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CFPB Proposes Comprehensive New Regulatory Regime for Prepaid Cards

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The Consumer Financial Protection Bureau (“CFPB”) has proposed a comprehensive new rule (“Proposed Rule”) imposing a new regulatory regime on prepaid products, including both traditional prepaid cards as well as so-called prepaid accounts.¹ In sum, the Proposed Rule would impose certain requirements on prepaid products under Regulation E² provisions applicable to debit transactions. In addition, issuers offering prepaid cards with credit features would be required to comply with existing credit card protections found in the Truth in Lending Act (“TILA”)³ and Regulation Z,⁴ implementing various consumer protection enhancements addressed by the CARD Act.⁵ The Proposed Rule would also impose certain unique requirements such as a 30-day waiting period before a consumer can be offered any credit features associated with a prepaid product. Finally, consistent with the CFPB’s mandate to ensure an orderly marketplace, the Proposed Rule would establish standardized disclosure requirements, creating a safe harbor for issuers who use the model disclosures provided by the CFPB.

The Proposed Rule would apply to physical prepaid cards as well as “prepaid accounts,” a term that would encompass prepaid accounts not linked to physical cards, including a wide range of emerging mobile products that store consumer funds. Given the broad proposed definition of prepaid accounts, various digital wallet providers may also be covered. In this regard, the CFPB noted that its review of mobile financial products and virtual currencies is “ongoing,” and “recognize[d] that the Proposed Rule may have potential application” to such products and services.⁶

I. Background

Banking regulators have historically declined to subject many types of prepaid cards to a comprehensive regulatory regime.⁷ However, regulators have previously mandated specific types of prepaid cards—such as gift cards⁸ and payroll cards⁹—to adhere to Regulation E. In addition, prepaid cards onto which federal benefits are placed must offer Regulation E error resolution provisions.¹⁰ Thus, many issuers of general purpose reloadable prepaid cards already comply with many of the requirements of Regulation E. The Proposed Rule would, for the first time, generally subject prepaid products to a single standardized federal regulatory framework.

II. Accounts Covered Under the Proposed Rule

Under the Proposed Rule, “prepaid accounts” would include any “card, code, or other device used primarily for personal or household purposes.” A prepaid account would be covered by the Proposed Rule if the account is capable of being used for purchases at multiple, unaffiliated merchants, at ATM

machines, or for peer-to-peer transfers. Consistent with the CFPB's proposed broad construction, an account would be a "prepaid account" under the Proposed Rule whether or not the account is:

- prepaid at the time of the acquisition or loaded with funds after acquisition;
- reloadable or non-reloadable; or
- sold directly to a customer or distributed to the customer by an employer or other provider.

The Proposed Rule does not, however, appear to cover accounts or products that do not store funds, such as virtual wallets that store only payment information and do not permit customers to store funds within the digital wallet itself. Similarly, the Proposed Rule would not apply to gift cards, which would remain regulated under the gift card provisions of Regulation E.¹¹

III. Key Requirements Under the Proposed Rule

A. Standardized Disclosure Requirements

A key component of the Proposed Rule would be to standardize disclosure requirements for prepaid accounts regardless of who is the issuer. Under the Proposed Rule, issuers would be obligated to provide disclosures in two forms: (1) a short form standardized disclosure, highlighting what the CFPB has classified as "key fees" that should be communicated prior to acquisition; and (2) a long form standardized disclosure, providing more comprehensive fee information.¹² Issuers also would be required to post terms and conditions information about prepaid accounts on both the issuer's own website and the CFPB's website, as well as by other means upon consumer request.

B. Access to Account Information

Another important aspect of the Proposed Rule is the requirement for issuers to enable prepaid account holders to access their account information. Under the Proposed Rule, institutions issuing prepaid accounts must provide periodic statements or provide online account access to prepaid account holders. Such information would be required to include account balance information, as well as transaction and fee history.

C. Fraud and Card Loss Protections

The Proposed Rule also includes credit card-type protections for unauthorized and fraudulent withdrawals or purchases, including protections for lost or stolen prepaid cards where the cards are registered with the issuer. Under the Proposed Rule, account holder responsibility for fraudulent, unauthorized, or lost card charges is limited to a maximum of \$50, provided the consumer promptly notifies the issuer of the unauthorized charges.

D. Error Resolution Requirements

The Proposed Rule would apply existing error resolution and limited liability requirements to all prepaid accounts and not merely to payroll cards and those on which Federal benefits are loaded. As proposed, upon receiving consumer notice of an error on a registered account, an issuer would be obligated to investigate and resolve the error within the provided timing guidelines. If the issuer is unable to resolve the error quickly,¹³ the consumer would be required to receive a temporary credit in the amount of the disputed error during the issuer's investigation. The Proposed Rule, however, does not extend these error resolution and limited liability requirements to unregistered prepaid accounts.

E. Credit Product Requirements

The Proposed Rule's most extensive requirements are provisions that would impose existing credit card-type protections on prepaid accounts with credit features. While the CFPB did not seek to prohibit issuers from extending credit to consumers in connection with prepaid accounts, the Proposed Rule seeks to apply various TILA protections—and certain additional requirements—to prepaid card issuers. The CFPB also takes the position in the Proposed Rule that offering overdraft protection services constitutes the provision of credit, thereby requiring additional credit card-like protections.¹⁴ These protections include:

- Requiring issuers to verify each consumer's ability to pay (regardless of the size of the credit line) before offering credit features, prohibiting the issuer from opening such an account or increasing the value of a credit line if the consumer is found not to be creditworthy;
- Preventing issuers from requiring payment on credit products or charging late fees for non-payment within 21 days of mailing the consumer a billing statement;
- Limiting total prepaid account fees to 25% of the credit limit during the first year a credit account is open;
- Restricting issuers from increasing the interest rate on an existing credit balance unless an account holder misses two consecutive payments; and
- Requiring issuers to provide 45 days' advance notice (during which the consumer may cancel the credit account) to an account holder before increasing the interest rate prospectively on new purchases.

The Proposed Rule would also impose novel requirements that are more stringent than those currently applicable to credit cards under Regulation Z, including:

- Imposing a 30-day waiting period after a prepaid card is registered to formally offer credit to the consumer; and
- Precluding an issuer from exercising a right of set-off to draw on the funds loaded into the account to repay any outstanding credit without affirmative consumer consent.

IV. Outstanding Issues Under the Proposed Rule

A. Potential Regulatory Impact

The Proposed Rule would make comprehensive changes to the regulatory landscape for prepaid accounts that may impose significant costs on issuers offering these products. This could reduce access to credit for many consumers, while imposing additional consumer costs. In so doing, it could limit the value of prepaid accounts as a lower-cost alternative to checking accounts, particularly for unbanked and underbanked populations.

While many issuers already adhere to Regulation E and evaluate their disclosures for compliance with the CFPB's prohibition on unfair, deceptive, and abusive acts or practices, several new provisions could impose significant compliance costs. For example, forcing consumers to wait 30 days to obtain credit could hurt consumers caught in a bind and force them to consider more expensive alternatives for a minimal loan amount. Even with clear disclosures and assuming the ability to repay, the 30-day waiting period requirement may restrict consumer choice by eliminating an option that some

consumers may find particularly useful. The utility of the 30-day waiting period is also questionable given that many prepaid issuers often waive fees if the overdraft is repaid quickly or is for a nominal amount.

Finally, the new disclosures—short-form and long-form—when coupled with the already-mandated initial disclosures, appear likely to impose compliance costs that should be evaluated, given that many of the mandated disclosures are duplicative. This could have an effect opposite to what the CFPB intends by obscuring the provision of clear information to consumers with multiple, varying disclosures. The Proposed Rule also raises issues regarding the prohibition under Regulation E of compulsory use of prepaid payroll cards, as well as regarding the foreign language component of Regulation E, but does not appear to alleviate the burden of complying with substantially similar state laws.¹⁵

B. Action Plan

Comments on the Proposed Rule are due 90 days following its publication in the Federal Register. It appears that compliance with most of the rule's requirements could be mandated within nine months of being finalized, but the Proposed Rule also suggests issuers could continue to sell pre-existing non-conforming products for a period of twelve months after publication of a final rule. As such, a final rule would not likely be effective until mid-year 2016, if not later.

In the meantime, the proliferation of traditional and nontraditional prepaid products will continue, and the impact of any changes coming out of the Proposed Rule could restrict the future utility of these products. This warrants careful review of the Proposed Rule by industry participants, as well as by unbanked, underbanked, and traditional banking customers.

Prepaid card issuers—including digital wallet providers—should create an action plan to address issues with the potential impact from implementation of the Proposed Rule. The plan should include:

- Analysis of the issuer's existing disclosures, error resolution procedures, and credit products associated with prepaid cards that may be affected by the Proposed Rule;
- Submission of the issuer's views and concerns on the Proposed Rule in a comment letter to the CFPB in advance of the deadline; and
- Review of new disclosure requirements, including plans to allow for the modification of existing materials and plans to distribute new materials.

Paul Hastings attorneys are actively working with clients to identify and address the impact of the Proposed Rule on their operations and to assist in drafting comments to provide to the CFPB.

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- ¹ CONSUMER FINANCIAL PROTECTION BUREAU, *Prepaid Accounts under the Electronic Fund Transfer Act (Regulation E) and the Truth In Lending Act (Regulation Z) ("Proposed Rule")* (Nov. 13, 2014), available at http://files.consumerfinance.gov/f/201411_cfpb_regulations_prepaid-nprm.pdf.
- ² 12 C.F.R. Part 205.
- ³ Truth in Lending Act, 12 U.S.C. § 1601 *et seq.*
- ⁴ 12 C.F.R. Part 226.
- ⁵ Credit Card Accountability Responsibility and Disclosure Act of 2009, Pub. L. No. 111-24.
- ⁶ Proposed Rule at 74.
- ⁷ See 77 *Fed. Reg.* 30923 (May 24, 2012).
- ⁸ 12 C.F.R. § 1005.20.
- ⁹ 12 C.F.R. § 1005.2(b); CONSUMER FINANCIAL PROTECTION BUREAU, CFPB BULL. No. 2013-10, PAYROLL CARD ACCOUNTS (REGULATION E) (2013), available at http://files.consumerfinance.gov/f/201309_cfpb_payroll-card-bulletin.pdf.
- ¹⁰ 31 C.F.R. § 210.5(b)(5)(iii)(C).
- ¹¹ 12 C.F.R. § 1005.20.
- ¹² The CFPB's proposed model disclosures are available at http://files.consumerfinance.gov/f/201411_cfpb_prepaid-model-sample-disclosure-forms.pdf.
- ¹³ Under 12 C.F.R. § 1005.11, a financial institution must investigate a consumer complaint and report its results to the consumer within ten business days. If the institution is unable to complete its investigation within this time frame, it must provide provisional credit.
- ¹⁴ Proposed Rule, Proposed Section 1026.12(a)(2). See *also* Proposed Rule at 94 ("the Bureau believes it is reasonable to interpret 'credit' to include when overdrafts are paid in relation to prepaid accounts").
- ¹⁵ A more in-depth analysis of the impact of the Proposed Rule on payroll cards will be addressed in a forthcoming Stay Current.

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