Colloquy in Support of Legislation Clarifying the Definition of Creditor under the FTC "Red Flags" Rule

Senator Thune: Mr. President, I wish to engage my colleagues Senator Dodd and Senator Begich in a colloquy.

I rise today in support of (S. XXXX), the Red Flag Program Clarification Act of 2010, legislation that Senator Begich and I have introduced to narrow the scope of section 114 of the Fair and Accurate Credit Transactions Act of 2003 (the FACT Act). This section of the FACT Act directed financial regulatory agencies, including the Federal Trade Commission (FTC), to promulgate rules requiring "creditors" and "financial institutions" to implement programs to detect and respond to Red Flags (patterns, practices, or specific activities) that could indicate identity theft.

The purpose of the Red Flag Program Clarification Act of 2010 is to identify and limit the type of "creditor" that must be covered. If the FTC's final Red Flags Rule is implemented, this rule could require small businesses to undertake costly, burdensome measures to prevent identity theft in industries where it poses little threat. Identity theft is a serious problem, but the definition of "creditor" for purposes of the FTC's Red Flags Rule is too broad and would cover small businesses that pose little risk to consumers.

Under the legislation that Senator Begich and I are proposing, only a "creditor" that regularly and in the ordinary course of its business obtains or uses consumer reports in connection with a credit transaction, furnishes information to consumer reporting agencies in connection with a credit transaction, or advances funds would be required to develop and implement a written identity theft prevention and detection program.

So, for example, an accountant would not become a creditor simply for obtaining a consumer report (with the permission of any consumer whose report is obtained), in order to examine the integrity of a company's management.

And the legislation makes clear that an advance of funds does not include a creditor's payment in advance for fees, materials, or services that are incidental to the creditor's ability to provide another service that a person initiated or requested, such as the advance payment of expert witness fees by a lawyer to support the representation of a client.

Any other type of creditor may only be covered through a rulemaking based upon an agency's determination that these types of creditors offer or maintain accounts that pose a reasonably foreseeable risk of identity theft. Such creditors would receive notice that they could be covered by a rule, and there would be a public airing of the issues when the proposed rule is published for notice and comment.

Senator Dodd, as Chairman of the committee of jurisdiction, the Senate Banking Committee, could you provide us with some context regarding the legislation under which the FTC's rule was promulgated?

Senator Dodd: Gladly. The FTC's Red Flags Rule implementing section 114 of the FACT Act became effective on January 1, 2008. The rule applied to "creditors," defined under the FACT Act the same way as in the Equal Credit Opportunity Act ("ECOA"), to include any person that sells a product or service for which the consumer can pay later.

After the Red Flags Rule became final, many businesses and other entities indicated that they were not aware that they would be covered by this rule. At first, the FTC delayed enforcement of the rule several times to allow these entities time to come into compliance with the rule. Then, a number of professional organizations, including the American Bar Association and the American Medical Association, sued the FTC for taking the position that professionals were "creditors" when they allowed consumers to pay later, and would have to comply with its Red Flags Rule. On May 28, 2010, the FTC announced that it would delay enforcing its Red Flags Rule through December 31, 2010 and asked Congress to pass legislation that would resolve any questions about which entities should be covered as "creditors" and to obviate the need for further enforcement delays.

Senator Begich: Thank you Senator Dodd. Unless this bipartisan bill becomes law, many small businesses for which identity theft is not a threat could be required to spend time and effort to comply with the Red Flags Rule implementing the FACT Act. This could require them to take time away from growing their businesses and creating jobs. Small businesses are the economic driver of our country, and in a time of high unemployment and stagnant economic growth, businesses should be focused on job creation, and should not have to spend the money to comply with regulatory burdens disproportionate to the scope of the identity theft problem.

This bill would address what Chairman of the FTC, Jon Leibowitz, called "the unintended consequences of the legislation establishing the Red Flags Rule." While this list isn't exclusive, many small businesses such as doctor's and dentist's offices, pharmacies, veterinary clinics, accounting offices, and other types of health care providers and other service providers were classified as "creditors" because they sometimes let clients pay after they provide their services. This legislation makes clear that these small businesses should not be swept under the Red Flags Rule in the future just because they allow payment to be deferred, when they don't offer or maintain accounts that pose a reasonably foreseeable risk of identity theft.

I would ask the Chairman of the Banking Committee if he agrees with my description of what the Red Flag Program Clarification Act of 2010 will accomplish?

Senator Dodd: Yes, I agree that this bill narrows the applicability of the Red Flag identity theft provisions of the FACT Act to cover those creditors where identity thieves can do the most harm – creditors that use consumer reports, furnish information to consumer reporting agencies, and other creditors that loan money, such as payday lenders, that do not necessarily use consumer reports or furnish information to consumer reporting agencies.

The legislation also makes clear that lawyers, doctors, dentists, orthodontists, pharmacists, veterinarians, accountants, nurse practitioners, social workers, other types of health care providers and other service providers will no longer be classified as "creditors" for the purposes of the Red Flags Rule just because they do not receive payment in full from their clients at the time they provide their services, when they don't offer or maintain accounts that pose a reasonably foreseeable risk of identity theft.

Senator Thune: I applaud the FTC's cooperation in delaying implementation of their Red Flags Rule to wait for Congressional clarification on this issue and thank Senator Dodd for his assistance in drafting this legislation. I am confident that our efforts to provide a legislative solution that protects consumers and businesses alike can be achieved through this legislation.