



Managing Chargebacks to Boost Profits



Radial
a bpost company

The purpose of the chargeback program is to keep businesses accountable for their products or services. It gives consumers an avenue of protection by which they can contact their payment provider and dispute an unauthorized charge, or voice their dissatisfaction with a product or service rendered by a merchant. In either scenario, consumers are attempting to get the charge in question credited back to their account.

However, a chargeback is a two-way process that gives both the consumer and the merchant an opportunity to build a case and present evidence to support their claim.

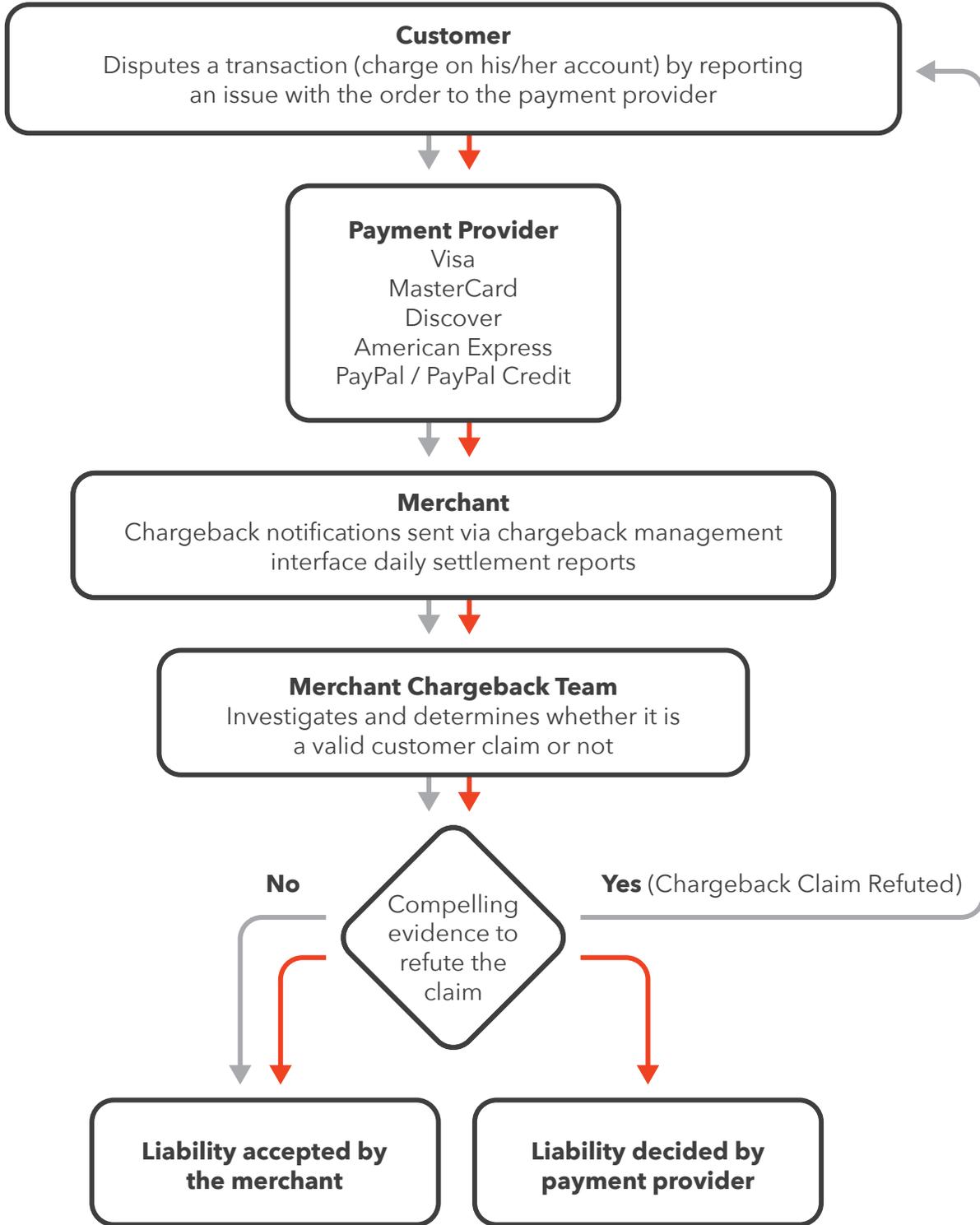
The merchant has only two windows of opportunity to combat chargebacks: before purchases are made and during the chargeback investigation. First and foremost, the merchant must do everything it can to prevent chargebacks from occurring. This requires merchants to put the right processes and resources in place, including a comprehensive fraud management solution, high-quality products, superior service, and clear policies to deliver a fantastic customer experience. Second, when chargebacks do occur, the merchant needs to be prepared to fight them to recoup losses. Routinely accepting every chargeback negatively impacts a merchant's profitability, particularly when some chargebacks can actually be recovered. However, chargeback representment—the process that allows the merchant to present evidence to the issuing bank that a chargeback is not warranted—will only improve a merchant's bottom line if executed properly. An overly aggressive approach could actually increase costs far beyond the disputed charge.

Understanding the lifecycle of a chargeback is an essential step in preparing a merchant to prevent, resolve, or minimize chargebacks.

The chargeback lifecycle is a series of interactions between several participants. It is comprised of four phases:

1. Retrieval/dispute/pre-notification/request for information (no financial impact to the merchant)
2. First chargeback (financial impact to the merchant)
3. Second chargeback/pre-arbitration (financial impact to the merchant)
4. Arbitration chargeback (financial impact to the merchant + additional penalty/fees if the dispute is lost)

Chargeback Lifecycle Workflow



- First Chargeback
- Pre-arbitration / Arbitration Chargeback

During the first three dispute phases (retrieval, first chargeback, and second chargeback/pre-arbitration) the merchant and the cardholder and payment provider work together to mutually resolve the chargeback issue.

In Phase 1, it's critical for the merchant to address and respond to all retrievals since this is the first step in potentially avoiding an actual chargeback and the associated costs from arising altogether. If the retrieval request is not responded to within the timeline specified by the payment provider, the merchant may be at risk of receiving the same as a chargeback which, in essence, reverses the transaction.

After reviewing the merchant's initial representation, it is ultimately the payment provider who decides if the merchant-supplied information is sufficient to remedy a chargeback. For second chargeback/pre-arbitration and arbitration phases, the merchant should determine if the available evidence is sufficient to remedy or win the chargeback in the merchant's favor. The evidence should be in strict accordance with what is acceptable as a remedy or compelling per the payment provider's dispute rules. In some cases, accepting the chargeback may be the best option because it will save the chargeback fees, arbitration fees, penalties, etc. when there is little or no chance of winning. This is particularly true for low dollar cases where the potential loss to the merchant may be higher than the value of the order.

If the merchant and the cardholder and payment provider are unable to reach a dispute settlement in the retrieval, first chargeback, or pre-arbitration phases, the chargeback may be escalated to the arbitration phase where both parties will present evidence supporting their claim. The payment provider will make the final liability decision on the chargeback case.

The arbitration process involves time and money in order to take the case directly to any of the payment providers. Also, there is no guarantee that the outcome of the chargeback will be different than the ruling in the first three chargeback phases, and regardless of whether the merchant wins or loses, it will incur a chargeback fee from the payment provider.

Card network operating and dispute regulations play a major role in determining the final arbitration decision. Be aware that each dispute phase has additional chargeback fees and penalties. The chargeback fees vary for each payment type, but typically range from \$4.00 to \$20.00 per chargeback case. The pre-arbitration filing fee may range from \$250.00 to \$500.00. The arbitration loser is then obligated to pay the cost of the arbitration (i.e., up to \$500.00 plus the disputed value of the order).

It's essential to understand the merchant representment process for each payment provider.

Just as a cardholder knows his right to dispute a transaction, it is equally important that the merchant understands its representment rights to be protected from unwarranted financial losses.



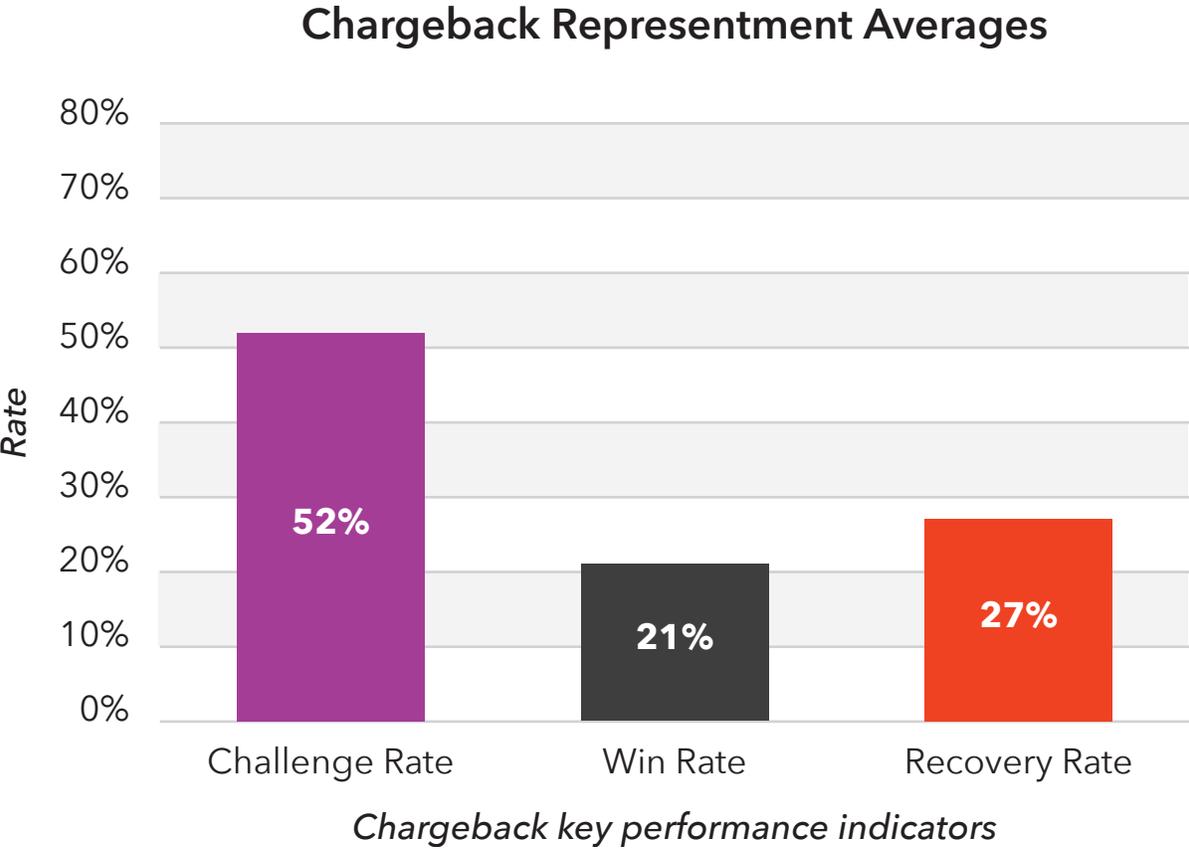
Card network operating regulations, dispute manuals, chargeback guides, or alternate payment provider (PayPal, PayPal Credit, etc.) user guides and agreements can help the merchant understand its representment rights, and also provide information regarding actions and compelling evidence that can remedy the chargeback. To contest a cardholder dispute and recoup a chargeback loss, the merchant needs to provide validity of the charge in writing with appropriate documented evidence to support the representment. Before deciding to refute a chargeback claim, the merchant should analyze the business case to determine the appropriate course of action. It never makes sense to spend more money to fight a chargeback than the merchant will recoup from investing in the process.

It is also important to know that building a representment case differs by payment providers. Although in some cases the reason codes may be the same, supporting documentation required to remedy individual chargeback scenarios may vary, and they are all governed by the framework set up by the payment provider. Regardless, having the necessary evidence and following the correct procedures are major factors in determining whether the merchant will win the dispute.

It's important to think about chargeback recovery as part of your business strategy.

Since the burden of proof lies with the merchant, deciding to challenge the cardholder's claim can be a very time consuming and costly task. The merchant must manually collect all of the supporting facts in documentary form and build a rebuttal for each individual chargeback case. With the payment provider's rules usually favoring consumers, there is no guarantee that the merchant will win the chargeback despite detailed representation efforts.

Based on Radial's 2017 matured chargeback data analysis, on average, merchants win the representation 21% of the time. Unfortunately, the huge uptick in online fraud is hampering merchant's win and recovery rates, with both decreasing year over year.



The merchant's chargeback strategy should involve three "checks" that will largely determine what action it can take to remedy a chargeback situation or recover the chargeback loss:

- 1. Is the merchant financially liable, or is the cardholder/payment provider liable for the charge per the operating regulations and dispute rules?** If the latter, the merchant should definitely represent the chargeback.
 - Does the cardholder/payment provider have the chargeback right? For example, was the chargeback created within the permissible timeframe? If not, the merchant is not liable for the chargeback loss.
 - Is the merchant insured against chargeback loss? For example, does the merchant have 3DS/VBV authorization authentication (Visa/MasterCard) or seller protection eligibility (PayPal payment types) where chargeback liability is covered by the payment provider?
 - Was an unsupported AVS (response code of "U") received for the transaction from the issuer (domestic credit cards only)? If so, the merchant is not liable for fraud chargebacks since domestic credit card issuers are mandatorily required to support AVS authentication.

- 2. Is the cardholder's chargeback claim valid or unwarranted?** If the cardholder claim is unwarranted, the merchant should refute the claim providing appropriate supporting facts as follows:
 - The merchant is able to verify that the cardholder participated in the transaction, received the goods or services, or benefited from the transaction and has raised an unwarranted chargeback claim.
 - The merchant is able to verify that the cardholder is disputing a charge to fraudulently benefit based on an issue that does not exist (friendly fraud).
 - The cardholder is disputing a charge based on an issue that has already been resolved by the merchant.

- 3. Does the merchant have sufficient compelling evidence to refute a cardholder claim, which is acceptable per the payment provider dispute rules?** If yes, the merchant should consider representing the chargeback to recover the financial loss. Compelling evidence varies based on the type of chargeback.

Compelling evidence for fraud chargeback reason codes:

- Proof that Verified by Visa was utilized by the merchant and 3DS authentication was obtained (ECI 5/6, UCF 1/2) for the disputed electronic commerce transaction.
- Proof that merchandise was shipped to a positive AVS-confirmed address (response of "X" or "Y"), proof of delivery was obtained, and the cardholder verifies to be residing at that address.
- Documentary evidence that proves or links the cardholder's participation on the order. There is evidence that the transaction was completed by a member of the cardholder's household or was shipped to the cardholder's relative or friend, business address, etc., evidence to prove a link (i.e., photographs or emails between the person receiving the merchandise and the cardholder), or proof that the cardholder disputing the transaction is in possession of the merchandise.
- Evidence that the transaction uses data such as an IP address, email address, physical address, or telephone number that was used in a previous undisputed transaction.

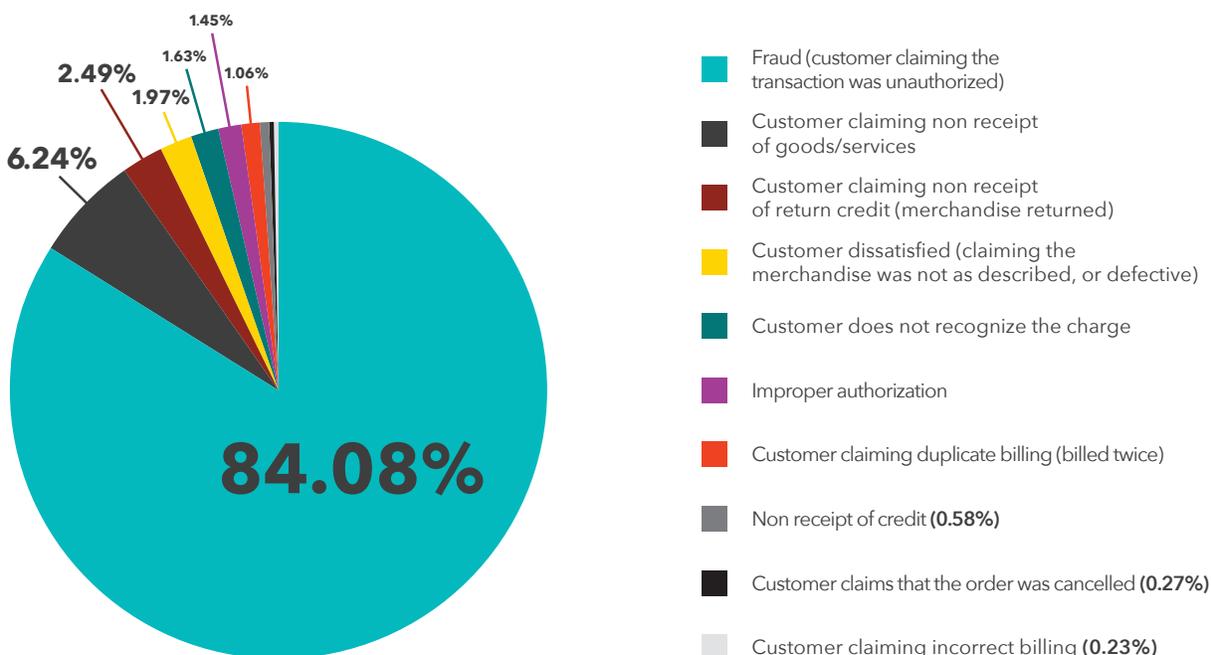
Compelling evidence for service chargeback reason codes:

- A sales invoice, itemized order details, and proof of delivery (POD) for shipped merchandise and services rendered.
- A copy of the store policy (merchandise return, order cancellation, refund processing, etc.) and requirements for the same.
- A written rebuttal addressing all of the cardholder's chargeback concerns and copies of all transaction receipts, order forms, invoices, or contracts as applicable.
- The cancellation, return, and refund policies as clearly disclosed on the merchant website and mailed to the customer in support of its rebuttal that explains the terms for service and the customer's non-compliance for the disputed service.

Compelling evidence for authorization chargeback reason codes:

- Proof that a valid authorization was obtained on the transaction date for card present transactions, or proof of authorization and the date authorized.
- Proof that the transaction was deposited and processed within the required time limit.
- Proof that the customer was charged only after the merchandise was shipped.
- Proof that the merchant followed all of the payment provider's operating protocols.

Top Chargeback Reason as a percent of 2017 Chargeback Loss (\$)



Based on Radial's 2017 chargeback data results, the above graph shows the top five chargeback dispute reasons that attribute to more than 96% of the total annual chargebacks.

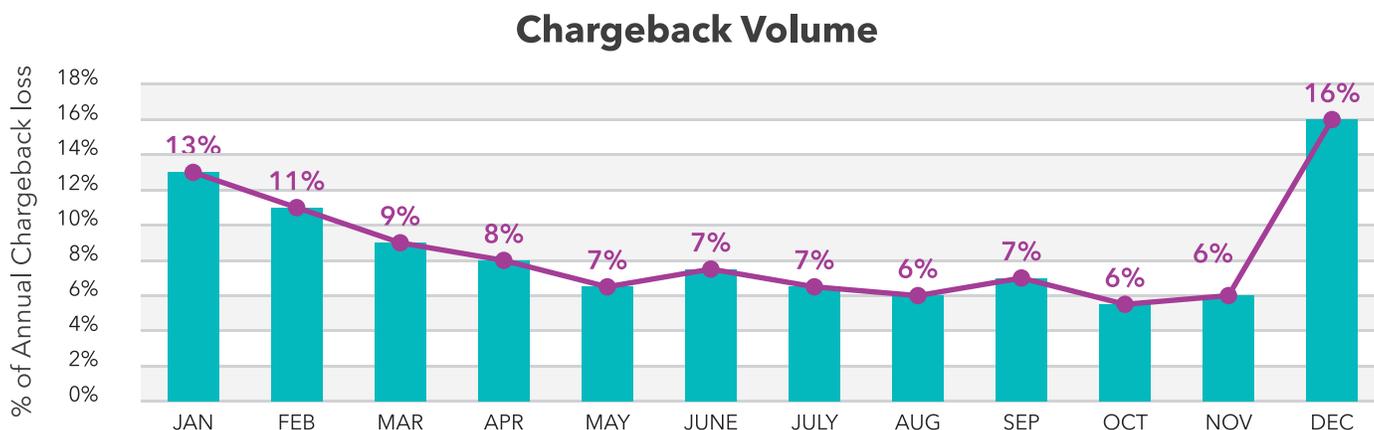
The merchant should dispute chargeback cases aggressively if it has sufficient compelling evidence to refute the cardholders' claim. However, when the merchant finds that battle simply isn't worth the investment, it should accept the liability and limit the negative impact to its bottom line and customer experience.

In general, the merchant should be selective on which chargebacks to fight. Not all chargebacks are the same and each chargeback needs to be researched individually to determine the appropriate course of action. Also, keep in mind that the merchant only has a limited timeframe to respond to and dispute a chargeback, and timeframes may vary for each card brand. Visa, MasterCard, and American Express give the merchant 20 days to respond; Discover gives 20 days for retrieval and 45 days for a chargeback response; and PayPal gives seven to 10 days depending on the chargeback reason code.

Chargeback volumes directly correlate to sales volumes

The chargeback volume is directly proportional to the sales volume, so the chargeback peak volume months are typically from December to February each year. The customer may have a right to file a chargeback for any transactions within 180 days from the original transaction date. Therefore, chargeback maturity can span anytime within six months from the date the customer was charged.

The below graph depicts an average expected annual chargeback volume spread per customer spending patterns and chargeback maturity rate.



Service related (non-fraud) chargebacks can also impact the merchant's chargeback volume, and they can be a good indicator for:

- A merchant system issue (e.g., a glitch causing customers to be double charged, incorrectly billed, etc.)
- A customer service policy that may not be practical (e.g., an excessive number of specific types of service disputes)
- A customer abusing return policies

It is critical for the merchant to ensure chargeback coverage scalability as it relates to sales volume. If coverage for chargeback management is not planned, the merchant may risk impacting the processing time for customer dispute resolution and thereby impact the customer experience as well as chargeback recovery rates.

Below are best practices that merchants should follow to minimize chargeback losses and increase the likelihood of success when it comes to chargeback disputes:

- 1. Enhance your fraud detection and controls.** The majority of the transactions that are disputed as chargebacks are due to fraud (unauthorized by the cardholder). Hence, merchants need to continually enhance measures for fraud detection and control.
- 2. Insure your business against chargeback liability.** Participate in Verified by Visa, MasterCard Secure Code and American Express Card Identification Digits, and enroll in Seller Protection coverage for PayPal transactions to reduce the risk of chargeback exposure.
- 3. Improve communications with your customers.** When an order is received, immediately email customers a receipt with product details, shipping and billing information, estimated delivery date, and return policy. Pre-notify customers of recurring charges, keep customers informed about order status (particularly if a shipment is delayed), and make billing descriptors clear to ensure your customers can easily recognize the charge. This will decrease consumer disputes and further reduce expenses.
- 4. Resolve customer issues promptly.** When cardholders contact you directly to resolve an issue, take immediate action and, when appropriate, issue a credit in a timely manner to avoid further escalation of the problem. After all, according to Gartner Group, loyal customers represent about 20 percent of a merchant's total customer base, but loyal customers also drive an additional 80 percent of business.
- 5. Clearly disclose your company's policies and practices.** This is especially important for billing, shipping, refunds, and returns. This will help you avoid customer disputes, reduce expenses, and strengthen your customer relationships.
- 6. Describe your goods and services thoroughly on your website.** Develop detailed product and service descriptions and include images to avoid disappointment when a customer receives the product. This will lead to fewer disputes over product quality.
- 7. Follow operating procedures and regulations.** Make sure that a transaction authorization and settlement process is in line with the payment provider's operating regulations since those play a big role in determining the financial chargeback liability.
- 8. Maintain detailed order life cycle records.** In order to dispute a chargeback, appropriate documentation that serves as compelling evidence is needed. If appropriate records are not maintained from start to finish, defending and winning a chargeback could be challenging and costly. Keeping accurate records of customers' authorization information, the dates and amounts of credit card transactions and receipts, and customer interactions can protect the merchant in the event that a chargeback occurs. Card networks' rules books provide information regarding acceptable forms of compelling evidence that can remedy a chargeback.

9. **Collaborate with third parties.** Partner with payment providers and third-party agencies to get early chargeback or fraud alerts and notifications. This helps merchants prevent chargebacks and take action to stop chargebacks before they occur.
10. **Respond to retrievals.** Respond to and resolve all retrieval requests and non-financial disputes to prevent them from turning into chargebacks.
11. **Make chargeback response time a priority.** Speed is essential when attempting to remedy a chargeback. The chargeback process consists of several phases and each one has a defined time limit to take action. The time allowed for the representment varies by payment provider and ranges from 7 to 43 days. If a chargeback is not responded to within the time specified, the merchant may not be able to remedy the chargeback. Also, longer dispute resolution processing times may adversely impact the customer experience and customer retention.
12. **Understand the chargeback process.** Education is key. The chargeback process is complicated because there are various dispute and chargeback workflows based on the payment type, the type of customer claim (fraud or non-fraud), and the variable time allowed for representment. Understanding the payment provider's operating procedures and dispute rules enables the merchant to know its representment rights in order to avoid and recoup unnecessary losses.
13. **Decipher the chargeback reason code.** The chargeback reason code helps the merchant understand why the chargeback was filed, which facilitates creating a defense for that particular customer complaint. Also, understanding chargeback reason codes and their effect on chargeback rates can help merchants prevent chargebacks before they become an issue and successfully represent those that can't be prevented.
14. **Compile compelling evidence.** A chargeback rebuttal is dependent on compelling evidence. The written explanation of the chargeback representment will need to be supported by persuasive and acceptable documentation.
15. **Create the "first time" right response.** Second chargebacks, or pre-arbitration chargebacks, needlessly increase costs. Creating the most compelling argument possible in the first chargeback phase and giving the "first time" right response can avoid second chargebacks.
16. **Dispute with confidence.** If the necessary steps to verify the authenticity of the transaction have been taken and measures to eliminate merchant error and minimize criminal fraud have been employed, the merchant should represent with confidence—especially for account take over issues where the payment provider should be held liable for security breaches.
17. **Analyze chargeback data.** A chargeback report is one of the most powerful representment tools available. It helps the merchant detect patterns, strengths, weaknesses, risks, liabilities, and other important factors. Analyze chargeback data to quickly spot problem areas earlier to avoid larger problems with fraud or customer service down the road.
18. **Train staff.** Educate employees on eCommerce risk and chargeback management to help prevent avoidable chargeback and fraud losses through effective, timely, and accurate dispute resolution.

19. **Create negative lists.** Develop and maintain an internal negative file and use it to screen transactions. Once a fraud chargeback has been issued, block that compromised card from further use.
20. **Know your customer.** Merchants should use chargeback data and customer service data to help analyze a customer's profile and assist in identifying abusive claim patterns. Customers' claims history and chargeback data (for both fraud and non-fraud issues) should be analyzed to pinpoint friendly fraud and improve prevention methods. Merchants should look for customers who are repeatedly filing disputes or contacting the customer service team directly to get a refund. To combat friendly fraud, it is very important for merchants to know their customers and, more importantly, to know the repeat offenders. By maintaining a list of customer names, shipping addresses, and other data points from customers claiming non-receipt, merchants can cross reference this information when a new order is placed. If the same customer, shipping address, or other data point is repeatedly associated with more than one of these types of chargebacks, it is likely that this person is committing friendly fraud and the appropriate action can be taken.
21. **Collect signature confirmation for the delivery of merchandise.** The top chargeback reason for non-fraud issues is that the customer claims non-receipt of the merchandise ordered. Also, as mentioned above, one of the ways to identify friendly fraudsters would be to maintain a list of customers that have made such claims and have them flagged for any future purchase attempts on the merchant's website. The merchant should make it mandatory to collect a signature as delivery confirmation for all future friendly fraud orders and high value merchandise.
22. **Monitor chargeback rates.** Monitoring chargeback rates can help merchants pinpoint problem areas in their businesses and improve prevention efforts. Merchants should work proactively to develop a detailed chargeback reduction plan that identifies the root cause of chargebacks and an appropriate remediation plan. Doing this exercise proactively can help merchants keep chargebacks to a minimum and prevent major payment provider's (Visa, MasterCard, and American Express) from placing the merchant in excessive fraud and chargeback programs. These programs may impose additional assessment fees and fines to the merchant. If the merchant's chargeback rate continues to cross the thresholds, it may incur steeper chargeback fees. The merchant may become labeled by the credit card institution as high-risk, and it may also lead to the potential termination of the online merchant account.
23. **Monitor chargeback representment performance.** It is critical for the merchant to track key chargeback representment performance indicators—chargeback dispute rate, win rate, and recovery rates. These metrics give the merchant a measureable assessment of the success of its in-house chargeback operations compared to industry averages.



Conclusion

Managing chargebacks can be a labor intensive and costly undertaking. Chargebacks can range from nuisance to a legitimate risk to the viability of a business. While chargebacks cannot be completely eliminated, they can be minimized with smart fraud management, quality products and service, clear policies, timely response and informed intelligence to know when to flee or fight.

About Radial

Radial brings more than 15 years of experience and 24x7x365 resources that work in concert and adjust in real time to ensure cyber criminals don't get the upper hand. We are committed to our clients' success including indemnifying fraud – even for high-risk markets – and only charging for approved orders. Flexible options allow merchants to leverage the solutions that best meet the needs of their organization whether it's for complete fraud management for all orders, fraud management for high-risk orders only, or a risk rating to supplement a merchant's existing tool set. We are obsessed with fraud so merchants don't have to be.

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