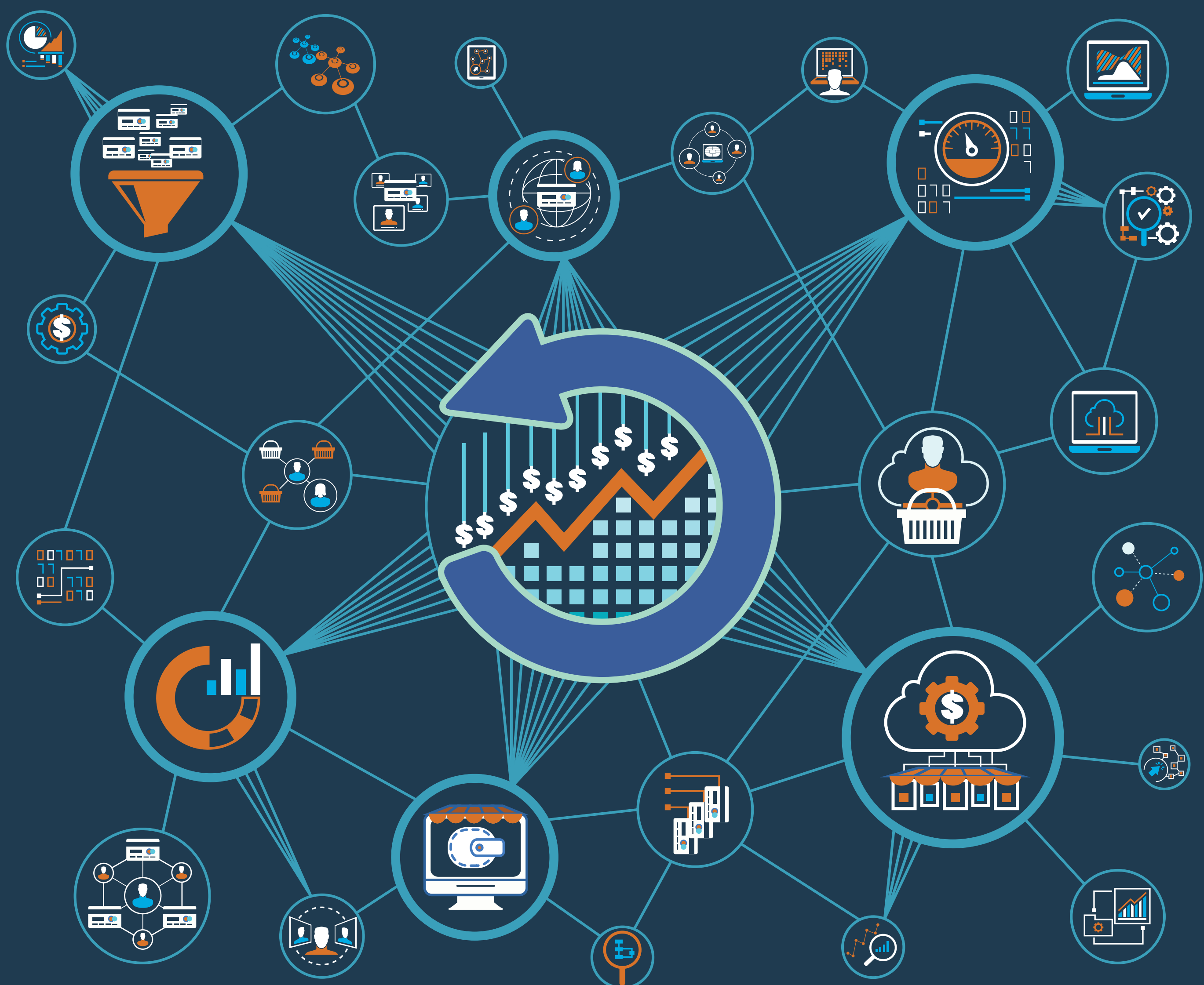

WHY CHARGEBACKS ARE NO LONGER A COST OF DOING BUSINESS

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The Growth of Chargebacks

In every business, there are unavoidable expenses that affect your bottom line. You don't get anything out of them, and wouldn't pay them if you had the choice, but you just have to accept them as the cost of doing business. Many merchants see chargebacks as one of these costs you just have to live with, but that's a category error.

Many chargebacks are avoidable, and you shouldn't just accept them as a cost of doing business. Chargebacks are growing at an estimated rate of 20% per year, clawing back nearly $4 billion in annual revenue from merchants. Ignore chargebacks, and you could see up to 40% of your revenue lost to fraudsters and unhappy customers.

The growth of the ecommerce sector and recent security improvements to card-present transactions have driven even more fraud to online stores in recent years. Card-not-present merchants cannot afford to let chargebacks run their natural course—left unchecked, they'll eat away as much revenue as they can.

The "True" Cost of Chargebacks

There are two widely-held misconceptions about chargebacks. The first is the idea that chargebacks are just an inevitable cost of doing business. The second is that chargebacks only cost you the amount of the transaction that's being reversed.

The real cost of a chargeback is much more than just the original transaction amount. To see what chargebacks are really costing you, you have to put your accountant visor on and look at all the hidden and indirect costs associated with them: transaction fees, product cost, marketing costs, operational expenses, and chargeback fees levied by your bank, which can range from 15% to 40% of the transaction amount, depending on your bank.

Assuming a transaction value of $100, let's calculate the true cost of a chargeback:

Transaction value	$100
Transaction fee (4%)	$4
Product costs (23%)	$23
Marketing costs (35%)	$35
Operational costs (20%)	$20
Chargeback fee ($25)	$25
TOTAL	**$207**

A chargeback is much more damaging to your bottom line than a return or a declined sale. Even with our conservative estimates, the true cost of a single chargeback is more than double the actual transaction value. For many businesses, the loss of revenue is over two and a half times the amount originally paid, and that's not including other penalties that could include the loss of your merchant account.

So, it's not a good idea to treat chargebacks as the cost of doing business; if you've fulfilled your end of the bargain and delivered your product or service as promised, it's your right to fight chargebacks and recover your revenue.

The Problem of Not Knowing Your Root Causes

To prevent chargebacks and fight them effectively, you have to understand where they are coming from. Every chargeback has a reason to justify its existence, and some of your business practices and policies may be responsible for making those chargebacks happen—these are the root causes of your chargebacks.

Card networks use reason codes to identify the explanation the customer gave for filing a chargeback. Merchants can learn a lot by analyzing the reason codes attached to the chargebacks they incur. There are a wide variety of reason codes, and they can tell you what specific steps to take to prevent and dispute your chargebacks.

If you don't understand why a chargeback was filed, you won't be able to put together the correct explanation and evidence needed to fight them. You'll waste time and effort, and your win rate in chargeback representation will be low.

Also, you can't proactively stop chargebacks if you don't know why they're happening in the first place. For example, prevention strategies aimed at stopping card fraud will do nothing to stop chargebacks that are occurring because of customer service issues related to a flawed returns policy.

The Consequences of Not Fighting Chargebacks

Chargebacks exist for a reason: to protect consumers, and make them more confident about using credit cards, especially in potentially insecure environments like the internet. They're more likely to make purchases with them when they know that they have protection from merchants who misrepresent or fail to deliver their products, and that any damage done by card thieves can be undone.

The flip side of this is that the chargeback process can be abused, and often times is. Representment—the part of the process that allows merchants to fight back against invalid chargebacks—is a way for merchants to protect their business, safeguarding themselves against fraudsters and unscrupulous customers.

What happens if you decline representment and don't fight your chargebacks?

- **Lost revenue and lower profitability.** The continued growth of chargebacks will equate to more and more lost revenue and nose-diving profits.

- **Repeated fraud.** There's nothing a fraudster likes more than a business that won't fight or protect itself. They will prey on those businesses as many times as they can get away with it. It is estimated that a "friendly fraud" chargeback customer will try to victimize a merchant at least two or three times after their initial success in having a legitimate charge reversed.

- **Penalties for not acknowledging chargebacks.** In response to the new regulations launched in 2018, some payment processors charge merchants a penalty for ignoring chargebacks. You are required to acknowledge all chargebacks by either accepting or disputing them, and failure to do so can lead to penalties ranging from $2 to $10 per chargeback.

3 Common Myths About Chargebacks

As common as they've become, there are still a lot of myths and misconceptions about chargebacks floating around. Here are three of the most commonly-held false beliefs about chargebacks.

• Myth #1: If I fight a chargeback, I will earn a bad reputation.

Merchants often think that fighting a chargeback will automatically lead to a bad review from a customer who wanted a refund. This isn't necessarily true. As long as you conduct your business with honesty, maintain efficient operations, and provide high-quality customer service, you will preserve your good name and reputation.

• Myth #2: I'll never win a chargeback dispute.

You can, and you will. Chargebacks are not just part of the cost of doing business. You can almost always recover money that was lost, provided you submit the right compelling evidence to your payment processor at the right time. You have a 50% chance of winning when you fight a chargeback. By default, acquiring banks take money out of the merchant's account when a chargeback is filed by a customer—but if the customer is found to be at fault, the money will be returned to you. If you don't respond to the chargeback, you automatically lose any chance of getting that money back.

• Myth #3: Chargebacks cannot be prevented.

If you pay closer attention to your chargebacks by analyzing the data points and identifying the root causes, you can take the relevant precautionary measures and proactively prevent up to 60% of similar chargebacks from occurring in the future. Chargebacks can easily be prevented by either analyzing the root causes in-house or by hiring third-party providers who can help you identify and eradicate your vulnerabilities.

4 Options for Handling Chargebacks

Any time a chargeback occurs, there are going to be four parties involved in the process:

1. The cardholder
2. The issuing bank
3. The acquiring bank
4. The merchant

The chargeback process begins when the cardholder contacts their issuing bank within a specified timeframe (usually 120 days) from the date of the transaction they're challenging. The merchant often doesn't learn about the chargeback until up to three months later (most chargebacks are filed within 30 to 45 days from the transaction date).

At that point, the merchant has four options:

- **Let it go.** Accept the chargeback as a cost of doing business. For chargebacks that have a legitimate basis (true fraud or merchant error, for instance), this is usually the best approach. It may also be advisable if you get chargebacks very infrequently.

- **Fight chargebacks with an in-house team.** This is recommended if you have high-volume or high-value chargebacks. The advantages are data security and minimal cost, but it can be difficult for an in-house team to keep up with all of the policy changes banks and card networks make to the chargeback process, and to adequately respond to all chargebacks within the required timeframe.

- **Use an automated tool to fight chargebacks.** Automated and semi-automated tools are available for disputing chargebacks. These can be valuable tools for small companies that deal with a low number of chargebacks, but it's not a viable option for medium-sized and larger businesses. These tools have a relatively low win rate, provide limited insights about your company's vulnerabilities, and are limited in how well they are able to analyze the root causes of your chargebacks.

- **Hire a chargeback management company.** The right company will have a solid knowledge of the industry as well as the tools and resources needed to effectively fight chargebacks and identify their root causes. They can be available 24/7 and should be able to provide useful suggestions, reports and insights that can help you identify your vulnerable areas and incur fewer chargebacks. The downside is that these companies can be expensive, and the wrong company can drain your money while providing little in the way of useful representation and actionable information.

Chargeback Management: In-House or Outsourced?

When it comes to chargeback representment, the burden of proof is on the merchant to supply the requisite evidence that they handled their part of the transaction properly and fulfilled their obligations to the customer.

In practice, the representment process can be confusing, and the rules and regulations governing it are frequently revised and updated. For most businesses, dedicating the resources required to effectively fight chargebacks in-house isn't economically feasible.

On the other hand, outsourcing chargeback management can be costly as well. How do you know which path to take?

The benefits of managing chargebacks in-house:

- **Cost.** Business owners often think they can save money by handling chargeback management themselves. In reality, while they are saving the upfront costs of paying for representment services, they're usually losing more money to chargebacks in the long term.

- **Data security.** Many merchants are (justifiably) reticent to share their internal operations data with third parties. Not only do they want to ensure that their customers' personal information and stored payment credentials are safe, they don't necessarily want an outside company to know the intricacies of how they conduct their business and generate sales. In some cases, they may even be ashamed to reveal exactly how many chargebacks they've been hit with.

- **Emotion.** When companies discover that their chargeback win rate is very low, they will often resist the idea of hiring outside representment services if doing so means they'd have to lay off their in-house chargeback team. In small businesses especially, you build a bond with your staff, and it can be hard to let them go for the good of your bottom line. For this reason, many merchants stick with their in-house staff despite the drawbacks.

- **Assumption.** It's very common for companies that fight chargebacks in-house to grossly overestimate their win rate. Evaluating your win/loss ratio is not a straightforward process, and many in-house teams make the mistake of assuming they've won a chargeback before the process is finished and they are informed otherwise. This happens because most payment processors don't provide merchants with a report of their chargeback data, and most small and medium-sized businesses don't have the time to chase down this information.

The benefits of outsourcing chargeback management:

- **Expertise.** Chargeback representment firms make a living off of helping merchants recover their money. They are the industry's top experts in the chargeback management field, with knowledge of all the nuanced rules and regulations, the best practices for disputing, and the expertise to track and report your data accurately and completely.

- **Tools.** Small and medium-sized businesses can't afford to spend the money and resources to develop a robust in-house system for managing chargebacks. They have to rely on manual labor, spreadsheets, and the limited experience of their staff. Representment companies, on the other hand, dedicate 100% of their resources to designing, building, and improving tools designed to track and eliminate chargebacks.

- **Strategy.** With years of experience working with hundreds—if not thousands—of clients, chargeback representment companies are experts at preventing chargebacks. A good company should be able to identify the root causes of your chargebacks and provide you with tried and tested strategies for improving prevention and increasing your win rate.

- **Reliability.** The most common challenge companies face when fighting chargebacks is that they have limited resources for handling disputes. If one of their in-house team members quits, or they have a spike in chargebacks during a busy season, the in-house team can quickly become overwhelmed, and chargebacks go unchallenged because they can't properly respond to them in time. Outsourcing can not only help you handle your chargebacks during peak season, it also gives you access to a deep bench of experts who can ensure that all of your chargebacks are represented on time.

Measuring the True Return on Investment in Chargeback Management

Whether you're handling in-house or outsourcing, it's very important to make sure that your chargeback prevention and representment efforts aren't costing more money than they're reclaiming for you. You have to track, gather, and analyze chargeback data to determine your true return on investment.

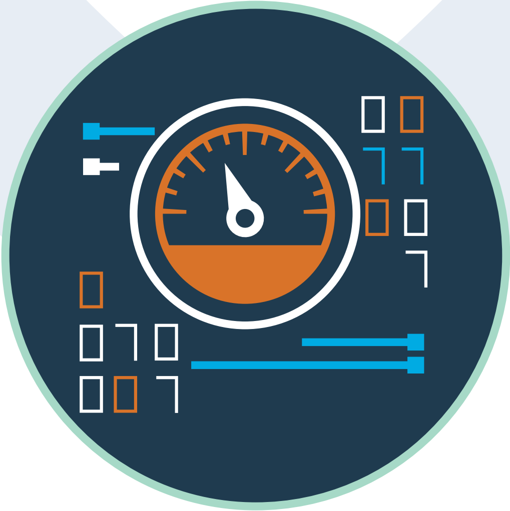
In-House:

When using an in-house team, the following metrics are helpful in determining the true ROI for chargeback representment:

1. Chargebacks per month
2. Average transaction amount
3. Total revenue subject to chargebacks
4. Chargeback win rate percentage
5. Total chargeback revenue recovered
6. Total cost to dispute chargebacks (include payroll, overhead, and other associated costs)

Evaluating Performance

- **Net ROI =** Chargeback Recovered Revenue - Total Cost to Dispute Chargebacks
- **A good rule of thumb:** if your recovered revenue is less than 40%, you are losing revenue that could potentially be recovered by using a team of experts.
- **Regarding win rates:** when you dispute a chargeback, you send in the relevant documents to the acquiring bank who then forwards them to the issuing bank for a ruling. Often, the issuing bank doesn't respond within a reasonable amount of time, so you interpret the lack of response as meaning you've won the dispute. However, if the dispute is rejected by the issuing bank or the customer files for arbitration to challenge your dispute, it comes back to you as a new chargeback, when in reality it's just the original dispute that you've already lost. This can lead to incorrect win/loss ratio calculations. You may think you're winning 60%-70% of the time, but when you analyze the data properly, the real figure is only 30%. This realization happens to nearly 95% of merchants when they switch from in-house to outsourced chargeback management.



Outsourced:

If you're outsourcing chargeback management to a third-party firm, these metrics can help you evaluate the true ROI you're getting.

1. Chargebacks per month
2. Average transaction amount
3. Total revenue subject to chargebacks
4. Chargeback win rate percentage
5. Total chargeback revenue recovered
6. Total cost paid to vendor to dispute chargebacks

Evaluating Performance

- **Net ROI =** Chargeback Recovered Revenue - Total Cost Paid to Vendor
- **A good rule of thumb:** if your chargeback representment firm is unable to recover at least 50% to 60% of your chargebacks, you can rest assured that they are not actual representment experts.
- **Make sure the company you hire** provides all the insights and analytical tools you need to identify the root causes of your chargebacks and proactively reduce chargebacks by at least 10% to 15%.

Case Study: Turning an Expense into A Revenue Stream

Magnum Inc. is an ecommerce business that sells beauty products. When we met them in 2014, their chargeback rate was exceeding 4%, resulting in over $900,000 in lost revenue from chargebacks and fraud. The chargeback management company they had previously been using was not able to implement effective prevention strategies and was winning less than 35% of their chargebacks.

They wanted a way to identify their root causes and get real-time updates about whether they were actually saving any money. They dropped their old provider and contacted Chargeback Gurus.

The Gurus began fighting their chargebacks using Smart Chargeback Representment and our FPR-360 tool, recovering money from existing chargebacks and stopping new ones from occurring. We identified sources that were driving bad traffic to their site and recommended that they be blocked. We also suggested customer service improvements, such as increasing call answering times and tracking returns and refused shipments.

After outsourcing their chargeback management to Chargeback Gurus, Magnum Inc. was able to reduce their chargeback rate by 30% and increase their win rate to 64%. In 2016 alone, they were able to recover $600,000 in revenue. The Gurus were also able to help them increase customer retention by 19% and reduce true fraud chargebacks by 11%.

	FIGHTING CHARGEBACKS IN-HOUSE	AFTER HIRING CHARGEBACK GURUS
CHARGEBACK LIABILITY		
Chargebacks faced per month	1073	803
Average chargeback amount	$70.00	$70.00
Total chargebacks per year	12,876	9,636
Total chargeback revenue loss per year	$901,320.00	$674,520.00
PERFORMANCE		
Chargeback recovery rate (win%)	10%	64%
Chargeback monthly recovered revenue	$7,511.00	$35,974.40
Chargeback prevention rate	0%	30%
Savings due to prevention tools & strategies	$0	$404,712.00
Annual recovered revenue due to representment	$90,132.00	$431,692.80

About Chargeback Gurus

Chargeback Gurus helps businesses prevent, fight, and recover their chargebacks. We take the pain out of chargeback management by providing simple, effective solutions that deliver a real return on investment for our clients.

We offer chargeback representment and chargeback prevention services to help companies recover lost revenue, prevent future chargebacks, and increase their bottom line. Our proprietary FPR-360™ technology analyzes over 40 different business data points to identify root causes and help prevent up to 50% of chargebacks, and our Smart Chargeback Representment™ process combines automation, data analytics, and expert analysis to help companies recover up to 70% of their chargebacks.