

Debit Card Fast Facts: Banks Promote Fraud-Prone Transactions

Fact #13: Banks continue to argue that interchange fees are necessary to cover their costs related to fraud, yet the current interchange fee structure gives banks an incentive to steer customers away from entering their PIN numbers. The banks' steering dramatically increases fraud.

There are currently two types of debit card transactions: PIN and Signature. Signature is when a customer does not enter a personal identification number. PIN transactions are much more secure because they require the cardholder to authenticate the card they are using. Despite PIN being significantly more secure, big banks are steering customers toward signature purchases. What incentive do they have not to when merchants are bearing at least 43% of fraud losses¹ on those transactions?

The average active consumer debit card is used to perform 17.3 point-of-sale purchases per month, 65% signature- based and 35% PIN-based. Average gross interchange rates are 1.42 % on signature debit and 0.65 % on PIN debit.² PIN debit card fraud losses in 2009, as measured in dollars per card per year, were \$0.17, while signature debit cards fraud losses were \$2.29. Signature point-of-sale fraud losses average 0.075 % while PIN point of sale losses average 0.01 % or 1 cent on every \$100.³

Despite PIN debit being much more secure, last spring, JP Morgan chase told their customers signature was safer than PIN.⁴ The *American Banker* covered the story:

"From a technical security standpoint, there's no question about it, a PIN adds a level of safety, which is why ATM transactions have required a PIN for years," said Avivah Litan, a security analyst at Gartner Inc.

But banks do collect higher interchange fees from merchants on signature debit transactions.

"PIN is actually more secure, but PIN does not generate as much revenue to the bank," said Adil Moussa, an analyst at Aite Group in Boston. "If they get you to use signature debit, then they are going to make much more money."

This is not a new concern. As early as 2002, consumer advocates said consumers were better off punching in a PIN for check-card transactions. Bill Apple of Consumer Reports told Bankrate.com: "We generally don't like these cards with a signature. They're not as secure. Also, if people sign, the bank collects much higher fees and ultimately it will raise the cost of goods and services for everyone. The merchants will be paying higher transaction fees, and that's coming out of overhead somewhere. Eventually, they may have to jack up prices."⁵

If this problem was identified in 2002, why are big banks still steering customers toward signature debit cards? The answer is simple - they don't have any incentives in the current system not to.

¹ <http://edocket.access.gpo.gov/2010/pdf/2010-32061.pdf>. Pg. 81741.

² Pulse Debit Issuer Study. June 2010.

³ Ibid, pg. 17.

⁴ Lepro, Sarah. Counterintuitive Pitch for Higher-Fee Debit Category. *American Banker*. April 21, 2010. http://www.americanbanker.com/issues/175_75/debit-1017958-1.html.

⁵ <http://www.bankrate.com/brm/news/cc/20020710a.asp>