

## The Importance of Regulatory Flexibility for California Small Businesses

### **What is a Flesch Reading Ease Score Anyway?**

In 1996, Congress passed the Gramm-Leach-Bliley Financial Services Modernization Act which includes provisions to protect consumers' nonpublic personal information held by financial institutions, including insurance companies. In 2003, the California Department of Insurance (CDI) issued new privacy regulations to implement the federal law.

Among other things these regulations clarify the standards for privacy notices and opt-out notices to ensure that they are helpful to and readable by consumers, and they establish guidelines for safeguarding the confidentiality of personally identifiable information. In particular, they require agents, brokers and insurers to provide a privacy notice to consumers and to give consumers the opportunity to "opt-out" from having personal information shared.

The CDI regulations also provide complicated details on the required contents of a privacy notice. For example notices must be "clear and conspicuous" which is defined as a notice that is "reasonably understandable." Notice is "reasonably understandable" if, for example, it achieves a minimum Flesch Reading Ease Score of 50. To determine this score the licensee must work a complicated formula that takes into account the average sentence length and average number of syllables per word. The higher the score, the easier it is to understand the document.

During the rulemaking process, the CDI determined that the proposed rules would not have a significant impact on small business and therefore did not solicit small business input. However, the regulations are having a significant impact on small business as they are repeatedly required to send numerous privacy notices to their customers. Initially, notices are required for new customers, again any time there are privacy notice changes and again on an annual basis to allow them to shop for less expensive insurance rates for their customers. These rules require more paperwork, more staff, and more administrative costs such as filing and storing opt-in and opt-out documentation, and sending self-addressed stamped return envelopes or obtaining a toll-free number to comply every time a privacy notice is sent.

A successful state regulatory flexibility scheme requires agencies to consider the economic impact of a proposed rule on small businesses and to consider less burdensome alternatives. Allowing small business to voice their concerns early in the rulemaking process enables the agency to craft a regulation that accomplishes their objective while also achieving greater compliance by the regulated entities. A strong regulatory flexibility law may have helped avoid the situation that resulted in California.