

September 18, 2006

Federal Deposit Insurance Corp
Legal Division
Legal Information Technology Unit
550 17th St. NW
Washington, DC 20429-9990

Re: Joint proposal rulemaking
Implementation of Sections 114 and 315
of the FACT Act
Identity Theft Red Flag guidelines
OCC Docket No. 06-07; FRB Docket No. R-1255; FDIC RIN 3064-AD00; OTS No. 2006-19;
NCUA (No Docket Number); FTC RIN 3084-AA94
71 *Federal Register* 40786, 18 July 2006

To Whom It May Concern:

Washington Trust Bank respectfully submits its comments to the Federal Deposit Insurance Corporation on the proposed regulations related to implementation of Sections 114 and 315 of the Fair and Accurate Credit Transactions Act of 2003 ("FACT Act"). As required by Section 114, the Agencies are jointly proposing guidelines for financial institutions and creditors identifying patterns, practices, and specific forms of activity that indicate the possible existence of identity theft. In addition, the proposal includes a provision requiring credit and debit card issuers to assess the validity of a request of a change of address under certain circumstances and a provision related to procedures users of consumer reports must employ when they receive a notice of address discrepancy from a consumer reporting agency.

Summary of Comments.

Washington Trust Bank, as other similarly situated commercial banks, has a long history of combating financial fraud, to include variations of identity theft. This experience teaches us that we must have broad flexibility to develop and implement appropriate controls to respond effectively to evolving financial crime threats faced by our banks. While the Agencies state that the proposed Regulation is intended to be flexible and reflect a risk-based approach, we conclude that the proposed regulatory language in many cases falls short of these stated intentions. Instead, we believe that the proposal runs a high risk of creating an artificial, stagnant, mandatory checklist regime that will not effectively advance the goals of detecting and preventing identity theft and fraud. We fear that unless these shortcomings are addressed, the result will be a diversion of resources from effective detection, investigation, and corrective action and instead will necessitate wasteful expenditure on burdensome, paperwork-laden compliance exercises. Bankers' attention will be drawn into wasteful but obligatory drills to justify each judgment call made under a good faith effort to defeat identity thieves and fraudsters.

For these reasons, we strongly recommend that the agencies substantially simplify the final Regulation and re-cast it to meet the following principles to apply necessary flexibility in the common effort to fight identity theft and fraud:

- Regulate by objective, **not** prescription,
- Take advantage of synergies with existing regulatory standards and operational efficiencies,
- Avoid requirements not mandated by the statute,
- Keep compliance simple, and
- Recognize that *risk-based* considerations work best as guidance and allow for appropriate judgment, rather than rely on fixed rules.

Washington Trust would appreciate your consideration of the following comments:

Regulate by objective, not prescription.

Flexibility to combat identity theft is critical because of the changing nature of fraud practices. Fraud and fraudsters are dynamic, constantly altering methods and targets, as must be the fraud detection techniques and solutions. Fraudsters are continually seeking to detect any vulnerability to exploit and when they encounter an obstacle, they search for a way around it.

Similarly, we can expect the proposed Red Flags to become less effective with time. The identity thieves will find a way around obstacles once they are identified. The mere notoriety of a red flag is a major step towards its obsolescence as a reliable detector. The proposed rule indicates financial institutions “must have a reasonable basis for concluding that a Red Flag does not evidence a risk of identity theft. . .” Most financial institutions would be fearful not to adopt one of the Red Flags from these lists set out in the regulation because of the requirement to “justify” any exceptions to the recommended list. By insisting on this static, one-size-fits-all-or-tell-us-why standard, the proposed rule converts the Red Flags into a regulatory checklist of mandates regardless of their current effectiveness as fraud detectors.

We believe that this approach misses the purpose of the statutory Red Flag provision, which was to merge the strengths of regulators and financial firms to fight fraud more effectively.

We recommend that the Agencies adopt similar language in the Red Flag regulation, which will allow financial institutions the discretion and flexibility necessary to have up-to-date effective programs that best fit the needs of their customers and their activities.

Take advantage of existing synergies.

The proposed regulation pursues the goal of taking advantage of synergies with existing regulatory standards and operating efficiencies in two noticeable ways that Washington Trust Bank supports.

First, the Supplementary Information suggests that a financial institution may wish to combine its program to prevent identity theft with its information security program, “as these programs are complementary in many ways.”

Second, the proposed regulation implements the statutory directive of conforming to the existing Customer Identification Program (CIP) requirements by stating that banks in compliance with the CIP rules satisfy the proposed Regulation’s requirement “to obtain identifying information about, and verify the identity of, a person opening an account.”

Washington Trust Bank supports both of these policy positions and encourages the Agencies to recognize that financial institutions have other existing fraud prevention, suspicious activity detection, and security risk management practices and procedures that play a valuable role in detecting, preventing, and mitigating identity theft. To realize the synergies of these existing efforts, the Agencies and their examiners should not expect the Identity Theft Program to be represented as a written document separate and apart from a financial institution's overall financial crime risk management processes as long as such over-arching programs contain the elements appropriate for detecting, preventing and mitigating identity theft.

Avoid requirements not mandated by the statute.

Washington Trust Bank believes that the proposed regulation unnecessarily insists on requirements not mandated by statute. These requirements limit flexibility, impose undue costs, and get in the way of effective identity theft and fraud prevention.

Among the non-mandated regulatory requirements are the following:

- A definition of "account" that overreaches in scope
- A written Identity Theft Prevention Program
- A specified obligation for boards of directors that is cumbersome, at best

The definition of "account" should not be expanded to cover business purpose credit or services.

While the statute calls for reasonable procedures for implementing Red Flag guidelines, it does not demand the formality imposed by requiring a separate, specific, written Identity Theft Prevention Program. As previously noted, identity theft prevention is an initiative seamlessly integrated in institutions' financial fraud and crime risk management processes.

Board awareness is important but the level of board involvement required in the regulation would be extremely burdensome. Requiring board approval of a Program hinders change, which is critical when addressing fraud.

Keep compliance simple.

As proposed, the regulation erects a number of burdensome compliance exercises that limit flexibility and add costs, which in turn divert resources from the ultimate objective of combating identity theft. In addition to the non-mandatory elements of the proposed Regulation, the rigidity of the Red Flag implementation process is also packed with unnecessary compliance hurdles.

The proposal assumes that all the Red Flags are relevant to every financial institution and puts the burden on the financial institution to research, analyze, document, and then persuade examiners that a particular Red Flag does not apply to a product. In many cases, it will be self-evident that a Red Flag does not apply, but the financial institution will nevertheless have to justify and document its exclusion.

Moreover, financial institutions will have to incur costs to re-design identity theft and fraud programs into artificial packages in order to fit into the regulatory scheme examiners will expect. In practice, many identity theft and fraud prevention components are integrated throughout the institution, from the teller to the back office, and not neatly set out to conform to the proposed regulatory list.

As prescriptive as the proposed regulation is it invites examiner and internal auditor micro-managing and potentially pointless criticism—not because a bank's program does not detect or prevent identity theft, but because it does not have all the required regulatory paperwork justifying each and every element either contained or not contained in the Program.

The regulations should emphasize risk-based consideration.

Washington Trust Bank endorses true risk-based compliance. There is wide latitude in such an approach for banks to conduct their business. The key to any risk-based approach is the ability to evaluate the likelihood and severity of adverse events and to prioritize one's response in a manner that applies greater resources to the event of greater expected significance and fewer resources to events of lesser significance. In other words, control programs are to be tailored to expected experience.

How financial institutions go about a risk-based approach varies widely, as do the risks themselves and the environments in which they occur, and can be just as successful informally in modest risk circumstances as when formally conducted in diverse, complex operations. Accordingly, the regulation itself should stress the risk-based aspect of Red Flag Programs.

Conclusion.

Bankers have been in the forefront of fighting identity theft.

We strongly advocate simplifying the Regulation and revamping the Red Flag guidelines to put the emphasis where it belongs—on reasonably designed procedures that assist banks in fighting identity theft prevention, rather than on new regulatory programs with extensive compliance documentation that divert resources from the problems we all wish to solve.

We also strongly recommend that an Official Staff Commentary accompany the final Regulation, as is the case with many other regulations. We believe that a Commentary will be critical to financial institutions for implementation of the Regulation as well as for continued compliance. A Commentary will ensure that financial institutions have convenient access, in an understandable format, to important guidance related to the final Regulation. Further, the Agencies will have a mechanism for providing additional guidance as the need arises.

Sincerely,

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