

Fraud in Fintech Ecosystem- Digital Lending Perspectives

Tolulope Omoleye-Osindero



DIGITAL LENDING - KEY FACTS

Over 170 Lending Mobile Apps

Using the number of applications received by the FCCPC as a guide

Transitioning to Super Finance Apps

big digital lenders are transitioning from digital lending to super finance apps - Branch, Carbon, Fairmoney, Kuda, PalmCredit, PayHippo etc.



Common Business Forms/Structures

Moneylenders, Microfinance Banks, Finance Companies.



Access To Credit

Progress in access to credit for individuals and SMEs can be attributed to these startups. Now you have banks and even payment companies in the digital lending space.



Digital Lending- Features

- Instant Loans (BNPL, Business Loans, Asset Financing)
- Limited (Not Zero) Documentation
- Digital Verification - identity, occupation, residence etc
- Digital Credit Scoring /Assessment
- Extensive reliance on alternative data - access to contacts, sms, social relationships, bank/transactional data etc. Up to thousand data points
- Simple Application Process - Web, Mobile App, USSD, Whatsapp.
- Higher Risk Appetite compared to Traditional Banks
- Largely digital collection - auto debits for repayment, mobile collection,
- Heavy on innovative model around the end to end credit journey



Digital Lending - What to Note

- Players are mostly startups funded with venture capital.
- Expectations on growth and transaction numbers towards next funding and eventually, exit.
- Tendency to ignore common risk pitfalls with lending
- **Higher Fraud Exposure** - Fintechs experience an average fraud rate of 0.30%, twice as high as the credit card fraud (Not Nigerian Data)
- **Significant Fintech Space** - Digital Lenders have raised north of \$500m (Nigeria)

Fraud in Fintech - Useful Facts



- True state of the amount lost remains unknown as many entities do not report, cover up fraud as other forms of operational losses.
- According to NIBSS, about NGN3.5b was lost to fraud via mobile channels between December 2022 and May 2023.
- Fraud results in financial losses which threatens a FI's ability to scale or grow or even attract investors.
- For Digital Lenders, when fraudulent borrowers do not repay over time, it eventually leads to erosion of capital as a result of the credit losses.

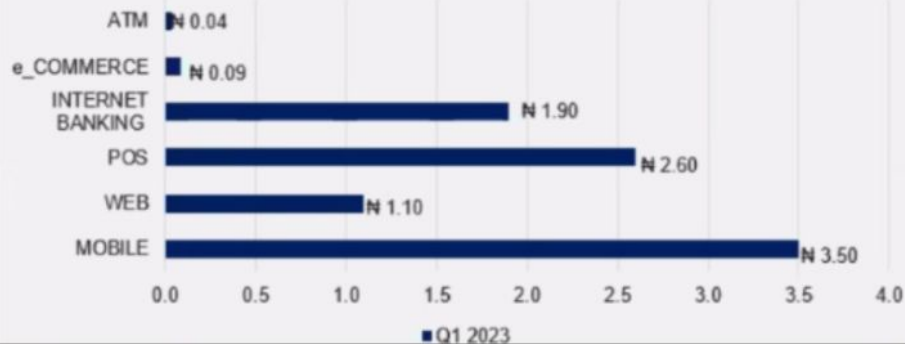
**Fraud Count Dec 2022 - May 2023
In Thousands**



Actual Loss Value Dec 2022 - May 2023 (NGN, In Billions)



**Actual Loss Value by Channel
Dec 2022 to May 2023
(NGN, In Billions)**



Fraud Expressions



1. Identity fraud
2. Account Takeover
3. Scams
4. Unwillingness and refusal to repay loans
5. Employee collusion/connivance
6. Exploitation of loopholes - using knowledge of technology, infrastructure to carry out nefarious actions. This could be by staff or ex staff or just highly skilled people.
7. Unauthorised funds transfer

Issues

- **People**

- Young, innovative workforce with little or insufficient experience or knowledge of banking/financial markets especially at the decision making level.
- Dishonest employees that have not undergone background checks .
- Friction between engineering/product and compliance teams

- **Process**

- Simple onboarding versus outright negligence
- Absence of controls and safeguards in product development and operations
- Limited audits or reconciliation
- Harmonised testing of separate products and susceptibility to exploitation. If the user journey for loans is easier than wallets, can bad actors get on your platform through wallets?
- Weak or non existent transaction monitoring systems

- **Infrastructure**

- Access to database - Identity, BVN etc..
- Stale and out of date software or systems.
- Failure to adopt or invest in fraud detection tools
- Weak Security

**How do you keep Fraudsters
Away?**

The background is a solid orange color. In the upper right quadrant, there are several decorative elements: a small circle with a pie chart, a larger circle with a pie chart, and another small circle with a pie chart. These circles are semi-transparent and overlap each other.

Current Fraud Arsenals - Digital Lending

- Improved KYC- Liveness check, Matching Against Database
- Internal Watchlist
- Stricter Account Recovery Processes
- Bespoke Red Flags List
- Bespoke or Third Party Transaction Monitoring Tools
- Device Uniqueness
- Background Checks on Employees
- Fraud Solutions - Machine Learning Models for detection and prevention
- Mobile Device Management for remote companies
- Cybersecurity Regime - Access Policy, Traffic Monitoring, Vulnerability Assessments,
- Proactive detection using data - analysing loan defaults data, specific locations, transaction patterns, specific institutions etc. running experiments.
- Fraud Teams - risk professionals, engineers, compliance teams.

Way Forward -



- Strengthen our Digital Identity Framework (Digital Footprint Analysis, Linking NIN/BVN/Phone Numbers/Social Identity/Residential Information).
- Capacity Building
 - Fintech NGR/FSI/CIBN collaboration on certification
 - Investment in Technology- AI and Fraud Analytics, Fraud Detection Software etc
 - Investment in Security

Way Forward -

- Collaboration
 - Knowledge sharing sessions with Fintech Partners
 - Clarity on expectations especially around risk management with Fintech Partners. For example what is the minimum security and KYC/KYC requirements you require from your FIntech Partners. Exclusion and Indemnity are insufficient
 - Legal Framework for Sharing Data that includes non CBN licensed entities.
- Enforcement
 - Service Restriction
 - Blacklisting erring partners
 - Blacklisting Bad Actors- BVN Watchlist, Industry Watchlist

Thank You

The image features a solid orange background. In the top right corner, there are three decorative elements: a small circle, a medium-sized circle, and a large circle. Each of these circles contains a smaller, semi-transparent version of itself, creating a layered effect. The circles are arranged in a roughly triangular pattern.