

## **Rising Regulatory Costs Hit Small Firms Hardest**

The annual costs of federal regulations in the United States rose to \$1.75 trillion in the United States in 2008, before many large, new government programs were enacted. Regulatory costs in 2008 accounted for 14 percent of national income, or a burden of \$15,586 on the average household. By the end of 2010, the burden would have substantially exceeded that level. Regulatory costs are equivalent to an additional, hidden tax on each person and business.

A recent study for the Office of Advocacy of the U.S. Small Business Administration, by Nicole and Mark Crain, economic professors at Lafayette College, estimated annual costs of regulation per employee in all businesses was \$8,086. However, small businesses (defined as those with fewer than 20 workers) incurred regulatory costs of \$10,585 per employee, compared to \$7,454 for medium sized firms (20 to 499 workers) and \$7,755 for large firms with 500 or more employees. That is, regulatory costs per employee for small firms were 42 percent higher than for medium-sized firms and 36 percent higher than for large firms.

In 2008, small firms accounted for 89.3 percent of all non-farm firms in the U.S., 18 percent of all employees and 15 percent of all non-farm payrolls, so their economic clout was significant.

Higher regulatory costs for small firms was common throughout all industries and service businesses. Environmental regulations were a particularly heavy burden on small businesses, making up 39 percent of all regulatory costs, compared to only 17 percent for medium firms and 11 percent for large firms. Since most regulatory costs are fixed, larger firms can benefit from economies of scale in reducing the burden per unit.

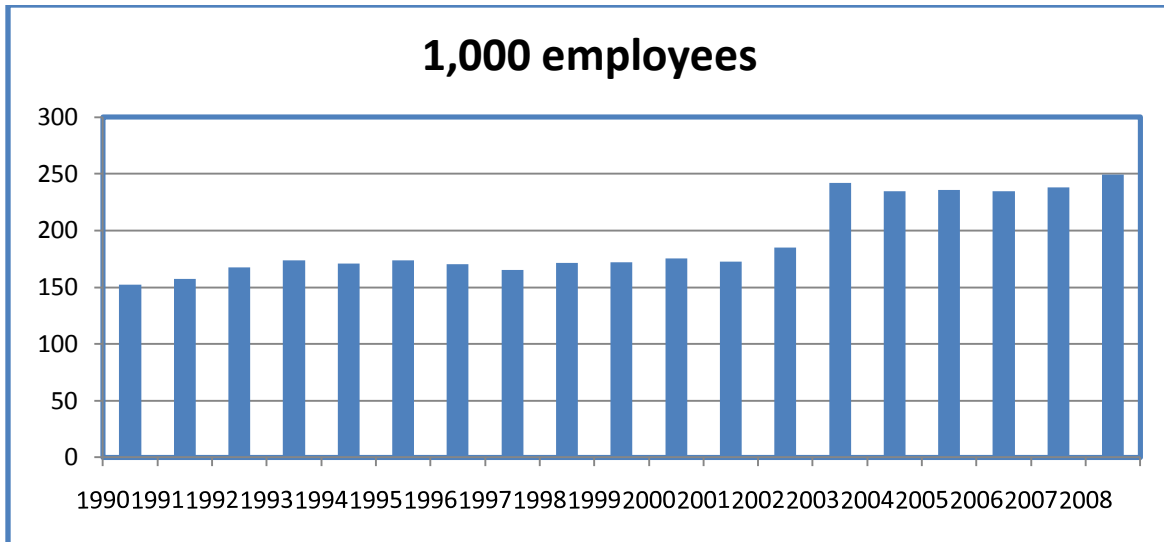
The authors concluded that small businesses bear a proportionately large share of the costs of complying with regulation and that such costs are a major factor in causing businesses to close, reallocate activity or pass on costs to customers. Since small businesses are the engine of job creation in the modern economy, the negative effects of regulation can offset positive steps by government to stimulate economic growth.

### **Homeland Security Costs Soar**

Between the attack on the New York World Trade Center in September 2001 and the end of 2008, 17 homeland security regulations added \$10.4 billion to U.S. regulatory costs for such items as securing transportation facilities and chemical plants, electronic availability of passenger manifests, cargo security, notice of imported food, and regulation of food facilities that might be vulnerable to bioterrorism.

After rising rapidly in the early-1990s, the number of federal regulatory employees stagnated for the next 8 years. The expansion of Homeland Security concerns was responsible for much of the bump up in federal regulatory employees after 2001. The subsequent surge in 2008 was probably just the beginning of a new wave of expansion as many federal agencies gained new responsibilities under various stimulus and bailout packages.

## **United States: Federal Regulatory Activity, Fiscal Years ending September, 1990-2008 (Full-time Equivalent Employees)**



Source: Crain, Nicole V and W. Mark Crain. "The Impact of Regulatory Costs on Small Firms," Small Business Administration, Office of Advocacy, September 2010.

#### **Impact of Regulation on the Agricultural Sector**

Unfortunately, the study by Crain and Crain did not include firms in the agricultural sector of the economy. However, it is likely that agricultural firms were most affected by environmental regulations, like firms in manufacturing and mining.

Previous articles in the World Apple Report have documented some of the regulatory burdens on agriculture. In "The Regulatory Threat to Agriculture", March 2007 issue, page 7, we cited a survey of California farmers where over 44% of responding farmers classified the regulatory environment in California as either complex or very complex. In coping with regulations, "A staggering 45.2% had considered leaving agricultural production, 44.5% had considered reducing operation size, 31.6% had considered increasing operation size and about one in six producers (16.4%) had considered moving operations out of California."

An article in the March 2010 issue of the World Apple Report, "Food Safety Compliance Costs", cited estimates by Hardesty and Kusunose of "Growers' Compliance Costs for the Leafy Greens Marketing Agreement." The average costs of one-time modifications needed to come into compliance were \$13.60 per acre. Seasonal food safety costs had more than doubled from \$24.03 per acre in 2006 to \$54.63 per acre in 2007 to keep operations in compliance. The authors surmised that under a full accounting, compliance costs would come close to \$100 per acre.

During interviews to prepare a strategic plan for Washington State Agriculture to 2020 and Beyond (published in 2010), producers and agribusinesses complained frequently about the problems that various regulations were creating for their competitiveness, sustainability and ability to keep the next generation in farming. The second major recommendation of the strategic plan was "Eliminate Regulatory Barriers." The more detailed recommendation was to "Assess and reform the accumulated and complex regulations impacting agriculture to promote the competitiveness of farming in Washington".

#### **Uncertain Future of Renewed Debate**

The debate over the proper role of government intervention and regulation has spilled over into national elections in many countries. The results of those elections could influence whether the new governments will ride the current wave of regulatory expansion, or take the difficult path of assessing and (where necessary) reforming the complex of regulations. The decisions made in the next few years will have a major influence on the long-term viability of U.S. farmers and of foreign farmers that supply the U.S. market.

**First published in the World Apple Report, November 2010, page 7.**