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FTC Lacks Authority to Regulate Lawyers Under the Fair and Accurate Credit Transactions Act

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Lawyers for the Profession® Alert

American Bar Association v. Federal Trade Commission, __ F.Supp.2d __, 2009 WL 4289505 (D.D.C. 2009)

Brief Summary
The Federal Trade Commission's statutory authority to regulate "creditors" in order to combat identity theft does not include the power to regulate lawyers. The power of a federal agency to regulate lawyers in the lawyer-client relationship here would require evidence of clear Congressional intent and would have to take into account a lawyer's ethical duties and the essential aspects of the lawyer-client relationship.

Complete Summary
In 2006 the Federal Trade Commission (FTC) took the first steps in creating what is commonly referred to as the Red Flags Rule under the Fair and Accurate Credit Transactions Act (the FACT Act). The rule requires financial institutions and creditors to establish policies targeted at preventing identity theft. After multiple delays in implementation to clarify which individuals and entities were covered, and shortly before the rule was scheduled to take effect, the FTC issued a press release in April 2009 indicating — for the first time — the FTC's policy that attorneys who bill clients after services are rendered would fall under the rule's definition of "creditor," and thus be subject to the provisions of the FACT Act. A "creditor" is defined by the law here as someone who *regularly* extends the right of a debtor to defer payment.

A firestorm of criticism from the legal profession ensued, and the American Bar Association (ABA) sought declaratory and injunctive relief, arguing that application of the rule to attorneys exceeded the FTC's statutory authority. The U.S. District Court, District of Columbia, granted the ABA summary judgment, supplementing the court's oral ruling.

The court held that Congress neither explicitly nor implicitly, in language or in purpose, granted the FTC authority to regulate attorneys under the FACT Act. The court noted that the terms used to describe the entities regulated by the Act and the population that the Act sought to protect did not correspond with terms applicable to the legal profession. Regarding the former, the terms "financial institution" and "creditor" do not squarely describe law firms or the relationships law firms have with their clients. Regarding the latter, the Act

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sought to protect "account holders" and "customers," which are terms that do not squarely describe clients or the relationships clients have with their attorneys.

The court found that nothing in the legislative history or the administrative record, which never considered the subject of regulating lawyers, indicated that the FACT Act or the Red Flags Rule applied to the legal profession. The court held that Congress unambiguously did not intend the FACT Act to apply to attorneys.

The court also noted that, even if Congress' intent was ambiguous, the FTC's construction of the FACT Act was unreasonable, completely arbitrary, post-hoc without any inquiry or fact-finding, and thus impermissible and entitled to no deference. The FTC argued that monthly billing of clients constituted deferred payment, but the court noted that ethical constraints prevent a lawyer from taking ownership over client funds before they are earned, and as a practical matter lawyers generally must bill on a periodic basis. The court found that the Commission failed to demonstrate the need to redress identity theft in the legal profession, citing a number of ethical rules that already give lawyers incentive to prevent identity theft, namely Model Rules 1.1, 3.3, 4.1(b), 4.4(a), and 7.1. In addition, the court distinguished *Heintz v. Jenkins,* 514 U.S. 291 (1995) (regulating lawyers as "debt collectors" under 15 U.S.C. § 1692a(6) if they regularly collect or seek to collect debts), and *Goldfarb v. Va. State Bar,* 421 U.s. 773 (1975) (the practice of law constitutes "commerce" subject to Section 1 of the Sherman Act).

Finally, the court held the FTC's construction impermissible based on federalism concerns. The court noted that regulation of attorneys is traditionally a state prerogative and cited precedent indicating that if Congress' language is ambiguous, it is unreasonable for a federal agency to decide Congress has chosen to regulate lawyers without a clear statement of congressional intent to do so.

Significance of Opinion

The federal court here refused to defer to an agency's post-hoc policy implementing an administrative rule that would alter the federal-state balance of power in regulating lawyers, without a clear statement of congressional intent and lacking any administrative record to support the agency's position.

Although the FTC's unsupported policy is unlikely to be repeated, the court's reliance on federalism concerns, ethical duties of lawyers, and protection of essential aspects of the lawyer-client relationship from federal regulatory intrusion, stands as an important, precedent-setting holding with potentially broad implications for any future federal administrative regulation of lawyers.

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