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Congress of the United States
House of Representatives
107th Congress
Committee on Small Business
2361 Rayburn House Office Building
Washington, DC 20515-6315

July 8, 2004

VIA E-MAIL
Mr. Gary M. Jackson
Assistant Administrator for Size Standards
United States Small Business Administration
409 Third Street, S.W., Mail Code 6530
Washington, DC 20416

RE: Small Business Size Standards; Restructuring of Size Standards, 69 Fed. Reg. 13,130 (March 19, 2004)

Dear Mr. Jackson:

On March 19, 2004, the Small Business Administration (SBA) promulgated regulations to modify all of its small business size standards, 69 Fed. Reg. 13,130 (2004) (hereinafter referred to as "Proposed Rule" or "NPRM"). On July 1, 2004, the SBA withdrew the proposed rule. *Id*. at 39,874. The Committee applauds the agency for taking this appropriate step and starting the process over in a much more deliberative manner.

Despite the withdrawal of the rule, the Committee still feels it is necessary to file comments on the withdrawn rule. Modification to SBA size standards have significant implication for SBA programs, federal procurement opportunities for small businesses, the Regulatory Flexibility Act, Executive Order No. 12,866, and federal regulatory programs in which the term "small business" is used. The Committee was highly troubled by the proposed rule on legal grounds that are conflated with significant policy concerns. The Committee finds that the proposed rule: a) failed to follow longstanding interpretations of the Small Business Act; b) did not comport with SBA's own size standard regulations; c) was not supported by an adequate regulatory flexibility analysis as required by the Regulatory Flexibility Act, 5 U.S.C. §§ 601-12, (RFA); d) constituted an irrational regulation because it did not achieve the objectives sought by the SBA in promulgating the rule; and e) represented bad policy because it modified size standards otherwise applicable to other federal agency regulatory programs without undertaking an assessment of the rule's impact on those programs. The Committee is filing these comments and requests that they be included in the record of the withdrawn rule and incorporated, along with the comments already filed or that are filed by the close of business on commences with respect to a general revision to the size standards. The Committee still believes that the most appropriate action has already been taken by the SBA – withdrawal and starting the process over with an advanced notice of proposed rulemaking followed by hearings in the regional offices before a proposed rule is republished. In addition, we strongly urge the SBA to work closely with the Office of Advocacy and the Office of Information and Regulatory Affairs (OIRA) at the Office of Management and Budget to identify those federal programs that use the SBA's size standards, refer to the term "small business concern" or otherwise directly address the concept of small business in statutory or regulatory language. Following the guideposts of these comments and undertaking a truly deliberative rulemaking process should result in a rule that is legally sufficient, withstands judicial scrutiny, and does not force Congress to take appropriate ameliorative action.

I. The Small Business Act – Statutory Background to the Proposed Rule

Section 3(a)(1) of the Small Business Act, 15 U.S.C. § 632(a)(1), provides, in pertinent part:

> [a] small business concern ... shall be deemed to be one that is independently owned and operated and which is not dominant in its field of operation.

The Act does not define the terms "independently owned and operated" or "dominant in its field of operation." Instead, the Administrator is authorized to:

> specify detailed definitions or standards by which a business concern may be determined to be small for purposes of this Act or *any other Act*.

15 U.S.C. § 632(a)(2)(A) (emphasis added). The Administrator is authorized to consider number of employees, dollar volume of business,[1] net worth,[2] net income, other factors, or any combination of those factors. In short, Congress has granted the Administrator substantial discretion in the factors that will be utilized in calculating the size of a small business. The SBA's discretion is tempered by the fact that any size standard determined by the factors set forth in § 3(a)(2) of the Small Business Act must meet the overarching principle – the business must be independently owned and operated and not dominant in its field.

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[1] Current SBA size standards use gross revenue as a measure of dollar volume. Nothing in the Act requires reliance on dollar volume and other measures could be used.

[2] The net worth standard is used, for among other purposes, to determine eligibility for investments made by small business investment companies, loans made pursuant to Title V of the Small Business Investment Act of 1958, and for participation in the program established by § 8(a) of the Small Business Act.

II. SBA's Exercise of Discretion Prior to the Proposed Rule

The SBA took the authority granted by Congress and developed size standards for individual categories of small businesses. Originally, the size standards were developed based on four-digit classifications of each type of business using Standard Industrial Classifications or SIC codes. When the federal government moved to the more exact North American Industrial Classification System or NAICS for data collection, the SBA modified its size standards to fit the new NAICS codes.

Historically, the SBA utilized two distinct standards for determining whether a business was not dominant in its field.[3] Manufacturers, distributors, and certain utilities[4] were measured by the number of employees. All other businesses, both services and retail establishments, are calculated by the gross revenue of the firm. The two standards never overlapped. If the SBA determined that a particular industry was measured by gross revenue, the SBA also did not impose an employee threshold. Thus, the SBA created a bright line standard in which a business either was required to enumerate employees or tabulate gross revenue. Until the issuance of this proposed rule, the SBA has not varied from that bright line standard.

Congress did not expect that the determinations of size would be etched into tablets on Mount Sinai. By using the ambiguous term "independently owned and operated and not dominant in its field," Congress expected that determinations would be updated on a regular basis. And, in fact, the SBA regularly revises its size standards. Those revisions are guided by its regulations that provide, in pertinent part:

> (a) SBA considers economic characteristics comprising the structure of an industry, including degree of competition, average firm size, start-up costs and entry barriers, and distribution of firms by size. It also considers technological changes, competition from other industries, growth trends, historical activity within an industry, unique factors in occurring the industry which may distinguish small firms from other firms, and objectives of its programs and the impact on those programs of different size standard levels.
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> (b) As part of its review of a size standard, SBA will investigate if any concern at or below a particular standard would be dominant in the industry. SBA will take into account consideration market

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[3] These comments will focus on the "dominance" criterion in § 3(a) because the proposed rule makes no modifications to the affiliation standards that the SBA utilizes to ascertain whether a business is independently owned and operated.

[4] Determinations of non-dominance in electric utilities have always been based on the amount of electricity generated during one calendar year by all plants owned by the electric utility.

> share of a concern and other appropriate factors which may allow a concern to exercise a major controlling influence on a national basis in which a number of business concerns are engaged. Size standards seek to *ensure that a concern that meets a specific size standard is not dominant in its field of operation*.

13 C.F.R. § 121.102(a)-(b) (emphasis added). [5]

The SBA regularly establishes or revises specific size standards and applies the requirements set forth in 13 C.F.R. § 121.102(a)-(b). Standard operating procedures (SOPs) issued by the SBA provide additional expatiation on the regulations. Specifically, these SOPs require that the SBA consider the impact of different size standards on SBA programs, whether a size standard excludes those businesses which are dominant in their field, and other relevant factors. *See* UNITED STATES SMALL BUSINESS ADMINISTRATION, STANDARD OPERATING PROCEDURES 90 01 3. Various factors are not weighted by the SBA, i.e., one factor does not bias the decision either for or against a particular size standard. Instead, the criteria are examined holistically to calculate or revise a size standard.

The last time the SBA made a comprehensive change to its size regulations (exclusive of conversion from SIC to NAICS and inflation adjustments) was 1984. The final rule published on February 9, 1984, 49 Fed. Reg. 5024, was preceded by two advanced notices of proposed rulemaking, public hearings in each of the SBA's ten regions, and a proposed rule published on May 6, 1983, 48 Fed. Reg. 20,560. During the rulemaking process, the SBA analyzed a wide variety of industries and the economic impact that rule changes would have on those industries, including their ability to obtain federal government contracts. In short, the four-year process for finalizing the size standard regulations enabled the SBA to examine the impact of different size standards on SBA programs, whether size standards excluding dominant firms, distribution of firms in a particular industry, the impact of an inflation adjustor on the size standards, and effect of those size standard changes on the ability of firms to obtain federal government contracts. Thus, the SBA complied with its rules and standard operating procedures for developing size standards.

In 1984, the SBA established size standards for financial institutions. 49 Fed. Reg. 40,398 (Oct. 16, 1984). The SBA reviewed several opinions on the size of banks and then examined the percentage of banks within various asset size ranges. In arriving at a result, the SBA reasoned that too small a standard would not incorporate a sufficient number of banks or

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[5] At one time, the SBA excluded from its regulations considerations of dominance on a national basis. This led to considerable confusion over whether businesses needed to be dominant in a particular region or on a national basis. In *California Dredging Co. v. Sanders*, 657 F. Supp. 38 (D.D.C. 1986), the court concluded that dominance may occur on a regional basis and, if so, then regionally dominant firms are not small businesses. *Id*. at 40. The SBA resolved this dilemma by modifying its regulations to make explicit that it measured dominance on a national basis. Nothing in *California Dredging* undercuts the regulatory amendment because the court noted that the statute is silent on the size of the area in which the business must be dominant.

bank assets[6] and that a size standard that was too large would result in only a few banks in each state exceeding the proposed size standard. One significant consideration in calculating the size standard was the determination that the "size standard excludes only the largest 15 percent of all financial institutions in the United States, which are clearly not in need of the benefits available by being categorized as small." *Id*.

Nearly 20 years later, the SBA issued a notice of proposed rulemaking to revise the size standard for the Facilities Support Services industry. 68 F.R. 5234 (Feb. 3, 2003). The SBA cited the evaluation factors specified in 13 C.F.R. § 121.102, as the key criteria in developing the revisied Facilities Support Services industry. Detailed analyses are provided of: average firm size, distribution of firms by size, start-up costs, industry competition,[7] and impact of the revision on SBA programs, including a separate assessment on the number of businesses in the industry that would gain or lose eligibility for loans made pursuant to § 7(a) of the Small Business Act. *Id*.

Thus, the SBA has adopted detailed criteria for determining the size of a business that is not dominant in its field. These standards have been in existence for at least 20 years and the SBA regularly uses[8] them to adopt bright-line standards within an industrial classification of a small business concern.

III. The Proposed Rule

The SBA issued a NPRM making significant changes to the size standards. The rules represent the first major overhaul of SBA size standards since 1984, exclusive of the changeover from SIC to the NAICS systems and modifications for inflation indexing.

The purpose of the proposed rule according to the SBA is to make them "more uniform and easier to use." 69 Fed. Reg. at 13,139. The SBA asseverates that the standards are complicated because there are multiple employee size standards and, in addition, multiple revenue standards. The SBA focuses particular attention on the complexity associated with the 30 different revenue-based size standards. *Id*. at 13,131. By eliminating the proliferation of revenue-based size standards, the SBA believes that they will make the size standards "less complicated." *Id*. The SBA achieves this regulatory objective through conversion of revenue-based size standards to a employee-based size standards. *Id*. According to the SBA, the

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[6] Although left unstated by the SBA, it appears that concerns about a too small size standard would not prove beneficial to "small banks."

[7] This is done by calculating the four-firm concentration ratio. The standard is the same one used as a starting point by the Department of Justice and the Federal Trade Commission in determining whether a specific merger of firms will violate the antitrust laws. This standard also is referred to as the Hirschman-Herfindahl or HHI index.

[8] Pursuant to a Lexis database search of the Federal Register, the SBA has revised size standards in 46 different industries from 1984 to the present using the rules established in 13 C.F.R. § 121.102.

utilization of employees as basis for size determinations will be particularly beneficial for those small businesses that compete in industry sectors in which currently one sector is an employee-based standard and the other sector is a revenue-based standard. *Id*.

The proposed rule also recognizes the possibility that an employee-based size standard could lead to abuse through subcontracting of nearly all the work thereby keeping the number of employees below the appropriate threshold. For these industries, the SBA believes that a combination of employees and revenues will prevent this gaming of the system. *Id*. at 13,135.

In converting to an employee-based standard, the SBA uses its existing regulation, 13 C.F.R. § 121.106, that counts full-time and part-time employees on an equivalent basis.[9] The conversion also utilizes 1997 Bureau of the Census data to calculate a receipts per employee ratio for each industry and then applies an inflation factor to arrive at the correct ratio. The SBA then adopts that ratio as the basis for converting to employees and comes up with 50 employees as the "anchor"[10] standard for non-manufacturing businesses converting from the existing "anchor" standard of $6 million in gross revenue. *Id*. at 13,132. The SBA then adjusted the anchor standard based on existing differences from the existing revenue-based "anchor" standard. *Id*.

The proposed rule makes no changes to existing employee-based size standards for manufacturers despite the significant alterations in the economic landscape on manufacturing in the past 20 years. While making no general changes to the manufacturing size standards, the SBA did modify the size standard for petroleum refiners to incorporate a refining capacity of 125,000 barrels per day in addition to the 1,500 employee standard. *Id*. at 13,136. The SBA also modified the size standard for tire manufacturers by eliminating the ceiling on the manufacturers share of the worldwide tire market. *Id*.

Three other general changes were made in specialized SBA size standards. The non-manufacturing rule[11] was reduced from 500 employees to 100 employees in order to comport these non-manufacturers with the existing standard for wholesale trade of 100 employees. The SBA raises the size standard for the purchase of special salvage timber from 25 to 50 employees but does not change eligibility for the overall timber set-aside program operated under a memorandum of understanding between the United States Department of Agriculture and the SBA. *Id*. at 13,137. For purposes of conformity, the SBA raised the size standard for leasing of

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[9] If the new size standard is 50 employees and the business, such as a restaurant, has 15 full-time employees and 45 part-time employees, the restaurant would not be considered a small business because it has 60 employees.

[10] Unless industry characteristics dictate otherwise, the SBA assigns all businesses within a particular two-digit NAICS sector the anchor standard.

[11] The non-manufacturing rule addresses the size standard of a business that provides a manufactured product to the government but does not manufacture the product itself. 13 C.F.R. § 121.406(b).

coal mining lands from the federal government from 250 to 300 employees and eliminate the separate revenue standard for the surety bond program.[12] *Id*. at 13,136-37.

Finally, the SBA did not modify certain existing dollar standards. A small business concern involved in agricultural enterprises remains at the statutorily-mandated level of $750,000. Nor does the SBA modify existing standards of net income and net worth for participation in the programs established by Titles III and V of the Small Business Investment Act of 1958.[13]

IV. The Proposed Rule Violates Long-Standing Interpretations of the Small Business Act Without an Adequate Explanation by the Agency

The Small Business Act provides the Administrator with the authority to promulgate regulations that define small business concerns. The Administrator's discretion is not unbridled and the regulations are not permitted to classify a business concern as small if the business is not independently owned and operated or is dominant in its field. *See California Dredging Co. v. Sanders*, 657 F. Supp. 38 (D.D.C. 1986).

The current proposal does not modify the SBA's affiliation rules and therefore does effect a change in the agency's interpretation of the term "independently owned and operated." The proposal changes the size standards for hundreds of NAICS codes and thus alters the categorization of the business concerns as dominant in their field. As will become clear, the SBA violated its longstanding interpretation of how it determines whether a business is dominant in its field without explaining the reason for the change.

The basic policy for establishing size standards has not changed for, at a minimum, thirty years. When the SBA last began a generic examination of its size standard regulations in the early 1980's, the SBA stated, in its second advanced notice of proposed rulemaking, that size standards "specifically reflect the structure of each individual industry."[14] In that same notice, the SBA went on to note that "[s]ize standards continue to be based on a detailed analysis of the industrial structure of each industry in question."[15] The final rules promulgated by the SBA, in 1984, incorporated that type of analysis with the following regulatory language:

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12 The only requirement for the surety bond program is that the business meet the existing size standard for that industry.

13 The alternative size standards for the Certified Development Company and the Small Business Investment Company program remain the same.

14 SMALL BUSINESS ADMINISTRATION, Small Business Size Standards; Size Standard Revisions, Second Advance Notice of Proposed Rulemaking, 47 FR 18,992 (May 3, 1982).

15 *Id*.

> Size standards vary by industry with particular attention to the structure of the designated industry.... Factors, among others, which are examined for the purpose of setting size standards include maximum size of firms, average firm size, the extent of industry dominance by large firms, the number of firms, the distribution by firm size of sales and employees in the industry, the presence of Federal procurement, and relation to other SBA programs.

13 C.F.R. 121.1(b) (1985). While the language is slightly different in the current version of the SBA's rules, *see supra* 13 C.F.R. § 121.102(a)-(b), the SBA size standard process has for at least 20 years revolved, first and foremost, around the structure of the industry.[16] The SBA's 1984 rules followed the practice from ten years earlier that factors involved in formulating size standards shall include, among other things, concentration of output,[17] ratios of the amount of output by the industry of its primary product in relation to the total output of that product by all industries (again a variation of firm concentration ratios), number of firms, and size of industry leaders. 13 C.F.R. § 121.3-1(b)(3) (1981), *citing* 39 Fed. Reg. 44,424 (Dec. 24, 1974). In sum, for at least 30 years, the SBA has focused its size standard calculations by examining the structure of the industry in order to determine which firms are dominant and which firms are not.

Agency regulations are not carved in granite ever immutable. Rules must be subject to modification in order to meet new circumstances or revisions in data that undergirded the regulation as originally drafted. *E.g.*, *FDA v. Brown & Williamson Tobacco Corp.*, 529 U.S. 120, 157 (2000); *Chevron, U.S.A., Inc. v. NRDC*, 467 U.S. 837, 842 (1984); *Motor Vehicle Manufacturers Ass'n of the United States v. State Farm Mut. Auto. Ins. Co.*, 463 U.S. 29, 57 (1983). Nothing prevents the SBA from modifying its size standard rules to use factors other than industry structure in determining whether a concern is dominant in its field. While the SBA may have the authority to so, we are at a loss to explain how such a determination could be made

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[16] In fact, a rational argument can be made that the SBA's current rules provide an even more explicit economic focus on industry structure. In determining dominance, economic theory examines items such as four-firm concentration ratios, the number of firms in an industry, and the barriers to entry (be they economic, legal or otherwise). *E.g.*., J. CHURCH & R. WARE, INDUSTRIAL ORGANIZATION 425-31(2000).

[17] This measure is akin to the Herfindahl-Hirschman four firm concentration ratio (which measures the amount of sales/revenue of the four largest firms in an industry). The Herfindahl-Hirschman Index is used by the Department of Justice and the Federal Trade Commission in merger reviews to determine whether an industry is already highly concentrated or whether the proposed merger of two firms would significantly increase concentration. UNITED STATES DEPARTMENT OF JUSTICE & FEDERAL TRADE COMMISSION, HORIZONTAL MERGER GUIDELINES § 1.5 (1997).

in a rational fashion without a close scrutiny of a particular industry's structure, including firm concentration ratios, barriers to entry, and firm size distribution within that industry.[18]

It is not the changing of the agency's mind that violates the Administrative Procedure Act (APA). Rather, it is the failure of the agency to adequately explain its change of position that runs afoul of the APA's rational rulemaking requirement. *E.g.*, *Smiley v. Citibank (South Dakota), N.A.*, 517 U.S. 735, 742 (1996); *Rust v. Sullivan*, 500 U.S. 173, 187 (1991); *United States Air Tour Ass'n v. FAA*, 298 F.3d 997, 1006 (D.C. Cir. 2002), *cert. denied*, 538 U.S. 977 (2003); *Texas Office of Public Utility Counsel v. FCC*, 265 F.3d 313, 322 (5th Cir. 2001), *cert. denied sub nom*., *National Ass'n of State Utility Consumer Advocates v. FCC*, 535 U.S. 986 (2002). Thus, the SBA is required by the APA strictures of rational rulemaking to explain in a detailed and cogent[19] manner a reasoned analysis for its change in how it determines dominance.

The only industry-specific metric utilized by the SBA in the proposed rulemaking is a revenue per employee statistic derived from 1997 Census data and may also incorporate data from firms dominant in their particular industry. What the SBA did not examine in determining whether the proposed size standards excluded dominant firms were the structure of each industry as they had done for at least 30 years. The SBA's failure to address this rejection of a longstanding interpretation of the Small Business Act violates the rational rulemaking requirements of the APA as established by the Supreme Court in *Motor Vehicle Manufacturers Ass'n of the United States*. In preparing a final rule, we strongly urge the SBA to explain why it has chosen to ignore this longstanding interpretation of the term "dominance."

V. The Proposed Rule Violates the SBA's Own Regulations

Prior to 1946, government agencies utilized a welter of inconsistent and ad hoc rules for executing their statutory mandates. The APA introduced standardized procedures throughout the

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[18] Recent advances in industrial organization theory suggest that a game-theoretic approach makes more sense for determining the cause of a particular industry's market structure. *E.g.*, J. SUTTON, TECHNOLOGY AND MARKET STRUCTURE 33-62, 265-94 (1998). Using this game-theoretic approach, it is possible to estimate (using standard econometric techniques) a comparative statics model of an industry based on supply-demand relationships, different market structures within an industry, and market power. J. CHURCH & R. WARE, INDUSTRIAL ORGANIZATION 440-52 (2000). While the game-theoretic approach is economically elegant, the SBA does not have the resources or data needed to build a comparative statics model for the approximately 1100 North American Industrial Classification codes that it uses to classify business concerns. In fact, antitrust enforcement still relies to a great extent on the structure, conduct and performance measured inherent in the SBA size standard regulations. *See* UNITED STATES DEPARTMENT OF JUSTICE & FEDERAL TRADE COMMISSION, HORIZONTAL MERGER GUIDELINES, *in passim* (1997); *accord* J. CHURCH & R. WARE, INDUSTRIAL ORGANIZATION 599-619 (2000).

[19] The APA only requires a statement of basis and purpose. The D.C. Circuit has taken agencies to task for failing to explain significant aspects of their rules and orders in a cogent fashion. *See McElroy Elec. Corp. v. FCC*, 990 F.2d 1351, 1366 (D.C. Cir. 1993). Of course, an agency cannot be overly cogent because it will then fail to meet the minimum standards for a statement of basis and purpose. *Cf. Automotive Parts & Accessories Ass'n v. Boyd*, 407 F.2d 330, 338 (D.C. Cir. 1968) (establishing standards for completeness of basis and purpose statement). Thus, agencies must find a middle ground between Shavian pithiness and Gibbonian expatiation.

government and provided a framework for distinguishing among various quasi-legislative, executive, and juridical functions of federal agencies. *See Wong Yang Sung v. McGrath*, 339 U.S. 33, 41 (1950). As the Supreme Court noted, the APA prohibits ad hoc decisionmaking and requires agencies to treat similarly situated persons and entities in the same manner. *See Morton v. Ruiz*, 415 U.S. 199, 232 (1974).

The APA establishes procedures by which agencies must issue regulations. 5 U.S.C. § 551(12); *see* 1 K. DAVIS & R. PIERCE, ADMINISTRATIVE LAW TREATISE §§ 6.4, 7.2 (1994). Rules, including the size standards, are considered informal rules and issued pursuant to the requirement of 5 U.S.C. § 553. Since the SBA intends that these size standards have legal consequences to those business concerns that fall within their ambit,[20] the size standards are considered "legislative" rules that are required to be issued pursuant to notice and comment. *United States v. Mead Corp.*, 533 U.S. 218, 229-30 (2001); *Appalachian Power v. EPA*, 208 F.3d 1015, 1020 (D.C. Cir. 2000); *American Mining Cong. v. EPA*, 995 F.2d 1106, 1110 (D.C. Cir. 1993). A rule that is required to be issued pursuant to the notice and comment procedures of § 553 is deemed to have the force and effect of law. *Chrysler Corp. v. Brown*, 441 U.S. 281, 301-02 (1979); *Batterton v. Francis*, 432 U.S. 416, 425 n.9 (1977); *Appalachian Power v. EPA*, 208 F.3d 1015, 1020 (D.C. Cir. 2000). Once a regulation has the force and effect of law, the agency promulgating the regulation is required to comply with its own regulations. *United States v. Nixon*, 418 U.S. 683, 695 (1974); *A.D. Transp. Exp., Inc. v. United States*, 290 F.3d 761, 766 (6th Cir. 2002); *Cherokee Nation v. Babbitt*, 117 F.3d 1489, 1499 (D.C. Cir. 1997). Failure of an agency to follow its own regulations constitutes arbitrary and capricious action under the APA leading to reversal of the agency decision. *Morton v. Ruiz*, 415 U.S. 199, 235 (1974); *Nelson v. INS*, 232 F.3d 258, 262 (1st Cir. 2000).

The reason for mandating that an agency follow its own regulations is twofold. Legislative rules are binding on parties outside the agency. If entities subject to those regulations are to conform their behavior to those regulations, the agency cannot casually ignore those rules because such ad hoc discretion makes it impossible for regulated entities to know whether they are in compliance. *Morton v. Ruiz*, 415 U.S. at 232-35. Secondly, courts presume regularity and rationality in existing federal regulations because the absence of such presumption would lead to a dangerously unstable regulatory regime. *Radio-Television News Directors Ass'n v. FCC*, 184 F.3d 872, 880 (D.C. Cir. 1999); *accord Bowen v. American Hosp. Ass'n*, 476 U.S. 610, 626-27 (1986); *Corrosion Proof Fittings v. EPA*, 947 F.2d 1201, 1214 (5th Cir. 1991). Such regularity ensures reasoned decisionmaking because nothing in the APA or the caselaw interpreting that statute gives the SBA the discretion to pick and choose the regulations that it will follow.

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[20] Business concerns that fall outside of the standards are not eligible for business loans under § 7(a) of the Small Business Act, disaster loans under § 7(b) of the Small Business Act, or procurement programs established under § 15 of the Small Business Act. In sum, the size standards are imbued with significant legal consequences to the universe of business concerns seeking assistance from the federal government.

The SBA established a very specific procedure for calculating size standards. Those regulations require that the agency examine the structure of a particular industry including, but not limited to: the degree of competition, average firm size, start-up costs, entry barriers, growth trends, and historical activity within an industry. Assessment of these factors simply dehors the record in the NPRM. The SBA did not follow its own regulations for determining size standards.[21] In fact, the SBA admits the failure to comply with its own regulations in the initial regulatory flexibility analysis. In that document, the SBA identified an alternative that it did not adopt – categorization by NAICS industry sector or sub-sector. 69 Fed. Reg. at 13,141.

Failure to follow its own regulations has created size standard problems in the past for the SBA. During its last major revision to its size standards in 1984, the SBA did not adopt a rule that required it to assess dominance on a national basis. A size standard was established for dredging on a national basis without regard to whether or not dredging firms were dominant on a regional basis. The SBA adopted this conclusion despite the fact that, after examining the industry structure as required by its regulations, the evidence in the record demonstrated that dredging firms were dominant on a regional, not national, basis. In *California Dredging Co. v. Sanders*, 657 F. Supp. 38 (D.D.C. 1986), the court held that a valid size standard required consideration of dominance on a regional basis and national standard constituted arbitrary and capricious rulemaking. *Id*. at 40. In a similar vein, the SBA's failure to follow its regulations and examine the structure of each industry that it is developing a size standard for constitutes arbitrary and capricious action. The SBA can avoid the problems of a court challenge by reexamining the proposed size standard under the methodology set forth in 13 C.F.R. § 121.102.

Requiring each industry to be examined individually is designed to ensure that an appropriate size standard is selected for each industry. The SBA's failure to follow its own rules is evidenced by the adoption of an inappropriate size standard for banks. The current standard for a small bank is assets of $100 million or less. This is an appropriate size standard on which to measure banks for a number of reasons peculiar to the banking industry. Regulators limit lending by banks based on a percentage of their overall assets. *See*, *e.g.*, *United States v. Winstar Corp.*, 518 U.S. 839, 845-46 (1996) (noting that bank regulators reduced capital reserves for thrifts from five to four percent); 12 U.S.C. § 3907 (mandating that financial regulators impose adequate capital levels); 12 C.F.R. § 3.6(b) (requiring capital reserves based on total assets). For certain regulatory purposes, the Board of Governors of the Federal Reserve establishes separate regulatory requirements for small bank holding companies and measures that by the amount of assets held by the bank. *Id*. at Part 225, App. C. If the regulators of banks use the measure of total assets as the appropriate measure of the size of a bank to regulate their activities, presumably they have reached this conclusion based on their expert examination of the structure of the banking industry. A more relevant statistic for determining bank size than an employee number is asset size (as in the current SBA regulations) because banks are regulated

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[21] Nor can the SBA take solace in the fact that it examined one aspect of each industry. Utilization of Bureau of the Census data on revenues per employee cannot be considered an examination of the structure of a particular industry. For the SBA to have done that, it would have had to at least examine whether the revenue per employee was the same for dominant firms as for small firms. No such analysis is apparent in the record.

based on the amount of money they control not the number of employees who control that money. Even the SBA does not rely on employee size when determining whether to accord certified lending or preferred lending status to banks. *Compare* 13 C.F.R. §§ 120.441, .451 (establishing standards without reference to number of employees). Had the SBA complied with its own regulations, it would not have proposed a size standard that it does not even consider valid for its own regulatory purposes.

The SBA's failure to examine industry structure is not limited to industries in which the SBA has adopted neither a revenue or employee parameter. Currently, the SBA defines a small cable operator as one with less than $12.5 million dollars in revenue. The Federal Communications Commission (FCC), the Office of Advocacy of the United States Small Business Administration, and the industry, *e.g.*, Farrell, *Vogel Eyes '04 Growth*, MULTICHANNEL NEWS at 27 (May 17, 2004); Scanlon, *Basic Sub Losses Continue to Plague Cable*, CABLE WORLD at 31 (Aug. 11, 2003), all measure the size of cable companies based on the number of subscribers.[22] Nowhere does industry or the FCC examine cable company size based on the number of employees. The number of cable subscribers can be translated into a revenue figure by multiplying the yearly revenue per subscriber by the total subscribers. Thus, the current SBA standard represents a reasonably good proxy for the appropriate measure of cable system size by regulators and the industry. The SBA failure to examine the structure of the cable industry resulted in a proposed size standard inapt for the industry.

Similar arguments could be made for other industries. The comments should not be viewed as an exhaustive examination of the SBA's failure to comply with its own regulations. Rather, the close scrutiny of the cable and banking industries only highlight the resultant problematic size standards that were proposed due to the agency's noncompliance with its regulations.

Nor can the SBA simply argue that it is conducting a simple conversion process to an employee-based size standard. SBA regulations specifically address revisions to size standards in order to take account of inflation. 13 C.F.R. § 121.102(c). Nothing in part 121 of the SBA's regulations provide any guidance on how the agency will convert a revenue-based size standard into an employee-based size standard. Nor does the SBA provide in the NPRM any modification to its existing regulations that would permit it to undertake the general conversion in the proposed rule. Promulgation of a rule dictating the procedures for that process would enable affected small business concerns, during the notice and comment process, to address issues on whether the conversion factor is appropriate for their industry, whether the conversion factor

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[22] *Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992: Rate Regulation, Sixth Report and Order and Eleventh Order on Reconsideration*, 10 FCC Rcd 7393, 7400 (1996) (establishing a size standard for small cable operator based on total subscribers). This standard was concurred in by the Office of Advocacy, *see* Pineles, *The Small Business Regulatory Enforcement Fairness Act: New Options in Regulatory Relief*, 5 COMMLAW CONSPECTUS 29, 36 (1997) and approved by the Administrator pursuant to his authority under § 3(a)(2) of the Small Business Act.

takes in the latest data on growth in productivity, or other relevant conditions that address the change from a revenue to employee-based standard.

In essence, the SBA was required to modify its existing regulations to cover this conversion process or be prohibited from undertaking that process. Courts are consentient in holding that an agency is required to follow its own regulations until it has amended the existing regulations or adopted new ones. *E.g.*, *Mullins Coal Co. v. Director, Office of Workers Compensation Programs*, 484 U.S. 135, 170 (1987); *BCS Fin. Corp. v. United States*, 118 F.3d 522, 525 (7th Cir. 1997); *Clean Ocean Action v. York*, 57 F.3d 328, 333 (3d Cir. 1995); *National Family Planning & Reproductive Health Ass'n v. Sullivan*, 979 F.2d 227, 234 (D.C. Cir. 1992); *City of Fredericksburg v. FERC*, 876 F.2d 1109, 1112 (4th Cir. 1989); *Romeiro de Silva v. Smith*, 773 F.2d 1021, 1024 (9th Cir. 1985). Thus, the SBA is required to undertake one of two actions: either it must comply with its existing rules and examine the structure of each industry or develop a regulation that specifies the procedures for making that conversion. The SBA has done neither so it has violated its own regulations and undertaken arbitrary and capricious rulemaking.

VI. The Regulation is Arbitrary and Capricious because it is Irrational

The polestar of APA rulemaking is rational rulemaking. While the focus typically revolves around an examination of whether the agency followed proper procedure, *see*, *e.g.*, *Vermont Yankee Nuclear Power Corp. v. NRDC*, 435 U.S. 519, 547 (1976); *Chocolate Mfrs. Ass'n v. Block*, 755 F.2d 1098, 1103 (4th Cir. 1985), the process must result in a substantively rational rule. For a rule to be substantively rational, an agency must address all relevant statutory factors, *see Citizens to Preserve Overton Park v. Volpe*, 401 U.S. 402, 416 (1971), examine *relevant* data, and articulate a satisfactory explanation for its course of action. *E.g.*, *Motor Vehicle Manufacturers Ass'n of the United States v. State Farm Mut. Auto. Ins. Co.*, 463 U.S. 29, 43 (1983); *California v. FCC*, 905 F.2d 1217, 1230-31 (9th Cir. 1994), *cert. denied*, 514 U.S. 1050 (1995). A decision by an agency that is so implausible that it cannot be ascribed to its expertise, *Motor Vehicle Manufacturers Ass'n*, 463 U.S. at 43, or constitutes a clear error of judgment will be considered arbitrary and capricious rulemaking in violation of the APA. *Arent v. Shalala*, 70 F.3d 610, 617 (D.C. Cir. 1995), *quoting Citizens to Preserve Overton Park* at 416. An agency that promulgates a regulation in which the rule is not rationally related to its statutory mandate or objectives also will be considered to have acted arbitrarily and capriciously in violation of the APA's mandate of rational rulemaking. *E.g.*, *Mourning v. Family Publications Serv. Inc.*, 411 U.S. 356, 369 (1973); *Sidell v. Commissioner*, 225 F.3d 103, 106 (1st Cir. 2000); *Texas Oil & Gas Ass'n v. EPA*, 161 F.3d 923, 935 (5th Cir. 1998); *American Paper Inst. v. EPA*, 996 F.2d 346, 351 (D.C. Cir. 1993). When examined under these standards, the proposed rule fails all tests of rational rulemaking mandated by the APA.

Only two statutory factors govern the establishment of size standards by the SBA. First, the business concern must be independently owned and operated. As already noted, the SBA proposal does nothing to modify its existing interpretation of that term. Thus, the proposed rule must be measured against the other criterion – whether it properly avoids classifying dominant firms in an industry as non-dominant and therefore within the statutory classification set forth in § 3(a)(1) of the Small Business Act, 15 U.S.C. § 632(a)(1). *See California Dredging Co. v. Sanders*, 657 F. Supp. 38 (D.D.C. 1986).

A. The SBA's Rationale that the Proposed Rule Simplifies Size Standards is not Supported by the Record

The SBA asserts that "a single measure of size helps make size standards less complex." 69 Fed. Reg. at 13,131. The agency goes on to claim that "[h]aving a single size measure simplifies the structure and enables SBA to establish fewer size standard levels. *Id*. Unfortunately, the SBA does not accomplish this objective in the proposed rule.

Currently, there are 37 different size levels which apply to the 1,151 industry classifications and 11 separate size standards (although some of them coincide with existing employee-based standards)[23] for various financial and procurement programs. Size determinations for banks are based on amount of assets and those for electric utilities are calculated on the total amount of electricity generated in a given year. In the proposed rule, the SBA increases the number of employee size standards from 5 to 10 and reduces the number of revenue standards from 30 to 11. This contradicts the SBA's stated objective that a single measure of size, i.e., implying either an employee measure or a revenue measure, simplifies the SBA regulations. SBA's own explanation for the change does not match its expressed rationale for the change and thus does not articulate a satisfactory explanation for its course of action as mandated by *Motor Vehicle Mfrs. Ass'n of America*.

Nor does the SBA meet its goal of simplification of size standards. Except for banks and electric utilities, a business must meet either an employee standard or a revenue standard but not both. Under the proposed rule, the SBA would require 36 industries to meet both a revenue and employee standard. 69 Fed. Reg. at 13,134. No conceivable logic or ratiocination can reach the conclusion that size standards that must meet both an employee number *and* a revenue level is less complex than the existing standards of either one *or* the other. The proposed rule represents arbitrary and capricious rulemaking because it neither is rationally related to achieving the SBA's regulatory objective nor can it, given the inherent illogic of it, be considered an exercise of agency expertise.

The aforementioned conclusion is buttressed by the SBA's own inconsistent asseverations about the use of an employee-based standard rather than a revenue limitation. On the one hand, the SBA contends "[s]mall businesses will benefit because they will find it easier to use the small business size standards to determine if they are a small business." *Id*. at 13,139. Although left unstated, the assumption by the SBA is that accounting for the number of employees is easier than calculating gross revenue. The rectitude of this assumption is belied by

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[23] For example, the size standard for participation in the Small Business Innovation Research program is 500 employees without regard to industry classification. This is the same size standard that the SBA uses for many of the manufactuing NAICS codes.

the SBA's own acknowledgment "that, in the event it must determine a business' employment size status, it may be more difficult to verify the accuracy of the payroll records submitted. At times, SBA may request a business to provide more information to substantiate its employment information." *Id*. at 13, 141. The SBA does not even state what additional records will be needed by it to make a definitive determination of size status. Even though the SBA is unable to provide small businesses with the information that they would have to provide to the agency for a size status determination, the SBA nevertheless concludes that employee counts will be easier for the small business. The leap of logic that such a conclusion requires seriously calls into question the rationality of the proposal. We are even more troubled by the conclusion that the SBA will have a more difficult time of determining size status than a small business concern. Congress delegated size standard responsibility to the SBA, 15 U.S.C. § 3(a)(2)(C), and thus imbued it with expertise.[24] Such an argument gives pause to whether the agency should have been afforded the broad grant of power to determine size standards if it believes that it is incapable of determining whether a business is small more readily than the business itself. In short, the SBA cannot contend on the one hand that the rule makes it easier for small businesses while making it more difficult for itself. Whatever standards of rationality are mandated by the APA, such internal inconsistencies certainly cannot be met by two such mutually exclusive conclusions.

B. The SBA Proposed Rule does not Utilize Relevant Data for the Conversion and Fails to Satisfy the Standards for Rational Rulemaking

The SBA calculates the conversion by utilizing a revenue per employee derived from 1997 Bureau of the Census data. That data includes total number of employees and total revenue. Calculation of a revenue per employee is then a simple arithmetic process. 69 Fed. Reg. at 13,132. The SBA admits "these criteria were designed to convert a receipts-based size standard to an ***equivalent*** employee-based size standard." *Id*. at 13,132 (emphasis added). That conversion only is valid if the revenue per employee adopted by the SBA approximates the revenue per employee for small business concerns in each industry. The revenue per employee figure adopted by the SBA patently is not limited to revenue per employee for small businesses. In many instances, the revenue per employee could be based primarily on the revenue per employee of large businesses. For example, in the discount merchandising sector (the proposed standard is 150 employees converted from a current standard of $23 million), the top four firms control almost 88 percent of the revenue. UNITED STATES BUREAU OF THE CENSUS, 1997 ECONOMIC CENSUS – RETAIL TRADE, Table 6, at 210 (2000). While not as dramatic, concentration of sales among the four largest firms in radio, television and other electronic stores exceeds 62 percent of total revenue. *Id.* at 199. The four largest firms in the cosmetics and beauty supply sales represented nearly 50 percent of total sales. *Id*. at 204. A similar exercise

[24] Under *Chevron USA, Inc. v. NRDC*, 467 U.S. 837 (1984), an agency that administers or has a policymaking role is given deference based on its expertise in implementing the statute. *Scheduled Airlines Traffic Offices v. Department of Defense*, 87 F.3d 1356, 1361 (D.C. Cir. 1996). Given the categorical prohibition on other agencies making size standard determinations without the approval of the Administrator of the SBA, Congress has delegated both an administrative and policymaking role to the SBA.

could be done for all of the industries in which the SBA converted to an employee number to show that a revenue per employee based on total industry sales is not representative of the sales per employee for small businesses. In granting discretion to the SBA to enumerate size standards, Congress could not have intended the Administrator to rely on data from large businesses to classify small businesses. The only possible explanation is that the resulting calculations are irrational because the data the agency used was not relevant to the task – determining what constitutes a small business.

Equally troubling is that the SBA made no attempt to weight the revenue data by examining other available information from the 1997 data. We already have cited firm sales concentration from the same data set. Those data sets also provide breakdowns by employee size and sales within given categories of employee size firms. In trying to ensure that the conversion factor reflects revenue per employee only from small businesses, the SBA could have requested the Census develop a weighting factor for each NAICS code that eliminates large firm data from the calculation. While it is true that the data is categorized based on employee size, the SBA could have, for example, subtracted the revenue of the four or eight largest firms from their calculation of revenue per employee. This simple mathematical step, although not eliminating the potential inclusion of dominant firm data in the conversion factor, certainly would dramatically reduce the overrepresentation of such data, particularly in sectors that, like discount retail stores, have most of their revenue generated by the four largest firms. Even if one argues that the SBA examined one aspect of the relevant data, it did not examine *all* the relevant data that is mandatory to conduct rational rulemaking. *Motor Vehicle Manufacturers Ass'n of the United States*, 463 U.S. at 43.

Nor can the SBA logically argue that revenue per employee is the same for large and small businesses. Economic theory teaches that larger firms generally have lower unit costs than smaller ones. J. CHURCH & R. WARE, INDUSTRIAL ORGANIZATION 54 (2000). This results from either the existence of economies of scale or economies of scope or some combination thereof. Economies of scale exist when the long-run average cost declines as output increases. *Id*. Economies of scope exist when it is cheaper to produce two outputs in one facility than produce the same amount of output in single product facilities.[25] *Id*. at 58. This basic economic theory is even embedded in law; Congress, in the Robinson-Patman Act, 15 U.S.C. §§ 13-13c, prohibits price discrimination by manufacturers unless the manufacturer can demonstrate that it costs less to supply one retailer. *Id*. at § 13(a); *see Texaco, Inc. v. Hasbrouck*, 496 U.S. 543, 556 (1990). When Congress passed the Small Business Act, it is deemed to be aware of existing legislation and court interpretations. *Holloway v. United States*, 526 U.S. 1, 9 (1999); *Cannon v. University of Chicago*, 441 U.S. 677, 697-98 (1979). In the context of the Small Business Act, Congress was presumed to recognize the Robinson-Patman and the existence of economies of scale and

[25] In the context of retail establishments, the economies of scope would exist if it is cheaper to sell clothes and groceries in the same store rather than selling clothes in one store and groceries in a different store. Economies of scope also exist in the service business where it might be cheaper to have one facility in which real estate is purchased and also have architects to design the building rather than having them in separate office complexes.

scope. Congress could not have intended the SBA, when it delegated the responsibility of size standard determinations, to ignore these basic economic facts. However, as currently drafted, the proposed rule does exactly that by determining that revenue per employee is static across an entire industry sector without regard to economies of scale and scope. Only one conclusion is reachable given this reasoning – the conversion factor adopted by the SBA in the proposed rule cannot be a relevant statutory factor in making determinations pursuant to § 3 of the Small Business Act.

Another reason the conversion factor is not a relevant statistic relates to the SBA's enumeration of employees. SBA regulations count each employee, whether full-time or part-time, on an equivalent basis, i.e., as an employee. 13 C.F.R. § 121.106(b)(2). The conversion factor simply establishes a revenue per employee figure. Applying this conversion factor to the SBA's regulation on enumerating employees results in a conclusion that revenue per employee is equal for a full-time and part-time employee. Basic economic theory demonstrates that, in a competitive market, that a firm will pay a real wage equal to the marginal value of productivity. P.CAHUC & A. ZYLBERBERG, LABOR ECONOMICS 174-75 (2004). By equating the revenue per employee of full-time and part-time employees, profit maximizing firms never would pay the real wage of a full-time employee if the they could obtain the same revenue from hiring part-time employees. An agency's use of a model (in this case the conversion factor of revenue per employee) is arbitrary if it "bears no rational relationship to the reality it purports to represent." *American Iron & Steel Inst. v. EPA*, 115 F.3d 979, 1005 (D.C. Cir. 1997). Clearly, the real world distinguishes between full-time and part-time employees. The use of the conversion factor therefore is arbitrary because it does not have any relationship to the reality it attempts model. If that is the case, then the SBA has not examined or utilized relevant data in drafting the proposed rule.

The conversion factor is not a relevant factor for another reason. The data utilized by the SBA in calculating revenue is from1997. That data, coming at the embryonic stage of a dramatic increase in utilization of desktop computing and the Internet, fails to account for dramatic changes in productivity during the last seven years. Agencies must adopt their regulatory regimes to changed circumstances and advances in technology. *Detsel v. Sullivan*, 895 F.2d 58, 64 (2d Cir. 1990). As the D.C. Circuit noted, it would be futile to require an agency to follow correct procedure in promulgating a regulation based on data that was five years old. *NRDC v. Herrington*, 768 F.2d 1355, 1408 (D.C. Cir. 1985). Changes in productivity would drastically increase the revenue per employee. Keeping everything else equal, increases in productivity would result in far fewer workers needed to reach the revenue levels set by the SBA for determining a small business. If the stated goal of the SBA is to maintain equivalency between current size standards and new size standards, the SBA must examine more relevant data based on revenue per employee that incorporates dramatic productivity increases not reflected in the 1997 Census data. The SBA failed to do that and, even if it had followed its own regulations, the data is so outdated that the resultant size standards, based on irrelevant data, constitute arbitrary and capricious rulemaking. Given that the SBA is withdrawing the current proposal, the agency should utilize 2002 Census data which should be available shortly. That data will reflect significant changes in productivity and will not be fraught with the problems of using seven-year old information.

VII. The SBA Failed to Prepare an Adequate Initial Regulatory Flexibility Analysis

The RFA requires federal agencies to assess the economic consequences of proposed rules, and if the proposed rule will have a significant economic impact on a substantial number of small entities, prepare an initial regulatory flexibility analysis (IRFA). 5 U.S.C. § 603. We concur with the SBA that the proposed rule will have a significant economic impact on a substantial number of small entities. We further agree with the SBA that it was required to prepare an IRFA. However, the SBA's IRFA is wholly inadequate to the task of assessing the impact on small entities and advising them of the potential consequences to their business operations.

The RFA delineates the contents of an IRFA: a) the need for and objectives of the rule; b) an estimate of the number of small entities affected; c) projected reporting, recordkeeping, and other compliance costs of the proposed rule; d) identification of duplicative, overlapping, or rules that conflict with the proposal; and e) development and evaluation of alternatives to the proposal that lessens the adverse consequences on small businesses. *Id*. at § 603(b)-(c). Compliance with the RFA is not based on same irreducible mathematical formula. Instead, agencies must make a good faith effort to examine the criteria specified in § 603. *See Associated Fisheries of Maine v. Daley*, 127 F.3d 104, 114 (1st Cir. 1997).

The SBA satisfied the first criterion required for an adequate IRFA. The SBA provides a clear explanation of its reasons for proposing the modification to size standards. While small entities may disagree with the need for the alterations, the RFA, like the National Environmental Policy Act (NEPA), requires an agency to perform a specified analysis but does not mandate a particular outcome. *Id*. at 116; *compare Stryckers' Bay Neighborhood Council v. Karlen*, 444 U.S. 223, 227 (1980) (noting that NEPA not substantive statute mandating environmentally friendly decisions).

The SBA estimated that there would be a net impact of increasing the number of firms defined as small by 1,100. 69 Fed. Reg. at 13,140. This total is derived from the SBA's determination that 35,200 businesses will gain small business status while 34,100 will lose that attribution. *Id*. The SBA then notes that the total numbers are small relative to the total number of small businesses in the United States and that an even smaller number of such businesses utilize SBA programs or are involved in federal government procurement. *Id*. Finally, the SBA identified certain industries, such as Full Service Restaurants, that would have the largest number of businesses losing their status as small business concerns. *Id*. While the SBA makes an effort to describe and estimate the number of businesses affected, it fails to meet the requirements of the RFA.

In estimating and describing the number and type of entities affected by a proposed rule, the SBA committed a cardinal error that undercuts its efforts at complying with § 603(b)(3). The

Office of Advocacy has taken a longstanding position that federal agencies, when describing the entities affected by the rule, should not aggregate economic effects to obtain an overall impact if identifiable subsectors of a particular industry are subjected to a greater impact than other parts of an industry.[26] The rationale for disaggregating economic effects applies with equal force to the division of small businesses into affected sectors for a description of the entities affected by the size standard rule. Absent disaggregation, it would be impossible for the SBA to perform two critical aspects of an IRFA – determining the economic consequences of the proposal on small entities and developing appropriate alternatives to reduce impacts on various classes of small businesses.[27]

The SBA notes that only 200,000 businesses are involved in federal procurement. *Id*. Because that represents only 4 percent of the total number of small businesses, the SBA performed no further analysis. This failure clearly violates the RFA. In its guidance document on compliance with the RFA, the Office of Advocacy stated:

> [t]he analyst best serves the process [of identifying potentially affected small entities] each group of regulated entities with similar economic and industrial characteristics. Each group constitutes its own universe of regulated small entities that the proposal may influence significantly.

OFFICE OF ADVOCACY, UNITED STATES SMALL BUSINESS ADMINISTRATION, A GUIDE FOR GOVERNMENT AGENCIES: HOW TO COMPLY WITH THE REGULATORY FLEXIBILITY ACT 15 (2003). The SBA failed to identify by industry class the small businesses currently involved in federal government procurement and ascertain the number and types of the businesses that might no longer qualify as small businesses and therefore be eligible for various socioeconomic

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26 *Notice of Proposed Rulemaking on Valencia Oranges Grown in Arizona and Designated Parts of California; Proposed Weekly Levels of Volume Regulation for the 1989-90 Season*, Comments of the Chief Counsel for Advocacy at 4 (July 13, 1990) (noting that average masks structural differences in industry that benefit large handlers while harming small handlers). The Chief Counsel reaffirmed this conclusion in the recent guidance document issued pursuant to Executive Order 13,272. OFFICE OF ADVOCACY, UNITED STATES SMALL BUSINESS ADMINISTRATION, A GUIDE FOR GOVERNMENT AGENCIES: HOW TO COMPLY WITH THE REGULATORY FLEXIBILITY ACT 15-16 (2003).

27 *Notice of Proposed Rulemaking on Navel Oranges Grown in Arizona and Designated Parts of California; Proposed Weekly Levels of Volume Regulation for the 1990-91 Season*, Comments of the Chief Counsel for Advocacy at 4-5 (Oct. 25, 1990). In the proposed rule, the Department of Agriculture certified the proposed rule as not having a significant economic impact on a substantial number of small entities. The Chief Counsel responded by concurring in the Department's assertion that most of the businesses involved in handling navel oranges were small. However, the Chief Counsel noted that such conclusion is "akin to viewing a forest from a plane and saying the trees are green. Nothing specific about the makeup of the forest is gleaned form such a statement. Similarly, nothing about the handlers of navel oranges is obtained from the Department's conclusion." *Id*.

contracting programs established by the Small Business Act and federal procurement officials.[28] The failure is made more problematic by the fact that the SBA has access to detailed information from the Federal Procurement Data System, a more comprehensive and accurate database than the PRO-NET database used in its IRFA. However, what is most distressing is that the SBA failed to utilize the Federal Procurement Data System to undertake the type of rigorous analysis needed to identify how the proposed alteration of size standards would affect the number of small business participants in various NAICS code sectors. For example, a particular size standard change might significantly reduce the number of small business concerns that received government contracts because they obtained them through small business set-asides and the alteration in size might force them to open competition where they would lose to large businesses. When the SBA last performed a major overhaul of its size standards, it was sensitive to the possible adverse implications for federal procurement. *See* 48 Fed. Reg. at 20,567-68 (1983) (discussing possible adverse consequences to small businesses involved in federal government procurement). No such discussion or analysis exists in the current record.

The SBA compounds its analytical failures by focusing exclusively on the number of loans made pursuant to § 7(a) of the Small Business Act. However, the SBA does not assess the potential adverse consequences of the change with respect to the disaster loan program established under § 7(b) of the Small Business Act. The SBA is well aware of the potential adverse consequences from failing to establish appropriate small business size standards with respect to a disaster. Numerous small businesses were denied expanded economic injury disaster loans after the terrorist incidents on September 11, 2001 because they did not meet the size standards. Any proper IRFA must assess the number of small businesses that might be denied a disaster loan due to the size changes. Such data is readily available by examining past disasters and making a rough estimate as to the type of businesses that would be affected in the future.

The SBA's assessment of economic impact based on the type of recordkeeping and reporting requirements also was inadequate. The SBA noted that verification of payroll records may be difficult and require small businesses to submit additional records. 69 Fed. Reg. at 13,141. Yet, the SBA does not identify what those records will be or how much it will cost to maintain such records. The SBA's estimate that it will take four hours to complete the application for a size standard determination as the sole recordkeeping and reporting requirement is without any basis in fact. Thus, no one could conclude that the SBA made a reasonable effort to comply with this requirement of the RFA because the basis for its conclusion is undermined by its own analysis of the new standard. *See Motor Vehicle Manufacturers Ass'n*, 463 U.S. at 43.

The failure to estimate and describe the number of businesses is problematic in and of itself for complying with the RFA. However, the failure is critical to examining the economic consequences on various industry sectors or access to SBA programs and developing less burdensome alternatives as required by § 603(c). Without a deep understanding of each

[28] For a detailed list of such programs, please refer to 48 C.F.R. Part 19.

subsector of the economy affected by the rule, the SBA cannot identify and analyze alternatives that might reduce the adverse consequences on small businesses. For example, there are more than 30 industry sectors that will have both an employee and revenue-based size standard. Without understanding the economic consequences of meeting both standards (such as elimination from certain federal contracting programs for small businesses), the SBA is unable to examine more tailored alternatives in its IRFA than simply maintaining the status quo or doing a sector-by-sector analysis of each industry (as is mandated by the agency's own regulations). Similarly, with respect to the impact on small businesses involved in federal procurement, proper estimation could have resulted in the elimination of the combined employee and revenue standards for the business category, modified some of the employee standard levels, or resorted back to the existing revenue standard, or created a new revenue standard.[29]

For example, the Department of Transportation, for purposes of its disadvantaged business enterprise program adopts the SBA standards for calculating whether a concern is a small business. 49 C.F.R. § 26.5. However, for purposes of participating in the disadvantaged business airport concession program, the Department adopts revenue standards (most of which are significantly higher than the equivalent SBA standards) except for banks and pay telephone service providers (adopting the identical standard to that in current SBA regulations). *Id*. at Part 23. The Department of Transportation recognized the need to adopt standards to meet the needs of different programs and only could accomplish that by performing an analysis that the SBA failed to undertake.

Nor can the SBA rely on input from commenting agencies to overcome its inadequate assessment of regulatory alternatives. While it is true that the purpose of notice and comment is to educate the agency based on the regulated community's assessment of pitfalls and advantages of the proposal, *e.g.*, *Buschmann v. Schweiker*, 676 F.2d 352, 357 (9th Cir. 1982); *Spartan Radiocasting v. FCC*, 619 F.2d 314, 321 (4th Cir. 1980); *National Tour Brokers Ass'n v. United States*, 591 F.2d 896, 902 (D.C. Cir. 1978), reliance on public comments to comply with the development of alternatives requirement violates the RFA. First, the RFA imposes the obligation on the agency not the public. Given the parallels between NEPA and the RFA, *Associated Fisheries of Maine*, 127 F.3d at 114, it would be akin to a federal agency requiring the public to derive the actions that mitigate the adverse environmental consequences. No court would sanction the adequacy of an environmental impact statement that relied solely on public input, *see*, *e.g.*, *Robertson v. Methow Valley Citizens Council*, 490 U.S. 332, 349-50 (1989); *Baltimore Gas & Elec. Co. v. NRDC*, 462 U.S. 87, 97 (1983)[30] and we do not believe any court would sanction the SBA's dereliction of its statutory responsibilities in that manner. Even if the

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29 Of course, the type of granular analysis suggested by the criticism in these comments would not have been necessary had the SBA followed its regulations concerning the examination of size standards on an industry basis.

30 In fact, the likelihood that an agency would transfer its NEPA responsibilities to public commenters is so outside the contemplation of federal agencies that no court reviewing compliance with that Act has ever had the reason to address the issue.

SBA were permitted to transfer its responsibility to the regulated public for developing alternatives, that would undermine the entire concept of the RFA. The primary purpose behind the RFA is for agencies to find methods of complying with their regulations that will be less burdensome on small entities. If the purpose of the RFA is burden reduction on small entities, it defies all logic for the SBA to shift the burden of regulatory analysis from itself to those small businesses that it will regulate. Taking the SBA's analogy to its logical conclusion would result in a complete evisceration of the RFA by empowering agencies to impose analytical burdens on small entities in order to avoid regulatory burdens. Congress certainly did not intend this result when it enacted the RFA.

The final omission, in the SBA's IRFA, is the inadequate examination of overlapping rules. The SBA only made a cursory examination of other agency regulations and programs which will be discussed in greater detail below. Nevertheless, the cursory examination, given the Administrator's power to determine small businesses for all other federal statutes, simply fails to comply with the RFA. No one examining the SBA's assessment of overlapping regulations would conclude that it made even a reasonable effort, *see Associated Fisheries of Maine*, 127 F.3d at 114, to ascertain the programs in which the Small Business Act or the SBA's regulations are cross-referenced when defining small businesses.

VIII. The SBA Failed to Examine the Impact that the Proposal has on Other Federal Regulatory Programs

As already noted, the Administrator has the power to establish size standards for the purposes of the Small Business Act or any other Act. Size standards set forth in 13 C.F.R. Part 121 represent the default standard for all other federal agencies when those agencies wish to define a small business for purposes of carrying out their statutory responsibilities.[31] Agencies either adopt the standards set by the Administrator or follow the procedures outlined in § 3(a)(2) to develop a new size standard that would require the Administrator's approval prior to the adoption of the standard at variance from those set forth in the SBA's regulations. To the extent that the agencies simply cite or adopt the standards set forth in the Small Business Act, modifications to those standards then alters the management of those programs. In addition, the RFA adopts, as a baseline determinant of small business, the definition (and the regulations adopted to implement them promulgated by the SBA) of a small business in the Small Business Act. 5 U.S.C. § 601(3). Modifications made to the SBA size standard will then have a ripple effect across various federal programs, both in the analytical development of such rules and in their implementation. Given the delegation of power to the Administrator, close scrutiny of size standard changes in other federal programs becomes a relevant statutory factor that the SBA

[31] The authority granted to the Administrator does not apply if a statute has a specific definition of a small business that is different than the one established by the SBA. The proviso in § 3 of the Small Business Act simply codifies the canon of statutory construction that the specific always applies if it conflicts with a more general provision. *E.g.*, *Edmond v. United States*, 520 U.S. 651, 657 (1997); *Morales v. TWA, Inc.*, 504 U.S. 374, 384 (1992).

must consider if its rulemaking is to be considered rational. *Citizens to Preserve Overton Park* , 401 U.S. at 416.

A. The SBA failed to Examine the Implications of the Size Change on the Implementation of the RFA

Federal agencies are required by the RFA to adopt the size standards developed by the Administrator for determining whether a business is small, unless they follow special procedures for developing a different definition. *Id*.; *accord* OFFICE OF ADVOCACY, UNITED STATES SMALL BUSINESS ADMINISTRATION, A GUIDE FOR GOVERNMENT AGENCIES: HOW TO COMPLY WITH THE REGULATORY FLEXIBILITY ACT 11-12 (2003). Modifications to the size standards then alters the universe of small businesses that are subject to the analytical requirements of the RFA. In addition, for two agencies, it will change the universe of businesses that would be examined to determine whether to convene panels to obtain input from small entities on significant rules proposed by EPA and OSHA pursuant to § 609 of the RFA. Some examples will illustrate the potential adverse consequences on small entities.

The Department of Labor during the Clinton Administration proposed a rule to impose requirements to make workplaces more ergonomically sound. One of the industries adversely affected by the proposal was the restaurant industry. Under the SBA's new standards, OSHA would have been able to ignore the impact, under the RFA, on tens of thousands of restaurants because they would not have been classified as small. The SBA makes no mention of this in its examination of the impact of the proposed rule on the restaurant industry. If another effort is made to resurrect an ergonomics rule (or limit it to restaurants), OSHA would not have to examine the effect on these restaurants and would not, under § 609 of the RFA, seek out representatives from these restaurants prior to publication of the proposed rule. Given that the primary purpose of the RFA is to reduce burdens on small businesses, the modification of the size standards might exclude these businesses from any burden reductions that OSHA would arise from that agency's compliance with the RFA. A similar analysis could be done with numerous other agencies, their compliance with the RFA, and the small businesses they regulate. We are astounded that the SBA failed to recognize the implications of the proposal to modify the size standards.

Equally troubling is the fact that the record does not reveal any discussion between the SBA and the Chief Counsel for Advocacy on the implications of this proposed rule on the implementation of the RFA. While it may be difficult for the SBA to ascertain all of the agencies and the programs that utilize the Small Business Act's definition of a small business, the SBA should have simply consulted with the Chief Counsel whose office is in the same building as the Administrator. A simple consultation would have alerted the SBA to this issue and could have highlighted the issue in the questions that it posed in the NPRM. Focusing attention on the issue could have led to additional comments that would have provided the basis for a more narrowly tailored rule or one that examined the wider implications of the proposed change on small businesses subject to regulation by other agencies.

B. The SBA Failed to Assess the Impact of the Proposed Rule on Other Agency Regulatory Programs

The SBA recognized that its definitions are used by other agencies for defining small businesses or small business concerns. The SBA identified six agencies that use its size standards "for various programs specific to their agencies." 69 Fed. Reg. at 13,141. The SBA did not list the six programs. More troubling is that a cursory review by committee staff through a Lexis search came to the conclusion that the assessment by the SBA is not even close to being accurate. The agency's failure to examine the implications of these changes is important because it may alter the businesses eligible for various programs or the availability of exceptions and exemptions from various regulatory requirements.

The Bayh-Dole Act, 35 U.S.C. §§ 200-12, provides that small businesses are entitled to retain the rights to inventions made using federal assistance without regard to whether the invention was developed pursuant to the Small Business Innovation Research Program. Section 6(a) of the Bayh-Dole Act defines a small business by cross-reference to § 3 of the Small Business Act. Any change in the size standards then results in the concomitant ability of small businesses to retain patent rights developed in federally-funded grants or cooperative research and development agreements.[32] Given the fact that the size standard changes apply to many engineering and research service firms, it is likely that they would be affected by the changes in the size standards applicable to the Bayh-Dole Act, but any examination of that program dehors the record. It is an oversight that is highly problematic given the importance of intellectual property in global, technologically-sophisticated economy.[33]

The Department of Energy also operates programs that provide financial assistance to small businesses that participate as grantees in various epidemiological and energy research studies. 10 C.F.R. §§ 602.14, 605.15. As with the retention of patent rights, the Department of Energy determines eligibility for these programs by citing the Small Business Act and the Administrator's regulations. While it is likely that the number of small businesses affected by this program is not terribly large, the failure to identify this program represents yet another evident failure by the agency to undertake even the barest of reasonable measures to identify other federal agency programs that utilize the SBA's size standards.

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[32] For an example of agencies' regulations on cooperative development agreements and the Bayh-Dole Act, see 10 C.F.R. §§ 600.301-.81 (Department of Energy regulations); 14 C.F.R. Part 1274 (NASA regulations). Rules generally implementing the Bayh-Dole Act can be found at 37 C.F.R. Part 401 (Department of Commerce rules). The Department of Commerce regulations, *id*. at § 401.2(g), specifically adopt the standards set forth in 13 C.F.R. § 121.201.

[33] The SBA cannot be heard to argue that its patent fee regulations apply to the Bayh-Dole Act. Those regulations are specific to the reference in the patent laws permitting the Patent and Trademark Office to charge reduced fees for small businesses. No reference is made to the retention of patent rights under the Bayh-Dole Act in the SBA regulations or the Patent and Trademark Office rules.

Banking regulators, as already noted elsewhere in these comments, have developed standards for safety and soundness. These standards are now risk-based and mandate alternative capital calculations for banks with small business obligations. *E.g.*, 12 C.F.R. Part 3, App. A, § 4(i) (Comptroller of Currency risk-based capital standards).[34] The banking regulators mandate that banks, in making this calculation, use the definition of small business developed by the Administrator. By modifying the standards, the Administrator potentially is causing numerous banks to recalculate their needed capital reserves. To compound the SBA's error to analyze the implications of the alteration on bank regulation is the fact that smaller banks are likely to have a higher percentage of their outstanding obligations made to small businesses. Thus, small lending institutions may be doubly affected by the change but the SBA, at least on the public record, failed to address this relatively significant issue.

Congress imposed restrictions on the operations of savings and loan institutions. 12 U.S.C. § 1467a(m). They are limited in making business loans only to small businesses and the Director of the Office of Thrift Supervision is authorized to define, by regulation, the term "small business." *Id*. at § 1467a(m)(4)(E). The Director's simply cross-referenced the Small Business Act and the SBA's size standards in Part 121. 12 C.F.R. § 560.3. The proposed size standard change, then, would affect the types of businesses that can borrow from savings and loans. The SBA's proposed size standard change then has a multiplier effect; it modifies the types of loans that can be made by small savings and loan institutions while rendering some businesses ineligible to obtain debt financing from the savings and loans (be they large or small). No assessment was made of the impact which is even more troubling considering the efforts of the SBA (through the elimination of an appropriation) to reduce the number of institutions that might make loans pursuant to the program established by § 7(a) of the Small Business Act.

Federal Home Loan Banks are permitted to make long-term advances to member institutions in order to provide funds to a community financial institution that lends to small businesses. 12 U.S.C. § 1430. The Board that oversees the Federal Home Loan Banks is authorized to define the term small business and has done so by adopting the standards set forth in Part 121 of the SBA's regulations. 12 C.F.R. § 952.1. Despite the importance of community financial institutions in providing funds to targeted low-income communities, the SBA never assessed the impact that its proposed size standard changes would have on the ability of businesses located in these areas to obtain funds from community financial institutions.

The Securities and Exchange Commission regulates investment companies pursuant to the Investment Company Act of 1940. Registered investment companies are prohibited from undertaking certain types of joint enterprises unless it has submitted a request and obtained approval from the Commission. 17 C.F.R. § 270.17d-1. However, any loan or other advance of credit made to a "small business concern" (the words used in the Commission's regulations) will

[34] Similar rules exist for financial institutions regulated by the Board of Governors of the Federal Reserve, Federal Deposit Insurance Corporation, and the Office of Thrift Supervision.

not be considered a joint enterprise needing prior approval. *Id*. at § 270.17d-1(d)(3).[35] Thus, registered investment companies that currently advance credit to small business concerns, might have to spend significant resources filing an application with the Commission simply due to a modification of the size standards imposed by the SBA. No examination or mention of this impact was identified by the SBA (or at least not identified in the Federal Register notice).

Congress created a program to assist states in providing for vocational education. 20 U.S.C. §§ 2301 et seq. For states to participate, they must establish a state board to provide advice on how such money is spent. 34 C.F.R. § 403.10. Department of Education rules require that at least one member must be the representative of small business concerns. *Id*. at § 403.18(b)(1)(i)(A). Given the significant changes proposed for various sectors of the construction industry, it is certainly conceivable that a business serving on such a board no longer would be eligible if the proposed rule went into effect unchanged.

The SBA proposes to modify its standards for petroleum refiners by extending the 125,000 barrels per calendar day capacity to all federal government programs. 69 Fed. Reg. at 13,136. Although the SBA notes that the Department of Energy uses this standard, the agency failed to mention that it also is changing the status of refiners who are eligible to purchase federal royalty oil from the Outer Continental Shelf. The Minerals Management Service adopts the size of the Administrator. 30 C.F.R. § 208.2. The SBA assesses the implications of the change on the federal government's procurement of petroleum but not on small business purchase of federal property (an analysis the SBA undertakes with respect to timber sales size changes in the proposed rule).

One of the biggest problems facing many businesses is liability under the Comprehensive Environmental Response, Compensation, and Liability Act of 1980 (CERCLA) but known by its common name as the Superfund program. CERCLA imposes a strict, joint and several liability, 42 U.S.C. § 9607(a), on all persons that have contributed hazardous waste to a site that EPA designates. *Id*. at § 9605. In many instances, small businesses, such as restaurants, were being forced to litigate against the federal government and all other contributors as well even though the small businesses may have contributed very little in the way of waste, much less hazardous waste. Congress responded in 2002 with an exemption for small businesses if the waste was municipal solid waste. *Id*. at § 9607(p)(1). Qualification for this exemption entails being a small business concern defined pursuant to the SBA's regulations and having fewer than one hundred employees. *Id*. Modification of the size standards proposed by the SBA could eliminate thousands of restaurants, as well as other businesses, from being able to take advantage of this

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[35] Although the Commission's rules do not define a "small business concern," the typical rule of construction is that, unless the context requires a different result, the same term has an identical meaning irrespective of where it is used. *See White v. Mercury Marine*, 129 F.3d 1428, 1434 (11th Cir. 1997); *Greenwood Trust Co. v. Massachusetts*, 971 F.2d 818, 827 (1st Cir. 1992), *cert. denied*, 506 U.S. 1052 (1993). In the case of the Commission rules, they must be intending to have the term "small business concern" mean the same thing as it does in the Small Business Act because they adopted the use of that specific term rather than the more generic term "small business." *See Gustafson v. Alloyd Co.*, 513 U.S. 561, 570, 575 (1995).

exemption and save themselves significant capital. In some cases, the exemption will enable the small business concern to stay in business. The SBA, in considering the impact on restaurants, failed to notice this important consequence even though the Chief Counsel for Advocacy had spoken favorably of such an exemption from the rigorous CERCLA liability provisions.

The above discussion represents instances in which the term "small business concern" and the SBA's regulations are adopted for other federal regulatory purposes. This exceeds the six identified by the SBA. In fact, this represents only a sample of the instances in which the term "small business concern" or a direct cross-reference to SBA size standards are used by other federal agencies.[36] The point of this peroration is to demonstrate the potential impacts that the size standard proposal has on other agency programs. The SBA had the obligation to assess these impacts and enter a productive dialogue with the Chief Counsel for Advocacy to ensure that these effects were examined in a proper IRFA.

IX. Conclusion

For the foregoing reasons, we believe that the proposed rule, if promulgated without significant change, is legally insufficient and subjects the SBA to substantial litigation risk. Proper rulemaking procedure by the SBA would eliminate the obvious legal inadequacies of the proposal. Nor do we feel that the standards we hold the SBA to are any stricter than a court would use in reviewing the SBA's action. Even if an argument can be made that the SBA is being held to a higher standard in these comments, we believe that it is entirely appropriate. We also believe that the Chief Counsel could have done more outreach to assist the SBA in complying with the RFA and avoiding the potential burdens that could have been imposed on small businesses had the rule been adopted substantially as proposed . The SBA's compliance with the requirements of the RFA for rational rulemaking and compliance with the RFA should

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[36] The following is a list of Code of Federal Regulation citations that utilize the term "small business concern" or cross-reference the SBA size standards or cite the definition of small business as used in the RFA: 7 C.F.R. § 1485.11 (Department of Agriculture's market access program of which SBA should be aware given efforts by cooperatives to have the size standards modified to maintain eligibility), Part 2903; 10 C.F.R. §§ 2.810; 420.2; 760.1; 16 C.F.R. Part 1020; 19 C.F.R. Part 171, App. B, § N; 19 C.F.R. § 213.3; 24 C.F.R. § 570.3; 29 C.F.R. § 2704.104; 34 C.F.R. 472.5; 37 C.F.R. §§ 1.27, 404.3; 40 C.F.R.Part 21, 92.2, 1051.635; 43 C.F.R. §§ 3420.1-3(b)(2), .3472.2-2(d); 49 C.F.R. § 107.612(b)(1). The list does not include programs related to management of federal procurement, timber set-aside programs, programs identical to those already discussed in comments, or programs that cite the term "small business" but do not define the term, such as the Rural Utilities Service's development program or the Department of Commerce's promotion of private sector industrial partnerships with small businesses. The following list of United States Code cites reference the term "small business concern": 5 U.S.C. § 3703; 7 U.S.C. §§ 2009cc-10, 5623, 5923; 12 U.S.C. §§ 635, 3013(b)(1)(A); 13 U.S.C. § 91(d)(4)(A); 15 U.S.C. § 1841 note, § 201(c); 15 U.S.C. §§ 3703(12), 4721(j)(6); 22 U.S.C. § 6729(c)(1); 29 U.S.C. § 3031(a); 31 U.S.C. § 3554(c)(2) (relating to payments for experts and attorneys in bid protests before Comptroller General); 38 U.S.C. § 3742; 42 U.S.C. § 1883; 42 U.S.C. §§ 4012(a), 4013(b)(1)(B), 5512, 5591, 5801, 5919(w), 6881(a)(3), 7661f(c)(1), 9211; 44 U.S.C. § 3506(c)(4) (mandating that Administrator of OIRA reduce paperwork burdens on small business concerns defined pursuant to Small Business Act); and 49 U.S.C. § 13709(h) (special provisions for resolving claims of small business concerns who shipped goods with bankrupt motor carriers).

with the requirements of the RFA for rational rulemaking and compliance with the RFA should be held to the highest possible standards. In particular, if the SBA, the agency charged with promoting the interests of small businesses in the federal government, is unwilling to comply with the RFA, other agencies will see less of a reason to comply. The SBA should be the exemplar that all other agencies follow when protecting small business concerns from adverse and untoward regulation.

We are pleased that SBA has decided to withdraw the rule and commence a more deliberative process that mirrors the procedures utilized by the agency when it last made a general overhaul of its size standards between 1980 and 1984. We will be paying close attention to ensure that the rulemaking process comports with the overall mandates of the APA and the RFA – ensuring that any modification to the size standard rules are rational and designed to minimize burdens on small business concerns. This again demonstrates the need not only to examine the impact of the size standard changes on SBA programs but also to examine how those changes will affect business concerns currently designated as small for other purposes but not so designated after the size standard change. Close cooperation with the Office of Advocacy and OIRA will prove particularly helpful in this regard. Should the SBA's rulemaking process stray from these basic principles of agency decisionmaking and result in a rule that unnecessarily burdens small businesses, we will have no alternative but to take appropriate legislative action.

Sincerely,

Donald A. Manzullo
Chairman

Nydia M. Velázquez
Ranking Democratic Member