INFORMATION TECHNOLOGY INDUSTRY COUNCIL

FEDERAL TRADE COMMISSION RECEIVED DOCUMENTS APR 3 2000 SECRETARY

March 31, 2000

Secretary
Federal Trade Commission
Room H-159
600 Pennsylvania Avenue, N.W.
Washington, D.C. 20580

Re: Gramm-Leach-Bliley Act Privacy Rule
16 CFR Part 313 -- Comment

Dear Mr. Secretary:

The Information Technology Industry Council ("ITI") is pleased to respond to the Federal Trade Commission's request for public comments on the rules proposed by the FTC in connection with the Gramm-Leach-Bliley Act (the "Act"). ITI commends the FTC for the substantial efforts it has made (in cooperation with the other agencies granted rulemaking authority under the Act) to draft regulations that balance the burdens to be imposed on industry against the privacy needs of consumers.

ITI represents the leading product and service providers in the information technology industry: 3Com Corporation, Agilent Technologies, America Online, Inc., Apple Computer, Inc., Cisco Systems, Inc., Compaq Computer Corporation, Corning, Inc., Dell Computer Corporation, Eastman Kodak Company, Gateway, Hewlett-Packard Company, IBM Corporation, Intel Corporation, Lexmark International, Inc., Microsoft Corporation, Motorola, Inc., NCR Corporation, Nortel Networks, Panasonic, Pitney Bowes Inc., SGI, Sony Electronics Inc., StorageTek, Symbol Technologies, Inc., Tektronix, Inc., Tyco International (US) Inc., and Unisys Corporation. ITI and its members are dedicated to building relationships with customers that are based on trust and transparency. Consumer notice of the manner in which their information will be treated is central to these trusting relationships, and ITI strongly supports good privacy practices.

Our members are involved in virtually all aspects of software development and licensing, hardware manufacture and sales, and electronic commerce. ITI is committed to advancing the global competitiveness of its members through supporting policies that encourage innovation and enable consumer choice. In 1999, our members had worldwide revenue of over $460 billion and employed more than 1.2 million people in the United States.

In general, ITI believes that the FTC's proposed financial privacy regulations, and, in particular, the definition of "financial institution" included in the proposed regulations, contain worrisome ambiguities that could sweep within the coverage of the regulations broad segments of the U.S. economy that Congress never intended to subject to detailed privacy regulations under the Act. For example, ITI does not believe that the FTC intended to include in the scope of its proposed regulations either (a) all retailers that merely refer their customers to credit-granting institutions in connection with the purchase of goods from those retailers or (b) all manufacturers of computer software and hardware. But the language of the FTC's commentary introduces ambiguity with respect to both of these subjects. ITI submits these comments in an effort to clarify these existing ambiguities in light of the structure and purpose of the Act as a whole.

I. BACKGROUND

The Act was designed to permit banks, securities firms, and insurance companies to merge with each other and to offer a broad array of financial products to consumers, notwithstanding a variety of legal restrictions that had been designed decades ago to keep these industries separate. As Congress considered the ramifications of allowing combinations among firms in these largely separate industries, the issue of financial privacy took a central place in the debate.[1] The result was the addition of Title V to the Act ("Disclosure of Nonpublic Personal Information"), designed to protect the financial privacy of consumers by (a) limiting the instances in which a financial institution may disclose nonpublic personal information about a consumer to nonaffiliated third parties, and (b) requiring a financial institution to disclose to all of its customers the institution's privacy policies and practices involving both affiliates and non-affiliates.

At the time the Act was passed, many businesses assumed that these privacy protections would apply only to traditional financial institutions -- like banks, brokers, and insurers. But the financial institutions at the center of the debate over the Act had successfully insisted on including in the Act broad definitions of the kinds of financial activities in which their newly created financial holding companies could lawfully engage. When the same definitions of activities deemed to be "financial in nature or incidental to such financial activity" were transposed into the new Title V, the result was a privacy law that could be read as applicable to a broad range of activities outside the traditional fields of banking, securities, and insurance.

As a tradeoff for allowing banks, insurance companies and securities firms to affiliate with each other, Congress required that consumer financial information be treated with increased care by firms wielding these new, broader powers. ITI understands that, in order to have a level playing field, traditional "financial" institutions have insisted that "competitors" be subjected to the same new regulatory burdens they will face, lest they be placed at a competitive disadvantage in exercising the new powers they have won.

ITI is confident that the privacy provisions found in subpart A of Title V of the Act were not intended to be applied to the provision of consumer goods or services by entities that are not

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1 Commentators have suggested that the privacy provisions of the Act were last-minute additions to a piece of legislation that had been under consideration for years. E.g., American Bankers Association, Banking Online Journal, "The Gramm-Leach-Bliley Act," December 1999 (http://www.banking.com/aba/law_1299.asp) ("It has been an amazing ride, long in anticipation, quick in retrospect. . . . .What we did not expect was the rush to judgment by Congress during 1999 regarding financial privacy. The financial modernization train was leaving the station and privacy was a last-minute stowaway. ")

themselves performing functions traditionally performed only by banking, securities, or insurance companies. The overall purpose of the Act should translate to regulations that hold financial holding companies (including those holding companies who have expanded into ancillary lines of business) to certain financial privacy obligations. Entities that *happen* to be providing consumer goods or services that are *also* provided as ancillary lines of business by financial holding companies (like travel agencies, hardware manufacturers, courier companies, and software licensors) should not be subjected to the same regulations. Nor should this coverage extend to non-financial entities that offer their customers financial services provided by other entities that may, because of their traditional financial activities, have independent responsibilities under the Act.

A. Summary of the proposed regulations

The FTC's proposed regulations:

1. Require a financial institution to provide notice to customers about its privacy policies and practices;

2. Describe the conditions under which a financial institution may disclose nonpublic personal information about consumers to nonaffiliated third parties; and

3. Provide a method for consumers to prevent a financial institution from disclosing that information to nonaffiliated third parties by "opting out" of that disclosure.

The notice and disclosure requirements of the proposed rules apply to information about individuals who obtain from a "financial institution" a "financial product or service" to be used for personal, family, or household purposes. The threshold question, therefore, is whether a particular entity is a "financial institution."

B. Key definitional questions

Section 509(3) of the Act defines "financial institutions" broadly to include all institutions "the business of which is engaging in financial activities" as described in Section 4(k) of the Bank Holding Company Act, 12 U.S.C. 1843(k). Section 4(k) includes not only a number of traditional financial activities, but also activities that the Federal Reserve Board has found to be ***closely related to banking*** or ***usual in connection with the transaction of banking or other financial operations***, including but not limited to:

- lending, exchanging, transferring, investing for others, or safeguarding money or securities;
- insuring, guaranteeing, or indemnifying against loss, harm, damage, illness, disability, or death, or providing and issuing annuities, and acting as principal, agent, or broker for purposes of the foregoing, in any State;
- providing financial, investment, or economic advisory services, including advising an investment company;

- issuing or selling instruments representing interests in pools of assets permissible for a bank to hold directly;
- underwriting, dealing in, or making a market in securities;
- brokering or servicing loans;
- extending credit and servicing loans;
- leasing real or personal property (or acting as agent, broker, or advisor in such leasing) without operating, maintaining, or repairing the property;
- appraising real or personal property;
- check guaranty, collection agency, credit bureau, and real estate settlement services;
- providing financial or investment advisory activities including tax planning, tax preparation, and instruction on individual financial management;
- management consulting and counseling activities (including providing financial career counseling);
- courier services for banking instruments;
- printing and selling checks and related documents;
- community development or advisory activities;
- selling money orders, savings bonds, or traveler's checks;
- providing financial data processing and transmission services, facilities (including hardware, software, documentation or operating personnel), data bases, advice, or access to these by technological means.

Thus, because "financial activities" can include everything from lending money and extending credit to selling money orders, from providing insurance to providing courier services for banking instruments, and from underwriting securities to operating a travel agency "in connection with financial services" (and facilitating all of these services), the privacy provisions found in Title V of the Act could theoretically be stretched to cover some activities of virtually every business in the country that supplies products or services to consumers.

The FTC's proposed rules adopt the broad outlines of the definition of "financial institution" used in the Act. The FTC has proposed a limitation of the new rules to entities that are "significantly engaged" in a financial activity. The Commission has invited comments as to whether and how "significantly engaged" should be defined. More generally, the FTC has invited comments on the application of its proposed rules to nontraditional financial institutions. ITI discusses these two issues below.

II. NECESSARY REVISIONS

A. "Financial Institutions" Should Not Include Referring Entities

In its commentary, the FTC has provided the following helpful example: "a department store that issues its own credit card directly to consumers provides a financial service (credit) to consumers who utilize the card, but when it sells merchandise, it provides a nonfinancial product or service."[2] This is the right approach to the definition of "financial institutions." A retailer

[2] NPRM at 8.

selling merchandise is not a financial institution with respect to that merchandise -- because no traditional banking, insurance, or securities goods or services are being provided by the retailer.

But the commentary also includes the following contradictory statement in connection with "customer relationships": customer relationships would include "cases where an institution opens a credit account for the consumer, a loan broker undertakes to assist a consumer to obtain a home mortgage, **or an automobile dealer helps a consumer arrange credit to purchase a vehicle.**"[3] (Emphasis supplied.) Thus, in the course of providing a nonfinancial product or service (a car) to a customer, an institution that "helps" a consumer arrange credit (like a car dealer) appears to be a "financial institution" in the eyes of the FTC.

This statement creates many questions for retailers. If a retailer has credit card applications sitting on its counters, is it "helping" consumers arrange credit? If a retailer tells consumers it prefers a certain credit card, is it "helping" consumers arrange credit? If a retailer refers consumers to an entity that will loan the consumer money to buy a product, is it a "financial institution"? If it contracts with a bank to offer private label credit card services, is the non-bank retailer itself now a "financial institution"? Does it matter whether the bank is affiliated with the retailer or is wholly independent?

The FTC has more work to do with respect to the definition of "financial institution." The FTC should clarify that mere recommendation or referral does not constitute a "financial activity." The FTC should also clarify that the mere forwarding of consumer financial information to a financial institution does not render the forwarder a financial institution. There may also be a need to clarify that a retailer's mere affiliation with a traditional financial services company does not obligate that retailer to provide the required disclosures under the Act. (Just as an agent of a creditor does not become a consumer reporting agency under FCRA by gathering consumer information for that creditor, a retailer should not be subject to the Act's strictures if it merely gathers information for forwarding to an affiliate.) As long as the entity extending credit (or providing other traditional banking, security, or insurance goods or services) provides the disclosures and choice-related notices required by the Act, the privacy of the consumer to which the Act is directed will be protected.[4] There is no need for the consumer to be the recipient of duplicative disclosures from each entity along the chain leading to the provider of financial products or services.

ITI respectfully requests that the FTC issue amended regulations that more clearly define the scope of business relationships between consumers and retailers that trigger the Act's obligations. Retailers that merely forward or refer consumers (or consumer financial information) to entities providing traditional financial products or services should not be captured within the definition of "financial institutions."[5]

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[3] Id. at 6.

[4] If the FTC is concerned that access by the retailer to personally identifiable consumer financial information that the retailer gathers as agent may undermine the privacy policies of the covered provider of financial services, it could mandate that any financial institution that uses agents in this fashion require, by contract, that such agents adhere to the financial institution's privacy policies.

[5] To the extent a software or hardware company is itself providing traditional financial services, and is therefore subject to Title V's requirements, ITI suggests that the FTC's proposals with respect to the definition of "customer relationship" will require further work. In light of the accelerated nature of ecommerce interactions, imposition of

B. "Financial Institutions" Should Not Include All Hardware and Software Companies

The day after the FTC released its proposed regulations under the Act, The Wall Street Journal ran an article about the proposals bearing the following headline:

> Hardware, Software Firms May Face Proposed FTC Consumer-Privacy Rules.[6]

The article included the following sentence:

> The agency outlined proposed consumer-privacy rules that could affect a broad range of companies performing financial services that aren't normally considered to be financial institutions, such as Dell Computer Corp. and Gateway Inc., which sell directly to consumers and finance purchases.

The Journal was looking for a headline that captured the striking breadth of the proposed regulations, and found it in the definition of "financial institutions" on which the FTC has asked for comments. But the headline of the article, and the sentence quoted above, are not necessarily accurate. ITI respectfully requests that the FTC clarify that not all hardware and software companies are necessarily "financial institutions" under its proposed regulations. ITI also suggests that the structure and purpose of the Act mandate that, in general, the definition of "financial institutions" obliged to provide the notices required by Title V be interpreted narrowly.

1. The Structure of the Act Mandates a Narrow Interpretation of "Financial Institutions" for Purposes of Title V's Requirements

As outlined above, the Act states that financial holding companies *may* engage in any activity that the Board finds to be "financial in nature." The Act goes on to state that activities financial in nature include "engaging in any activity that the Board has determined, by order or regulation that is in effect on the date of the enactment of the Gramm-Leach-Bliley Act, to be so closely related to banking or managing or controlling banks as to be a proper incident thereto (subject to the same terms and conditions contained in such order or regulation, unless modified by the Board)." 12 U.S.C. 1843(k)(1) and 1843(k)(4)(F). This is a *permission-granting* definition; it allows traditional financial institutions to expand into additional, "closely-related" areas.

Title V of the Act (the privacy section) then incorporates by reference the broad and permission-granting definition of financial institutions found in the Bank Holding Act into the privacy *requirements* of the Act.[7] This simple use of a handy cross-reference should not be applied mechanically. Instead, the scope of each portion of the Act should be interpreted

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complicated periodic notice requirements based on (for example) the mere opening of a single credit account by a consumer, or a single "understanding" under which the institution will "arrange" credit (even if the credit is not granted), may be inappropriate. In order for a continuing customer relationship to exist, ITI believes an ongoing pattern of repeated financial interactions should be required. We suggest that the FTC amend the definition of "customer" to encompass only consumers who regularly effect financial transactions with the institution in question.

[6] Michael Schroeder, The Wall Street Journal, Feb. 25, 2000 at C18.

[7] Act, Section 509(3).

thoughtfully in light of the structural mandates of the Act and the purposes underlying the quite different regulatory regimes being created.

As outlined above, the Act sets forth a quid pro quo: traditional financial institutions are given *permission* to expand into other business areas (as long as they are closely related to traditional financial activities). In exchange, such institutions (to the extent they are providing core financial activities) will have to comply with certain notice and disclosure requirements. The first part of the Act, thus, sets forth the "benefit" -- "you" (institutions providing traditional financial goods and services) can participate in other businesses. Subpart A of Title V then sets forth the "burden" -- "you" (entities providing traditional financial goods and services) have privacy obligations. "You" ("financial institutions") means, in the context of the Act's structure, core traditional financial institutions (or institutions providing traditional financial goods and services) that may supplement their financial services with permissible, inextricably intertwined additional activities. The Act was not intended to impose privacy burdens on entities that are not themselves providing traditional financial goods and services.

"Financial institutions" means, in this context, entities that are providing traditional financial goods and services and are using nonpublic personal information of consumers in order to provide those consumers with financial goods and services. The FTC should make clear that Section 509(3) should not be uprooted from the overall structure of the Act. That structure mandates that the group provided with the benefit should match the group on which the burden is imposed. In light of this structure, it makes no sense to impose these burdens on institutions that *happen* to be selling some of the ancillary, non-financial goods and services traditional financial institutions are being given permission to provide (but which are not themselves providing traditional financial goods and services). This narrow reading is clear and logical, serves the purposes of the Act, and will avoid the turmoil, sensationalism, and unpredictability sensed by the Journal reporter.[8]

2. In Light of this Narrow Interpretation, the FTC Should Clarify That Not All Providers of Ancillary Services are "Financial Institutions" Subject to Title V

In its commentary, the FTC has noted that section 509(3) of the Act defines "financial activities" to include activities found by the Federal Reserve Board to be closely related to banking. These activities include "providing financial data processing and transmission services,

[8] Another structural argument drawn from Title V mandates a narrow interpretation of the definition of "financial institution": Section 527, which proscribes fraudulent access to consumer financial information, defines the term entirely differently. Under that section, "financial institutions" are defined as "any institution engaged in the business of providing financial services to customers who maintain a credit, deposit, trust, or other financial account or relationship with the institution." In the context of Subpart B of Title V, which applies to everyone who tries to unlawfully obtain nonpublic consumer information from a financial institution, the definition of "financial institution" is not a *permission granting* definition. Instead, it is a narrower definition that more closely approximates what most people think of as traditional financial institutions (and does not include, for example, courier services, travel agencies, and hardware and software companies). This narrower definition -- one that does not match the scope of the "benefit" provided in the first section of the Act -- shows what Congress understood to be the realistic scope of financial institutions outside the context of the quid pro quo structure of the Act. By its mere presence, it reflects that Congress was quite aware that a "benefit and burden" deal was being struck by the Act -- a deal the FTC should keep in mind when deciding who should be the subjects of the "burden."

facilities (including hardware, software, documentation or operating personnel), data bases, advice, or access to these by technological means." They also include operating a travel agency "in connection with financial services . . . " and "courier services for banking instruments."

In light of the structural mandates of the Act described above, this set of definitions should be read narrowly. Again, these ancillary services have to be provided by entities that are themselves providing traditional banking, securities, or insurance goods and services (the beneficiaries of the "benefit" provided for in the Act) in order to qualify as financial activities. They are additional goods and services that are inextricably intertwined with the entity's basic financial goods and services. These definitional phrases should not be separated from the overall entity-based structure of the Act by being read to apply to entities that are not helped by the "benefit."

Any other reading would defeat the purposes of the Act and defy reality. After all, as the FTC hints, <u>every</u> travel agency that has a corporate account from a bank is potentially operated "in connection with financial services."[9] Every computer hardware manufacturer, knowingly or not, provides "facilities" in connection with financial services. Every software licensor provides financial data processing and transmission services. Every web site that facilitates or provides credit card processing provides "access" to financial facilities by technological means. Every switch and router in the internet provides "access" to financial facilities and data processing. The wheels of ecommerce would grind to a halt if each entity falling within these definitions had to provide disclosures to the consumers whose nonpublic information was passing across their screens or over their wires.

As the plain language of the Board's definitions suggest, the FTC should clarify that only providers of software and hardware products and services that are <u>ancillary to</u> and <u>inextricably intertwined with</u> financial products and services provided to consumers by <u>those same entities</u> should be subject to Title V's privacy requirements.

The FTC should also clarify that third-party information technology companies that furnish services to providers of traditional financial products are not necessarily swept within the definition of "financial institution." For example, when an <u>independent contractor</u> software provider sets up a system for a bank, that service provider may be exposed to consumer financial information. The service provider, however, will not retain this information (although it may need to see it in order to perform its functions), and will be bound by confidentiality agreements with the bank. Mere exposure to personally-identifiable consumer financial information should not trigger Title V's burdens.

C. The FTC's "Significantly Engaged" Limitation Does Not Go Far Enough to Limit the Potential Applicability of Its Proposed Regulations.

The FTC has made a significant effort to remedy the potential overbreadth of its regulations. The Commission views an entity as a financial institution "only if it is significantly

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[9] <u>See</u> n.4 (requesting comment as to how "in connection with financial services" limits the activity of operating a travel agency).

engaged in a financial activity."[10] In providing an example of what "significantly engaged" may mean, the Commission states: "Thus, a retail business that issues its own credit card directly to consumers is a financial institution engaged in the extension of credit, but a retail business that merely establishes lay-away or deferred payment plans is not a financial institution."[11] Additionally, the FTC 's commentary contains the following statement: "The effect of this ["significantly engaged"] definition is twofold: it encompasses and subjects to its requirements those institutions that are not solely in the business of a financial activity but that are significantly engaged in such an activity as part of their business; and excludes from coverage those entities, large or small, that may engage in financial activities as some small, insignificant portion of their business."[12]

This suggested dichotomy between a retailer offering a credit card (covered) and one offering a deferred payment plan (not covered) is wholly opaque and unexplained. Nor is the largely unexplained concept of "significantly engaged" helpful in providing practical guidance about the scope of the regulation.

To clarify these issues, ITI respectfully suggests that the Commission add examples or safe harbors that use the "significantly engaged" concept to explicitly exempt from the scope of its regulations the following activities:

- the acceptance of payment for goods and services on a deferred basis under applicable law, even if interest or finance charges are collected;
- sale of goods and services under a revolving credit plan, as long as no one other than the seller is permitted to honor any card issued under the plan or otherwise access the plan;
- honoring credit and charge cards issued by other entities, whether or not those entities are affiliated by contract or common corporate ownership.

These limitations should also include examples of the actions an entity can take in communicating with consumers that do not trigger the obligations of the Act: referring consumers to a credit-granting entity; forwarding data as an agent of a traditional financial institution, assisting consumers in finding traditional providers of financial services; recommending particular vendors of financial services; providing advice about different financial services in which the consumer may be interested, etc. As long as the entity providing financial goods and services to the consumer makes the disclosures and provides the notices required by the Act (and the intermediary entity either does not retain nonpublic consumer financial data provided by the consumer in connection with his/her request for financial goods and services or complies with the disclosed privacy restrictions applicable to that data), the purposes of the Act will be served.

Unless its regulations are explicitly limited in this fashion, the FTC will, in effect, be requiring virtually every retail seller, including millions of small businesses, to create and bombard consumers with privacy disclosures covering the routine, everyday interactions every American has with all the entities that provide goods and services in exchange for payment of an

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[10] NPRM at 7.
[11] Id.
[12] Id. at 28.

agreed-on price at an agreed-on time and place. In passing the Act, Congress never intended to impose such a far-reaching regulatory regime on non-financial businesses.

ITI appreciates the opportunity to comment in this proceeding. We look forward to working with the Commission as it refines the definitions set forth in its proposed regulations in light of the structure and purpose of the Act as a whole.

Respectfully submitted,

Rhett Dawson
President