Friendly Fraud and Chargeback Fraud

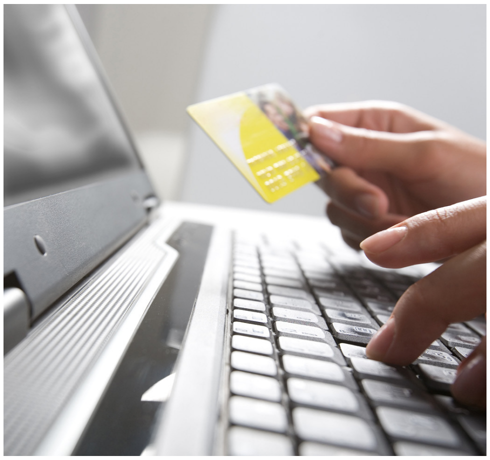
by Sue C. Quimby, CPCU, AU, CIC, CPIW, DAE

ANY CLIENT WHO DOES BUSINESS with the public, especially online, is exposed to various types of fraud. It is interesting to note that not all fraud is planned or intended. No matter the type of fraud, it has a significant impact on the economy. Helping clients understand and battle various types of fraud is another value-added service of the professional insurance agent.

The digital on demand economy has increased the avenues for potential fraud. In the past, there was less chance of misappropriation or malfeasance since credit cards were kept in a wallet and physically handed to the merchant at the point of sale. Now, account information can be stored on multiple sites and purchases are regularly made on "good faith". The merchant provides the goods or services based on an implied promise that the electronic payment transaction will be completed by the customer.

"True fraud" involves identity theft, or use of a stolen credit card. It is usually committed by someone unknown to the victim. "Friendly fraud" or "chargeback fraud" are types of fraud committed by the account holder. There is an important distinction between the two. While chargeback fraud is an intentional effort to obtain goods or services without paying for them, friendly fraud is most often a case of misunderstanding.

"Friendly fraud" could come from several sources - misunderstanding of a merchant's return policy, forgetting about a purchase, or purchases made by another cardholder (such as a spouse) that the cardholder may not know about. A customer could sign up for a subscription service and not understand that there would be ongoing recurring charges. In cases of friendly fraud, the merchant must strike a delicate balance. They want to solve the issue without



alienating the customer and losing future sales.

Chargebacks came about as a result of The Fair Credit Reporting Act of 1974, to protect consumers and increase confidence in the use of credit cards. In nearly half the cases, the chargeback was a simple misunderstanding- the consumer did not realize they were filing a chargeback. Confusion over how the transaction is listed on a credit card statement can lead to a chargeback – the billing description needs to be more than just the merchant's name (https://smallbiztrends.com/2017/10/chargeback-fraud-small-business.html).

"Chargeback fraud" occurs when a customer attempts to obtain a credit for items that they have received. This is an intentional attempt to defraud the seller. Examples include a claim that items were never received, or the items were returned but not credited. Friendly fraud is not insignificant. Estimates place the cost to merchants at over $25 billion by 2020 (https://chargebacks911.com/chargeback-stats-2017).

In cases of legitimate disputes, it is essential for customers to contact the merchant directly, rather than the bank or credit card company. While it may seem faster and easier to contact the bank, the process has a number of unpleasant consequences, for merchants as well as consumers. When a customer disputes a charge directly to the bank, the payment to the merchant is blocked, the charge is reversed and the merchant is assessed a nonrefundable fee of between $5-$35 per item. This is done without the merchant having the chance to prove the purchase was real, without having to first fill out a lot of paperwork. It is time-consuming for merchants to dispute chargeback cases, and therefore they may not do so, except if the dollar amount of the purchase is significant. The loss may be turned back to all of the merchant's customers in the form of increased prices (https://www.cbsnews.com/news/friendly-fraud-an-enemy-to-everyone-in-the-e-commerce-chain/).

The most common targets of chargeback fraud include: clothing, digital content, furniture, high-end merchandise, and anything that can be easily resold. Service industries are also common victims, including financial services, gaming, media, software and travel (https://chargebacks911.com/chargeback-stats-2017/). Sellers can help to prevent chargeback fraud by monitoring for unusual sales – such as large purchases in terms of dollar amount or number of items. Several purchases from the same IP address but using different credit cards may also signify fraudulent activity (https://smallbiztrends.com/2017/10/chargeback-fraud-small-business.html).

Fraud impacts all facets of society – from lost productivity of the merchant who has to deal with the issue to increased costs passed onto the consumer. Although not all fraud is intentional, it still is costly. Helping clients understand the types of fraud and possible ways to manage their exposure is another sign of the true insurance professional.

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