

# The DeCoupled Debit Card:

How risky is it?

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Federal Reserve Bank of Chicago

2008 Payments Conference

Payments Fraud: Perception versus Reality

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# Agenda

- The Debit Market in the U.S.
- How Decoupled Debit works
- Case Studies
- Risks and Mitigation

# About Two Sparrows Consulting

- Independent Boutique Consulting Firm
- Payments Specialists
- Credit Cards, Debit Cards, ACH, Internet Payments
- Chip Cards, Stored Value, Loyalty, Merchant Acquiring, Bill Payment, Electronic Banking
- Project Management
- Training
- Marketing and Business Development
- M&A Services

# The Debit Market in the U.S.

## 2007 U.S. Statistics (in millions)

Pinned Debit Cards	Pinned Debit Trans	Signature Debit Cards	Signature Debit Trans	Credit Cards	Credit Cards Trans
85.5	11,667	312.2	16,980	678.1	25,415

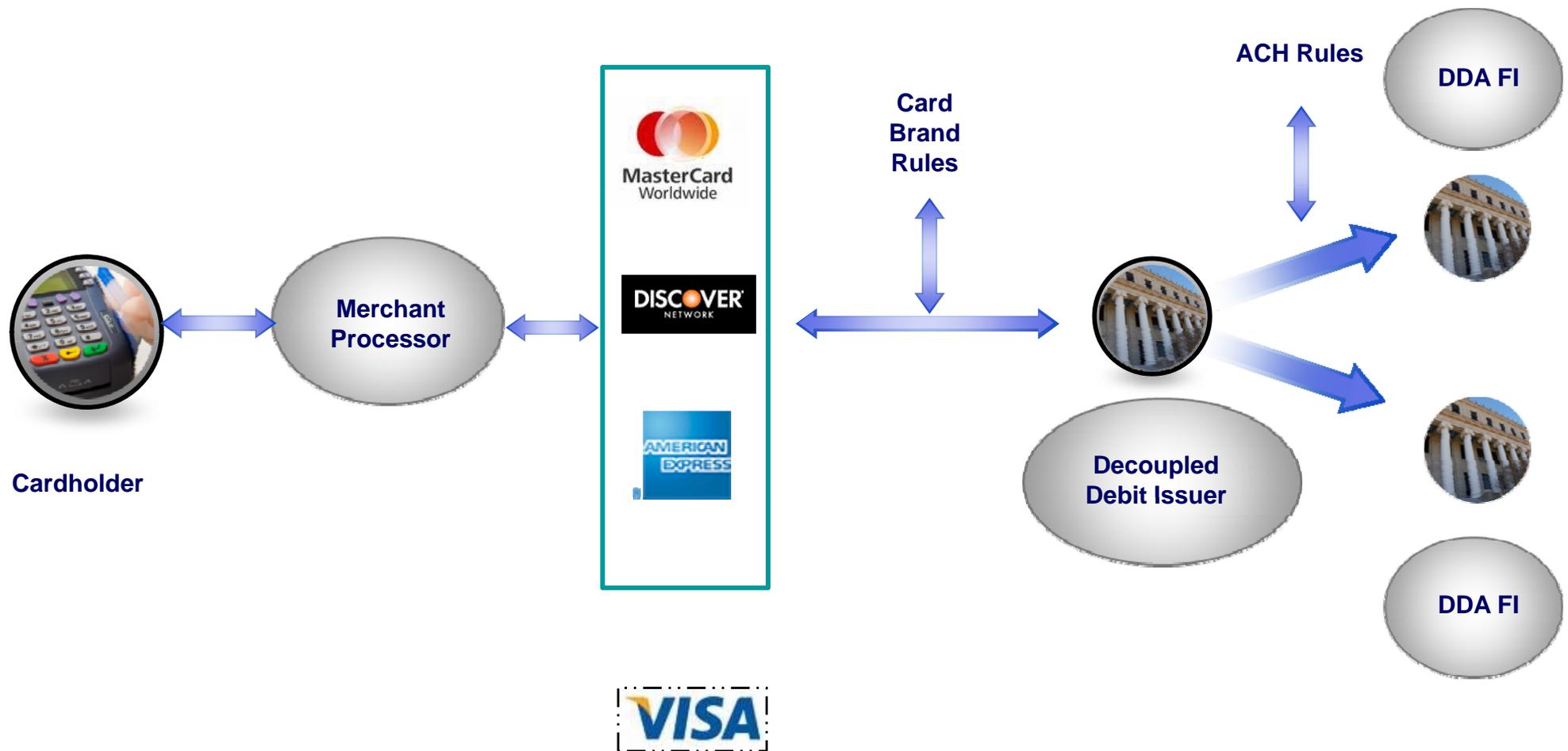
Source: ATM & Debit News

# Debit Market in the U.S.

- VISA has over 75% market share in US Signature Debit.<sup>1</sup>
- 80% of U.S. consumers carry a debit card.<sup>2</sup>
- Active Debit users do 11 transactions per month.<sup>2</sup>
- Top 5 Signature Debit FIs account for only 22% of total cards issued.<sup>3</sup>

Sources: <sup>1</sup>VISA, <sup>2</sup>First Data Corporation, <sup>3</sup>ATM & Debit News

# Decoupled Debit: How it Works



# PayPal ATM/Debit Card

- MasterCard branded debit card
- Funded by ACH Debit to Checking account
- Used for both online and physical payments
- Can be used at POS or ATM
- 1% Cash Back on Signature Debit
- Daily limits for ATMs and POS

# Capital One Decoupled Debit Card

- MasterCard branded debit card
- Issued by Capital One
- Cardholder need not have DDA at Capital One
- Can be used at POS or ATM (Limits)
- Co-Brand Partner Focus
- Richer Rewards
- Suspension of two current programs

# HSBC

- Decoupled debit is part of a broader payments innovation, now called OptiPay
- Single card with multiple, selectable payment options
  - Decoupled debit, credit, accrued rewards
- Card program sponsors configure the program to offer some or all OptiPay components

# Challenges

- Decoupled Debit Issuer (DDI) must manage risk
  - DDA balance unknown
  - MasterCard authorization rules apply
  - DDA may be closed or blocked by consumer
- Customer Service
  - Consumer may be confused on what FI to call when a transaction is in doubt
- DDI must offer increased cardholder utility vis a vis DDA FI (richer rewards)

# Threats to Traditional Model

- Eliminates need for consumer to use DDA FI's debit card.
- Introduces a low cost way for DDI to get consumer wallet share; cross sell additional products
- Eliminates DDA FI interchange income
- Could provide an entry for American Express and Discover
- Co-Brand Non-Bank Threat

# Key Risk Challenges

## ■ Issuance risk

- Verification that the applicant owns the checking account

## ■ Transaction Risks

- NSF risk due to lack of visibility into DDA account balance
- Customer service processes

## ■ Exception Handling Risks

- Managing the ACH representment process

# Mitigating Risk

## ■ Issuance Risk

- Tools for assessing Know Your Customer (KYC), anti money-laundering (AML), and NSF/fraud risk

## ■ Transaction Risk

- 3rd party databases
- Experience-based data for decision support criteria
- Transaction Dollar Limits

## ■ Exception Handling

- Configurable representment processes

**The Chinese use two brush strokes to write the word 'crisis.' One brush stroke stands for danger; the other for opportunity. In a crisis, be aware of the danger - but recognize the opportunity.**

***John F. Kennedy, Speech in Indianapolis, April 12, 1959***

**Drive thy business or it will drive thee.**

***Benjamin Franklin***

# Questions?

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