First-Party Fraud Explained

The Risks of Disputing Authorized Transactions

Picture this: You're reviewing your credit card statement and spot a $89.99 charge from a merchant you don't recognize. Concerned about potential fraud, you call your bank to dispute the transaction. Only after the chargeback is processed do you realize it was a streaming service subscription renewal. You had simply forgotten that you upgraded to the premium tier months earlier.

Scenarios like this are becoming increasingly common as digital transactions rise and billing descriptors become more cryptic. What starts as genuine confusion often evolves into something more problematic: first-party fraud. While cases like this are innocent, millions of cardholders find themselves in similar situations where the line between legitimate disputes and fraudulent claims becomes blurred.

What Is First-Party Fraud?

First-party fraud, often referred to as friendly fraud, occurs when cardholders dispute legitimate transactions as fraud. Unlike traditional fraud where a criminal steals payment information to make unauthorized purchases, first-party fraud involves the legitimate accountholder disputing their own authorized transactions.

The scale of this problem is staggering. First-party fraud has led to $100 billion in loss for businesses. First-party fraud is the main driver for the increase in cardholder disputes, with 79% of merchants reporting first-party fraud in 2024, up from 34%. The trend shows no signs of slowing, with a 19% rise overall in chargeback rates over the past year, encompassing merchant error, true fraud, and first-party fraud.

The reasons people end up filing disputes on their own authorized transactions vary widely. Sometimes it's a good faith accident. Other times, cardholders simply don't understand the difference between requesting a refund directly from a merchant and filing a chargeback through their bank. Many skip contacting merchants entirely, viewing chargebacks as an easier path to resolution. During economic hardship, some cardholders may rationalize disputing legitimate purchases they regret or can no longer afford. And unfortunately, a segment of consumers deliberately exploit the chargeback system, knowing that banks often side with cardholders in disputes.

First-Party Fraud vs. Friendly Fraud: Understanding the Distinction

While the terms "first-party fraud" and "friendly fraud" are often used interchangeably, there's an important distinction that affects how these incidents are perceived and handled.

Friendly fraud typically refers to cases where the cardholder acts without malicious intent. The root cause of friendly fraud is often transaction confusion, like when the cardholder mistakes a legitimate charge for a fraudulent one. These situations often arise from genuine misunderstandings, forgotten purchases, or household confusion where one family member doesn't recognize a transaction made by another.

First-party fraud, in its broader definition, encompasses both innocent mistakes and intentional abuse. First-party fraud is where a person knowingly misrepresents their identity or gives false information for financial or material gain. This includes deliberate attempts to obtain goods or services without paying, often by exploiting consumer protection built into the payment system.

The MRC brought together top global eCommerce merchants and card issuers to form the Merchant-Issuer Executive Committee, which redefined friendly fraud as "first-party misuse," a term now adopted across the industry.

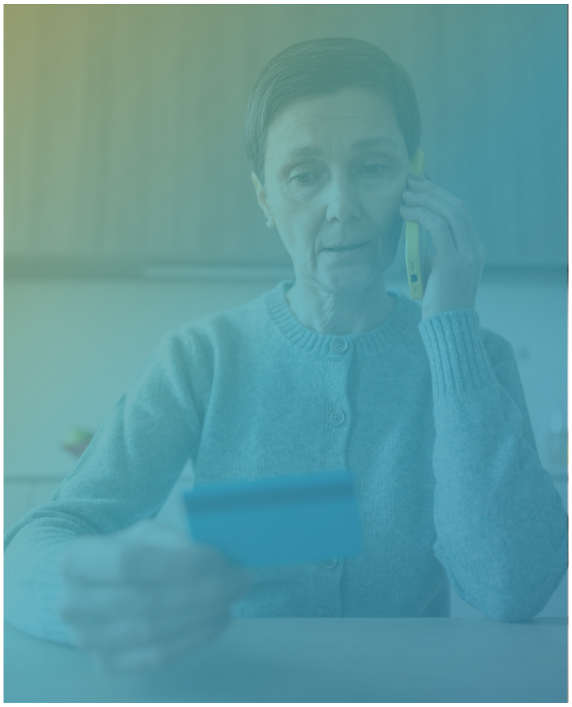
Impact on Banks and Financial Institutions

First-party fraud creates significant operational and financial burdens for financial institutions (FIs). When consumers file chargeback disputes, FIs must investigate each claim, often with limited information, distinguishing between legitimate fraud and first-party abuse.

Banks and credit unions face a complex balancing act. Consumer protection regulations require them to advocate for their cardholders and reverse charges when fraud is suspected. However, excessive chargebacks can damage relationships with merchant partners and payment networks. FIs that exceed certain chargeback thresholds may face penalties and increased processing fees.

The investigation process itself is resource-intensive. Fraud investigators must review transaction details, contact cardholders for additional information, and often make decisions based on incomplete data. Confusing or unrecognizable billing descriptors was the leading cause of chargebacks among cardholders surveyed in Chargebacks911's 2024 Cardholder Dispute Index. This means FIs frequently process disputes that could have been resolved by the cardholder simply contacting the merchant.

Impact on Cardholders



While consumers might view chargebacks as a convenient way to resolve payment disputes, first-party fraud can have serious consequences for cardholders themselves.

Relationship damage with financial institutions: FIs use sophisticated fraud detection systems that can identify patterns suggesting first-party fraud. Those who repeatedly file invalid disputes may find their accounts flagged for additional review or face lower spending limits.

Credit implications: In severe cases, FIs may report the activity to credit bureaus or close accounts. This can impact credit scores and make it difficult to obtain banking services elsewhere.

Legal consequences: Deliberately fraudulent chargebacks constitute a form of fraud that can result in legal action. While enforcement varies, consumers who systematically abuse the chargeback system may face criminal charges.

Wrap Up

First-party fraud is a complex challenge that touches every participant in the payment ecosystem. While the majority of cases likely stem from confusion rather than malicious intent, the cumulative impact is substantial, affecting merchants, banks, and ultimately cardholders themselves through higher costs and reduced options.

The solution isn't to eliminate consumer protections, but rather to improve education and communication. Cardholders should understand that contacting merchants directly is the fastest, most effective method to resolve payment issues.

As digital commerce continues to grow and transaction volumes increase, addressing first-party fraud becomes increasingly critical. The goal for FIs should be maintaining excellent customer experience while eliminating first-party abuse early on in the dispute process.

For consumers, the key takeaway is this: when you don't recognize a charge, your first call should be to the merchant, not your bank. This simple step can prevent unnecessary disputes, save time, and ensure that you receive the best care when real fraudulent activity happens.