Data Breaches Hasten EMV Migration Plans; Latest Debit Issuer Study Shows Renewed Card Security Focus

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The Debit Issuer Study, commissioned annually by PULSE, has proven its value during its first nine years. For instance, five years ago, the *2009 Debit Issuer Study* predicted the rise of mobile banking. Six years ago, the study identified quick-service restaurants and bill payment as important growth opportunities for debit. Seven years ago, the study stated, "Mobile devices may replace the traditional card as the primary debit transaction source."

Well, you can't get them all exactly right.

As has been the case since the first Debit Issuer Study was commissioned in 2005, the 2014 study objectively presents facts about debit card issuer performance and perspectives across electronic payments. It reaches far beyond PULSE issuers, seeking data and insights from 71 banks and credit unions across the spectrum of type, size, location and network participation. In fact, participating financial institutions collectively represent more than 140 million debit cards and 76,000 ATMs.

Some findings have been constant over the years, such as optimism about debit growth, concerns about fraud and the constant tweaking of rewards programs.

The impact of major disruptive events also has been tracked and reported, such as how belt tightening following the recession increased consumer preference for debit, and how Regulation II prompted financial institutions to reassess business strategies related to their debit programs.

The *2014 Debit Issuer Study* reported on the impact of another major disruptive event: high-profile data breaches.

Many financial institutions are reacting by ramping up their plans to issue EMV cards – something that previously seemed stuck in neutral. The Target breach over the holidays last year proved to be a great motivator for financial institutions and the cardholders they serve.

The highly publicized breach affected between 70 million and 110 million customers, many of whom lost both payment card data and personal information, and impacted every one of the 71 financial institutions that participated in our study. Eighty-four percent reported reissuing all cards exposed in the breach. This is far greater than the 29 percent of banks and credit unions that typically reissue exposed cards as a standard response to a breach.

This year's study confirms the industry is reaching a tipping point toward EMV, with 86 percent of respondents telling us they plan to begin issuing EMV cards in the next two years, a significant increase from 50 percent in 2012. Indeed, the industry continues to come together to look for solutions to advance EMV implementation and increase security.

Security a Key Objective

To say the Target breach was a watershed event for the industry is an understatement. Separate reports from the Consumer Bankers Association and the Credit Union National Association estimate the cost to financial institutions of replacing the payment cards compromised in the breach at more than $200 million.

The Debit Issuer Study found that issuers are responding by re-evaluating their strategies for improving card security in 2014. After the previous Debit Issuer Study showed a drop in net fraud during 2012, fraud increased in some areas during 2013, the study showed. PIN debit fraud loss rates remained constant at 0.3 cents per transaction on average, while signature debit loss rates increase to 2.2 cents per transaction, up from 2.0 cents.

Overall, the percentage of debit cards exposed in data breaches nearly tripled in 2013. Fourteen percent of all debit cards were exposed last year, compared to five percent in 2012. The resulting 2013 fraud losses to financial institutions amounted to 5.7 basis points for signature debit and 0.7 basis points for PIN debit.

Another measure found that loss rates from international transactions were more than six times greater last year compared to 2012. The study found that international transactions experienced loss rates of 51 basis points, compared to two basis points for domestic card-present transactions (PIN and signature combined).

Broad Commitment to EMV

Highly publicized data breaches have helped many financial institutions overcome their hesitancy to commit to EMV. The cost of the Target breach, paired with EMV's promise to reduce card fraud, provided the catalyst for financial institutions to re-examine their strategies to migrate to EMV technology.

Tony Hayes, a co-leader of the study and partner at Oliver Wyman, said, "We were surprised by the across-the-board embrace of EMV by debit issuers. There has been a dramatic shift from their tepid interest last year to active plans to implement EMV beginning in 2015."

Most issuers said they would begin issuing EMV debit cards by 2015, with the most common strategy to provide account holders with EMV debit cards as part of their regular card reissuance cycle. As a result, institutions say the migration will take about three years. International travelers and heavy debit users will be first to migrate, in many cases in advance of the liability shift in October 2015.

Issuers Focus on Growth

Despite the security issues surrounding several high-profile data breaches, we saw growth in both consumer and business debit in 2013. This was a welcome development, following a turbulent 2012 with significant regulatory changes.

During 2013, active cardholders increased their usage of debit and increased transactions per active card to 20.1 per month from 19.4 a year earlier. Metrics such as penetration, active rate and ticket size remained consistent year-over-year. Business debit card usage grew, with transactions rising to 14.5 per active card per month from 13.5.

We continue to see a decline in signature debit's share of total transactions. In 2013, signature debit made up 62 percent of consumer transactions, down slightly from 64 percent in 2012. This continues a trend we saw a year ago, and is driven by that fact that large debit issuers now tend to prefer PIN transactions, due to lower processing costs.

Rewards programs, which declined following Regulation II implementation, are rebounding. Many financial institutions are moving to merchant offers as traditional debit rewards programs have unsustainable economics in the post-Reg II environment for regulated issuers. Almost half (47 percent) of issuers now offer debit rewards programs. Of those, 55 percent feature merchant offers.

The study also revealed continued growth in general purpose reloadable (GPR) prepaid cards, with issuers expecting spending to increase 20 percent and card loads projected to jump 7 percent between 2013 and 2016, to around $250 billion. However, the study shows the percentage of financial institutions that issue prepaid cards dropped 4 percentage points in 2013 to 80 percent.

Overall, the 2014 study shows that debit continues to grow, proving its resilience as a preferred method of payment, even after a turbulent year.

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