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September 18, 2006

Federal Trade Commission
Office of the Secretary
Room H-135 (Annex M)
600 Pennsylvania Avenue, NW
Washington, DC 20580

Re: Comments on Joint Notice of Proposed Rulemaking – The Red Flags Rule, Project No. R611019

To Whom It May Concern:

The National Federation of Independent Business (NFIB) and the NFIB Legal Foundation hereby submit these comments on the joint notice of proposed rulemaking (JNPRM), "Identity Theft Red Flags and Address Discrepancies Under the Fair and Accurate Credit Transactions Act of 2003." This proposed rulemaking would implement sections 114 and 315 of the Fair and Accurate Credit Transactions Act of 2003 (FACT Act).

NFIB is the nation's leading small-business advocacy association, with offices in Washington, D.C. and all 50 state capitals. Founded in 1943 as a nonprofit, nonpartisan organization, NFIB's mission is to promote and protect the right of its members to own, operate and grow their businesses. The NFIB Legal Foundation, a nonprofit, public-interest law firm established to be the voice for small business in the nation's courts and the legal resource for small business, is the legal arm of NFIB.

NFIB, its members, and the Legal Foundation appreciate the hard work of Federal Trade Commission staff in working to ensure that the identities of customers are protected. We share this commitment.

However, NFIB and the Legal Foundation believe that FTC has grossly underestimated the burden that its requirements will have on the 11.1 million affected entities, particularly with regard to section 114. This is because FTC has made flawed assumptions about the time it would take the affected entities to educate themselves about the requirements, develop and implement plans, train staff and fill out paperwork. FTC has also, we believe, made an inaccurate assumption with regard to which staff will actually be performing the duties required to comply with section 114.

FTC suggests that the average annual labor costs associated with section 114 are \$134,621,000. That equals just \$12.13 per year in total compliance costs for each of the 11.1 million entities FTC estimates will be affected.

FTC has Underestimated the Burden on ‘High-Risk’ Entities

FTC estimates that there are 93,487 high-risk entities. It also estimates that it would take these entities an average of 25 hours to set up their program, with a subsequent annual implementation burden of one hour; a training time of two hours, plus a subsequent annual training burden of one hour; and time to prepare an initial annual report of four hours, with a subsequent annual burden of one hour. Averaged over a three-year period, this equates to 12 hours and 20 minutes per high-risk entity, equaling \$36,896,203 or \$394.67 per year per entity. FTC uses an estimate of \$32 per hour for the labor rate for these entities – while we also used this rate in our estimates, an NFIB Small Business Poll conducted by Gallup found the average cost of paperwork for small business to be more than \$48¹.

We believe however, that even if one assumes that the 25 hour setup estimates are accurate, the remaining yearly approximations are underestimated. Despite being familiar with systems for verifying credit information, the systems are still complex – especially for small businesses that have no expert staff. We estimate, based on our knowledge of members that would be considered high-risk entities, that it would take at least eight hours to find the information, three hours to assess it, another three to organize it, and another six to do the paperwork for a total of 20 hours annually after the initial setup. Based on our figure, it would take an average of 21 hours and 40 minutes per high-risk entity (45 hours/3 years = 21:40). This equals \$64,817,654 or \$693.33 per year per entity at the FTC estimate of \$32 per hour.

We also believe that automobile dealers should be considered high-risk entities for the purposes of this regulation. Therefore, the average annual cost of \$693.33 for high-risk entities multiplied by the 173,115 auto dealers that the FTC estimates would cost these entities a total of \$120,025,823 per year. When you combine our high-risk total with the total for the auto dealers, the estimated labor costs associated for compliance for these entities is \$184,843,477.

FTC has Underestimated the Burden on ‘Low-Risk’ Entities

FTC estimates that there are 10,813,525 low-risk entities. It also estimates that it would take these entities an average of 20 minutes to set up their program, with a subsequent annual implementation burden of five minutes; an initial training time of 10 minutes, plus a subsequent annual training burden of five minutes; and time to prepare an initial annual report of 10 minutes, with a subsequent annual burden of five minutes. Averaged over a three-year period, this equates to 23 minutes per low-risk entity, equaling \$66,320,000 or \$6 per year per low-risk entity.

NFIB and the Legal Foundation find two aspects of this estimate troublesome. First, FTC assumes that administrative personnel will perform all functions of this process, from start to finish, at a rate of \$16 per hour. We believe that in fact, the owners, operators, or senior management of low-risk entities will take it upon themselves to fulfill each company’s legal obligations. This will occur because the low-risk entities that are small businesses (which FTC estimates at 90 percent) have no expert staff to perform this function and the owner, or his or her deputy, will perform the entire process. When the owners take charge of the process, the value of their time – and labor cost – goes up, likely to at least the \$32 level FTC used to estimate the senior management rate for high-risk entities (if not the \$48 per hour rate found in the NFIB study). Therefore, FTC’s \$16 per hour estimate for these entities is far too small.

Second, we believe the estimate of 23 minutes is far too low, because it assumes that low-risk entities have the expertise and systems in place to comply with section 114. Rather, we assume that it would take at least 5 hours to set up their program, with a subsequent annual implementation burden of one hour; a training time of two hours, and subsequent annual training burden of one hour; and time to prepare an

¹ *NFIB Small Business Poll: Paperwork and Record Keeping* (2003)
<http://www.nfib.com/object/4131277.html>

initial annual report of three hours, with subsequent annual burden of two hours, for an average annual burden of 6 hours ($7+4+7=18$ hours/3 years = 6 hours).

Therefore, we calculate the total labor cost on low-risk entities as \$2,076,196,800 or \$192 per entity per year at the FTC estimate of \$32 per hour.

FTC has Underestimated the Burden on All Entities

We believe it is clear from FTC's estimates that the agency has failed to realize the actual cost for small businesses to comply with these requirements. Small businesses lack the expertise and the systems to easily adapt to the law. Also, since the owners tend to be the ones to develop programs like this and they have multiple priorities, they would be much more likely to develop this program in intermittent sessions – so that they can tend to customers, vendors, employees, and other regulatory obligations – as opposed to one session.

Even when these entities establish their systems the first year, it will still take longer than FTC is assuming to fulfill the obligations in subsequent years. Reasons for this include having to tweak the system to make it as efficient as possible, as well as staff turnover. Staff turnover tends to be particularly high in small businesses – training new employees each year adds significant time costs on these entities.

NFIB and the Legal Foundation estimate that the total average annual burden on all of these entities is \$2.26 billion. This means that FTC could be underestimating by as much as \$2.13 billion. FTC's average estimated cost for all 11.1 million affected entities is \$12.13 per entity. We believe it is in the neighborhood of \$204 per entity in actual cost. We hope that FTC will consider reevaluating the time and labor costs associated with implementing section 114.

Suggestions to Make Implementation Less Burdensome

FTC has requested that comments include suggestions on how to make implementation of section 114 less burdensome. NFIB and the Legal Foundation would hope that FTC could develop a 'short form' or less time-consuming method for low-risk entities to comply with the obligations, if there was a way of doing so that would not expose customers of low-risk entities to a greater chance of having their identities compromised.

Also, though this was not specifically addressed in the JNPRM, we would hope that FTC would allow for sufficient time between adoption of rules implementing section 114 and enforcement of compliance. The vast majority of small-business owners make good-faith efforts to comply with federal and state regulations; however they need time to educate themselves on new requirements so they can comply appropriately.

NFIB and the Legal Foundation appreciate this opportunity to comment on FTC's JNPRM, "Identity Theft Red Flags and Address Discrepancies Under the Fair and Accurate Credit Transactions Act of 2003." If you require any additional information, please contact Daniel Bosch at 202-314-2052.

Sincerely,

Dan Danner
Executive Vice President
Federal Public Policy and Political