

Posted with permission from The Nilson Report, Carpinteria, California.

ADDRESS-CHANGE RISK ASSESSMENT

Statistics on identity theft vary and usually include instances of stolen and counterfeit cards, but true identity theft occurs when a thief uses stolen information to either open a new financial account or take over an existing one. Most of the solutions for combating this type of crime try to stop thieves from gathering the information in the first place. Another approach is to stop thieves when they go to use the data. In 2003, the U.S. government set out to do this by amending the Fair and Accurate Credit Transactions Act (FACTA) to include two new sections that would require card issuers to investigate address discrepancies.

Section 114 covers instances where an address on an existing account has been changed and there has been a subsequent request for a new credit or debit card. Section 315 covers discrepancies between an address supplied on a credit application and the address on file with the credit bureaus. Both go into effect on January 1, 2008. Compliance will be mandatory by November 1.

Each year 15% to 17% of American households change their residence, so issuers know that they are going to deal with a fair amount of legitimate address discrepancies. They also know that the fraud that results from the relatively few discrepancies that are not legitimate has been a manageable cost of doing business — a lower cost, in fact, than separating the valid discrepancies from the ones generated by fraud. Most issuers err on the side of accepting the risk. The new FACTA rules will take away that option.

Now, when faced with address discrepancies on new applications, issuers will need to find the most cost-efficient way to cull the valid majority from the fraudulent few. The number of applications to sort through can be significant. When new applications are submitted to a credit bureau, about 60% meet an issuer's credit criteria and about 25% of those have an address mismatch.

In California, where more stringent laws already approximate FACTA's new rules, issuers have been sending mismatched addresses through Identity Verification (IDV) solutions available from several vendors. These solutions attempt to resolve discrepancies by consulting an external source such as the white pages of a telephone book.

IDV can reduce the number of mismatched addresses to 15%. Verifying these remaining applications can require manual strategies such as requesting supporting documents (e.g., utility bills) — a process that causes some valid candidates to drop out in frustration, and still leaves upwards of 5% unapproved.

ID Insight offers an additional layer to their IDV. The addition, called Safe2Change, uses a patent-pending algorithm to predict the risk associated with an address mismatch (see box). The algorithm can also be used when there's an address change on an existing account. When it predicts a high level of risk, the issuer can send a letter to the cardholder requesting validation. Then, if there is a subsequent request for a replacement card, the situation has already been assessed. Clients pay the company for the analysis on a per-file basis that decreases with volume and starts at about \$1.00 per transaction. Adam Elliott is President at ID Insight in Northfield, Minnesota, (651) 343-5380, adam.elliott@idinsight.com. Prior issue: 814

Safe2Change Risk Scores

ID Insight's approach, which includes verification, also uses Address Differential Analysis to predict which address changes are legitimate. The analysis looks for suspect patterns based on demography, dwelling types, distance metrics, criminality statistics, and address velocity. Resulting scores range from 1 to 99 with higher scores indicating higher risks.

When evaluating costs associated with address changes, ID Insight looks at a variety of factors — the cost of attempting to verify all mismatches automatically, the expense of manual intervention on

applications that require it, unrealized income due to legitimate customers who were declined when they shouldn't have been, and chargeoffs due to fraud from illegitimate customers who were accepted when they shouldn't have been. The company estimates that the costs to lenders who employ IDV solutions alone is \$31 per mismatch, largely due to the number of potential customers that don't make it through the system. The cost of using Safe2Change is estimated at \$5.20 per application because it cuts down on the number of applications that have to be verified manually. The estimated cost to lenders who did not reject applications due to mismatches alone, which will not be possible under new FACTA rules, has been \$8.00 per mismatched application.

