

IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF COLORADO

Civil Action No. 10-CV-01546-REB-CBS

The Direct Marketing Association,

Plaintiff,

v.

Roxy Huber, in her capacity as Executive
Director, Colorado Department of Revenue,

Defendant.

EXPERT REPORT OF F. CURTIS BARRY

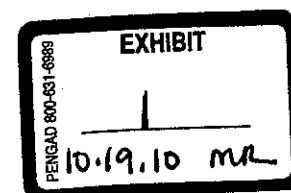
I am **F. Curtis Barry**, the Founder and President of F. Curtis Barry & Company, with offices in Richmond, Virginia. I have been retained by the law firm of Brann & Isaacson, counsel to the Direct Marketing Association ("DMA"), to offer my expert opinions regarding the costs of compliance with certain requirements of a new Colorado statute (House Bill 10-1193) and regulation that will be incurred by retailers located outside of Colorado who are subject to the law.

My compensation is on a per consulting day used at \$1,850 (or \$231.25 on an hourly basis). We are paid regardless of the outcome.

I. STATEMENT OF OPINIONS

After reviewing and considering the data and information described in Section II,

I offer the following opinions:



- Each of the three broad requirements of the law (Transactional Notice, Annual Purchase Summary, and Annual Disclosure Report) will require retailers affected by the statute and regulation to incur costs of compliance. In many cases, those costs will be significant, particularly given the relative size of the Colorado market as a percentage of the national market.
 - The Transactional Notice has estimated first year costs of \$10,000 to \$28,000 and ongoing annual compliance costs of \$1,500 to \$2,000 (Exhibit A.1);
 - The Annual Purchase Summary has estimated first year costs of \$8,000 to \$20,000; in addition this requirement has variable costs of \$2.00 to \$3.00 per customer mailed (Exhibit B.1);
 - The Customer Disclosure Report has estimated annual costs \$8,500 to \$13,000 (Exhibit C.1).
- The Colorado statute and regulation thus dictate changes in systems and practices for out-of-state retailers to implement that will result in substantial expense. The required level of initial investment is particularly high, especially if one considers the relatively small number of purchasers spending over \$500 annually who must receive Annual Purchase Summaries.
- The Colorado statute and the regulation will require that a considerable effort be spent on Information Technology (IT) systems. IT costs will vary between retailers and software vendors depending on the age of the order processing and website technologies; the flexibility of the development technology; and the internal IT cost structure.
- In my view, there are various categories of costs for each statutory/regulatory requirement:
 - Costs incurred to satisfy basic statutory/regulatory requirements

- Costs that are necessary but not discretionary
- Costs that are discretionary but good business practice
- Colorado in-state retailers will have a competitive advantage over out-of-state retailers as a result of the substantial costs of compliance with the new law.
- We anticipate that this regulation will cause out-of-state retailers to lose customers and sales.
- There are a number of potential expenses that simply cannot be estimated at this time, that affected out-of-state retailers may well incur (Exhibit D).

II. DATA AND INFORMATION CONSIDERED IN FORMING OPINIONS

The data or other information I considered in forming my opinions includes:

A. Documents Detailing Legal Requirements of the Statute and Regulation

1. House Bill 10-1193
2. Colorado Regulation 39-21-112.3.5
3. DMA Amended First Complaint

B. Data/Information Supporting Cost Estimates

Over the course of 25 years, F. Curtis Barry & Co. has worked with hundreds of customers, software companies and marketing service bureaus. Our experience provides a wealth of expertise in estimating the costs associated with the redesign of the systems and processes of direct marketers. We cite in this section the data and assumptions that we have used to develop these estimates.

1. Systems Development Costs

The cost to develop computer systems, whether designed and programmed internally or done using commercial software vendors, is typically substantial. We feel it is important to consider such systems costs in several contexts:

- Professional programming rates
- Systems development process and tasks involved to make the required/desired change
- Complexity of evaluating, programming and implementing Colorado's statutory/regulatory requirements

a. Professional Programming Rates

i. Commercial Systems Development Rates

We assist our clients with Requests For Proposals for commercial systems from software vendors, third-party fulfillment providers and marketing service bureaus on a continual basis. We look at dozens of vendor responses each year for proposed work.

From external vendors, commercial programming rates for evaluating, programming and implementing programs in today's marketplace vary from \$140 per hour (\$1,120 per day) for less-skilled trainers and programmers to \$225 per hour (or \$1,800 per day) for project managers.

ii. Internal IT Systems Development Costs

Internal IT programming rates can vary widely depending on the skill level, company and regional marketplace. Much like the commercial rates cited above for varying skill sets/levels and positions, the labor costs (salaries) can vary from \$50,000

per year (\$24.00 per hour) to \$100,000 (\$48.00 per hour) for experienced programmers. Project managers can earn more than \$100,000 per year.

In addition, company benefit rates often add 20% to 30% to the cost of employing professionals. A 25% benefit rate added to these hourly costs brings the labor rate to \$31 and \$62 per hour when work is performed internally. (The costs of performing changes using internal resources are not simply "absorbed" within existing company cost structures. Well-run companies carefully budget internal IT projects. Taking on a project necessitated by new regulatory requirements has real cost – other projects must either be deferred or abandoned, or IT staff increased/compensated through overtime to handle the additional work.)

b. The Systems Development Process

In reviewing the costs of implementing the changes necessitated by the Colorado regulation, it is important to take into account the types of work required to develop and implement the changes. System development is a multi-phased process which is governed by industry best practices and company IT standards to ensure the best solution for the company.

i. Cost to Evaluate Requested Systems Changes

IT industry best practice – for both internal IT departments and commercial systems providers – is to conduct an evaluation of proposed changes and secure mutual approval of the provider and management alike. In most cases, the customer or requesting department has to pay for (or cover through its budget) a detailed evaluation

of the programming requested, which can be \$1,000 to \$5,000 on the low end, to much higher costs for complex changes and new subsystems.

These evaluation tasks include: how the proposed changes will impact the system or services; how many hours are required and for what skill levels; the availability of programming resources; IT's opinion of the change; a schedule that can be met; and a requested sign off between the parties. In addition, the customer or vendor may choose not to proceed with the evaluated change.

ii. Program Development Costs

There are costs associated with developing user requirements; designing program changes; developing program specifications; programming the changes; and testing at the program, subsystem and total system level. At various control points in the process, management signs off on the work.

iii. Implementation Costs

The cited costs include all the costs to implement the system within the company departments. These include the IT department training the company trainer on the new system; program documentation for the change, and operational production tasks.

iv. Complexity of Evaluating, Programming and Implementing Colorado's Regulation

F. Curtis Barry & Co. reviews and negotiates software contracts and modifications for clients with vendors on a regular basis. We have used our knowledge and experience to make a judgment about the complexity of changes necessitated by the Colorado statute and regulation, and to provide an estimate of some of these order management systems and e-commerce costs.

How difficult the changes will be for companies to make will vary based on how flexible the company's system application and technology is. Users of commercial systems of newer design will have an easier time of implementing the regulation, but all companies will incur meaningful systems costs.

We believe we have provided a conservative range of cost estimates.

2. Cost For Marketing Service Bureaus

For the costs we have cited, we have knowledge of a number of marketing service bureaus' pricing models for building, updating and analyzing customer purchases.

For this opinion we have also used knowledge of the mailing service costs to print, insert, and send First-Class mail pieces.

III. EXHIBITS

The Exhibits are used to summarize or support my opinions are:

Exhibit A.	The Transactional Notice – Requirements and Costs
Exhibit A.1.	The Transactional Notice – Total Costs
Exhibit B.	The Annual Purchase Summary – Requirements and Costs
Exhibit B.1.	The Annual Purchase Summary – Total Costs
Exhibit C.	The Customer Information Report – Requirements and Costs Exhibit
Exhibit C.1.	The Customer Information Report – Total Costs
Exhibit D.	Other Potential Costs Not Estimated

In Exhibits A – C, we have organized costs into three categories:

- o Costs incurred to satisfy basic statutory/regulatory requirements
- o Costs that are necessary but not discretionary
- o Costs that are discretionary but good business practice

IV. QUALIFICATIONS AND PUBLICATIONS

Attached hereto is a copy of my current *curriculum vitae*. In the last ten years, I have published hundreds of articles and other works, but I do not maintain a listing of all of my publications going back ten years. My CV includes a list of publications I have authored in the previous four years.

V. RECENT TESTIMONY

I have testified as an expert at trial or at deposition during the past four years in the following matter:

Deposition in 2007 in: *Casual Male Retail Group, Inc. and Casual Male RBT, LLC vs. Robert H. Yarbrough, RKC Mail LLC, d/b/a Mile Post Four and Westport Big & Tall, LLC*, United States District Court, District Court of Massachusetts, Civil Action No. 1:05-cv-12049-NMG.

VI. STATEMENT OF COMPENSATION

My compensation, as noted above, is \$1,850 per day.

s/ F. Curtis Barry
F. Curtis Barry

CURRICULUM VITAE

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Curt Barry is founder and president of F. Curtis Barry & Company, a national fulfillment and operations consultancy, with a specialty in systems for the multichannel industries (retail, e-commerce and catalog). These systems include website and e-commerce, call center and order management, warehousing, marketing, merchandising, inventory control, finance, point of sale (POS) and retail merchandising systems, etc.

Mr. Barry has extensive experience with clients that are developing direct and retail systems internally as well as with clients that are selecting and implementing commercial systems.

In his work with clients to select and implement commercial systems, his experience includes but is not limited to:

- Developing user requirements for the new system at a management, department and system functional level;
- Project management and participation in the vendor selection process including development of Requests For Proposal (RFP), evaluating vendors against the RFP, leading user demonstrations by vendor software, vendor due diligence (e.g. reference checks, site visits) and helping to make final vendor selection.
- Working with the vendor and the client to guide the system modification process including macro level and program specifications, cost estimation and understanding the severity of modifications to the base system;
- "Best of breed" systems integration to other systems including high level and detail data flows;
- Negotiating vendor software services contracts including defining client and vendor scope and deliverables, required system modifications, payment schedules, license and service agreements, project schedules, training and implementation plans, client/vendor responsibilities, etc.;
- Planning system testing prior to implementation including program testing, full systems and acceptance by the client;

- File conversion planning and execution for the new system;
- Project planning and management of client and vendor tasks for successful implementation;
- Gaining client and vendor project sign-offs at critical points in the project;
- Status reporting daily and weekly involving detail task plans, estimates and task completion management for clients and software vendors;
- Working with clients on best practices for selecting systems;
- Applying industry best practices in functional areas with the new application software system.

Mr. Barry's internal design, programming and implementation experience includes:

- F. Curtis Barry & Company development of proprietary systems for measuring product profitability and inventory forecasting systems.
- Currently, through a partnership with Taurus Software, F. Curtis Barry & Company co-develops an executive dashboard and analytics system, Manage Metrix (managemetrix.com).
- Mr. Barry was a principal in Molster, Barry & Mason, Inc. 1983 to 1985. The firm designed and programmed catalog order management systems for catalog companies Tiffany & Company, Henri Bendel and DH Holmes.
- Manager of Research and Development for the Corporate Data Center of Garfinckel, Brooks Brother, Miller & Rhoads from 1973 to 1983. The department Mr. Barry managed designed and programmed all of the information systems for the retail and catalog chain of 250 stores with sales of \$500 million.

Mr. Barry has extensive experience with point of sale (POS) and store level merchandising systems. From 1970 to 1973, Mr. Barry was employed by NCR Corporation in selling and installing point of sale and retail systems in dozens of major retail department and specialty store chains.

In the F. Curtis Barry & Company, they have completed assignments for selecting and implementing POS systems for multichannel clients.

Bachelor of Science degree, Cornell University, 1970.

Published Articles By Curt Barry 2006 to 2010

Since 1983, Mr. Barry has authored hundreds of articles in catalog and e-commerce trade publications. Other articles appear on the firm's blog and website. Mr. Barry authored the book Best Practices in Multichannel Operations & Fulfillment, ISBN 13:978-1-4196-9298-7. Published in 2008. Additional articles and blog opinions are available on www.fcaco.com.

Multichannel Merchant Magazine and Operations & Fulfillment Magazine

These are Penton Magazines and the articles are available from the magazines' website archives.

How Barcode Use Can Help Reduce Warehouse Costs

Sep 13, 2010, Multichannel Merchant, By Curt Barry

How to Reduce Warehouse Costs

Sep 01, 2010, Multichannel Merchant, By Curt Barry

Proper Slotting Can Reduce Warehouse Costs

Aug 30, 2010, Multichannel Merchant, By Curt Barry

How to Reduce Labor Management Costs

Aug 17, 2010, Multichannel Merchant, By Curt Barry

12 Mistakes to Avoid in Systems Selection

Jul 01, 2010, Multichannel Merchant, By Curt Barry

Evaluating Web Platform Systems

May 01, 2010, Multichannel Merchant, By Curt Barry

Tips for Finding Third-Party Fulfillment

Mar 29, 2010, Multichannel Merchant, By Curt Barry

Managing Your Fulfillment Folks

Mar 01, 2010, Multichannel Merchant, By Curt Barry

The State of Free Shipping Offers

Feb 01, 2010, Multichannel Merchant, By Curt Barry

Web Expenditures: Sharpening your e-commerce Spend

Dec 01, 2009, Multichannel Merchant, By Curt Barry

Why Some Merchants are Saying Yes to SaaS

Nov 23, 2009, Multichannel Merchant, By Curt Barry

Sharpening Your E-Commerce Spend

Nov 19, 2009, Multichannel Merchant

Is Outsourcing an Option for You?

Oct 01, 2009, Multichannel Merchant, By Curt Barry

10 Steps to Better Manage Your Stock | Take a Financial View of Inventory
Sep 01, 2009, Multichannel Merchant, By Curt Barry

Sorting Out Warehouse Automation
Jul 07, 2009, Multichannel Merchant, By Curt Barry

Tips to help with technology options with budget costs | Time to Automate your DC?
Jul 01, 2009, Multichannel Merchant, By Curt Barry

Bean Backorder Customer Service Says The Magic Words
Jun 10, 2009, Multichannel Merchant, By Curt Barry

On Which Version of Data Should We Base Our Decisions? | Business Information Systems Across the Enterprise
May 01, 2009, Multichannel Merchant, By Curt Barry

Surveying the Software Landscape | E-commerce Platform Providers are Expanding Offerings into Order Management
Apr 01, 2009, Multichannel Merchant, By Curt Barry

Is Now a Good Time to Invest in Systems? | Excellent Time to Invest in the e-commerce, Order Management and Warehouse Management Software that Your Business Needs
Apr 01, 2009, Multichannel Merchant, Curt Barry

Paying for Free Shipping and Handling | High Shipping and Processing has been Driven Upwards by Record Freight Increase and Accessorial Charges
Feb 01, 2009, Multichannel Merchant, By Curt Barry

A Database Marketer's Perspective on Free Shipping
Jan 06, 2009, Multichannel Merchant, By Curt Barry

Virtualization and Going Green in IT
Dec 23, 2008, Multichannel Merchant, By Curt Barry

OF Conducting a Post Season Audit, Part I
Dec 18, 2008, Operations & Fulfillment, by Curt Barry

Sales Without Inventory
Dec 03, 2008, Multichannel Merchant, By Curt Barry

Prioritizing Your Tech Spend | Where to Put Your Technology Dollars During Downtown
Dec 01, 2008, Multichannel Merchant, By Curt Barry

IT Spending Priorities
Nov 25, 2008, Multichannel Merchant, By Curt Barry

Keeping Contact Center Costs in Line | Balancing Expenses with Service Levels
Oct 01, 2008, Multichannel Merchant, By Curt Barry

Home Agent Trend Key to Reducing Attrition
Oct 01, 2008, Multichannel Merchant, By Curt Barry

Tough Times or Opportunities Knocking?
Sep 30, 2008, Multichannel Merchant, By Curt Barry

More Green Thoughts
Sep 10, 2008, Multichannel Merchant, By Curt Barry

Let Them Know You're Green
Sep 03, 2008, Multichannel Merchant, By Curt Barry

Eying IT Expenditures | Where Merchants Should Put Information Technology Dollars |

SaaS
Aug 01, 2008, Multichannel Merchant, By Curt Barry

IT Investment Intelligence
Jul 30, 2008, Multichannel Merchant, By Curt Barry

Get a Grip on Your D.C.
May 2008, ROI (Formerly Catalog Success Magazine), By Curt Barry

Keeping DC Costs at Bay
Apr 01, 2008, Multichannel Merchant, By Curt Barry

Post-Holiday Liquidation Strategies
Feb 01, 2008, Multichannel Merchant, By Curt Barry

Clear It Out
Feb 01, 2008, Multichannel Merchant, By Curt Barry

Reducing Costs in the Contact Center, Part 2 of 2
Jan 2008, ROI (Formerly Catalog Success Magazine), By Curt Barry

Liquidation Tactics for the Holiday Hangover
Jan 29, 2008, Multichannel Merchant, By Curt Barry

Post-Season Audits, Part 2: Reducing Costs in the DC
Jan 02, 2008, Multichannel Merchant, By Curt Barry

OF The Fulfillment Doctor....On Third-Party Fulfillment
Jan 31, 2007, Operations & Fulfillment, By Curt Barry

Multichannel Inventory Management
Jan 01, 2008, Multichannel Merchant, BY Curt Barry

Give me the Goods
Jan 01, 2008, Multichannel Merchant, by Curt Barry

Reducing Costs in the Contact Center, Part 1 of 2
Dec 2007, ROI (Formerly Catalog Success Magazine), By Curt Barry

Conducting a Post Season Audit, Part 1
Dec 18, 2007, Multichannel Merchant, By Curt Barry

Balancing Your Budget and Investment:

When is the Right Time to Outsource?

Nov 2007, ROI (Formerly Catalog Success Magazine), By Curt Barry

15 Tips to Combat Parcel Rate Increases

Nov 28, 2007, Multichannel Merchant, By Curt Barry

Rising Transportation Costs and What To Do About Them

Nov 13, 2007, Multichannel Merchant, By Curt Barry

Fulfillment Doctor: The Real Cost of Employee Turnover

Nov 07, 2007, Multichannel Merchant, By Curt Barry

Twelve Trends in Fulfillment

Nov 01, 2007, Multichannel Merchant, BY CURT BARRY

The Fulfillment Doctor on... The Price of Free Holiday Shipping

Oct 31, 2007, Multichannel Merchant, By Curt Barry

E-commerce isn't the only facet of multichannel marketing to advance

Oct 01, 2007, Multichannel Merchant, by Curt Barry

Merchandising 2.0

Oct 01, 2007, Multichannel Merchant, by Curt Barry

Juggling Web and Phone Contacts

Nov 01, 2006, Multichannel Merchant, by Curt Barry

OF Thinking of Relocating Your DC? Consider These 5 Factors

Oct 4, 2006, Operations & Fulfillment, by Curt Barry

OF Quick Tip: Little Touches Can Yield Big Gains in Customer Service

Sept 13, 2006, Operations & Fulfillment, by Curt Barry

Multichannel Inventory: What You Need to Know

Sept 1, 2006, Operations & Fulfillment, by Curt Barry

Exhibit A. The Transactional Notice – Requirements and Costs

Legal Requirement: The regulation requires that the customer be notified that they are responsible for self-reporting Colorado sales/use tax when purchasing from out-of-state retailers. This is required on every purchase, either on the purchase invoice or, for Internet orders, on the retailer's website.

1. Costs incurred to satisfy basic statutory/regulatory requirements.

a. *Change web order path*

We believe that companies' e-commerce system will need to be modified by Information Technology (IT) personnel to notify the customer of the Colorado requirements while s/he is in the order path but has not completed the transaction. I assume that most affected retailers will use a "linking notice" in the e-commerce shopping system / order path to alert a Colorado purchaser to the fact that they will be required to pay Colorado sales tax on merchandise purchased from the out-of-state retailer. We would expect that the customer would then be referred to the e-commerce site's Frequently Asked Questions (FAQs and answers) to provide the text of the required notice. The customer would have the option to abort (cancel) the shopping cart or basket and void the transaction.

Companies strive to make the checkout process in e-commerce streamlined and with as few "clicks" or steps as possible. A complicated checkout process is one of online shoppers' leading reasons for abandoning the sale.

We believe that most affected retailers will take great care in making the change for that reason. Based on the assumption that companies adopt a "linking notice," rather than some form of "work around," the cost to modify the order path for the message is conservatively estimated at \$5,000; for older technologies and companies using outside vendors, the estimated cost is up to \$10,000.

b. *Print statement on invoice / packing slip*

Changing how the computerized order prints can be a significant change because of the comprehensiveness of the program logic that creates the form, the limited amount of space on some printed forms for additional messaging, and other factors. A message about sales tax payment will need to print on the order or pack slip. Unless printed on every form regardless of whether the order is destined for a Colorado location, the message will be triggered by the Colorado state abbreviation "CO" in the customer or ship to address record.

The cost to modify the computerized order or pack slip is on the same order of magnitude as the website order path change discussed above, and is conservatively

estimated at \$5,000, or, for older technologies and companies using outside vendors, the estimated cost is up to \$10,000.

2. Costs that are necessary but not discretionary.

a. *Call center training and procedures.*

Call centers develop written scripts and procedures for training company representatives to handle transactions and exception conditions. Because of the customer impact for Colorado purchasers associated with the Transactional Notice, call centers will need to develop procedures on how to explain the statutory requirements to customers who have questions.

The cost for developing such procedures is estimated at \$2,000 to \$3,000. This does not include the actual training time which will vary by the call center size (i.e. number of reps), which will increase costs.

b. *Customer service call center costs to answer inquiries and complaints.*

We would expect that inquiries and complaints regarding the Colorado statutory and regulatory notice and reporting requirements will result in a three to four minute call. In our experience, the fully loaded cost per call is typically between \$1.50 and \$2.00. In defining this as fully loaded costs we include call center rep direct hourly wages, management, employee benefits, space, telecom, etc. Our estimate is that 50% of the customers in Colorado will have questions about sales/use tax as a result of the Transactional Notice. We did not estimate a cost as it varies with the size of the house file and therefore the number of customers and inquiries.

c. *Professional assistance.*

This statute will require assistance from expert legal or accounting firms to ensure company's compliance. Also, the systems developed will need to be highly accurate and treated in a manner comparable to a financial system even though the information may come from a marketing system. Companies may also need to change their published Customer Privacy Policies in order to alert their customers to the disclosure of personal information to the Colorado Department of Revenue. In addition, the company's creative department will need to create descriptions which are as "customer friendly" as possible because of the customer sensitive nature of this information.

Initial costs of experts to set up disclosure and reporting and assure compliance are conservatively estimated at \$3,000 to \$5,000.

d. *On-Going Compliance Costs.*

Because of the possible affect on customer satisfaction and the need to ensure the accuracy of reported purchases, we believe there will be the necessity for on-going

compliance review. The estimated annual costs of on-going compliance are \$1,500 to \$2,000.

3. Costs that are discretionary but good business practice.

a. *Modify the order processing system to calculate sales tax amount.*

We expect that some retailers will want to provide information regarding the likely amount of Colorado tax due on the sale as a service to customers

Presently, systems use zip codes or geo codes combined with merchandise categories and dollar limits to determine if a customer is subject to sales tax. In all cases where there is customer tax liability, the system calculates it and stores the tax total on the ordering systems' customer order.

In this case the retailer would not be collecting taxes. There is no "info only tax field" in systems to store the calculated sales tax value. In order to advise the customer, the order processing system would have to be changed either by the software vendor or internally.

The estimated costs for this modification may be in a \$5,000 to \$10,000 range.

Exhibit A.1. – The Transactional Notice Total Costs

Basic statutory/regulatory requirements

Modify the e-commerce order path: \$5,000 to \$10,000

or

Print statement on invoice / packing slip: \$5,000 to \$10,000

Necessary but not discretionary

Call center training and procedures: \$2,000 to \$3,000

(per call cost to address inquiries) (\$1.50 to \$2.00/call)

Professional assistance (Initial Compliance):

Initial Compliance: \$3,000 to \$5,000

Totals for low end first year compliance costs (sums of items above) \$10,000

Discretionary but good business practice

Modify order processing to calculate sales tax amount: \$5,000 to \$10,000

Totals for upper end first year compliance costs (sum of items above) \$28,000

Ongoing compliance (year two forward) \$1,500 to \$2,000

Exhibit B. The Annual Purchase Summary – Requirements and Costs

Legal Requirement: The statute and regulation require the production of the Annual Disclosure Notice, as a separate, First-Class mailing listing the date, purchase amount, and category of products purchased for each customer transaction during the prior calendar year.

1. Costs incurred to satisfy basic statutory/regulatory requirements.

This section identifies the estimated costs to create the tracking and reporting system for the Annual Purchase Summary, including:

- Systems costs resulting from year end disclosure requirements.
- Identifying purchasers with \$500+ of aggregate purchases delivered to Colorado locations (including gifts, B2B multiple location ship tos, "house-holding" issues, etc.). (The retailer must run the analysis on entire customer file, with the same baseline expense, regardless of how many Colorado purchasers the retailer ultimately identifies with purchases over \$500.)
- Capturing all purchase info (dates, amounts, categories).

There are two potential sources for this detail order information – the operational order processing system and the direct marketing system. The order and customer number associated with the transaction will also be required to answer customer inquiries back to the operational file. As explained later in this section (see *Complication to Tracking and Notification Programming*), there are complexities involved with the data base programming and identifying how to aggregate purchases.

a. *Program Development of the Colorado Tracking and Reporting Required.*

The retailer will have to develop a tracking and reporting system to meet the regulation's requirements. In a generalized way, we have outlined below the production processing steps the system and the various departments would need to accomplish to meet the statute's annual requirements. Because the company would likely address the requirements for creating a data file to satisfy the requirement to provide the Department of Revenue an annual Customer Information Report at the same time it developed processes for generating a data file for purposes of the Annual Purchase Summaries to customers, we have included steps for that process, as well. The production steps are:

1. The new system will use as its base data a high data integrity marketing or operational customer purchase file. It must have all detailed order/purchase activity data and customer name, billing address, ship to addresses, and purchase amounts. It must be totally accurate as a financial system would be.

2. IT Department extracts each customer with a ship to address in Colorado.
3. IT system will track all Colorado customer purchases and report all purchases regardless of amount.
4. IT system logic determines which customers exceed \$500 annual purchases.
5. IT Department runs preliminary file of customers purchasing over \$500 and Annual Purchase Summary to customers.
6. Retailer's Accounting Department would check the file to determine if any corrections are necessary.
7. Retailer's Accounting Department makes any corrections and approves final IT production run.
8. IT Department runs final file for Annual Purchase Summary purchasers based on ship to address.
9. IT system outputs Annual Purchase Summary disclosures to magnetic media or transmits the required data and formats to mailing house.
10. Mailing house produces disclosures and Annual Purchase Summary; inserts the printed material in #10 envelopes; and mails First Class.
11. IT Department runs a file of all customers with a Colorado ship to address to generate Customer Information Report for Department of Revenue.
12. IT Department performs quality control and formatting for transmission of the Customer Information Report to the Colorado Department of Revenue.

Some retailers may be able to perform all steps internally, depending upon their mailing and insertion capabilities. Within the Retailer's organization the responsibilities cited above could be performed by several different departments.

If the company chooses to run the new Colorado system at an outside service bureau, then the service would process the year end file of purchasers. If the company has not done marketing system updates earlier in the year this would need to take place first. In many companies these updates take place monthly or quarterly.

Many smaller companies do not use merchandise categories, so compliance with the requirements to provide the category of purchases may be very costly.

b. Costs of Initial Systems Modifications

The estimated costs for developing the system to track and produce the Annual Purchase Summary are as follows:

- Company internal development costs to develop system internally internal costs of \$8,000 to \$10,000, representing 175 to 225 hours; or
- External programming by marketing or software vendor to create system: \$15,000 to \$20,000, representing 100 to 135 hours.

c. Annual Costs to Produce the Annual Purchase Summary Mailing

The total costs of creating the actual First-Class mail pieces will vary for each retailer depending upon the number of Colorado customers who purchase over \$500 and must receive the Annual Purchase Summary. Therefore, we have done a calculation of the cost on a per piece basis.

In order to get an estimate of the number of customers, one has to develop an estimate of the number Colorado customers that are affected by the regulation. In general we feel there are several factors which will determine how many customers get the Annual Purchase Summary:

- Size of the 12 month buyer (purchaser) file – varies by sales volume.
- Average order in dollars – many businesses have less than \$100 average order, but some retailers, such as consumer electronics vendors, have an average order value of several hundred dollars.
- The number of times a customer purchases annually is often less than 2 times on average, but many companies have a substantial number of loyal, repeat customers.
- Number of one time buyers – most businesses experience that 50% of all first time buyers are opportunistic and never buy again.

Our conclusion is that less than 20% of the Colorado purchasers (who are 1.6% of all purchasers based on Colorado's population or a percentage of total U.S. population) on a company file will buy \$500 or more per year. This yields a relatively small number of customers for most out-of-state retailers (perhaps between 50 and several hundred such customers annually for many retailers, although larger retailers will have substantially more). However, it bears repeating that a company with only a small number of customers over the \$500 threshold must still incur the initial set-up costs and annual processing costs, in order to be able to generate the required Annual Purchase Summaries.

The costs of the annual IT production processing, the mailing house insertion, the postage and mailing of the customer disclosures is a variable cost based on the number of customers over \$500. Steps in the process include, but are not necessarily limited to:

- Production run time costs annually. The cost of computer processing and the IT labor has a cost per hour which is not easily identified. This will be true whether internal company processing or through a marketing service bureau. If a company requires a marketing service bureau, such bureau generally will include a minimum set up charge (which could be \$200 to \$300 bundled into the per piece cost) and a cost of \$2 per 1000 names processed (or about \$0.002 per piece).
- Mailing service costs. Costs to run and insert the Annual Purchase Summary is a variable cost based on typically minimum set up cost (of \$100 to \$200 dollars bundled into the per piece cost) and a variable cost for 500 to 1,000 customers mailed. Based on our experience, I would expect this cost to be from \$1.25 to \$1.50 per piece.
- Supplies will cost \$0.10 to \$0.20 per piece.
(We assumed up to two inserts and a #10 envelop.)
- Annual Purchase Summary must be mailed First-Class Mail for \$0.44 per piece.

When all costs are summed and the estimated number of Colorado customers purchasing over \$500 annually is determined, the estimated costs including file generation and mailing costs, the average cost will be, on the low end, \$2.00 to \$3.00 per customer disclosure (per piece) including all minimums and set ups.

d. Complications to Tracking and Notification Programming

As mentioned earlier, there are several direct marketing data base IT system concepts that complicate the programming of "who the purchaser is" and who will receive the Annual Purchase Summary. For example:

- Business-to-Business (B2B) – it is not uncommon for B2B transactions to derive from complicated marketing data base structure and mailing concepts. If we use a school district as an example, it may be better understood. Public schools are part of an entity like a county or city. There are often many contact names, addresses, billing information, e-mails and telephone numbers in the total scheme of a customer record. For example, a teacher in a local school may be the one ordering the product. Customer purchase data might be grouped with other purchases under a school district; or school's department (e.g. science department). A county purchasing agent may pay for the

order. Or a school purchasing agent. Or the individual teacher may pay for the shipment. Determining who is the "customer" is becomes complicated.

- In consumer retailing, there is the concept of "householding". Think of a house that has two children and an adult. They all live at the same address, and companies often consider a household to be a buying unit for marketing and business purposes. Many retailers will need to confront problems created by "householding" logic built into existing systems to ensure compliance with the law.
- Customers often use different names. I will use myself as an example. My given Christian name is "Fred Curtis Barry". The name I choose to use for my company is "F. Curtis Barry & Company". The name many people know me by is "Curt Barry". The complexity associated with the very common use by consumers of variations on their name often generates multiple catalogs and other correspondence. In determining who the "purchaser" is, retailers will need to address such issues in ensuring compliance with the law.

2. Costs that are necessary but not discretionary.

Regarding the language of the Annual Purchase Summaries, we would expect that the required information would need to be carefully crafted and disclosed, similar to bank card and accounts receivable notices. However, retailers will want their notices to be more customer friendly in format and language than financial notices so that they do not lose the customer. There will be professional fees and creative/development costs that may be substantial (*i.e.*, several thousand dollars) in reviewing and finalizing the language of the notice and ensuring it contains all of the necessary disclosures for the Annual Purchase Summary set forth in regulation. I have not made a detailed estimate of such costs because the variables involved are too many to address, but such costs will clearly be necessary.

3. Costs that are discretionary but good business practice.

We believe that it would be prudent to have an internal person on site at mailing service to assure privacy when running and inserting the Annual Purchase Summary. This may include travel time and expenses for the trip to the marketing service bureau/mail shop, if it is not local. I have not made a specific estimate of such costs.

As discussed earlier, from a customer service perspective, we can envision companies wanting to be able to inform the customer of the approximate amount of Colorado sales/use tax due not only on a per order basis, but annually, as well. The cost of providing such capability would be derivative of the costs to change the system logic described above for the Transactional Notice, and would affect overall costs only incrementally.

Exhibit B.1. – Annual Purchase Summary Total Costs

Basic statutory/regulatory requirements (first year)

Company internal development costs: \$8,000 to \$10,000

OR

External programming by marketing or software vendors: \$15,000 to \$20,000

Totals for low end compliance costs \$8,000

Totals for upper range compliance costs \$20,000

In addition, the Annual Purchase Summaries will have a variable cost \$2.00 to \$3.00 per customer statement mailed each year

(Thus, if a Retailer has 250 customers who purchase in excess of \$500 in a calendar year, the costs for the mailing will be \$500 to \$750)

Exhibit C. The Customer Information Report – Requirements and Costs

Legal Requirement: Provide annually to the Colorado Department of Revenue a data file containing the name, billing address, all shipping addresses, and total purchase amount for each customer shipping goods into Colorado, regardless of total purchase amount.

1. Costs incurred to satisfy basic statutory/regulatory requirements.

In Exhibit B, regarding the costs associated with the Annual Purchase Summary, I included in the required systems modifications two additional steps for creation and transmission of the report to the Colorado Department of Revenue. The steps are:

11. IT runs a file of all customers with a Colorado ship to address to generate the Customer Information Report for Department of Revenue.
12. IT performs quality control and formatting for transmission of the Customer Information Report to the Colorado Department of Revenue.

The relevant systems development costs for these steps were also included in Exhibit B.

Unfortunately, the final specifications for the annual Customer Information Report have not yet been published by the Department. These specifications could dramatically impact the costs of creating the file if, for example, the Department requires specialized software that retailers do not normally use. At the very least, we expect that complying with Department file specifications will add \$1,000 to \$3,000 to the costs.

Customer information and purchase information is protected by privacy statutes and the data is typically encrypted when sent between locations. This is not specified in the Colorado regulations and could increase costs.

Although some of the initial investment is built into the costs detailed for developing systems to create the Annual Purchase Summaries for customers, the disclosure report to the Department of Revenue has much broader consequences and is a much larger file (because it must include ALL Colorado purchasers, not merely those purchasing over \$500).

Companies will spend hundreds of hours of general management, marketing, call center, IT and accounting time interpreting and implementing this regulation in their company business environment and systems.

Because the Customer Information Report is a compliance report, it will consequently require considerable management time to review, validate, transmit, etc. Errors in reporting can have severe consequences with Department of Revenue and the

company's customers. Even making a very conservative estimate of the additional management time for preparing such a file, the time required for such quality control/quality assurance tasks would be between 150 and 200 hours, or between \$7,500 and \$10,000, separate and apart from additional systems costs.

2. Costs that are necessary but not discretionary.

None identified.

3. Costs that are discretionary but good business practice.

None identified.

Exhibit C.1. – The Customer Information Report Total Additional Costs

Basic statutory/regulatory requirements

Final specifications	\$1,000 to \$3,000
Management time	\$7,500 and \$10,000

Totals for low end compliance costs \$8,500

Totals for upper range compliance costs \$13,000

Exhibit D. Other Potential Costs Not Estimated

There are a number of potential costs which we wish to point out that have not been estimated.

- Overhead. These estimates do not include much of the management time spent by Call Center, Marketing, Accounting and General Management personnel required to understand, develop and implement the required systems, changes in Customer Service and Privacy Policies, etc. These could easily exceed the stated costs in this opinion.
- High cost of losing customers and losing sales. Out-of-state retailers have existing relationships with Colorado purchasers and prospects. They have acquired Colorado customers by promoting and mailing to Colorado purchasers. For example, the cost to acquire a customer can be \$10 to \$25 because of the low response nature of direct marketing. It often takes 2 or 3 purchases for retailers to have a profitable customer relationship because of these acquisition and fulfillment costs. We anticipate that this statute's requirement will cause a major percentage of the customers to abandon the shopping cart or stop and call the Call Center. Ultimately, the customer may stop shopping through these channels.

Retailers may unfortunately find that it's far cheaper to not advertise or solicit business in Colorado, rather than incur substantial compliance costs for a process that will alienate many customers.

In general, in-state Colorado retailers will have a significant competitive advantage over out-of-state retailers because in-state retailers that collect Colorado sales tax will not have to incur these tremendous costs or turn over sensitive customer information to the Department.

- Other regulatory compliance expense. For larger companies, many of these costs will be higher, if they have to meet regulatory requirements, such as Sarbanes/Oxley compliance and/or changes for PCI compliance.
- Cost of litigation. Settling customer privacy and legal challenges by customers arising from inadvertent disclosure of customer information.