December 12, 2007

The Honorable Jennifer Johnson
Secretary
Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue, NW
Washington, DC 20551

Valerie Abend
Deputy Assistant Secretary for Critical Infrastructure Protection and Compliance Policy
Department of Treasury
Office of Critical Infrastructure Protection and Compliance Policy
Room 1327
Main Treasury Building
1500 Pennsylvania Avenue, NW
Washington, DC 20220

Re: Prohibition on Funding of Unlawful Internet Gambling Act of 2006
Federal Reserve: Docket Number R-1298
Treas-DO: Docket Number Treas-DO-2007-0015

Dear Ms. Johnson:

The Office of Advocacy of the U.S. Small Business Administration (Advocacy) submits this comment to the proposed rulemaking on the Prohibition on Funding of Unlawful Internet Gambling. The Office of Advocacy believes that Department of Treasury and the Federal Reserve System (hereinafter "the agencies") have not analyzed properly the full economic impact of the proposal on small entities as required by the Regulatory Flexibility Act (RFA). Advocacy recommends that the agencies prepare a revised initial regulatory flexibility analysis (IRFA) to address the concerns presented below.

Advocacy Background

Congress established the Office of Advocacy under Pub. L. 94-305 to represent the views of small business before Federal agencies and Congress. Advocacy is an independent office within the Small Business Administration (SBA), so the views expressed by Advocacy do not necessarily reflect the views of the SBA or of the Administration.

Section 612 of the RFA requires Advocacy to monitor agency compliance with the Act, as amended by the Small Business Regulatory Enforcement Fairness Act.[1]

On August 13, 2002, President George W. Bush enhanced Advocacy's RFA mandate when he signed Executive Order 13272, which directs Federal agencies to implement policies protecting small entities when writing new rules and regulations. Executive Order 13272 also requires agencies to give every appropriate consideration to any comments provided by Advocacy. Under the Executive Order, the agency must include, in any explanation or discussion accompanying the final rule's publication in the Federal Register, the agency's response to any written comments submitted by Advocacy on the proposed rule, unless the agency certifies that the public interest is not served by doing so.

The Proposed Rule

On October 4, 2007, the agencies published a proposed rule entitled *Prohibition on Funding of Unlawful Internet Gambling* to implement applicable provisions of the Unlawful Internet Gambling Enforcement Act of 2006 (the ''Act''). [2] In accordance with the requirements of the Act, the proposed rule designates certain payment systems that could be used in connection with unlawful Internet gambling transactions restricted by the Act. The proposed rule requires participants in designated payment systems to establish policies and procedures reasonably designed to identify and block or otherwise prevent or prohibit transactions in connection with unlawful Internet gambling. As required by the Act, the proposed rule also exempts certain participants in designated payment systems from the requirements to establish such policies and procedures because the Agencies believe it is not reasonably practical for those participants to identify and block or otherwise prevent or prohibit unlawful Internet gambling transactions restricted by the Act. Finally, the proposed rule describes the types of policies and procedures that nonexempt participants in each type of designated payment system may adopt in order to comply with the Act and includes non-exclusive examples of policies and procedures which would be deemed to be reasonably designed to prevent or prohibit unlawful Internet gambling transactions restricted by the Act. The proposed rule does not specify which gambling activities or transactions are legal or illegal because the Act itself defers to underlying State and Federal gambling laws in that regard and determinations under those laws may depend on the facts of specific activities or transactions (such as the location of the parties).

Requirements of the RFA

The RFA requires agencies to consider the economic impact that a proposed rulemaking will have on small entities. Pursuant to the RFA, the agency is required to prepare an initial regulatory flexibility analysis (IRFA) to assess the economic impact of a proposed action on small entities. Under Section 601(3) of the RFA "small business" has the same meaning as the term "small business concern" under section 3 of the Small Business Act. The IRFA must include: (1) a description of the impact of the proposed rule on small

[1] Pub. L. No. 96-354, 94 Stat. 1164 (1980) (codified at 5 U.S.C. §§ 601-612) amended by Subtitle II of the Contract with America Advancement Act, Pub. L No. 104-121, 110 Stat. 857 (1996). 5 U.S.C. § 612(a).
[2] 72 Federal Register 56680.

entities; (2) the reasons the action is being considered; (3) a succinct statement of the objectives of, and legal basis for the proposal; (4) the estimated number and types of small entities to which the proposed rule will apply; (5) the projected reporting, recordkeeping, and other compliance requirements, including an estimate of the small entities subject to the requirements and the professional skills necessary to comply; (6) all relevant Federal rules which may duplicate, overlap, or conflict with the proposed rule; and (7) all significant alternatives that accomplish the stated objectives of the applicable statutes and minimize any significant economic impact of the proposed rule on small entities.[3] In preparing its IRFA, an agency may provide either a quantifiable or numerical description of the effects of a proposed rule or alternatives to the proposed rule, or more general descriptive statements if quantification is not practicable or reliable.[4] The RFA requires the agency to publish the IRFA or a summary of the IRFA in the Federal Register at the time of the publication of general notice of proposed rulemaking for the rule.[5]

Pursuant to section 605(a), an agency may prepare a certification in lieu of an IRFA if the head of the agency certifies that the proposed rule will not have a significant economic impact on a substantial number of small entities. A certification must be supported by a factual basis.

The Agencies' Compliance with the RFA

The agencies prepared an IRFA for the proposed rule and solicited comments from the public regarding the information in the IRFA. Advocacy, however, is concerned that the IRFA may not comply with the RFA.

The Agencies Fail to Provide Sufficient Information About the Economic Impact of the Proposed Rule

The purpose of an IRFA is to describe the impact of the proposal on small entities. Although the IRFA submitted by the agencies identifies types of small businesses that are affected by the proposal, it fails to provide information about the nature of the impact as required by the RFA. Instead, the agencies state that they do not have sufficient information and request that the information be provided by the public.

Advocacy appreciates the fact that the agencies may need to obtain information and commends the agencies for soliciting additional information from the public. However, Advocacy is concerned that the agencies are not providing all available information in the proposal. In the Supporting Statement for Recordkeeping Requirements associated with Regulation GG submitted to the Office of Management and Budget, the Federal Reserve stated that the total cost to the public is $19, 899,325. This estimate was based on an assumption that 30 percent of the work would be provided by clerical staff at $25 per hour; 45 percent would be performed by managerial or technical staff at $55 per hour, 15 percent would be performed by senior management at $100 an hour, and 10 per cent would be

[3] 5 USC § 603.
[4] 5 USC § 607.
[5] 5 USC § 603.

performed by legal counsel at $144.[6] This information was found under the reporting forms section on the Federal Reserve's website but it is not in the preamble of the proposed rule. If the agencies provided this information to the public in the IRFA, the public would be able to provide the agencies with meaningful comments about whether the assumptions about the costs are correct for small entities.

Moreover, Advocacy questions whether the projected paperwork costs are the only costs involved. In the statement, the Federal Reserve states that the estimate does not include large money-transmitting businesses because they already have systems in place. It states that smaller firms acting as agents in these large systems may be able to rely on the large system's policies and not need to establish their own policies and procedures. Will smaller firms incur legal fees in determining whether the proposed rule applies to them? If the rules do apply, will those firms incur costs to develop policies and to train their employees on the policies? These are a few of the questions that the agencies may want to consider in determining the economic impact of this regulation on small entities.

Alternatives

In addition, as noted above, the RFA requires agencies to consider less burdensome alternatives that still meet the statutory objectives. Instead of considering alternatives and providing a discussion about the economic impact of the potential alternatives, the agencies state that:

> "Other than noted above, the agencies are unaware of any significant alternatives to the proposed rule that accomplish the stated objectives of the Act and that minimize any significant economic impact of the proposed rule on small entities. The Agencies request comment on additional ways to reduce regulatory burden associated with this proposed rule."

It is unfortunate that the agencies do not put forward a meaningful discussion of alternatives in their proposal. Simply soliciting information about alternatives from small entities does not relieve the agencies of their obligation to consider less burdensome alternatives as part of the IRFA (in the proposed rule).

One alternative that the agencies may want to consider is exempting small money transmitters from the proposed rulemaking. The National Money Transmitters Association (NMTA) has informed Advocacy that the existing customer agreements and contracts with counterparties already include clauses prohibiting network use for unlawful transactions. As such, transmitting funds for an unlawful gambling activity would breach the contract. Moreover, a money transmitting business is similar to a wire transfer system in that both types of businesses operate as send agents, not financial institutions. Since a wire transfer system is exempt, the money transmitting businesses should also be exempt.

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[6] The Supporting Statement for Recordkeeping Requirements associated with regulation GG can be found at http://www.federalreserve.gov/reportforms/review.cfm. The information regarding the paperwork burden is on pages 5-6 of that statement.

Identification of Duplicative, Overlapping, or Conflicting Federal Rules

As noted above, the RFA also requires an agency to identify duplicative, overlapping, or conflicting federal rules. In this proposal, the agencies sought comment on whether there are statutes or regulations that would duplicate, overlap, or conflict with the proposed law. The RFA places the duty to identify existing regulations on agencies, not small entities. Shifting that obligation to small entities usurps the purpose of the RFA.

Conclusion

The RFA requires agencies to consider the economic impact on small entities prior to proposing a rule, to provide the information on those impacts to the public for comment, and to consider less burdensome alternatives. Advocacy encourages the agencies to prepare and publish for public comment a revised IRFA to determine the full economic impact on small entities; identify duplicative, overlapping or conflicting regulations; and consider significant alternatives to meet its objective while minimizing the impact on small entities before going forward with the final rule.

Thank you for the opportunity to comment on this important proposal and for your consideration of Advocacy's comments. Advocacy is available to assist the agencies in their RFA compliance. If you have any questions regarding these comments or if Advocacy can be of any assistance, please do not hesitate to contact Jennifer Smith at (202) 205-6943.

Sincerely,

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Jennifer A. Smith
Assistant Chief Counsel for
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cc: The Honorable Susan E. Dudley, Administrator
Office of Information and Regulatory Affairs, OMB