The Complete Chargeback Management Guide

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Table of Contents

The Root of the Problem

Despite significant global payment innovation, merchants are at the mercy of an antiquated transaction dispute process.

When the transaction dispute system was institutionalized, it was intended for issuers to provide relief for their customers when they felt they were being improperly charged for a product and/or service.

40+ years later, the transaction dispute process hasn't changed much. What has changed is the sheer volume of disputes being pushed through this process.

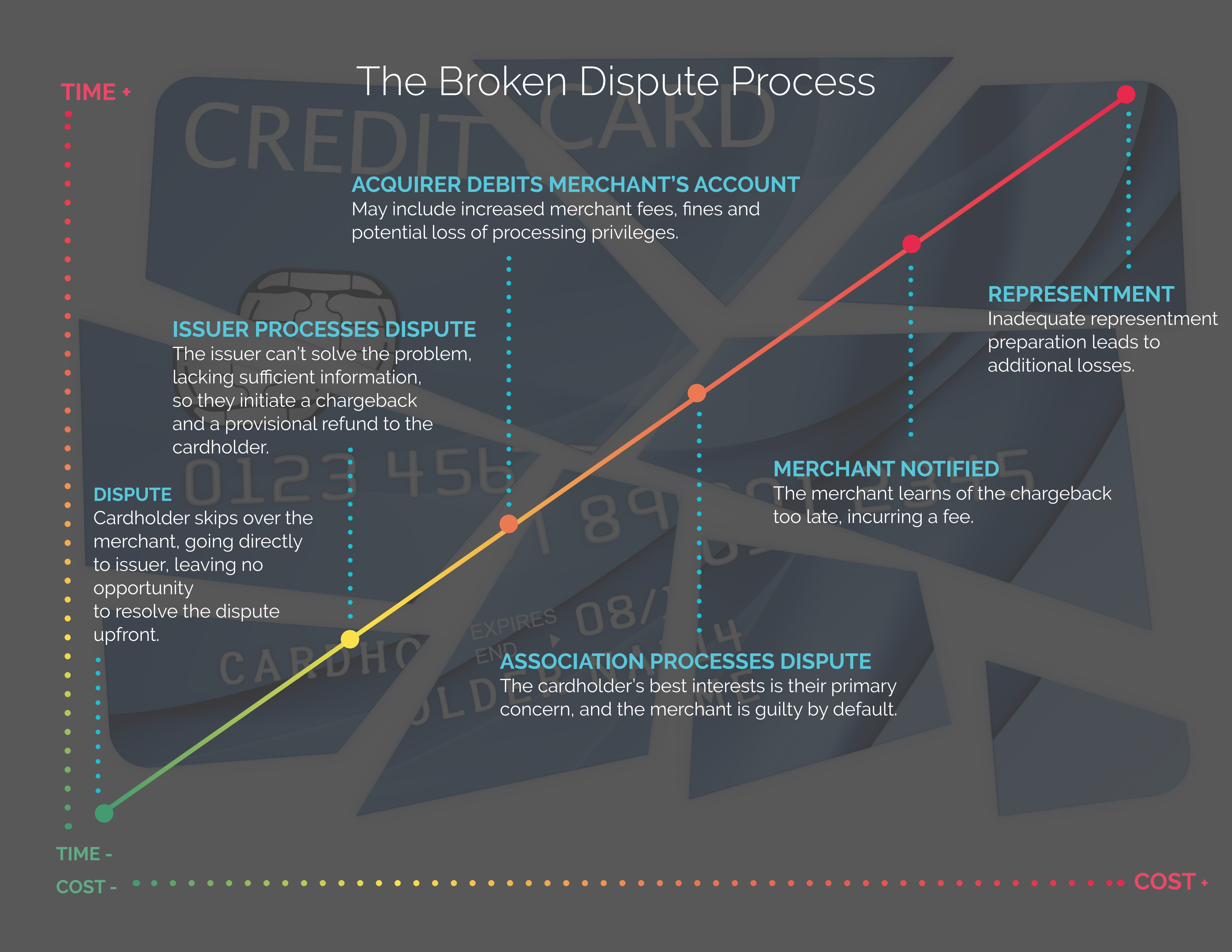
The many faces of transaction disputes have created a complex, expensive and aggressive problem for merchants and issuers alike.

It starts with the cardholder initiating a dispute with the bank for a number of possible reasons. The bank lacks the information needed to resolve the cardholder's concerns, and the issuer's only recourse is to escalate the dispute. The merchant doesn't learn about the dispute until it becomes a chargeback!

First-party and true fraud volume has increased too. Unscrupulous cardholders have learned how to manipulate the system to cheat merchants out of products, services, and unsubstantiated refunds.

This guide will show you how reducing transaction dispute volume and altering the process can yield immediate and significant profit improvements. However, it requires a unified approach to dispute management that includes fixes to customer service, marketing, and e-commerce -- PLUS a multi-layered defense in-depth fraud strategy AND improved issuer - merchant collaboration.

When thinking about transaction disputes, it helps to understand the flaws in the process as well as the costs that compound every step of the way.


The Broken Dispute Process
TIME +
TIME -
COST -
COST +
DISPUTE
Cardholder skips over the merchant, going directly to issuer, leaving no opportunity to resolve the dispute upfront.
ISSUER PROCESSES DISPUTE
The issuer can't solve the problem, lacking sufficient information, so they initiate a chargeback and a provisional refund to the cardholder.
ACQUIRER DEBITS MERCHANT'S ACCOUNT
May include increased merchant fees, fines and potential loss of processing privileges.
ASSOCIATION PROCESSES DISPUTE
The cardholder's best interests is their primary concern, and the merchant is guilty by default.
MERCHANT NOTIFIED
The merchant learns of the chargeback too late, incurring a fee.
REPRESENTMENT
Inadequate representment preparation leads to additional losses.

The Face of Transaction Disputes

For every customer seeking to game the system, another is just as likely to be confused, misguided, or even forgetful. There are many faces to transaction disputes that can be labeled as intentional or unintentional.

CONFUSION OVER BILLING DESCRIPTORS

Unrecognizable merchant billing descriptors

Transactions on a cardholder's billing statement are restricted to 25-character descriptor max. This challenges merchants to effectively describe business and transaction details.

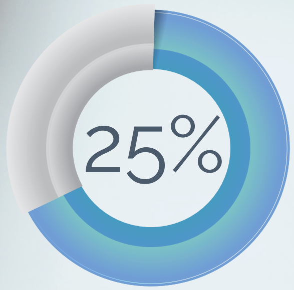
FRIENDLY FRAUD

The customer intentionally or unintentionally exploits gaps in the dispute process.

UNINTENTIONAL Friendly fraud transaction disputes are generally not filed out of malicious intent. One-click “buy buttons” are quickly becoming the norm for online checkout. The problem with enabling faster checkout and conversions is that it increases the chance of buyer’s remorse, which can result in more friendly fraud.

INTENTIONAL First-party, friendly fraud, or “I didn’t buy that” fraud are are largely deliberate forms of sophisticated shoplifting, where a customer attempts to obtain a refund for something they didn’t actually purchase. In fact, merchants believe that over 34% of chargebacks arise from friendly fraud [1].

40% of friendly fraudsters are repeat offenders[2]



OF CONSUMERS HAVE DISPUTED TRANSACTIONS MORE THAN ONCE[3]

The State of Friendly Fraud

Friendly fraud is an all too common problem that merchants face. Up to 45% of consumers have disputed at least one transaction in 2017, and 25% have disputed more than once. As it has been adopted industry-wide, the term "friendly" fraud is arguably a misnomer — there is nothing friendly about manipulating the system for ill-gotten personal gain.

Ironically, in the case of chargebacks, the lack of friction in the buying process has created a new set of risks for online merchants. This has spurred the "I didn't buy that" type of friendly fraud. Because it's so easy to make a purchase online, too easy to flag a transaction, too easy to bypass the merchant and too easy to "game" the system, difficulty has increased for both the issuer and merchant to differentiate true fraud from friendly fraud. In fact, the issuer commonly makes the mistake of marking an order as fraud even in the case of friendly fraud.

With the outgoing growth of online shopping, there is an expectation among modern shoppers of omnichannel functionality to expect faster checkout times. This has lead to the proliferation of friendly fraud, where vulnerabilities in the less tangible authentication process exist. As a result, losses are mounting for merchants.

FRAUDULENT CHARGES

Sensitive credit card information is stolen and used fraudulently.

A customer initiates a transaction dispute based on criminal activity. Usually, the credit card issuing bank will identify this and notify the cardholder first. CNP fraud has risen dramatically, as fraudsters discover new ways to exploit opportunities and vulnerabilities online.

The Financial Impact of Fraud

Chargebacks have become a $31 billion problem in the U.S. Worst of all, merchants bear the brunt by absorbing two-thirds of the costs associated with them[4]. Consumers have come to view transaction disputes as a common recourse to resolve issues with purchases, which has led to the prevalence of friendly fraud. In 2017, nearly half of all consumers (45%) disputed at least one transaction, and 25% have disputed more than one.

Merchants and issuers have very different perspectives when it comes to handling friendly fraud. Merchants believe that 34% of their chargebacks stem from friendly fraud, whereas issuers feel it is half that at 17%[5]. One theory for the discrepancy is that, as the most common first point of contact, issuers receive more information on the dispute from the customer, leading them to believe the customer is right.

Furthermore, merchants are at a disadvantage when responding to a dispute, particularly when they become involved late in the process. In this, merchants face three key challenges:

- Accessing all necessary documentation from different sources
- Deciding which disputes are worth fighting
- Keeping track of timelines of dispute timelines

Often, by the time they are informed of a disputed transaction, it is too late for the merchant to resolve the problem, and the resulting costs directly impact their bottom line.

Experiencing the worst hit of all, merchants feel the pain long after a dispute due to customer churn – with up to a 63% decrease of customer loyalty.

Chargebacks were a

$31 Billion

problem in 2017[6]

63%

of consumers cease merchant patronage after a dispute[7]

MERCHANT ERROR

The transaction wasn’t processed correctly or it was duplicated.

SUBSCRIPTION CANCELLATION ISSUE

An oversight in a subscription cancellation policy causes confusion or enables fraudulent behavior.

ITEM NOT RECEIVED

A failed authorization in the checkout process can lead to the cardholder not receiving the product, or receiving a different item.

Many of card associations’ transaction dispute reason codes are attributed to merchant error. A customer may not understand the functionality of the website, or inadvertently opt-in to a service. This is exacerbated with order by voice, mobile-shopping app and other digital payment options.

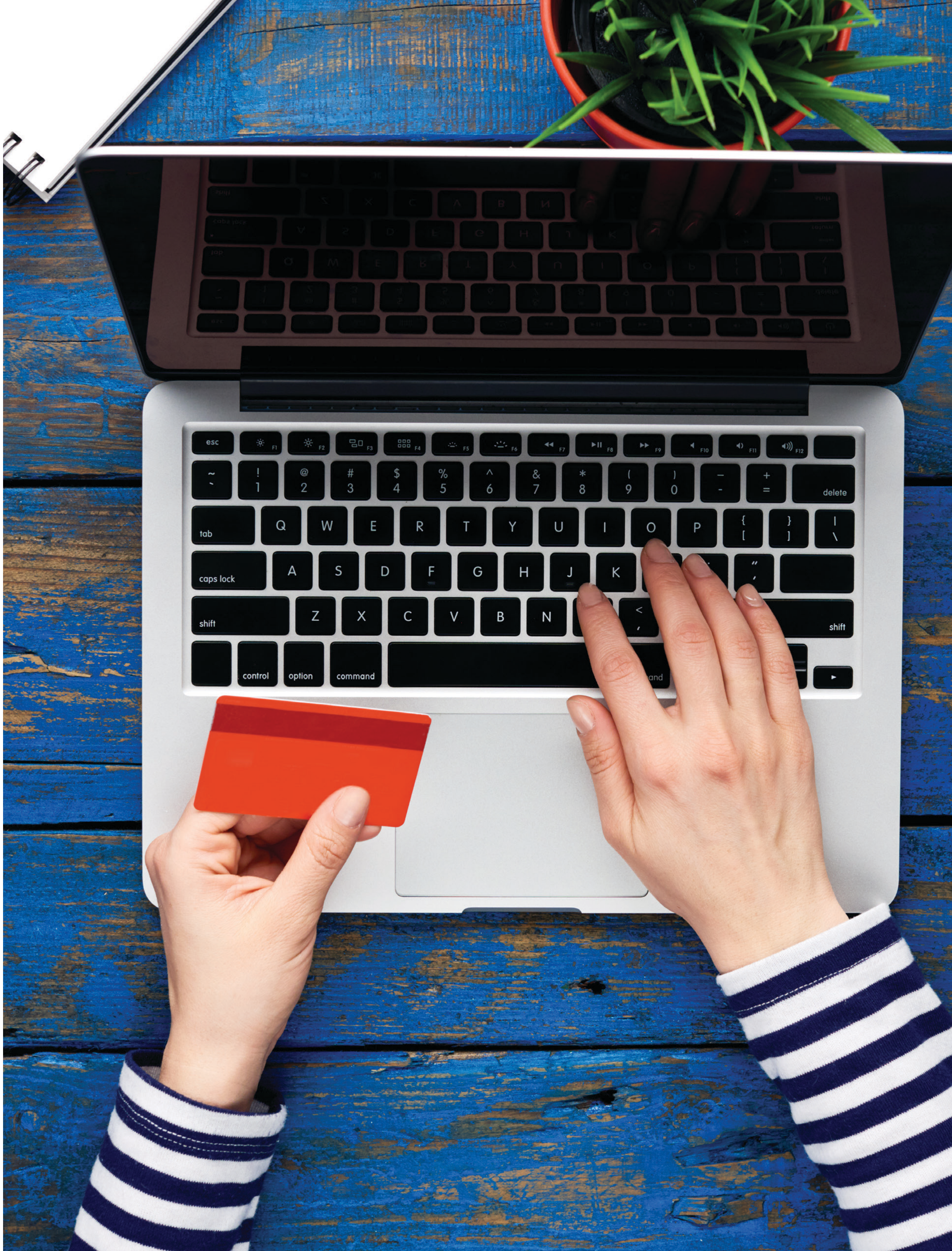
Issuer and Merchant Perspectives

Transaction disputes affect the entire payments ecosystem.

Issuers are under pressure from regulators to protect cardholders.

Merchants typically experience the worst effects from disputes, shouldering the greatest burden by paying fees, fines and penalties in addition to refunds and the cost of lost goods and services. Merchants don't benefit from a frictionless environment like the banks do – what comes across as poor customer experience is really just a missed opportunity to communicate with a shopper early in the transaction life-cycle.

Consumers are also adversely affected via the increased cost of goods and services, as merchants try to recover lost profits. We've outlined the specific impacts to each party in the following pages.



No Shortage of Pain for the Merchant

There are fees, fines, and penalties associated with every step of the transaction dispute process, leading to increased costs and potential loss of processing privileges.

Retrieval Requests: When the issuer requests an electronic copy of the receipt from the acquirer, the merchant is typically charged a processing fee of $5–$15 for each retrieval request.

Chargeback Fee: Merchants pay an acquirer fee — as high as $100 — for every chargeback, even when the cardholder's claim is rejected.

Arbitration Costs: For cases that escalate to arbitration, the merchant must pay for the costs associated with this process. If the merchant loses the case, They must pay the payment network a hefty fee, often up to $500.

Chargeback Penalties: If the merchant's collective chargeback rate exceeds 1% or 1.5% of their total sales volume, (as governed by Visa and Mastercard rules, respectively), that merchant is placed into a chargeback monitoring program, which can tack on escalating fees up to $100 per chargeback.

Other Fees: Some credit card companies may charge "review fees" or other fines for merchants that do not have a transaction dispute reduction plan in place.

Chargeback-to-Sale Ratio: Merchants who have excessive chargebacks could be put on a monitoring program or even face termination of their account.

No Shortage of Costs for the Merchant

INCREASED FRAUD: Merchants held out of the early dispute process have to catch up on cardholder disputes, giving fraudsters the upper edge.

MANUAL REVIEWS: Unwarranted transaction disputes lead to unnecessary manual processing, reconciliation and reporting — draining a merchant's time and resources that could be better spent towards forwarding business objectives.

LOST GOODS/SERVICES: Lost in the flood of fees, fines and operational costs are the actual losses of goods and services (as well as shipping costs). Recurring and subscription merchants feel the pain, too. 91% of businesses use the same fraud management tools for mobile and web channels, leaving these channels more susceptible to criminal activity.[8]

LOST CUSTOMERS & BRAND DAMAGE: Any dispute that isn't resolved quickly or efficiently is going to create a negative experience for a customer and a loss of sales.

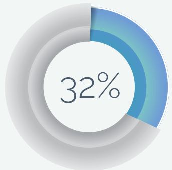
CUSTOMER EXPERIENCE: Due to payment advances and the informality of the merchant-customer online relationship, the merchant rarely gets the opportunity to directly communicate with the customer early in the transaction life-cycle. As a result, any lack of clarity at the point of sale can give rise to a transaction dispute.

FALSE POSITIVES: An increased fraud threat can lead to intensified fraud scoring or fraud prevention tactics. The result is highly sensitive fraud controls that can trigger false positive transactions, causing declines for legitimate purchases.

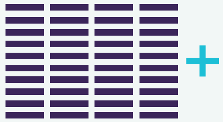
False Declines by the Numbers

$118B

$118 billion is lost per year to false declines.[9]



32% of customers who experience a false decline choose not to shop with that merchant again.[10]



There can be as many as 40 false declines for every legitimate transaction[11]

Operational Costs Are Hurting Issuers

While the merchant shoulders the biggest burden of the dispute problem, the issuer is by no means left unscathed. The payments ecosystem does not enable merchants and issuers to collaborate and communicate efficiently, and issuers are experiencing enormous losses as a result.

A cardholder that does not recognize a transaction (or is seeking to game the system) presents both an immediate and long-term impact for issuers. When a cardholder skips over the merchant to handle a transaction dispute with the issuing bank, the bank is immediately inundated with inquiries and becomes the unintended intermediary tasked with making a judgement call on the sale.

Issuers absorb huge operational costs and loss of revenue when they lack compelling and actionable order details to validate the disputed sale. Dispute volume rises, customers become angry, and the issuer is left to deal with time-consuming arbitration, an unnecessary increase in representment volume, brand damage and increased small balance write-offs.

$7.1B Cost from liability to U.S. issuers in 2017

How the Costs Add Up

MISSING DATA: The cardholder and issuer need access, upon the initiation of a dispute, to enhanced transaction information, such as when and where the order occurred, a detailed item description, or merchant name and other CRM details in order to address a transaction dispute.

LACK OF INFORMATION/DATA: A collaboration network is needed to seamlessly provide issuers with a scalable way to confirm fraud and understand transaction dispute data. This would dramatically reduce fraud losses and chargebacks and provide a better experience for cardholders.

UNHAPPY CUSTOMERS: Issuers with a high volume of disputes are often ill-prepared to handle cardholder disputes to the best of their abilities. This inefficiency and the lack of a speedy resolution damages the relationship between the cardholder and issuer, which hurts retention and damages the brand.

COMPLIANCE COSTS & INCREASED RISK: Reason code complexity forces issuers to implement and learn new systems and processes. Additionally, issuers face elevated compliance risks, fines or legal actions, not to mention increased regulatory scrutiny and reputational damage any time there is a dispute that isn't handled quickly.

UNMANAGEABLE PEND QUEUES: The back- office handling of disputes requires a large amount of outbound documentation. As disputes increase, operational costs mount as service representatives are being called in to help with simple disputes. What's more, association rules require that the issuer identify and block disputes that do not meet the criteria for the selected dispute category.

Cardholders dedicate time to reach a resolution on disputes, often having to contact the issuer several times to finalize the matter.

Issuers must often staff under-prepared customer service representatives to handle disputes. Such personnel typically do not have sufficient information on the transaction, nor are they comprehensively trained to provide a quick solution to the customer's satisfaction.

Inefficiency and the lack of a speedy resolution hampers the relationship between cardholder and issuer, damaging both customer loyalty and issuer brand association.

How to Prevent Chargebacks

Once the foundational process has been fixed, the next step is recovering losses accrued from the dispute process. In fact, many merchants are collaborating with issuers to improve fraud prevention strategies and mitigate disputes before they become chargebacks in the first place.

Without a process for early intervention, it is impossible to validate the legitimacy of the sale with the cardholder, or enhance identification of fraud – which increases the amount of time and money spent addressing these inquiries.

Foundational Process Improvement

What Can You Do Now (by Department) to Mitigate Disputes

Marketing/ WEB	• Clear articulation of billing and return policies in every offer • Clear payment descriptors	• Easy cancellation processes • Require strong customer passwords on registration	• Educate staff on Transaction Dispute fraud
Customer Service/Sales	• Deal with issues promptly • Train CSRs to spot fraud and unusually large orders	• Use of "spammy" or fake information to place an order • Track patterns and communicate these across departments	• Keep your credit card statement descriptions simple
Finance/ Billing	• Dedicate resources to analyzing the true reason for the disputes to better inform the subsequent handling.	• Invest in solutions that facilitate collaboration with issuers. • Investigate fraud and non-fraud disputes equally.	• Reduce false declines through alternative communication tactics outside the traditional authorization processes.
IT	• Investigate AVS, 3-D Secure and Tokenization • Improve data-sharing with issuers	• Ensure your systems maintain customer data accuracy and shipping and credit card security	• Use automation to flag suspicious orders in CRM
Shipping/ Fulfillment	• Monitor for suspicious use of international shipping addresses • Create lag between order and dispute	• Create a replicable procedure for preparing all necessary data to dispute	

Checklist to Improve the Dispute Process

Merchants should implement an end-to-end fraud and transaction dispute management system that ensures payments are protected early in the transaction life-cycle. It starts with including the merchant in the dispute process from the beginning. Your dispute mitigation strategy should accomplish the following:

- Increase first-call resolution - reduce downstream cost
- Rethink cardholder experience
- Quickly identify operational problems
- Proactive communication including up-to-the-minute order history and notifications
- Realistic shipping timeframes
- A seamless and simple checkout process
- Include feedback loop that drives process improvements
- Clear descriptors on credit card statements
- Improve dispute resolution cycle time

Transaction disputes don't have to be costly— they can be prevented.

The consumer's ability to dispute a charge is getting easier and easier. Consumers are guilty of gamesmanship, with an increasing population of consumers well aware of their transaction dispute rights and taking advantage of both the technological advances available and the leeway issuers give them.

To address the complexity, manual processes, and gray areas of the dispute problem, merchants and issuers alike need a solution that enables them to resolve the dispute at the customer level.

1. **A multilayered defense in-depth strategy:** One that is focused on addressing a transaction dispute before it escalates, and quickly handles chargebacks that are unavoidable. This provides merchants with more time, money, and resources available to invest in their own business and less time worrying about managing fraud and chargebacks.

While the complexities of costs associated with transaction disputes will always exist, there are already changes from the major card networks to help merchants reduce the number of disputes. Merchants need to stay informed about changes in the industry.

2. **What merchants need for better cost containment is the right tools:** Post-billing dispute alerts now enable communication between merchants and issuers about actual dispute data. This allows for problems to be resolved before they escalate, which avoids the chargeback altogether and stops a loss before it happens.

Merchants with high chargeback fees may be inclined to boost their fraud mitigation resources, when in reality they should be taking a proactive approach to preparing for and preventing disputes, learning from past cardholder motives and behaviors.

The transaction dispute problem isn't slowing down. Industry experts are predicting it's going to get worse before it gets better. Merchants must be equipped with the right partner to manage their disputes before the problem escalates beyond their control

Introducing Verifi's Total Chargeback Management Network

Verifi's Total Chargeback Management Network prevents and resolves costly chargebacks throughought the transaction dispute life-cycle.

Verifi allows timely and effective communication between everyone – issuers and merchants – on a collaborative network that lets all parties come together to prevent chargebacks. Verifi directly integrates with top U.S. issuers, providing unmatched service, quality, and accuracy for merchants in collaboration with issuers to resolve disputed payments, dramatically minimize fraud and non-fraud related chargebacks, and improve cardholder experience. With a focus on customer-merchant relationships, Verifi empowers all parties with revolutionary new transaction dispute and fraud mitigation service that enables the sharing of robust transaction and merchant CRM details to resolve billing confusion and flag true and first-party/"friendly" fraud before it occurs. Cardholders have access to merchant order details through the issuer-hosted mobile or online banking platform, providing answers to their questions immediately at the point of sale.

Verifi's Recent Milestones:

1M+

More than 1 million disputes managed through data-sharing network each month

20,000

Supports over 30,000 merchant accounts globally

No transaction dispute strategy is one and the same

Get a free assessment from our dedicated team of chargeback experts today at verifi.com

Citations

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