Smart UPI Fraud Detect: UPI Fraud Detection Using Machine Learning

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How to Cite this Article:

N, D. .. & Be, A. B. H. (2026). Smart UPI Fraud Detect: UPI Fraud Detection Using Machine Learning. International Journal of Creative and Open Research in Engineering and Management, 02(6). https://doi.org/10.55041/ijcope.v2i6.172

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Abstract:

The rapid proliferation of Unified Payments Interface (UPI) as a primary mode of digital financial transactions in India has simultaneously escalated the incidence and sophistication of payment fraud. Traditional rule-based fraud detection mechanisms have proven inadequate against dynamic and evolving fraud patterns due to their static nature, high false positive rates, and poor real-time adaptability. This paper presents Smart UPI Fraud Detect — a novel, intelligent fraud detection framework that leverages a hybrid machine learning architecture integrating Deep Q-Networks (DQN) for adaptive reinforcement learning with eXtreme Gradient Boosting (XGBoost) for high-precision classification. The proposed system is trained on a comprehensive dataset of UPI transaction records encompassing features such as transaction amount, timestamp, sender/receiver identifiers, device fingerprints, geographic location, and behavioral patterns. Advanced preprocessing techniques including SMOTE (Synthetic Minority Over-sampling Technique) are employed to address severe class imbalance inherent in fraud datasets. Experimental evaluation on a Kaggle-sourced real-world dataset demonstrates an accuracy of 98.7%, precision of 97.9%, recall of 98.5%, F1-score of 98.2%, and a minimal false positive rate of 1.2%, significantly outperforming baseline models including Random Forest, SVM, LSTM, and standalone XGBoost. The system supports real-time classification, adaptive learning from new fraud patterns, and explainability through feature importance analysis. This work contributes a scalable, production-ready fraud detection solution for the Indian digital payments ecosystem.

Keywords: UPI Fraud Detection, Machine Learning, Deep Q-Network, XGBoost, SMOTE, Digital Payments, Anomaly Detection, Reinforcement Learning, Real-time Classification, Financial Security

I. INTRODUCTION

The Unified Payments Interface (UPI), launched by the National Payments Corporation of India (NPCI) in 2016, has transformed the digital payments landscape in India. By enabling instant, 24/7 interbank fund transfers through mobile devices using virtual payment addresses (VPAs), UPI has achieved unprecedented adoption — processing over 10 billion transactions per month as of 2024, with a cumulative transaction value exceeding INR 180 lakh crore annually [1].

However, the exponential growth of UPI transactions has been accompanied by a parallel escalation in fraudulent activities. The Reserve Bank of India (RBI) Annual Report 2023-24 documented a significant rise in digital payment fraud cases, with UPI-related fraud accounting for a growing proportion of total reported financial cyber crimes [2]. Fraud categories include phishing via fake UPI applications, QR code manipulation, SIM swap attacks, KYC impersonation, and social engineering-based collect request fraud.

Traditional fraud detection systems deployed by banks and payment service providers (PSPs) rely predominantly on rule-based engines — static threshold checks on transaction amounts, velocity limits, and blacklisted accounts. While computationally efficient, these systems suffer from critical limitations:

- Inability to adapt to novel, previously unseen fraud patterns
- High false positive rates leading to poor user experience through legitimate transaction rejections
- Delayed detection requiring post-transaction analysis rather than real-time interception
- Poor handling of class imbalance — fraudulent transactions constitute less than 0.1% of total UPI volume

Machine learning (ML) offers a transformative solution to these challenges. By training statistical models on large volumes of historical transaction data, ML systems can learn complex, non-linear fraud signatures, adapt to emerging patterns through incremental learning, and classify transactions in milliseconds — enabling real-time fraud prevention rather than post-facto detection [3].

This paper introduces Smart UPI Fraud Detect, a comprehensive machine learning-based fraud detection system specifically designed for the UPI ecosystem. Our primary contributions are:

- A novel hybrid DQN-XGBoost architecture that combines reinforcement learning for adaptive strategy optimization with gradient boosting for high-accuracy classification
- A comprehensive feature engineering pipeline incorporating transactional, behavioral, temporal, spatial, and network-graph features specific to UPI payment semantics
- Application of SMOTE for effective class imbalance mitigation in highly skewed UPI fraud datasets
- Extensive comparative evaluation against six baseline ML algorithms demonstratingstate-of-the-art performance
- A real-time deployment architecture with sub-100ms classification latency suitable for live UPI integration

The remainder of this paper is structured as follows: Section II reviews related literature. Section III describes the dataset and preprocessing methodology. Section IV presents the proposed system architecture and algorithms. Section V details experimental evaluation. Section VI discusses results and implications. Section VII concludes with future directions.

II. LITERATURE REVIEW

The field of automated fraud detection has evolved significantly with advances in machine learning and deep learning. This section reviews key prior works relevant to UPI and digital payment fraud detection.

Traditional and Rule-Based Approaches

Early fraud detection systems in banking deployed rule-based expert systems encoding domain knowledge as conditional logic. Patel and Verma [4] evaluated threshold-based velocity checks and geographic distance rules for credit card fraud, reporting detection rates of 72-78% with false positive rates exceeding 15%. These systems required constant manual maintenance and failed to generalize across evolving fraud typologies.

Classical Machine Learning Approaches

The application of supervised machine learning to fraud detection gained momentum with the availability of large transaction datasets. Gupta and Sharma [5] compared Random Forest, SVM, and Naive Bayes for detecting cybersecurity anomalies in digital payments, finding Random Forest achieved 94.2% accuracy with an F1-score of 93.8%. Chakraborty [6] analyzed UPI fraud trends in India, identifying that behavioral feature engineering (transaction velocity, time-of-day patterns, recipient diversity) significantly improved detection precision compared to purely transactional features.

Rani, Alam, and Javed [7] developed Secure UPI, a machine learning-driven fraud detection system presented at IEEE ICDT-2024, employing feature importance evaluation to identify essential fraud indicators, achieving competitive performance with Random Forest and gradient boosting ensembles. Their work highlighted the importance of interpretable feature selection for fraud system deployment in regulated financial environments.

Deep Learning Approaches

The application of deep neural architectures to fraud detection introduced new capabilities for learning hierarchical feature representations. Raju et al. [8] investigated LSTM networks for detecting fraudulent activities in UPI transactions at the 7th International IEEE Conference, exploiting the sequential nature of transaction histories to model temporal dependencies in spending behavior. Detection accuracy of 95.1% was reported, with particular strength in detecting coordinated fraud patterns spanning multiple time windows.

Tamilselvi et al. [9] presented an elevated deep learning methodology for UPI fraud detection at IEEE ICETEMS-2024 employing Convolutional Neural Networks (CNNs) for feature extraction from structured transaction data, achieving 99.74% accuracy. However, their approach required substantial computational resources and extensive training data, limiting real-time applicability.

Hybrid and Ensemble Approaches

Recent research has converged on hybrid architectures that combine the complementary strengths of multiple learning paradigms. The most significant related work is presented by Reddy et al. [10] at IEEE ICISDP-2025, proposing the DQN-XGBoost hybrid model that serves as the primary inspiration for our framework. Their reinforcement learning component dynamically optimizes detection thresholds in response to evolving fraud distributions, while XGBoost provides robust classification on the extracted feature space, achieving 98.7% accuracy.

Rethisha, Cyindia, and Geetha [11] at IEEE ICISS-2025 demonstrated the efficacy of leveraging multiple ML techniques for real-time UPI fraud detection, emphasizing the importance of streaming data processing pipelines. Abdirahman et al. [12] extended fraud detection to mobile wallet platforms beyond UPI, demonstrating cross-platform generalizability of ML-based approaches.

Research Gap

Despite substantial progress, critical gaps remain in the existing literature: few works address the severe class imbalance problem specific to UPI fraud datasets using advanced oversampling techniques real-time deployment constraints with sub-100ms latency requirements are rarely addressed; explainability through SHAP values for regulatory compliance remains underexplored; and (4) multi-fraud-type unified detection frameworks are absent. This work directly addresses these gaps

III. METHODOLOGY

Dataset Description

The experimental evaluation employs a comprehensive UPI transaction dataset sourced from Kaggle, comprising 1,48,523 transaction

records collected over a 24-month period (January 2022 – December 2023). The dataset reflects realistic UPI transaction distributions with the following characteristics:

- Total transactions: 1,48,523 records
- Fraudulent transactions: 892 records (0.60% highly imbalanced)
- Legitimate transactions: 1,47,631 records (99.40%)
- Feature dimensionality: 23 raw attributes, 47 engineered features
- Geographic coverage: Pan-India transactions across 28 states and 8 union territories

Feature Engineering

Raw transaction attributes are supplemented with engineered behavioral, temporal, and network features that capture the contextual signatures of fraudulent activity. Table I summarizes the key input features employed in the proposed model.

Data Pre-processing

Missing Value Treatment:

Missing values in categorical features (location, device type) are imputed using the mode of the respective feature within the same user's transaction history. Numerical missing values are imputed using median imputation to preserve distributional robustness against outliers.

Class Imbalance Handling via SMOTE:

The severe class imbalance (fraudulent: 0.60%) poses a critical challenge for standard ML classifiers, which tend to be biased toward the majority class. We apply SMOTE (Synthetic Minority Over-sampling Technique) to the training partition exclusively, generating synthetic fraudulent transaction samples by interpolating between existing minority class instances in the feature space. Post-SMOTE training distribution achieves a balanced 50:50 ratio, eliminating majority-class bias without introducing data leakage through test set contamination.

Feature Scaling:

Numerical features (transaction amount, frequency counts, deviation indices) are standardized using Z-score normalization (mean=0, standard deviation=1) to prevent features with larger magnitudes from dominating gradient-based optimization. Categorical features are encoded using target encoding — replacing each category with the mean fraud rate observed for that category in the training set — preserving ordinality information inherent in fraud risk levels.

Train-Test Split:

The dataset is partitioned using stratified sampling into 80% training (1,18,818 records) and 20% testing (29,705 records), preserving the original class distribution in both partitions. SMOTE is applied exclusively to the training partition post-split to prevent data leakage.

Proposed system Architecture

System Overview

Smart UPI Fraud Detect is designed as a layered, real-time fraud detection pipeline described below illustrates the end-to-end architecture comprising four functional layers: Data Ingestion, Feature Processing, Hybrid ML Classification, and Decision Output with Explainability.

The system architecture operates as follows:

- UPI transaction events are streamed from the payment gateway in real-time via Apache Kafka message queues
- The feature extraction engine computes 47 features from raw transaction attributes within a 50ms window
- The SMOTE-augmented training pipeline produces a balanced training set for the hybrid DQN-XGBoost model
- At inference time, the trained model classifies incoming transactions as Fraudulent or Legitimate within 80ms
- SHAP (SHapley Additive exPlanations) values are computed for flagged transactions to

generate human-interpretable fraud explanations for compliance reporting

Deep Q-Network (DQN) Component

The DQN component frames fraud detection as a sequential decision-making problem under uncertainty, modeled as a Markov Decision Process (MDP). The MDP is defined as:

- State Space (S): The current transaction's 47-dimensional feature vector concatenated with recent account transaction history embedding
- Action Space (A): Binary decision {FLAG_FRAUD, APPROVE_LEGITIMATE} with continuous confidence score
- Reward Function (R): R = +10 for correct fraud detection, R = +1 for correct legitimate approval, R = -5 for
- false positive (customer inconvenience penalty), R = -20 for false negative (fraud missed penalty)
- Discount Factor (gamma): 0.95, balancing immediate vs. long-term fraud prevention

The DQN employs a 4-layer fully connected neural network with ReLU activations (input: 47 neurons, hidden: 256-128-64, output: 2 Q-values). Experience replay with a memory buffer of 10,000 transitions and a target network update frequency of 1,000 steps ensures training stability.

XGBoost Classification Component

XGBoost (extreme Gradient Boosting) serves as the primary classification backbone, trained on the SMOTE-augmented dataset using the DQN's state representation as additional features. Key hyper parameters optimized via 5-fold cross-validation grid search:

- Number of estimators: 500
- Maximum tree depth: 8
- Learning rate: 0.05
- Subsample ratio: 0.85
- Column sample by tree: 0.80
- Regularization (lambda): 1.2, alpha: 0.5

XGBoost's ensemble of gradient-boosted decision trees provides inherent feature selection through information gain splitting, making it robust to irrelevant features while handling the mixed numerical and categorical feature space effectively.

Hybrid Fusion Strategy

Table 1: Hybrid Fusion Strategy

Phishing Attacks	Fake UPI apps or spoofed payment screens capturing credentials	Device + Behavioral ML
QR Code Fraud	Malicious QR codes redirecting payments to fraudster accounts	Pattern Recognition
KYC Impersonation	Fraudsters posing as bank officials to extract OTPs	Anomaly Detection
Collect Request Fraud	Fake collect requests disguised as payment confirmations	NLP + Behavioral
SIM Swap Attack	Fraudulent SIM replacement to intercept OTPs	Device Fingerprinting
Account Takeover	Unauthorized access via credential stuffing	Login Pattern Analysis

The final fraud prediction is determined through a weighted ensemble fusion of the DQN's Q-value-derived confidence score and XGBoost's class probability: P(Fraud) = alpha * P_DQN(Fraud) + (1-alpha) * P_XGB(Fraud) where alpha = 0.35 is determined empirically through validation set optimization. The fusion leverages DQN's adaptive sequential reasoning for accounts with rich transaction histories and XGBoost's precise classification for novel accounts with limited history.

Fraud Types Addressed

Table II details the fraud categories addressed by the Smart UPI Fraud Detect system, along with the detection approach for each category.

IV. EXPERIMENTAL EVALUATION

Experimental Setup

All experiments are conducted on a workstation with Intel Core i9-13900K CPU, 64GB RAM, NVIDIA RTX 4080 GPU (16GB VRAM), running Ubuntu 22.04 LTS. The implementation uses Python 3.10 with TensorFlow 2.14 (DQN), XGBoost 2.0.3, scikit-learn 1.3, imbalanced-learn 0.11 (SMOTE), and SHAP 0.44. Evaluation employs stratified 5-fold cross-validation on the training set, with final performance reported on the held-out test set (n=29,705).

Evaluation Metrics

Given the class imbalance context, accuracy alone is insufficient. The following metrics are employed for comprehensive evaluation:

- Accuracy: (TP + TN) / (TP + TN + FP +
- FN) — overall correct classification rate
- Precision: TP / (TP + FP) — proportion of flagged transactions that are truly fraudulent
- Recall (Sensitivity): TP / (TP + FN) — proportion of actual frauds correctly detected
- F1-Score: 2 * (Precision * Recall) / (Precision + Recall) — harmonic mean balancing precision and recall
- False Positive Rate (FPR): FP / (FP + TN) — proportion of legitimate transactions incorrectly flagged
- Area Under ROC Curve (AUC-ROC): aggregate discrimination capability across all classification thresholds

Comparative Results

Table III presents the comparative performance of the proposed DQN-XGBoost model against six baseline algorithms. All baselines are trained on the same SMOTE-augmented training set with hyperparameters optimized via grid search.

The proposed DQN-XGBoost hybrid achieves the highest accuracy (98.7%), precision (97.9%), recall (98.5%), and F1-score (98.2%) while maintaining the lowest false positive rate (1.2%). The 2.4 percentage point accuracy improvement over standalone Random Forest and the 57% reduction in false positive rate versus Logistic Regression represent practically significant gains in a real-world deployment context where false positives directly translate to customer friction and false negatives to financial loss.

Ablation Study

To validate each component's contribution, an ablation study is conducted by progressively removing system components: (i) without DQN, only XGBoost: 96.1% accuracy; (ii) without SMOTE balancing: 91.3% accuracy (biased toward majority class); (iii) without behavioral features: 94.8% accuracy. This demonstrates that each component contributes meaningfully to the final performance, with SMOTE being particularly critical for minority class detection.

Real-Time Performance

Average inference latency on the test set is 78ms per transaction (P99: 112ms), comfortably within the 200ms UPI transaction timeout window. The system processes up to 1,200 transactions per second on the experimental hardware, demonstrating scalability for high-throughput UPI infrastructure.

V. RESULT AND DISCUSSION

Significance of Results

The 98.7% accuracy and 1.2% false positive rate achieved by Smart UPI Fraud Detect represent a significant advancement over both rule-based baselines and standalone ML approaches documented in the literature. In the context of UPI scale — over 10 billion monthly transactions — a 1.2% FPR implies approximately 120 million falsely flagged legitimate transactions per month if deployed naively, underscoring the importance of continuing to minimize false positives. Our FPR of 1.2% represents a 3x improvement over the 3.7% baseline achieved by Random Forest, directly translating to substantially fewer disrupted legitimate user transactions.

Limitations

Several limitations warrant acknowledgment. First, the dataset, while comprehensive, is sourced from Kaggle and may not capture the full diversity of real-world UPI transaction semantics from live banking systems. Second, the DQN component requires periodic retraining (suggested: weekly) to maintain adaptation to newly emerging fraud vectors — a computational overhead not present in static classifiers. Third, the current framework does not address privacy-preserving federated learning scenarios where transaction data cannot be centralized, a critical consideration for multi-bank deployments.

Explainability and Regulatory Compliance

Financial regulators increasingly mandate explainable AI for automated decision systems affecting customer accounts. Our system integrates SHAP value computation for every flagged transaction, producing human-readable explanations such as: 'Transaction flagged due to: (1) Amount 4.2x above 30-day average [SHAP: +0.42], (2) New recipient with no prior interaction [SHAP: +0.31], (3) Transaction initiated at 3:47 AM [SHAP: +0.18].' This explainability layer enables compliance reporting, dispute resolution, and auditor review without requiring ML expertise.

VI. CONCLUSION AND FUTURE WORK

Conclusion

This paper has presented Smart UPI Fraud Detect, a novel hybrid machine learning framework for real-time detection of fraudulent UPI transactions. The proposed DQN-XGBoost architecture, augmented with SMOTE-based class balancing and a comprehensive 47-feature engineered dataset, achieves 98.7% accuracy, 97.9% precision, 98.5% recall, and 1.2% false positive rate — outperforming all evaluated baseline algorithms. The system supports real-time classification with 78ms average latency and produces SHAP-based explainability reports for regulatory compliance.

The results demonstrate that hybrid reinforcement learning combined with gradient boosting represents a powerful paradigm for adaptive, high-accuracy fraud detection in the dynamic UPI ecosystem. The framework is designed for production deployment, with a scalable microservices architecture capable of processing over 1,200 transactions per second.

Future Work

Several promising directions are identified for future research:

- Federated Learning Integration: Deploying the model across multiple banks using federated learning to train on decentralized data without compromising customer privacy — eliminating the need for centralized transaction aggregation
- Graph Neural Networks (GNNs): Incorporating transaction graph topology through GNN layers to detect coordinated fraud rings spanning multiple UPI accounts through network-based anomaly patterns
- Natural Language Processing for Social Engineering: Integrating NLP analysis of UPI transaction remarks and associated SMS/notification content to detect social engineering-based collect request fraud
- Continual Learning: Implementing online learning capabilities allowing the model to update incrementally on real-time transaction streams without full periodic retraining, reducing operational overhead

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