



OVERVIEW

Outfoxing identity thieves

Like it or not, financial institutions must comply with new federal rules designed to thwart fraudsters.

Protecting your identity

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New red flag rules to stem ID theft

By [Steve Santiago](#) • Bankrate.com

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Identity thieves face tough going this year if they think pilfering your personal information will be a stroll through the park. Or at least that's what regulators hope.

This is because the new "red flag rules," aimed to impede identity thieves, are being phased in.

You've never heard of them? Join the crowd.

"There hasn't been a big consumer education push," says Chris Hoofnagle, a senior fellow with the Berkeley Center for Law & Technology in California. "These rules are not well-known, even among consumer advocates."

Hoofnagle says the information is relatively scarce because the rules stem from a 2003 law that took five years to implement.

"There's been a lot of waiting," he says.

The scoop on red flags

- [What are red flag rules?](#)
- [Who do the rules apply to?](#)
- [How will the rules benefit you?](#)
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What are red flag rules?

The red flag rules push financial institutions to make sure that people are who they say they are -- authenticating identities will be the name of the game. Red flag rules stipulate that financial institutions and creditors establish a written identity theft prevention program to "detect, prevent and mitigate identity

theft in connection with the opening of certain accounts or existing accounts," according to a [Federal Trade Commission report](#).

The [rules offer 26 examples](#) of suspicious behavior that financial institutions and creditors can use as red flag guidelines.

The presentation of altered documents, a suspicious address change, a fraud alert on a credit report and other unusual account activities are potential red flags.

The idea is to prompt banks and creditors to go into "authentication mode" and determine whether fraudsters are trying to apply for credit in someone else's

name or hijack someone else's accounts.

The red flag rules stem from the 2003 Fair and Accurate Credit Transactions Act. [Relevant financial institutions](#) have until November 2008 to come into full compliance or be subject to penalties.

Proponents say red flag rules will standardize how credit-issuing entities respond to suspicious activities regarding your accounts.

"These rules for the first time provide a uniform road map for protecting customer information and preventing identity theft," says Sai Huda, CEO of Compliance Coach, a San Diego-based company that provides red flag compliance software.

"Before the rule, there was only an implied obligation on business to protect information," he says.

-- Posted: May 27, 2008

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Hoofnagle says the red flag process is not foolproof. For example, he says that financial institutions need to keep an eye on sales where affiliate marketing agreements come into play. When consumers apply for a credit card or cell phone contract, oftentimes the agreement's privacy policy will provide for the right to share your information with third-party affiliates that sell products. Hoofnagle believes that some commissioned sales people may be highly incentivized to override the red flags.

He is also concerned that some banks may find ways to simply override authentication procedures.

"There has to be some counterweight to that problem," he says.

Heather Grover, a director of product management with Experian's Fraud & Identity Solutions, says that there has to be some balance between the consumer's best interest and an organization's need to keep its defenses opaque to thieves.

"Fraudsters are students of their craft and they'll really game the system as soon as they find the hole," she says.

Who opposes the rules?

The red flag rules give businesses the flexibility to design a program that works best with their respective business model and available resources.

However, some creditors and financial institutions aren't too happy about what they see as the added financial and bureaucratic burden of being forced to comply with the rules.

Some smaller institutions have complained that the red flag rules place an unnecessary financial and operational burden on them that they cannot afford. Many will face the prospect of having to hire a third-party company to ensure red flag rule compliance.

So while financial giants may have a legion of in-house staffers dedicated to fraud prevention, your local community bank may opt to use a third-party vendor to ensure red flag compliance.

The National Automobile Dealers Association, or NADA, says it supports the government's goal of trying to protect consumers from identity theft, but believes the red flag rules will hurt smaller dealers with limited financial resources.

"We anticipate most dealers will find it challenging to develop and implement a comprehensive identity theft program as required by the red flag rules," says Paul Metrey, director of regulatory affairs for NADA.

Metrey says the program will demand significant time and attention from managers and service providers. He says many provisions of the red flag rules have already been addressed in prior laws, like the FTC Safeguards Rule and FTC Privacy Rule.

Not surprisingly, lobbyists for the banking industry also rejected the rules as heavy handed.

The Illinois Bankers Association in a statement to the FDIC called the rules "excessive and overly burdensome."

There may be some reluctance to accept red flag rules as a best-practice measure, Grover says, but adds that many will eventually come around when they see the benefits of protecting their customers, as well as a decrease in fraud losses.

More: Review the list of [red flag triggers](#).

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Now, financial institutions and creditors must update their programs periodically to ensure they reflect changes in risks to protect customers from identity fraud. In other words, the program must remain pliable enough to handle new threats as they emerge.

Who do the rules apply to?

The FTC says that financial institutions and creditors that "offer or maintain covered accounts" must implement a red flag rule program.

So what exactly is a covered account?

"Red flag rules apply to financial institutions and creditors like banks, credit unions, auto dealers, mortgage brokers, utility companies and telecommunications companies," says Pavneet Singh, a Federal Trade Commission spokeswoman.

Compliance Coach's Huda says you don't necessarily have to be an account holder for the rules to apply to you.

Credit reporting agencies are exempt from the red flag rules, but at least one, Experian, is getting involved at some level. Experian hosted a red flag rules Web seminar in February that attracted more than 700 clients.

"We tried to make sure that all our existing and prospective clients understood what these red flag rules meant," says Keir Breitenfeld, a senior product manager with Experian's Fraud & Identity Solutions. "We tried to do that educationally."

How will red flag rules benefit you?

Red flag advocates say that banks and creditors with sloppy fraud prevention programs will eventually be exposed by litigation and negative publicity.

"The public disclosure of identity theft will create more of an onus for these companies to be up to par," says Huda. "At the end of the day, consumers will eventually benefit because of the higher standards."

Hoofnagle says the prospects of the agencies, such as the Federal Trade Commission and the FDIC, enforcing red flag rules combined with possible litigation, "will involve some transparency of procedures."

Another added benefit of the red flag rules is that employees may be more vigilant in spotting identity fraud.

Anita Marchion, assistant vice president of regulatory compliance at Navy Federal Credit Union in Virginia, says the training of new "recruits" has been beefed up to include more focus on identity theft.

She says the nation's largest credit union will be in compliance by the November deadline and that "members should have a comfort level knowing that we are taking extra steps to protect them from identity fraud."

Hoofnagle says he has been pushing for a ratings system for banks like the ones that measure vehicle safety. His 2006 study of ID theft incidents among financial institutions reveals a wide [variance in frequency of customer complaints](#).

"You can go online and look at the crash test of your car and the rollover rating and all this is available to consumers now," he says. "It wasn't available 40 years ago, but I think we will have a similar situation with banks."

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