

**GOVERNMENT CODE CHAPTER 2006
SMALL BUSINESSES and RURAL COMMUNITIES
IMPACT GUIDELINES**

Updated: December 2017

The 80th Legislature adopted HB 3430 which, among other things, requires that, as part of the rulemaking process, state agencies prepare an Economic Impact Statement that assesses the potential impact of a proposed rule on small businesses and a Regulatory Flexibility Analysis that considers alternative methods of achieving the purpose of the rule if the proposed rule will have an adverse economic effect on small businesses. The 85th Legislature adopted HB 3433 which adds rural communities to the requirements set out in chapter 2006 of the Texas Government Code. HB 3430 and HB 3433 both require that the Attorney General, in consultation with the Comptroller, prepare guidelines to assist agencies in determining a proposed rule's potential adverse economic effect(s) on small businesses and rural communities, and in identifying and evaluating alternative methods of achieving the purpose of the proposed rule. Please note that these are guidelines only to assist state agencies in performing their own analysis to evaluate the impact of their proposed rules. These guidelines do not add to the statutory requirements contained in chapter 2006 of the Texas Government Code.

Attached to these guidelines are the following examples: Economic Impact Statement and Regulatory Flexibility Analysis; Statement Regarding the Public Health, Safety, and Welfare; and Rural Communities Impact Statement and Regulatory Flexibility Analysis for Rule Affecting Rural Communities.

I. REQUIREMENTS

The requirements for an Economic Impact Statement and Regulatory Flexibility Analysis are set forth under sections 3 of HB 3430 (80th) and HB 3433 (85th), which amend Texas Government Code § 2006.002. HB 3433 adds a definition to Texas Government Code § 2006.001(1-a) to define "rural community" as a municipality with a population of less than 25,000.

HB 3430 and HB 3433 require that before adopting a rule that may have an adverse economic effect on small businesses or rural communities a state agency shall prepare an Economic Impact Statement that separately estimates the number of small businesses and rural communities subject to the proposed rule, projects the economic impact of the rule on small businesses and rural communities, and describes

alternative methods of achieving the purpose of the proposed rule. An agency's consideration of alternative methods must be set forth in a Regulatory Flexibility Analysis (§ 2006.002(c)). The agency must consider using alternative regulatory methods that will accomplish the objectives of regulation while minimizing adverse impacts on small businesses and rural communities if those alternative methods are consistent with the health, safety, and environmental and economic welfare of the state. The state agency must include in the analysis several proposed methods of reducing the adverse impact of a proposed rule on small businesses and rural communities (§ 2006.002(c-1)). Each agency must assess for itself the quality and quantity of the data needed to prepare an Economic Impact Statement for a proposed rule.

The Economic Impact Statement and Regulatory Flexibility Analysis must be included in the notice of the proposed rule (§ 2006.002(d)). Copies of the notice of the proposed rule that are submitted to the *Texas Register* must also be provided to the Senate and House standing committees that are charged with reviewing the proposed rule (§ 2006.002(d)). Additionally, an agency must provide copies to each member of the legislature who represents a rural community adversely impacted by the proposed rule, if feasible. (§ 2006.002(d)(2)).

Section 2006.002, as amended by HB 3433, applies to a rule that is proposed on or after September 1, 2017.

II. OUTLINE OF REQUIRED STEPS

Is an Economic Impact Statement required?

Would the proposed rule have an adverse economic effect:

- 1) on small businesses?; or
- 2) on rural communities?

If the answer to either question is yes, an agency must prepare an Economic Impact Statement that includes:

- An estimate of the number of small businesses and/or rural communities subject to the proposed rule;
- A projection of the economic impact of the proposed rule on small businesses and/or rural communities; and

- A Regulatory Flexibility Analysis, which reflects an agency's consideration of the alternative methods described in the Economic Impact Statement, that must include:
 - o Consideration of the use of regulatory methods that will achieve the purpose of the proposed rule while minimizing adverse impacts on affected small businesses and/or rural communities, if consistent with the health, safety, and environmental and economic welfare of the state; and
 - o An analysis of several proposed methods of reducing the adverse impact of the proposed rule on affected small businesses and/or rural communities.

Notice and Comment is required:

- Include the Economic Impact Statement and the Regulatory Flexibility Analysis in the notice of the proposed rule in the *Texas Register*. Provide copies to the standing committees of each house of the legislature that is charged with reviewing the proposed rule. Provide copies of the proposed rule to all members of the legislature representing adversely affected rural communities, if feasible.
- Respond to any comments on the Economic Impact Statement and Regulatory Flexibility Analysis as required in any adoption preamble.

III. WHAT IS A SMALL BUSINESS?

As provided under § 2006.001(2), a small business is a legal entity that is:

- 1) for profit;
- 2) independently owned and operated; and
- 3) has fewer than 100 employees or less than \$6 million in annual gross receipts.

Each of these three elements should be met for an entity to qualify as a small business under § 2006.001(2). A business must be operated for profit. Consequently, rules that apply exclusively to non-profit and governmental entities need not comply with § 2006.001(2).

Independently owned and operated businesses are self-controlling entities that are not subsidiaries of other entities or otherwise subject to control by other entities and entities that are not publicly traded. To qualify as a small business, an entity must have either fewer than 100 employees or less than \$6 million in annual gross receipts. Practically, the standard of fewer than 100 employees will be the easiest to determine and implement. Data on an entity's annual gross receipts are generally not publicly available.

In some cases, individual persons licensed by an agency might be small businesses. Whether an individual licensee might be a small business will depend upon the nature of the regulated profession or trade and the governing statute. An agency should look to see if any of its licensees might practice as small businesses.

IV. WHAT IS A RURAL COMMUNITY?

Section 2006.001(1-a) defines a rural community as any “municipality with a population of less than 25,000.”

V. ADVERSE ECONOMIC EFFECT

Section 2006.002(c) requires that “[b]efore adopting a rule that may have an adverse economic effect on small businesses, or rural communities, as applicable, a state agency shall prepare” an Economic Impact Statement and Regulatory Flexibility Analysis. One of an agency's first inquiries should be whether a proposed rule may have an adverse economic effect on small businesses or rural communities.¹ If a proposed rule will not have an adverse economic effect on small businesses or rural communities, an agency should include a finding to that effect in the notice of the proposed rule. An agency is not required to prepare an Economic Impact Statement and Regulatory Flexibility Analysis if there is no adverse economic effect.² An agency should, however, provide a reasoned explanation in the preamble for the

¹ Courts have not interpreted the meaning of “adverse effect” under § 2006.002. See *Unified Loans, Inc. v. Pettijohn*, 955 S.W.2d 649 (Tex. App.—Austin 1997, no pet.). Merriam-Webster's Dictionary defines “adverse” as “acting against or in a contrary direction,” “opposed to one's interests,” and “causing harm.” <http://www.merriam-webster.com/dictionary/adverse>.

² *Tex. Shrimp Ass'n v. Tex. Parks & Wildlife Dep't*, No. 03-04-00788-CV, 2005 WL 1787453, at *6 (Tex. App.—Austin July 27, 2005, no pet.) (mem. op.) (“The requirements in section 2006.002 are not absolute, but rather are conditioned on the adoption of ‘a rule that would have an adverse economic effect on small businesses.’” (quoting Tex. Gov't Code § 2006.002(c) (West 1993))).

proposed rule as to why an Economic Impact Statement and Regulatory Flexibility Analysis is not required for the proposed rule.³

Adverse economic effects can include mandatory costs incurred by a small business for compliance with a proposed rule and may include a loss of business opportunities as the result of the regulation. Adverse economic impacts to rural communities may include mandatory costs incurred by the communities to comply with the new rules that are disparate from the economic impact that the rule would have on a larger municipality. If the rule imposes a direct cost, such as a fee, to a local government, that cost should appear in both the rural communities impact statement and the local government fiscal note required by Administrative Procedure Act (APA) § 2001.024(a)(4)(D). Tex. Gov't Code § 2001.024(a)(4)(D). Similarly, if the rule's adverse economic impact to a rural community will result in harm to a local economy, that information should be included in, or clearly cross-referenced to the local employment impact statement required by APA §§ 2001.022 and 2001.024(a)(6). Tex. Gov't Code §§ 2001.022, .024(a)(6).

What constitutes an adverse economic impact may depend upon the characteristics of a regulated industry, or rural community, and upon the effect of a proposed rule. However, an agency need only consider direct adverse economic effects. An agency need not consider indirect economic effects, such as impacts on small businesses that are not regulated entities.⁴ Generally, there is no need to examine the indirect effect of a proposed rule on entities outside of an agency's regulatory jurisdiction.

³ An objective of statutes such as § 2006.002 “is to afford adequate notice—to place the agency’s assessment before interested persons in advance in order that (1) interested persons might comment intelligently on the proposed rules and (2) the agency might exercise intelligently its responsibilities in arriving at the contents of the rule as finally adopted, in stating reasons for and against adoption, and in formulating the required contents of the adopting order, including a ‘reasoned justification’ for the rule.” *Unified Loans*, 955 S.W.2d at 652.

⁴ Courts have held that the federal Regulatory Flexibility Act, 5 U.S.C. §§ 601-12, applies only to direct economic impacts. *See Mid-Tex Elec. Coop. v. Fed. Energy Regulatory Comm’n*, 773 F.2d 327 (D.C. Cir. 1985) (regulations for generating utilities did not need to consider potential adverse effect on transmission utilities); *Am. Trucking Ass’ns v. U.S. Env’tl. Prot. Agency*, 175 F.3d 1027 (D.C. Cir. 1999) (EPA’s national ambient air quality standards did not have a direct impact on small entities which were regulated directly through state implementation plans), *aff’d in part, rev’d in part on other grounds, Whitman v. Am. Trucking Ass’ns*, 531 U.S. 457 (2001); *United Distribution Cos. v. Fed. Energy Regulatory Comm’n*, 88 F.3d 1105, 1170 (D.C. Cir. 1996) (Regulatory flexibility analysis provision applies only to small entities that are subject to the requirements of the rule and the agency had no obligation to analyze the effects on entities which it did not regulate.).

However, an agency should carefully evaluate a proposed rule where an indirect effect may be of particular concern, such as the impact of a proposed rule on other regulated entities.

Adverse economic effects need not be limited to regulatory programs. Adverse economic effects should be explored to determine whether they could be associated with grant programs or other voluntary programs.

VI. ECONOMIC IMPACT STATEMENT AND REGULATORY FLEXIBILITY ANALYSIS

Agencies should make a reasonable, good-faith effort to prepare an Economic Impact Statement and Regulatory Flexibility Analysis that will provide the public and the affected small businesses or rural communities with information about the potential adverse effects of the proposed rule and about potentially less-burdensome alternatives.⁵ Substantial compliance requires that the Economic Impact Statement provide interested persons with an opportunity to comment intelligently on the basis for an agency's projected economic impact of a proposed rule on small businesses or rural communities.⁶

An agency should individually analyze the impacts of each proposed rule or rule amendment. While an agency may be able to take advantage of the data and analysis compiled as part of an Economic Impact Statement for a prior rulemaking, the agency should confirm that the data are appropriate for each proposed rule.

A. Determining the Number of Small Businesses

To know whether a proposed rule affects a number of small businesses, an agency must first know how many regulated entities exist and which are small businesses. For some agencies that regulate only one industry or profession, this may require determining only how many of the businesses that the agency regulates meet the definition for a small business. For some agencies, most of their regulated individuals and entities, if not nearly all, may qualify as small businesses.

⁵ See *S. Offshore Fishing Ass'n v. Daley*, 995 F.Supp. 1411, 1437 (M.D. Fla. 1998) (interpreting the federal requirement to examine impacts on small entities). One court required that a federal agency consider comments not submitted during the formal notice and comment period because the agency's proposed rule did not properly inform the regulated industry that its interests were at stake. *Nw. Mining Ass'n v. Babbitt*, 5 F.Supp.2d 9 (D.D.C. 1998).

⁶ See *Unified Loans*, 955 S.W.2d at 652-54.

The most readily determinable factor will be whether a for profit, independently owned and operated business has fewer than 100 employees. If a business does, then it is clearly a small business and an economic impact statement and regulatory flexibility analysis should be prepared if the proposed rule would have an adverse economic effect on the small business.

The Comptroller of Public Accounts has developed a web site to assist agencies in determining a proposed rule's potential adverse economic effect on small businesses (<https://fmx.cpa.state.tx.us/fmx/legis/ecoeffect/>). Additional information on employers with fewer than 100 employees is available from the Texas Workforce Commission's TRACER web site (www.tracer2.com).

An agency that regulates only one industry or profession may only need to conduct this analysis once to determine the number and/or percentage of small businesses that it regulates. That analysis can then be used in future rulemakings, however, the analysis should be reviewed and updated periodically to reflect changes in the number of regulated businesses or changes to the agency's jurisdiction. An agency may wish to review and revise the analysis during each four-year rule review to ensure continued accuracy.

Agencies that adopt rules affecting multiple industries will likely need to determine for each proposed rule the number of small businesses that may be affected. The first step in this analysis would be to identify the industry sectors to be regulated. In the past, many agencies used the Standard Industrial Classification (SIC) codes to categorize regulated businesses on an industry-by-industry basis. In 1999, the SIC system was replaced by the North American Industry Classification System (NAICS), which breaks down industry sectors in much greater detail.

For a grant program or other voluntary program, an agency can develop an estimate of the number of small businesses affected by anticipating the potential number of applicants and potential number of grant recipients. The number of applicants from past years of a program could be used as examples, or the number of applicants for similar programs can be used as the basis for an estimate. An agency should strive to provide some reasoned explanation for an estimate of the number of applicants and the methodology and quality of the data used to derive the estimate.

An agency does not need to provide an exact accounting of the number of small businesses that a proposed rule may affect.⁷ The number of businesses may be reported as an approximation, such as “more than,” or in a range such as: 1-100, 101-500, 501-1000, 1001-5000, 5001-10,000, or 10,000+.

In some instances, an agency may regulate businesses that are located outside of Texas. In that case, an agency should look to see whether any of these businesses are small businesses that should be included in the number that the proposed rule might affect. However, an agency need only assess the general adverse effect of a proposed rule on small businesses doing business in Texas; it need not perform a detailed analysis of how a proposed rule might have a different effect, if any, on small businesses that are located outside of Texas.

B. Determining the Number of Rural Communities

Section 2006.002(1-a) defines a rural community as a municipality with a population of less than 25,000. This is an objective measure that should be determined by reference to data available through the Texas Demographic Center. Population estimates are published at <http://txsdc.utsa.edu/Data/TPEPP/Estimates>.

As is the case with small business impact analysis, an agency need only assess the general adverse effect of a proposed rule on rural communities within Texas.

C. Projecting the Economic Impact

Under § 2006.002(c)(1), an agency is required to project the economic impact of a proposed rule on small businesses and rural communities if the proposed rule may have an adverse economic effect. Every rule is different. The level, scope, and complexity of analysis may vary significantly depending on the characteristics and composition of the industry or small-entity sectors to be regulated. The projection need only assess the potential adverse economic effects on small businesses or rural communities.

Agencies are also required, under § 2006.002(f), to reduce the adverse effect of rules on micro-businesses. Under § 2006.001(1), a micro-business is defined as a legal entity that is for profit, independently owned and operated, and has no more than 20 employees. Consequently, the number of micro-businesses in a regulated industry

⁷ See <https://www.sba.gov/advocacy/guide-government-agencies-how-comply-regulatory-flexibility-act>.

or profession is a subset of the number of small businesses. In some instances, however, a proposed rule may have a disparate effect on micro-businesses as compared to small businesses. An agency's projection of economic impact should include an analysis as to whether a proposed rule may have an adverse effect on micro-businesses distinct from any potential adverse effect on small businesses.

Examples of the costs associated with a proposed rule may include:

- recordkeeping;
- reporting;
- requiring professional expertise, such as legal counseling, accounting, or engineering;
- capital costs for any required equipment;
- costs for modifying any existing processes and procedures;
- lost sales and profits resulting from the proposed rule;
- changes in market competition as a result of the proposed rule and its effect on the balance between specific submarkets;
- extra tax costs;
- additional employees that may need to be hired; and
- required fees.

D. Regulatory Flexibility Analysis

In preparing the Regulatory Flexibility Analysis, as required under § 2006.002(c)(2), an agency must consider alternative methods of achieving the purpose of the proposed rule. As provided under § 2006.002(c-1), the alternatives should:

- be consistent with the health, safety, and environmental and economic welfare of the state;
- accomplish the objectives of the rule;
- minimize adverse impacts on small businesses; and
- minimize adverse impacts on rural communities.

An agency must also include in the analysis several proposed methods of reducing the adverse impact of a proposed rule on small businesses or rural communities. The

Regulatory Flexibility Analysis and Economic Impact Statement can be combined into a single report.

1. Exception for the Public Health, Safety, and Welfare

Under § 2006.002(c-1), an agency must consider—if consistent with the health, safety, and environmental and economic welfare of the state—using regulatory methods that will accomplish the objectives of applicable rules while minimizing adverse impacts on small businesses. An agency is not required to consider alternatives that, while possibly minimizing adverse impacts on small businesses, would not be protective of the health, safety, and environmental and economic welfare of the state.⁸ For example, a legislative or federal mandate that requires an agency to adopt as rules specific fees or specific standards and procedures may not be subject to alternative policy choices. In such a situation, the mandated language may be considered *per se* consistent with the health, safety, or environmental and economic welfare of the state and the agency need not consider other regulatory methods. Thus, the agency may lack discretion to implement another alternative rule. Other situations may not be as clear, and each agency should exercise professional discretion and expertise in making this determination. It is recommended that this *per se* exception be narrowly applied, for example in situations where the governing standard has left the agency with no discretion as to the standard to be applied and the method for implementing the rule. It is helpful if the agency states that this exception applies to a specific rule, so that if challenged in court, the agency’s rationale for not undertaking the analysis is transparent.

2. Alternatives Analysis

The available alternatives possible will vary based on the particular regulatory objective and the characteristics of the regulated industry. Examples of alternatives that an agency may identify and evaluate include:

- Establishment of different compliance or reporting requirements for small businesses or rural communities or timetables that take into account the resources available to small businesses and rural communities;
- Clarification, consolidation, or simplification of compliance and reporting requirements for small businesses and rural communities;

⁸ Protection of the public health, safety, and welfare is part of the inherent power of a sovereign state. *See Barshop v. Medina Cty. Underground Water Conservation Dist.*, 925 S.W.2d 618, 633-35 (Tex. 1996).

- Use of performance rather than design standards;
- Implementation of different requirements or standards for micro-businesses;
- Exemption for certain or all small businesses from coverage of the rule, in whole or in part;
- Adopting different standards for the size of businesses or size of the local government unit;
- Modifying the types of equipment that are required for large and small businesses or rural communities; and
- The effect of not adopting the proposed regulation, a “no action” alternative.

It is recommended that an agency consider including in the analysis several methods of reducing the adverse impact of a proposed rule on small businesses.

VII. REVIEW AND COMMENT ON THE ECONOMIC IMPACT STATEMENT AND REGULATORY FLEXIBILITY ANALYSIS

Section 2006.002(d) provides that an agency must “include the economic impact statement and regulatory flexibility analysis as part of the notice of the proposed rule that the agency files with the secretary of state for publication in the Texas Register.” Thus, it is advisable to include the Economic Impact Statement and Regulatory Flexibility Analysis in the preamble for a proposed rule along with other required findings such as the fiscal note and note on public benefits and costs required under APA § 2001.024(a)(4) and (a)(5).⁹

Pursuant to § 2006.002(d)(1), an agency must also provide copies of the notice of the proposed rule, which includes the economic impact statement and the regulatory flexibility analysis, to the standing committee of each house of the Legislature that is charged with reviewing the proposed rule. Typically, these will be the legislative committees that have primary jurisdiction over the agency or over the area of law or the subject matter under which the rule is adopted. In addition, the agency must provide copies, if feasible, to each member of the legislature who represents a rural

⁹ A court has held that § 2006.002 constitutes “any other statement required by law” which must be included in the notice of a proposed rule as described under § 2001.024(a)(8) of the APA. *Unified Loans*, 955 S.W.2d at 651.

community adversely impacted by the proposed rule. Tex. Gov't Code § 2006.002(d)(2).

While the Economic Impact Statement and Regulatory Flexibility Analysis are not required to be included in the preamble for the rule adoption, an agency should respond to any comments received regarding the Economic Impact Statement and Regulatory Flexibility Analysis as required under APA § 2001.029.

VIII. QUESTIONS

For further information or a response to any questions that you may have regarding these guidelines, please contact:

Nichole Bunker-Henderson
Chief, Administrative Law Division
OFFICE OF THE ATTORNEY GENERAL OF TEXAS
(512) 475-4300
Nichole.Bunker-Henderson@oag.texas.gov

David Gordon
Assistant Attorney General, Administrative Law Division
OFFICE OF THE ATTORNEY GENERAL OF TEXAS
(512) 475-4300
David.Gordon@oag.texas.gov

Doyle R. Fuchs
Director, Labor Market and Career Information
TEXAS WORKFORCE COMMISSION
512) 936-3105
Doyle.Fuchs@twc.state.tx.us

APPENDIX

The following are examples only and are not intended to reflect the level of detail required for all agency rulemaking actions.

Example: Economic Impact Statement and Regulatory Flexibility Analysis

The Board has approximately 5,000 doctor of chiropractic licensees and 3,000 registered facilities, and nearly all of these entities are small businesses and many of them are micro-businesses. The projected economic impact of this rule amendment on these small businesses will be neutral to positive for licensees and clinics in that licensees will be able to more effectively use their practice time by delegating approved tasks to qualified assistants when appropriate. In preparing this proposed rule, the Board considered several alternative methods for achieving the purposes of this rule amendment. The Board considered requiring, under proposed subsection (j), that each person performing treatments sign the patient records, but this was rejected as excessively burdensome recordkeeping. The Board considered not modifying the standards for “qualified and properly trained” in proposed subsection (d), but the Board decided that the public welfare would benefit from clearer standards. The Board considered adopting more specific standards regarding the required education, training, and skills of personnel, but the Board decided instead that it would be easier for licensees to implement the general standards included in the proposed rule under subsection (d).

Example: Statement Regarding the Public Health, Safety, and Welfare

The Agency estimates that there are approximately 7,500 widget manufacturers in Texas and that approximately nine out of ten of these manufacturers are small businesses and that three out of ten are micro-businesses. The Agency estimates that the projected economic impact of this proposed rule will be increased costs of compliance for safety training and reporting. Under § 2006(c-1), an agency is required to consider alternative regulatory methods only if the alternative methods would be consistent with the health, safety, and environmental and economic welfare of the state. The Agency has developed this proposed rule in accordance with a legislative mandate and in compliance with the requirements of the regulations of the U.S. Environmental Protection Agency. Consequently, any variance from the federal standards would not be consistent with the health, safety, and environmental and economic welfare of the state, and no alternative regulatory methods have been considered.

Example: Rural Communities Impact Statement and Regulatory Flexibility Analysis for Rule Affecting Rural Communities

The Department acknowledges that a prohibition on lead ammunition under the size restrictions designated in this proposed rule could have a potential adverse economic impact on rural communities that attract hunters during permissible bird hunting seasons. After undertaking a review of bird hunting licenses issued in fiscal year 2016, the Department estimates that approximately 250 rural communities in Texas may be impacted by the proposed rule. However, the proposed rule's projected economic impact is likely neutral because lead ammunition that would still be permitted by the rule's size restrictions is widely available by commercial retailers. Further, lead ammunition allowable under the rule has been shown to be equally effective for bird hunting purposes. In developing the proposed rule, the Department considered alternative methods of achieving the purpose of the proposed rule. Specifically, the Department considered adjustment of the ammunition size restrictions to limit the environmental impacts of small lead particulates. The Department also considered more restrictive measures that would have prohibited the use of lead ammunition entirely. Ultimately, the Department determined that it could prevent lead contamination consistent with the mandates outlined by the Legislature while simultaneously allowing ammunition sizing that would not impact the economic activity generated from hunting in rural communities.