



## Many still unprepared for federal ID-theft rule

### Takes effect Aug. 1 despite efforts to exempt attorneys

**Published:** July 27, 2009

The Federal Trade Commission is warning lawyers that a first-of-its-kind identity-theft rule that goes into effect on Aug. 1 absolutely applies to members of the bar.

The "Red Flags Rule" requires businesses that have consumer accounts - including many law offices - to implement written identity theft prevention policies.

"There is no question there are a lot of entities out there, including law firms, that aren't even aware they have to be in compliance by Aug. 1," said Linn F. Freedman of Nixon Peabody. "The FTC has taken a strong stance that there needs to be widespread concern about stopping identify theft, and that means lawyers and their practices are going to be impacted."

Arguing that the risk of ID theft in their industries is minimal, organizations representing lawyers, doctors, accountants and other professionals have unsuccessfully lobbied the FTC that the rule should not apply to them. As recently as mid-July, the American Bar Association met with the FTC to make such an argument.

"The position [the organizations] have been advancing is that these rules are like taking a sledgehammer or using a nuclear bomb for a little fight in the sandbox," said Freedman, who has been preparing her firm and health care clients for the new rule.

The American Medical Association, she said, put up a "big fight and pretty much lost with the same arguments, so I'm not confident the ABA will be successful in this fight either."

The FTC has twice delayed enforcement of the rule in order to give businesses more time to comply. The original compliance deadline of November 2008 and a subsequent May 1 date were both postponed. As of press time, the Aug. 1 date remained in place.

A similar data breach regulation for Massachusetts is slated to go into effect in 2010.

#### Covered accounts

Mark E. Schreiber, chairman of the privacy group at Edwards, Angell, Palmer & Dodge in Boston, said the ABA took up the cause after his firm reached out to the association in March.

Estimating that 95 percent of the Massachusetts legal community is still in the dark with regard to the FTC rule, Schreiber said Edwards Angell asked the ABA whether it believes the regulation applies to law firms

"because there was a lot of debate about what the right answer was."

He said part of the confusion stems from the rule's broad definition of "creditor." That definition includes businesses or organizations that regularly accept deferred payment, or provide goods or services and bill clients at some later date.

To be subject to the rule, a creditor must have "covered accounts," which include those provided to clients for personal, family or household purposes on a continuing basis. Other accounts that have a reasonably foreseeable risk of identity theft also fall under the rule. Creditors with covered accounts must implement written policies on detecting and responding to the "red flags" of identity theft, such as inconsistent personal information.

Each business may have different red flags depending on its industry and size. Breaches of the rule, which was adopted under the Fair and Accurate Credit Transactions Act, can lead to civil penalties, such as monetary sanctions and FTC enforcement action.

Schreiber said the new rule means law firms with trusts and estates and employment departments are likely to have covered accounts. Similarly, he said lawyers who handle plaintiffs' class-action work in which they are in possession of client Social Security numbers will also be impacted.

"It's not just large firms," he said. "It could be any number of offices where Social Security numbers or other data are kept that could create some risk of identity theft."

When asked how a rule that impacts numerous lawyers and clients seemingly could have slipped through the cracks, Schreiber said many firms are simply unaware they fall under the FTC's definition of "creditor."

"Most firms and most lawyers think in terms of clients and cases and not in terms of data," he said. "But barring any last-minute injunctions, the directive coming from the FTC is that they are going to be treated like everyone else. Nobody can really determine when or where malicious attacks are going to come from."

### **Leave us alone**

If the FTC refuses to change its position, ABA President J. Thomas Wells Jr. told Lawyers Weekly last week that his organization will file suit in Washington, D.C., before Aug. 1

Wells, who said he has met with all the commissioners on the FTC, noted that Proskauer Rose had agreed to represent the organization on a pro bono basis.

"At this point, with Aug. 1 staring us in the face, it's fair to say that all options are on the table, including a lawsuit," he said. "Barring the announcement of some further delay in the enforcement of the rule, that would have to be our final option."

ABA representatives argued that Congress intended the rule to apply to financial institutions and other businesses that extend credit, not lawyers who merely bill for services after they are performed.

In a statement published on the ABA's website, Wells says that two U.S. circuit courts have already held that legal fees are not "credit transactions" under the law. In addition, he says regulations on the practice of law are traditionally left to the states and can be disturbed only by federal law if statutory language expressly says so.

"Nowhere in the FACT Act did Congress even imply that it intended to regulate lawyers with respect to their client relationships," writes Wells.

Treating lawyers as creditors, he adds, would impose an undue burden, particularly on sole practitioners. Where compliance with the Red Flags Rule would complicate client arrangements and require a major time commitment, Wells accuses the FTC of failing to identify a single case of ID theft in the legal services context.

Betsy Broder, assistant director in the FTC's Division of Privacy and Identity Protection, confirmed to Lawyers Weekly that efforts by the ABA to exempt lawyers are still under way. She said, however, that the ABA is unlikely to prevail.

"Legal professional groups have certainly advocated their position that lawyers should not be covered, but Congress directed the FTC to develop rules that cover creditors, and our position is that the definition Congress provided to us says that lawyers can and should be covered," she said.

Broder said that several appellate decisions have held the definition of creditor includes lawyers and other professional industries "who regularly defer payments from clients."

But she acknowledged that many attorneys have not even begun the process of determining whether the rule applies to them and said the FTC does not expect all lawyers to be in full compliance by Aug. 1.

"From an enforcement perspective, we are aware that many entities have been struggling with this," she said. "All we are looking for at this point is good-faith compliance. We are not going to be on the prowl for technical violations of this rule. Our primary interest is to help covered entities come into compliance."