

# Retail Fraud – Don't Make the Cure Worse than the Disease

By Anne Lockner & Kaitlyn Johnson



Retailers are in the business of selling, but preventing return fraud is also important to a healthy bottom line. The National Retail Federation estimated that holiday season return fraud cost retailers \$2.2 billion in 2015. Retailers can expect that number to rise in 2016. To maximize profitability, retailers use various methods to prevent fraudulent

returns, but some of these methods can lead to other problems. Those representing retailers need to know how return fraud happens, what retailers are doing to prevent it, and how retailers' efforts should be tweaked to avoid legal problems.

## Return Fraud Techniques

To help retail clients respond to return fraud, counsel must understand how it happens. Those defrauding retailers use several techniques:

- Return stolen merchandise.
- Return used products (termed “ward-robing,” often seen with special occasion wear and electronics).
- Create false receipts, especially e-receipts.
- Return another retailer’s product, usually purchased at a lower price and returned for a larger refund.

## Retailer Response

Return fraud hurts retailers in the aggregate; individual instances are too small to justify the expense of legal action. For this reason, prevention is key. Retailers discourage fraud in various ways, including:

- Using external tags on special occasion items to discourage returns post-event.
- Charging a restocking fee when an item is returned.
- Keeping digital receipts.
- Identifying “serial returners” by collecting personal information.

However, in an effort to protect themselves financially by preventing fraud, retailers may inadvertently expose themselves to even greater financial peril.

## Financial Risks Posed by Fraud Prevention Efforts

Retailers must take care not to make a bad situation – fraud – worse, by alienating good customers or violating anyone’s legal rights. Either outcome may cost retailers more than they save by preventing the fraud.

L.L. Bean, for instance, has an incredibly

generous return policy: “Our guarantee is a handshake – a promise that we’ll be fair to each other. So, if something’s not working or fitting or standing up to its task or lasting as long as you think it should, we’ll take it back.” This can sometimes result in seemingly absurd returns. For instance, This American Life recently reported on an L.L. Bean customer who returned a shirt that he estimated he bought *40 years ago*. L.L. Bean refunded him \$84.19. Most retailers are not willing to be that accommodating, but they may lose business if the fraud prevention efforts irritate and inconvenience the up-standing customer.

Customer relationships are not the only concern. Some preventive measures expose retailers to legal liability. A retailer could be subject to consumer class actions if restocking fees are unfair or not properly disclosed to customers. To mitigate this risk, counsel should advise clients of laws limiting restocking fees. In addition, good practice dictates clearly communicating the restocking fee policy to the customer at the time of sale and not charging restocking fees when the customer requests an exact exchange for a defective product.

Collecting personal information from customers to track returns may also expose the retailer to legal liability. Federal and state laws protect data privacy. California, for example, regulates what credit card information may be stored by retailers under the Song-Beverly Credit Card Act of 1971. In addition, retailers have suffered major data breaches, giving rise to lawsuits concerning compromised confidential information. Retailers should institute sound data collection and privacy practices that comply with all applicable laws to reduce their legal and financial exposure.

The holidays bring more sales but also more returns. Because retailers estimate that 3.5 percent of 2016 holiday returns will be fraudulent, the holiday period is the perfect time to review and tweak methods of preventing retail return fraud. Prevention is key, but make sure retail clients’ efforts help, not hurt their bottom line.

Anne Lockner is a partner, trial lawyer and co-chair of the retail industry group at Robins Kaplan LLP. Ms. Lockner handles complex litigation and internal and government investigations, and has extensive experience in solving a broad array of problems for her clients. She can be reached at [ALockner@RobinsKaplan.com](mailto:ALockner@RobinsKaplan.com). Kaitlyn Johnson is an associate at Robins Kaplan LLP. She focuses her practice on financial markets litigation and American Indian law and policy. She can be reached at [KJohnson@RobinsKaplan.com](mailto:KJohnson@RobinsKaplan.com).



Anne Lockner



Kaitlyn Johnson