

Targeting Debit Card Fraud

A Multi-pronged Approach to Educate, Prevent and Detect

By David A. Poe, CEO Edgar, Dunn & Company and
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The mounting awareness of payment-related fraud has consumers worried, legislators galvanized and the media buzzing. Although credit card fraud incidents have declined dramatically due to payment industry efforts, the creativity and resourcefulness of fraudsters has reached new heights as the Internet, globalization, and new forms of currency create unprecedented opportunities for fraud. At risk is the underlying consumer trust that is the foundation of the economy, and the basis of the payment industry's continued growth and success. Preserving and protecting this trust and confidence requires collective, proactive efforts and information to effectively fight fraud and strengthen security across every link in the payments value chain.

A white paper, titled *Payment Fraud: Protecting Your Debit Business*, was developed by the STAR® Network and First Data in partnership with Edgar, Dunn & Company (EDC). The paper draws on our collective in-depth experience and expertise in the areas of fraud and risk management and provides forward-thinking strategies and tactics to help managers protect their debit business. This month's Insight offers a summary of the paper, providing a high level perspective on what financial institutions are facing and outlines a multi-pronged approach to better educate, prevent and detect debit card fraud today and in the future.

Why Target Debit Card Fraud?

While credit cards still experience the highest dollar losses of card fraud, debit card business managers are reporting increased PIN and Signature debit card incidents and losses. It is clear that without adequate control over debit card fraud, the integrity of the core customer relationship product – their checking or current account – could be at risk.


A number of factors are driving the growth in debit card fraud:

- Rapid growth in debit transactions and usage.
- Unlike credit card fraud, few financial institutions have focused on debit card fraud prevention and detection.
- Fraudsters are using advanced technologies to keep pace with leading-edge security tools.
- The global migration to chip cards will likely cause fraudsters and payment fraud to migrate to non-chip products and geographies, such as debit cards in the US.

Understanding Debit Card-Related Fraud

Payment fraud is an increasingly complex topic. To assist in identifying the many points of compromise in a debit business, EDC has identified four areas of focus in developing the Payment Fraud Framework shown in Figure 1-1. This framework shows:

- Methods to Obtain Information: There are a variety of ways to obtain personal consumer information.
- Illegal Use of the Information: Possession of this information can lead to specific types of illegal activities.
- Channels and/or Payment Types: These illegal activities enable fraudsters to use financial institutions' channels and/or payment types.



David A. Poe CEO, Edgar, Dunn & Company

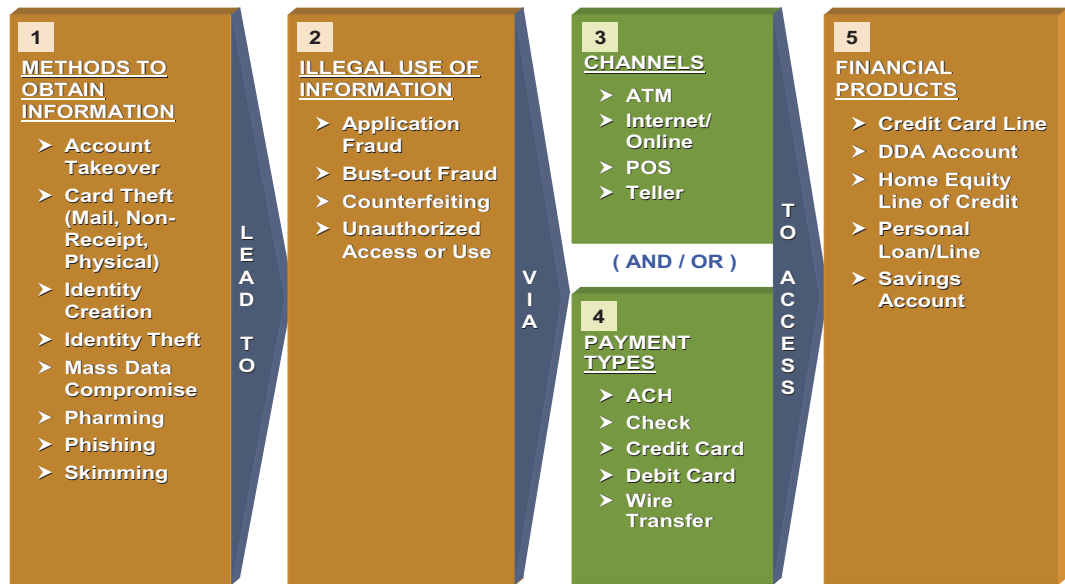
As CEO, Dave has directed the firm's expansion into global markets and practice areas that have made it a world renowned strategy consulting firm in the payments and financial services industry. For over 25 years, Dave has played an advisory role in the major events that have shaped the evolution of the payments industry. His insight and thought leadership continue to help clients throughout the payments value chain win in today's changing market landscape.

Debra A. Janssen President, First Data Debit Services

As president, First Data Debit Services, Debra A. Janssen has overall management responsibility of the division, which includes the STAR® Network, a coast-to-coast electronic payments network and an expert in secure, real-time electronic transactions. Janssen joined First Data in 2004, bringing with her over 20 years of payment leadership experience.

- **Financial Products:** Use of the personal consumer information through various channels and/or payment types allows access to money in the financial products entrusted to financial institutions by their customers.

Figure 1-1 Payment Fraud Framework



Source: Edgar, Dunn & Company

There is no universal solution to combating the dynamic and complex fraud environment. Rather, it takes a mix of preventative and detective measures to control the various aspects of fraud. Every channel and payment type, including debit cards, requires perimeters of defense. Each type of fraud needs to be guarded against. Each financial product needs to be monitored for suspicious activity.

A lack of standardization in fraud definitions, coupled with inadequate reporting tools and policies, makes it difficult to accurately quantify the size of fraud affecting debit businesses today. Among PIN debit, Signature debit, and credit card products, however, the findings from industry interviews and experience reveal that:

- Credit card fraud is the highest in terms of dollar volume, although the rate of credit card fraud (basis points per dollar volume) has been declining. Today, issuer-reported credit card fraud is estimated to be approximately five basis points across the US industry.
- PIN debit card fraud dollar levels are the lowest of the three leading card types, but the rate of increase in incidents and losses related to PIN debit cards have recently been growing.
- Debit-related fraud rates vary widely across the industry, ranging from two to nine basis points.

Strategies for Protecting Your Debit Business

Protecting your debit business from fraud losses involves a multi-pronged approach to educate, prevent, and detect debit card fraud.

Education and Awareness

The first line of defense against attacks on debit card transactions and portfolios is education and awareness. Understanding the types of fraud, how and why crimes can be perpetrated against debit businesses, and the potential impact of such crimes is a very important perimeter of defense. This education and awareness must occur within the financial institution, with consumers, across the payment card industry, and incorporate the global perspective.

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“...PIN is not strong enough to act as a stand-alone defense against all aspects of fraud.”

Prevention

In the past, financial institutions placed more emphasis on recovering losses once they occurred, but today more and more institutions are investing resources in proactive prevention. Today’s proactive institutions have applied three rules:

Prevention Rule #1: Save the Data

To facilitate monitoring, identifying, tracking, and resolving debit card fraud, all relevant information pertaining to the debit card and transactions is retained by the financial institution, including information on each customer, debit card, debit transaction, and fraud case.

Prevention Rule #2: Use Similar Prevention Tools for PIN, Signature and Credit

To prevent fraud in PIN debit portfolios, proactive financial institutions are monitoring these portfolios by using similarly robust tools and procedures that are being applied to Signature debit and credit card portfolios, including:

- Velocity checking and transaction scoring
- Card verification programs
- Address verification services
- Cardholder verification
- Identity authentication and age verification
- Office of Foreign Assets Control (OFAC) database lookup
- PIN offset edits

Prevention Rule #3: Defend on Multiple Fronts

Although PIN is viewed by the industry as a stronger cardholder verification method than signature, it is not strong enough to act as a stand-alone defense against all aspects of fraud. Proactive financial institutions employ multiple approaches to manage fraud and protect their debit business, including:

- Employing multi-factor authentication for online (Internet) purchase transactions including information the cardholder knows, additional information the cardholder has, and data that is available within the financial institution
- Deploying more sophisticated ATMs and testing new security devices on ATMs to protect against skimming
- Subscribing to periodic audits of the financial institution’s fraud and risk management functions to uncover weak links in their policies, processes, tools, and technology

Detection and Resolution

Neural Network

Proactive financial institutions continue to improve their detection capabilities by investing in new technologies and solutions. The most prevalent tool used to detect card-based fraud is a neural network. The neural network relies upon historical purchasing patterns to identify out-of-pattern spending. Since consumers tend to use debit cards in different situations than credit cards, enhancing a neural network to recognize debit-specific patterns is essential when fighting debit-related fraud.

Tagging and Tracking

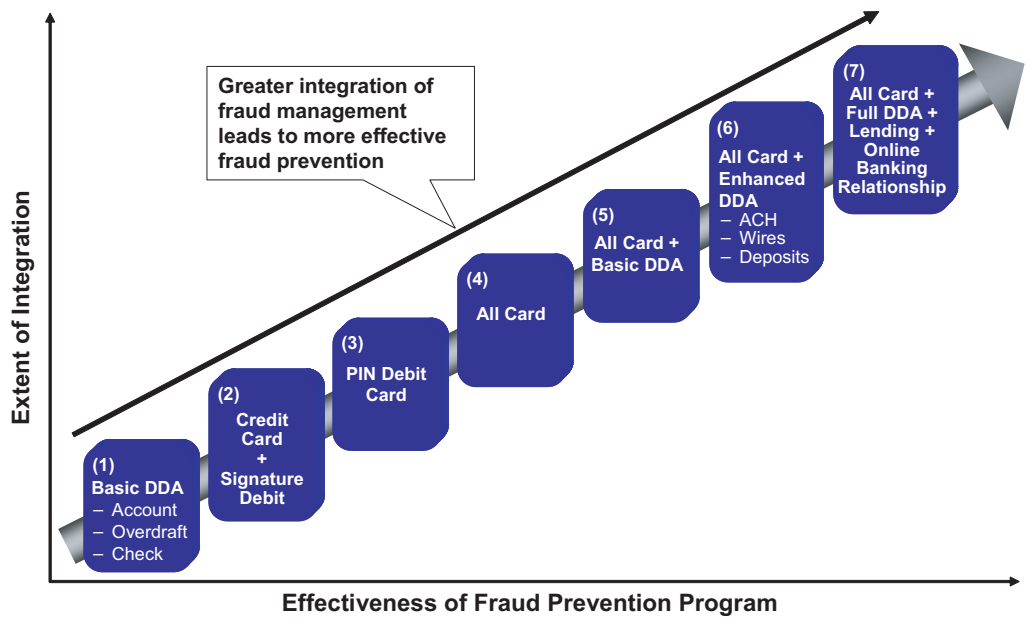
Another critical element of detection and resolution is the need for correct and thorough tagging and tracking of fraud. Knowing which transactions actually resulted in losses, as well as identifying what type of fraud resulted in which losses, provides critical intelligence in detecting the next fraudulent debit transaction.

Future Vision: An Integrated Approach

To augment the education, prevention, and detection strategies and tactics being employed by proactive financial institutions today, financial institutions can move their organization along an ‘evolutionary path’ towards an integrated fraud control approach, as shown below;

“Financial institutions can move their organization along an “evolutionary path” towards an integrated fraud control approach...”

Figure 1-2 Fraud Control Roadmap



Source: Edgar, Dunn, & Company

All aspects of fraud management should be integrated and focused on defending against payment fraud – including the organizations, tools, technologies, and channels. Centralized, shared databases, policies, practices, and experiences will enable more robust fraud mitigation tools to be constructed and deployed.

Financial institutions, payments associations, payment processors, and technology companies all rely heavily on an underlying consumer trust for the continued growth and success of their respective businesses. Further strengthening of the security around your debit business will help to preserve and protect this consumer trust and confidence into the future.

Copies of this paper are available to all STAR® Network members and First Data clients by sending an email to brand.management@star.com.

About Edgar, Dunn & Company

Edgar, Dunn & Company (EDC) is a global strategy consulting firm specializing in payments and financial services. Founded in 1978, the firm is widely regarded as trusted advisors in the payments industry providing a full range of strategy consulting services, expertise and market insight through in-depth industry and consumer benchmarking including its proprietary data intelligence platform, PaymentDynamicsSM. Additional areas of expertise include new financial services channels, technologies and retail financial services. EDC’s offices are located in San Francisco, New York, Atlanta, London, Frankfurt and Sydney and serve clients in over 30 countries on six continents. More information can be found at www.edgardunn.com

About First Data

First Data Corp. (NYSE: FDC) is a leading provider of electronic commerce and payment solutions for businesses and consumers worldwide. Serving 4.1 million merchant locations, 1,500 card issuers and millions of consumers, First Data powers the global economy by making it easy, fast and secure for people and businesses around the world to buy goods and services using virtually any form of payment. The company’s portfolio of services and solutions includes credit, debit, private-label, smart and stored-value card issuing and merchant transaction processing services; money transfer services; money orders; fraud protection and authentication solutions; check guarantee and verification services through TeleCheck; as well as Internet commerce and mobile solutions. Western Union and its subsidiary, Orlandi Valuta, together make up one of the world’s largest money transfer networks with approximately 242,000 Agent locations in more than 200 countries and territories. The company’s STAR Network offers PIN-secured debit acceptance at 1.7 million ATM and retail locations. For more information, visit www.firstdata.com.