Fee Income Growth Opportunities in the Identity Protection Market

Provided by Harland Clarke and Javelin Strategy & Research
(Updated February 2011)

Introduction

Identity fraud has become a problem of increasing concern among consumers and businesses. According to Javelin Strategy & Research, 8.9 million U.S. adults became victims of identity fraud in 2010. The overall incidence rate of 3.5% has resulted in a total fraud amount of $37 billion, a decrease of $19 billion from 2009. This total amount represents the face value of the crime — essentially, what the criminals are able to get away with. Meanwhile, consumer costs, or the average out-of-pocket dollar amount victims pay, increased in 2010 reversing a downward trend in recent years. This increase can be attributed to new account fraud, which showed longer periods of misuse and detection and therefore more dollar losses associated with it than any other type of fraud. Identity fraud continues to be a billion-dollar problem, fueled by an increasingly global and specialized criminal enterprise.

In response to fraud victimization and greater awareness of identity fraud, many consumers have demonstrated interest in identity protection products, with millions of users subscribing to credit monitoring, personal information monitoring, and the like. The market for identity protection services is thus poised for growth, especially with the incidence of identity fraud having increased in recent years. Seventy-four percent of consumers do not currently subscribe to any identity protection services, presenting a tremendous opportunity for providers.[1] Among those who do subscribe, more than half of subscribers utilize a fee-based service, with 87% paying between $5 and less than $15 per month.[2]

The identity protection industry has experienced tremendous expansion, development and interest from players in the financial services space who have a vested interest in consumer security. While the market for identity protection services will continue to be lucrative, financial institutions stand to gain the most traction among security-concerned consumers as trusted providers of fraud protection.

Unless otherwise noted, all figures on identity fraud are provided by Javelin's 2011 Identity Fraud Survey Report. A nationally representative sample of 5,004 U.S. adults, including 470 fraud victims, was surveyed via a 50-question phone interview, providing comprehensive insight into this crime and the effects on its victims.

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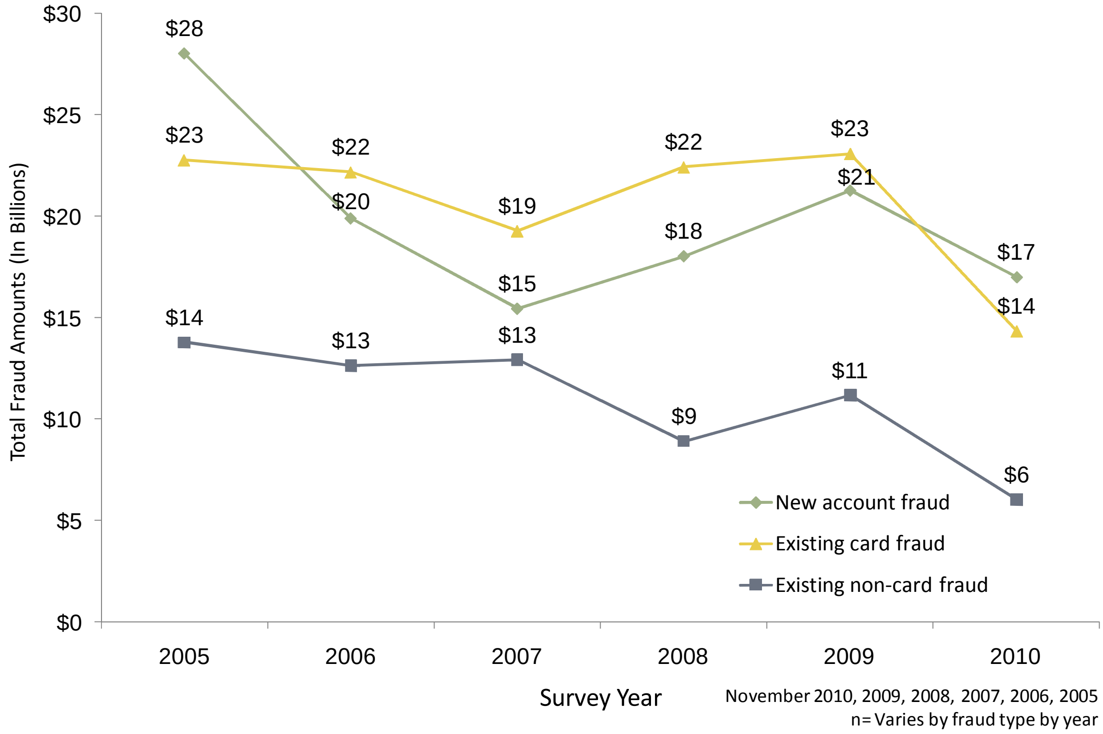
[1] 2010 Annual Household Finance Survey, Javelin Strategy & Research.

[2] 2010 Annual Household Finance Survey, Javelin Strategy & Research.

Trends in Identity Fraud: New Accounts Fraud Losses Take the Lead

Total Fraud Amounts by Fraud Type, 2003 – 2010



November 2010, 2009, 2008, 2007, 2006, 2005
n= Varies by fraud type by year
Base: New account fraud victims, existing card fraud victims, existing non-card fraud victims.
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Q29: What is the approximate total dollar value of what the person obtained while misusing your information?

New account fraud is the most pernicious type of fraud, and the very fraud type that identity protection services are designed to mitigate. This year revealed that new account fraud is responsible for more dollar losses (46%) than existing card fraud (38%) and existing non-card fraud (16%). The elevated amount of new account fraud losses may be linked to higher consumer costs in 2010. With new account fraud being the most difficult fraud type to detect, the duration of misuse continues for longer periods of time, leading to greater losses and severe victim impact.

Theft of Social Security numbers (SSNs) (29% of victims reported having their SSN stolen in 2010) — the single most valuable piece of information coveted by criminals — still remains one of the top thefts for critical data. The loss of SSNs is particularly devastating to identity fraud victims. This is because they can be used to open fraudulent new accounts, which are very difficult to detect without access to a credit report, credit monitoring service, or other type of personal information monitoring service. Compared with existing accounts fraud, which is detected more quickly and easily, new account fraud can be very damaging both financially and emotionally to victims since the fraud will go on undetected for longer periods of time.

State of the Industry: Changes Continue to Affect the Market

There remains a lot of innovation within the identity protection space — as credit bureaus continue to emphasize their different "levels" of credit monitoring services, third parties are beginning to specialize in personal identity fraud monitoring, and financial institutions are enhancing their traditional credit monitoring packages with internet surveillance or personal information monitoring. During the past year, a few companies have shown some interest in medical identity fraud protection and partnerships with traditional security companies. Below are several emerging trends that financial institutions should take note of when considering how they might approach their own product strategy for identity protection.

Financial institutions leveraging identity protection services for customer acquisition/retention

Historically, financial institution-provided identity protection offerings have not been directly tied to bank accounts. While some of the larger financial institutions are resellers of credit monitoring services, the consumer relationship ultimately belongs to the credit bureau or provider of the identity protection service being offered through the financial institution's website. Recently, however, some financial institutions have begun embedding security offerings and services into customer account plans either as a complimentary value-added service or for an added monthly service fee. Other financial institutions have begun incorporating identity protection services into basic financial account offerings to enhance overall account value, as well as to position these security services in an acquisition and retention strategy.

For example, KeyBank's Key Coverage Checking Account is a checking account package that includes credit monitoring in addition to standard checking account benefits such as free online banking. In addition, BBVA's CompassPlus package offers identity theft insurance with fraud resolution assistance, plus free checks and other features.

With recent regulations eliminating automatic overdraft fees, banks are considering new ways to add value to checking account products. Financial institutions are responding to recent regulatory changes and impending legislation to leverage products such as identity protection to acquire new account holders and retain existing accounts to offset losses.

Independent vendors continue to enter the identity protection space

The pace at which new players have been entering the identity protection market has slowed down to some extent in recent years, although some independent vendors have managed to hold their ground. The industry was disrupted when vendor-placed credit fraud alerts were ruled to be against public policy in a lawsuit involving one of the credit bureaus and an independent provider of fraud alerts. As trusted entities, financial institutions will continue to maintain an advantage over standalone companies, with consumers preferring to look to their banks for protection of their financial assets.

Incorporating personal finance management into identity protection

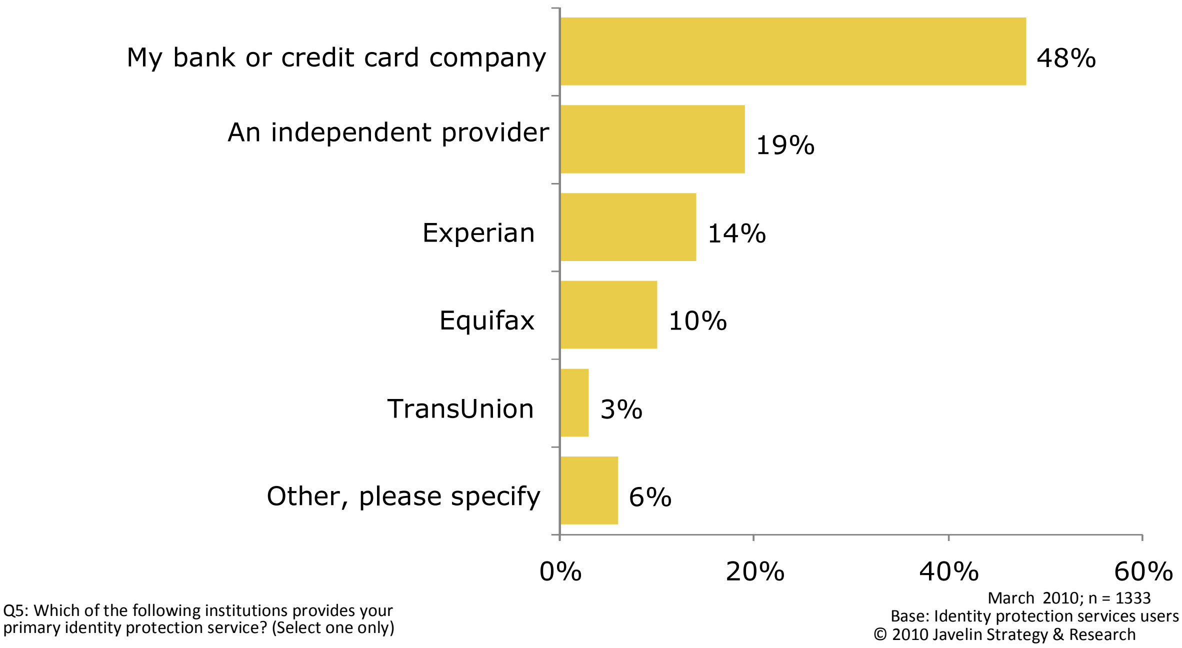
In addition to providing credit monitoring tools, some services provide a window into financial management by offering FICO scores and other tools to monitor your credit-to-debt ratio. In the absence of providing actual FICO scores, identity fraud protection services allow customers to take the data from their credit report and run scenarios to forecast the credit score impact of certain actions, such as eliminating credit or adding a car loan.

Consumers Prefer to Receive Identity Protection From Their Financial Institutions

Nearly one in two identity protection subscribers are obtaining their service from a bank or credit card company, while only 27% are subscribing to credit monitoring services through one of the three big credit bureaus.[3] Despite having less of an identity protection brand presence and shying away from embarking upon aggressive advertising or promotional efforts, financial institutions are taking the lead as the most common provider of identity protection. It makes sense that consumers look to their financial institutions and issuers to protect them against identity fraud. Despite the fact that the overall financial services industry has received some negative backlash because of the recent financial crisis, consumers still regard their primary financial services providers as trusted entities. Financial institutions are already doing an excellent job of safeguarding existing financial accounts, and would therefore be a natural consideration for providing secure protection against new accounts fraud. Therefore, financial institutions are uniquely positioned to maintain a leading edge among other market players, as security-concerned consumers draw upon already established relationships with their financial institutions.

[3] 2010 Consumer Survey, Javelin Strategy & Research.

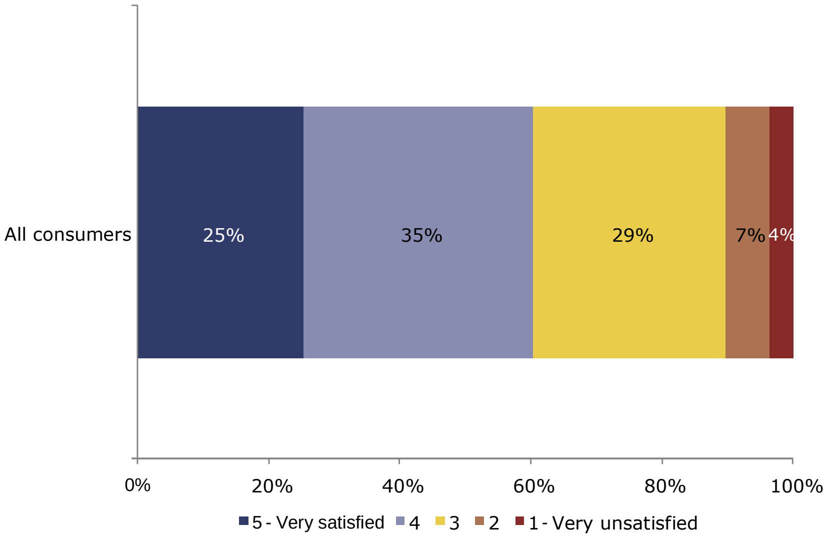
Where are Consumers Obtaining Identity Protection Services?



Overall satisfaction across all identity protection product categories is slightly lower than expected. Approximately six out of ten customers are satisfied with their current identity protection services, 29% are on the fence, and 11% are not satisfied at all.[4] Because lower satisfaction will directly impact retention rates, service providers must effectively communicate the long-term value of these products to their customers. Financial institutions have been addressing the value proposition by enhancing their traditional, "vanilla" credit monitoring products and incorporating financial management tools, internet surveillance, and other information monitoring features. Fear-inducing advertising may work initially with customer acquisition, but providers must successfully deliver on value and a meaningful user experience in order to retain customers.

[4] 2010 Consumer Survey, Javelin Strategy & Research.

Satisfaction Rates Directly Impact Retention Rates



Q7: How would you rate your satisfaction with your current identity protection service(s)?

March 2010, n= 1,376
Base: All consumers that have identity protection services.
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Satisfaction can also be negatively impacted by an actual fraud incident. Most providers offer either third-party insurance or a service guarantee to help victims recover their costs in the event of an identity fraud. When a fraud does occur, consumers rely on insurance to help mitigate the impact of the crime, in terms of fraud-dollar losses and out-of-pocket costs. Consumers also rely on customer service, which should take the form of a dedicated and trained fraud resolution specialist. When consumers were asked which feature they would most like their existing financial institution to implement with respect to identity theft, respondents unanimously chose zero liability.[5] As with existing account holders, users of fee-based identity protection services expect 100% coverage in an unlikely event of fraud.

[5] 2010 Consumer Survey, Javelin Strategy & Research.

Recommendations for Financial Institutions

1. For financial institutions that are considering launching an identity protection product, it is important to partner with a trusted provider that has a longstanding history of protecting consumer information.

2. Improve upon the identity fraud educational information provided on your institution's website by highlighting the use of credit monitoring as a method to protect against new accounts fraud, particularly in the context of financial accounts. Educate consumers on the difference between fraud on an existing financial account vs. fraudulently created new accounts using stolen information, particularly fraudulent new credit cards or checking accounts. Inform consumers about how to reduce their risk. Using the preventive approach to identity fraud through education, financial institutions are well positioned to educate consumers via online banking.

3. Many financial institutions' offerings have expanded upon the traditional credit monitoring service to include either internet surveillance or personal information monitoring in order to differentiate their identity protection products and in response to consumer interest in such services. Consider incorporating an additional monitoring service that looks beyond changes in credit report information, covering additional data sources such as the internet or public records.

To learn how your financial institution can drive revenue with identity protection services, contact your Harland Clarke account executive.