

April 7, 2006

MEMORANDUM TO: The Board of Directors

FROM: Sandra L. Thompson
Acting Director
Division of Supervision and
Consumer Protection

Douglas H. Jones
Acting General Counsel

SUBJECT: Interagency Notice of Proposed Rulemaking Regarding Identity
Theft Red Flags and Address Discrepancies under Sections 114
and 315 of the FACT Act

RECOMMENDATION:

We recommend that the Board of Directors (Board) of the Federal Deposit Insurance Corporation (FDIC) authorize the Executive Secretary to publish in the *Federal Register* a notice of proposed rulemaking (NPR) jointly with the Board of Governors of the Federal Reserve System (FRB), the Office of the Comptroller of the Currency (OCC), the Office of Thrift Supervision (OTS), the National Credit Union Administration (NCUA), and the Federal Trade Commission (FTC) (collectively, the “Agencies”).

The NPR would establish: (a) interagency guidelines for financial institutions and creditors identifying patterns, practices, and specific forms of activity, that indicate the possible existence of identity theft; (b) interagency regulations requiring each financial institution and creditor to establish reasonable policies and procedures for implementing the guidelines, including, where applicable, a provision requiring credit and debit card issuers to assess the validity of a request for a change of address under certain circumstances; and (c) interagency regulations that provide guidance regarding reasonable policies and procedures that a user of consumer reports should employ upon receiving a notice of address discrepancy from a consumer reporting agency.

We also recommend that the Board authorize the Executive Secretary and the General Counsel to make technical, nonsubstantive, or conforming changes to the text of the NPR where necessary to ensure that the Agencies can jointly publish the NPR, and to take such other actions and issue such other documents as they deem necessary or appropriate to fulfill the Board’s objectives.

DISCUSSION:

1. Background. The proposed guidelines and regulations are required by sections 114 and 315 of the Fair and Accurate Credit Transactions Act of 2003 (FACT Act). Section 114 of the FACT Act requires the Agencies to jointly issue guidelines for use by financial institutions and creditors regarding identity theft. In developing the guidelines, the Agencies must identify patterns,

practices, and specific forms of activity that indicate the possible existence of identity theft, and they must consider requiring financial institutions and creditors to follow reasonable policies and procedures that provide for notice to a consumer when a transaction occurs with an inactive account. In addition to the guidelines themselves, the Agencies must issue regulations requiring financial institutions and creditors to establish reasonable policies and procedures for implementing the guidelines. The Agencies also must issue regulations requiring credit and debit card issuers to assess the validity of change of address requests. (The guidelines and regulations required by section 114 of the FACT Act are referred to collectively as the Red Flag Regulations.)

Section 315 of the FACT Act requires the Agencies to issue regulations providing guidance regarding policies and procedures that users of consumer reports shall use when they receive notice from a consumer reporting agency of a substantial difference between the consumer address used to request the consumer report and the address for that consumer in the consumer reporting agency's file.

2. Red Flag Regulations. The proposed Red Flag Regulations adopt a flexible risk-based approach similar to the approach used in the *Interagency Guidelines Establishing Information Security Standards* (Information Security Standards) issued by the federal banking agencies (FDIC, FRB, OCC and OTS), and the *Standards for Safeguarding Customer Information* issued by the FTC, to implement section 501(b) of the Gramm-Leach-Bliley Act. (The FDIC's Information Security Standards, for insured state non-member banks, insured state licensed branches of foreign banks, and the subsidiaries of such entities, are set forth at 12 C.F.R. Part 364, Appendix B. The proposed Red Flag Regulations, which would apply to the same entities, would be codified in 12 C.F.R. Part 334 and cross-referenced in Part 364.)

Under the proposed Red Flag Regulations, financial institutions and creditors must have a written Identity Theft Prevention Program (Identity Theft Program) that is based upon the risk assessment of the financial institution or creditor and that includes controls to address the risks identified. As with the program described in the Information Security Standards, the Identity Theft Program must be appropriate to the size and complexity of the institution and the nature and scope of its activities, and be flexible enough to address changing identity theft risks as they arise.

The appendix to the proposed Red Flag Regulations lists various patterns, practices, and specific activities that indicate a possible risk of identity theft (Red Flags). (These Red Flags would be set forth in a new Appendix J of Part 334.) The Identity Theft Program must take into account those Red Flags as well as other Red Flags that are based on applicable supervisory guidance, methods of identity theft that the financial institution or creditor has experienced, and other methods of identity theft the financial institution or creditor has identified that reflect changes in identity theft risk. Some institutions and creditors may wish to combine their programs to prevent identity theft with their information security programs, as these programs are complementary in many ways.

Under the proposed Red Flag Regulations, the Identity Theft Program of each financial institution or creditor must be designed to address the risk of identity theft to customers and the

safety and soundness of the financial institution or creditor. The Identity Theft Program must include policies and procedures to prevent identity theft from occurring, including policies and procedures to:

- Verify the identity of persons opening accounts;
- Identify those Red Flags that are relevant to detecting a possible risk of identity theft to customers or to the safety and soundness of the financial institution or creditor;
- Detect the Red Flags that the financial institution or creditor identifies as relevant;
- Assess whether the Red Flags detected evidence a risk of identity theft;
- Mitigate the risk of identity theft, commensurate with the degree of risk posed;
- Train staff to implement the Identity Theft Program; and
- Oversee service provider arrangements.

The proposed Red Flag Regulations also require the board of directors or an appropriate committee of the board to approve the Identity Theft Program. In addition, the board, an appropriate committee of the board, or senior management must exercise oversight over its implementation. Staff implementing the Identity Theft Program must report to their board, an appropriate committee, or senior management, at least annually, on compliance by the financial institution or creditor with the Red Flag Regulations.

Finally, the proposed Red Flag Regulations provide that a credit or debit card issuer who receives notification of a change of address for an account, and within a short period of time afterwards (during at least the first 30 days after it receives such notification) receives a request for an additional or replacement card for the same account, may not honor the request and issue such a card, unless it assesses the validity of the change of address request in at least one of three ways:

1. Notifying the cardholder of the request at the cardholder's former address and provide to the cardholder a means of promptly reporting incorrect address changes;
2. Notifying the cardholder of the request by any other means of communication that the card issuer and the cardholder have previously agreed to use; or
3. Using other means of assessing the validity of the change of address, in accordance with the policies and procedures that the card issuer has established pursuant to the Red Flag Regulations.

3. Address Discrepancy Regulations. Section 315 of the FACT Act requires that a nationwide consumer reporting agency (CRA), when providing consumer reports to a requesting user, must notify the requesting user of the existence of a discrepancy if the address provided by the user in its request "substantially differs" from the address the consumer reporting agency has in the consumer's file. Section 315 also requires the Agencies to jointly issue regulations that provide guidance regarding reasonable policies and procedures that a user of a consumer report should employ when the user receives a notice of address discrepancy. These regulations must describe reasonable policies and procedures for users of consumer reports to (a) enable them to form a reasonable belief that the user knows the identity of the person for whom it has obtained a consumer report, and (b) reconcile the address of the consumer with the CRA, if the user establishes a continuing relationship with the consumer and regularly and in the ordinary course

of business furnishes information to the CRA. The proposed regulations implement these requirements of section 315 and would be codified in Part 334.

4. *Current Status of NPR.* The NPR will be published in the Federal Register shortly after all of the Agencies have approved it.

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Attachment

RESOLUTION

WHEREAS, section 114 of the Fair and Accurate Credit Transactions Act of 2003 (the “FACT Act”), Pub. L. No. 108-159, 117 Stat. 1952, requires the Federal Deposit Insurance Corporation (“FDIC” of “Corporation”), the Board of Governors of the Federal Reserve System, the Office of the Comptroller of the Currency, the Office of Thrift Supervision, the National Credit Union Administration, and the Federal Trade Commission (the “Agencies”) to jointly issue regulations and guidelines for use by financial institutions and creditors regarding identity theft; and

WHEREAS, section 315 of the FACT Act requires the Agencies to issue regulations providing guidance regarding policies and procedures that users of consumer reports shall use when they receive notice from a consumer reporting agency of a substantial difference between the consumer address used to request the consumer report and the address for that consumer in the consumer reporting agency’s file.

NOW, THEREFORE, BE IT RESOLVED, that the Board of Directors (“Board”) of the FDIC hereby authorizes the Executive Secretary, or his designee, to publish in the *Federal Register*, in a form and manner acceptable to the Executive Secretary, or his designee, and the General Counsel, or his designee, and jointly with the other Agencies, a notice of proposed rulemaking entitled “Identity Theft Red Flags and Address Discrepancies under the Fair and Accurate Credit Transactions Act of 2003,” as set forth in the attached draft *Federal Register* notice document.

BE IT FURTHER RESOLVED, that the Board hereby delegates authority to the Executive Secretary, or his designee, and the General Counsel, or his designee, to make technical, nonsubstantive, or conforming changes to the text of the *Federal Register* notice

document where necessary to ensure that the Corporation and the other Agencies can issue this document jointly in the *Federal Register* and to take such other actions and issue such other documents incident and related to the foregoing as they deem necessary or appropriate to fulfill the Board's objective in connection with this matter.