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The High Cost of E-Commerce Fraud

By **Rafael Lourenco**, EVP at **ClearSale**

Despite merchants employing advanced security measures like biometric screening, multifactor authentication and advanced machine learning tools on their websites, e-commerce fraud is still on the rise.

Fraud as a percentage of revenues also shows no signs of slowing down — growing from 0.51% in 2013 to 1.80% in 2018. This translates into increased costs for merchants. In fact, each dollar of fraud costs e-commerce merchants $2.94 in fees and expenses. Not high enough? That number jumps to $3.29 for e-commerce merchants selling digital goods.

With fraudsters regularly launching new attacks on businesses, e-commerce merchants are finding themselves out far more than just the dollar value of the lost merchandise. Here are the surprising ways e-commerce merchants are losing money after fraudulent transactions and what can be done to lower the high cost of online fraud.

Acquiring Bank Fees

When a customer disputes a credit card transaction, the acquiring bank will assess the merchant a chargeback fee. This fee — which often ranges from $20-$100, depending on how high-risk the merchant is — covers the costs the acquirer incurs during the chargeback process. Even if a merchant is successful in disputing the chargeback, they're still out the acquiring bank's chargeback fees.

False Declines

Too many chargebacks and too-high fraud levels can lead to an e-commerce retailer becoming exceptionally conservative when it comes to approving orders. Retailers might think they're saving on fraud costs, but they're actually adding in a new cost to their business: the cost of false declines.

Not only did U.S. merchants expect to lose an estimated $331 billion in 2018 alone to false declines, but there are longer-term costs, too. Up to 80% of customers say they'd take their business elsewhere after a bad experience. Negative experiences may force merchants to increase their marketing and advertising spend to replace the customers who've left. The replacement costs aren't cheap: the cost of customer acquisition can range from as little as $10 to more than $100 per customer.

Fraud Prevention Solutions

Preventing the expenses that come from fraud and chargebacks comes with its own cost. Merchants may find that the "free" fraud prevention tools that came with their shopping cart platform don't do a great job at keeping fraud costs down, so they find themselves researching (and investing in) new solutions.

Merchants might decide to keep their program entirely in-house, or they may opt to outsource some or all of it. Some services may even cover the cost of fraud-related chargebacks, allowing the company to take that line item out of their budget.

Depending on the solution they choose, merchants might also find they need to invest in additional staff during high-volume sales periods, training to keep the fraud team current on emerging trends and program upgrades that scale as the business does.

High-Risk Merchant Costs

Acquiring banks are keenly aware of which businesses have high chargeback ratios or sell in high-risk verticals, and those merchants may find themselves subject to additional fees for chargebacks. If these merchants can't control their chargeback volume, acquiring banks may put them into chargeback monitoring programs – incurring even more fees.

These merchants also face rising processing fees and even having their merchant accounts terminated. If merchants find themselves blacklisted by acquirers entirely, it's virtually impossible for them to accept credit cards. This consequence can be devastating to an online business.

Marketing and Advertising Budgets

It can take a robust marketing and advertising budget — sometimes up to 40% of revenue — for an e-commerce merchant to successfully build a great customer base. When unhappy customers begin filing chargebacks and making negative social media posts, that investment can be wasted.

Operational Expenses

It's not unusual for chargeback and friendly fraud to cause a merchant to lose up to 20% of revenue to operational expenses, like:

- The value of the goods lost
- The manpower time associated with processing and shipping an order
- The costs involved with storing and managing inventory
- The shipping costs incurred on each order

Processing Fees

For each credit card transaction, credit card processors charge merchants a fee that generally includes the wholesale cost of the transaction and the processor's rate markup. If the transaction results in a chargeback – whether it's legitimate or not – the merchant is out these processing fees.

Whatever the dollar amount your e-commerce business is directly or indirectly losing to fraud, it's too much. That's why it's important for merchants to analyze their fraud prevention solutions and understand if those solutions are doing all they can to add to the bottom line.

In the end, it's those merchants who are more likely to be successful in reducing chargebacks and false declines and retaining loyal customers — ensuring they can safely grow their business in 2019 and beyond.

Author:

Rafael Lourenco is Executive Vice President and Partner at ClearSale, a card-not-present fraud prevention operation that helps retailers increase sales and eliminate chargebacks before they happen. The company's proprietary technology and in-house staff of seasoned analysts provide an end-to-end outsourced fraud detection solution for online retailers to achieve industry-high approval rates while virtually eliminating false positives.

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