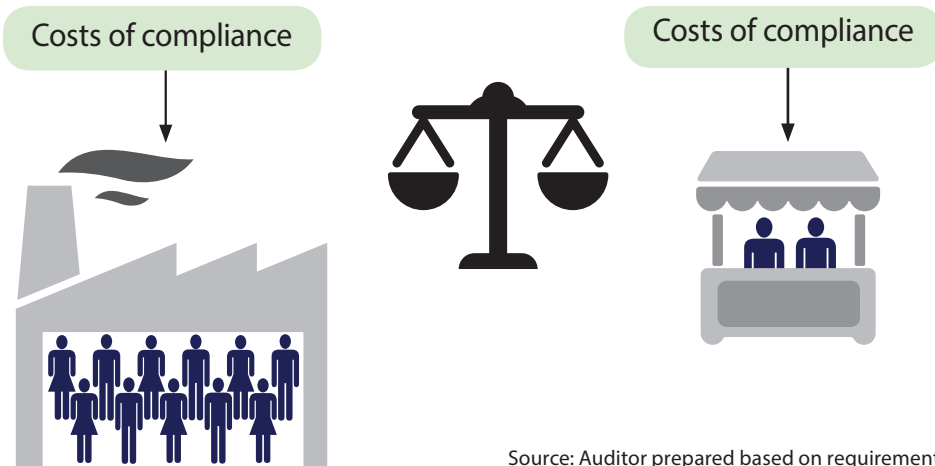
or

Provide a clear explanation of why agency did not reduce costs if it determined it cannot do so.

Among the many categories of information required in an SBEIS is a demonstration of whether the proposed rule will have a disproportionate cost impact on small businesses.

The law requires agencies to calculate disproportionate cost by comparing the cost of compliance for small business with the cost of compliance for the largest 10 percent of businesses required to comply (see **Exhibit 8**).

Exhibit 8 – Agencies must consider that costs of compliance with a rule can be very different for large and small firms, as they spread the cost across the size of their business



Source: Auditor prepared based on requirements of RFA.

Based upon the extent of disproportionate impact on small business, and where legal and feasible, the law states that “agencies must consider, without limitation, each of the following methods of reducing the impact:”

- Reducing, modifying, or eliminating substantive regulatory requirements
- Simplifying, reducing, or eliminating recordkeeping and reporting requirements
- Reducing the frequency of inspections
- Delaying compliance timetables
- Reducing or modifying fine schedules for noncompliance; or
- Any other mitigation techniques including those suggested by small businesses or small business advocates

If agency staff conclude that it will not be possible to mitigate costs imposed by the rule on small businesses, the SBEIS must clearly explain how the agency came to that determination.

Twenty-five out of 331 (8 percent) proposed rules cited more-than-minor cost impact to businesses, therefore resulting in an SBEIS. Of the 25, seven contained all of the information required by law (see **Exhibit 9**). In some cases, however, the omission was only one or two of the numerous requirements. For example, four statements were complete in every way except the analyses did not include demonstration that they considered whether compliance would cause a loss of sales or revenue.

Detail of Exhibit 1 – Agency’s 3rd decision point

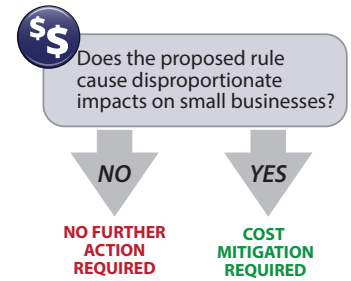
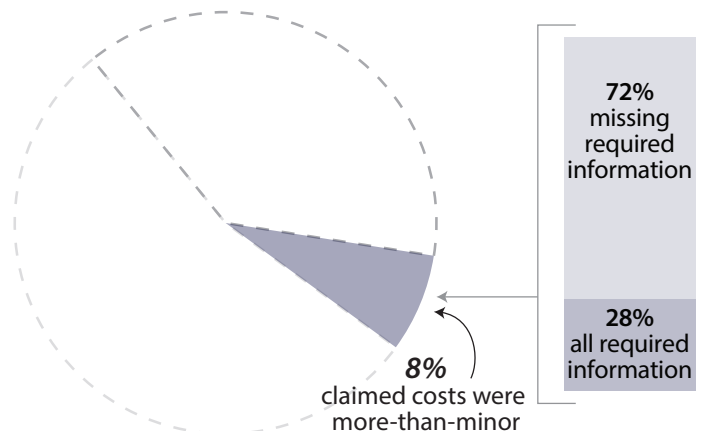


Exhibit 9 – Only 28 percent of filed SBEIS had all necessary information



Source: Auditor analysis of proposed rules.

Additionally, in 11 of the filings, agencies acknowledged that disproportionate costs would be borne by small businesses, but only three filings included documentation of consideration without limitation all of the required cost mitigation strategies. Others addressed some of the cost mitigation strategies, but we considered them to be incomplete in our evaluation because the agency did not document that it considered every strategy.

Another seven lacked analysis to demonstrate the extent of disproportionate costs to small businesses, or reached unclear conclusions. For example, one SBEIS contained a summary of complaints from the business community and suggested that the business community misunderstood the rule, rather than comparing costs between small businesses and the largest 10 percent, as the law requires.

Disproportionate cost calculations varied considerably; Ecology's stood out as practical and efficient

Agencies that did complete the cost calculations used a variety of methods to calculate the extent of disproportionate costs, such as relying on business surveys. One agency, the Department of Ecology, developed an efficient process that acknowledges it is sensible to expect disproportionate costs to small businesses from any rule that imposes more-than-minor costs on all businesses, given the basic difference in the size of the businesses and the number of employees. Ecology divides the total costs calculated in the original minor cost calculation by the number of employees. Calculated in this way, rules causing more-than-minor costs for businesses would by definition disproportionately affect small businesses. We considered that in the absence of easily accessible or reliable cost information to complete the calculation of disproportionate costs, Ecology's method is a practical and conservative way to comply with the law.

In a few cases, for proposed rules that would by definition affect only small businesses, the rule filing concluded that the cost could not be disproportionate because there were no large businesses to compare the effect to. We examine this assumption, which we consider incorrect, in Question 2.

Question 2: Are there opportunities for the state to improve the implementation of the Regulatory Fairness Act?

Answer in brief: Yes. There are low-cost opportunities to help agencies provide clear and complete information required by the Regulatory Fairness Act.

We recognize that the RFA requires a number of complex calculations that – judging from the number of errors and omissions we found – some agencies found difficult to complete. We identified a number of low- or no-cost opportunities for the state to help agencies better understand and implement the law. Clarification in the language of the law, for example, could resolve some misunderstandings about requirements. Templates and step-by-step guidance could help agencies complete necessary calculations and include all required items in their proposed rule filings.

In addition to the low- and no-cost opportunities to support better proposed rule filings, the process could benefit from ongoing support and oversight from a central entity.

Clarifying some sections of the law could help agencies better understand the requirements

Based on our evaluation of proposed rules, we found that agencies did not agree on the meaning of some important sections in the law, or had difficulty in understanding the requirements. Among the areas that caused confusion were allowable exemptions, differentiating between affected and unaffected businesses, and responding to the requirement for disproportionate cost analysis. Clarifying those sections could help agencies improve their proposed rule filings.

One exemption defined in the Administrative Procedures Act led to differing responses from agencies

Various types of proposed rules are exempt from the RFA; for many of them, the RFA points to exemptions defined in the Administrative Procedures Act (APA). Agencies, however, did not interpret one of the exemptions defined in the APA (34.05.310 (4) (f)) consistently.

The APA states that rules are exempt that “...set or adjust fees or rates pursuant to legislative standards...” Some agencies interpreted the term “legislative standards” broadly – as “set or adjust fees based on the law” – others narrowly, as “the specific amount of the fee or rate change has been prescribed by the Legislature.” We asked the Attorney General’s Office for an informal interpretation and were told that the law refers to “setting or adjusting rates or fees as allowed by statute with any kind of guidance,” such as “to cover costs.”

Agencies interpreting the APA narrowly spent time and resources completing an SBEIS in situations where the RFA’s required cost mitigation strategies may not apply.

Agencies did not always understand which exemptions are allowed by law

As we have already shown, agencies did not always claim clear, allowable exemptions when filing proposed rules with the Code Reviser. The Code Reviser's rule proposal form (CR-102), which agencies fill in when they propose new or revised rules, does not guide agencies through exemptions; instead, it leaves free space for agencies to explain why they did not conduct an SBEIS.

Exhibit 10 illustrates a portion of the current form. We developed a mockup of a revised CR-102 form with our suggested improvements, including a checklist of all allowable exemptions, illustrated below in **Exhibit 11**.

Exhibit 10 – The current Code Reviser's CR-102 form does not allow staff to select from a list of allowable exemptions

Has a small business economic impact statement been prepared under chapter 19.85 RCW or has a school district fiscal impact statement been prepared under section 1, chapter 210, Laws of 2012?

Yes. Attach copy of small business economic impact statement or school district fiscal impact statement.

A copy of the statement may be obtained by contacting:
Name: _____
Address: _____

phone () _____
fax () _____
e-mail _____

No. Explain why no statement was prepared.

Exhibit 11 – A checklist on the CR-102 form could help agencies claim only allowable exemptions

Regulatory Fairness Act cost considerations
This rule proposal **may be exempt** from requirements of the Regulatory Fairness Act (see RCW 19.85). Please check these statements to see if it qualifies for exemption:

This rule is exempt under RCW 19.85.061 because this rulemaking is being adopted solely to conform or comply or both with federal statute or regulations. Please cite the specific federal statute or regulation this rule is being adopted to conform or comply with, and describe the consequences to the state if the rule is not adopted.
[form field for text] _____

This rule is exempt because the agency has completed the pilot rule process defined by RCW 34.05.313 before filing the notice of this proposed rule.

This rule is exempt because it was adopted by referendum under the provisions of RCW 15.65.570(2).

This rule is exempt under RCW 19.85.025(3). Check all that apply:

<input type="checkbox"/> RCW 34.05.310(4)(b)	<input type="checkbox"/> RCW 34.05.310(4)(e)
<input type="checkbox"/> RCW 34.05.310(4)(c)	<input type="checkbox"/> RCW 34.05.310(4)(f)
<input type="checkbox"/> RCW 34.05.310(4)(d)	<input type="checkbox"/> RCW 34.05.310(4)(g)

If the proposed rule is **not exempt**, does it impose more-than-minor costs (as defined by RCW 19.85.020(2)) on businesses?

No – Briefly summarize the agency's analysis showing how costs were calculated.
[form field for text] _____

Yes – Calculations showed the rule imposed more than-minor cost to businesses, and a small business economic impact statement is attached as required.

Is a School District Impact Statement required?

No

Yes – The statement is attached as required.

The public may obtain a copy of the statement by contacting:
Name: _____
Address: _____

phone () _____
fax () _____
e-mail _____

Appendix D provides a further comparison of the current CR-102 form and our suggested format.

Agencies interpreted the distribution of small and large businesses differently

Two remaining areas of confusion for some agencies related to the distribution of large versus small businesses within the regulated industries. The first occurs when no small businesses are affected by a proposed rule, and the second occurs when only small businesses are affected.

The first area of confusion related to conducting cost analyses for proposed rules that did not affect any small businesses. While the statute as written appears to require an SBEIS if the rule imposes more-than-minor costs on any business without regard to the size of the regulated businesses, we concluded there is no purpose for the analysis if the agency knows that small businesses are unaffected. For example, we examined a proposed rule related to commute trip reduction programs that we included in the tally of those that did not meet the requirements of the law as currently written. However, the agency provided documentation to show that commute trip reduction programs are only required for businesses with more than 100 employees. Small businesses, by definition, cannot be affected by the rule.

The second area of confusion related to the “disproportionate cost analysis” required by an SBEIS. Three different agencies concluded that when a proposed rule addressed only small businesses, its costs could not be disproportionate because there were no large businesses to compare them to. One agency wrote its staff rulemaking guidance materials with this assumption.

Because the intent of the Regulatory Fairness Act is to reduce the disproportionate impact of agency rules on small businesses, we concluded that a rule imposing costs on small business and no cost on large businesses should be considered to have a disproportionate impact on small businesses.

Agencies could improve proposed rule filings with statewide access to complete and accurate guidance

The last example raises the issue of the quality and availability of accurate guidance materials for employees tasked with composing the agency’s rulemaking proposals. Because the RFA requires regulatory agencies to complete a series of complex cost calculations, guidance and training are critical to ensuring agency employees have a clear understanding of the law, and are able to completely and accurately meet the law’s requirements. In Washington, however, no entity provides guidance or training statewide.

Both the federal government and other states offer guidance and training to help agency staff comply with their regulatory flexibility laws. The Small Business Administration’s (SBA) Office of Advocacy publishes a guide to compliance; prepared with input from regulatory agencies, it is effectively a step-by-step manual to help agency rule writers and policy analysts comply with federal law. The SBA supplements the manual with training for agency personnel.

The Code Reviser’s website does not provide adequate guidance or templates

One duty of the Office of the Code Reviser is to publish rules of executive branch agencies (also called Washington’s Administrative Code, or WAC) which are issued by authority of statutes (laws). The Regulatory Fairness Act applies to agencies filing those regulatory rules. The Code Reviser, however, provides only minimal guidance related to meeting the requirements of the Regulatory Fairness Act on its website. The Code Reviser said they do on occasion point agencies to the law, their attorney general, or other agencies, but do not consider it their role to help agencies comply with the law. In several other states, the equivalent of Washington’s Office of the Code Reviser provides both templates and guidance to help agency staff comply with similar laws.

We found few agencies give employees complete and accurate guidance or templates relating to the RFA

In our evaluation of agencies’ filings and the information required by the RFA, we found that agencies with written guidance prepared a better SBEIS than agencies with either no written guidance or guidance containing significant errors.

We asked the 16 agencies in our audit for any written materials they use to help employees complete the requirements of the RFA. Half told us they had written guidance; of the eight who did, only three had materials that we concluded were both complete and accurate. We found various problems with the materials the agencies showed us.

Written guidance supplied by several agencies included inaccurate information. For example, one agency’s guidance incorrectly directed staff to use the minor-cost definition that applies exclusively to proposed rules filed by the Department of Social and Health Services. Three agencies’ guidance directed staff to complete an SBEIS only if costs to businesses were both more than minor and disproportionate for small businesses. Another agency’s guidance incorrectly said the only fees exempt from the RFA were fees related to obtaining a trade name or applying for a business license through the Business Licensing Service.

Five of the eight agencies that provided written guidance included language that directed staff to document and retain the analysis that showed how they determined costs would be less-than-minor. The RFA does not specifically require agencies to attach this analysis to the rule filing, but including a brief explanation could greatly improve transparency of government agency decisions. In addition, staff in other agencies could benefit from the information as they prepare their proposed rule filings in the future.

We also found that few agencies provide templates to help their employees complete an SBEIS: only two of the 16 showed us a complete and accurate SBEIS template. Several other agencies gave us templates that were incomplete and/or did not offer their staff sufficient guidance to help users understand when and how to use the templates to meet the requirements of the RFA.

Examples from Health could help other regulatory agencies

Two agencies, the departments of Health and Agriculture, have developed excellent tools to help their employees. They provide complete and accurate guidance and a template that walks the user through all of the steps needed to complete an SBEIS. We found Health's materials more user-friendly, and observed that it resulted in the highest overall compliance.

With some small modifications, we believe Health's template could help other agencies' staff ensure they include all information required in an SBEIS. An example of our modified template is included in **Appendix E**. Requiring agencies to use such a template likely offers additional benefits, including increasing transparency and understanding of the filings by members of the public or business community.

Health's related training could help employees in other agencies complete the template, so with the Department of Health's permission, we have posted the modified template and PowerPoint training presentation on our website.

View the template and training materials on our website at www.sao.wa.gov/state/Pages/RegReform.aspx

Better access to accurate cost information may also help agencies meet the law's requirements

Based on our evaluation of the proposed rules and discussions with both agencies and business associations, we found that completing the cost calculations required in the law posed problems for some agency employees. Their difficulties are evident in the fact that nearly half the filings claiming less-than-minor costs lacked sufficient supporting documentation.

In discussions with business association representatives and agency staff, we learned that businesses often consider their cost information proprietary or fear that shared information could be used against them. Some agency managers also said that when they have surveyed businesses for potential costs, the responses they received did not always seem reasonable. In addition, some agency employees we spoke with said they would like help analyzing the data needed for their calculations.

Some payroll and revenue data for the minor cost calculation can be found online

When agencies struggle to obtain necessary data, some industry-wide data that could be useful for cost calculations is readily available online. The U.S. Census Bureau conducts an economic census every five years and publishes its data online, including total annual payroll, the number of employees, the number of firms, and the value of sales, shipments, receipts, revenue, or business done. Dividing annual payroll or the value of revenue by the number of businesses or establishments will yield the average, industry-wide per-business payroll and revenue, which can be multiplied by 0.01 or 0.003 respectively to generate the amount that would constitute a more-than-minor cost for the average business in the industry (not accounting for size).

Finally, some straightforward tools, such as a calculating spreadsheet, could help agency employees calculate costs. For example, we developed an Excel minor cost calculator spreadsheet using data available from the U.S. Census. A detailed description of how to access the specific data and an illustration of the spreadsheet are in **Appendix F**.

State agencies can access U.S. Census data at <http://factfinder.census.gov/faces/nav/jsf/pages/searchresults.xhtml>.

Business associations can help agencies get information they need from small business owners

To better understand business owners' understanding of the RFA's requirements, and to learn more about their expectations for participating in rulemakings, we distributed a questionnaire through two business associations: Washington's chapter of the National Federation of Independent Businesses and the Independent Business Association. We also met with representatives from eight business associations.

Slightly more than half of the business owners who responded to our questionnaire said they would like to be more involved in agencies' determinations of cost impacts to their companies, but very few of them had ever been involved in agency rulemaking.

Representatives from the business associations we met with described various barriers to business owner involvement, including their lack of available time to participate and difficulty establishing good contacts with agency staff. They told us small business owners typically look to associations to represent their interests, but noted that agencies rarely asked them for advice or information.

They suggested agencies could work with industry groups to survey their members, send representatives to association meetings so members could provide feedback to agency staff, and meet with them outside the rulemaking process to gather input from business owners and data on regulated industries. While it might require time and effort up front, in the long run, working more closely with these associations could reduce agency staff time and the cost of administering surveys, and could improve response rates by businesses.

Inter-agency communication and cooperation could help develop expertise across the state

In our discussions with agency staff, we found several had gained expertise or had knowledge of agency information that could help other agencies with the cost estimates required by the RFA. For example, employees in one agency told us they found it very hard to access data for a particular industry, but staff at another agency showed us detailed data they had gathered for that same industry. Staff members at various agencies said it would be easier to meet the requirements of the RFA if they had access to information available at other agencies, especially related to revenue and employment.

Also, one agency representative suggested that standardizing costs and formats to guide cost estimates would help improve accuracy. For example, agencies consistently struggled to estimate costs if the data varied depending on decisions made by business owners: basic examples and templates would make it easier to model various scenarios. Another agency representative proposed additional economic impact models and greater access to economists who could help agencies meet requirements in the RFA. At present, however, the state does not have a single central authority to provide or coordinate this kind of support or oversight.

Agencies could improve their filings with support and oversight from a central entity

While no single agency or office possesses authority for reviewing agency filings or for providing templates and guidance across agencies, this has not always been the case. Before 1996, the Regulatory Fairness Act charged the Business Assistance Center within the Department of Community, Trade, and Economic Development (now the Department of Commerce) with these responsibilities, and allowed agencies to ask for its help in preparing an SBEIS. The Legislature eliminated the Business Assistance Center in 1995 (effective the following year), and struck the provisions of the RFA associated with its oversight and support. It has not delegated those responsibilities to another agency.

One business association representative believes the current lack of oversight contributes to agencies not meeting the requirements of the RFA. In 2007, the Legislature gave the Joint Administrative Rules Review Committee the authority to review SBEIS, and gave citizens the ability to petition this committee to do so. This appears to support the view that the Legislature recognizes the need for accountability.

Beyond the need for a centralized entity to support agencies, agencies themselves have recognized they need to provide centralized support within their own organizations. For example, within some agencies, program managers may be responsible for writing new rules for their programs, and are less likely to understand the complex requirements of the RFA. Managers at one agency suggested that a centralized rulemaking function within the agency is best suited to ensuring proposed rules are consistent with the RFA. In addition, managers at another agency told us that they find it consistently challenging to ensure that staff with technical expertise engage in basic economic thinking when initiating new rules. Agencies suggested more centralized coordination within and across agencies could help staff share information and expertise to improve their proposed rule filings.

Recommendations

To ensure agencies meet all requirements of the Regulatory Fairness Act, we recommend the Legislature:

1. Make the following clarifications in the Act:
 - a. A proposed rule is exempt from the Act if the proposing agency can demonstrate that it affects only businesses with more than 50 employees
 - b. A proposed rule that affects only small businesses inherently imposes disproportionate costs, and the proposing agency must consider all cost mitigation options defined in the Act
 - c. In the absence of sufficient data to calculate the disproportionate impacts, an agency whose rule imposes more-than-minor cost must mitigate the costs to small businesses, where legal and feasible, as defined in the Act
2. Require the Code Reviser to:
 - a. Modify the proposed rule form (CR-102) to include a checklist of allowable exemptions
 - b. Provide access to an SBEIS template that includes all required information
3. Assign a central entity to:
 - a. Collaborate with and provide support to state agency employees to help them meet the requirements of the law. Such support could include:
 - Providing online guidance and tools to help agency staff understand and complete the requirements
 - Providing access to available cost data
 - Facilitating sharing of information among agencies and between agencies and business associations
 - b. Hold agencies accountable for ensuring all proposed rules meet the requirements of the law

Agency Response



STATE OF WASHINGTON
OFFICE OF FINANCIAL MANAGEMENT

Insurance Building, PO Box 43113 • Olympia, Washington 98504-3113 • (360) 902-0555

December 21, 2016

The Honorable Troy Kelley
Washington State Auditor
P.O. Box 40021
Olympia, WA 98504-0021

Dear Auditor Kelley:

On behalf of the audited agencies, thank you for the opportunity to review and respond to the State Auditor's Office (SAO) performance audit report, "Assessing Implementation of the Regulatory Fairness Act." The Office of Financial Management worked with the Gambling Commission, Liquor and Cannabis Board, Washington State Patrol, Washington Utilities and Transportation Commission, and the departments of Agriculture, Early Learning, Ecology, Fish and Wildlife, Health, Labor and Industries, Licensing, Revenue, Social and Health Services and Transportation to provide this consolidated response.

We appreciate the SAO's efforts to determine whether agencies are fulfilling Regulatory Fairness Act (RFA) requirements when proposing rules and whether there are opportunities for the state to improve. We are committed to the RFA's intent of reducing the disproportionate cost to small businesses to comply with state administrative rules. We believe the concepts and tools in the SAO's recommendations to the Legislature could strengthen processes that would benefit small businesses and agencies. We support and would like to be part of the effort to refine and develop tools that could be used successfully by all agencies.

Nevertheless, we are concerned that your recommendation to revise the law is premature. Before the Legislature considers specific changes to the RFA or the Office of the Code Reviser modifies rulemaking forms such as the CR-102, we urge the Legislature to gather additional information about how any proposed changes to the RFA, or alternative statutes, would impact small businesses and the agencies that serve them. What may seem like simple changes to the law may have unintended consequences. For example, the suggested minor cost estimation methodology could result in reducing the number of analyses completed under the RFA. In addition, a one-size-fits-all solution may be problematic given the differences between agencies and small businesses affected by individual agency rulemaking.

We also note the limited scope of the audit. Some of the SAO's findings were based on its own legal review and advice. The audit did not consider the legal advice agencies received from their assigned assistant attorneys general or how that advice affects agency analysis of obligations and the corresponding impacts on small businesses. Obtaining a single legal interpretation from the



The Honorable Troy Kelley
December 21, 2016
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Attorney General's Office would better inform the Legislature and state agencies of the current meaning of the RFA and the need for any clarifications or revisions.

Another limitation of the SAO report is that it focuses almost entirely on the small business economic impact statement (SBEIS) procedures at the end of the rulemaking process. The report does not describe the due process components of rulemaking required by the Administrative Procedures Act (APA). The APA has requirements for public notice, participation and input. These actions mitigate impact to businesses because input is sought and considered while rules are being developed and finalized. Agencies spend considerable time and effort working with stakeholders early in the rule drafting process to address and mitigate impacts prior to developing the SBEIS required by the RFA. Much of that effort occurs prior to filing the rules and is documented in the rulemaking file, which this audit did not take into account.

Resources and assistance toward rulemaking vary across agencies. We appreciate the SAO's recognition of several agencies using leading practices that could benefit other agencies. Those examples will be a good starting point to further refine and develop some standard tools and trainings that all agencies could use.

As a next step, the Governor's Office plans to invite rulemaking agencies, small business customers, stakeholders and representatives from the Office of the Attorney General and Office of the Code Reviser to better understand how any proposed changes to the act, or alternative statutes, would impact small businesses and agencies. Convening a robust workgroup such as this could also help increase consistency in how agencies follow the RFA and allow them to participate in efforts to refine and develop standardized implementation tools.

Currently, the RFA guides agencies in performing rulemaking analyses suited to each agency's unique customers and situations. This allows agencies to incorporate concerns from stakeholders related to particular situations while maintaining statutory goals of protecting health, safety and the environment. Despite best efforts, there are times when agencies cannot and should not mitigate the impact of rules on small business if that impact is necessary for the agency to comply with statutory requirements or goals. The RFA allows that flexibility so long as the agency provides a clear and reasonable explanation.

As you know, agencies must strike a balance between maintaining the intent of the regulations mandated by law and limiting the costs to businesses. We look forward to working with small business stakeholders to improve the state's rulemaking activities.

Sincerely,



David Schumacher
Director

The Honorable Troy Kelley
December 21, 2016
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cc: David Postman, Chief of Staff, Office of the Governor
Kelly Wicker, Deputy Chief of Staff, Office of the Governor
Matt Steuerwalt, Director, Executive Policy Office
Roselyn Marcus, Assistant Director, Office of Financial Management
Scott Merriman, Legislative Liaison, Office of Financial Management
Rich Roesler, Acting Director, Results Washington, Office of the Governor
Tammy Firkins, Performance Audit Liaison, Results Washington, Office of the Governor
Derek Sandison, Director, Department of Agriculture
Maia Bellon, Director, Department of Ecology
John Wiesman, Secretary, Department of Health
Pat Kohler, Director, Department of Licensing
Rick Garza, Director, Liquor and Cannabis Board
Vikki Smith, Director, Department of Revenue
John Batiste, Chief, Washington State Patrol
Steve King, Executive Director, Utilities and Transportation Commission
Roger Millar, Secretary, Department of Transportation
Pat Lashway, Acting Secretary, Department of Social and Health Services
Joel Sacks, Director, Department of Labor and Industries
Jim Unsworth, Director, Department of Fish and Wildlife
Ross Hunter, Director, Department of Early Learning
David Trujillo, Director, Gambling Commission

Appendix A: Initiative 900

Initiative 900, approved by Washington voters in 2005 and enacted into state law in 2006, authorized the State Auditor’s Office to conduct independent, comprehensive performance audits of state and local governments. Specifically, the law directs the Auditor’s Office to “review and analyze the economy, efficiency, and effectiveness of the policies, management, fiscal affairs, and operations of state and local governments, agencies, programs, and accounts.” Performance audits are to be conducted according to U.S. Government Accountability Office government auditing standards.

In addition, the law identifies nine elements that are to be considered within the scope of each performance audit. The State Auditor’s Office evaluates the relevance of all nine elements to each audit. The table below indicates which elements are addressed in the audit. Specific issues are discussed in the Audit Results section of this report.

I-900 element	Addressed in the audit
1. Identify cost savings	Yes. We identified opportunities for cost savings at state agencies through reduced staff work resulting from clarification of requirements, provision of guidance and tools, and identification of ways to better access information needed to determine impacts on businesses.
2. Identify services that can be reduced or eliminated	Yes. We identified agencies that were preparing small business economic impact statements when they did not need to.
3. Identify programs or services that can be transferred to the private sector	No. Agencies are required by law to prepare a small business economic impact statement if the cost of the proposed regulatory change is more than minor. This cannot be transferred to the private sector.
4. Analyze gaps or overlaps in programs or services and provide recommendations to correct them	No. Each agency is required by law to do this analysis.
5. Assess feasibility of pooling information technology systems within the department	No. Our audit focused on whether or not agencies are preparing small business economic impact statements in accordance with the law, not the underlying information technology systems used to prepare them.
6. Analyze departmental roles and functions, and provide recommendations to change or eliminate them	Yes. This audit reviewed agencies’ internal processes to ensure staff meet the requirements of the Regulatory Fairness Act.
7. Provide recommendations for statutory or regulatory changes that may be necessary for the department to properly carry out its functions	Yes. This audit found areas where agency practices relied on either debatable or incorrect interpretations of the law. We recommend clarifying sections of the law, providing better direction on the CR-102 form, and assigning an entity for oversight and support.
8. Analyze departmental performance, data performance measures, and self-assessment systems	Yes. The lack of oversight contributed to lack of performance measures statewide. This audit was the first comprehensive review of agency implementation of the Regulatory Fairness Act.
9. Identify relevant best practices	Yes. We identified practices at state agencies that helped staff meet the requirements of the Act as well as practices in other states likely to help agencies with regulatory flexibility requirements.

Appendix B: Methodology

This performance audit examined agency implementation of the Regulatory Fairness Act (RFA). Research for the report focused on these questions:

1. Did state agencies fulfill all Regulatory Fairness Act requirements when proposing rules?
2. Are there opportunities for the state to improve implementation of the Regulatory Fairness Act?

To answer these questions, we evaluated all proposed rules published in the 2014 and 2015 state register, reviewed tools available to help agencies meet the requirements of the RFA, and sought input from business associations and small businesses about their experience with agency rulemaking processes.

Evaluation of proposed rules

Selecting proposed rules

We created a list of all proposed rules published in 2014 and 2015 by the 26 state agencies that regulate businesses in Washington. We only included proposed rules agencies filed with the Code Reviser on a CR-102. We did not include certain other rulemaking filings, such as Expedited Rules or Emergency Rules, because they are categorically exempt from the RFA and are not filed as proposed rules.

Also, we eliminated proposed rule filings that duplicated previous filings. When an agency changes the text of a proposed rule in the course of its development, they will file a supplemental notice. When they wish to extend the amount of time that the rulemaking is open, they will file a continuance. When they wish to withdraw the proposed rule, they will file a withdrawal. These are not distinct proposed rules; had we included them, we would have evaluated some proposed rules multiple times.

We then narrowed the scope of our audit to agencies that had proposed multiple rules and that regulate small businesses. The final list contained 502 proposed rules from 16 state regulatory agencies: Departments of Agriculture, Early Learning, Ecology, Fish and Wildlife, Health, Labor and Industries, Licensing, Natural Resources, Revenue, Social and Health Services, and Transportation; Gambling Commission; Liquor and Cannabis Board; Office of the Insurance Commissioner; State Patrol; and Utilities and Transportation Commission.

Finally, we reviewed all 502 proposed rules to determine which ones were likely to affect businesses. For example, we eliminated rules related to professional licenses or rules of general applicability such as a speed limit. This resulted in a final sample of 331 proposed rules.

Reviewing for RFA requirements

We reviewed the narrowed list of 331 proposed rulemakings and noted if they included a Small Business Economic Impact Statement (SBEIS), claimed to be exempt from the RFA (such as clarifying the language of an existing rule without changing the effect), or gave another reason for not conducting an SBEIS (such as the potential cost to business being less than the definition of minor costs).

Our preliminary review of Small Business Economic Impact Statements revealed that some agencies filed analyses labeled as a “Small Business Economic Impact Statement” where the analysis concluded the cost to business was less-than-minor. If the cost to business is less-than-minor, the agency is not responsible for filing an SBEIS, so we reviewed these documents as cost analyses because it would be unfair to hold the agency to the requirements of an SBEIS when the filing demonstrated one was not needed.

We evaluated all proposed rules that affected business in three stages.

1. We verified whether exemptions identified by agencies were consistent with the RFA.
 - A number of filings stated that a proposed rule did not affect small businesses and provided support for this claim. While this is not currently an allowable exemption, we understand that performing an analysis to determine whether costs are disproportionate between large and small business is not beneficial to the agency or to the small business community if no small businesses are affected by the rule. We set aside these rules in a separate category as not affecting small businesses.
2. When agency filings stated that an SBEIS was not required because the costs of the rule would be less-than-minor, we evaluated the documentation to see if it applied these four elements of a good cost analysis:
 - Did the agency identify the costs of the proposed rule to businesses?
 - Was that identification of costs consistent with the Regulatory Fairness Act's definition of minor costs?
 - Did the agency provide credible support? We considered support to be credible if the agency explained what they did to generate the costs, provided specific numbers or statistics, and described a plausible source for this data (for example, price quotes from a major retailer). Or, if the agency provided a qualitative analysis, we considered it to be credible if they had a plausible source for their information and clearly explained how they reached their conclusions (for example, an explanation of how the proposed rule would reduce requirements on businesses).
 - Did the agency reach a clear conclusion about whether costs are less-than-minor?
3. We evaluated rules in which agencies filed an SBEIS for whether they contained all the required information needed in an SBEIS under RCW 19.85.030 and RCW 19.85.040.

We did not review any proposed rules to determine whether an allowable exemption was properly applied. For example, if the agency stated that the content of the rules was explicitly and specifically dictated by statute, we did not return to the underlying statute to determine if the agency was correct in that assertion. Nor did we review the cost analyses agencies gave us to determine if they were correct. When we reviewed SBEIS, we reviewed them for the presence of the required analysis, but did not attempt to determine if the agency was correct in their conclusion that the proposed rule would or would not disproportionately impact small business. We considered it sufficient if an agency compared the costs between the 10 percent of affected businesses that are the largest and small businesses. Finally, we did not evaluate the quality or accuracy of the information contained in the SBEIS.

Also, our evaluation of proposed rules did not include a determination of how additional clarification, documentation or completion of requirements would ultimately affect the cost of any rule to small businesses.

Review of available tools to help agencies meet the requirements of the RFA

In addition to information on rules, we assessed available tools to help agencies meet the requirements of the RFA.

We reviewed available information on the Code Reviser's website and met with staff at the Office of the Code Reviser to gain an understanding of how they help agencies meet the RFA when filing proposed rules. We also reviewed the websites of other states' equivalent of the Code Reviser to see how they might be assisting agencies.

Additionally, we asked each agency to describe how it ensures that proposed rules meet the requirements of the RFA and to send us any guidance it gives agency staff to help them meet those requirements. We reviewed that guidance for errors and omissions, as well as practices that might be helpful at other agencies. Also, we sought agencies' perspectives on challenges they face obtaining required cost information, and gathered their suggestions on how the state can help them obtain better data and perform better analysis of that data, and their advice for other agencies.

Input from business associations and small businesses

We sought input from the business community to understand their perceptions regarding agency implementation of the RFA and usefulness of SBEIS.

We met with the following eight associations that represent small businesses to discuss their experiences with agency rules and with the SBEIS process: Building Industry Association, Independent Business Association, National Federation of Independent Businesses, Pest Management Association, Salmon for All, Shellfish Growers Association, Washington Association of Home Care Agencies, and Washington Farm Bureau.

We used a structured interview guide and asked:

- Are you or others in your association regularly involved in state regulatory agency rulemaking?
- Do you do any kind of facilitation with your members to help them be involved in rulemaking?
- Have you or anyone in your association ever been contacted by a state regulatory agency asking for information to determine whether a proposed rule will impose more-than-minor costs on businesses?
- Have you or anyone in your association ever been asked to provide input into the preparation of an SBEIS?
- Do you ever access SBEIS forms that agencies have prepared?
 - Do you think they are helpful?
 - How could they be more helpful?
- Do you think your members would be interested in being more involved in the preparation of an SBEIS?

Six of the associations we met with represent specific economic sectors; two represent a broad array of industries. The latter two agreed to send their members our questionnaire asking about their experience with agency rulemaking. We asked business owners about their dealings with agency staff, their involvement with agency rulemaking processes, and their awareness of small business economic impact statements. Forty-three small business owners responded to the questionnaire during its open period from April 25 to August 16, 2016.

Appendix C: Exemptions from the RFA

A dozen laws or subsections address exemptions from the Regulatory Fairness Act

Rules are exempt if they:	RCW	Text of the RCW
Are expedited rules	19.85.025	(1) Unless an agency receives a written objection to the expedited repeal of a rule, this chapter does not apply to a rule proposed for expedited repeal pursuant to [RCW 34.05.353]. If an agency receives a written objection to expedited repeal of the rule, this chapter applies to the rule-making proceeding.
		(2) This chapter does not apply to a rule proposed for expedited adoption under [RCW 34.05.353], unless a written objection is timely filed with the agency and the objection is not withdrawn.
	34.05.353	(3) The expedited rule-making process must follow the requirements for rule making set forth in RCW 34.05.320, except that the agency is not required to prepare a small business economic impact statement under RCW 19.85.025.
Are emergency rules	19.85.025	(3) This chapter does not apply to the adoption of a rule described in RCW 34.05.310(4).
	34.05.310	(4)(a) Emergency rules adopted under RCW 34.05.350.
Relate only to internal governmental operations	19.85.025	(3) This chapter does not apply to the adoption of a rule described in RCW 34.05.310(4).
	34.05.310	(4)(b) Rules relating only to internal governmental operations that are not subject to violation by a nongovernment party.
Adopt federal or state laws or regulations by reference without material change	19.85.025	(3) This chapter does not apply to the adoption of a rule described in RCW 34.05.310(4).
	34.05.310	(4)(c) Rules adopting or incorporating by reference without material change federal statutes or regulations, Washington state statutes, rules of other Washington state agencies, shoreline master programs other than those programs governing shorelines of statewide significance, or, as referenced by Washington state law, national consensus codes that generally establish industry standards, if the material adopted or incorporated regulates the same subject matter and conduct as the adopting or incorporating rule.
Make typographical or clarifying changes without changing the effect	19.85.025	(3) This chapter does not apply to the adoption of a rule described in RCW 34.05.310(4).
	34.05.310	(4)(d) Rules that only correct typographical errors, make address or name changes, or clarify language of a rule without changing its effect.
Have content explicitly dictated by statute	19.85.025	(3) This chapter does not apply to the adoption of a rule described in RCW 34.05.310(4).
	34.05.310	(4)(e) Rules the content of which is explicitly and specifically dictated by statute.
Set or adjust fees or rates according to legislative standards	19.85.025	(3) This chapter does not apply to the adoption of a rule described in RCW 34.05.310(4).
	34.05.310	(4)(f) Rules that set or adjust fees under the authority of RCW 19.02.075 or that set or adjust fees or rates pursuant to legislative standards, including fees set or adjusted under the authority of RCW 19.80.045.

Rules are exempt if they:	RCW	Text of the RCW
Relate to the process of agency hearings or applying for a license or permit	19.85.025	(3) This chapter does not apply to the adoption of a rule described in RCW 34.05.310(4).
	34.05.310	(4)(g) Rules that adopt, amend, or repeal: (i) A procedure, practice, or requirement relating to agency hearings; or (ii) A filing or related process requirement for applying to an agency for a license or permit.
Include a cost-benefit analysis with all requirements of an SBEIS	19.85.025	(4) An agency is not required to prepare a separate small business economic impact statement under RCW 19.85.040 if it prepared an analysis under RCW 34.05.328 that meets the requirements of a small business economic impact statement, and if the agency reduced the costs imposed by the rule on small business to the extent required by RCW 19.85.030(3). The portion of the analysis that meets the requirements of RCW 19.85.040 shall be filed with the code reviser and provided to any person requesting it in lieu of a separate small business economic impact statement.
Complete the pilot rule process	19.85.030	(1)(a)(ii) ... However, if the agency has completed the pilot rule process as defined by RCW 34.05.313 before filing the notice of a proposed rule, the agency is not required to prepare a small business economic impact statement.
Are adopted by a referendum under the Agricultural Enabling Act	15.65.570	(2) Rule-making proceedings conducted under this chapter are exempt from compliance with RCW 34.05.310, chapter 19.85 RCW, the regulatory fairness act, and RCW 43.135.055 when the adoption of the rules is determined by a referendum vote of the affected parties.

Source: Revised Code of Washington, www.leg.wa.gov.

Appendix D: Changes to the CR-102 form

The current format of the CR-102 form, supplied by the Office of the Code Reviser (shown in **Figure 1**), leaves agency employees to determine for themselves the possible exemptions that apply to the rule they are proposing. To help agency staff with this process, we have drafted a revision of the form that lists all currently allowable exemptions, shown in **Figure 2** (on the following page). Providing exemptions in a checklist makes it more likely employees would identify and select the exemption applicable to the rule they are proposing.

Figure 1 – The current form, although short, leaves agencies to guess at content

Has a small business economic impact statement been prepared under chapter 19.85 RCW or has a school district fiscal impact statement been prepared under section 1, chapter 210, Laws of 2012?

Yes. Attach copy of small business economic impact statement or school district fiscal impact statement.

A copy of the statement may be obtained by contacting:

Name: _____

Address: _____

phone () _____

fax () _____

e-mail _____

No. Explain why no statement was prepared.

Figure 2 – Our proposed revision offers more guidance

Regulatory Fairness Act cost considerations

This rule proposal **may be exempt** from requirements of the Regulatory Fairness Act (see RCW 19.85). Please check these statements to see if it qualifies for exemption:

This rule is exempt under RCW 19.85.061 because this rulemaking is being adopted solely to conform or comply or both with federal statute or regulations. Please cite the specific federal statute or regulation this rule is being adopted to conform or comply with, and describe the consequences to the state if the rule is not adopted.

[form field for text] _____

This rule is exempt because the agency has completed the pilot rule process defined by RCW 34.05.313 before filing the notice of this proposed rule.

This rule is exempt because it was adopted by referendum under the provisions of RCW 15.65.570(2).

This rule is exempt under RCW 19.85.025(3). Check all that apply:

RCW 34.05.310(4)(b)

RCW 34.05.310(4)(e)

RCW 34.05.310(4)(c)

RCW 34.05.310(4)(f)

RCW 34.05.310(4)(d)

RCW 34.05.310(4)(g)

If the proposed rule is **not exempt**, does it impose more-than-minor costs (as defined by RCW 19.85.020(2)) on businesses?

No – Briefly summarize the agency’s analysis showing how costs were calculated.

[form field for text] _____

Yes – Calculations showed the rule imposed more than-minor cost to businesses, and a small business economic impact statement is attached as required.

Is a School District Impact Statement required?

No

Yes – The statement is attached as required.

The public may obtain a copy of the statement by contacting:

Name: _____

Address: _____

phone () _____

fax () _____

e-mail _____

Appendix E: Sample SBEIS Template

Small Business Economic Impact Statement	WAC [246-XX-XXX] A Rule Concerning [X]																				
Date:																					
<p>1. Describe the proposed rule, including:</p> <ul style="list-style-type: none"> • a brief history of the issue • an explanation of why the proposed rule is needed • a brief description of the probable compliance requirements and the kinds of professional services that a small business is likely to need in order to comply with the proposed rule 																					
<p>2. Identify which businesses are required to comply with the proposed rule using the North American Industry Classification System (NAICS) codes and what the minor cost thresholds are.</p> <table border="1" style="width: 100%; border-collapse: collapse; margin-top: 10px;"> <thead> <tr> <th style="width: 15%;">NAICS code (4, 5 or 6 digit)</th> <th style="width: 25%;">NAICS business description</th> <th style="width: 15%;"># of businesses in WA</th> <th style="width: 20%;">Minor-cost threshold = 1% of average annual payroll</th> <th style="width: 25%;">Minor-cost threshold = 0.3% of average annual receipts</th> </tr> </thead> <tbody> <tr> <td> </td> <td> </td> <td> </td> <td> </td> <td> </td> </tr> <tr> <td> </td> <td> </td> <td> </td> <td> </td> <td> </td> </tr> <tr> <td> </td> <td> </td> <td> </td> <td> </td> <td> </td> </tr> </tbody> </table>		NAICS code (4, 5 or 6 digit)	NAICS business description	# of businesses in WA	Minor-cost threshold = 1% of average annual payroll	Minor-cost threshold = 0.3% of average annual receipts															
NAICS code (4, 5 or 6 digit)	NAICS business description	# of businesses in WA	Minor-cost threshold = 1% of average annual payroll	Minor-cost threshold = 0.3% of average annual receipts																	
<p>3. Analyze the probable cost of compliance. Identify the probable costs to comply with the proposed rule, including: cost of equipment, supplies, labor, professional services and increased administrative costs. Based on input, describe how compliance with the rule may cause lost sales or revenue.</p>																					
<p>4. Explain how you determined the rule may impose more-than-minor costs on businesses in the industry.</p>																					

5. Determine whether the proposed rule may impose a disproportionate impact on small businesses compared to the 10 percent of businesses that are the largest businesses required to comply with the proposed rule.

Use one or more of the following as a basis for comparing costs:

- Cost per employee
- Cost per hour of labor
- Cost per one hundred dollars of sales

6. If the proposed rule is likely to impose a disproportionate impact on small businesses, identify the steps taken to reduce the costs of the rule on small businesses. Include consideration of each of the following cost mitigation strategies:

- (a) Reducing, modifying, or eliminating substantive regulatory requirements
- (b) Simplifying, reducing, or eliminating recordkeeping and reporting requirements
- (c) Reducing the frequency of inspections
- (d) Delaying compliance timetables
- (e) Reducing or modifying fine schedules for noncompliance
- (f) Any other mitigation techniques suggested by small businesses or their advocates

If the costs cannot be reduced, provide a clear explanation of why.

7. Describe how small businesses were involved in the development of the proposed rule.

8. Identify the estimated number of jobs that will be created or lost as the result of compliance with the proposed rule.

9. Summarize the results of the analysis, including the determination if costs are disproportionate.

Appendix F: Minor-cost Threshold Calculators

Agencies are required to prepare a small business economic impact statement if the proposed rule will impose a more-than-minor cost on businesses in an industry. For agencies other than the Department of Social and Health Services, a minor cost is defined as the greater of: 0.3 percent of revenue, or \$100, or 1 percent of payroll.

To determine whether costs are more-than-minor, agencies must calculate 1 percent of payroll or 0.3 percent of revenue for the businesses in the affected industries. The U.S. Census Bureau's Economic Census of the United States provides payroll and revenue by industry for non-agricultural industries. For agricultural industries, we used the payroll information from the U.S. Department of Labor's Quarterly Census of Employment and Wages.

We created a calculator that can help agencies determine what level of cost to business would exceed 1 percent of payroll or 0.3 percent of revenue. In addition to the examples illustrated in Figures 3 and 4, we have posted the Excel spreadsheet on our website at www.sao.wa.gov/state/Pages/RegReform.aspx. Instructions for using the calculator are posted in the spreadsheet but are also described on the following page.

Figure 3 – Illustration of minor-cost calculator: Agricultural industries

Industry description	Industry 4-digit or 6-digit 2012 NAICS Code	NAICS Code definition	Number of establishments	Total annual payroll	Avg annual payroll	1% of avg annual payroll	Data source	Year of data source
Agency staff fill in. Should closely match NAICS Code definition	Agency staff fill in	Column auto-fills	Column auto-calculates	Column auto-calculates	Column auto-calculates	Column auto-calculates	Column auto-fills	Column auto-fills
Apple growers	111331	Apple orchards	885	\$637,673,814.00	\$720,535.38	\$7,205.35	Q'tly Census of Empl & Wages (BLS)	2015
Cattle ranchers	112111	Beef cattle ranching and farming	247	\$16,833,593.00	\$68,152.20	\$681.52	Q'tly Census of Empl & Wages (BLS)	2015
Goat farmers	112420	Broilers and meat type chicken production	12	\$825,495.00	\$68,791.25	\$687.91	Q'tly Census of Empl & Wages (BLS)	2015
Loggers	113310	Logging	453	\$190,934,913.00	\$421,489.87	\$4,214.90	Q'tly Census of Empl & Wages (BLS)	2015

Figure 4 – Illustration of minor-cost calculator: Non-agricultural industries

Industry description	Industry 4-digit or 6-digit 2012 NAICS Code	NAICS Code definition	Number of establishments	Total annual payroll	Total annual revenue	Avg annual payroll	Avg annual revenue	1% of avg annual payroll	0.3% of avg annual revenue	Data source	Year of data source
Agency staff fill in. Should closely match NAICS Code definition	Agency staff fill in	Column auto-fills	Column auto-calculates	Column auto-calculates	Column auto-calculates	Column auto-calculates	Column auto-calculates	Column auto-calculates	Column auto-calculates	Column auto-fills	Column auto-fills
Casinos	713210	Casinos (except casino hotels)	39	\$329,172,000.00	\$1,384,580,000.00	\$8,440,307.69	\$35,502,051.28	\$84,403.08	106506.1538	Economic Census of the U.S.	2012
Coffee manufacturers	311920	Coffee and tea manufacturing	45	\$39,323,000.00	\$592,021,000.00	\$873,844.44	\$13,156,022.22	\$8,738.44	39468.06667	Economic Census of the U.S.	2012
Home furnishing wholesalers	423220	Home furnishing merchant wholesalers	157	\$99,955,000.00	\$1,091,743,000.00	\$636,656.05	\$6,953,777.07	\$6,366.56	20861.33121	Economic Census of the U.S.	2012
Jewelry retailers	448310	Jewelry stores	423	\$72,067,000.00	\$455,864,000.00	\$170,371.16	\$1,077,692.67	\$1,703.71	3233.078014	Economic Census of the U.S.	2012
Paper mills	322121	Paper (except newsprint) mills	5	\$134,449,000.00	#VALUE!	\$26,889,800.00	#VALUE!	\$268,898.00	#VALUE!	Economic Census of the United States	2012

To use the minor cost threshold calculator, agency staff take the following steps:

1. Open the calculator, which is an Excel spreadsheet, and enter the “Industry Description” in the first column. Add rows for all industries that will be subject to the proposed regulation. Note: the spreadsheet will show errors in all cells at first until the next step is completed.
2. Look up the 4- or 6-digit North American Industry Classification System (NAICS) code that applies to the first industry in the list, and enter it in the second column, titled “Industry 4- or 6-digit 2012 NAICS Code.”
3. The third column, “NAICS Code Definition,” populates automatically. The first and third columns should be similar to each other. If they are very different, and the NAICS code does not at all describe the industry being regulated, check the code number you selected and consider others until you find a close match. (See circled row in Figure 3.)
4. Once the NAICS code is filled in, the calculator will populate all remaining fields.
5. You now have the data needed to choose the threshold for comparing more-than- or less-than-minor costs to businesses. These columns are titled:
 - “1% of Avg Annual Payroll”
 - “0.3% of Avg Annual Revenue”
6. If 0.3 percent of average annual revenue in the industry is less than \$100, then you should use \$100 per business as the definition of a minor cost. This is an unlikely scenario, but represents the appropriate time to use a threshold of \$100 to compare the costs of the regulation against. Agencies may always choose to use 1 percent of annual payroll as the threshold.
7. It may be that a field does not fill in for any given industry. (See circled row in Figure 4.) This is because the U.S. Census suppresses some data for confidentiality reasons in industries with a small number of businesses. If this happens, you should use whichever threshold can be calculated.
For example, if the rule regulates medical equipment manufacturers – NAICS Code 3391 – annual revenues cannot be calculated, but payroll can. In this case, you would use the payroll number for the definition of minor costs.
8. If both the revenue and payroll are suppressed, then you must find a different source for the necessary information, including other data sets and working with businesses.

A full list of NAICS codes can be found at <https://www.census.gov/cgi-bin/sssd/naics/naicsrch?chart=2012>

Note: Because the Economic Census of the United States does not include agricultural industries, we created a separate calculator on the same spreadsheet for agricultural, farming, fishing and forestry industries. This calculator uses the U.S. Department of Labor’s Quarterly Census of Employment and Wages (QCEW), which does not include data on revenue. The QCEW will work for any industry and is subject to data limitations similar to those in the Economic Census of the United States and is an acceptable source for non-agricultural agencies. We decided not to use it across the board because it does not include an estimate of annual revenues.

As with the first calculator, fill in the first column with an industry description and the second with the appropriate NAICS code, and check to make sure the two closely match.