

Deception Concerns Loom Large At CFPB Over Prepaid Cards

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Created in 2010, the Consumer Financial Protection Bureau is an independent bureau in the Federal Reserve system with oversight authority for federal consumer compliance rules. The CFPB has focused its rulemaking and enforcement authority on traditional consumer financial products and institutions, including consumer credit card issuers, mortgage brokers and insurers, debt collectors and student loan lenders. Recent rulemaking suggests the CFPB is expanding its oversight to high-tech financial products and services to capture how an increasing number of Americans make payments and save money in the 21st century. Silicon Valley favorites like PayPal Inc., Google Wallet, Venmo, Square Cash, and potentially even Bitcoin wallet providers, appear to be targets of the CFPB's latest proposed regulations. This article addresses the proposed rule's scope of covered products, consumer and industry response and implications for providers of prepaid cards and related products.



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Summary of the Prepaid Cards Proposed Rule and Scope of Covered Products

The use of prepaid products is growing exponentially. Not only are consumers using prepaid cards for online shopping and bill payments, they are increasingly using them to receive wages, benefits and other disbursements. Just in the last four years, the number of prepaid card transactions has skyrocketed from \$1.3 billion in 2009 to \$3.3 billion in 2013.[1] And this year, consumers are expected to upload almost \$100 billion to general purpose prepaid cards, compared to less than \$1 billion in 2003.[2] As consumers continue to use this relatively new financial tool in greater numbers, an increasing number of traditional financial institutions, such as JP Morgan Chase & Co. and American Express Co., are venturing into the prepaid market.[3]

On Nov. 13, 2014 the CFPB issued its much-anticipated proposed rule regarding prepaid products. With this new rule, the CFPB's stated intent is to close purported loopholes in the prepaid card market and provide regulatory protection to prepaid consumers "whether they are swiping a card, scanning their smartphone, or sending a payment." [4] CFPB Director Richard Cordray explained that the CFPB has stepped into this area of financial products because "[c]onsumers are increasingly relying on prepaid products to make purchases and access funds, but they are not guaranteed the same protections or disclosures as traditional bank accounts." [5]

The scope of the products covered by the proposed rule is broad and includes some high-tech stars of the mobile and peer-to-peer payment industry. The proposed rule would cover traditional plastic prepaid cards (also known as general purpose reloadable cards) that are used to pay expenditures just like cash wherever debit and credit cards are accepted, and to directly deposit payroll checks. Moreover, the CFPB apparently believes that the proposed rule will also apply to the following financial products:

- PayPal and PayPal-type providers that transfer funds between businesses and/or people, including Google Wallet, Venmo and Square Cash;
- mobile and other electronic prepaid accounts that store funds;
- virtual currencies such as Bitcoin;
- payroll cards used by employers to pay employees who don't hold their own checking accounts;
- certain government benefit cards, including those used to distribute unemployment insurance, child support and pension payments;
- student financial aid disbursement cards; and
- tax refund cards.

The CFPB proposes to impose certain additional responsibilities on institutions that issue these financial products, including[6]:

- verifying the consumer has the ability to repay the debt before offering credit and giving consumers at least 21 days to repay their debt before charging late fees;
- providing periodic statements to consumers or making account information accessible online and for free;
- investigating and working to resolve reported errors, such as double charges or incorrect amounts;
- protecting consumers against fraud and limiting their responsibility for unauthorized transactions in the event a prepaid card is lost or stolen; and
- disclosing costs and risks associated with prepaid accounts prior to opening the account.

Notably, the CFPB wants the same rules and regulations for overdrafts in credit cards to apply to overdrafts and charges to consumers for using prepaid cards. The CFPB's adoption of this overdraft policy appears to be in response to comments by consumer groups and community organizations that argued prepaid cards with overdraft fees are inherently deceptive because consumers allegedly do not expect such fees to apply to prepaid cards.

Consumer groups, while largely supportive of the proposed rule, have also suggested that the CFPB should have been more aggressive in protecting consumers. Consumers Union, a consumer advocacy group, stated that the CFPB could have gone further, such as by requiring issuers to provide Federal Deposit Insurance Corporation coverage on prepaid cards.[7] The National Consumer Law Center called the proposed rule "a big improvement" for consumers but stated the rule should entirely prohibit overdrafts on prepaid cards.[8]

Some in the financial services industry have expressed concerns regarding certain aspects of the proposed rule. NetSpend — a leading provider of reloadable Visa Inc., MasterCard Inc. and other prepaid cards and related financial services — has publicly stated that increased regulation of overdraft fees in the prepaid card market may make offering overdraft options to prepaid card users too burdensome to continue.[9]

And NetSpend's former general counsel has also flagged the proposed rule's potentially adverse impact on technological innovation, noting that "the proposal threatens to trap the burgeoning ecology of next generation digital wallets and cryptocurrency innovations in a consumer protection regime narrowly tailored to the unique characteristics of reloadable prepaid cards sold to underbanked consumers." [10]

Implications for the Prepaid Card and Related Products Industry

Since its inception, the CFPB has targeted the credit card industry. It has ordered financial institutions to pay as much as \$727 million to consumers and imposed penalties as high as \$27.5 million.

Based on the CFPB's track record, financial service providers should anticipate that the CFPB's enforcement office will begin investigating alleged noncompliance with its proposed prepaid card rule once the rule is finalized. In the past, when the CFPB has focused its attention on a specific credit card industry practice — either by issuing guidance in the form of rulemaking or warnings — enforcement actions have quickly followed. Notably, on July 18, 2012, the CFPB issued guidance to industry on the marketing of credit card add-on products. Thereafter, between 2012 and the present, the CFPB brought a number of enforcement actions against banks for allegedly deceptive practices related to credit card add-on products. [11] At least five of these actions terminated in highly publicized consent orders and large monetary judgments. [12]

The wave of enforcement actions following the expansion of the CFPB's authority to its rulemaking powers is not expected to subside, especially given the CFPB's increasing budget and employee ranks. Though the CFPB brought its first enforcement case little more than two years ago, between 2012 and 2014, it has more than tripled its enforcement actions (from five in 2012 to 16 in 2014). The volume of enforcement actions in 2015 is also expected to rise as the CFPB has received a further increase in its enforcement budget (from \$105 million in 2013 to \$175 million in 2015) and expanded its employee ranks (from 527 in 2013 to 834 in 2015).

Consequently, companies and institutions dealing with prepaid cards and services should consider the current proposed rule carefully. The proposed rule will be published in the Federal Register shortly. Thereafter, companies and institutions have 90 days to comment before the CFPB addresses those issues and publishes a final rule.

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[1] "Prepared Remarks of CFPB Director Richard Cordray at the Prepaid Products Field Hearing," (Nov. 13, 2014), available at <http://www.consumerfinance.gov/newsroom/prepared-remarks-of-cfpb-director-richard-cordray-at-the-prepaid-products-field-hearing/>.

[2] "CFPB Proposes Strong Federal Protections for Prepaid Products," (Nov. 13, 2014), available at <http://www.consumerfinance.gov/newsroom/cfpb-proposes-strong-federal-protections-for-prepaid-products/>.

[3] Alan Zibel and Robin Sidel, "CFPB to Propose New Rules for Prepaid Debit Cards," WSJ (Nov. 13, 2014), available at <http://online.wsj.com/articles/cfpb-to-propose-new-rules-for-prepaid-debit-cards-1415854862>.

[4] "CFPB Proposes Strong Federal Protections for Prepaid Products," (Nov. 13, 2014), available at <http://www.consumerfinance.gov/newsroom/cfpb-proposes-strong-federal-protections-for-prepaid-products/>.

[5] Id.

[6] "Prepared Remarks of CFPB Director Richard Cordray at the Prepaid Products Field Hearing," (Nov. 13, 2014), available at <http://www.consumerfinance.gov/newsroom/prepared-remarks-of-cfpb-director-richard-cordray-at-the-prepaid-products-field-hearing/>.

[7] Daly, Jim, "Major Prepaid Card Providers Give a Polite Response to the CFPB's Proposed Regs," Digital Transactions (Nov. 16, 2014), available at http://www.digitaltransactions.net/news/story/Major-Prepaid-Card-Providers-Give-a-Polite-Response-to-the-CFPB_s-Proposed-Regs.

[8] Witkowski, Rachel, "Cheat Sheet: Details of the CFPB's Sweeping Plan to Regulate Prepaid Cards," American Banker (Nov. 13, 2014), available at <http://www.americanbanker.com/news/regulation-reform/cheat-sheet-details-of-the-cfpbs-sweeping-plan-to-regulate-prepaid-cards-1071208-1.html>.

[9] Alan Zibel and Robin Sidel, "CFPB to Propose New Rules for Prepaid Debit Cards," WSJ (Nov. 13, 2014), available at <http://online.wsj.com/articles/cfpb-to-propose-new-rules-for-prepaid-debit-cards-1415854862>.

[10] Brown, Christopher. "CFPB's Prepaid Card Rules Put a Freeze on the Future," American Banker (Nov. 26, 2014), available at <http://www.americanbanker.com/bankthink/cfpbs-prepaid-card-rules-put-a-freeze-on-the-future-1071391-1.html>.

[11] "Marketing of Credit Card Add-on Products," CFPB Bulletin (July 18, 2012), available at http://www.consumerfinance.gov/f/201207_cfpb_bulletin_marketing_of_credit_card_addon_products.pdf.

[12] "Consumer Financial Protection Bureau: Enforcing Consumer Protection Laws," CFPB (July 2014), available at http://webcache.googleusercontent.com/search?q=cache:fJ9mygq4WqcJ:www.consumerfinance.gov/f/201407_cfpb_factsheet_supervision-and-enforcement.pdf+&cd=1&hl=en&ct=clnk&gl=us.