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Best practices - Proposed Red Flags rule

by Gil Van Over

This year's columns have been dedicated to describing this whole thing called compliance. We are now in the process of describing best practices that, if implemented, are designed to help reduce exposure to litigation and regulatory inquiries. Today's topic is proposed regulation called the Red Flags Rule.

Federal Requirement

The Red Flags Rule is not yet implemented, but the regulators are at it again. They're ready to implement the Red Flags Rule, which aims to help stem the tide of identity theft and is as a result of the FACT Act passed in 2005.

Under the proposed rule, a dealership must implement six essential components:

- Assign a compliance officer
- Conduct a risk assessment
- Develop a policy and procedure manual
- Provide employee training
- Conduct periodic audits

Submit annual written reports on program's sufficiency to dealership's owner(s)

The regulators are serious about implementing this rule. Some estimates peg the percentage of American affected by identity theft at close to 25%.

I believe the only people who would disagree with eradicating identity theft are the thieves themselves. These people are a bold group and they get bolder when they realize that many victims are hesitant to press charges.

That being said, the proposed rules for dealers to follow to assist in the identity theft are either common sense and things prudent dealers are already doing, or seemingly onerous.

Onerous Proposed Red Flag Definitions

How onerous? Contemplate running every single customer against a list of over thirty potential red flags before being able to deliver a car in order to be compliant with the proposed rule.

Here are a few of the proposed Red Flags:

The address, social security number or home or cell phone is the same as that submitted by other applicants. Presumably, this would require the F&I or Sales Manager to ping every customer's information against the dealer's database to make sure this information was not provided to the dealer by any other applicant.

Personal information provided is not consistent with information that is on file. Sounds like the Manager would have to compare the credit application and identifying information with the same information submitted by the customer in past transactions.

Personal information is associated with known fraudulent activity or is of a type commonly

associated with fraudulent activity. Good luck in keeping up with knowing fraudulent activity or types commonly associated with fraudulent activity. Better luck in catching an identity thief with this red flag.

The photo or physical identification is inconsistent with the appearance of the applicant or customer. Based on the poor quality of some of the photocopies of driver's licensed in files, this red flag could easily trip up some dealers for non-compliance unless the dealer invests in a new copier or one of those new scanning systems.

A consumer report indicates a pattern of activity that is inconsistent with the history and usual pattern of activity of an applicant or customer. Some dealers have a hard time getting Sales and F&I Managers to look past the bureau score on a credit report. Now the Manager will have to analyze the report for recent, significant increases in inquiries, an unusual number of recently established credit relationships, or an account that was closed for cause or identified for abuse of account privileges by a creditor.

As long as dealers continue to spot deliver cars, it will be difficult for a dealer to lean on the banks and finance companies for help with the proposed Red Flag Rule as the customer and the car will be gone before the application is submitted to the bank.

Dealer's Requirement

Start getting prepared for the upcoming implementation of the Rule. Five of the six required components of the Red Flags Rule are identical to your requirements under the Safeguards Rule. The sixth component, submitting an annual written report to the owner of the dealership, is an added wrinkle that you will have to add to your other annual reporting requirements.

We should all exercise a reasonable standard of care to help slow down identity theft. Some dealers have reported positive results by obtaining thumb prints of all customers or by implementing a video recording system. Both ideas have reportedly scared off some potential identity thieves.

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