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FRAUD 101

Understanding Fraud, Chargebacks, and How to Fight Them

Scott Adams
CEO/Founder, Fraud Deflect

Key Takeaways

1. Understand how CNP (Card-Not-Present) fraud happens and why it's rising.
2. Learn the difference between criminal fraud and friendly fraud and why the latter is harder to detect.
3. Get familiar with the full chargeback process, thresholds, and risks to your business.
4. Discover simple and effective tools to fight fraud and reduce chargebacks.

Brian Cullen: Sr. Payments Strategist, Sony Interactive Entertainment (PlayStation)

- Started at PSN in May 2012 as Fraud Manager
- Working in Payments and Risk for 18 years
- Live in San Diego by way of NY and Maryland
- In Fraud & Payments by way of banking and derivatives
- Two daughters: One studying forestry at Oregon State, and a dancer currently at an intensive dance program in NYC for a month
- My 3rd daughter (pictured) is presumed by the others to be my favorite

Payments – Vocabulary

ISSUER

- This is the bank that provides the credit card to the consumer.
- *Example: Chase Sapphire Card*
- In this example then, Chase Bank is the Issuer.

ACQUIRER

- This is the company (possibly a bank) that provides the merchant with their account to process credit cards.
- *Example: Chase Paymentech or Vantiv*
- This can be a bank or a non-bank company. If it's a non-bank, there is a bank sponsoring it as well though the merchant may be unaware.
- This could also be via a facilitator … basically a fin tech that is the interface with the merchant but then they work with an acquirer. The merchant may not be aware here, either.

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Payments – Vocabulary

MERCHANT (MERCHANT OF RECORD)

- This is the entity that is selling directly to the consumer.
- *Example: BestBuy.com*
- BestBuy.com takes the credit card online and sells the product to the consumer.
- This can get confusing, as some merchants use aggregators or facilitators and may not be the merchant of record.

CARDHOLDER

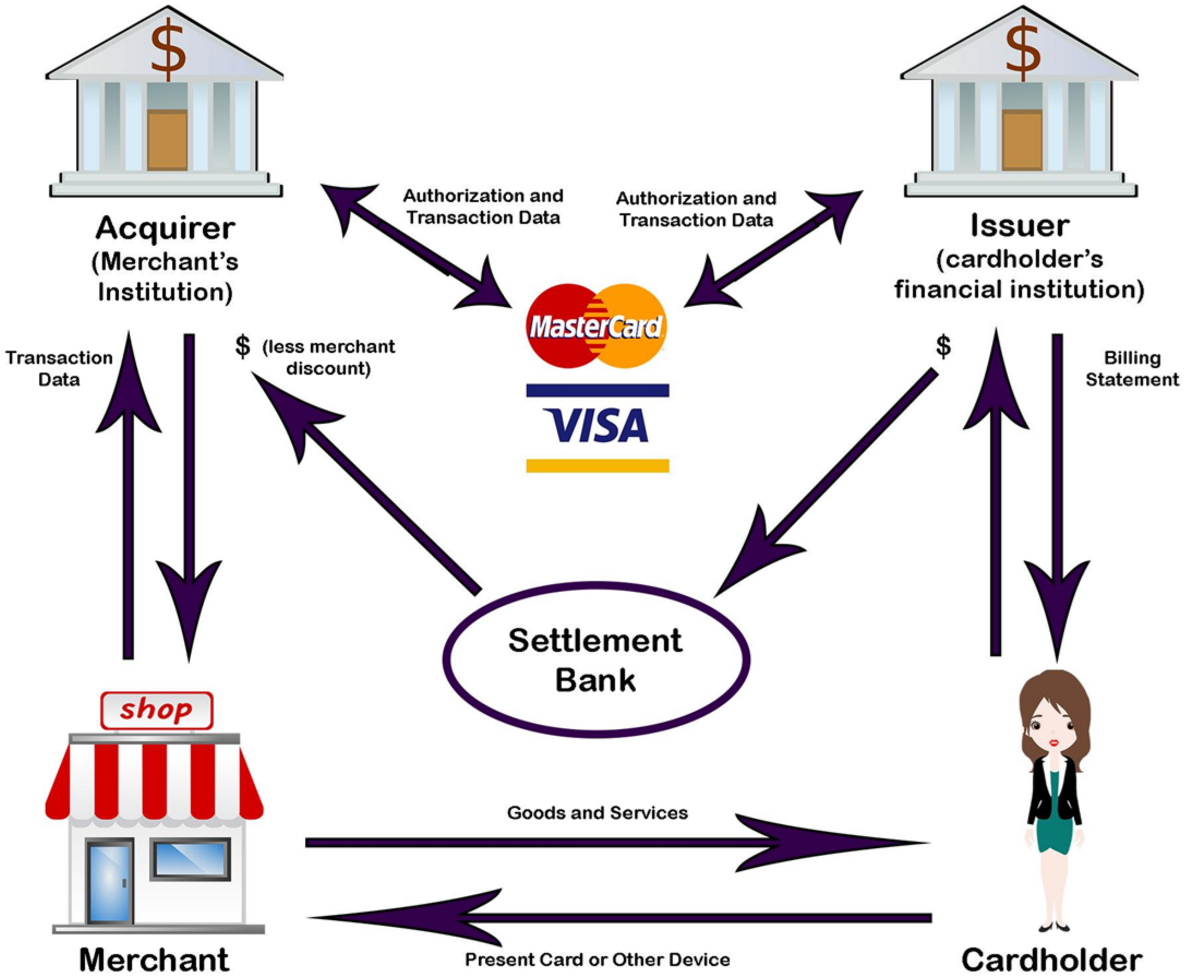
- This is the person who is liable for the credit card.
- Often is the customer, but not always.

Payments – Vocabulary

CARD BRANDS

- We are going to focus on Visa and Mastercard.
- They make up 90%+ of the card volume online.
- Card volume can be credit or debit (including prepaid).
- American Express, Discover and JCB work similarly but different since they are closed loop.
- They act as their own issuer, acquirer and bank in most cases.
- They also do not have strict chargeback and fraud programs.
- The cards provide a worldwide network and standards by which cards with their logos process transactions. Thus, they are accepted at nearly any merchant worldwide.
- The brands mainly deal with acquirers and issuers, but they do set rules for merchants such as the Fraud and Chargeback monitoring programs.

The Card Payment Ecosystem



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Fraud in CNP Payments

Credit Card CNP Merchants "Fraud"

CRIMINAL VS FIRST PARTY ("FRIENDLY") FRAUD

Criminal fraud is fraud with intent to steal money from the merchant and generally the card holder is unaware.

Many Types

- Card Running
- Stolen / Hacked Card Use
- Stored Card (ATO) Abuse

First Party Fraud or friendly fraud is where the card holder or a friend or family member is involved.

No real criminal intent and, often from known devices/accounts.

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Fraud in CNP Payments

Credit Card CNP Merchants First Party Fraud

EXAMPLES

- Children
- Spouse
- Forgotten charge

Fraud in CNP Payments

Credit Card CNP Merchants "Fraud"

ACCOUNT TAKE OVER (ATO)

This is a huge vector for fraud right now and will be more so in the future.

How it works

- This is where a fraudster will "hack" a user's account and make purchases.
- Phishing scams
- Known "victim"
- Family member / Account Sharing

Why its difficult

- Account age no longer useful
- Could be same device
- Often good card history

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“Fraud” in CNP Payments

How the card networks measure merchant "Fraud”

Visa Old World / Current MC (for now)

- Chargebacks
  - Card holder or issuer initiated
  - 0.9% limit
- Fraud
  - Cardholder or Issuer Initiated
  - $75k and 0.9% limit

New World ... Visa brought us Visa Acquirer Monitoring Program (VAMP)

- Chargebacks Plus TC40
- 2.20% limit
  - (Jan. 1.5% ... But acquriers limit is 0.3%)

More on this later ...

Chargeback Process

1. Cardholder disputes transaction and contacts card issuer.

2. Card issuer returns transaction to Acquirer through credit card network.

3. Credit card network forwards chargeback to Acquirer.

4. Acquirer receives chargeback and resolves dispute or forwards to merchant.

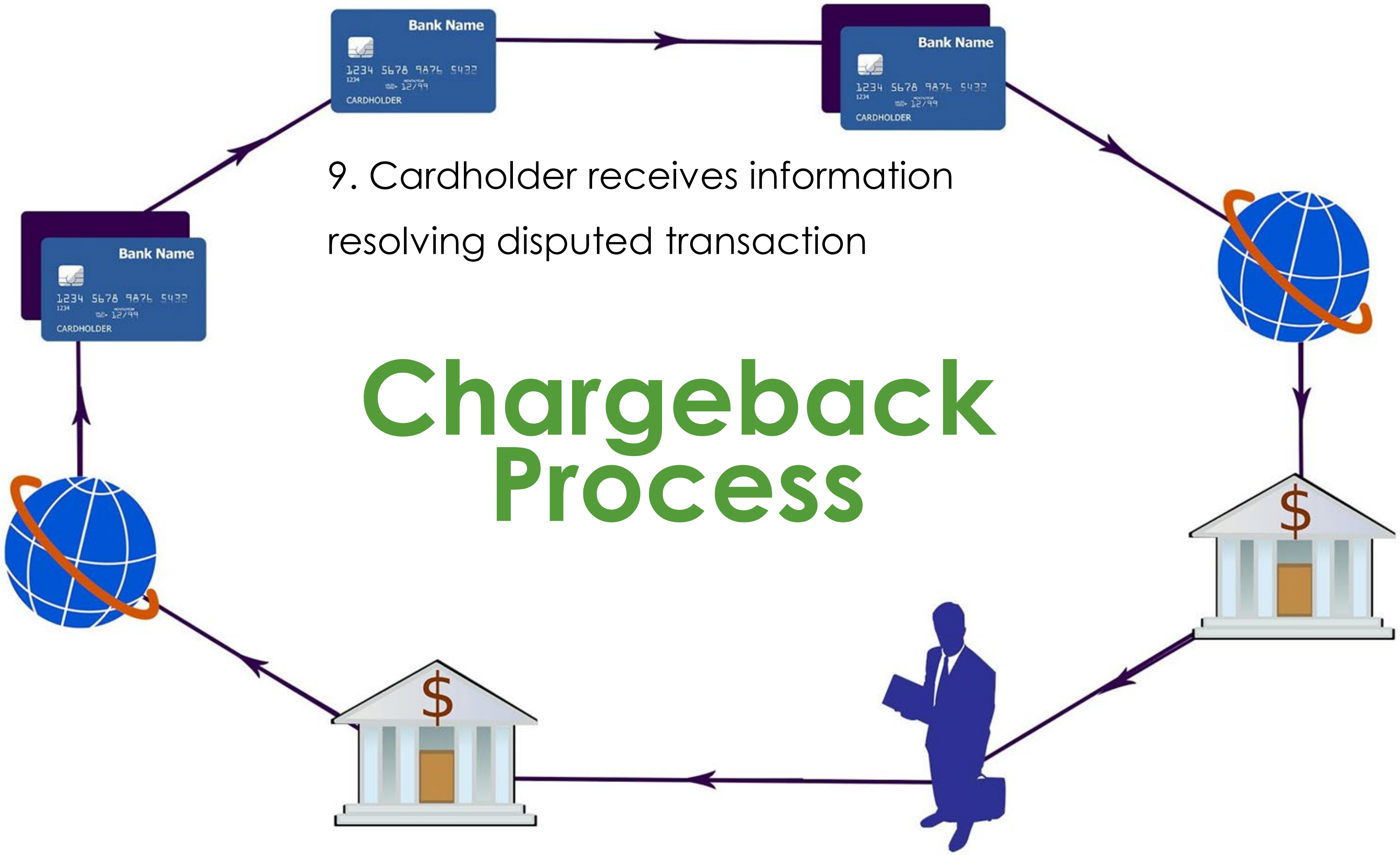
5. Merchant receives chargeback and either accepts or represents it to Acquirer.

6. Acquirer forwards representation to credit card network.

7. Credit card network receives representation and, if appropriate, forwards it to card issuer.

8. Card issuer receives representation and, if appropriate, reposts to cardholder's account.

9. Cardholder receives information resolving disputed transaction



Why CNP Fraud? Why me?

WHY CNP FRAUD?

- Shift to online over the years
- Offline prevention technology
- Online is way easier

WHO IS AFFECTED? WHY ME?

- Small Business vs Large Businesses
- Physical vs Digital

Fraud/CB Limits

Visa Acquirer Monitoring Program

- Merchant - Disputes plus Fraud (TC40)
    - Now 2.20%
- Acquirer
    - Early Warning: 0.4%
    - Above Standard: 0.5%
    - Excessive: 0.7%
- One month under to clear program

Fraud/CB Limits - Mastercard

Mastercard

- Excessive Chargeback Merchant (100 to 299)
  - 1.50% Chargeback Rate
- High Excessive Chargeback (300+)
  - 3.0% Chargeback Rate
- Excessive Fraud Merchant (1000+)
  - $50,000 USD Fraud &
  - 0.5% Fraud Rate
- 3 consecutive months under threshold to clear program

Exception: You can often get a 6 month pause in fines with a good plan to attack

Chargeback/ Fraud Math

MASTERCARD

- **CHARGEBACKS IS BASED ON #S CARD**

$$\text{Chargeback Rate} = \frac{\text{\# of Chargebacks REPORTED this month}}{\text{\# of Sales Transactions LAST month}}$$

- **FRAUD IS BASED ON VOLUME ($ USD)**

$$\text{Fraud Rate} = \frac{\text{USD \$ Amount of Fraud REPORTED this month}}{\text{USD \$ Amount of Sales Transactions REPORTED LAST month}}$$

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New VAMP Rate Calculations

$$\text{VAMP Rate} = \frac{\text{\# of Chargebacks REPORTED this month} + \text{\# of TC40 Trx Reported this month}}{\text{\# of Sales Transactions this month}}$$

Chargeback/ Fraud Math

VISA

As of May 15, 2025, Visa includes both fraud-related chargebacks and TC40s in VAMP thresholds. You can no longer exclude them. Both volume and count now impact your risk score.

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* Chargeback count is after RDR has been removed

Fighting Fraud - Basics

Best practices / Basic Tools

AVS

- Checks the billing address against the address you collect during the checkout process
- Only USA / CA / UK
- I suggest digital merchants only require partial match or ignore it. Physical should do partial or full.

CVV / CVV2 / CARD CODE

- This is the 3 digits code on the back of the card or 4 digit on front of Amex.
- Require CVV, at least, the first time you see the card
- This tends to fight friendly fraud.

Fighting Fraud - Basics
Best practices / Basic Tools

CUSTOMER SERVICE

- This is the entity that is selling directly to the consumer.
- Example: BestBuy.com
- BestBuy.com takes the credit card online and sells the product to the consumer
- This can get confusing as some merchants use aggregators or facilitators and may not be the merchant of record

BRUTE FORCE / CARD RUNNING PREVENTION

- Velocity Checks
- Make sure no single IP / Device / Card / Email / Account can place more orders than humanly possible in a short period of time.
- Set limits for how many orders per day an account can place.

Fighting Fraud - Basics

Best practices / Basic Tools

Understand "**disputes**" vs "**chargebacks**"

PROCESS TC40 / FRAUD ALERTS

- Most acquirers will provide you the TC40 reports if you ask nicely.
- Process these based on your situation.
- At least ½ will come back as chargebacks so it’s a good leading indicator.

ACCOUNT SECURITY

- Don’t trust a transaction just because the account has been around a long time.
- Enforce good account security.

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Fighting Fraud - Basics

Best practices / Basic Tools

BASIC DATA MINING

- Data, Data, Data!
- Excel is your friend – Sort by things like Country, Affiliate, Product.
- Slightly more advance – Sort by BIN if you have it
- Sort by Email, Account, about any variable

ANTI-FRAUD PRODUCTS

- Verifi Order Insight, Compelling Evidence 3.0, CDRN, Rapid Dispute Resolution
- Ethoca Alerts, Consumer Clarity, Mastercard First Party Trust
- Fraud Scoring
- Rules Engines
- Machine Learning

Fighting Fraud – Basics

Chargeback Representment – High Level

Representing chargebacks believed to be first party or illegitimate disputes is a key part of an effective mitigation strategy.

The benefits of employing an effective CBR strategy are:

- **Recovery** – Representing chargebacks known to be bogus disputes provides ROI to offset losses.
- **Deterrence** – First party offenders will think twice about attempting future disputes.
- **Measurement** – Allows experimentation using various data points to assist merchants in identifying true fraud vs first party.

Depending on volume, effective CBR can be cost and labor intensive. There are many 3rd party vendors specializing in providing this service to merchants.

***Important*:**

- Avoid over-representment
- Include the most effective data points in evidence
- Measure, measure, measure

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Summary & Key Takeaways

1. Chargebacks and fraud are different — but both impact your merchant risk.

2. Friendly fraud is hard to detect and often comes from known customers.

3. Visa and Mastercard monitor chargebacks and TC40 alerts (e.g., VAMP thresholds).

4. Tools like CVV, velocity checks, and account security still make a big difference.

5. Strategy: Deflection and interception products exist to stop disputes before they happen. Alerting post-dispute to allow for pro-active refunds is also a viable option, and can help alleviate card network risk program pressure.

6. Chargeback representment is part of risk strategy.

Thank you

- **Brian Cullen, Sr. Payments Strategist – Sony PlayStation**
  brian.cullen@sony.com

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