

Supporting Statement
Rule on Informal Dispute Settlement Procedures
16 C.F.R. 703
(OMB Control Number 3084-0113)

1. Necessity for Collecting the Information

Section 110(a)(2) of the Magnuson-Moss Warranty Act (15 U.S.C. Section 2301, *et seq.*) directed the Commission to prescribe rules setting forth the minimum requirements for any informal dispute settlement procedure that the warrantor requires the consumer to use before pursuing any legal action in court. On December 31, 1975, the Commission issued its Rule on Informal Dispute Settlement Procedures, 16 C.F.R. 703 (“the Rule” or “Rule 703”), which sets minimum standards for informal dispute settlement mechanisms (“IDSM”) established to resolve consumer warranty disputes. The purpose of the Rule is to carry out Congress’s intent to encourage the fair and expeditious handling of consumer disputes through the use of alternative dispute resolution methods.

Rule 703 applies only to those warrantors who (1) provide a written warranty, (2) on a consumer product, and (3) place a “prior resort” requirement in their warranty (i.e., require consumers to use a dispute resolution mechanism before exercising their legal remedies in court). Neither the Act nor Rule 703 requires warrantors to set up IDSMs. Furthermore, a warrantor is free to set up an IDSM that does not comply with Rule 703 as long as the warranty does not contain a “prior resort requirement.”

Rule 703 contains procedural standards that must be followed by every IDSM that is incorporated, through a prior resort clause, into the terms of a written consumer product warranty. These standards include requirements concerning the mechanism’s structure, the qualifications of staff or decision makers, the mechanism’s procedures for resolving disputes, recordkeeping, and annual audits.

The recordkeeping provision of the Rule, Section 703.6, requires IDSMs to maintain three types of information:

- (a) Individual records for each dispute submitted to the IDSM [§ 703.6(a)];
- (b) Indexes that categorize disputes by product model and show the extent to which the warrantor has abided by decisions of the mechanism [§ 703.6(b) - (d)]; and
- (c) Statistical summaries that group disputes according to various status and final disposition categories [§ 703.6(e)].

Section 703.6(f) requires the records specified in Section 703.6(a) through (e) to be retained for four years after final disposition of a dispute. Section 703.7 of the Rule requires IDSMs operating under Rule 703 to conduct an annual audit of their procedures and submit the audit to the FTC.

2. Use of the Information

Information that IDSMs are required to maintain under Section 703.6(f) is available for review by consumers and by the FTC to determine compliance. In addition, the annual audit required under Section 703.7 must be submitted to the Federal Trade Commission, where it is placed on the public record for review by any interested party. Finally, states have incorporated the Rule by reference in many of their “lemon law” statutes and may use the records and audits required by Rule 703 in their own review and enforcement actions.

3. Consideration of the Use of Improved Information Technology to Reduce Burden

Rule 703 requires that warrantors disclose any IDSM subject to the Rule, sets out guidelines for operating the mechanism, and specifies recordkeeping and reporting functions. The recordkeeping functions are the primary area where entities subject to the Rule could employ new or improved information technology to reduce burdens under the Rule. In this regard, the Rule does not specify how the information required to be maintained and reported is to be kept. Thus, those IDSMs subject to the Rule are free to use whatever information systems they wish to use. In addition, there is nothing in Rule 703 that would preclude mechanisms from allowing interested parties the option of viewing audits and other public information online. Indeed, the FTC and some IDSMs make the annual audits available on their websites. Accordingly, consistent with the Government Paperwork Elimination Act, Pub. L. No. 105-277, Title XVII, 112 Stat. 2681-749, nothing in the Rule prescribes that disclosures be made, records filed or kept, or signatures executed, on paper or in any particular format that would preclude the use of electronic methods to comply with the Rule’s requirements.

4. Efforts to Identify Duplication/Availability of Similar Information

There is no other statute or regulation of nationwide applicability that governs the operation of dispute resolution mechanisms for consumer product warranty disputes. Some states have incorporated Rule 703 by reference in their state lemon laws; others have set up arbitration systems under their lemon laws. Where states have set up their own systems, they have used Rule 703 as a guide. Accordingly, staff believes there is little, if any, duplication. There are no other sources of information concerning the operation of the Rule 703 IDSMs.

5. Efforts to Minimize the Burden on Small Businesses

Although warrantors of any size may utilize informal dispute settlement procedures, the IDSMs that currently operate under the Rule are maintained by very large organizations. However, the Rule is flexible in terms of the type of procedures that can be offered. The Act does not require warrantors to set up IDSMs. Furthermore, a warrantor is free to set up an IDSM that does not comply with Rule 703 as long as the warranty does not contain a “prior resort requirement.” Thus, a small warrantor is free to set up an IDSM that does not comply with Rule 703 if there is no prior resort requirement in the warranty; alternatively, a small warrantor can choose to contract with organizations such as the Better Business Bureau to handle any consumer warranty disputes that might arise.

6. Consequences of Conducting the Collection Less Frequently

If the individual case files required by Section 703.6(a) of the Rule were compiled less frequently, the IDSM would not be able to comply with Section 703.8(e) of the Rule, which requires it to provide (upon request) to either party to a dispute access to all records relating to the dispute and copies of any records relating to the dispute at a reasonable cost. It is essential that these files be maintained by the mechanism and that they be made available to the parties because they would provide the basis for any subsequent arbitration, legal or other proceedings following action by the IDSM.

The indexes required by Section 703.6(b) are intended to enable the mechanism to analyze patterns of complaints and report indications of consistent problems to the warrantor. Less frequent compilation of the information in the index would not affect the Commission's or the public's ability to monitor the IDSM's compliance, but it would prevent the mechanism from imparting useful information to the warrantor.

Less frequent compilation of the indexes required under Sections 703.6(c) and (d) would hamper the Commission's ability to monitor compliance with the Rule. These indexes provide key indicators of a warrantor's good faith participation in an IDSM and the mechanism's ability to resolve disputes expeditiously.

The statistical reporting requirements set forth in Section 703.6(e) provide the basis for review by interested members of the public. On the basis of the statistically reported performance of an IDSM, an interested person could determine whether to file a complaint with the FTC pursuant to Section 110(a)(4) of the Magnuson-Moss Warranty Act, and thereby initiate an FTC review of the bona fide operation of the IDSM. The statistics required under Section 703.6(e) must be compiled semiannually. If the statistics were compiled less frequently, the ability of the public to evaluate the performance of the IDSM would be hindered.

The audit report is intended to be a comprehensive evaluation of the IDSM's performance and its compliance with the Rule. If the audit report were required less frequently, public review of the mechanism as well as the Commission's evaluation of the mechanism would most likely be based on outdated information.

7. Special Circumstances Requiring Collection Inconsistent With Guidelines

The collection of information required by the Rule is consistent with all applicable guidelines contained in 5 C.F.R. § 1320.5(d)(2).

8. Public Comments/Consultation Outside the Agency

(a) Public comments

As a prelude to this request, the Commission sought public comment. See 72 Fed. Reg. 44,140 (Aug. 7, 2007). No comments were received. Pursuant to the OMB regulations that implement the PRA (5 C.F.R. Part 1320), the Commission provided a second opportunity for public comment. See 72 Fed. Reg. 61,648 (Oct. 31, 2007). No comments were received.

(b) Consultation Outside the Agency

In connection with this request, staff consulted recently with representatives of IDSMs currently operating under the Rule to determine whether previous estimates were still accurate or whether they needed updating.

The Commission has also consulted with industry members as part of its periodic evaluation of Rule 703. In 1997, the Commission published a request for public comment on whether to modify, rescind or retain Rule 703 (62 Fed. Reg. 15,636). In that request, the Commission requested comments about the overall costs and benefits of the Rule and its overall regulatory and economic impact as part of its systematic review of all current Commission regulations and guides. Thirteen comments were received. The comments generally reflected strong support for the view that the Rule is achieving the objective it was fashioned to achieve – i.e., to facilitate the fair and expeditious handling of consumer product warranty disputes through informal dispute settlement. Several commenters suggested modifications to the Rule that would enhance consumer protections and/or minimize the burden on the IDSM. Only one commenter submitted cost data regarding the impact of the Rule. The BBB estimated that the Rule’s recordkeeping and related annual audit reporting requirements cost the BBB AUTO LINE about \$100,000 annually. On April 22, 1999, the Commission announced that it would retain Rule 703 unchanged (64 Fed. Reg. 19,700).

9. Payments or Gifts to Respondents

Not applicable. There have been no payments or gifts to respondents in connection with Rule 703.

10. & 11. Assurances of Confidentiality/Matters of a Sensitive Nature

Section 703.8(b) of the Rule provides that all records of a mechanism may be kept confidential, except the statistical summaries specified in Section 703.6(e). Therefore, the Rule presents no issues concerning confidentiality or questions of a sensitive nature. The Rule does not require any confidential or sensitive information to be filed with the FTC as part of the audit report mandated by the Rule.

From time to time, the Commission may require a warrantor or IDSM to submit information as part of a law enforcement investigation to determine whether it has engaged in any practices that might have violated Rule 703. Any information provided to the Commission in connection with

such law enforcement investigations is treated as confidential under Sections 6(f) and 21(f) of the Federal Trade Commission Act, 15 U.S.C. § 46(f) and 61(f).

12. Hours and Labor Cost Burden

Total annual hours burden. The primary burden from the Rule comes from the Rule's recordkeeping requirements that apply to those IDSMs incorporated into a consumer product warranty. The burden of the Rule's disclosure requirements is limited. Although the Rule's paperwork requirements have not changed since its last submission to OMB in 2004, FTC staff has found that fewer consumers are filing claims covered by the Rule. As a result, staff now estimates the burden of Rule 703's recordkeeping and reporting requirements has decreased to approximately 16,321 hours annually while the disclosure burdens have decreased to 408 hours. Thus, staff estimates that the total burden imposed by the Rule is approximately 17,000 hours (rounded to the nearest thousand).

Recordkeeping Provisions. The Rule requires IDSMs to maintain individual case files. Because maintaining individual case records is a necessary function for any IDSM, much of the burden would be incurred in the ordinary course of the IDSM's business. Nonetheless, staff has retained its previous estimate that maintaining individual case files imposes an additional burden of 30 minutes per case. The amount of work required will depend on the number of dispute resolution proceedings undertaken by each IDSM. After a review of the annual audits filed by the IDSMs from 2002 through 2005, staff estimates that the average number of disputes handled annually by the IDSMs covered by the Rule is approximately 24,482. Accordingly, staff estimates the total annual recordkeeping burden attributable to the Rule to be approximately 12,241 hours (24,482 disputes x 30 minutes of burden ÷ 60 minutes).

Reporting Provisions. The Rule requires IDSMs to update indexes, complete semi-annual statistical summaries, and submit an annual audit report to the FTC. Staff retains its previous estimate that covered entities spend approximately 10 minutes per case for these activities, resulting in a total annual burden of approximately 4,080 hours (24,482 disputes x 10 minutes of burden ÷ 60 minutes).

Disclosure Requirements. The Rule requires that information about the IDSM be disclosed in the written warranty. Any incremental costs to the warrantor of including this additional information in the warranty are negligible. The majority of disclosure burden would be borne by the IDSM, which is required to provide to interested consumers upon request copies of the various types of information the IDSM possesses, including annual audits. Consumers who have dealt with the IDSM also have a right to copies of their records. (IDSMs are permitted to charge for providing both types of information.)

Based on discussions with representatives of the IDSMs, staff estimates that the burden imposed by the disclosure requirements is approximately 408 hours per year for the existing IDSMs to provide copies of this information. This estimate draws from the average number of consumers who file claims each year with the IDSMs (24,482) and the assumption that twenty percent of consumers individually request copies of the records pertaining to their disputes, or approximately

4,896 consumers. Staff estimates that copying such records would require approximately 5 minutes per consumer, including a negligible number of requests for copies of the annual audit.¹ Thus, the IDSMS currently operating under the Rule have an estimated total disclosure burden of 408 hours (4,896 consumers x 5 minutes of burden ÷ 60 minutes).

Accordingly, the total PRA-related annual hours burden attributed to the Rule is approximately 16,729 hours (12,241 hours for recordkeeping + 4,080 hours for reporting + 408 hours for disclosures).

Total Annual Labor Cost Burden. Staff assumes that IDSMS use skilled clerical or technical support staff to comply with the recordkeeping requirements contained in the Rule at an hourly rate of \$16. Thus, the labor cost associated with the 12,241 annual burden hours for recordkeeping is approximately \$195,856 (12,241 burden hours x \$16 per hour). In addition, staff assumes that IDSMS also use skilled clerical support staff at an hourly rate of \$16 to comply with the reporting requirements. Thus, the labor cost associated with the 4,080 annual burden hours for reporting is approximately \$65,280 (4,080 burden hours x \$16 per hour). Finally, staff assumes that IDSMS use clerical support at an hourly rate of \$12 to reproduce records and, therefore, the labor cost associated with the 408 annual burden hours for disclosures is approximately \$4,896 (408 burden hours x \$12 per hour).

Accordingly, the combined total annual labor cost for PRA-related burden under the Rule is approximately \$266,032 hours (\$195,856 for recordkeeping + \$65,280 for reporting + \$4,896 for disclosures).

13. Estimated Capital/Other Non-Labor Costs Burden

(a) Total capital and start-up costs. The Rule imposes no appreciable current capital or start-up costs. The vast majority of warrantors have already developed systems to retain the records and provide the disclosures required by the Rule. Rule compliance does not require the use of any capital goods, other than ordinary office equipment, to which providers would already have access. In addition, according to a representative of one IDSMS, it has already developed systems to collect and retain information needed to produce the indexes and statistical summaries required by the Rule, and thus, estimated very low capital or start-up costs.

The only additional cost imposed on IDSMS operating under the Rule that would not be incurred for other IDSMS is the annual audit requirement. According to representatives of each of the IDSMS currently operating under the Rule, the vast majority of costs associated with this requirement are the fees paid to the auditors and their staffs to perform the annual audit.

¹ This estimate includes the additional amount of time required to copy the annual audit upon a consumer's request. However, because staff has determined that a very small minority of consumers request a copy of the annual audit, this estimate is likely an overstatement. In addition, at least a portion of case files are provided to consumers electronically, which further would reduce the paperwork burden borne by the IDSMS.

Representatives of the IDSMs estimated a combined cost of \$300,000 for both IDSMs currently operating under the Rule

(b) Total operation/maintenance/purchase of services costs. \$29,000 in copying costs. This total is based on estimated copying costs of 7 cents per page and several conservative assumptions. Staff estimates that the average dispute-related file is 35 pages long and that a typical annual audit file is approximately 200 pages in length. As discussed above, staff assumes that twenty percent of consumers using an IDSM currently operating under the Rule (approximately 4,896 consumers) request copies of the records relating to their disputes.

Staff also estimates that a very small minority of consumers request a copy of the annual audit. This assumption is based on (1) the number of consumer requests actually received by the IDSMs in the past; and (2) the fact that the IDSMs' annual audits are available online. For example, annual audits are available on the FTC's web site, where consumers may view and or print pages as needed, at no cost to the IDSM. In addition, the Better Business Bureau makes available on its web site the annual audit of the BBB AUTO LINE. Therefore, staff conservatively estimates that only five percent of consumers using an IDSM covered by the Rule (approximately 1,224 consumers) will request a copy of the IDSM's audit report.

Thus, the total annual copying cost for dispute-related files is approximately \$11,995 (35 pages per file x \$.07 per page x 4,896 consumer requests) and the total annual copying cost for annual audit reports is approximately \$17,136 (200 pages per audit report x \$.07 per page x 1,224 consumer requests). Accordingly, the total cost attributed to copying under the Rule is approximately \$29,131.

Thus, the total non-labor cost under the Rule is approximately \$329,131 (\$300,000 for auditor fees + \$29,131 for copying costs).

14. Estimated Cost to the Federal Government

Staff estimates that the yearly cost to the Federal Government resulting from administration of the Rule's warranty disclosure requirements is \$9,375, which is the cost of one-tenth of a professional work year.

15. Program Changes or Adjustments

There are no program changes. The estimated total annual hours burden has decreased to 17,000 hours from the 30,000 hours estimated in 2004. This decrease of 13,000 hours is due to the availability of more recent data that fewer disputes are handled by the IDSMs. Because the annual burden hours has decreased, the associated labor costs have also decreased, from \$438,000 in 2004 to \$266,000.

The estimate of the total capital and non-labor costs have increased from \$300,000 in 2004 to \$329,000. This new estimate is based on \$300,000 in capital and start-up costs and \$29,000 in copying costs. The estimated figure of \$300,000 in capital and start-up costs represents an increase

from staff's previous estimate of \$172,500 in 2004. This increase reflects more accurate figures that staff obtained from representatives of the IDSMs regarding costs associated with the annual audit requirement. The estimate of \$29,000 in copying costs represents a decrease from the \$127,500 estimate submitted in 2004. This decrease is due to a number of factors, including the decrease in the number of disputes handled by the IDSMs, the decrease in the number of consumers who request copies of their case files, and the even smaller number of consumers that request copies of the annual audit.

16. Plans for Tabulation and Publication

There are no plans to publish any information.