

# *FSA Response to the Home Office Consultation Paper Concerning Entitlement Cards and Identity Fraud*

*– 31 January 2003*

In our role as an authority with responsibilities in the areas of crime reduction and financial regulation, we consider this to be a very important topic. The availability of a simple and robust method of proving an individual's identity is key to the fight against crime and terrorism and the protection of consumers (by ensuring the integrity of individuals with significant positions in the financial system). It also has a role to play in facilitating access to the financial system for the most disadvantaged in our society. We believe that existing methods of establishing identity are costly and are becoming increasingly unreliable. As a result they risk losing credibility and support both with the financial industry, who are required to verify the identity of those with whom they deal, and their customers, who are expected to prove their identity. So we believe it is very important and probably essential in the medium term, that the government works with all stakeholders to develop a simple, single and reliable means by which individuals can verify their identity.

## **Our role**

The FSA is the UK's financial regulator, responsible now for the regulation of around 11,500 firms and 180,000 approved individuals. (In 2004 we shall become responsible for many more firms and individuals when our remit is extended to general insurance and mortgage intermediaries.)

The Financial Services and Markets Act 2000 requires us to pursue four statutory objectives: to maintain market confidence; to promote public understanding of the financial system; to secure appropriate consumer protection; and to reduce financial crime. We must also take into account the principles of good regulation, which require

us amongst other things to consider the international character of financial services and the UK's competitive position.

Additionally, the Act gives us a range of enforcement powers, both criminal and civil. These include powers to ensure that the firms we regulate comply with the Money Laundering Regulations 1993, which form part of the UK's criminal legislation, and our Money Laundering Sourcebook, which contains regulatory rules made by us.

## **Our financial crime objective and the UK's anti-money laundering regime**

We have been given the specific objective to reduce the scope for financial crime in relation to the firms we regulate, in particular to reduce money laundering, market abuse, and offences involving fraud and dishonesty. We have the powers to make requirements about firms' systems and controls in relation to money laundering, to monitor firms' compliance with those requirements and to take action against firms if their systems and controls fail.

The EU Money Laundering Directive, which has been implemented in the UK, by way of the Money Laundering Regulations 1993, requires firms to have systems and controls to reduce the scope for money laundering and terrorist financing. In turn we have issued a Money Laundering Sourcebook, which forms part of our Handbook of Rules and Guidance. This imposes a regulatory requirement on all firms, to identify their customers and mirrors the provisions of the Money Laundering Regulations. In line with government policy, we have made clear that we expect all financial firms to have strong and effective anti-money laundering procedures in place. We are prepared to use our enforcement powers and have recently fined a major firm for inadequacies in their anti-money laundering processes.

Additionally, an industry body called The Joint Money Laundering Steering Group produces Guidance Notes (the Guidance Notes), which give detailed guidance on good practice in confirming customers' identity, including listing the documents which provide best authentication of a customer's identity and address. The Sourcebook provides that the FSA will consider the firm's compliance with the Guidance Notes in assessing its compliance with its legal duty to identify a customer.

It is a standard feature of international anti-money laundering law and standards (including the relevant EU directive) that financial firms should verify the identity of their customers. Accordingly, both the Money Laundering Regulations and the FSA Sourcebook make clear that firms must not carry out relevant regulated activities for a customer, or potential customer, unless the firm has taken reasonable steps to confirm that customer's identity. Documents issued by government departments such as passports and driving licences are recommended by the industry's guidance notes as means by which firms can confirm a customer's identity, while recent bank, utility or tax statements are recommended as confirmation of address.

The fact that none of the documents listed in the Guidance Notes were designed to be universal or unique identification documents creates a number of problems. It is costly for firms to train their staff to check a wide variety of different documents and to have procedures in place to deal with exceptional circumstances where a customer cannot reasonably be expected to provide any of these documents. A significant number

of new customers of financial firms cannot provide any of the recommended means of verification (this number will increase substantially as the direct payments of state benefits is rolled out). Most seriously, the reliability of the suggested methods are being increasingly called into question as the reported incidence of counterfeiting standard documents increases.

Provided that the security features incorporated into the entitlement card scheme as well as the checks in relation to the issuing of cards were sufficiently robust, an entitlement card, backed by a population database would be of substantial benefit to the UK's anti-money laundering regime by creating a universal, simple and reliable system for authentication of identity and address.

The Consultation Paper also refers to other ways of reducing identity theft. In that respect:

- We strongly support government efforts to strengthen the underlying checks made before passports and driving licences are issued. Making it harder for criminals to obtain these documents will help to maintain a barrier to entry to the financial industry and prevent financial crime.
- If the results of checks associated with the issuing of more secure passports and driving licences were made available to the private sector on a controlled basis, it would produce significant efficiencies and cost reductions to firms in complying with the anti-money laundering requirements.

## **The competitive position of the UK financial services industry**

We believe that UK financial services firms are at a competitive disadvantage with firms in other jurisdictions, particularly in continental Europe, as a consequence of the UK not having a universal document capable of being relied upon as a sole proof of identity.

At present UK firms incur significant costs as a result of the need to check, copy, and retain copies of a variety of documents in order to comply with the provisions of the anti-money laundering regime. These costs are not incurred by competitors in other EU states who are able to rely on a single universal identification document such as a national identity card.

## **'Fit and Proper' Tests**

Our obligations as regulator include ensuring that individuals who occupy significant positions in firms are 'fit and proper' to carry out those functions. Currently we utilise the services of credit reference agencies in order to verify information about individuals applying to be approved by us. An entitlement card scheme, particularly if it were linked to a population database, could potentially improve the efficiency of our vetting procedures.

What would also be of significant value to us from the perspective of our vetting of individuals is a unique personal number or identifier. On occasions we can encounter problems in verifying an individual's identity, for example where a person has a particularly common name. If we had access to a population database holding core personal information, through which an individual's personal details could be verified by reference to a unique personal identifier, these problems could be alleviated.

## **Consumer protection and financial exclusion**

The section of the population often referred to as the financially or socially excluded includes many of those who are most likely to encounter problems proving their identity and address. Such individuals can have difficulty accessing financial services, as many firms are reluctant to disapply the normal anti-money laundering guidelines even though they have the discretion to do so in exceptional circumstances, and many consumers without conventional forms of identification are reluctant to approach financial services providers in the first place. The introduction of a universal entitlement card scheme would ease the problems faced by this sector by providing a system that enabled all UK residents to provide conclusive authentication of identity. As noted above, this will be an increasingly important issue under the government's direct payment of benefits policies.

## **Consequences of identity theft**

When identity fraud is discovered steps need to be taken to return the victim to the position they were in before the fraud took place. Greater co-operation is needed between law enforcement agencies, financial services firms and credit reference agencies to ensure that there is effective reporting and handling of identity fraud cases, including the swift repair of credit history. It would also be useful to explore whether a revocation or warning list needs to be developed and whether greater use should be made of industry initiatives such as CIFAS when an identity has been compromised.