THE STATE OF PAYMENT PROCESSING & FRAUD: 2018

Inaugural Report

PRESENTED BY:

Kount®

THE FRAUD PRACTICE

Survey Report and Overview

The State of Payment Processing & Fraud: 2018 Inaugural Survey & Report is a first-of-its-kind study brought to you by Kount and The Fraud Practice. The inaugural survey reached hundreds of acquirers, processors, gateways, payment facilitators and issuers to get their take on the state of the industry and what is most critical for attracting and retaining clients and growing processing volumes.

Payment processors and vendors that support card/customer-not-present (CNP) transactions across many channels and borders are an integral part of the payments ecosystem. Input from these organizations, including what they are doing to support merchants and facilitate payments (i.e. value added services), is often overlooked. The inaugural edition of this payment industry-focused study tests the hypothesis that value-added services have a meaningful impact upon improving the ability for payment processors to attract, acquire and retain merchant clients.

Whether it's facilitating cross-border payments, helping to detect and eliminate fraud or supporting new payment types, these benefits ultimately help merchants increase sales. As a result, the payment processors who offer value-added services enjoy increased processing volumes, stronger merchant retention and incremental revenue opportunities.

Key survey findings elaborated in the report include:

- Organizations continue to increase support and add new offerings. Nine-in-ten organizations that support mobile and alternative payment types are increasing support for these this year. More than 80 percent will increase support for business reporting and analytics, 75 percent will increase support for fraud scoring or integrated rules and nearly 70 percent will increase support for fraud technology tools.

- Fraud prevention is a concern for **all** payment organizations surveyed. More than half of survey respondents said CNP channel fraud is a challenge for their organization and 63 percent say they are “Very Concerned” with CNP channel fraud.

- Nearly 60 percent of payment organizations offer or support velocity checks while 45 percent offer or support fraud scoring, IP geolocation and rules engines. Only 26 percent of payment processors who offer or support fraud technology tools and 31 percent who offer fraud scoring or integrated rules do so without third party vendor partners.

- When it comes to payment companies that offer risk management as a value-added service, 70 percent are using at least one third party partner while 58 percent have two or more and 40 percent have three or more partners. Payment organizations are most concerned with ease of use for their clients, instant integration or “flip-a-switch” capabilities, and merchant demand for specific tools or solutions when deciding who to partner with to provide risk management services.

- Support for new mobile and alternative payment types followed by offering fraud prevention services are the two types of value-added services payment industry organizations consider most important for attracting new merchant clients.

- While about 60 percent of payment organizations that offer at least one value-added service say doing so has improved merchant retention, those who offer cross-border payments (83 percent) and integrated risk management rules or fraud scoring (79 percent) are even more likely to report benefits realized in terms of merchant client retention. Those offering these as value-added services are also significantly more likely to report improvements in the ability to attract new clients.

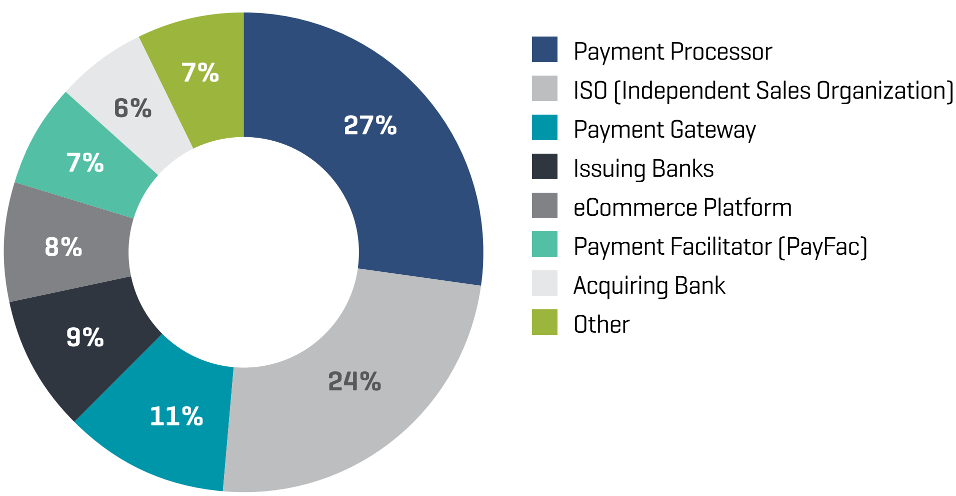
Methodology

This report was commissioned by Kount to understand payment processors and their strategic priorities over the next year as well as the value processors place on leveraging value-added services within their organization. Eligible participants included staff from acquiring banks, issuing banks, payment processors, payment facilitators (PayFacs) and payment gateways. Independent sales organizations (ISOs), ecommerce platforms, consultants and merchants were excluded from the survey and not included in the results. The survey was offered only in English.

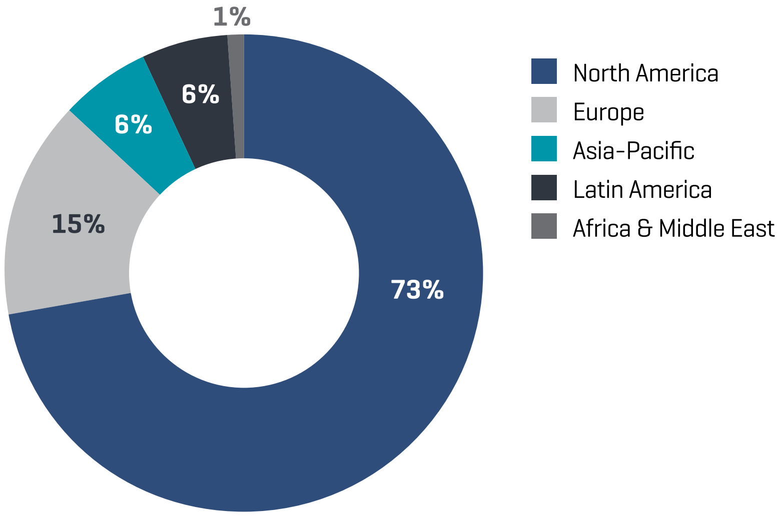
About the Survey Respondents

Approximately 150 organizations participated in the 2018 Payment Processor Industry Survey including about half who process payments. Although nearly three-quarters of these organizations are headquartered in North America, 88 percent of all organizations support cross-border payments and many have clients processing globally. Fifteen percent of respondents are headquartered in Europe, while 12 percent of payment processors surveyed are headquartered in either Latin America or the Asia-Pacific region.

Type of Organization

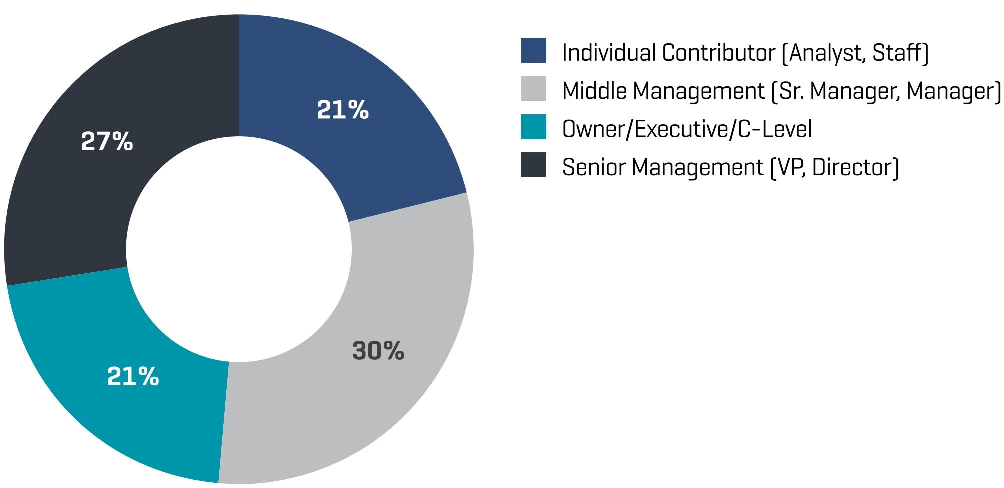


Where Organizations are Headquartered



Survey respondents represented a balance of different roles and responsibilities within their organizations. This included more than one-fifth of respondents who are executives within their organizations, more than one-quarter who are Directors, VPs or other senior management, and just over half who are individual contributors, analysts, senior analysts or managers. Nearly half of all survey respondents, 48 percent, are business owners, executive level or senior management. These individuals have deep experience and are knowledgeable of their organizations current operations and strategy plans, providing high quality information and results for this study.

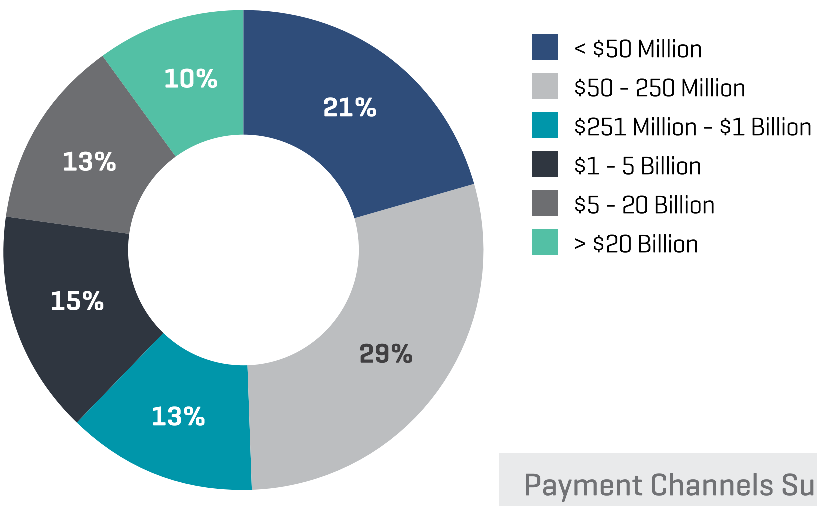
Survey Respondents by Career Level



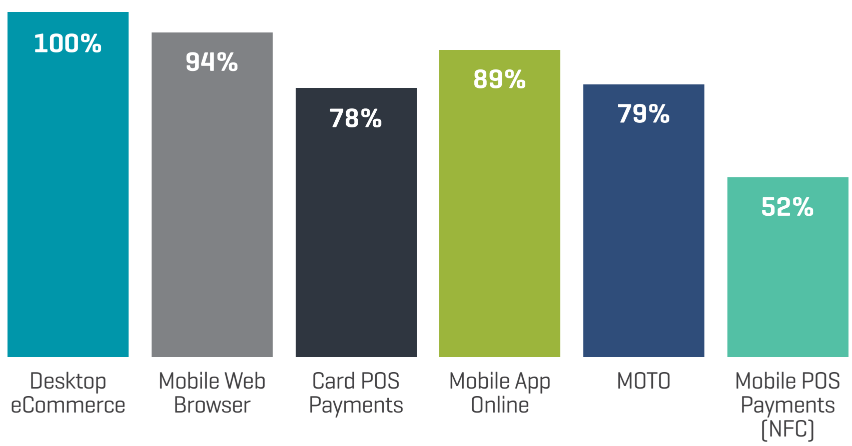
Among respondents who reported their organization's processing volume, 38 percent reported volume of more than $1 billion per year. This includes 23 percent of payment processors with $5 billion or more in annual processing volume and 10 percent with annual volumes exceeding $20 billion. Approximately half of payment organizations surveyed have processing volumes less than $250 million per year with 21 percent reporting annual volume below $50 million.

Those surveyed process or support payments across many channels and 100 percent support eCommerce payments. Nearly 90 percent of respondents process or support payments captured via mobile apps and 94 percent support mobile eCommerce payments within a mobile web browser. While all payment organizations surveyed support Card Not Present payments, less than 80 percent support the Card Present channel or transactions made at the physical point-of-sale. Just over half, 53 percent, support mobile payments at the point-of-sale such as with NFC mobile wallets or QR codes.

Annual Processing Volume



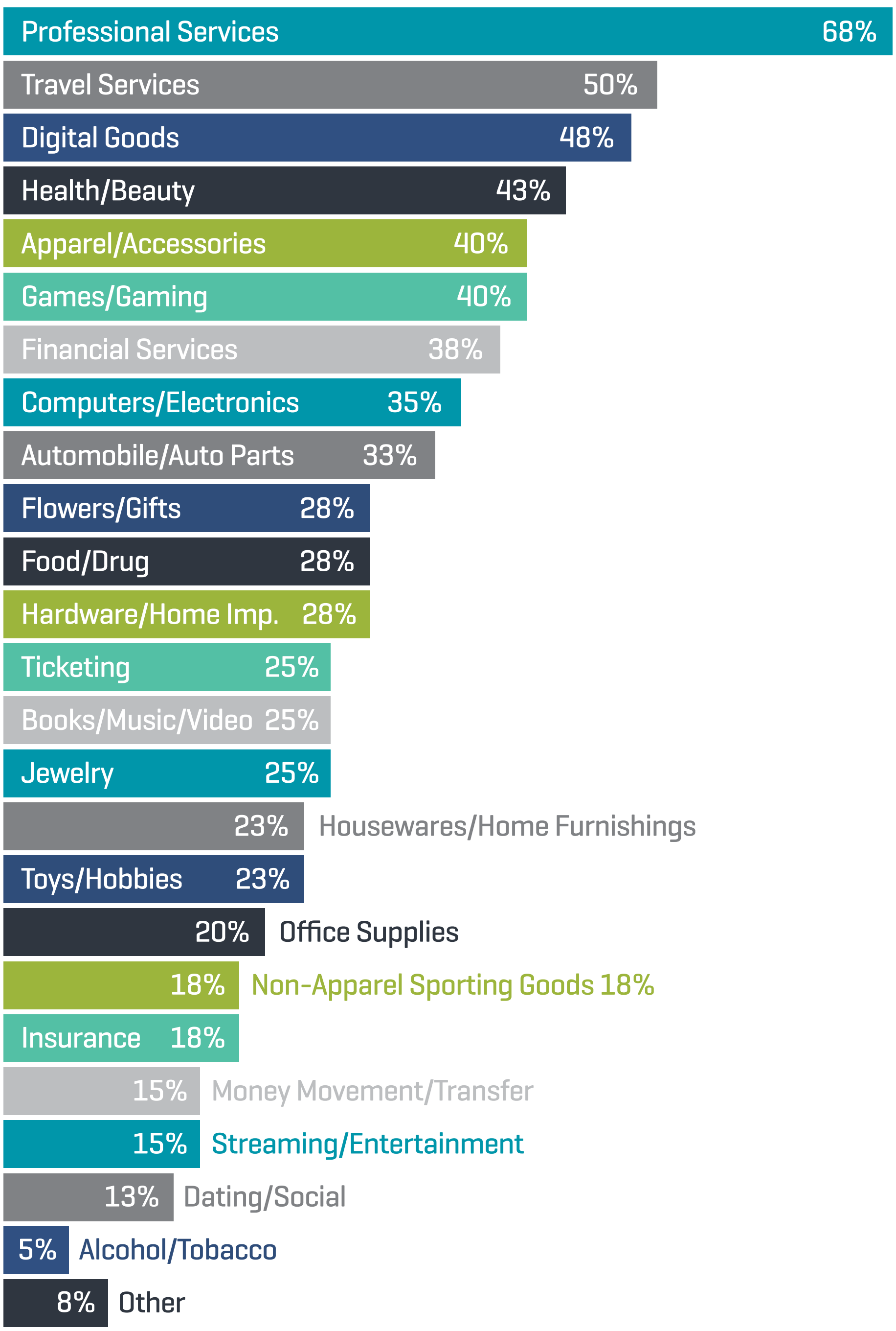
Payment Channels Supported



Merchants and Payment Types Supported

Fifty percent or more of the respondents support Professional Services and Travel industries, while nearly half support Digital Goods merchants (48 percent). There are fifteen industries served by at least one-in-four payment organizations, including several high-risk markets like Games/Gaming, Computers/Electronics, Jewelry and Money Movement.

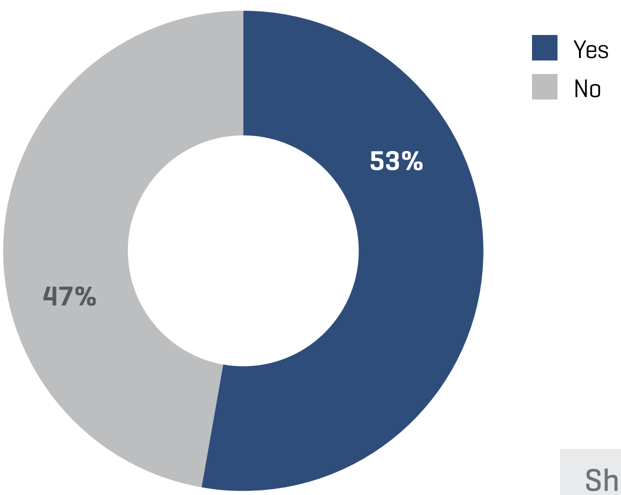
Merchant Industries Served



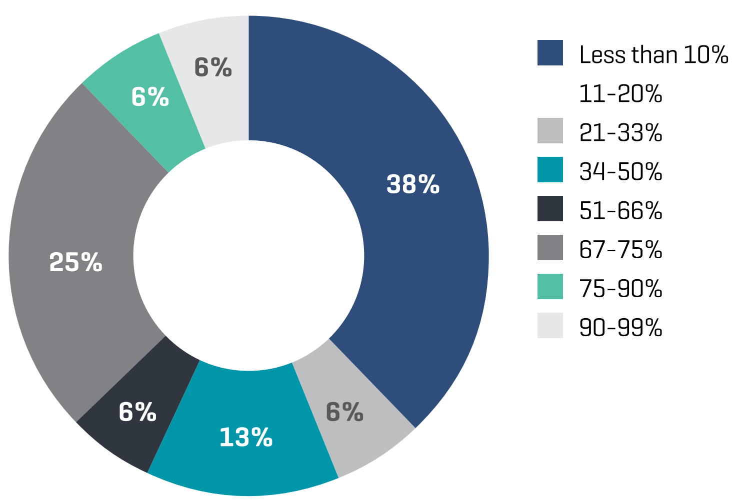
More than half of those surveyed, 53 percent, indicated they support payment processing or other services for high risk merchants, but this is primarily organizations with annual processing volumes less than $1 billion. While two-thirds of payment processors with annual processing volumes between $50 million and $1 billion underwrite high risk merchants, just 13 percent of payment processors who process more than $1 billion annually service high risk merchants.

Payment processors are most likely to either have just a small number of high risk clients or mostly high-risk merchant clients. The survey found that high-risk merchants comprise less than 10 percent of processing volume for 38 percent of payment processors, while 37 percent of payment processors stated that high risk merchants represent two-thirds or more of their total processing volume.

Payment Companies Working with High Risk Merchants



Share of Processing Volume with High Risk Merchants

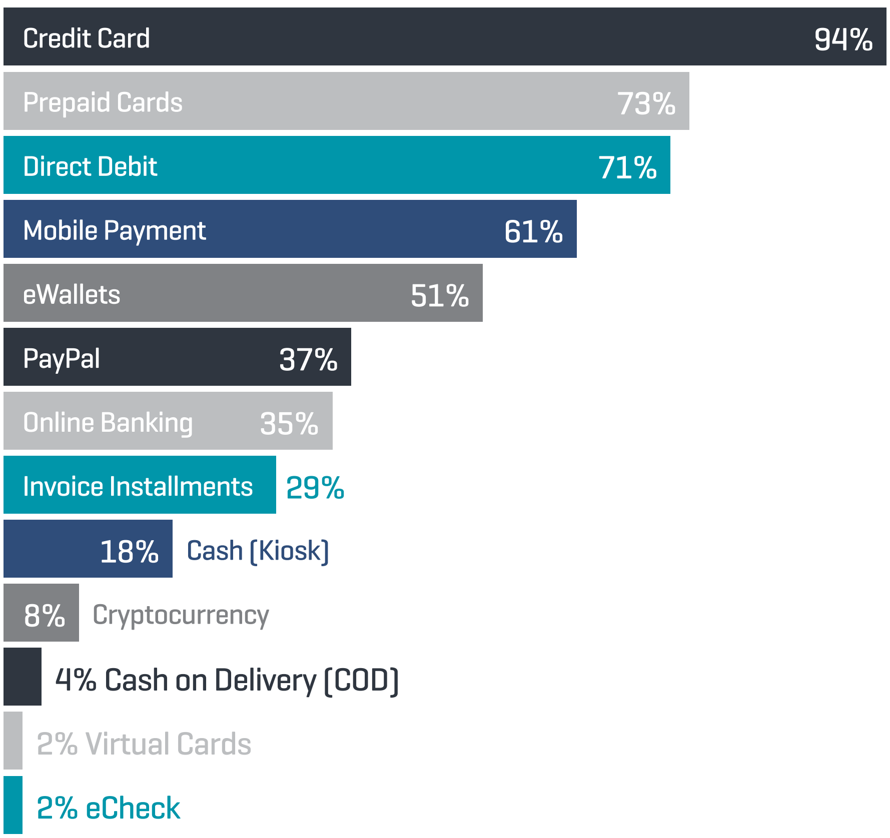


Those who choose not to process or facilitate payments for high risk merchants were then asked the reasons why not, with two-thirds of respondents stating simply because it does not align with their business strategies. Nearly one-in-five payment processors surveyed indicated they lack the fraud and risk management controls to support high-risk merchants. Those who indicated this also reported experiencing financial losses due to high-risk merchants in the past as reason for choosing not to underwrite these merchants today.

Why Payment Processors Do NOT Underwrite High Risk Merchants

Not surprisingly, 94 percent of payment processors surveyed process or facilitate credit or debit card payments. eWallets, ACH Direct Debit, mobile payments and prepaid cards are each supported by more than half of payment processors, gateways and PayFacs. Cash-on-Delivery, a service recently discontinued by PayPal in the U.S., is supported by just 4 percent of payment processors while only 2 percent process or support eChecks. Meanwhile nearly one-third support installment invoice payments and 8 percent of payment processors support cryptocurrencies like Bitcoin, Bitcoin Cash or Ethereum.

Payment Types Supported

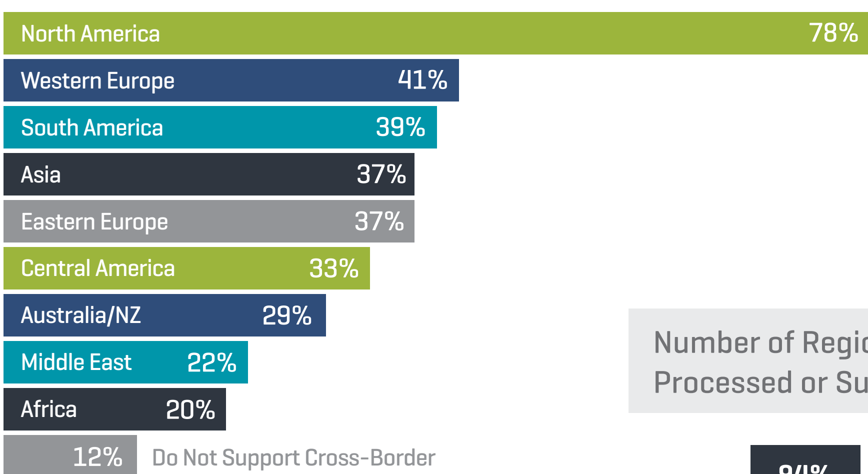


Cross-Border Payments

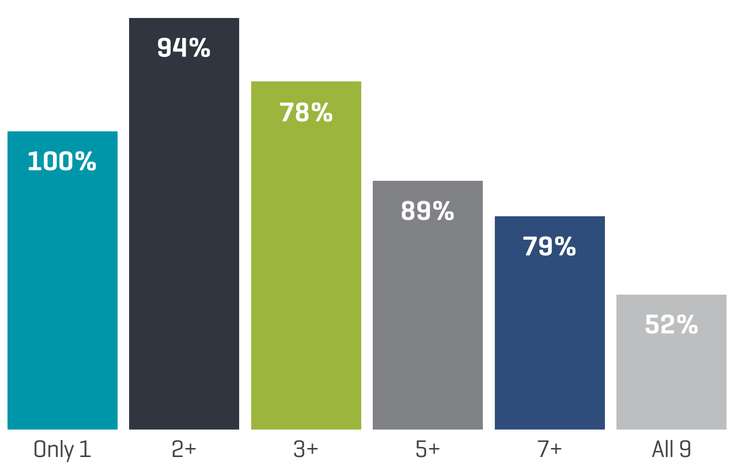
The majority of payment processors, acquirers, gateways and PayFacs surveyed support both Card Not Present and cross-border payments. This same group of payment processors considers the ability to process or support cross-border and CNP payments essential to their future growth. Nearly nine-in-ten of the payment processors surveyed facilitate cross-border payments today, whether that is for domestic merchants who transact with customers abroad or international merchants that do business outside of their country.

More than three-quarters of payment organizations that support cross-border payments enable merchants from other regions to do business in North America while 41 percent support international payment transactions across Western Europe. More than one-third of participants facilitate payments from consumers in Central and South America, Asia and Eastern Europe. Nearly 60 percent who support cross-border payments do so in two or more regions and nearly half support three or more. Around 20 percent of payment industry organizations surveyed support cross-border payments in all nine global regions, while 30 percent facilitate payments across at least seven regions.

Regions Where Payments are Processed or Supported



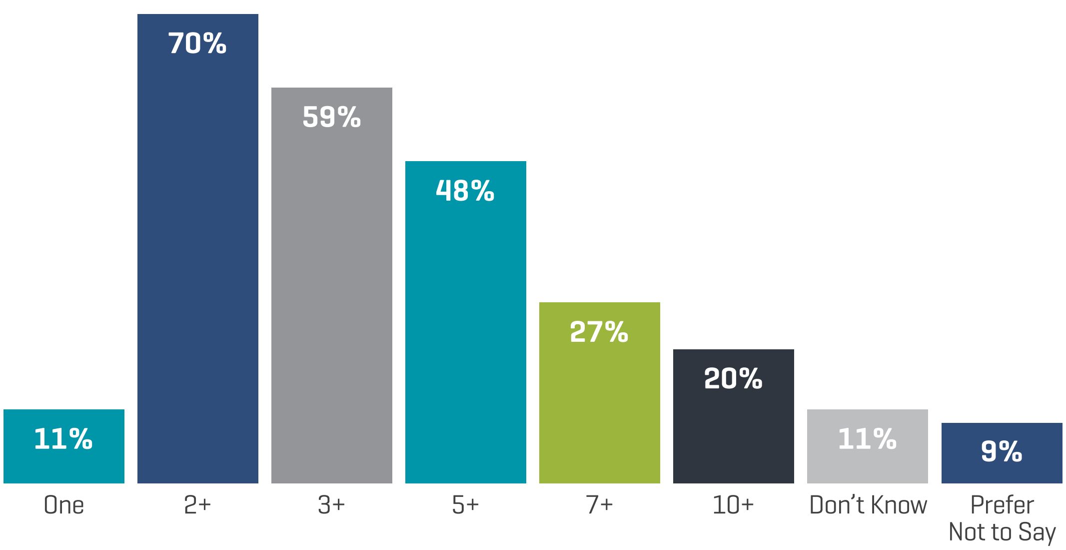
Number of Regions Where Payments are Processed or Supported



Results from The State of Payment Processing & Fraud Survey also show a disparity in support for cross-border payments between organizations with smaller and larger processing volumes. Just 12 percent of payment organizations overall indicated they do not support cross-border payments, but all of these organizations reported annual processing volumes less than $250 million and more than half reported annual volume less than $50 million. Amongst organizations that currently support cross-border payments, more than 60 percent with annual processing volume less than $5 billion only facilitate cross-border payments with one region. In contrast, nearly two-thirds of organizations with annual processing volumes greater than $20 billion support cross-border payments to all global regions, and 100 percent of these organizations facilitate international payments to at least seven regions.

To support cross-border transactions across regions, payment processors, gateways and others are partnering with multiple regional or country-specific acquiring banks. Just 11 percent of those surveyed overall said they have only one acquiring bank partner, all of which have annual processing volumes less than $5 billion and half of which only support payments within North America. Seven-in-ten payment organizations stated they have two or more acquiring bank partners, but when omitting the 11 percent who don't know and 9 percent who prefer not to say how many acquiring banks their organization processes payments through, this increases to 87 percent. Nearly half of payment processors are partnering with four or more acquiring banks while 20 percent have ten or more acquiring bank partners to facilitate global payments. Controlling for respondents who did not know or disclose their organization's number of acquiring bank partners, nearly one-quarter of organizations partner with ten or more acquiring banks and 60 percent have at least four such partners to support cross-border transactions.

Number of Acquiring Banks Processing Through

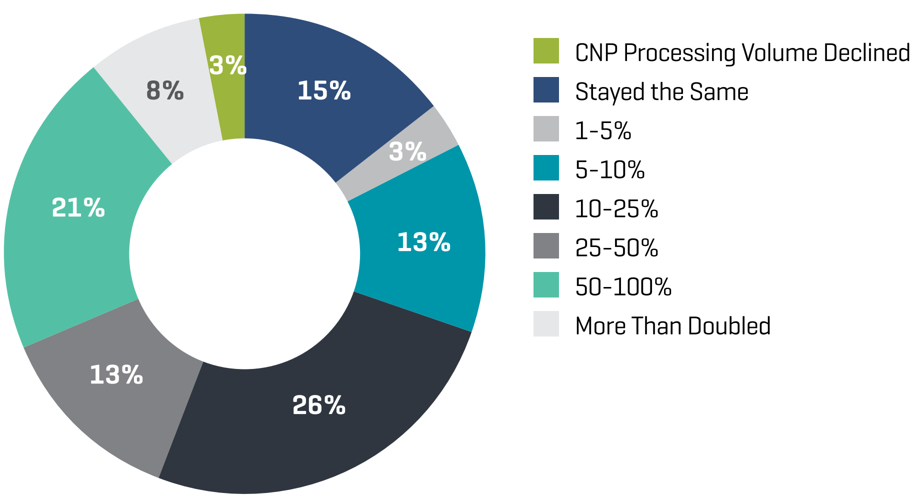


CNP Payments

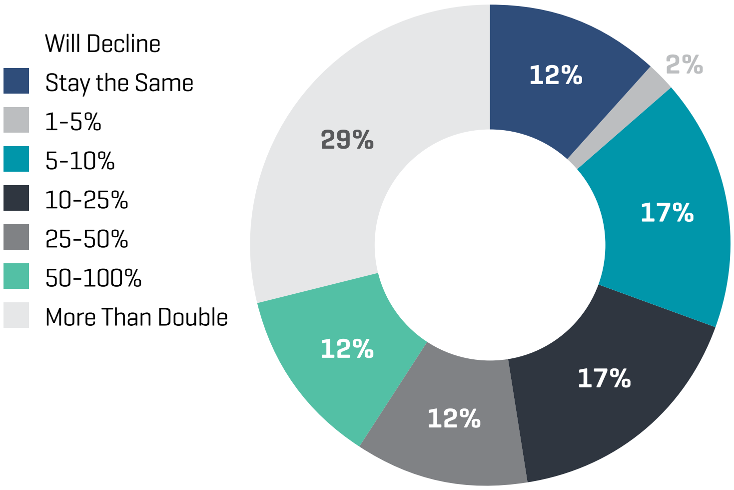
Be it cross-border or domestic transactions, more and more CNP transactions are being processed. Considering CNP transactions as a share of total processing volume, only three percent of survey respondents said this is declining. Meanwhile, 82 percent of payment industry organizations indicated CNP is increasing its share of their total processing volume. Nearly 30 percent of respondents said the CNP channel grew by 50 percent or more as a share of total volume in 2017. More than two-thirds of survey respondents indicated that CNP transactions increased by 10 percent or more last year.

After years of continued CNP channel growth, organizations in the payments industry are expecting more of the same for years to come. Not one survey respondent expects CNP to decline as a share of total processing volume and just 12 percent say it will stay the same between now and 2020. More than half of payment processors, 52 percent, expect the CNP channel to grow by 25 percent or more as a share of total processing volume by the year 2020, and nearly 30 percent expect CNP channel volume to more than double for their company by then.

Growth in CNP as Share of Total Processing Volume



Expected Growth in CNP as Share of Total Processing Volume by 2020



Key Takeaways – About the Survey Respondents

- Mobile web browser and native in app payments are vastly supported by respondents, 94 and 90 percent of payment organizations, respectively.
- Nearly half of payment processors choose not to support high-risk merchants while the majority who don't say it's because this doesn't align with their business strategy.
- There is strong support for cross-border payments overall, but organizations with smaller annual processing revenues are considerably less likely to facilitate cross-border payments or to as many regions.
- Most payment organizations (82 percent) reported CNP channel growth in 2017 and nearly 30 percent expect the CNP channel to more than double as a share of total processing volume by 2020.

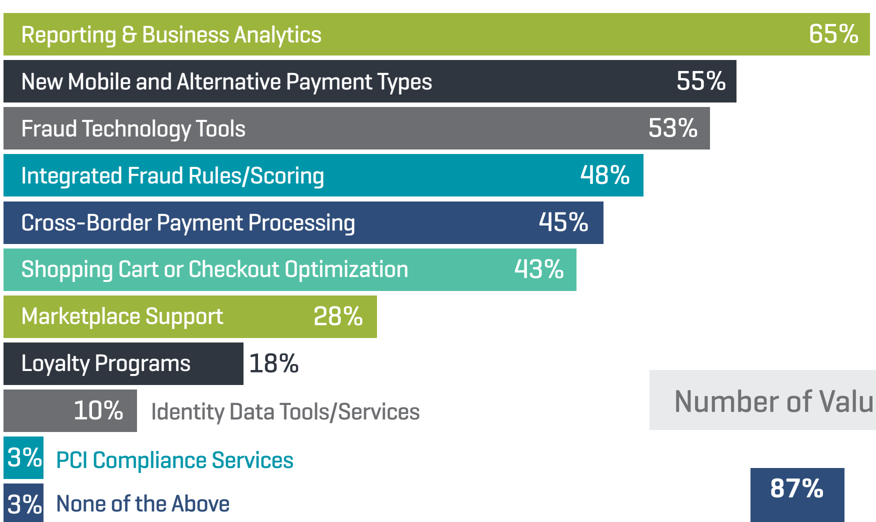
Support for Value-Added Services

The payments industry is very different in 2018 than it was twenty, ten or even five years ago. Being able to facilitate payments in the eCommerce (100 percent of survey respondents) and mobile (94 percent of respondents) channels is a must, and almost all organizations, 97 percent, are offering one or more types of value-added services. One of the primary purposes of the State of Payment Processing & Fraud survey was to understand what payment industry organizations are offering today in terms of value-added services, and how each benefit both the payment provider and their merchant clients.

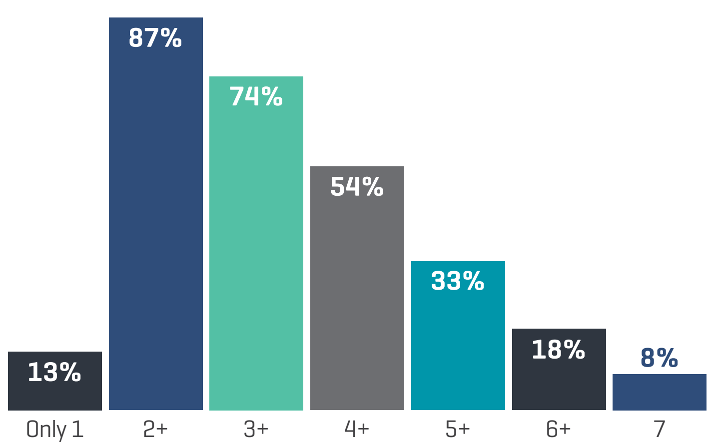
Just three percent of payment industry companies say they are not offering value-added services today, compared to more than half of organizations that offer four or more additional payment or transaction related services. Omitting the few organizations that don't support value-added services, 87 percent offer two or more and nearly one-third offer five or more.

More than half of respondents offer fraud technology tools as a value-added service, while 55 percent support mobile and alternative payments and nearly two-thirds of payment industry organizations offer their merchant clients reporting and business analytics. Nearly half of organizations provide integrated risk management rules or fraud scoring, while 45 percent offer cross-border payment processing.

Value-Added Services Supported Today



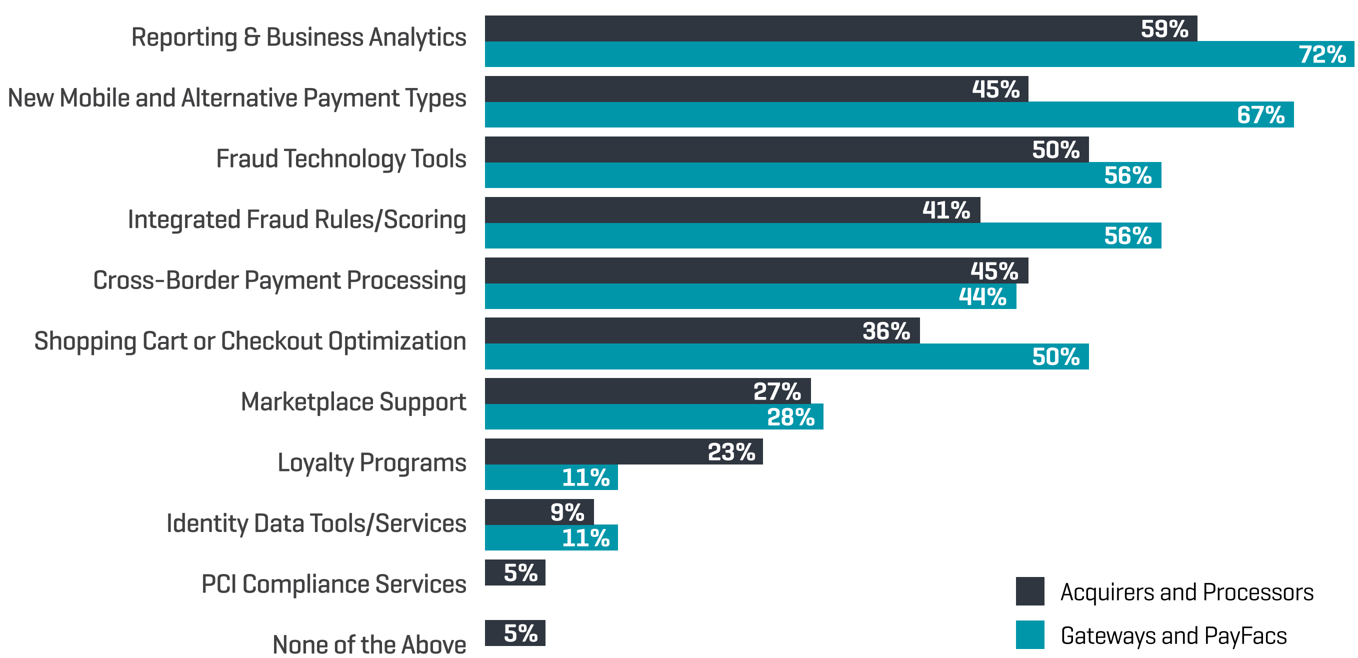
Number of Value-Added Services Offered



Broken down by type of organization in the payments industry, the survey shows that gateways and payment facilitators are likely to support more value-added services relative to acquirers and payment processors. Organizations with higher volumes tend to offer more services overall. All organizations surveyed with annual processing volumes greater than $20 billion support cross-border payment processing, fraud technology tools and business reporting analytics. Organizations with annual processing volumes less than $1 billion are most likely to provide reporting and business analytics, as indicated by 71 percent. Just 57 percent of these lower volume respondents support fraud technology tools and less than 40 percent support cross-border payment processing.

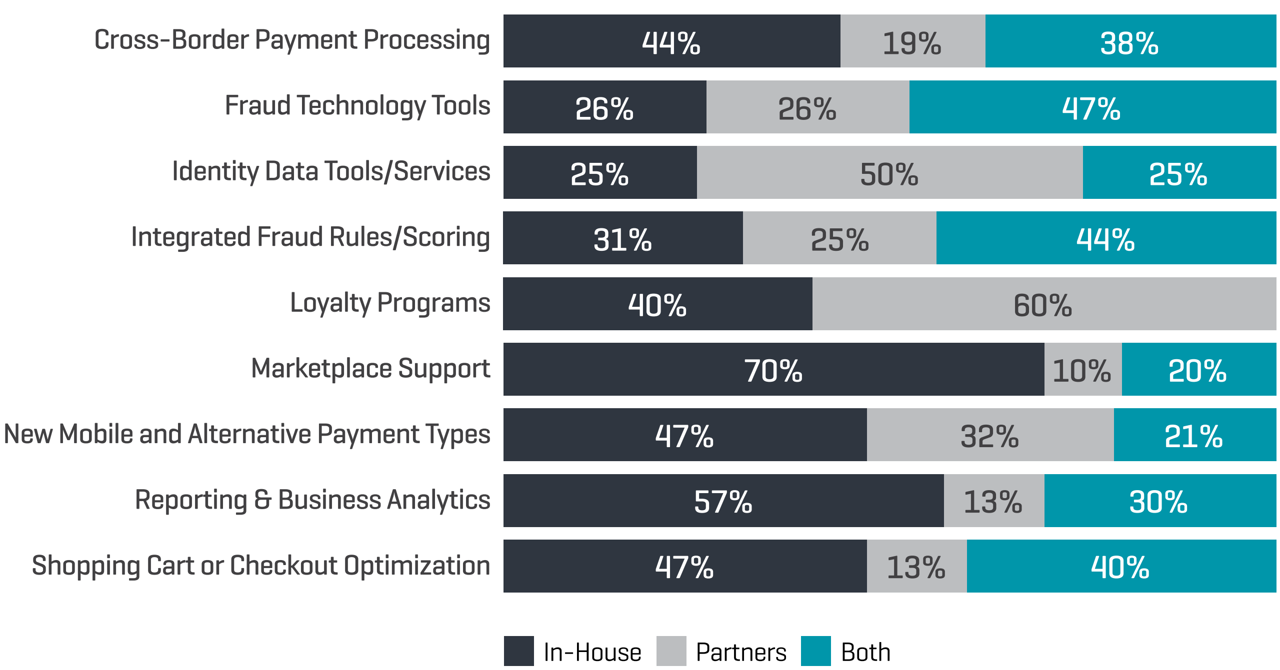
There are five different value-added services offered or supported by at least 50 percent of gateways and PayFacs, compared to just two value-added services supported by at least half of the acquirers and payment processors surveyed. Reporting and business analytics are the value-added services most likely to be offered by both groups, although gateways and PayFacs are considerably more likely to offer or support business reporting (72 percent versus 59 percent), as well as integrated risk management rules or fraud scoring (56 percent versus 41 percent), shopping cart or checkout optimization (50 percent versus 36 percent), and new mobile or alternative payment types (67 percent versus 45 percent). Acquirers and processors are more likely to support loyalty programs than payment gateways and facilitators, while the two groups are about equally as likely to support cross-border payments, offer identity tools or marketplace support.

Value-Added Services Supported by Type of Organization



In terms of how valued-added services are offered, organizations can build and provide these in-house, partner with vendors or both. There are just two services offered by more than half of payment companies in-house, including reporting and business analytics (57 percent) and market place support (70 percent). Nearly half of payment processors, gateways, acquirers and PayFacs currently offer or support checkout optimization, mobile and alternative payment types as well as cross-border payment processing. The value-added services these organizations are least likely to offer in-house are identity data and fraud technology tools. While 26 percent of organizations offering fraud technology tools do so through third party partners exclusively, 47 percent are using a mix of vendor and in-house services. Payment processors are most likely to go through third party vendors exclusively for identity tools and services as well as loyalty programs, as indicated by more than half of respondents offering these as value-added services.

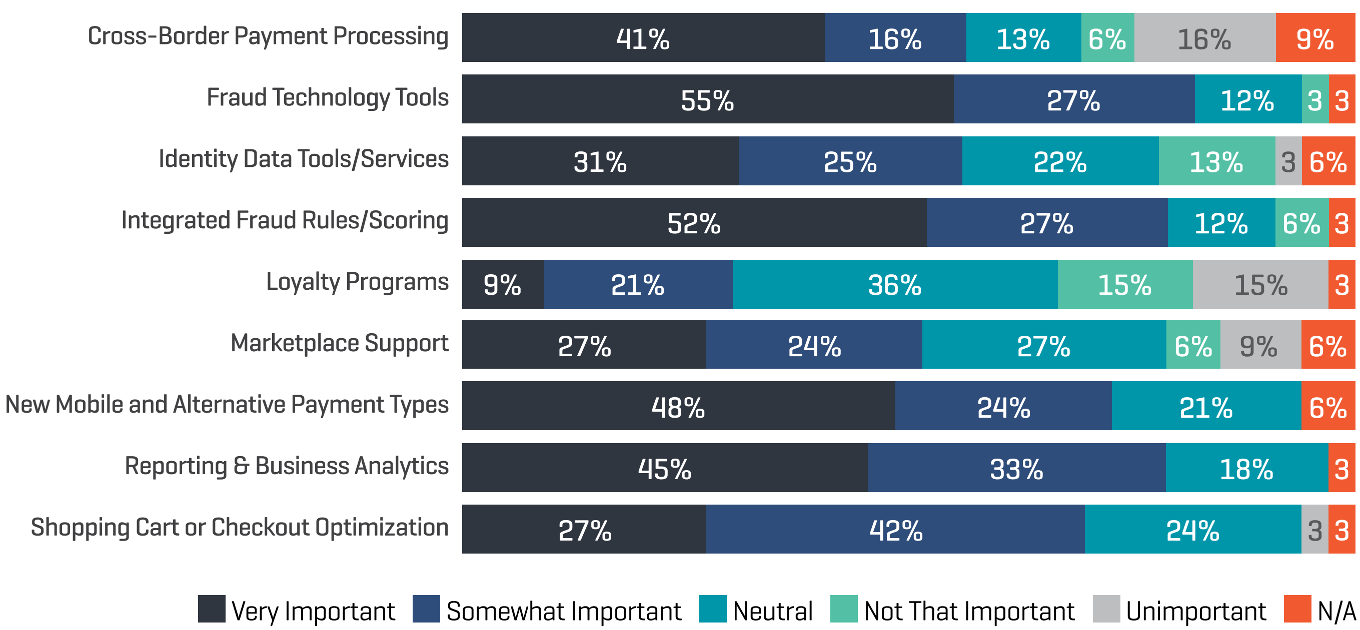
How Value-Added Services are Provided



Although payment industry organizations are most likely to offer or support business reporting and analytics or mobile and alternative payment types, the value-added services they are most likely to indicate as critical to their business strategies are fraud or risk management related. More than half of survey respondents consider fraud technology tools (55 percent) and integrated rules or fraud scoring (52 percent) to be "Very Important" to their business strategy, while about 80 percent each consider these to be at least "Somewhat Important."

Payment gateways and payment facilitators, who tend to offer or support more value-added services than acquirers and payment processors, are also more likely to indicate these services are "Very Important" to their overall business strategies. The only value-added service considered "Very Important" by at least 50 percent of acquirers and processors are fraud technology tools, while there are five value-added services considered "Very Important" by 50 percent or more of gateways and PayFacs. This includes fraud technology tools, integrated rules or fraud scoring and supporting new mobile or alternative payment types, each considered "Very Important" by at least 60 percent of PayFacs and gateways, as well as reporting and business analytics (53 percent) and support for cross-border payments (50 percent).

Value-Added Services Most Important to Business



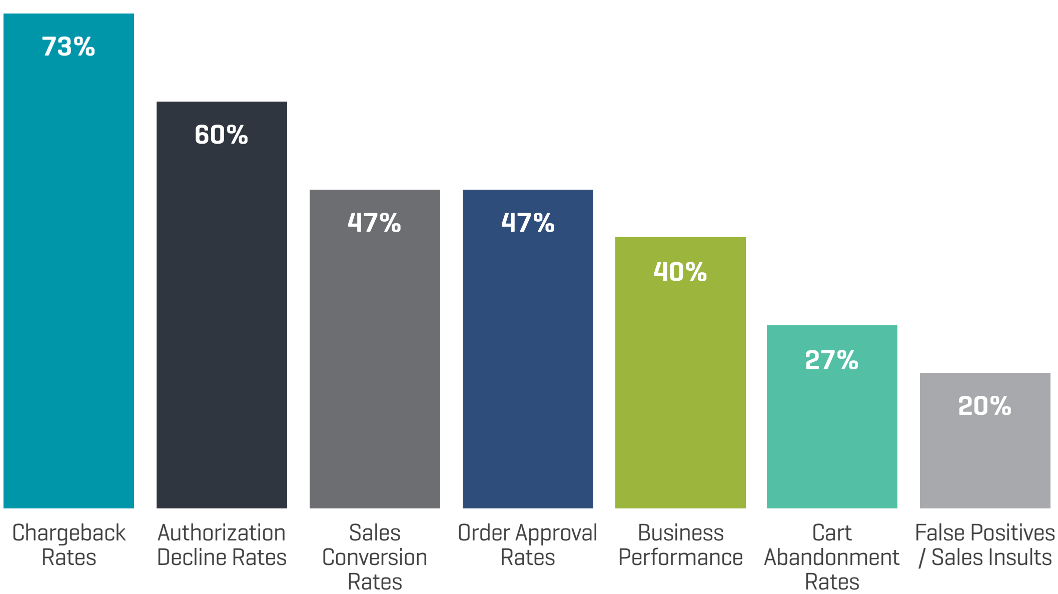
Analytics

Business analytics and reporting were recognized as the most supported value-added services and were an important focus of the 2018 The State of Payment Processing & Fraud Survey and Report. Payment industry organizations that offer or support reporting and analytics were next asked what key performance indicators (KPIs) and metrics they support and which are most critical and demanded by their merchant clients.

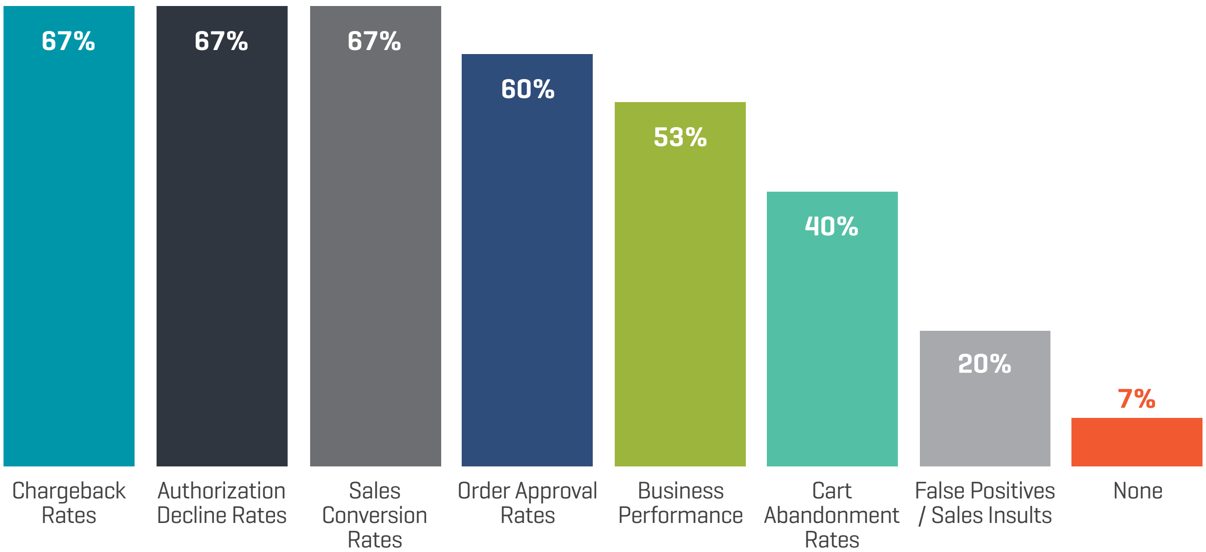
Payment organizations indicated their merchant clients care most about chargeback rates, while the next three most important and requested KPIs each pertain to sales optimization rather than fraud: authorization decline, order approval and sales conversion rates. Chargeback rates can result from many issues but are very often related to fraud, and while 73 percent of payment processors, acquirers, gateways and PayFacs say this is critical to track and is often requested by merchants, just 20 percent say the same for false positive or sales insult rates, which are an often-overlooked aspect of fraud and risk management.

False positives or sales insults, terms for preventing a legitimate transaction or user for suspected fraud, are difficult to track, which may support why just 20 percent of payment processors offering business reporting and analytics track metrics for false positives today. There are three metrics provided by two-thirds of payment organizations: business performance, order approval and authorization decline rates. These are three of five KPIs supported by at least half of payment processors, to also include chargeback and sales conversion rates. These metrics are the most likely to be offered, but false positive rates are not often requested by merchant clients, meaning many potentially good sales could be prevented with no reliable way to recognize and reduce this from happening.

Most Important KPIs for Merchants



KPIs Supported by Payment Processors

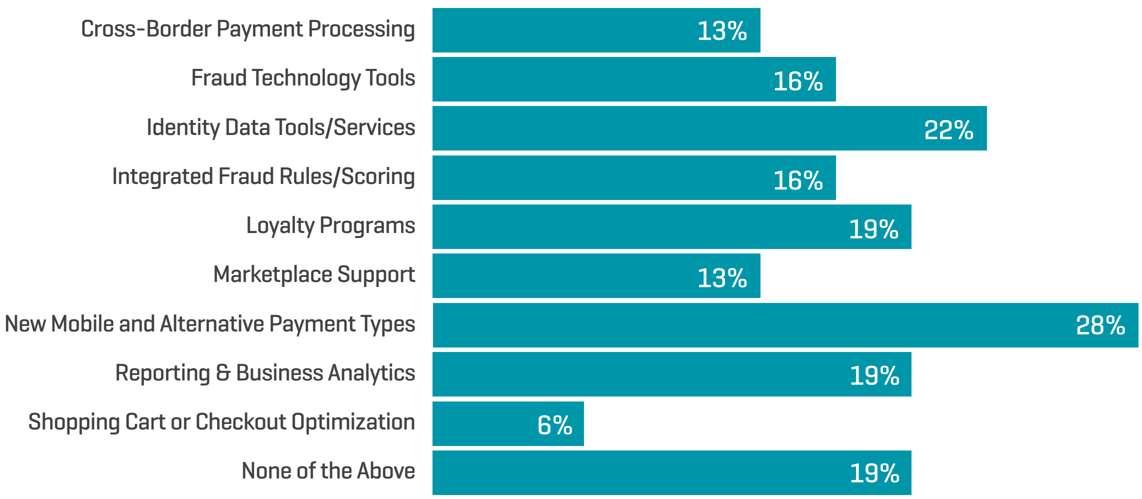


Future Support for Value-Added Services

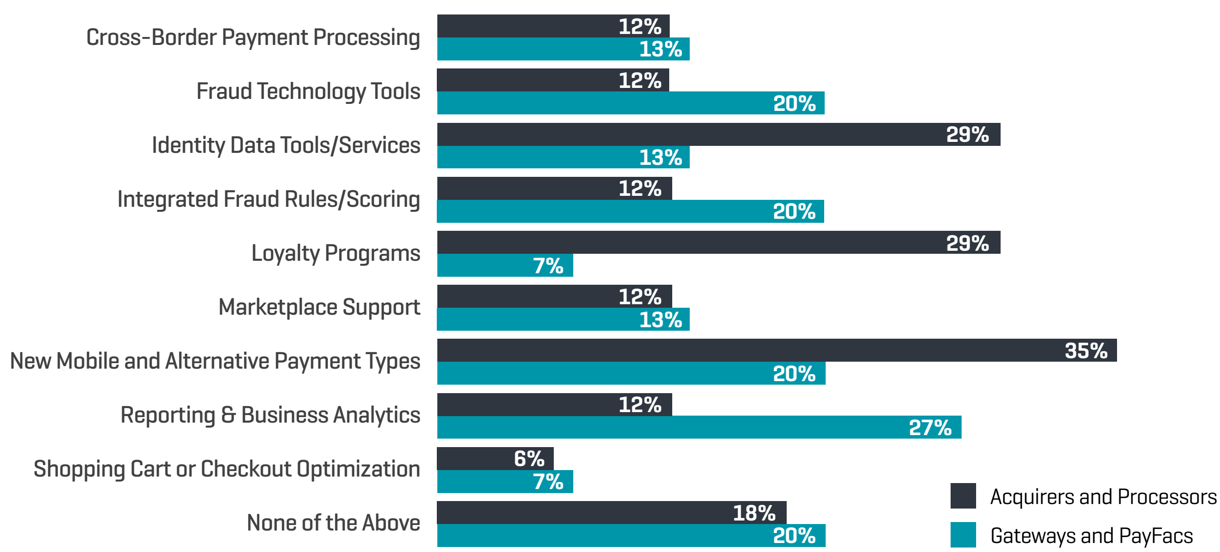
If a payment provider indicated they do not offer a given value-added service, they were later asked if they plan to add support for this service within the next year. Business reporting and analytics are something that 19 percent of payment processors not supporting today plan to add in 2018. Support for new payment types, the second most common value-added service provided today, is on the radar for 28 percent of organizations that don't already support this. The next value-added service most likely to be supported in the next year is identity data tools or services, as indicated by 22 percent of payment companies that don't currently offer these services directly or through partnership. Just ten percent of organizations surveyed offer or support identity tools and services as a value-added service today.

Less than 20 percent of organizations have no plans to add or increase support for a value-added service in the next year, while 56 percent of respondents plan to add two or more value-add services and 13 percent plan to add three. Among payment organizations not offering these value-added services, acquirers and processors are more likely than gateways or PayFacs to have plans to support new mobile and alternative payment types (35 versus 20 percent), identity tools and services (29 versus 13 percent) or loyalty programs (29 versus 7 percent) in the coming year. Payment facilitators and gateways, on the other hand, are more likely to add support for fraud technology tools and integrated rules or fraud scoring, each being added by 20 percent of gateways and PayFacs versus 12 percent of acquirers and processors.

Organizations Planning to Add These Services



Organizations Planning to Add These Services by Type

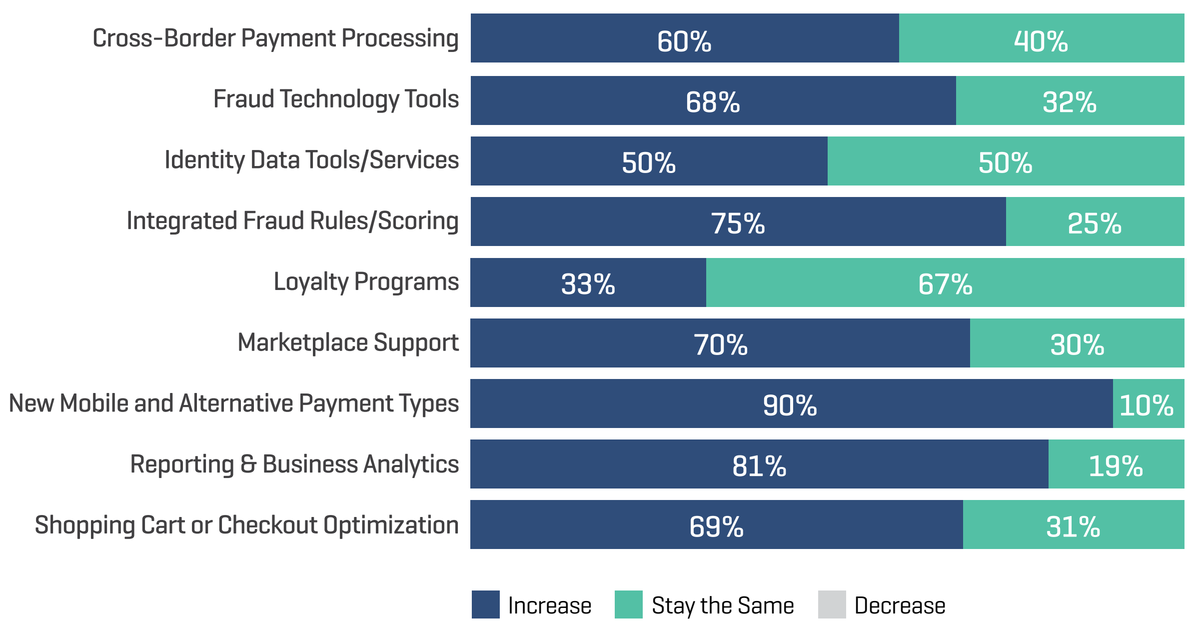


For the value-added services that payment industry organizations offer or support today, respondents were asked whether their organizations planned to increase or decrease sales and marketing efforts and overall support for each. Not a single payment industry representative surveyed said their organization had plans to decrease support for any of the value-added services they currently offer. Considering the value-added services currently supported by organizations surveyed, 72 percent will see an increase in support this year.

Underscoring the fact that the payments industry is dynamic, survey results show that 90 percent of payment processors who support new mobile and alternative payment types will be increasing support for new payment types in 2018. Reporting and business analytics, the most supported valued-added service today, is something that more than 80 percent of payment organizations plan to add or increase support for this year.

Nearly half of payment organizations support integrated risk management rules or fraud scoring and three-quarters of them plan to add or increase support for these services in 2018. Approximately 70 percent of the payment processors offering fraud technology tools, market place support and cart or checkout optimization will be increasing support for these value-added services by this year.

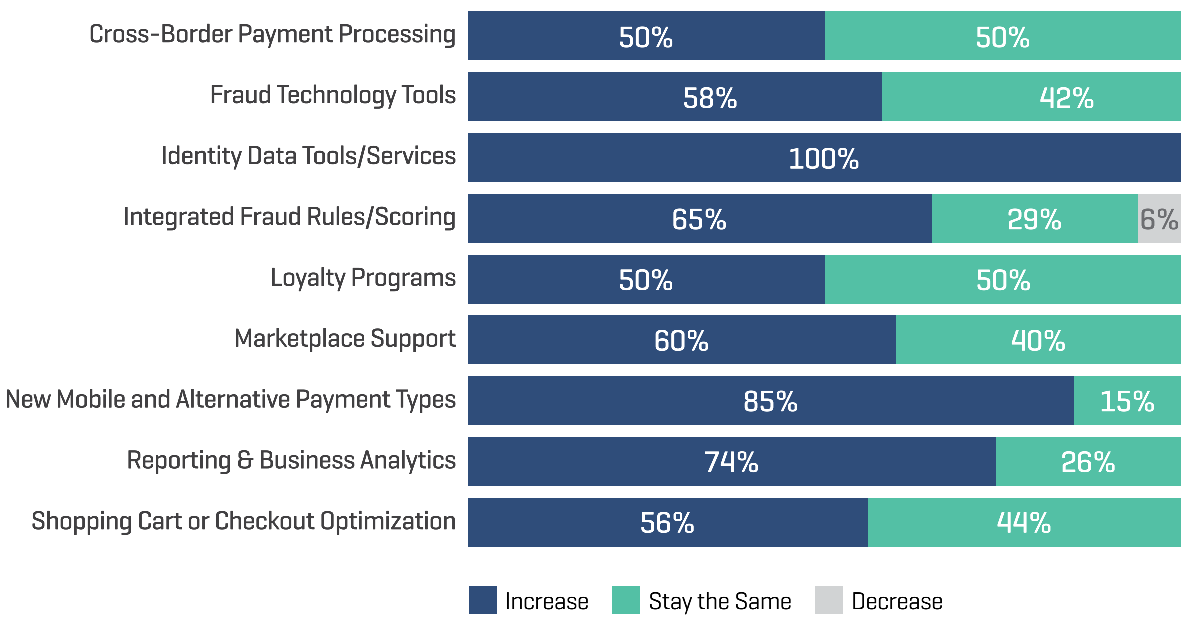
Increasing Support for Value-Added Services



The survey results were more mixed in terms of which types of value-added services would see an increase in marketing efforts and budget. Organizations who offer these services were about evenly split as to whether their marketing efforts would increase or stay the same around cross-border payment processing, loyalty programs and shopping cart or checkout optimization. More support is expected for marketplaces and fraud technology tools, as 60 percent offering these indicated they anticipate an increase in marketing efforts this year.

Although just 10 percent of organizations surveyed support identity tools and services, all who offer identity services plan to increase marketing efforts around support for this service. More than half of survey respondents, 55 percent, offer or support new mobile and alternative payment types, and among these organizations, 85 percent plan to increase marketing efforts around the mobile and alternative payment types they support, almost as many who are increasing overall support for new payment types (90 percent).

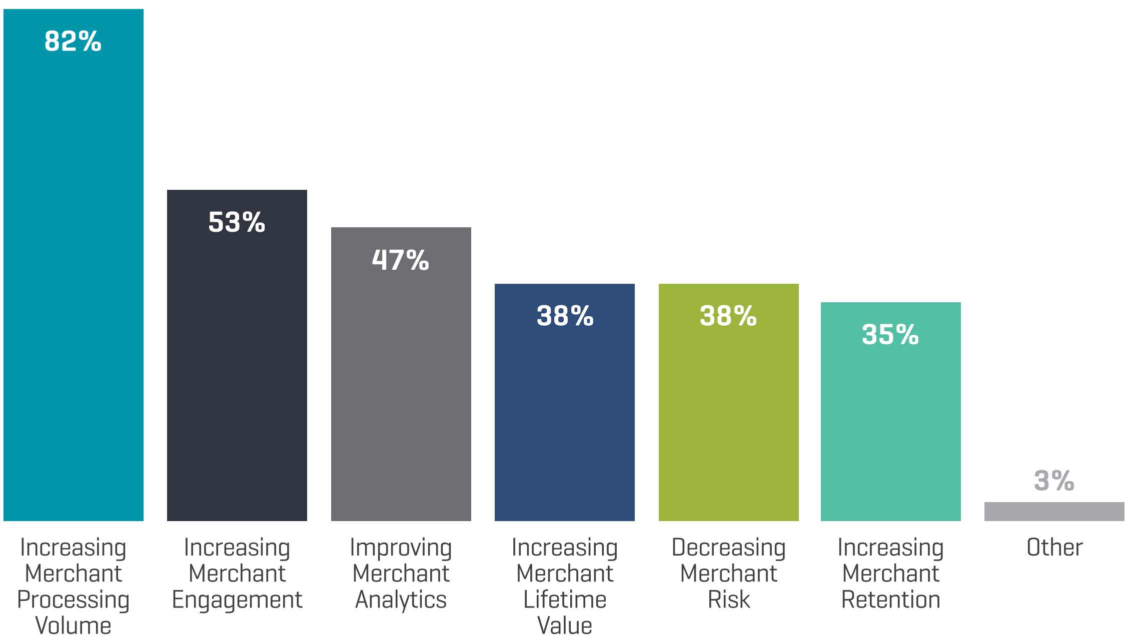
Increasing Marketing for Value-Added Services



Survey respondents were asked to pick their top three merchant initiatives for 2018. The most common response, as indicated by 82 percent of organizations, was initiatives to help their merchant clients increase processing volumes. More than half are concerned with increasing merchant engagement and nearly half seek to improve merchant analytics.

Just 38 percent of organizations say decreasing merchant risk is one of their top three initiatives this year. This is in contrast to the 60 percent of organizations that consider fraud technology tools and integrated rules or fraud scoring to be "Very Important" to their overall business strategies, and to the 73 percent of organizations currently offering fraud technology tools, integrated rules or fraud scoring who plan to increase support for these services in 2018.

Three Top Merchant Initiatives



Key Take Aways – Support for Value Added Services

- Gateways and PayFacs are more likely than acquirers and payment processors to offer value added services.
- Reporting and business analytics is the most supported Value-Added service, while about half of respondents support fraud technology tools and integrated risk management rules or fraud scoring.
- Most value-added services offered today are expected to receive more support and increased marketing efforts over the next year.

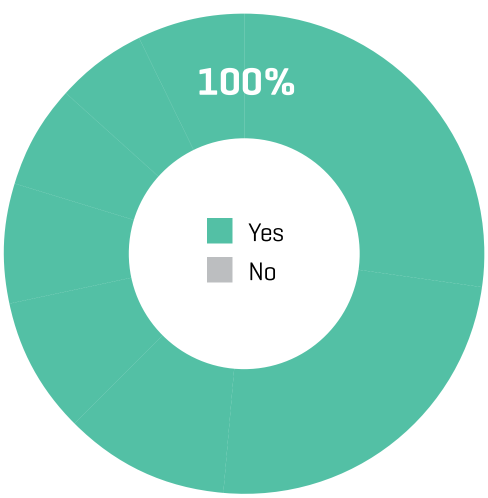
Fraud and Risk Management

Electronic payments are a significant and still growing part of the overall payments industry, making risk management a dynamic environment as well. All organizations surveyed are supporting at least one form of electronic payment, and therefore all should be concerned with fraud and risk management. Another major focus of the State of Payment Processing & Fraud Survey and the 2018 inaugural report is to understand fraud and risk management from the payment industry stakeholder's perspective. Specifically, what challenges the payment industry faces in terms of fraud – directly and with their merchant clients – as well as how fraud and risk management services are offered or supported by these organizations as value-added services.

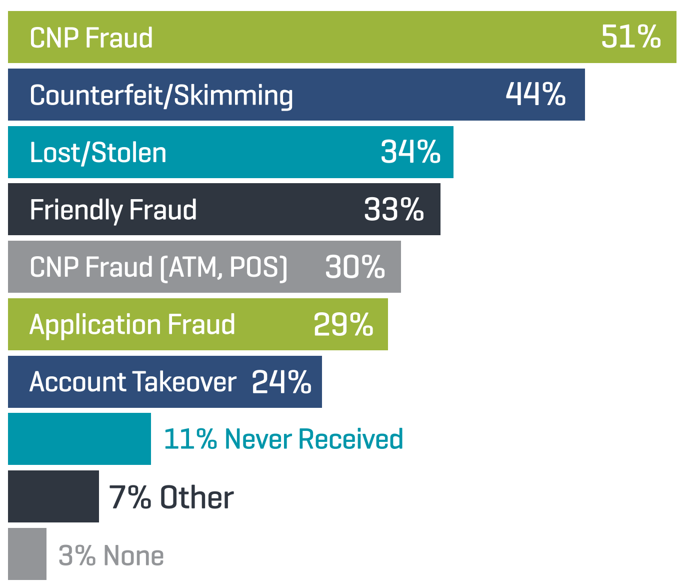
Challenges Payment Processors Face

Simply put, fraud mitigation and risk management are challenges for nearly all organizations operating in the CNP channel, and 100 percent of respondents indicated that fraud prevention is top of mind and a critical concern for their organization. Payment industry participants were asked to list each of the specific challenges facing their organization in terms of fraud with more than half citing CNP channel fraud as difficult. Approximately one-third of payment processors are concerned with friendly fraud and how it impacts their merchant clients, while about one-in-four consider account takeover a challenge to their organization. About 64 percent of payment industry organizations surveyed listed two or more challenges they face related to fraud and risk management, and about half cited three or more specific fraud challenges.

Is Fraud Prevention a Top Concern?



Fraud Challenges for Payment Processors

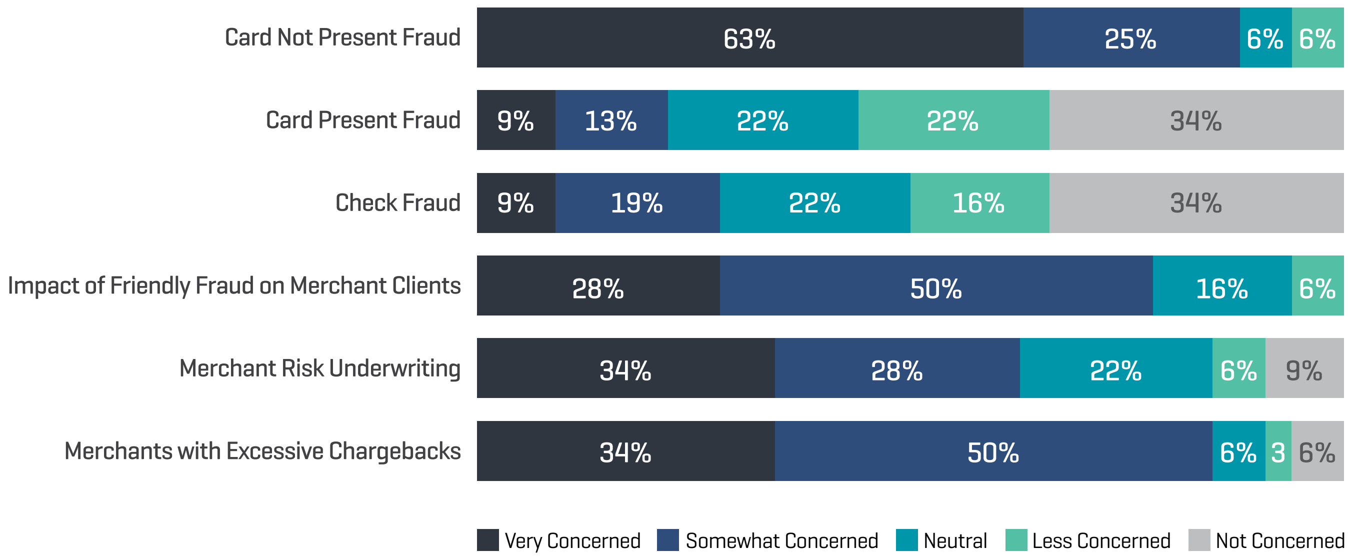


Payment industry organizations were also asked how concerned they were with different types of fraud and fraud in different channels. Card Not Present fraud rose to the top as nearly two-thirds of survey respondents indicated they are "Very Concerned" with merchant fraud risk in the CNP channel. Supporting this, 88 percent of respondents are at least "Somewhat Concerned" while just 6 percent are "Not Concerned" with CNP fraud. While more than one-third of organizations report they are not concerned with merchant risk as it pertains to card present channel and check fraud, this primarily includes organizations that focus on the eCommerce and mobile channels only.

Following CNP channel fraud, merchant risk payment processors are most likely to be "Very Concerned" with excessive chargebacks (34 percent) and merchants suffering from friendly fraud (28 percent). Nearly 85 percent of organizations consider chargeback risk at least "Somewhat Important."

Although all types of payment industry organizations are most concerned with CNP channel fraud when it comes to their merchant portfolio and risk exposure, 73 percent of payment gateways and PayFacs are "Very Concerned" with CNP fraud compared to 53 percent of acquirers and payment processors. Payment gateways and facilitators are also more concerned with merchants who may be dealing with excessive chargebacks (40 percent) and friendly fraud (33 percent) compared to acquirers and processors (29 and 24 percent).

Most Concerning Merchant Fraud Risks



Fraud Prevention as a Value-Added Service

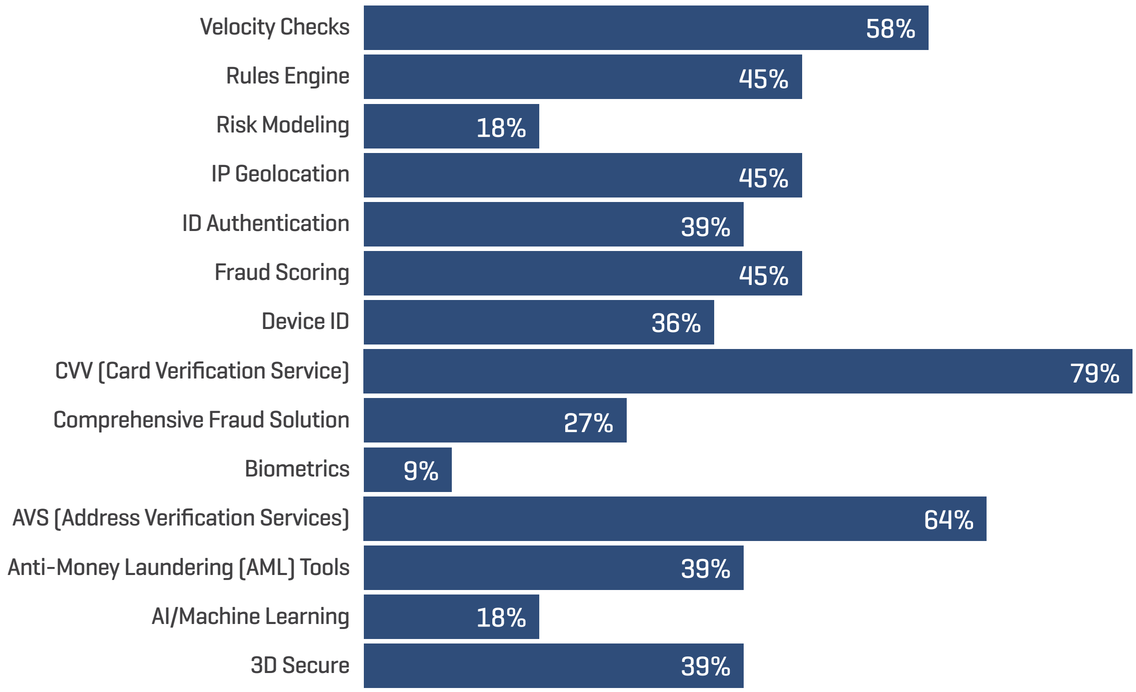
There are many types of value-added services that payment processors can offer, ranging from cross-border and alternative payments to a multitude of fraud and risk management controls, through analytics, reporting and other features to support sales optimization. Within each of these groups there is a large degree of variation in the specific types and levels of service each payment industry organization provides.

More than half of all survey respondents represent payment organizations that offer some fraud or risk management capabilities as a value-added service, including 53 percent that support fraud technology tools, 48 percent who offer fraud scoring or integrated rules and 10 percent who provide identity tools or services. About 25 percent of these organizations provide these value-added services entirely in-house while the remaining either offer them through partners or a combination of in-house and third-party services.

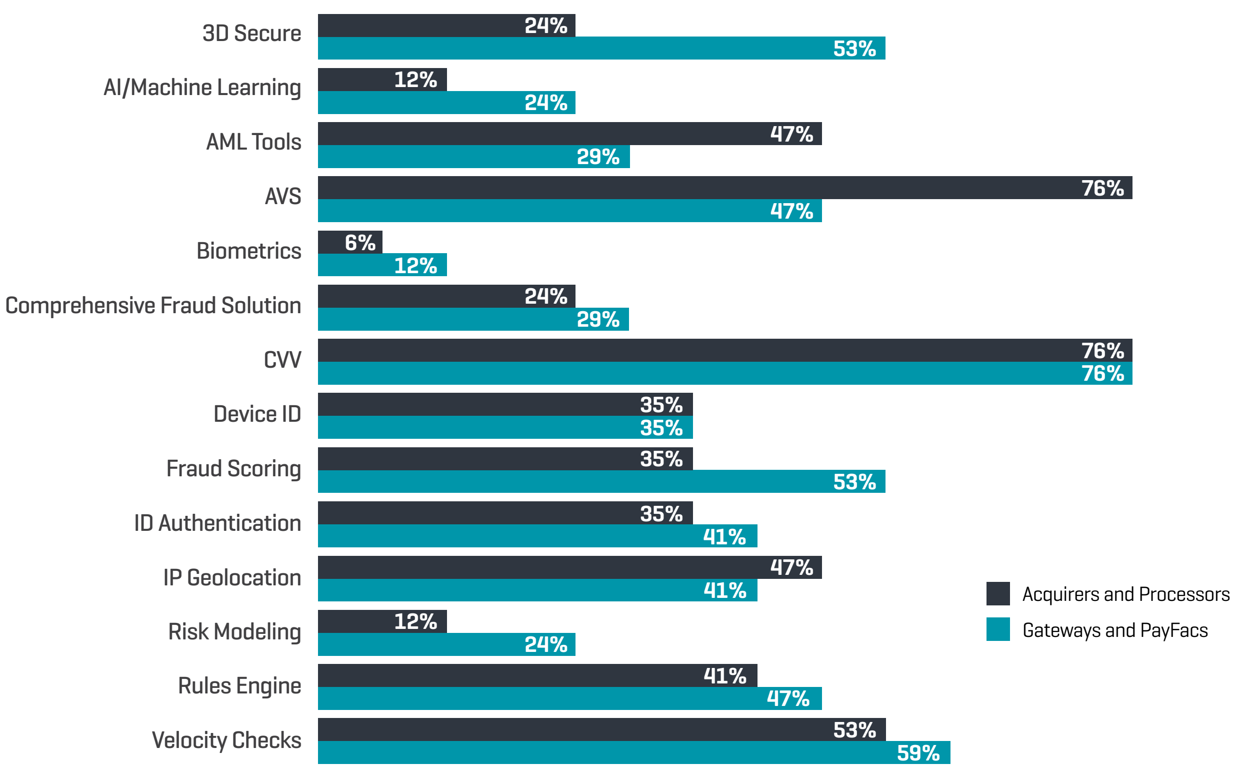
The State of Payment Processing & Fraud Survey went into further detail about the specific fraud and risk management services payment processors support today, with the most common being basic AVS (Address Verification Services) and CVV (Card Verification Value) checks. Velocity checks are the only other risk management technique supported by more than half of payment processors, at 58 percent. Fraud scoring, IP geolocation and rules engines are each offered by 45 percent of payment processors and there are ten different risk management tools or services supported by at least one-third of payment industry organizations surveyed.

Broken down by type of payment organization, gateways and PayFacs were considerably more likely than acquirers and processors to support 3D Secure programs like Verified by Visa and MasterCard SecureCode (53 versus 24 percent), and fraud scoring (53 versus 35 percent). Both groups were about equally as likely to offer or support device identification, rules engines, velocity checks and IP geolocation.

Fraud Services Offered by Payment Processors



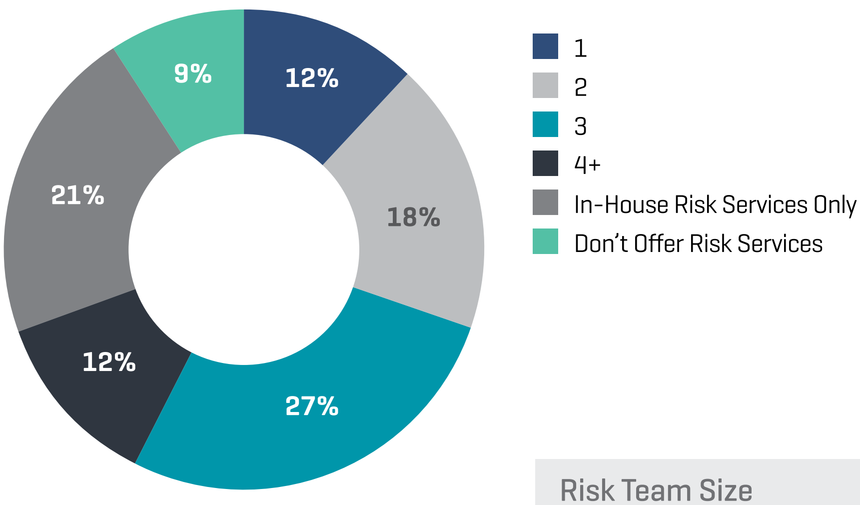
Fraud Services Offered by Payment Processors by Type of Organization



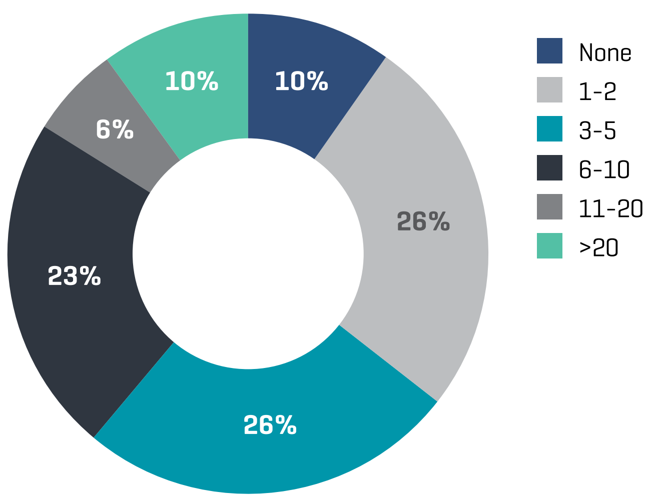
In terms of how risk management and fraud prevention is provided as a value-added service, 21 percent of organizations are supporting this entirely in-house, while 70 percent go through a third-party provider and 58 percent have multiple industry partners (9 percent do not offer risk services). This includes nearly 40 percent of organizations with three or more industry partners to offer fraud and risk management services for their merchant clients.

Whether they don't offer risk management value-added services or do so entirely through partners, ten percent of payment organizations do not have internal risk teams. More than half of those surveyed reported their organization has risk management teams between one and five people, while 16 percent have risk teams of more than ten people.

Number of Fraud Vendor Partners



Risk Team Size

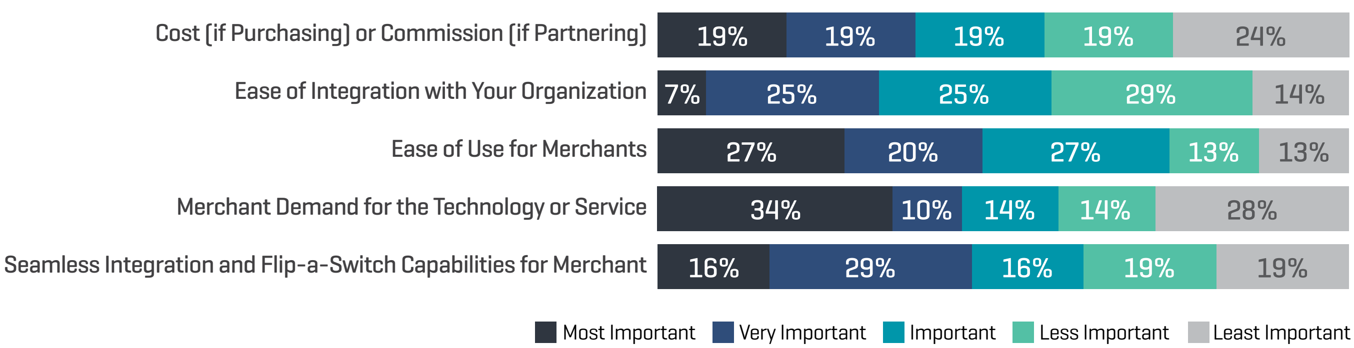


There are many reasons why payment-focused service providers consider partnering with fraud solution vendors to offer value-added services to their merchant clients, including helping merchants accept more sales, reducing merchant fraud risk exposure and increasing merchant retention.

Payment industry organizations were asked to rank five considerations when selecting industry partners for risk management services, from most important to least important. The top three factors when selecting a third-party fraud solution are the ease of use of the service for their merchant clients (47 percent), rapid integration or "flip-a-switch" ability to turn the service on for merchant clients (45 percent), and merchant demand for the service (44 percent).

Payment processors, gateways and PayFacs are more concerned with their merchant clients' well-being than their own when it comes to these priorities. Just 7 percent of organizations said the ease or difficulty of integrating a third-party service within their own organization is the most important factor when considering industry partners.

Most Important Factors When Considering Fraud Vendors for Partnerships



Key Take Aways – Fraud and Risk Management

- All respondents say that fraud prevention is a top concern in general, while 51 percent specifically mention CNP channel fraud as a challenge, one-third cite friendly fraud and one-quarter say list account takeover as challenges to their organizations.

- Nearly 60 percent of payment organizations surveyed offer velocity checks and there are three risk management tools or techniques offered by nearly half: IP geolocation, rules engines and fraud scoring.

- When considering who to partner with to offer value-added services payment organizations care most about the ease of use for their merchant clients, how quickly and easily their clients can start using it and what specific technology or tools their clients demand.

Significance of Offering Value-Added Services

The 2018 State of Payment Processing & Fraud Survey was in part developed to understand which value-added services industry stakeholders consider most important. This portion of the survey examined what was considered most critical in terms of attracting and keeping new merchant clients, as well as attempting to measure the benefits of offering value-added services and understanding which of these benefits payment industry organizations care most about.

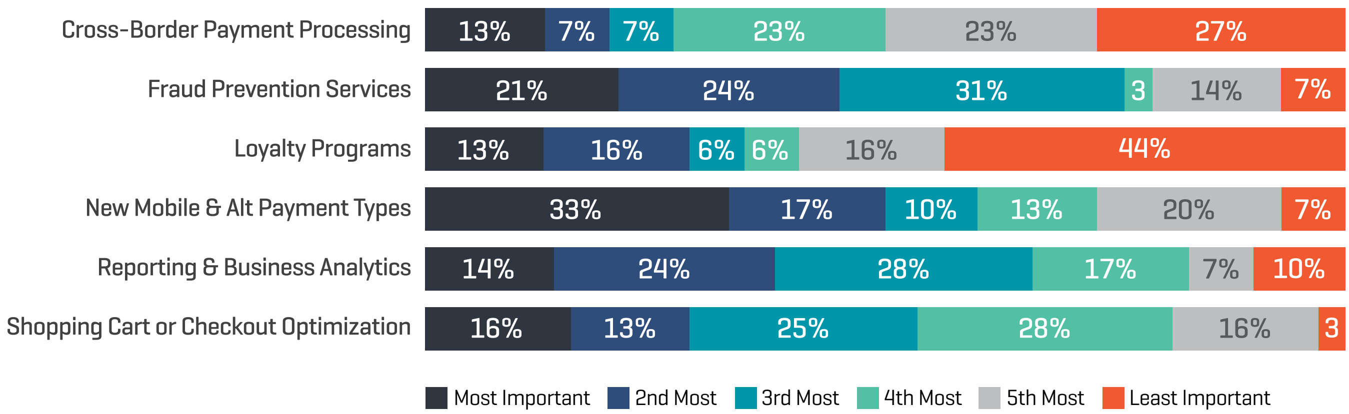
The Most Important Value-Added Services

Valued-added services were broken down into six different groups, some of which are offered by more than half, others by 10 to 25 percent of all payment organizations surveyed. Regardless of whether an organization offers each of these value-added services, they were asked to rank each from most to least important in terms of attracting merchant clients and improving merchant retention.

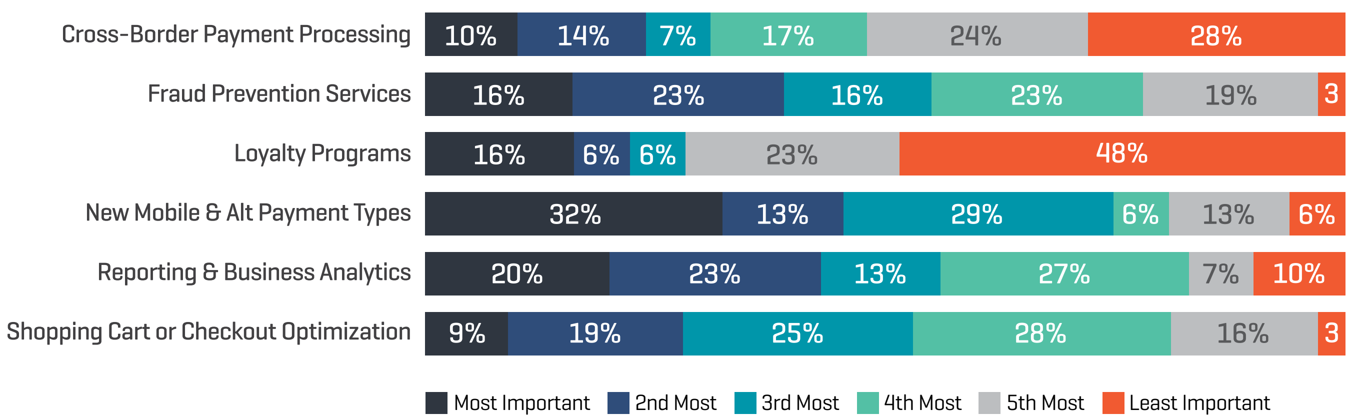
When it comes to attracting new merchant clients, half of payment organizations say offering new alternative and mobile payment types is one of the two most important valued-added services to offer, while one-third consider this the single most important. Offering fraud prevention is the next value-added service most likely to be considered the most important (21 percent) or at least the second-most important (45 percent). Many payment organizations, 44 percent, consider loyalty programs the least important value-added service to offer in terms of attracting new merchant clients. Just 7 percent consider fraud prevention or new mobile and alternative payment types to be the least important value-added service. Gateways and payment facilitators are more likely to place higher importance on new payment types than acquirers and processors.

With respect to merchant client retention, there is equally as much significance placed on supporting new mobile and alternative payment types as 55 percent say this is either the most or second-most important value-added service to support and about one-third say it is the most important. Reporting and business analytics outranks fraud prevention as the second most important value-added service in terms of merchant retention. One-in-five payment organizations consider reporting and business analytics the most important and 43 percent say it is at least the second-most important in terms of merchant client retention. Fraud prevention services are considered one of the top two most important by 39 percent and most important by 16 percent.

Most Important Value-Add Services for Attracting New Clients



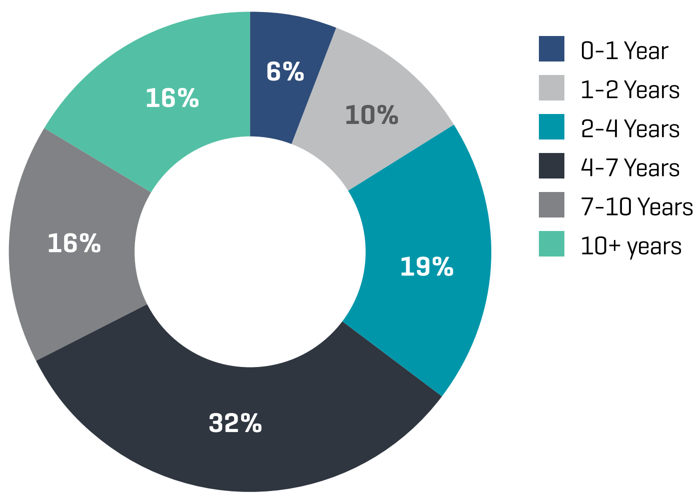
Most Important Value-Add Services for Client Retention



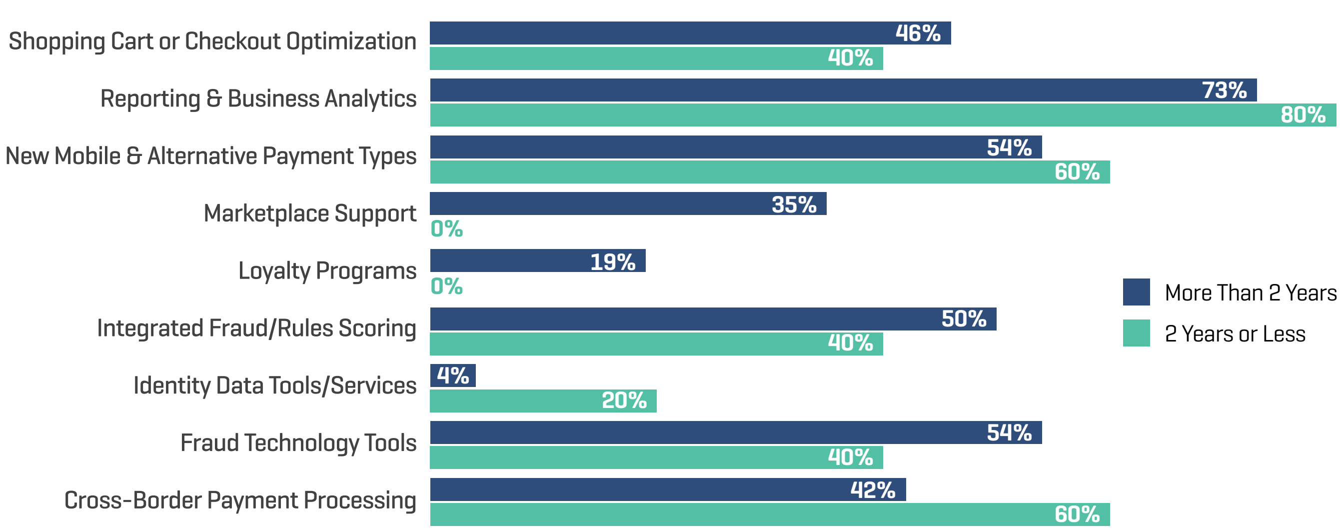
Among payment industry organizations surveyed, most reported strong average merchant client retention. Just 16 percent reported an average client lifespan of less than two years, compared to two-thirds reporting an average length of retention of at least four years. Nearly one-third have an average merchant retention of seven years or more.

Payment organizations that have an average merchant retention length of at least two years are more likely to support fraud technology tools (54 versus 40 percent) and integrated rules or fraud scoring (50 versus 40 percent) than those with average retention rates of two years or less. Organizations with longer average merchant client retention are also more likely to support checkout or shopping cart optimization, market place support and loyalty programs. Marketplace support and loyalty programs are only offered by the largest payment organizations by processing volume, which have longer average client retention rates as well (because they have been in business for so many years).

Average Merchant Retention



Types of Valued Added Services Offered by Average Merchant Retention



Benefits of Offering Value-Added Services

Most organizations surveyed offer or support at least one value-added service, and more than half support multiple. Regardless of which value-added services they support, payment industry companies were asked whether doing so has made it easier to attract new processing clients and if it has improved retention. Results from The State of Payment Processing & Fraud Survey were overwhelmingly positive.

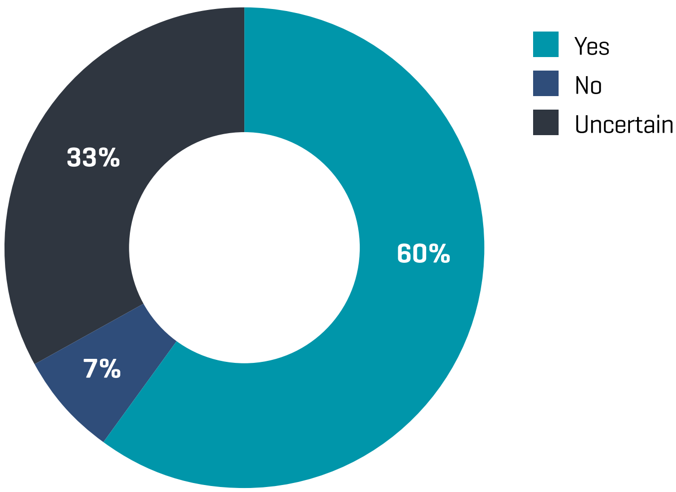
Nearly two-thirds, 60 percent, of payment industry organizations who offer at least one value-added service, definitively say that "Yes," providing value-added services improves merchant client retention, and nearly as many say it helps attract new merchant clients. Just 7 to 10 percent say offering value-added services does not help in both aspects, while one-third are just uncertain. The large share of respondents reporting they are uncertain is likely because the benefits and impacts are difficult to directly measure, and many organizations who have only offered such services a short time think it's too early to tell.

Payment organizations were then asked to consider whether offering value-added services were beneficial in terms of attracting, signing and retaining existing merchant clients by the specific types of value-added services they offer. The intent was to discover which types of services might yield the best results based on reported improvements in each of these areas.

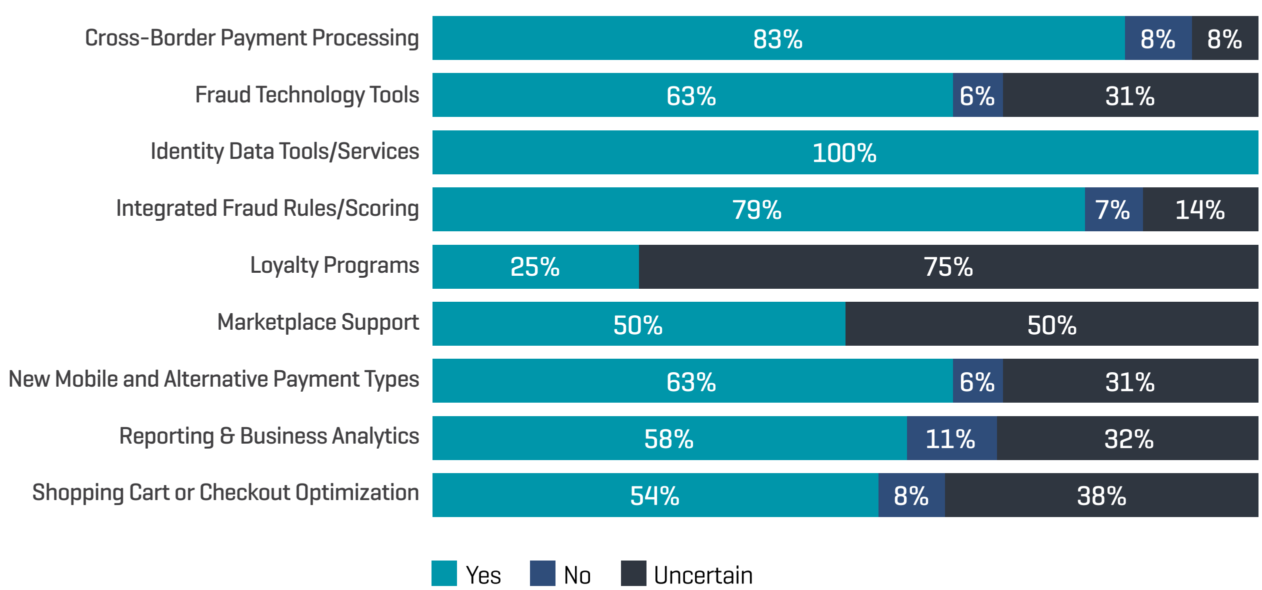
In terms of merchant client retention, 100 percent of payment organizations offering identity data tools or services say that offering value-added services improved client retention, while 83 percent of those who support cross-border payments and 79 percent who offer integrated rules or fraud scoring say these have improved retention as well. Organizations offering fraud technology tools or who support new mobile and alternative payment types are the next most likely to say the value-added services they provide have improved merchant retention, as indicated by 63 percent. The only value-added service where less than half of organizations said "Yes," that offering these services has increased retention, is support for loyalty programs.

In terms of offering value-added services and their ability to attract new merchant clients, results are similar with a few key differences. Support for cross-border payments (83 percent) and integrated risk management rules or fraud scoring (86 percent) are the two value-added services recognized for improving the ability to attract new clients. Organizations surveyed who offer fraud technology tools or services are even more likely to report a positive impact on attracting new clients (75 percent) than retaining them (63 percent). All who offer loyalty programs are uncertain about the impact these services have on attracting new clients, while two-thirds of organizations who offer identity services say it helps attract new clients. Business reporting and analytics, although the most commonly supported value-added service and considered important amongst payment organizations, is the most likely to be associated with companies who say value-added services did not provide benefits in terms of attracting new merchant clients.

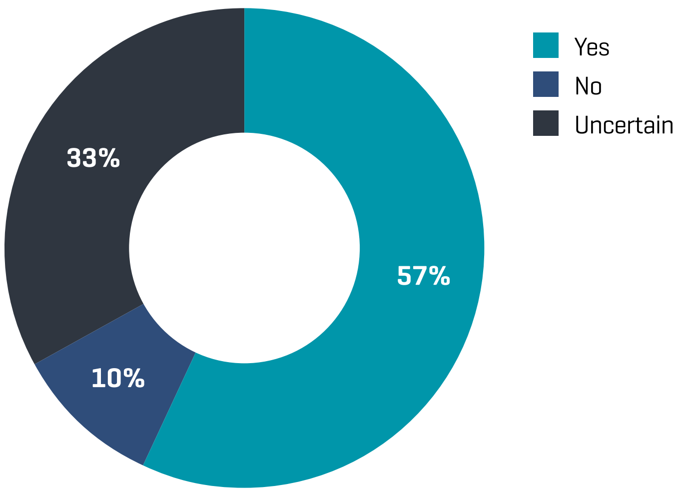
Has Offering Risk Management Services Improved Client Retention?



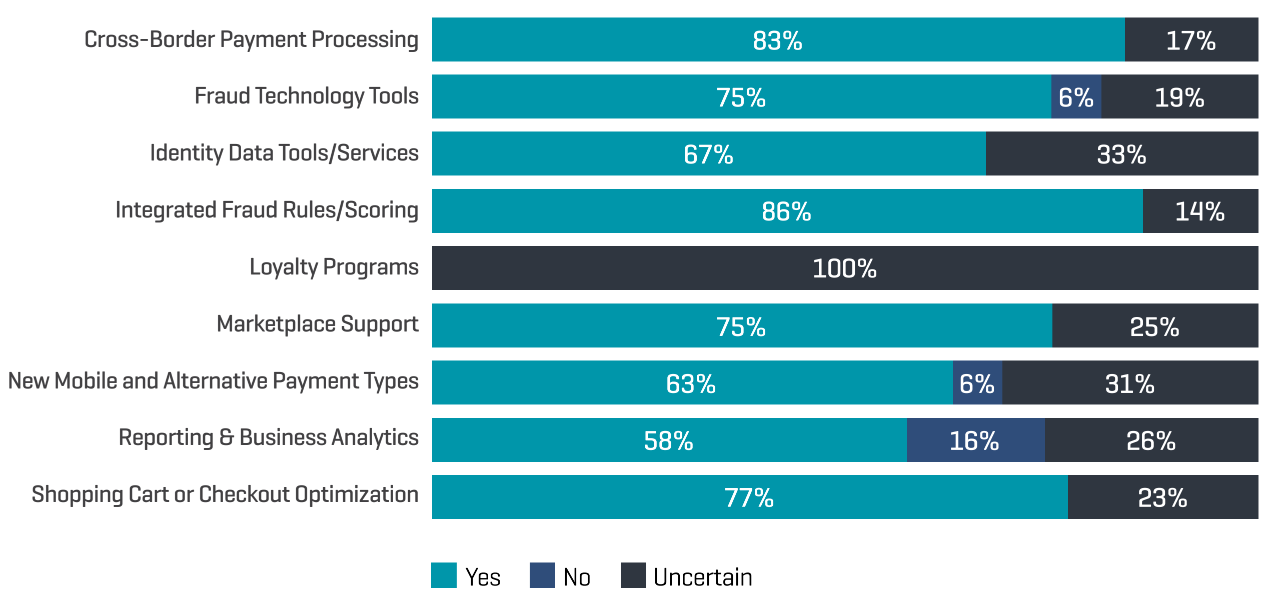
Has Offering Risk Management Services Improved Client Retention? By Types of Value-Added Services Offered



Has Offering Risk Management Services Made It Easier to Attract New Clients?



Has Offering Risk Management Services Improved Client Retention? By Types of Value-Added Services Offered



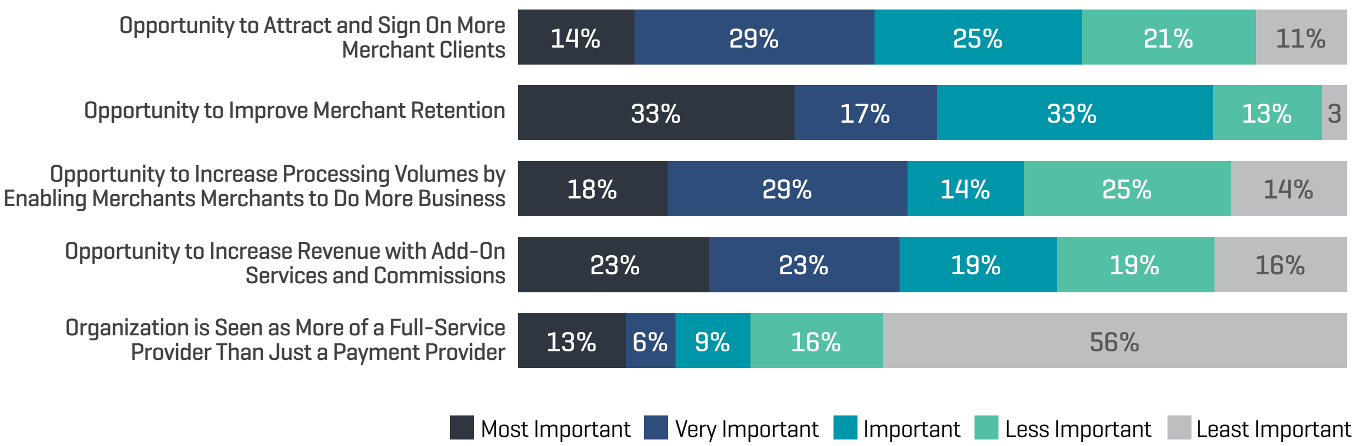
Finally, as part of The 2018 State of Payment Processing & Fraud Survey, respondents were asked to rank five benefits of offering value-added services to their merchant client-base. These benefits include the opportunity to:

- Attract and sign new merchant clients (which 57 percent say value-added services do)
- Improve merchant retention (which 60 percent say value-added services do)
- Enable merchants to do more business and therefore grow processing volumes
- Offer add-on services that provide additional revenue opportunities
- Be seen as a full-service provider rather than just a payment service provider

Each of these benefits are helpful to payment organizations that offer or support ancillary and value-added services, and results are somewhat mixed. Payment organizations are most likely to consider improving merchant retention the most important of these five benefits, as indicated by one-third of survey respondents. Half of respondents consider this one of the top two most important benefits of offering value-added services, while 47 percent consider the opportunity to grow processing volume by fostering that of their client's and 46 percent say new revenue opportunities are one of the two most important benefits.

The benefit payment organizations find least meaningful is being seen as a full-service provider rather than just a payments company. More than half of respondents, 56 percent, said this is the least important of the five benefits of offering value-added services. Although payment processors, gateways, facilitators, acquirers and issuing banks have made it clear that offering an array of value-added services is critical to their business strategy and success, being recognized as a full-service provider is not as important.

Ranking Benefits of Offering Valued-Added Services



Key Takeaways – Significance of Offering Valued-Added Services

- The ability to offer merchants new payment types and fraud prevention are the two most critical features for attracting new clients.
- The average length of merchant retention is at least four years for 64 percent of payment organizations surveyed, while those with longer retention rates are more likely to offer fraud technology tools and integrated rules or fraud scoring.
- Facilitating cross-border payments, offering fraud technology tools and integrated rules or fraud scoring are three of the value-added services payment organizations are most likely to say have improved their ability to both attract and retain merchant clients.

Conclusion

Nearly all payment processors, acquirers, gateways and PayFacs, 97 percent, support value-added services, with reporting and business analytics, new mobile and alternative payment types and fraud technology tools each being offered or supported by more than half of those surveyed. Nearly as many payment organizations offer integrated risk management rules or fraud scoring (48 percent), while 45 percent support cross-border payment processing, to round out the top five most offered value-added services today.

The State of Payment Processing & Fraud: 2018 Inaugural Survey & Report shows that payment gateways and facilitators, or PayFacs, must compete more in terms of value-added services, as there are five different services supported by more than half of these organizations. This is compared to just two value-added services supported by more than half of all acquirers and payment processors. Gateways and PayFacs are also more likely to indicate value-added services are “Very Important” to their overall business strategies.

Terms

Payment Organizations – Group collectively referring to all processors, acquirers, gateways, PayFacs and issuers that participated in the study.

Fraud Technology Tools – eCommerce technology-based point tools providing specific signals that give insight into the level of risk associated with an order or user. Examples include IP Geolocation, Device Identification and Proxy Detection.

Identity Tools / Services – Automated or manual reverse lookup and other identity authentication or verification related checks or services used to validate users or transactions.

Integrated Fraud Rules – Providing the ability for merchants to create custom business rules that can be executed on live transactions to risk decisions based on multiple risk factors.

Risk Scoring – Multi-merchant rules or models providing merchants a numerical representation of the level risk, allowing them to set custom thresholds for when to approve, review or deny an order attempt.

Fraud or Risk Management Services – In the context of value-added services, this refers to offering any of the above four terms: Fraud Technology Tools, Identity Tools/Services, Integrated Fraud Rules or Risk Scoring.

About Kount

Kount helps businesses boost sales by reducing fraud. Our all-in-one, SaaS platform simplifies fraud detection by applying patented machine learning through Kount's proprietary platform offering maximum protection for some of the world's best-known brands. Companies using Kount accept more orders from more people in more places than ever before. For more information about Kount, please visit www.kount.com.

About The Fraud Practice

The Fraud Practice, Inc. is a privately held US corporation based in Sarasota, Florida. The Fraud Practice provides consulting services, training, and research on eCommerce payments, fraud prevention and credit granting. Businesses throughout the world rely on The Fraud Practice to help them build and manage their fraud and risk prevention strategies. For more information about The Fraud Practice, please visit www.fraudpractice.com. For more information about our online training and Certification programs, please also visit www.CNPtraining.com.