Chargebacks Can Be a Major Problem for Small Businesses

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The *Wall Street Journal* has acknowledged the serious problem that chargebacks pose to businesses in an article posted on its website. Merchants pay a heavy price for these reverse credit card transactions, which cost them a lost sale, the lost product, and a fine imposed by the credit card company. What's more, courts have equated chargebacks to merchant fraud, using merchants' chargeback rates against them in lawsuits regardless of the reason for the reverse transaction.

Long considered evidence of consumer injury, chargeback rates are not a reliable indicator of merchant wrongdoing. When courts cite a merchant's chargeback rate in litigation, they do not analyze the reasons for the chargebacks, but only the percentage of the merchant's total sales that were charged back to credit cards. As the article discusses, chargebacks do not always indicate that a customer has been fraudulently charged. Rather, chargebacks can be triggered for any number of reasons, including when a card issuer finds an authorization or processing error, such as an invalid account number or an expired card.

Recent years have also seen the dramatic rise of "friendly fraud," or fraud carried out by customers to get items free of charge. According to the Better Business Bureau, the most common types of friendly fraud involve cases in which a customer falsely claims that he or she never received an item ordered online, received the wrong item, or had a credit card stolen and was charged for items that weren't ordered. The customer then either demands a refund from the business or issues a chargeback on his or her credit card. In some cases, the customer receives a "double refund" after receiving a refund from the company and a chargeback on the credit card. The *Wall Street Journal* has previously reported that many major online companies, such as Expedia, have seen a 50% increase in friendly fraud since October 2008.

Credit card companies have liberalized chargeback procedures, providing an inducement for consumers to purchase and use products and then demand a chargeback, without ever contacting the merchant's customer service department with complaints about the product or the manner in which it had been sold. Whereas consumers once had to go into the bank to request a chargeback, they can now view their statement online and merely click "dispute charge" in order for the charge to be reversed.

It is refreshing for the *Journal* to acknowledge the price that business owners pay for this customer convenience, which some customers unfortunately abuse. We hope that as this issue gains greater exposure, customers will realize how their actions harm merchants, many of whom are small businesses that cannot afford these losses. We hope customers will begin to think twice before contacting their credit card company for a chargeback, and instead first contact the merchant regarding a return or disputed charge.

FTC Beat is authored by the Ifrah Law Firm, a Washington DC-based law firm specializing in the defense of government investigations and litigation. Our client base spans many regulated industries, particularly e-business, e-commerce, government contracts, gaming and healthcare.

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