

As you know, enforcement of the new Red Flag rules, which require adoption of an identity theft policy and require training of all covered employees went into effect on January 1. As you also know, Congress passed an amendment on December 18 that initially appeared to limit the impact of the new rules. However, it also created a lot of confusion.

In the intervening few weeks, we have been trying to get our arms around this. Below is an alert sent out by the Oklahoma Municipal League to their member cities that provides excellent insight. It was prepared by OML's General Counsel, Diane Pedicord, who I believe is the pre eminent expert in the nation on Red Flag compliance for local government. She has spoken at a number of state municipal league conferences on the topic, and contributed significantly to the development of our online Red Flag class. I have huge respect for Diane and her insights and am sharing this with her permission.

This remains an area that has high liability for non compliance, but which is still a bit fuzzy regarding compliance. Of course, Diane's alert does not constitute legal advice. I suggest you share Diane's analysis with your City Attorney and have them provide you explicit guidance on which employees you need to train, and other Red Flag compliance related issues. I have highlighted a few key items in her alert in yellow. The highlights are mine not Diane's.

Based on the best information we have available, I believe you probably still need to train those who you previously thought you needed to train. We do have sample policies and other information available on our website at http://www.governmentresource.com/pages/everify_red_flag. If you want to train your covered employees using our online Red Flag class, you can contact Krisa@GovernmentResource.com. Krisa can also assist you if you prefer to conduct live training for your covered employees.

I hope the OML Red Flag Alert below helps you sort through all of the confusion created by this federal mandate that has been a moving target over the last three years. Let me know if I can ever do anything for you at all.

Warmest regards,

Ron Holifield

ALERT: Red Flag Rule Effective 12/31/10 with Congressional Clarification. As you know, the Federal Red Flag identity theft rules were delayed several times over the past three years due to controversy over how broadly they defined creditors. In May 2010, they were delayed until December 31, 2010 to allow Congress time to clarify the federal law. Congressional action was taken late in the recent lame duck session to amend the definition of "creditor".

We have contacted the National League of Cities (NLC) and they advise that the 2010 Clarification grants the Federal Trade Commission (FTC) a good deal of leeway in rulemaking to determine the Red Flag's impact on different sectors – including the operations of cities and towns. The key will be FTC's future decision on **whether municipal operations pose a "reasonably foreseeable risk of identity theft."**

The FTC currently has an Update on its website stating the Red Flag Program Clarification Act of 2010 "limits the circumstances in which creditors are covered" by the Red Flag requirements. While the website displays the text of the amendment, at this time it has no interpretation of the amendment's application to cities and towns. NLC is currently accessing its FTC contacts.

Meanwhile, the Red Flag Rule has gone into effect and creates duties and potential liabilities for municipalities that have covered accounts. **At this point, until the FTC provides guidance on**

“reasonable foreseeable risk”, it appears that most municipal operations, including utility accounts, will NOT be affected by the last-minute congressional action. NLC suggests that cities and towns should continue to apply their Identity Theft Prevention Plans developed to comply with the existing Red Flag Rule language.

Here is the applicable legal analysis:

Under the new congressional 2010 clarification, a creditor is defined in the same way as the Red Flag Rule:

The term “creditor” means any person who regularly extends, renews, or continues credit; any person who regularly arranges for the extension, renewal, or continuation of credit; or any assignee of an original creditor who participates in the decision to extend, renew, or continue credit.

However, the new Act applies the term in 3 categories:

1. Those who “regularly and in the ordinary course of business”:
 - Obtains or uses consumer reports, directly or indirectly, in connection with a credit transaction;
 - Furnishes information to consumer reporting agencies in connection with a credit transaction; or
 - Advances funds to or on behalf of a person, based on an obligation of the person to repay the funds or repayable from specific property pledged by or on behalf of the person.
2. Excluding those creditors who fall into the third bullet point above, if the creditor advances funds for expenses incidental to a service provided by the creditor to the person. Professional groups such as attorneys and physicians believe this relieves them of the requirements of the Red Flag Rules.
3. Including any other type of **creditor**, as defined in 15 U.S.C. 1691a as the FTC may determine appropriate by rule promulgated by the FTC based on a determination that such creditor offers or maintains **accounts** that are subject to a **reasonably foreseeable risk** of identity theft.

This last category captures municipal utility operations and other municipal accounts that the FTC determines will have a reasonably foreseeable risk of identity theft. Although we must await guidance from FTC, it appears that the new congressional clarification allows the FTC to fine tune what types of creditor activity will be governed by the Red Flag Rule by excluding those deferred payment arrangements that do not create a reasonably foreseeable risk of identity theft. (Under the existing definition of “account”, the Rule applies to all continuing relationships between a creditor and a customer providing for multiple deferred payments.)