Secrets of Success: How Digital Lenders Can Win the Fight Against Fraud

It’s not so hard to solve — with the right approach

LexisNexis® RISK SOLUTIONS
If you thought the lending business was tough, try separating truth from fiction

You know the digital space offers unlimited potential in lending. You’re also aware of the risks of dealing with remote borrowers. Maybe you’ve resigned yourself to accept some losses in the name of growth. But do you really understand what’s at stake?

Digital lenders of every size are experiencing a sizeable amount of fraud — more than you may realize. And this trend is likely to grow as new channels and customer touch points come online.

A startling proportion of fraud attempts make it past fraud detection systems and protocols:¹

<table>
<thead>
<tr>
<th>Fraud success rate:</th>
<th>Average amount per fraudulent transaction:</th>
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<tbody>
<tr>
<td>Against small/ midsized digital lenders</td>
<td>31%</td>
</tr>
<tr>
<td>Against large digital lenders</td>
<td>25.5%</td>
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Source: All figures presented throughout are from the 2017 LexisNexis® True Cost of Fraud™ Study
Considering the volume of transactions you deal with, this isn’t peanuts. In fact, every instance of fraud has a financial impact far beyond the transaction amount. Factor in additional, indirect costs such as fees and interest — and each fraud attempt not prevented becomes even more glaring.

The LexisNexis Fraud Multiplier℠ reveals that for every $1 of fraud, digital lenders are losing roughly 2.5 times or more that amount.

<table>
<thead>
<tr>
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<th>Small/Midsized Digital Lenders</th>
<th>Large Digital Firms</th>
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<tbody>
<tr>
<td>Fraud Costs Per $1</td>
<td>$2.67</td>
<td>$3.07</td>
</tr>
<tr>
<td>Revenue Impact</td>
<td>1.78%</td>
<td>2.24%</td>
</tr>
</tbody>
</table>

LEXISNEXIS FRAUD MULTIPLIER℠
Cost = The initial fraud loss plus related fees and interest for which the lender is held liable. Calculated as a per dollar total cost.
Is effective fraud prevention possible without overburdening customers or overextending resources?

Yes, with the right mix of tools—and a risk-based strategy that intelligently tailors the scrutiny based on the risk of each scenario.

Learn how best-of-breed digital lenders of all sizes are putting these best practices into action, and where many lenders still have room to improve.

Don’t be fooled by the numbers: The overall financial impact of fraud is harder on the small-to-midsized group. Fraud losses reduce bottom-line profit and are more difficult for lower-revenue firms to absorb.

Consider this: A $10 million lender loses, on average, $178,000 in fraud.

If their average profit margin is 10% ($1 million), that’s almost 20% of their profits wiped off the bottom line.

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SUCCESS STRATEGY #1: What gets tracked, gets measured

Top-performing digital lenders track their results, but here’s the rub: They tend to take a siloed approach.

Small/midsized firms tend to look at fraud by payment method (check, credit card, etc.)

Larger digital firms are more likely to look at both payment type and channel (mobile, in-store, etc.)

Large digital lenders are also more likely to track successful fraud.

But there are serious gaps

Still, not enough lenders are tracking both variables, and many lenders—especially small/midsized—still only track prevented fraud, and are unaware where the successful fraud transactions are coming from.
The many touchpoints of fraud — and their unique risks

Channels:
Remote multi-channels allow more ways for fraudsters to attack and/or steal customer information. In fact, the overwhelming majority of digital lenders perceive that mobile payment adds significant fraud risk.

Payments:
Traditional credit/debit payments still account for the largest proportion of fraud.

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<th>Small/Midsized Firms:</th>
<th>Large Firms:</th>
</tr>
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<tbody>
<tr>
<td>Credit</td>
<td>42%</td>
<td>29%</td>
</tr>
<tr>
<td>Debit</td>
<td>33%</td>
<td>26%</td>
</tr>
</tbody>
</table>
But beware: Alternative payments (PayPal, BillMeLater, etc.) and other transaction methods (gift cards, mobile wallets, virtual currencies) are growing — particularly among large digital lenders — and should be monitored closely as fraudsters adapt new payment methods.

**Geography**

Not surprisingly, larger digital firms experience a higher proportion of losses from international fraud than their smaller counterparts — 27% vs. 10%, respectively.

**30% of large digital lenders** say one of their biggest challenges is to assess fraud risk by country or region.

**Fraud Type**

Identity fraud accounts for at least half of fraud losses among digital lenders. That’s no surprise; lenders large and small find it difficult to authenticate and verify identities in a way that reduces customer friction while keeping “bad guys” out.

**REALITY CHECK**

It’s not enough to have high-quality solutions. You need solutions that attack the right problems for your organization — and can quickly adapt to emerging threats. Robust tracking mechanisms that track across multiple variables and fraud types provide clarity and fill in gaps you can’t detect.
Firms that are winning the battle against fraud understand that solutions must be tailored to who they are serving, and where. Some differences to consider:

**Generational**
Older consumers have been culturally trained to fiercely guard personal information — though they’re accustomed to knowledge-based authentication quizzes. On the other hand, mobile-minded Millennials typically don’t blink an eye about snapping and uploading a photo of their driver’s license. Fraud prevention measures need to address these differing attitudes.

**Locational**
Countries differ in how they gather—and provide access to—identity details on individuals. Best-in-class fraud solutions include strong data coverage for the specific countries with which you do business. But it’s not just about detecting “bad guys.” Customer expectations around data privacy, types of interaction and “routine” verification may be cultural.

**Unbanked/Underbanked Populations**
No doubt there’s a big, untapped opportunity here. But doing business with individuals without an established credit footprint can make it difficult to verify identities and assess financial and fraud risk. Any fraud solution must incorporate alternative data that can pull a broader set of attributes and insight.

Mobile transactions represent just over 1/5 of all lending transactions. But the steady growth of mCommerce will force lenders to adopt new ways to leverage its convenience without added risk.
SUCCESS STRATEGY #3: Layering Is Fundamental

Lenders that use a variety of fraud solutions — and layer them effectively — are outperforming their peers in key areas:

**Lower Fraud Costs**

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<tr>
<th>Average layered solutions:</th>
<th>8</th>
<th>4</th>
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</thead>
<tbody>
<tr>
<td>Fraud cost per $1:</td>
<td>$2.46</td>
<td>$2.69</td>
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</table>

Best-in-class firms implement layers of protection covering multiple factors:

- **Core Solutions**
  - Card/Check Verification
  - Address Verification
  - Browser Malware
  - PIN/Signature

- **Advanced Identity Solutions**
  - Device ID Fingerprinting
  - Geolocation
  - Authentication Via Quiz
  - Customer Profile Database

- **Fraud Transaction Risk Assessment Solutions**
  - Automated Transaction Scoring
  - Real-Time Transaction Tracking
  - Transaction Verification
  - Rules-Based Filters
  - Authentication by 3D Tools
But the real value comes in the efficiencies and cost savings. Digital lenders who understand their specific fraud risks and layer the right mix of core + identity + fraud transaction solutions report fewer false positives, manual reviews and successful fraud attempts.
But many firms are far too exposed.

Many digital lenders are leaving big gaps in their fraud mitigation.

**Small/Midsized Digital Lenders**

Nearly 2 out of 3 use a fraud mitigation solution *but not a flagging system.*

No wonder 41% cite “excessive manual reviews” as a challenge.

Many smaller lenders are also less likely to use identity verification — likely contributing to that 60% incidence of fraud mentioned earlier.
Large Digital Lenders

- Use 2x as many flagging systems as their smaller counterparts
- More likely to be using more risk mitigation solutions — including advanced identity authentication and transaction verification

However, despite using multiple solutions, some continue to battle high fraud costs — and may not be leveraging the right mix and/or layering of solutions.

The bottom line…

While the specific mix is highly dependent on transaction methods, channels, and customer base, **lenders should always start with low-friction, behind the scenes tools like device assessment and behavioral biometrics.** Then, step up only when necessary according to the risk of each consumer and/or transaction.
The moral of the story: you owe it to yourself to double-down on your defense.

The 2017 LexisNexis® Risk Solutions True Cost Of Fraud™ study results are telling: Despite implementing numerous piecemeal solutions to fight fraud, digital lenders are often falling short of their goals.

Workflow and decisioning gaps leave blind spots. Reduce the risk with a central platform that facilitates a multi-layered approach designed to reduce friction, and step up the rigor as needed.

Connect channels and transaction types for a unified view  
Track and measure fraud attempts and successes  
Support real-time, risk assessment — matched with the best verification and authentication solution for the event
We are one of the largest compilers of identity fraud intelligence, with the strongest arsenal of content in the industry:

65 billion records
globally from
10,000+ sources,
spanning
200 countries.

Our leadership in data science stems from 40 years of managing and analyzing big data. We are experts at seeing the connections between disparate data sets — and can quickly glean insight into identity and creditworthiness with exceptional accuracy.
We’ve harnessed our knowledge into a broad portfolio of capabilities and solutions designed to identify and prevent fraud:

**Predictive fraud analytics** that apply machine learning to analyze fraud signals and precisely identify multiple fraud types

**The first-of-its kind Fraud Defense Network**, built by us to enable cross-industry sharing of insight about suspicious credit- and service-seeking behaviors

**The LexisNexis® Risk Solutions Risk Defense Platform** that powers a multi-layered approach to risk management by integrating key tracking, fraud analytics, verification and authentication solutions

And because the type and scope of fraud is constantly evolving, we design solutions that enable lenders to adapt to rapidly evolving fraud threats with minimal resources.

A full Risk Management team is always there to assist and ease the burden on in-house departments. Transactional pricing make powerful fraud mitigation tools accessible to the smallest firms.
Don’t just take our word for it. See for yourself.

Contact us to set up a free demo of our Risk Defense Platform — and learn how it can reduce the cost of fraud in your lending business.

lexisnexis.com/risk

About LexisNexis Risk Solutions
At LexisNexis Risk Solutions, we believe in the power of data and advanced analytics for better risk management. With over 40 years of expertise, we are the trusted data analytics provider for organizations seeking actionable insights to manage risks and improve results while upholding the highest standards for security and privacy. Headquartered in metro Atlanta, LexisNexis Risk Solutions serves customers in more than 100 countries and is part of RELX Group plc, a world-leading provider of information and analytics for professional and business customers across industries. For more information, please visit www.lexisnexis.com/risk.