Image Exchange

2008 Payments Conference
Payments Fraud: Perception vs. Reality

Federal Reserve Bank of Chicago

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Industry Trends
Checks & Image Exchange
Avg # of Images Rec / Day

42.1 million Images/Day
Annualized =
10.6 billion Images/Yr
= 45% of all transit checks

Source: Federal Reserve, PaymentsNation, SVPCO and local / regional exchanges
# of Image Based Trans.  

Grew 89% from 3/07 & 3/08  

Transactions Originated as Images for Collection Totals 60% of Transit Items  

Source: Federal Reserve, PaymentsNation, SVPCO and local / regional exchanges
# of Receiving Institutions

Represents 9,784 Receiving Institutions

Or Approximately 60% of all U.S. Institutions

Source: Federal Reserve, PaymentsNation, SVPCO and local / regional exchanges
March ’08
Annualized = $17.5 Trillion

Source: Federal Reserve, PaymentsNation, SVPCO and local / regional exchanges
Check payment system is more valuable in 2006 than in 2000!

Data Source: Federal Reserve Payments Studies for 2004 and 2007
Average Check Value

Data Source: Federal Reserve Payments Studies for 2004 and 2007

Average check payment is more valuable in 2006 than in 2000!
Fraud Risk
Image Exchange
Check Image Fraud

Traditional Authorization Issues and Fraud Sources Continue

- Typically, these involve parties outside of the banking collection and return processes

- Those same parties continue to participate in the process at the same process points; for example

  - If a fraudulent signature is placed on a check or if the amount is changed, it will appear on the image as deposited with the bank

  - If a kite is initiated via paper checks and those checks are imaged, the kiting continues
Check Image Fraud

Traditional Authorization Issues and Fraud Sources Continue

- *These frauds are controlled in the traditional ways by the paying bank and its customer*

- For check images and for substitute checks
Complicating Factors

New, More Complicated Environment

– Possible confusion by financial institutions, their customers and vendors

• Was the payment authorized?
• Was the truncation authorized?
• What is it legally? A check or a non-check?
• Is it properly payable?
• Which payment is the duplicate?
• What is the return deadline?
• What do you return and to whom?
Complicating Factors

If It Looks Like a Check, Is It a Check?

- Electronically initiated payments that are formatted to look like checks

- Need to know how customers are creating their electronic deposits

- Need to have agreements in place to allocate appropriate liabilities between all the parties

  - No law to cover check image exchange
Complicating Factors

If It Looks Like a Check, Is It a Check?

Moo, Moo
Complicating Factors

Duplicate Images & Substitute Checks

- Need enhanced controls to:
  - Prevent the creation/acceptance of duplicates
  - Testing for duplicates
    - Across payments systems
    - Across multiple days

- Without a more efficient adjustment system it takes too long to unwind interbank-accounting
Complicating Factors

Non-Conforming Images (NCIs)

– *Intended to protect paying institutions from receiving poor quality images*

– *Current image quality assessment (IQA) applications are inadequate*

• High percentage of NCIs would not impact posting (if presented) verification of signature, customer service, etc.

• Primary impacts are delays in collection of the items and increases in the cost of the collection
Complicating Factors

Non-Conforming Substitute Checks

- *Mostly conforms except for technical deviations*
  - A Shakespearian dilemma:
    - *To post or not to post?*

Another Dilemma:

- *To keep or not to keep?*
  - Risk of subsequent entry into the payment stream creating duplicates
Loss of Controls

Loss of Traditional Controls

- Look and feel of the original paper
- Special security features
New Controls

Speed of Collection and Return

– On-demand electronic payments are faster than on-demand paper payments

– Later exchange windows for electronics

More Sophisticated Prevention, Detection and Resolution of Duplicates

More Sophistication in Pay / No Pay Decisions

– New analysis, new detections
New Controls

Enhanced Adjustment Processes

- To shorten windows of opportunities for would be fraudsters

Image Survivable Security Features

- Replaces some of the paper-based features
New Controls

Duplicate Detection & Prevention

– *Looking for dups at new places in the process; e.g. BOFD and at the paying bank*

– *Comparisons must be across multiple days and multiple payment channels*

Complication

– *There are some legitimate duplicates*
Closing Comments
Closing Comments

Check Payment System is Growing in Value and Therefore in Importance

Check Image & Substitute Check Fraud
  – Same as for paper

New Processes and Changes in Party Participation Create New Complications
  – Creates opportunities that could be exploited

New and Different Controls are Emerging
  – Should reduce the opportunity for losses generally
  – And reduce opportunity for fraud
Thank You

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