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The Impact of SCA Enforcement on Merchants

SURVEY RESULTS: EUROPEAN AND UK BUSINESSES SEEK TO BALANCE SECURE TRANSACTIONS AND A FRICTIONLESS CUSTOMER EXPERIENCE.

Presented by
PaymentsSource



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Between the COVID-19 pandemic and adapting to enforcement of the European Commission's Strong Customer Authentication (SCA) regulations, 2021 is a challenging year for many merchants. The new SCA rules have introduced more stringent fraud protection regulations around electronic payments. Those merchants who do not currently have the 3-D Secure (3DS) authentication protocol in place will inevitably see their transactions decline and will lose a significant part of their revenue.



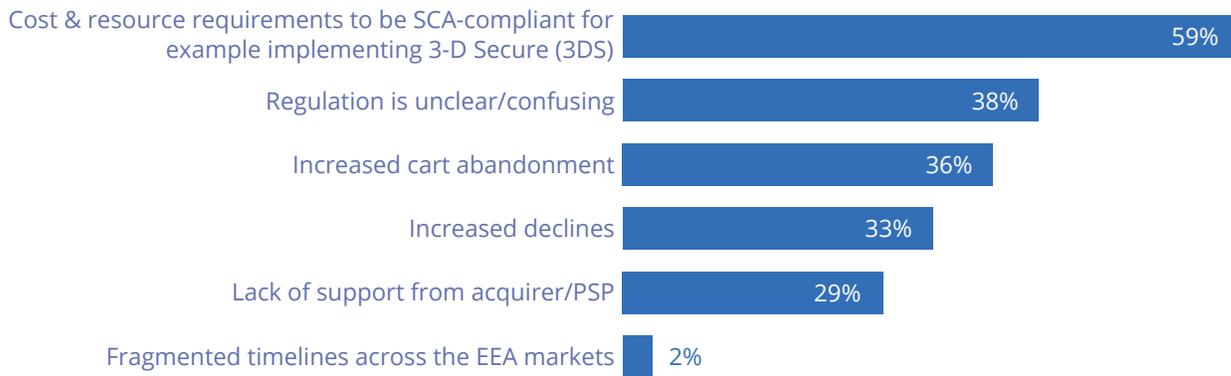
While 3DS provides greater security for merchants, it also brings the potential to add friction to the customer checkout experience. In a post-SCA landscape, merchants will need to balance the requirements of authentication with providing an optimal customer experience. To achieve this balance, merchants must have a good understanding of the regulation and implement a strategy to optimize both the geographical scope of the regulation and the exemption criteria.



In the long run, SCA and the requirement for two-factor authentication should reduce fraud across the European Economic Area (EEA), which will help to maintain consumer confidence and reduce the operational costs associated with fraudulent sales. Fraud has been on the increase for some time, a trend that has only been exacerbated by the pandemic. The largest increase was in car and other asset finance applications, which saw a rise of 181%, followed by current accounts (35%) and then saving accounts (28%). Fraudulent credit card applications (17%) and unsecured loans (10%) also went up. Most of the increase in fraud are not linked to ecommerce and would not be mitigated by SCA. And in the past two years, fraud has cost businesses roughly \$42 billion worldwide.² In response, merchants in the UK and across the European Union (EU) have taken a variety of approaches to identify and prevent fraud.

In the short run, however, the relatively complex nature of SCA has produced challenges for merchants. According to a survey commissioned by Accertify and conducted by Arizent Research/PaymentsSource, nearly 60% of merchants worry about the cost and resources required for SCA compliance, and 38% find the SCA rules unclear or confusing (see Figure 1).*

Figure 1: Biggest Concerns Regarding SCA Enforcement

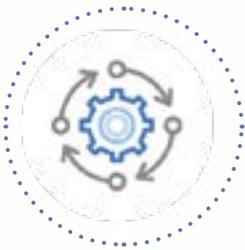


Partnerships with payment services providers/acquirers and vendors can play a crucial role in helping merchants manage SCA compliance and boost fraud prevention practices while also maintaining an optimal customer experience.

Source: Arizent Research/PaymentsSource, December 2020/January 2021

To address these challenges, merchants must provide an optimal customer journey through cost-efficient and effective ways of managing fraud while also meeting SCA requirements. Partnerships with payment services providers/acquirers and vendors can play a crucial role in helping merchants manage SCA compliance and boost fraud prevention practices while also maintaining an optimal customer experience.

MANAGING SCA



As enforcement of SCA rules ramps up, entities that initiate or process electronic payments for European consumers must meet new standards designed to authenticate the payer. These rules require two-factor customer authentication for payments, though the rules include exemptions for transactions such as low value, certain corporate payments and other transactions that are evaluated as low risk.

To route in-scope payments requests appropriately, merchants must be able to detect situations in which an exemption could apply. A majority of merchants (68%)* report that they have outsourced management of SCA exemptions and scope checks to their payment service provider (PSP) or acquirer. While outsourcing SCA scope and exemption checks to an acquirer or PSP should bring benefits and mitigate declines, it may not provide a solution that is effectively tailored to a specific merchant. Acquirers and PSPs have large portfolios to manage, which may lead them to implement a generic SCA policy for all their merchants. Meanwhile, nearly one in three* merchants report that they either do not use a PSP or acquirer to manage SCA or they simply do not have processes in place to deal with SCA exemptions or perform scope checks.

Merchants that use a PSP or acquirer to manage SCA tend to be more concerned about the cost and resource requirements to meet SCA requirements (65% versus 48%* that don't use a PSP/acquirer) and about the fragmented timelines for implementing the regulations across the UK and EU markets (34% versus 17%)*. At the same time, merchants who have outsourced meeting SCA requirements are less likely to be concerned that the regulations are unclear or confusing (31% versus 52%)*.

* Source: Arizent Research/PaymentsSource, December 2020/January 2021

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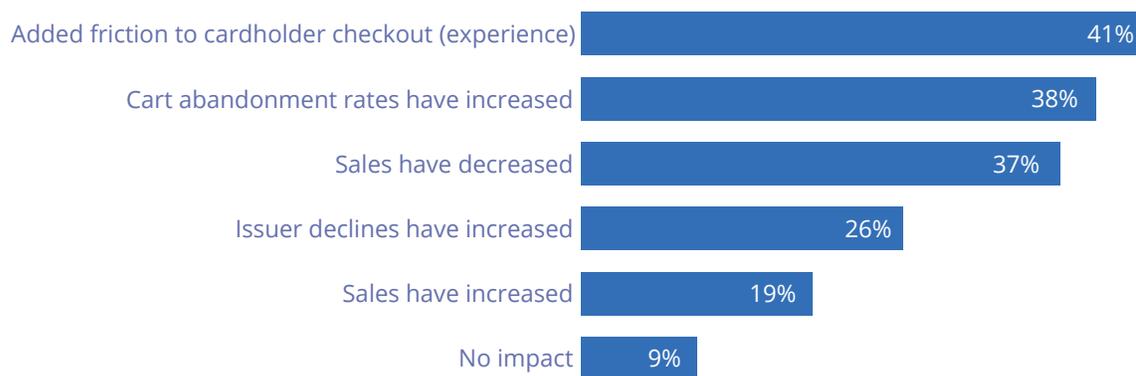
FOCUSING ON THE CUSTOMER



Exemptions to the new payment rules are designed to reduce friction for consumers in lower-risk situations where two-factor authentication is unnecessary. However, some of the biggest concerns merchants have about SCA revolve around burdens those rules place on customers.

Among merchants operating in the EEA, more than one-third report their sales have decreased due to SCA enforcement (see Figure 2)*. Furthermore, many report added friction to cardholder checkout and increased cart abandonment, suggesting that customer experiences have been negatively affected. “Unfortunately, in effectively targeting the issue of fraud, we are creating customer ‘friction’ at checkout,” says a senior manager at an organization in the UK hospitality sector.

Figure 2: The Impact of SCA on the EEA



Exemptions to the new payment rules are designed to reduce friction for consumers in lower-risk situations, but some of the biggest concerns merchants have about SCA revolve around burdens those rules place on customers.

Source: Arizent Research/PaymentsSource, December 2020/January 2021

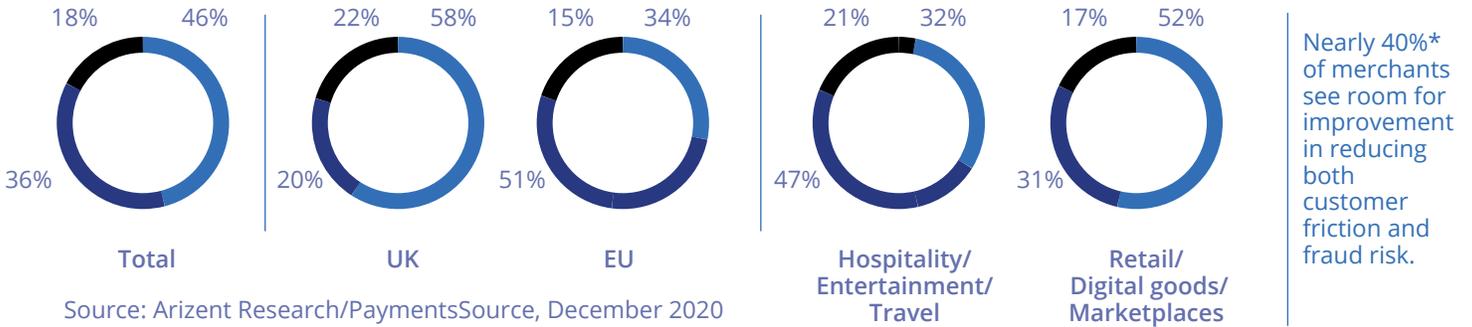
In a fast-changing retail environment, customers increasingly expect fast, secure and frictionless checkout experiences. The goal is to provide customers both a smooth and secure payment experience — something which is challenging to do. “In the end, what we are trying to do is find a balance between these two things [reducing customer friction and fraud risk], even though this is quite expensive to carry out,” explains a senior business unit executive at a Spanish retail firm.

As they look to balance these competing factors, different merchants and industries tend to prioritize different elements of the equation (see Figure 3).^{*} For example, in the UK, 58%^{*} of respondents report that they strive to strike a balance between customer experience and fraud losses, whereas in the EU, a larger percentage say providing a frictionless checkout experience is their priority.

^{*} Source: Arizent Research/PaymentsSource, December 2020/January 2021

Figure 3: Prioritization of Frictionless Checkout Experience Versus the Need for Liability Protection

- We look to find a balance between customer experience and fraud loss
- Managing fraud loss is our priority
- Providing a frictionless checkout experience is our priority



THE ADVANTAGES OF PARTNERSHIPS



Ultimately, merchants that partner with payment services providers/ acquirers and vendors to manage SCA are more likely to see themselves as effective at reducing both customer friction and fraud risk. Merchants with these partnerships are also more likely to offer mobile apps that use biometrics for secure login and checkout. And, these merchants are also more likely to report they are fully aware of all available exemptions than those that manage SCA themselves.

Overall, 61%* of respondents say they are effective at reducing both customer friction and fraud risk. That means that nearly 40%* of merchants see room for improvement. Considering a partnership with a PSP/acquirer or vendor could offer merchants an opportunity to better manage the complexity of these new regulations without sacrificing customer security or the customer experience.

1 <https://www.experianplc.com/media/news/2020/fraud-rate-rises-33-during-covid-19-lockdown/>

2 <https://www.pwc.com/gx/en/forensics/gecs-2020/pdf/global-economic-crime-and-fraud-survey-2020.pdf>

* Source: Arizent Research/PaymentsSource, December 2020/January 2021

METHODOLOGY

An online survey was conducted by Arizent Research/PaymentsSource in December 2020/January 2021 among 105 respondents who work at merchants that offer products/services through ecommerce/online channels. Respondents had to be knowledgeable about payments fraud technology.



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