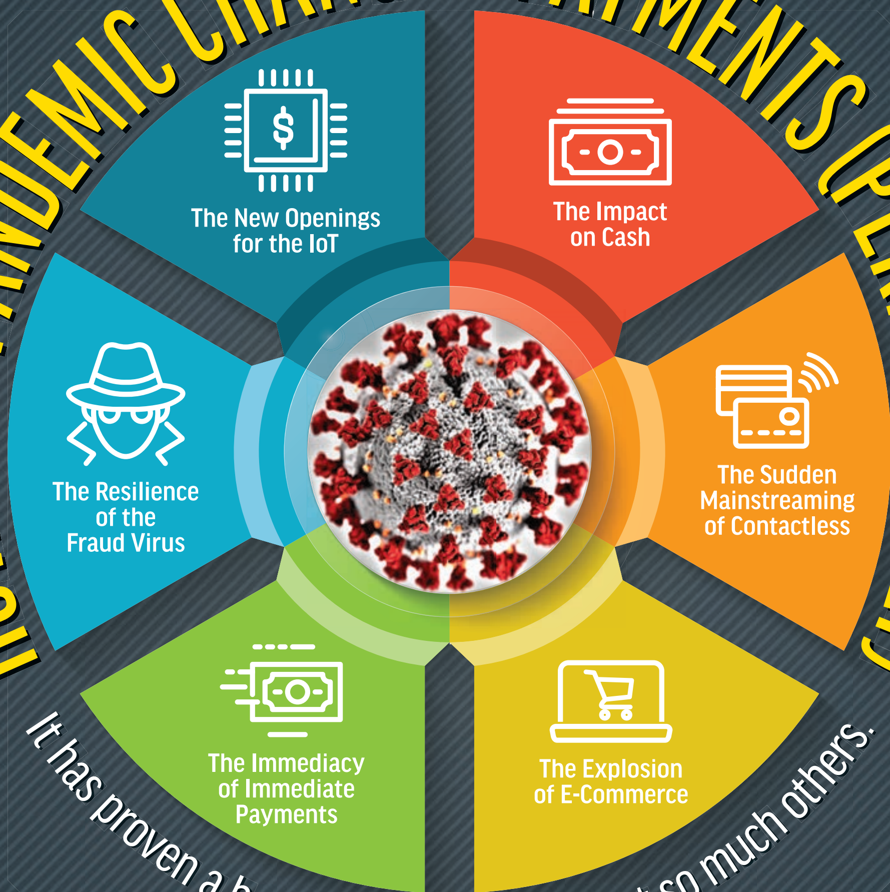
DIGITAL TRANSACTIONS

Trends in the Electronic Exchange of Value

HOW THE PANDEMIC CHANGED PAYMENTS (PERMANENTLY)



It has proven a boon for some trends, not so much others.

Volume Seventeen, Number Seven • DigitalTransactions.net • July 2020

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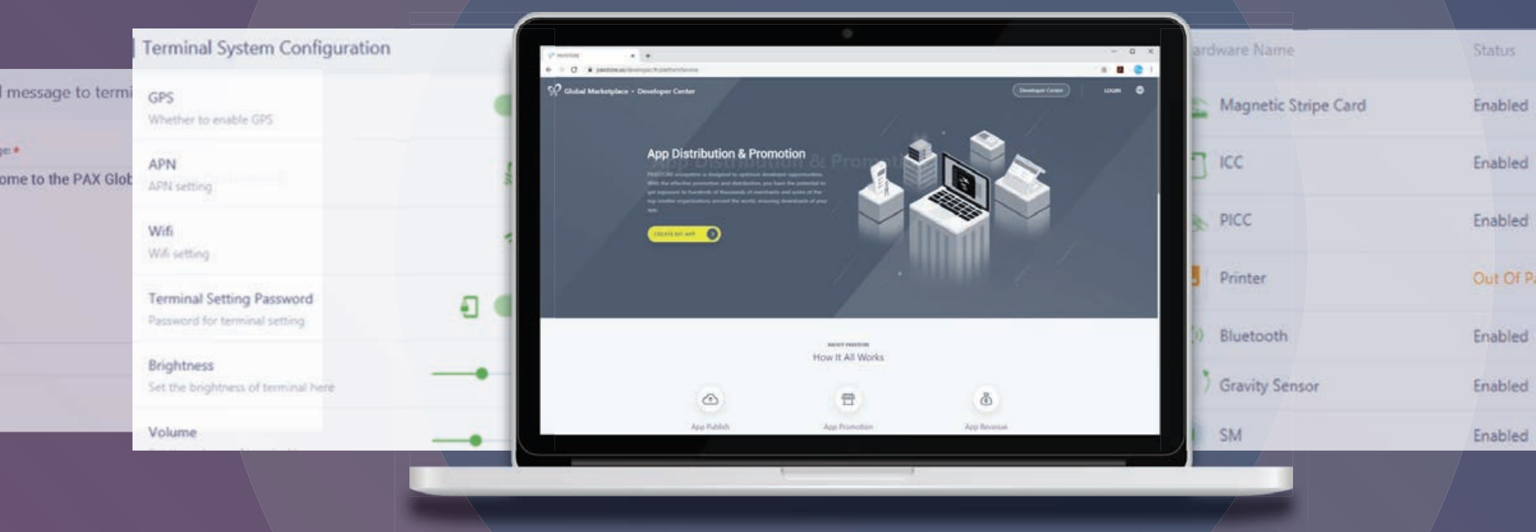

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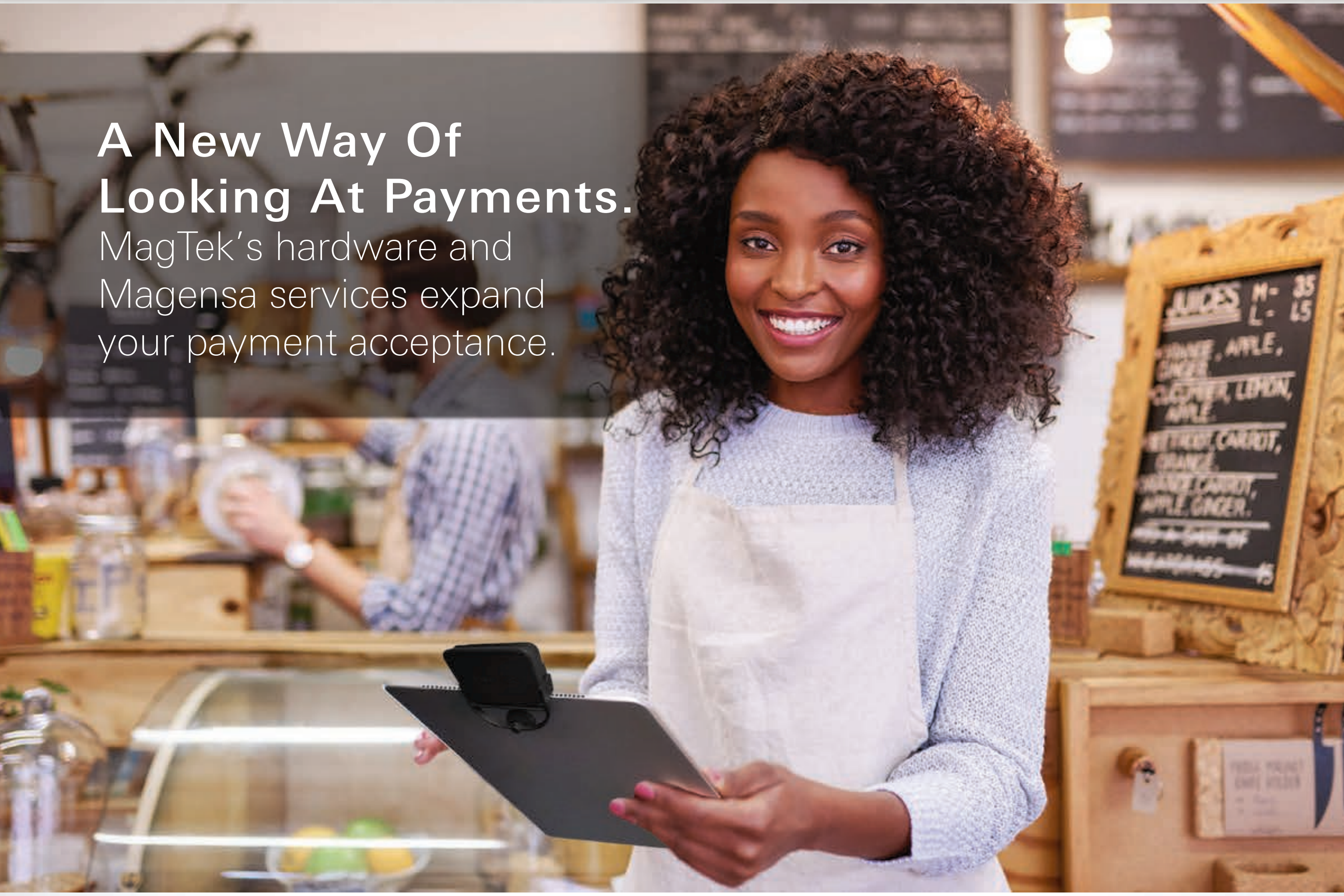

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the gimlet eye

A RESILIENT INDUSTRY

WE HERE AT DIGITAL TRANSACTIONS have for the past few months been considering the impact the novel coronavirus is having on the payments business, along with the adjustments the business is making to contend with business lockdowns, stay-at-home orders, and social-distancing recommendations.

Now the country is re-opening in many states and regions, allowing stores and restaurants to do a broader business within certain guidelines and restrictions aimed at stopping the spread of the virus. And we think we can say, based on the reporting we've done since this fell disease descended on the United States in force in March, that both merchants and payments providers have adjusted adroitly to some pretty hard restrictions.

Of course, it helps that they're relying on technology that, thankfully, had already been long in development and could be rolled out to meet such a moment as this.

In eateries, tech companies have found ways to let consumers call up digital menus and pay digitally at the table. Outside, they're fulfilling orders online and delivering them at curbside or to homes. Stores are finding that consumers can adapt pretty quickly to contactless payments, whether via cards or mobile wallets. Merchants that never knew they had NFC capability at the point of sale found out pretty quickly they do, and turned it on.

Online sellers found a ready customer base composed of consumers sheltering at home. Now that these quarantines are lifting, the rise in e-commerce may abate somewhat, but much of it will stick as those consumers enjoy the convenience of home delivery or in-store pickup. At the same time, the old distinction of card-present vs. card-not-present, in eclipse before Covid-19, may fade even faster in its aftermath.

What will that aftermath look like? Our stories in this issue take a look at that question in some detail. Our cover story, starting on page 24, examines the virus's impact on six key payments issues, from cash to the IoT, and separates the merely ephemeral changes from the longer-lasting trends.

We also look at other issues of vital importance. Our Acquiring story, starting on page 14, takes a deeper dive into the consequences of business and service shutdowns in the form of swelling chargebacks. And the Components story (page 20) reviews trends in point-of-sale technology, many of which have been hastened by the pandemic.

But the big theme all of our reporting for this issue has revealed is the sheer resilience of this industry, the grit and brains needed to counter the grim effects of a disease nobody could have predicted. So we raise a glass to the payments industry, merchants and providers alike. Well done.

John Stewart, Editor | john@digitaltransactions.net

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Trends in the Electronic Exchange of Value

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trends & tactics

THE PREPAID RULE'S LONG SHADOW

It was easy to lose track of it in the midst of all the impacts of the novel coronavirus, but a crucial federal lawsuit filed seven months ago still hangs over the payments industry, carrying far-reaching implications for nearly all players.

It's PayPal Holdings Inc.'s action against the Consumer Financial Protection Bureau over the CFPB's final prepaid rule. And while it very much hasn't gone away, some experts are worried its eventual resolution could hold very different implications from those they were expecting before PayPal brought its suit.

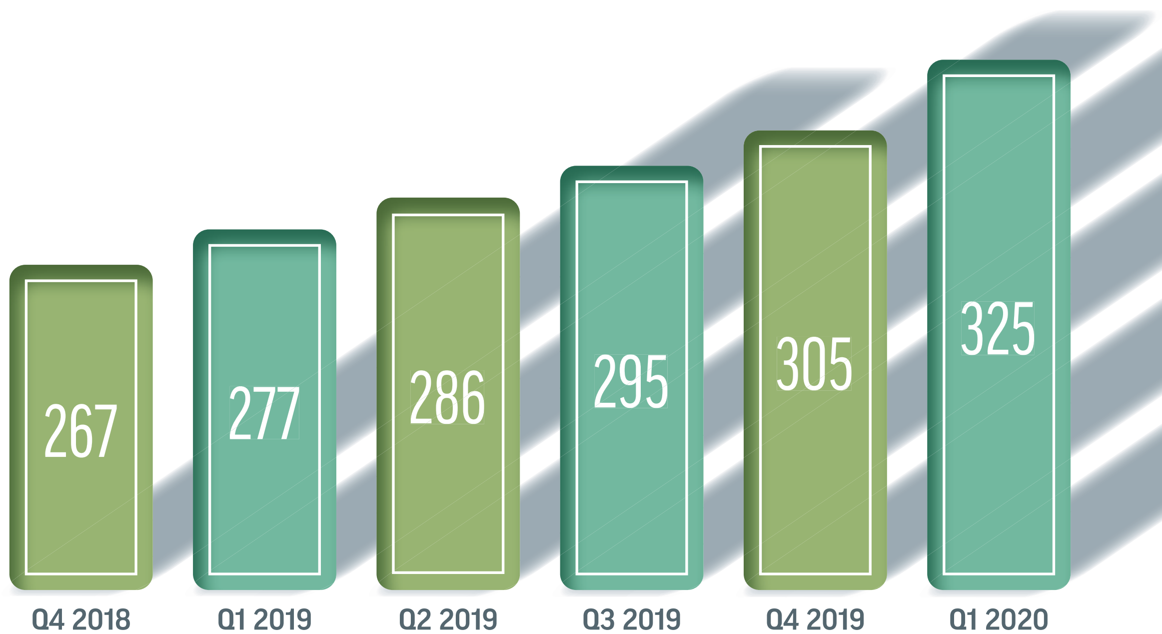
"We could be facing a different kind of environment by the time the case is rendered than we're in today," notes Ben Jackson, chief operating officer at the Innovative Payments Association, a Washington, D.C.-based trade group (Jackson also authors the monthly Payments 3.0 column for *Digital Transactions;* see page 13). "That's kind of what has us uncomfortable. We don't feel people are talking enough about this case."

PayPal alleges the CFPB's 1,600-page prepaid rule, which went into effect in April 2019 after years of wrangling between the agency and the payments industry, wrongly classifies digital wallets such as those PayPal has long offered as prepaid products and so subject to the rule's restrictions.

The payments company also seeks to have the rule quashed as a violation of its free-speech rights under the First Amendment. The suit is before the U.S. District Court for the District of Columbia.

PAYPAL'S WALLET WORLD

(Active accounts, in millions, by quarter)



Source: PayPal

One of Jackson's concerns is that the court could ultimately invalidate the rule, throwing oversight back to "a hodgepodge of regulations" from a long list of agencies, from the Federal Deposit Insurance Corp. to the Federal Trade Commission to state authorities.

Though the IPA has some reservations about the rule, it has the virtue of "centralized regulation of [prepaid] accounts," Jackson says. Another possible outcome, he adds, is that "Congress writes a new law, potentially handing more explicit power to the CFPB," presumably not the result PayPal is seeking.

A third possible outcome is that the court upholds the rule, which could freeze attempts by payments players to make even minor changes to it, Jackson speculates. "The final rule wasn't perfect, but the industry said we can live with that," he notes.

The "adjustments" the IPA would like to see have to do with when consumers can connect a credit account to a prepaid product and with clearer rules concerning disclosure, Jackson says. But the uncertainty surrounding the litigation's ultimate outcome throws that strategy into a cocked hat. "It's hard to predict what a court is going to do," he adds, "I think the case could be counter-productive."

But Jackson and the IPA are certain about one thing: invalidating the rule entirely would be a bad result. "We worked hard on the rule," he says. "We don't want to see the rule thrown out wholesale. There are too many secondary and tertiary effects."

Instead, he suggests, "The ideal outcome would be people sit down and ask how to change the rule to make it fair for everyone."

—John Stewart

COVID-19'S SOMBER RECKONING FOR RETAIL

Despite tentative signs of an economic recovery from the coronavirus-induced depression, some experts are forecasting a gloomy outlook for store closures as the year plays out and merchants struggle with debt loads and a consumer shift to e-commerce.

At least 20,000, and as many as 25,000, stores will likely shut down permanently this year as a result of the pandemic's impact, according to a study released June 9 by Coresight Research. That number includes fresh closings as well as failures by outlets that had temporarily closed during quarantines, the New York City-based research firm says. It is not net of new stores opening their doors between now and year's end.

This latest forecast contrasts sharply with the 9,821 stores Coresight estimates closed their doors in 2019 and represents a dramatic increase from the 15,000 closings the firm predicted in late March.

Mall retailers are particularly vulnerable, with anywhere from 55% to 60% of the failures likely to occur in these shopping meccas, the firm forecasts. While some experts fear a second wave of the novel coronavirus later this year, Coresight says it did not take account of this possibility in its calculations.

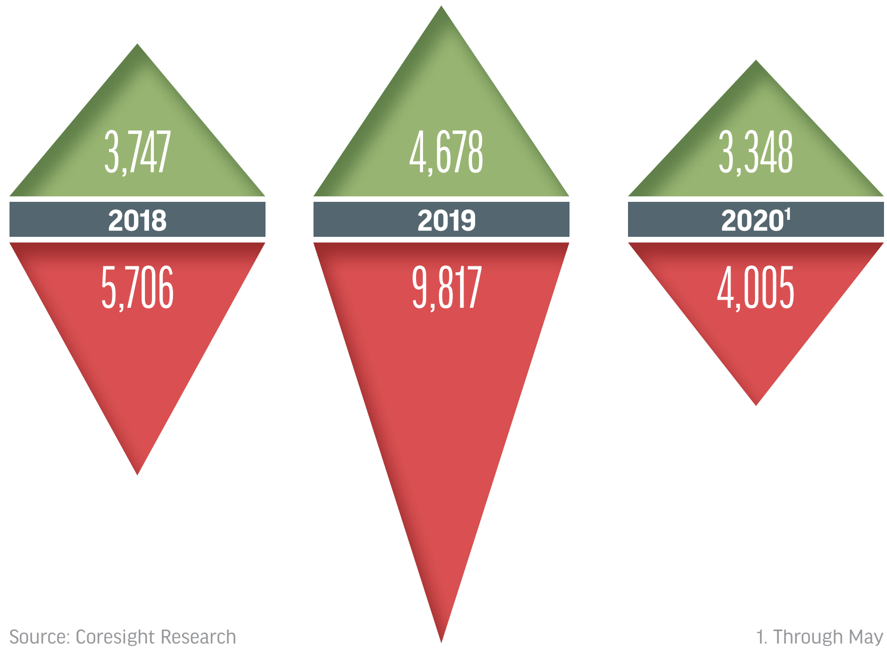
The dour prediction comes as stores around the country have been reopening their doors since early May and chains like Abercrombie & Fitch and Gap are reporting the recapture of much of their 2019 volumes. Such recoveries are not likely for many retailers, Coresight says, mainly because of skittish consumers wary of contracting Covid-19 inside stores and burdened with financial troubles of their own.

"We expect that a return to pre-crisis levels in offline discretionary retail sales overall will be gradual, as we expect consumer confidence, demand, and spending to be short of normal for some time," the report says.

At the same time, payments companies are reporting a rebound in spending, though their numbers are still far short of pre-pandemic levels. Mastercard Inc. early last month reported its U.S. switched volume was down 8% year-over-year for the week ending May 28, level with the previous week and a marked improvement from the 23% plunge seen for all of April.

The improvement, the network says, marks a transition from a "stabilization phase" to a "normalization phase," a time when stay-at-home orders and other mandates are lifted or relaxed and "spending begins to gradually recover."

A MOUNTING TOLL (Announced U.S. store **closures** and **openings**)



Source: Coresight Research

1. Through May

The recovery, however, may be driven more by online activity than by visits to brick-and-mortar retailers. "We continue to see strong growth in card-not-present volumes, excluding online travel-related spend," Mastercard's release says.

The week before, Visa Inc. said its U.S. payments volume in May had fallen 5% from May 2019, but that was an improvement on an 18% plunge in April.

Coresight's forecast indicates a sharp rise in store failures as the year wears on as merchants contend with the consequences of weak demand, rising chargebacks, and damaged balance sheets. As of June 5, the firm had logged a total of 4,005 planned closures, far short of the 7,222 it calculated at the same point in 2019.

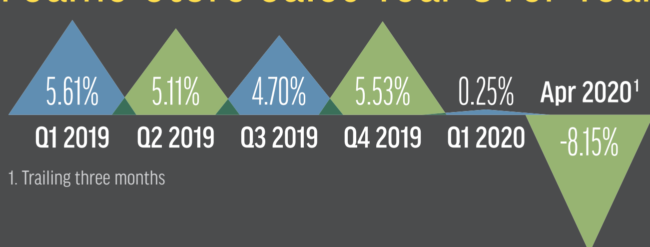
"We do not expect the year-to-date trends to be representative of the full-year pattern for store closures," says Coresight's report. "The total year-to-date permanent store closures in 2020 are currently significantly lower than this time in 2019 … but we predict that there will be a major uptick on the back of discretionary demand levels being below normal."

—John Stewart

MONTHLY MERCHANT METRIC

Growth in Same-Store Sales Year Over Year

Annual volume change/growth of retained (non-attrited) accounts for given period divided by total portfolio volume from same period of the prior year.



1. Trailing three months

Note: This is sourced from The Strawhecker Group's merchant data warehouse of over 3 million merchants in the U.S. market. The ability to understand this data is important as small and medium-size businesses (SMBs) and the payments providers that serve them are key drivers of the economy. All data are for SMB merchants defined as merchants with less than $5 million in annual card volume.

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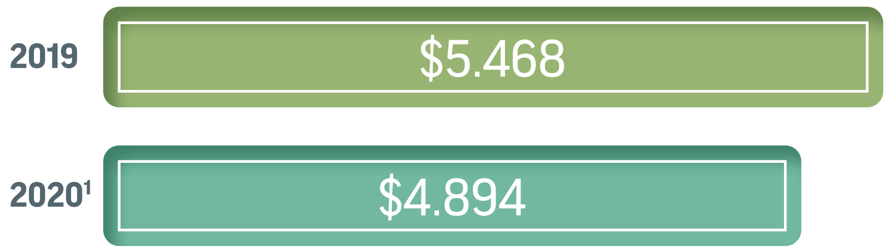
E-COMMERCE GAINS MOMENTUM

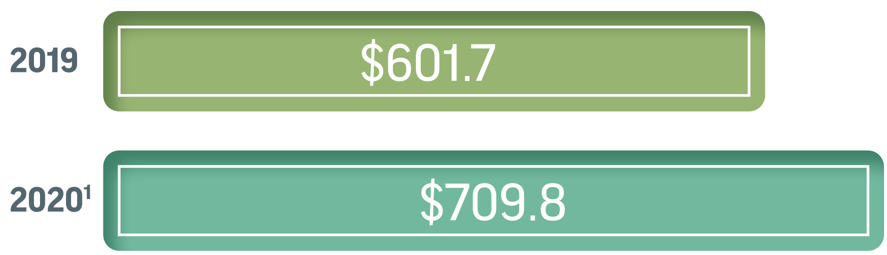
WHILE OVERALL RETAIL SALES SLUMP...

(In trillions)



...E-COMMERCE SALES ARE BOOMING

(In billions)



1. Full-year projection Source: eMarketer

Total U.S. retail sales, including auto and fuel, will drop 10.5%, to $4.894 trillion in 2020, a total not seen since 2016, forecasts eMarketer Inc. That's sharper than the 8.2% slump in 2009, in the midst of that recession more than 10 years ago.

E-commerce, however, is the bright spot. EMarketer says online retail sales will increase 18% this year to $709.8 billion from $601.7 billion in 2019.

Processors continue to report data that reflects online shopping growth. ACI Worldwide Inc. says its retail e-commerce transaction volume globally increased 81% in May compared to May 2019. The sportswear and sporting goods category was up 216% for the biggest gain.

The increase is coming with less risk. The fraud attempt rate by value clocked in at 3.4%, down 0.5 percentage points year-over-year and also down from 4.4% in April.

As strong as e-commerce sales have been, they have not been enough to offset declines at physical locations. New York City-based eMarketer says brick-and-mortar sales will weigh down overall retail sales in the long term.

It estimates sales at these locations will decrease 14% to $4.184 trillion this year. "It will take up to five years for offline sales to return to pre-pandemic levels," its report predicts.

"In just a couple weeks, as Americans sheltered in place, retail sales fell dramatically in March," said Cindy Liu, an eMarketer senior forecasting analyst at Insider Intelligence, the new parent company of eMarketer and Business Insider Intelligence. "With sales hitting their lowest point of the year in Q2, it will take years before consumer activity returns to normal levels."

The increase in consumer adoption of e-commerce has accelerated some trends. "Everything we're seeing with e-commerce is unprecedented, with growth rates expected to surpass anything we've seen since the Great Recession," said Andrew Lipsman, eMarketer principal analyst at Insider Intelligence.

"Certain e-commerce behaviors like online grocery shopping and click-and-collect have permanently catapulted three or four years into the future in just three or four months," Lipsman added. The top-growing e-commerce categories are food and beverage, at 58.5%, and health, personal care, and beauty at 32.4%.

The uptick in e-commerce sales will push online powerhouses into even stronger positions, eMarketer says. Amazon.com Inc. will control 38% of total retail e-commerce sales in 2020, followed by Walmart Inc. at 5.8%, and eBay Inc. at 4.5%. Other top 10 members are Apple Inc., The Home Depot Inc., and Best Buy Co. Inc.

—Kevin Woodward

ATMs CONFRONT COVID-19

Source: Company reports

Volume in some of its foreign markets is still way down as a result of the Covid-19 pandemic, but leading non-bank ATM network operator Cardtronics plc reported that same-store U.S. cash-withdrawal transaction volumes were off only 3% in the first half of June from a year earlier.

PSCU, a credit-union service organization, reported a different story last month, saying its ATM cash withdrawals are still down by more than 20%.

But Houston-based Cardtronics said in a business update that total cash dispensed in its U.S. ATMs jumped nearly 10% year-over-year on a same-unit basis in June following 3% growth in May from May 2019.

"With our recent performance and better than expected recovery, effective July 1 we will remove the companywide temporary salary reductions that we implemented on April 1," chief executive Edward H. West said in a statement.

With businesses closing or greatly reducing operations as states and cities implemented stay-at-home orders, Cardtronics' U.S. same-store withdrawals had plunged 28% in the second half of March and 23% in April before they improved to a 14% decline in May as restrictions began to ease in many places.

Transaction volumes have picked up the most outside the nation's 20 largest metropolitan areas, Cardtronics said, though large markets that re-opened early, such as Atlanta, Houston, and Dallas "are at prior-year transaction levels from May 31-June 12," Cardtronics said.

It's a different story in some of Cardtronics' other markets. In the United Kingdom, year-over-year transaction volumes have been down "less than 50% for the past several weeks," though that's an improvement from the 60% trough in late March. "Transaction levels in the U.K. continue to reflect the strict shelter-in-place orders that have been in place," the update says. "Additional easing of lockdowns are planned to begin this week; however, most bars, pubs, and dine-in restaurants are not expected to re-open until July."

Besides the United States and United Kingdom, Cardtronics, which owns 75,000 ATMs and manages 210,000 more, also operates in Canada, Mexico, Germany, Spain, South Africa, Australia, and New Zealand, according to a May investor presentation.

"In Germany, Canada, and Australia, performance through the pandemic and recovery has been gradual, with casino and gaming sites still heavily impacted," the report says. "However, most ATMs are now transacting, and we have seen more recent signs of accelerating improvement in early June as more restrictions have been lifted."

In South Africa, a high-growth market for Cardtronics, "transactions have nearly recovered to pre-Covid levels," the company said.

Meanwhile, St. Petersburg, Fla.-based PSCU, a credit union service organization, said in a mid-June Covid-19 impact report that cash-withdrawal transactions at ATMs "have been down 20% or more for 11 straight weeks, indicating less of a preference and desire for cash. For the most recent week, withdrawal amounts are down 23.8%." DT

—Jim Daly

UNDERSTANDING UNPREDICTABILITY

BY GIDEON SAMID
gideon@bitmint.com

ALAN TURING IS SEEN AS THE MOSES who led us all to the promised cyber land. His blueprint for a computing machine is the foundation of all the machines that have communicated worldwide, creating the ghostly universe of cyber. It was the same Alan Turing who posed the question: will it be possible to stealthily substitute humans in cyberspace? Could a machine in cyberspace become indistinguishable from a biological person?

Alan Turing foresaw what modern technology bears out. Increasingly we can't tell the difference. This conclusion comes with big philosophical baggage, and it also rings a loud alarm bell: fraud, deception, and crime have technology on their side.

With all the videos we watch, and with all the artificial reality that dazzles us, it is easy to forget that cyberspace is composed of streams of binary bits. It all breaks down to ones and zeros. And all those bits that flow out of humans can be imitated by a machine. One audio file of your normal conversation is all that is needed for a computer to fake your voice, your accent, to say something you did not say.

A few headshots become the input for a machine that instantly generates a video of you talking, smiling, frowning, etc. Indeed, deep-fake technology can generate fully believable pictures and videos of people who do not exist. As it goes, cyberspace has no guaranteed mooring in physical reality.

And then came Covid. As physical engagements became even more scarce, social engagement became close to 100% cyber—and 100% crime prone. And the most profitable field for the exploiters of this technology is payments. Indications are that personal identities are stolen at an alarming rate, all while the government is busy with more pressing challenges posed by the virus. The police, too, are too distracted to deal with non-violent cyber crimes. It's a perfect storm, with Bitcoin becoming the unofficial currency of the growing class of cyber criminals.

How to tackle this problem? Much hope and enthusiasm are vested in blockchain technology and in the power of the community of traders united by a governing protocol. Alas, if this community is made up of fake members, then so are its products.

The fundamental way to meet this Alan Turing imitation challenge is to moor cyberspace to physical space. Many solutions fit under this theme and they deserve strategic attention before it is too late.

Many mistakenly regard the use of biometrics as physical mooring. Biometrics is effective when a person is physically measured against his stored record, not in cyber space, where stolen biometric signatures readily steal identities.

A set of solution tools is being developed through nanotechnology, constructing sophisticated "physical anchors" for cyberspace. The flow of payment bits emanates from a physical chip where the money is stored in the chemical bonds therein, off the digital realm, immune to hacks. This technology leads to a hard digital wallet.

This is the revolutionary third leg. Normally, payees accept a payment by validating either the money or the payer. The hard wallet satisfies the payee on being paid from a trusted hard physical wallet. It's not very useful for remote payment, but it keeps the money flowing when the Internet is down since the wallet runs on a battery and operates on short-range communication.

It will take time, though, and until we turn the tide, we need to make the best use of the tools we have. In particular, it's best to keep changing payment habits. Our habit inertia is what hackers are counting on and homing into. Unpredictability is the powerful weapon we all underdeploy. DT

CASH ISN'T READY TO CASH OUT

BY BEN JACKSON
bjackson@ipa.org

HOW OFTEN HAVE YOU USED CASH in the last three months?

If you are like many people, the answer is not much. For me, the answer is twice, but more about that in a minute.

With the Covid-19 pandemic sweeping across the world, shoppers and merchants changed their habits as social distancing led to things like shopping and dining going virtual. Even the Federal Reserve quarantined cash coming back from Asia, according to news reports.

This has led some to ask whether cashless societies are near.

While people have asked this question off and on for years, the question has taken on a new urgency in the effort to prevent the spread of the novel coronavirus. The campaign against cash got to the point that Massachusetts Attorney General Maura Healey felt the need to remind the state's businesses that it was illegal to refuse cash.

In 2019, U.S. cash payments for all purposes totaled about $1.33 trillion, according to a study done by Javelin Strategy & Research for ATM provider Cardtronics. A follow-up online survey in April 2020 found that people were making fewer payments overall, but they were still using cash. Fifteen percent of U.S. consumers said they were using cash in April 2020, compared with 16% in the fall of 2019.

So, the push and pull over cash has intensified, but the real question is what will happen once the social distancing ends.

In the past few months, I've used cash twice: once for convenience—tipping a delivery driver—and once because it seemed like the safest option. My wife and I were driving to a curbside pickup from a butcher that didn't accept online payments. That meant paying in cash or with a card once we got there. It occurred to us that exact change meant we could pay without handling a card machine and an additional receipt.

So we pulled together the bills and coins and handed off the exact amount. It made the transaction smooth, easy, and more contactless than a card transaction would have been.

Contactless payments may be the big winner in the payments shakeout as people look to avoid touching card terminals. In January, Finextra reported on a Deutsche Bank study that predicted cash would hang around, but that cards might be displaced by phones, wearables, and other devices. The pandemic may accelerate this trend as shoppers try to avoid touching terminals.

There is even some evidence that the pandemic could lead to a cash revival of sorts. The town of Tenino, Wash., has started printing a local currency of wooden dollars to help its local businesses stay afloat, according to online news outlet The Hustle. The money is backed by U.S. currency, but the dollars can only be spent in town, which helps the local economy.

Shoppers concerned about their communities have been encouraged to shop local, and as towns, cities, and states continue to reopen, small business might begin encouraging a return to cash as a way to manage payments costs in a pandemic downturn. Shoppers looking to avoid debt in that same downturn may also return to cash as a way of controlling their budgets.

There is another trend that could lead to a return to cash. With talk of contact-tracing apps and health passports, the pandemic has raised new privacy concerns. Javelin's research found that over half of consumers say that cash protects privacy.

As the world enters whatever the new normal looks like, cash will still have a place in the payments landscape, and may even achieve a higher standing in some cases. DT

STEMMING THE TIDE

Yet another unwelcome effect of the Covid-19 pandemic is a wave of chargebacks. What can acquirers, merchants, and issuers do to limit the damage?

BY JIM DALY

AN INCREASINGLY SERIOUS manifestation of the economic damage caused by the Covid-19 pandemic is chargebacks, and plenty of them.

With the outbreak freezing the economy for most of the spring, consumers canceled trips and tickets for entertainment events. They looked forlornly for goods they had ordered but never received. Others kept getting billed from gyms and other recurring billers that had closed.

In these and many other instances, consumers often couldn't reach an agreement with the merchant about a credit or refund and instead initiated an expensive chargeback.

"I can tell you we definitely see chargebacks are up," says Johan Gerber, executive vice president of cyber and security products at Mastercard Inc.

PSCU, a St. Petersburg, Fla.-based credit-union service organization serving 1,500 institutions, had seen a 22% rise in chargebacks among its card-issuing members shortly before the pandemic hit, an increase driven mostly by fraud moving to online channels as a result of increased EMV chip card usage at the point of sale, according to chief risk officer Jack Lynch. But now PSCU is bracing for an even bigger increase.

"Now we're heading up to the higher 35-40% range," he says.

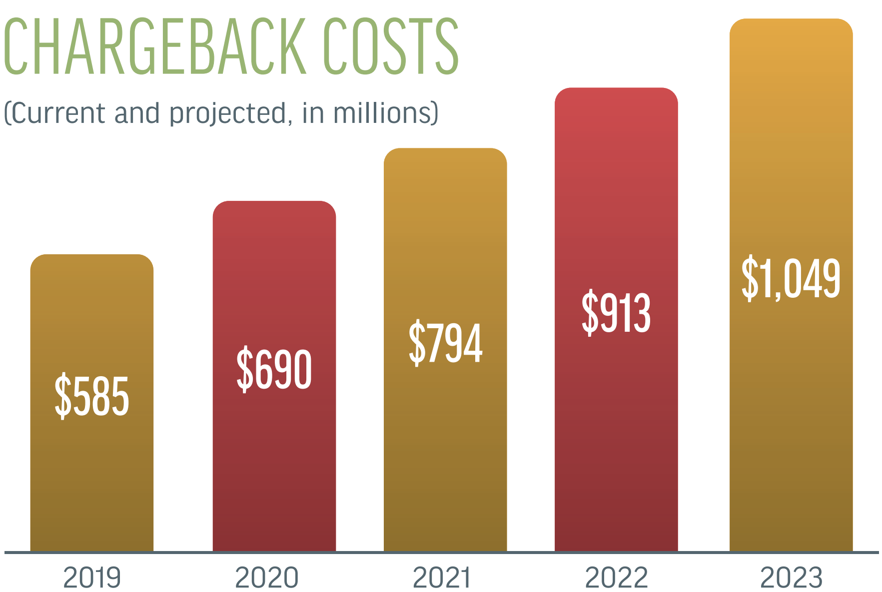
'A MASSIVE LOSS'

What's more, the nature of chargebacks has shifted. Until recently, fraud was the most common chargeback reason. "Now we see non-fraud chargebacks as the dominant form of chargebacks," says Gerber.

Mark Standfield, president of Midigator LLC, a chargeback prevention and reduction firm based in American Fork, Utah, describes the recent chargeback trends and experiences of some of his merchant and payment-processor clients as "seriously out of whack," "off the charts," and "catastrophic."

U.S. CARD ISSUERS' ANNUAL CHARGEBACK COSTS

(Current and projected, in millions)



Source: Aite Group estimates

The worst hits are being absorbed by travel-and-entertainment merchants, which have high chargeback exposure because they typically take orders well ahead of providing the service. Most of Midigator's T&E clients are online booking sites, agencies and ticket brokers.

"A couple" already have gone out of business, says Standfield. Another had been refunding customers until its bank stopped that practice because no new deposits were coming in. That set the stage for more chargebacks.

"It's going to be a massive loss for them and a massive loss for the acquirer," he says.

Many credit card issuers with travel-oriented rewards cards "are seeing pretty marked increases" in chargebacks, adds Trace Fooshee, a senior analyst at Boston-based research firm Aite Group LLC and the former head of fraud strategy at SunTrust Banks.

One driver of chargebacks was the refusal of many consumers who had canceled travel reservations to accept credits for future travel. "Immediately, people weren't wanting credits, they just wanted their money back," Lynch says.

Beyond the travel industry's woes, many retailers struggled to fulfill a tide of online orders from stuck-at-home consumers. For various reasons, sometimes the goods didn't arrive, Lynch says. Some short-staffed online retailers also had trouble handling returns, generating more chargebacks.

And chargebacks on recurring payments for gym memberships "just skyrocketed" when gyms kept billing customers after they closed, says Lynch, who also holds the title of CU recovery president at PSCU.

Besides gyms, chargebacks have increased from recurring billers ranging from parking garages to dancing schools to child-care centers, according to Gerber.

'FRIENDLY FRAUD'

How to resolve chargebacks, and who is financially responsible for them, is the subject of lengthy network rules. Compliance with Federal Reserve regulations to protect cardholders also comes into play.

'Now we see non-fraud chargebacks as the dominant form of chargebacks.'

—**JOHAN GERBER**, EXECUTIVE VICE PRESIDENT OF CYBER AND SECURITY PRODUCTS, MASTERCARD INC.

Excluding costs to merchants and acquirers, a single chargeback costs a card issuer $25 on average to process, according to a recent Aite report based on interviews with 1,004 consumers and executives at 10 large North American credit and debit card issuers as well as some large e-commerce merchants. Aite estimates issuers' chargeback costs at $690 million this year, and they'll grow about 15% annually to $1.05 billion by 2023 (chart, page 14).

Fraud has played a role in the recent chargeback surge, including "friendly fraud" in which the fraudster is not a hacker or unknown criminal, but the cardholder himself or a someone working with the cardholder. In the wake of Covid-19, some consumers initiated chargebacks on goods they claimed hadn't come, but the merchant had tracking information saying they had, according to Lynch.

"That also fits back into that friendly fraud thing," he says.

In fact, the Aite report says friendly fraud "represents a substantial portion of disputes." Among eight reasons presented for stopping their use of a card or person-to-person payment service, some 16% of the consumer respondents answered, "I disputed a transaction that was mine."

To ease merchants' burdens, Mastercard and Visa Inc. this spring temporarily relaxed some of their chargeback-related rules and fees. Both networks said they would not put certain T&E merchants into chargeback-monitoring programs until July 31, according to a Midigator blog post. Merchants get placed into such programs when their chargebacks exceed set thresholds.

Visa also suspended placement of T&E merchants into its fraud-monitoring program until the end of July, and the attendant fees. Mastercard suspended fraud-monitoring fees for e-commerce merchants until Sept. 30.

"Everybody is struggling with the unknown," says Jessica Velasco, marketing strategist at Midigator. "They [the networks] are probably doing it just to be fair."

'FRANKENSTEIN'S MONSTER'

There is plenty companies can do to prevent chargebacks, a major source of which is unclear information about purchases listed on a customer's online card or bank statement that spurs inquiries to issuers' call centers. More detail could deflect many of those disputes from becoming chargebacks, according to the Aite report.

"Twenty-seven percent of consumers report that, once they connected with the institution, the charge wound up being correct, which indicates that a substantial portion of call volume could be eliminated if the online statement provided more descriptive detail," the report says.

Most cardholders did some research before calling to resolve a transaction they didn't recognize or agree with, but only 23% of credit card holders and 22% of debit card holders called the merchant first. More than 70% of cardholders first called the issuer—the entity that gets the formal chargeback process going.

Aite's Fooshee says confusing transaction descriptors on statements are a legacy of the imperfect translation of merchant information issuers receive from networks into something cardholders will understand.

"It's sort of this inherited Frankenstein's monster of data elements," he says. "It's makes plain-English descriptions a real headache."

Payments firms also are deploying more technology to settle disputes before they get to the chargeback stage. Mastercard is trying to steer as many contested transactions as possible to Ethoca, a dispute-management tech firm it acquired last year.

"Ethoca is designed to facilitate cooperation among the parties, outside the chargeback process," says Gerber. As part of that effort, Mastercard has temporarily waived merchant fees for using Ethoca, he says.

"What they've really done is broker between issuer and acquirer," says Lynch.

Visa, which did not make an executive available for an interview for this story, provides a similar service through Verifi, a company it acquired in 2019.

DISTRACTED FRAUDSTERS

A third major tactic for reducing chargebacks is to continue attacking fraud, including friendly fraud. Aite's Fooshee notes that despite the long-term—and with Covid-19 turbocharged—growth of e-commerce, which traditionally has been more fraud-prone than point-of-sale card payments, the level of fraud "hasn't been as big as everybody thought it was."

But fraud-control executives "are waiting for the other shoe to drop," Fooshee says. That's because many fraudsters apparently have turned their attention to new opportunities presented by the Paycheck Protection Program and related federal stimulus efforts to counteract the Covid-induced economic downturn. They'll get back to card fraud once those programs are over, he predicts.

So when will the chargeback scene return to something resembling the normal days before the pandemic? Not for months, or perhaps even longer if people don't stay healthy.

"I don't think we're going to get to pre-Covid levels until some time next year," says Gerber. "We should see an improvement going on from here onwards, unless we have a second wave." DT

PLEASE PASS THE CASH—OR ELSE

The unwelcome message some merchants are getting from their acquirers in these Covid-19 days is that they must pony up more cash to reserve against potential chargebacks.

Payments and fintech attorney Darvin R. Davitian, counsel at the Washington, D.C., office of Perkins Coie LLP, estimates 15% to 20% of his merchant clients recently have received notices from their processors that they want to at least discuss the possibility of adding to their reserves. He didn't have figures on how many actually have had increases.

Davitian and two of his Perkins Coie colleagues recently wrote a blog post about reserves, a sensitive topic for both merchants and payment processors in the Covid-19 era. Airlines, hotels, resorts, and others that take orders well ahead of delivery of goods and services have experienced huge increases in cancellations, and many retailers have struggled with shipment delays, leading to canceled orders.

That affects their processors, which face financial exposure from chargebacks and related merchant problems.

For example, merchant acquirer Square Inc. increased its provision for transaction losses by 300% in the first quarter to $79.3 million from $19.8 million a year earlier, according to a Square regulatory filing.

But hard-pressed merchants might not have enough cash lying around to satisfy a demand for more reserves. Such demands often come with just three to five days' notice, otherwise the processor might hold back settlement proceeds.

"The merchant may not be in a position to do that," Davitian says. "It puts the merchant in a real pickle."

A mid-June story in *The Wall Street Journal* detailed how some small merchants using Square, Stripe, and PayPal for payment processing have been hit with holdbacks—one Square merchant had 30% of its transactions held for 120 days—for extended periods to cover possible refunds or chargebacks.

The Perkins Coie post lists eight reasons for so-called reserve triggers: excessive chargebacks; material deterioration of a merchant's financial condition; default under the processing agreement; the merchant entering into a chargeback-monitoring program; violations of payment card network rules; an increase in the merchant's time between taking payment and fulfilling orders; compliance violations; and the processor's determination of a merchant's insecurity or risk.

Agreements on the amount of a reserve can vary widely, though a frequent benchmark is three times average monthly chargebacks. As usual, small merchants have less clout to negotiate than big ones.

"Basically the processor can just pick a number," Davitian says.

But with Covid-19 still wreaking havoc, Davitian senses more processors are willing to talk with merchants about financial risks. "No matter what the rights of processors are, or no matter what the rights of merchants, it's really in their best long-term interest to sit down and have a conversation," he says.

'WE'RE ALL OMNICHANNEL NOW'

The pandemic accelerated developing trends at the point of sale. POS vendors that have mastered hardware, software, and processing could be best positioned to benefit.

BY JOHN STEWART

WHEN THE NOVEL CORONAVIRUS STRUCK in March, it drove consumers into their homes, leading to a surge in e-commerce spending. Brick-and-mortar merchants soon learned the arts behind contactless payments as virus-shy customers shunned keypads.

And dealing in cash became decidedly unwelcome. Only 8% of merchants equipped by Square Inc. were "effectively cashless" as of March 1, just before the pandemic struck, according to David Talach, Square's head of payments. By April 23, just 54 days later, that number was 31%.

But Covid-19 has underscored other, even more deepseated, lessons, as well. A big one is that POS technology that can integrate with accounting software, online shopping carts, and marketing systems confers a big advantage when dealing with a twitchy, stuck-at-home customer whose patience has worn thin.

"Ten years ago, integrated payments wasn't part of the jargon," notes Eric Grover, a Minden, Nev.-based payments consultant. "Now, it's all the rage."

Another, even bigger, one is that it really makes a difference when a multipart transaction can offer the customer one simple experience instead of multiple, disjointed steps. In this way, customers interacting with a merchant online, at the store, via mobile app, on social media, get the same no-fuss, no-muss treatment, with the same messaging, the same payment offerings.

That's not only a magnet for customers, it's also essential when the physical store isn't available. POS technologists who were sussing out the hardware and software for this before March are really hard at it now, with several pressing questions driving them.

For example, "How can I seamlessly move from card-present to card-not-present?" asks Ellen Linardi, rhetorically. "How can I be able to stand up an e-commerce store, or allow purchase online and return in store, with the business shut down because of Covid?" Linardi is head of product for Clover Network Inc., a POS technology firm that is part of Fiserv Inc.

That's neither easy nor cheap to pull off. But it was a trend before the pandemic, and now it's on fire. Indeed, to one extent or another, "every small business is in some way an omnichannel merchant now," says Derek Webster, founder and chief executive at CardFlight Inc., a POS technology provider.

'SOMETHING COMPELLING'

That could be a bit more aspirational than real as things stand, but it represents the next big market for companies that at one time simply styled themselves as POS terminal makers. That market may seem worlds away now, but none of these companies is standing pat.

Now, with the lessons of the last several months in hand, the market is rewarding providers that can combine hardware with software and processing. Look what happened early last month when Shift4 Payments Inc. went public. It priced its offering at $23 per share, but as soon as the bell rang the stock soared to $33. Almost two weeks later, it was trading at nearly $40.

Some observers aren't surprised. Stores need hardware, but they also need software and processing capability to tie together disparate shopping and payment venues, everything from the storefront to the Facebook store.

A single platform for accounting, data analytics, and processing, "is where the value is," notes Jared Drieling, senior director of consulting and market intelligence at The Strawhecker Group, an Omaha-based advisory firm.

Shift4 isn't alone. POS hardware firms saw this advantage years before the pandemic, but now there's urgency to move faster. For some vendors, it could be a matter of survival.

"One-off, standalone, or non-integrated POS systems will struggle to adapt, while integrated ecosystems will become commonplace," notes Square's Talach. "For example, if the POS system comes well-integrated with an online store, a business can be up and running with curbside pickup and other types of consumer-centric experiences in a matter of hours or less."

It doesn't hurt that combining software and processing can offer an attractive recurring-revenue stream, what the industry refers to as an "annuity." That provides a handy insurance policy against a slump in sales, which at least partly explains such deals as French processor Worldline S.A.'s move earlier this year to acquire terminal kingpin Ingenico Group S.A., also a French concern but a major terminal provider in North America, as well.

That $8.6-billion merger hadn't closed by mid-June, but more such deals are likely. "That is definitely a trend," says Rob Hayhow, vice president for business development, North America, at rival POS technology supplier Equinox Payments.

It's a trend, in part, because it takes considerable resources to build out the capacity for omnichannel transaction platforms. This includes not just money but high-level programming and routing expertise. Some players have concluded that, as expensive as such resources are, it's cheaper to buy it than to build it.

The proposed Worldline-Ingenico transaction "would not have happened if they didn't believe something compelling could be done with the Ingenico assets," says Grover.

'PLUGGING AWAY'

For now, Ingenico is focusing on streamlining the point of sale with technology like biometrics, says Bradford Giles, senior vice president of marketing and sales enablement. A device that can recognize a customer's voice or face, he says, not only supersedes EMV cards, it jumps over contactless waving or tapping. "It enables that completely frictionless transaction," he adds, referring to the POS industry's closest thing to a holy grail.

The concept got a boost from the Covid-induced mania for touch-free commerce, Giles says, but it's going to take time to work out its complexities. Not only does the biometric recognition have to work flawlessly, but transactions must be matched accurately with cards on file.

"We've been plugging away on this for several years in our labs," notes Giles. "It works, so now it's just how do you scale it, and how do you enable the third-party apps you need to support it?" Also, cardholders must opt in for it. "This isn't Big Brother," Giles adds.

But as attractive as the idea of melding hardware and software with processing could be, it comes with a potentially big problem: it can alienate the very entities that would otherwise refer business and certify new equipment.

Equinox, which relies on independent sales organizations and other third parties for sales leads, has avoided taking a position in processing for that very reason. "We've pushed back on that trend," says Hayhow. "We have strong partners we don't want to compete with in that space."

Rod Hometh, a payments consultant and former Ingenico executive, concedes the allure of processing is strong for a terminal company. But he estimates that offering services in line with those sold by established processing providers could put at risk certifications for new products that might otherwise have sailed through. "You go into competition with them and you jeopardize 50% of your sales," he estimates.

'Ten years ago, integrated payments wasn't part of the jargon. Now, it's all the rage.'

—**ERIC GROVER**, PRINCIPAL, INTREPID VENTURES

'TABLE STAKES'

For now, the exigencies induced by the pandemic have already altered the POS experience while hastening trends that were under way before the virus struck. The urge not to touch surfaces has not only boosted contactless cards but also lent momentum to mobile payments.

Necessity has introduced countless restaurants to complex offline/online blends, such as quick-response codes for menu callup and online ordering for curbside pickup. "We're seeing a surge in support requests" from eateries, says Chip Kahn, founder of Boomtown Network Inc., which helps merchants untangle POS problems.

And major-brand mobile wallets long in the market may finally be winning more usage as consumers seek out touchless payments. "Most of the merchants we're working with are doing Apple Pay when we turn it on," says Chris Lybeer, chief strategy officer at Revel Systems Inc.

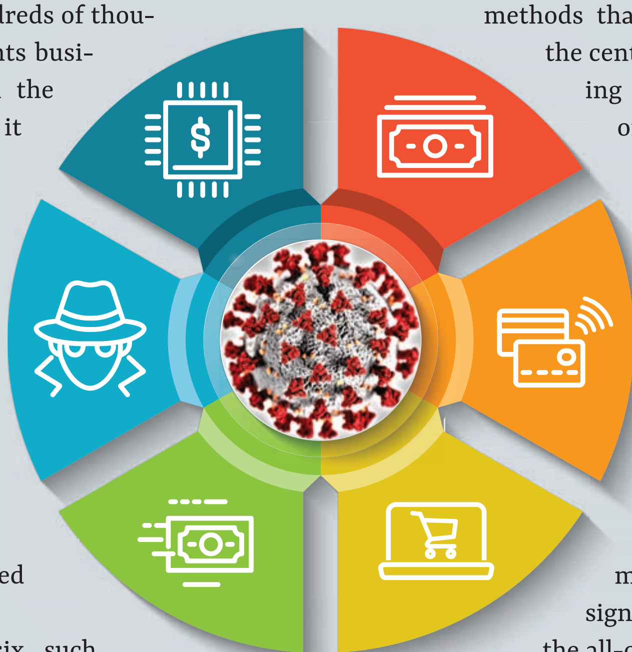
But the trend that overarches everything else, now and post-Covid, is the urge to go omnichannel. Traditional terminal companies ignore it at their peril. Says Clover's Linardi: "It's becoming somewhat table stakes." DT

HOW THE PANDEMIC CHANGED PAYMENTS (PERMANENTLY)

A deadly disease has proven a boon for some key trends while threatening cash and opening new avenues for fraud.

By Jim Daly, John Stewart, and Kevin Woodward

AN INDUSTRY WHOSE CLOSEST FAMILIARITY with viruses has come from the kind that infects computers has for most of this year had to contend with a pathogen that has sickened millions of people and killed hundreds of thousands. While the payments business is hardly alone in the sweeping adjustments it has had to make to contain the impact of the novel coronavirus, it is finding that a number of trends that were emerging pre-pandemic are now moving forward much more rapidly.



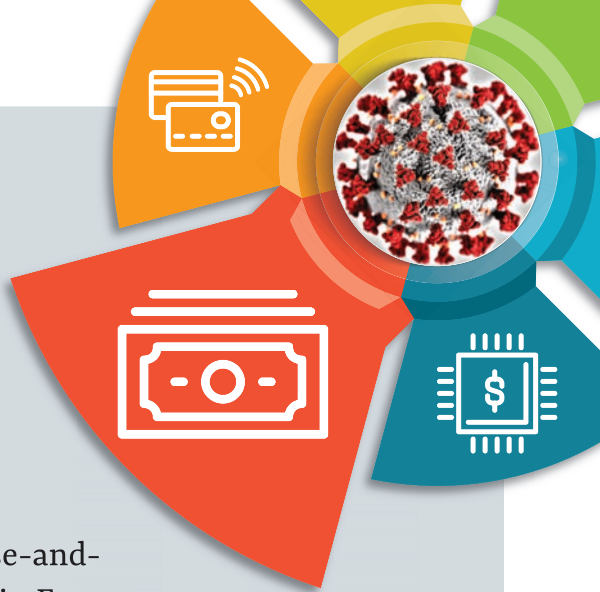
Indeed, some might now have such momentum as to be considered permanent.

Here, we consider six such trends. There may be a number of others, but these are the ones we have heard about most in our conversations with people in the business. Some, such as the moves to contactless payments and e-commerce, have gained understandable prominence in view of the urge to avoid infection and get shopping done under lockdown conditions.

Others, such as the impact on cash, illustrate ways that fear of infection can threaten payment methods that have survived through the centuries. And, as our reporting shows, crime in the form of payments fraud has rapidly made its own adjustments.

As we write this, the U.S. economy is fitfully reopening after long weeks in lockdown, and progress reports are arriving regarding a vaccine, though it may be long months before one becomes commercially available. All good signs, but it's too soon to sound the all-clear klaxons. For the foreseeable future, fear of Covid-19 will remain a factor to be reckoned with. We here present how the pandemic has, for good or ill, affected some of the most fundamental currents in modern payments.

CASH TO BE CASHIERED?



IT SEEMED LIKE CASH, the epitome of up-close-and-personal payments, had become the Payments Public Enemy No. 1 as the Covid-19 pandemic raged this spring. Some news reports vilified cash as a medium that fast-tracked the highly infectious disease. A number toll-road and bridge authorities stopped accepting cash, and many merchants encouraged payment with anything but cash.

Credit-union service organization PSCU reported that, as of the week ending May 31, ATM cash withdrawals were down 30% or more year-over-year for ten straight weeks.

Government added to the public's confusion about whether cash was safe. The Centers for Disease Control and Prevention issued guidance for commercial establishments to practice good hygiene, in part by promoting tap-and-pay contactless payments "to limit handling of cash."

But the U.S. Department of Homeland Security declared workers who service ATMs to be part of an "essential critical infrastructure workforce." The Bank of Canada urged retailers to keep accepting cash to ensure consumers could buy needed products and services. "The risks posed from handling Canadian bank notes are no greater than those posed by touching other common surfaces such as doorknobs, kitchen counters, and handrails," the central bank said in a news release.

David Tente, executive director for the U.S., Canada, and the Americas at the Sioux Falls, S.D.-based ATM Industry Association, isn't too worried about cash's long-term future. He acknowledges people haven't had much need for it in recent months during lockdowns.

"I think cash is going to come out of this just fine," says Tente, whose organization in June published its "ATM & Cash Revival Plan," which includes continuation of its fight to ban cashless stores and development of ATM hygiene and safety protocols. "People still prefer cash in a lot of instances." Tente adds that without cash, "You've got financial-inclusion issues" for people who don't want or can't get credit or debit cards.

Houston-based Cardtronics plc, the nation's largest ATM owner, is betting its future on performing more tasks cost-conscious banks traditionally have done, such as directly operating ATMs. At a May investor conference, Cardtronics chief executive Ed West expressed confidence consumers will continue using cash.

"Cash at the point of sale has been declining for a long period time, but that's primarily driven by an increase in the number of total transactions," West said. Citing Federal Reserve data, West argued that "cash continues to be in the United States roughly 26% of the most frequently used consumer payments, so it still has a significant number of transactions that are out there."

—Jim Daly

THE SUDDEN MAINSTREAMING OF CONTACTLESS

FOR YEARS, THE U.S. PAYMENTS INDUSTRY has talked about contactless payments. After this year, it may start talking about touch-free payments. Fearing infection, consumers have made it plain they don't want to touch anything at the point of sale, not keypads, not pens, not even a proffered stylus to peck out a PIN.

But that contact phobia is also reshaping some traditional arrangements in payments.

For example, restaurant patrons are demanding apps that let them scan a code to call up a menu, place an order, and pay for the meal—all while they're sitting at the table. In cases like this, the traditional card-present world is dissolving into the card-not-present space, says Ellen Linardi, head of product at Clover, a unit of Fiserv Inc. that makes point-of-sale payments technology (for more on POS trends, see page 20).

It's part of a broader definition of contactless, and it's likely to long outlast the Covid-19 pandemic. "Trends like scan and pay, that is going to persist," says Linardi.

To be sure, contactless payments have been available in the U.S. for years, and were making headway even before the pandemic struck. One big factor was the mass rollout of EMV technology, which lets card terminals read the EMV chip embedded in payment cards. Trouble was, not all merchants turned on the near-field communication capability in their new devices that lets them read the ultra-short-range radio signals from customers' cards.

That's changing fast. "We've been working with many customers lighting that up. I don't think anybody is thinking they can operate without it," says Chris Lybeer, chief strategy officer at POS device vendor Revel Systems.

In many cases the urgency has led to a clamor for contactless from merchants that still hadn't installed the devices in the first place. "We're seeing a lot of activity with existing customers. They want it now," says Bradford Giles, senior vice president of marketing and sales enablement at Ingenico, a major POS terminal maker. "Before, they wanted to squeeze the last year or two of life out of what they had on the floor."

Other vendors are seeing the same urgency, particularly as businesses reopen and merchants seek to soothe the anxiety of a fretful, mask-donning, social-distancing customer base. "Absolutely, folks are sticking this in right and left," says Lybeer.

Look for variations on the contactless theme, some sources report, including renewed interest in NFC-based mobile wallets and some experiments with quick-response (QR) codes, popular in Asia, less so in North America. Also on the docket for some merchants is text-to-pay, another technology that lets users avoid touching anything at the point of sale.

—John Stewart

THE EXPLOSION OF E-COMMERCE

STORE SHELVES STARTED EMPTYING early this spring as multiple states adopted shelter-in-place rules, so consumers turned increasingly to online shopping to buy groceries, replenish household goods, equip their newly-created home offices, and get toys, games, and books to keep their children occupied.

The result? The Covid-19 pandemic has pushed e-commerce to the forefront for many.

E-commerce sales accounted for 11.8% of all U.S. retail sales in the first quarter, which only included a couple of weeks of the shutdown, according to the U.S. Census Bureau. Until its next set of data arrives, businesses are providing insights into how the pandemic has altered e-commerce.

"We're seeing growth in full-assortment grocery and click-and-collect, while general-merchandise merchants really have not been that successful in terms of growth rate," says a spokesperson for Rakuten Intelligence, the San Mateo, Calif.-based data research platform of e-commerce powerhouse Rakuten.

Click-and-collect is a trend that is best positioned to have staying power beyond the Covid-19 crisis," says Lisa Tadje, corporate communications, Rakuten Intelligence.

"Beyond the 130% year-over-year increase in click-and-collect orders we saw in April and the 123% increase we saw in May, we're also finding an influx in new first-time click-and-collect buyers," she says. "This lends itself to long-term success as existing users become increasingly engaged with the method and new users become accustomed as well.

Indeed, a new natural level of e-commerce may be in the offing, suggests a report from Signifyd Inc., a San Jose, Calif.-based fraud-prevention firm. Signifyd has produced a weekly e-commerce pulse report since March, when most non-essential retail shut down across the country. In its first report for June, the company's data indicated a nearly 30% increase in e-commerce sales over its baseline, March 3-9.

Most verticals had increases in online spending in early June compared to early March. "In fact, of the 13 categories tracked by the Ecommerce Pulse, all but two—business supplies and beauty and cosmetics—are selling more online today than they were before the pandemic. The two down categories have suffered through much of the period of stay-at-home orders," the report says.

Will these changes persist following the pandemic's demise, whenever that comes? It's hard to say. "While plenty goes into shifts in consumer spending, it will be interesting to see, as in-store shopping becomes more accessible, whether awkward Covid-19 shopping experiences will drive consumers back to online options for more purchases," the Signifyd report says.

—Kevin Woodward

THE IMMEDIACY OF IMMEDIATE PAYMENTS

HISTORY MAY RECORD THAT 2020, the year of Covid-19, was the year that real-time payments proved their utility in the United States. From stimulus payments to peer-to-peer transfers, the need to get money into the hands of people with immediate needs was seldom more acute.

"I don't think there's any question that over the last 14 weeks we've seen a greater need to move money between people," Michael Bilski, chairman of the Faster Payments Council and chief executive of North American Banking Co., told *Digital Transactions* last month. The council is a cross-industry group working on ways to stitch together a real-time payment network in the United States.

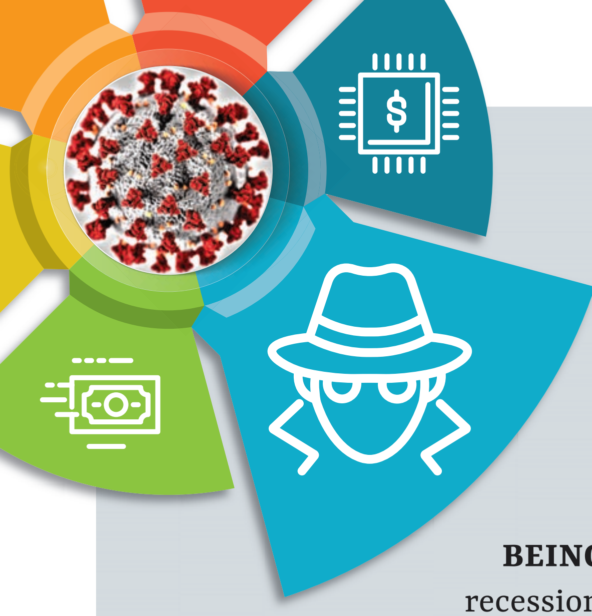
The emergency arose as millions were thrown out of work by business shutdowns, which helped control the rate of infection but triggered a deep recession. That left consumers in dire need of cash and made essentials, such as groceries, more frequent objects of transfers via real-time P2P systems like the bank-owned Zelle network. Zelle said in April it was already seeing a rise in paybacks to people for charities and groceries, as indicated by how users filled out the system's memo fields. Zelle is operated by the bank-owned Early Warning Services LLC, Scottsdale, Ariz.

The U.S. market is late in adopting the immediate movement of money, which caught on in Europe and other regions years ago. But now it could catch up fast, thanks to the market's experience during the Covid-19 emergency. "In general, businesses and consumers started to realize getting things faster is advantageous when a pandemic strikes," says Bilski, who adds there's now "a great need for safe, secure, and faster" payments.

Networks are moving to fill that need. The Clearing House Payments Co. LLC, a New York City-based operation owned by 24 big banks, early last month announced Huntington Bancshares Inc., Columbus, Ohio, was the latest institution to join TCH's Real-Time Payments Network. Huntington is one of the 24 TCH owners. At the same time, the Federal Reserve is moving toward launching its own real-time system, called FedNow, within the next three to four years.

Issues remain, however. The FPC recently issued a white paper on the matter of interoperability, which means getting financial institutions to link to each other when they're not all running the same systems. While enabling legacy batch systems to talk to newer real-time flows is part of the problem, Bilski says the larger issue lies in the looming need for seven-day weeks in back offices. "Are we all willing to do that?" he asks. 'We just have to start migrating the change. It's going to take some patience."

—John Stewart



THE RESILIENCE OF THE FRAUD VIRUS

BEING A PAYMENTS FRAUDSTER may be a pandemic- and recession-proof occupation. In good times, when all parts of the economy are open and consumer shopping is unimpeded, fraud activity is up. Now, as the Covid-19 pandemic proved, fraud activity is still rampant, just often in different ways.

It's reasonable to assume that with the boom in online shopping and other digital transactions, fraud would spike in this area. Instead, LexisNexis Risk Solutions has seen physical identity-focused fraud attacks rise, particularly in new-account openings. But mostly what the company has seen are changes in behavior, says Kimberly Sutherland, vice president of fraud and identity strategy at Alpharetta, Ga.-based LexisNexis Risk Solutions.

"We definitely saw an increase in individuals transacting digitally more than before," Sutherland says. A person might, when in the office, use a bank's mobile app to check on her account, but when working from home, she might use a PC. "In general, digital-transaction growth was two times faster than we saw before." LexisNexis Risk Solutions says new-device use increased nearly 40% in April compared to the average of January and February volume.

As more consumers adopt digital payments—a trend Sutherland suggests will continue—organizations will need to adapt their fraud-mitigation efforts. "As an organization they will continue to need to look at all channels a customer interacts with," Sutherland says. "That concept of having an omnichannel experience will be very important."

Information on scams may have broader appeal among consumers because so much more of the population is using digital channels than before. That's the assertion from Ashley Town, director of fraud services at Co-Op Financial Services, a Rancho Cucamonga, Calif.-based credit-union services organization.

"Fraudsters found greater success in using ... scams ... during the pandemic because of its widespread impact to cardholders," Town says. "Previously, when confusion would occur, it often was not something that a significant population was looking into. With Covid-19 having such a widespread breadth, we saw consumers across the country looking for information."

And with the increase in online commerce, businesses that have not historically handled card-not-present transactions find themselves learning to do so at speed, says Rich Stuppy, chief customer experience officer Kount Inc., a Boise, Idaho-based fraud-prevention firm.

"Shoppers are requiring BOPIS—buy online, pick up in store, and BORIS—buy online, return in store, which presents potential for fraud that businesses might not have been prepared to address, especially with the speed of approvals that are required for a frictionless experience," Stuppy says.

—Kevin Woodward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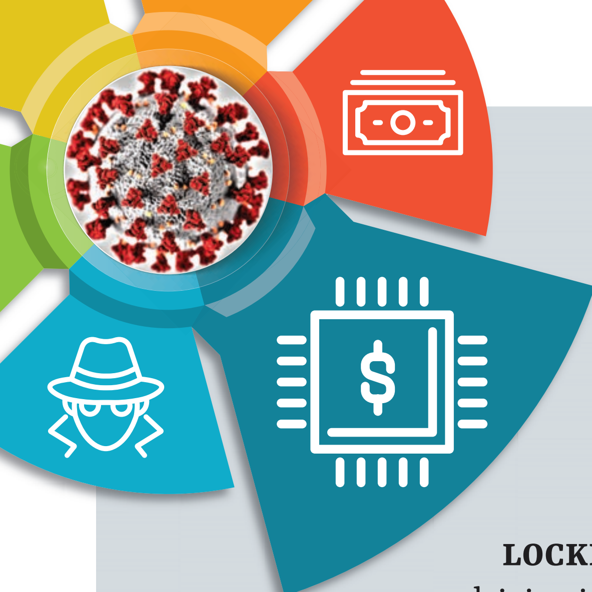


IoT PAYMENTS: DOWN, BUT NOT FOR THE COUNT

LOCKED-DOWN AMERICANS drastically reduced their driving in the spring, which naturally reduced demand for gasoline. Not quite so intuitively, reduced driving is also shaving Internet of Things payment volumes, according to David Nelyubin, a research analyst who monitors the IoT at Marlborough, Mass.-based Mercator Advisory Group Inc.

That's because many consumers hoping to get lower auto-insurance premiums now have so-called telematics devices in their cars that feed all sorts of driving information to their insurers—and generate automatic IoT-based premium payments ("Wellsprings of IoT Payments," May). But fewer miles traveled translates into fewer dollars paid in premiums, according to Nelyubin.

In addition, sales are down for such things as Internet-connected printers that track ink usage and automatically order and facilitate IoT payment for new ink cartridges, Nelyubin says. And if you've lost your job, do you really need an IoT electric toothbrush capable of tracking the wear on the brush head and ordering a new one, when a traditional electric model or manual toothbrush will do the job? Many payment-enabled IoT devices are still luxury goods that can be substituted for cheaper replacements.

"Overall, just from the virus, there is definitely going to be a decrease in IoT payments," says Nelyubin, who predicts a 5% decline this year.

The long-term outlook is brighter. Nelyubin foresees 7% to 15% annual IoT payment growth in the next few years "depending on how the economy rebounds."

Some of the growth will come from new IoT devices which, unlike their predecessors that facilitate payment between the device owner and only a single manufacturer or provider, enable the consumer to choose from an assortment of similar products from different vendors.

An example is the "Smart Feed Automatic Dog and Cat Feeder, 2nd Generation" device from Radio Systems Corp.'s PetSafe brand. The device, which looks like a coffee maker, lets the pet owner, using a smartphone app, program the amount and time when food is dispensed into a bowl. Instead of being locked into one food brand, the pet owner can shop among multiple vendors and order refills through Amazon.com Inc.'s Amazon Dash Replenishment service.

Nelyubin says the PetSafe dispenser is the first consumer example he's found of this new "open-loop" IoT model. "It's really cool," he says. DT

—Jim Daly

The PetSafe automatic pet feeder can order more pet food through Amazon's Dash Replenishment service.


DIGITAL TRANSACTIONS
News

THE $43 BILLION PAYOFF

The FIS-Worldpay merger not only created a processing behemoth, it set the stage for an operation with diverse revenue streams that can withstand shocks like Covid-19.

BY KEVIN WOODWARD

A YEAR LATER, the FIS/Worldpay merger—one of three giant processor combinations in 2019—appears to be reaping the promised benefits.

If a company that created itself in a $43 billion merger and that processed a combined $1.34 trillion in volume in 2019 can be summed up in one word, "agile" may not come to mind straight away. But, that is the word most apt for FIS, which closed on its merger with Worldpay Inc. last summer.

It was the largest of the three giant 2019 deals. Fiserv Inc. and First Data Corp. was valued at $22 billion and the Global Payments Inc./Total System Services Inc. (TSYS) combination was a $21.5 billion transaction.

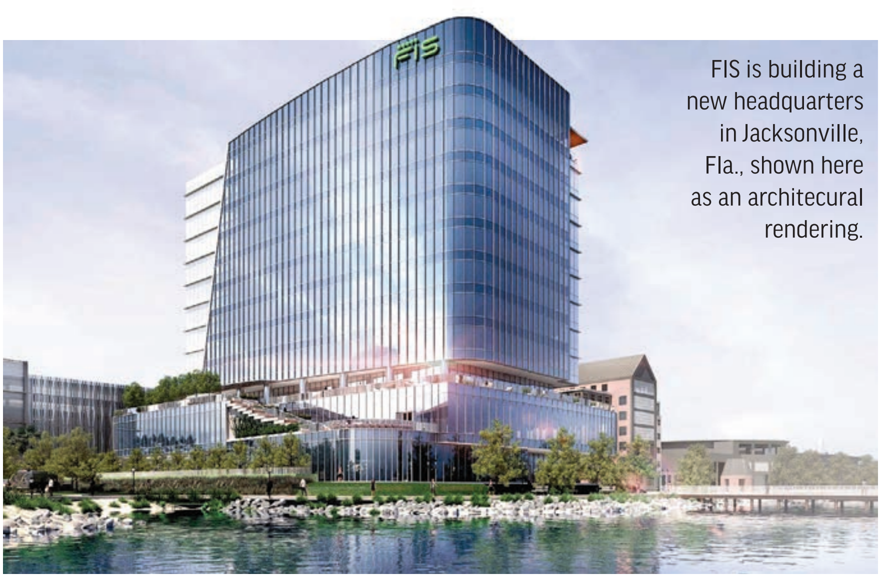
While every payments company can pride itself on being attuned to change and having the flexibility to adapt, FIS—legally Fidelity National Information Services Inc.—has been rash enough to make these characteristics part of its overall strategy.

Where some processors developed or bought a point-of-sale system, FIS opts to provide the payment processing and related services to a variety of providers. It's a partnership model that preceded both companies. Harking back six years ago, Vantiv Inc., a predecessor to Worldpay, bought Mercury Payment Systems LLC, which created a strong demand for integrated payments by working with software developers. Even before Worldpay, FIS had completed its share of acquisitions, such as the 2009 deal to buy Metavante Technologies Inc.

Now, the integration of FIS and Worldpay is essentially realized. "From an integration standpoint, things are going extremely well," says Jim Johnson, executive vice president and head of merchant solutions at Jacksonville, Fla.-based FIS. "I've been with FIS for 20 years. I've been through a few of these."

'BLURRING THE LINES'

The combo already has notched some notable wins. Likely drawing on Worldpay's e-commerce capability, a global retailer is consolidating



FIS is building a new headquarters in Jacksonville, Fla., shown here as an architecural rendering.

(Illustration: FIS)

agreements with some 40 providers exclusively with FIS, Gary Norcross, chairman, president, and chief executive said during the company's most recent earnings call in May.

Johnson lists other recent accomplishments, such as developing a corporate-payments service that takes advantage of Worldpay's accounts-receivable expertise and FIS's legacy accounts-payable business. FIS is consolidating its data operations under a chief data officer to tap into insights from each legacy company and shape them into an improved service. The post-merger FIS now operates in 100 countries and has had success in its cross-sales efforts, Johnson says.

The international expansion was a major opportunity made possible by the merger. "We've done extremely well with our loyalty as a currency product with some marquee wins we talked about publicly," Johnson says. In February, FIS said consumers at financial institutions enrolled in its FIS Premium Payback network can use rewards points to pay for purchases at PayPal-accepting merchants globally.

The ability to cross-sell into client portfolios is continuing to shape new product development, Johnson says. Everything in development is done with an eye to cross-selling capabilities, he adds.

"People are reaching out to new places for financial capabilities," he says. "Financial institutions have to compete against the likes of Amazon Pay and Apple Pay more so than in the past." Competition is driving some of that. New technology companies are blurring the lines between the types of products a retailer might want and the needs of financial institutions, he says.

Making cross-selling capability a paramount element will be essential for growth. "Growth in the merchant section for FIS/Worldpay will be in cross-selling services," says Krista Tedder, director of payments at Javelin Strategy & Research, a Pleasanton, Calif.-based advisory firm.

"Some solutions available to U.S. financial services will prove valuable to FIS merchants, specifically around the areas of protecting digital assets," she says. "The experience of protecting online and mobile banking will help merchants. Identity fraud [involving] merchant accounts is growing with fraud spiking to 39% of all new account fraud in 2019 compared with 24% in 2018. Account-takeover tools would also benefit merchants. Merchant-account takeover fraud and email payments such as PayPal also saw significant spikes in 2019."

COHESIVE PRODUCTS

Analyst Jared Drieling views the cross-sale opportunity as a chief tactic for FIS. "They're not trying to own the whole cycle," Drieling, senior director of consulting and market intelligence at Omaha, Neb.-based The Strawhecker Group, tells *Digital Transactions*. "First and foremost, they will focus on cross-selling opportunities."

What will materialize, Drieling says, are more cohesive products that can tap the assets of each side of FIS, merchant processing and bank technology. "They're utilizing both sides," he says. "As you weave in some of these solutions into the banking operations, there's a lot of synergies. Over time we will see more products and services that take on an FIS flavor or Worldpay flavor, from a single standpoint. That's clearly unfolding with their recent announcements."

Just in June, FIS announced Open Banking Hub, which enables Worldpay merchants to enable digital bank-account payments as an option in their online stores. Starting in the United Kingdom, the service enables consumers to pay directly from a bank account and get real-time balance updates during the checkout process.

Like any large player in payments—FIS had $935 million in revenue in its merchant-solutions segment in its 2020 first quarter—FIS faces competition from like-size peers and small organizations. By comparison, Fiserv, the Brookfield, Wis.-based processor that bought First Data, counted $1.25 billion in revenue for its merchant acceptance unit in its first quarter.

"When you think about merchant acquirers that have really dominated, there's pros and cons of that model," Drieling says. "When First Data was the 800-pound-gorilla, that left the door open to entities that could specialize."

But FIS says its model has the flexibility to serve a broad swath of merchants. FIS doesn't have to provide its own point-of-sale system if it can partner with those who do. "Any part of the supply chain is not out of scope for us," Johnson says.

In the small-merchant space, it partners with independent sales organization, independent software vendors, and payment facilitators in multiple verticals, he says. "We partner and integrate tightly with them," he says. "We're very focused on the customer experience."

'Financial institutions have to compete against the likes of Amazon Pay and Apple Pay more so than in the past.'

—JIM JOHNSON, EXECUTIVE VICE PRESIDENT AND HEAD OF MERCHANT SOLUTIONS, FIS

MORE TO COME

The full implications of the FIS/Worldpay merger have still to play out, suggests Javelin's Tedder. "The merchant market has not yet seen the most impactful changes that will come from the FIS/Worldpay merger," Tedder says.

"The coronavirus impacts to commerce will most likely accelerate the changes needed to … build an interoperable issuer and merchant platform–leveraging consumer payment habits that can be gleaned from understanding the financial-services relationship, and building payment strategies for merchants," she adds.

And there's no discounting the impact of the Covid-19 pandemic. Tedder expected 2020 to be rife with requests for proposals for new processing agreements, but that has not happened as the pandemic suspended much of this activity. FIS's diversification will help it weather the pandemic.

"Out of the three mergers (Fiserv/First Data, Global Payments/TSYS, and FIS/Worldpay), the most diverse company will come out of the coronavirus stronger," Tedder says. "FIS/Worldpay, balancing merchant and financial-service providers, will have the most diverse client base and revenue diversification."

Johnson says the short term goal for FIS is to continue to focus on cross-selling opportunities by bringing more products to the merchant and financial-institutions spaces. In the long term, "we're going to continue very much on new product development," he says. "We will continue on the modernization to improve self-service in the client experience and continue to use data insights to reduce fraud." DT

THE PROGRAMS AND SOLUTIONS SALES PARTNERS AND MERCHANTS NEED NOW

Given the challenging set of circumstances we are all currently facing, time is of the essence. That is why it is absolutely imperative that payments technology companies equip both Sales Partners and their merchants with the solutions, programs, and support they need to compete right now. At North American Bancard, that's precisely what we have committed to doing.

We continue to add to our lineup of proprietary Payanywhere Smart Solutions, with our new Smart Terminal Mini and Smart POS+, which are coming soon. They'll join payment devices like our Smart Terminal, Smart Flex, and Smart Point of Sale to give business owners even more solutions they need today, like those that enable curbside, NFC contactless checkout, and online ordering. No matter which solution business owners choose, they'll enjoy reliable, lightning-fast EMV transactions that take just two seconds on average.[1]

We've also made multiple enhancements to our innovative Edge program, which combines Flat Rate Pricing with Cash Discount. Now, Edge allows for exact deposits as well as simplified statements that allow merchants to reconcile their processing easier than ever.

We've noticed that due to the COVID-19 situation, even merchants who previously passed on the Edge Program are now flocking to it. So, while you're working remotely, instead of focusing exclusively on landing new merchants, now is the time to make sure your existing customers are set up with Edge.

We've even added a Competitive Edge promo that allows you to earn an additional $50 for every new or existing merchant you upgrade to Edge. Plus, a $500 kicker for every 10 qualifying merchants, and a free Smart Terminal demo unit once you reach 10 new or upgraded MIDs on Payanywhere Smart Solutions with Edge pricing.[2] You also have the option to purchase a Smart Terminal now, and we'll reimburse you once you hit 10 deals during the promo period. That's on merchants already 2-3 times more profitable than traditional ones!

Finally, we have also committed to helping our Sales Partners up their earnings with our newly enhanced Peak Bonus program. Now, you can pocket a $500 activation bonus for every Payanywhere Smart Solution merchant you board on Electronic Payment Exchange (EPX), our wholly owned in-house payment processor, up from $400. Plus, you'll take advantage of a profitability multiplier that's been increased from 12x to 14x, not to mention a cap that's been doubled from $5,000 to $10,000.

1. Transaction time is measured from the time the card is inserted until approval.
2. Requires 3.8461%+ Flat Rate Pricing and a Payanywhere Smart Solution, Salido, or POS Pros' point of sale solution. Must be submitted and approved Friday, May 1st, 2020 through Tuesday, June 30th, 2020. Merchants must activate by Tuesday, June 30th, 2020. $500 per-10 kicker paid Thursday, July 2nd, 2020. $50 per-MID bonus paid weekly. You must be on our standard compensation program to qualify.

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To learn more about these and other ways North American Bancard can help you nurture your merchant relationships and grow your portfolio, call 877-223-6577 or visit www.gonab.com.

Fintechs in particular face the risk of meritless lawsuits.

HOW FINTECHS CAN LOWER LIABILITY

The key is to review customer contracts at least annually. Here are three crucial reasons why.

BY STEVEN ROSENWASSER

Steven J. Rosenwasser is an Atlanta-based shareholder in the commercial litigation practice of Greenberg Traurig LLP.

WHEN USED PROPERLY, litigation is an important and effective tool for enforcing a company's contractual obligations and other rights. However, some individuals and entities misuse the legal process, bringing meritless lawsuits in an attempt to force companies into paying monetary settlements to avoid the disruption, risks, and cost of litigation.

Fintech companies are particularly at risk of facing meritless lawsuits. They are customer-facing and often have contracts with hundreds of thousands, if not millions, of customers. That broad contractual reach substantially increases the risk of litigation, including class-action lawsuits that can cost millions of dollars to defend and irreparably harm a company's reputation.

Fortunately, there is one simple step companies can take to minimize the likelihood of lawsuits and financial exposure: Fintech companies should review their contracts at least annually, particularly customer-facing contracts such as merchant terms and conditions.

THE LAW CHANGES

Why? Here are three reasons.

First, regular reviews are important to ensure that previously enforceable terms have not become unenforceable through a recent change in the law. This is a particularly important issue in the fintech industry, where laws are still being developed and constantly changing.

For example, last year Maryland passed HB777, which prohibits certain payment processors from charging a termination fee greater than $500. Though payment processors conducting business in Maryland may be generally familiar with the new law, there are nuanced provisions they may overlook.

Notably, under one provision, certain payment processors can charge a termination fee under $500, but only if the fee is disclosed clearly and conspicuously in a bold, 12-point font.

Another important example involves restrictive covenants, such as non-solicitation agreements. Many fintech companies rely on an internal or external sales force to solicit merchants and to maintain goodwill with those merchants once they become customers. That goodwill is invaluable, and it is important that it be protected.

While many fintechs wisely rely on non-solicitation agreements to protect their customer relationships, they typically do not regularly review the terms of those

MORE STRAIGHT TALK FOR ISOs:
MAINTAINING A RELATIONSHIP DURING A CRISIS

A Q&A from First American's Angela Carranza and Ross Paup

Failure to communicate with customers during a crisis can come at a high cost: lost business, lack of trust, etc. How is First American ensuring customers know they are top of mind in today's environment?

Ross: Hard times will always reveal true friends. While COVID-19 has challenged the efforts of many companies in recent months, First American remains true to its reputation and is working proactively with ISO partners to help alleviate the pressure on merchants, wherever possible, through minimization or suspension of fees. We are in this together, and First American's making every effort to mitigate the pressures of today's business environment.

Angela: We're showing top of mind attention by focusing on products that can help our customers protect their livelihoods and that of their merchants. For example, our digital app, 1stPayBlaze, allows fast onboarding to help ISOs sign new merchants and drive revenue. From a merchant-facing perspective, contactless payment solutions, such as SwipeSimple, are enabling merchants to sell in a wide range of environments without touching a credit card or asking customers to touch a payment device. And hosted payment forms are enhancing online payments with the highest level of data security. Customers want to know that they are top of mind, but they also want to know that you 'get' what they need—and that you're willing to find or create the solution to match. That's the First American difference, and it's what helps our partners and their merchants to thrive.

Accessibility is key to customer satisfaction, particularly in a technology-driven industry. What is First American doing to maintain its high-touch reputation when business looks different right now?

Ross: We are an extremely accessible organization; getting to know both our prospects and our partners on a personal level is a point of pride for First American. As our office-based staff began working remotely, our IT team quickly mobilized resources to avoid any interruption of service to our ISOs and merchants. Our standard communication has been enhanced with video to maintain "face-to-face" interaction, and our relationships remain fully intact, and possibly stronger, as a result of our continued support.

Angela: While we look forward to the return of trade shows and the business opportunities that come with that, we, like everyone else, have had to get comfortable with interaction in a very different way. We've welcomed the virtual component as a chance to show partners what we are really made of. Our accessibility is evident every time we help a partner expand their sales team or grow their merchant portfolio. Each of those takes a series of steps, no matter who you process through. First American's proving ground is in the positive business outcomes we create for our partners and their organizations.


Angela Carranza is Manager, Strategic Partnerships


Ross Paup is Senior Manager, Strategic Partnerships

You know you're in good hands when the chips are down, and your payment processor does "this" to help your business survive and prepare to once again thrive?

Ross: There are three things to ask yourself: "Was my processor taking good care of me when everything was "'normal?'" If so, "Have they maintained that standard during the crisis?" And, "Do they have a plan to help me maximize my opportunities through and after the crisis?" Having the right partner has never been more important as both ISOs and merchants adjust to the 'new normal' of driving business in a social distancing environment.

Angela: Your payment processor should have your best interests in mind regardless of the situation; that's where First American excels. We treat every partner as a part of the family and consider ourselves an extension of their business. We create defined sales strategies to benefit our partners across dozens of industries, provide the tools that make it easy for developers to integrate payments within their software, and offer powerful ecommerce and mobile solutions that help businesses withstand difficult times and thrive for the long-term.

If there is one takeaway your ISO should bring from COVID-19, it's this…

Ross: We need to focus on what we can control; how we react to the situation, how we prepare for what is to come. For some of our ISOs, that means diversifying merchant types to be better equipped for the future. For others, it means leveraging technology for themselves and their merchants. Being adaptable and willing to embrace change are the keys to recovering—and prospering—in the post COVID-19 landscape.

Angela: Whether they have reduced your fees, protected your revenue with contactless solutions or bolstered your online presence, you should be able to name one tangible result your processor has helped your business achieve.

agreements to make sure they comply with current laws.

For example, in many states, the laws are becoming friendlier to employees/independent contractors, meaning that broad non-solicit provisions that may have been enforceable a few years ago are not enforceable now. If a fintech company does not regularly review its restrictive covenants, it may learn that they are unenforceable when it is too late, for example, when it loses a lawsuit seeking to hold a former employee accountable for stealing its customer or proprietary information.

KEY PROTECTIONS

Second, fintech companies should review their contracts, particularly merchant terms and conditions, to ensure that they contain all of the available contractual protections.

For example, many fintech companies are unaware that their contracts can often include terms that (1) shorten the statute of limitations by several years, and (2) allow merchants or others to bring written complaints about errors or overcharges within a few months or waive any claims relating to such issues.

These terms and others can materially reduce, if not eliminate, liability. Indeed, I recently represented a fintech company that used a contractual written notice provision and, as a result, it was able to have a class action dismissed.

Moreover, even where litigation continues, these terms can dramatically reduce financial exposure. For example, a contractual term reducing the statute of limitations from four years to one year will effectively reduce financial exposure to any claim by 75%.

The right time to add these provisions is before a lawsuit is filed. Waiting until litigation commences is often too late and will likely result in the loss of benefits of the protections.

LEGACY RISKS

Third, over the last several years, the fintech industry has experienced substantial consolidation through mergers and acquisitions. As a result, many fintech companies are now using legacy contracts—i.e., contracts from the company they acquired—without having reviewed and/or revised them to ensure they contain critical protections.

For example, in light of the Supreme Court's decision in the Concepcion case and the more recent cases applying and expanding it, it is relatively easy to prevent the massive exposure associated with class-action litigation: simply include in your terms and conditions an arbitration clause with a class-action waiver.

But many fintech companies lack that basic term in their contracts, often because they use legacy contracts they acquired through an acquisition without reviewing them for this detail. As a result, the acquiring company does not realize that it has inherited, and is unknowingly using, contracts that lack an arbitration clause with a class-action waiver; i.e., they are using contracts that unnecessarily leave them exposed to class-action litigation.

A simple review of legacy contracts allows an acquiring company to make sure its contracts have all the necessary protections, including, where appropriate, a class-action waiver. This is not to say that it is always appropriate to have an arbitration clause with a class-action waiver, but the decision about whether to incorporate such a clause should be made knowingly after careful and thoughtful deliberation. But it is important to determine whether you have a class-action waiver and, if not, decide whether one is appropriate before a class-action lawsuit has been filed, that is, before it is too late.

Having your contracts reviewed and updated can ensure they contain the protections a fintech company needs while materially reducing the risk of facing costly and disruptive litigation in the future. By avoiding litigation, fintech companies can focus on growing their business and their profits. DT