

STATEMENT OF

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BEFORE THE

SUBCOMMITTEE ON FINANCIAL INSTITUTIONS AND
CONSUMER PROTECTION

SENATE COMMITTEE ON BANKING, HOUSING
AND URBAN DEVELOPMENT

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Chairman Brown, Ranking Member Corker and Subcommittee Members, my name is Rick Fischer. I am a partner in the law firm of Morrison & Foerster LLP, and I practice in the firm's Washington, D.C. office. I have over 40 years of experience in advising banks and other financial services companies on retail banking matters, including those relating to prepaid cards, particularly cards that are issued by banks and branded by a system mark, such as Visa. I am pleased to appear before you today on my own behalf to discuss the prepaid card market. The underlying message of my testimony is that legislative activity relating to the prepaid market is unnecessary at this time. Overall, the structure and oversight of the prepaid card market meets the needs of both consumers and card issuers. Specifically, the prepaid card market provides appropriate consumer protections while still enabling this new consumer product to develop. And, any perceived deficiencies can be addressed through the new regulatory authority Congress has given the Consumer Financial Protection Bureau ("CFPB").

The Benefits and Popularity of Prepaid Cards

Prepaid cards are an innovative financial product that satisfies the consumer financial service need between traditional deposit accounts and alternative financial services, such as check cashing. Although still a relatively small segment of the overall payment card market, the number of prepaid card users is growing rapidly. In fact, prepaid card payments are the fastest growing segment of noncash payments in the United States;¹ "the number of prepaid card transactions increased 21.5 percent per year from 2006 to 2009."²

¹ 2010 Federal Reserve Payments Study, Noncash Payment Trends in the United States: 2006-2009, at 17, April 5, 2011, http://www.frbservices.org/files/communications/pdf/press/2010_payments_study.pdf.

² *Id.*

Prepaid cards function like checking accounts, but without the checks and at a significantly lower cost. Prepaid cards allow a user to add or “load” funds onto the card, store the funds with the prepaid card issuer and then spend or withdraw the funds in a variety of ways, including purchases at a wide variety of merchants. The term “prepaid card” encompasses a variety of financial products such as general purpose reloadable cards, government benefit cards and payroll cards. A variety of entities issue prepaid cards including banks, retailers, and other private companies. Merchant-branded prepaid cards, which can only be used at that merchant or group of affiliated merchants, were the most frequently used cards in 2009 with 2.7 billion transactions, and general purpose reloadable cards were used to fund 1.3 billion transactions.³

Prepaid cards are an attractive, cost-effective payment option for consumers, and allow consumers with less than perfect credit, or who prefer not to use credit or a traditional deposit account, to function in an increasingly noncash world. For example, prepaid cards enable consumers to shop on the internet and to purchase travel-related services, such as rental cars, airline tickets and hotel stays, which otherwise would require a credit card or a debit card to complete the purchase. Prepaid cards also allow a consumer without a deposit account to receive payroll funds and government benefits through direct deposit, and easily access those funds through use of the card. So, prepaid cards benefit government agencies and employers as well.

Prepaid cards also permit a consumer to make purchases and pay bills without carrying large amounts of cash or risking the imposition of overdraft fees. However, if the need for cash arises, many prepaid card programs permit a consumer to obtain cash at an ATM. Even if a consumer has access to credit and a traditional deposit account, prepaid cards provide consumers an

³ *Id.*

additional tool to better budget their transactions and avoid fraudulent access to their deposit accounts if the card information is compromised through a data breach.

As the popularity and use of prepaid cards increases, issuers are adding product features, including rewards, mobile phone interfaces and limited credit features. All of these benefits explain why prepaid cards are a growing financial product choice for U.S. consumers, including the approximately 60 million unbanked and underbanked consumers in the United States.⁴ Not only do consumers appreciate the convenience afforded by prepaid cards,⁵ they also appreciate the simplicity and transparency of prepaid products. For example, debanked consumers, those who formerly used deposit accounts but now rely on prepaid cards, appreciate the absence of unanticipated overdraft fees.

Prepaid Card Regulation Consumer Protections

With the growth of prepaid cards in the United States, state laws regulating the sale and administration of prepaid cards are proliferating and existing federal rules are evolving to address prepaid card practices. And payment system rules like the Visa Operating Rules enable consumers to dispute, or “charge back,” transactions and protect consumers from unauthorized use of their prepaid cards in the same manner as debit cards tied to traditional checking or savings accounts. Moreover, under Federal Deposit Insurance Corporation (“FDIC”) guidance, all prepaid card funds maintained at insured financial institutions must be protected by FDIC deposit insurance.

⁴ Federal Deposit Insurance Corporation National Survey of Unbanked and Underbanked Households, at Section 3, December 2009, www.fdic.gov/householdsurvey/full_report.pdf.

⁵ Center for Financial Services Innovation, A Tool for Getting by or Getting Ahead? Consumers’ Views on Prepaid Cards 2009 <http://cfsinnovation.com/node/330566>.

At the federal level, certain prepaid cards are governed by the Electronic Fund Transfer Act (“EFTA”) and its implementing regulation, Regulation E. For example, on May 22, 2009, President Obama signed the Credit Card Accountability Responsibility and Disclosure Act of 2009 (“CARD Act”), which amended the EFTA by adding new provisions regulating certain gift cards and other prepaid cards. This rule covers “general-use prepaid cards” and “store gift cards,” “issued on a prepaid basis primarily for personal, family, or household purposes to a consumer . . . in exchange for payment . . . and redeemable upon presentation.”⁶ The rule requires that a consumer be provided with specified disclosures prior to purchase of a card, restricts the circumstances under which a consumer may be charged certain fees, and restricts the circumstances under which a card may have an expiration date.

In addition, the Federal Reserve Board (“FRB”) has applied other provisions of Regulation E to certain types of prepaid cards. Specifically, the FRB extended to payroll cards the Regulation E requirements relating to initial disclosures of the terms and conditions, liability protections, change-in-terms notices, error resolution notices, and more convenient card balance and transaction information. Regulation E requirements also apply to certain non-needs tested government benefit cards, including state unemployment cards and prepaid cards issued to Social Security recipients.

When the FRB promulgated the gift card and payroll card rules, it concluded that the differing consumer protections were appropriate for specific types of prepaid cards, given the current state of the prepaid card market, and stated that the Board would continue to monitor the market to

⁶ 12 C.F.R. § 1005.20(a).

determine when additional regulatory action was warranted. As discussed below, this oversight authority now resides with the Consumer Financial Protection Bureau.

State prepaid card regulatory regimes further supplement the federal structure by providing additional consumer protections. In particular, state consumer protection laws regulate the sale and administration of prepaid cards and often limit or prohibit expiration dates or fees, require specified disclosures and address cash redemption of unused card balances. Generally, such prepaid card laws are based on the notion that a consumer should not be deprived of his or her right to the underlying of the prepaid card value. Moreover, under the federal EFTA, such state laws are preserved if the state laws are not inconsistent with EFTA and are more protective of consumers. This preemption provision has preserved state consumer protection laws relating to prepaid cards, affording consumers with additional protections.

For example, California prohibits certain prepaid cards from expiring.⁷ California law also prohibits service fees in connection with certain prepaid cards except for the imposition of a dormancy fee if the value on the card is five dollars or less at the time each fee is assessed and the fee is not in excess of one dollar per month.⁸ Furthermore, such prepaid cards must be redeemable in cash or must be replaced at no cost to the holder.⁹

⁷ Cal. Civ. Code § 1749.5. The statute applies to “gift certificates” which include gift cards, but does not include any gift card usable with multiple sellers of goods or services, provided the expiration date, if any, is printed on the card. This exemption does not apply to a gift card usable only with affiliated sellers of goods or services. Cal. Civ. Code § 1749.45(a).

⁸ Cal. Civ. Code § 1749.5(e).

⁹ Cal. Civ. Code § 1749.5(b).

The Consumer Financial Protection Bureau

The CFPB has the authority to regulate the offering and provision of “consumer financial products,” including prepaid cards. The CFPB is directed to implement and enforce federal laws to facilitate the consistent, fair, and orderly functioning of the consumer financial services markets and, thus, has the ability to empower consumers to more effectively control their personal and household finances.

In particular, the CFPB has been given primary federal regulatory authority over “consumer financial products,” including prepaid cards,¹⁰ and most federal consumer financial protection statutes. This authority includes the ability to promulgate rules that the CFPB determines to be “necessary or appropriate” to carry out the objectives of federal consumer financial laws. With respect to prepaid card products, the CFPB has inherited the authority of the FRB to apply Regulation E, including its disclosure requirements and error resolution provisions, to prepaid cards. Also, the responsibility of the FRB to monitor the developments in the prepaid market to determine whether to propose additional consumer protections under Regulation E now rests with the CFPB, and the CFPB has made it clear that a review of prepaid card fees, disclosures and practices is a priority.

Moreover, the proposal of regulatory changes is not the only consumer protection option available to the CFPB. The CFPB also has the ability to take enforcement action to prevent a card issuer or a covered service provider from “committing or engaging in an unfair, deceptive,

¹⁰ See Section 1002(15)(A)(v) of the Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, 124 Stat. 1376, 1958 (July 21, 2010).

or abusive act or practice” with respect to a transaction with a consumer that involves a consumer financial product or service, including prepaid cards.

Congress has created the CFPB and directed it to oversee a fair market for consumer financial products and services, including prepaid cards. The authority vested by Congress in the CFPB is sufficient to address any additional consumer protections needed for prepaid cards. The CFPB has announced its intention to address prepaid cards and the CFPB should be given the opportunity to do so.

Thank you for the opportunity to appear before the Subcommittee, and I would be pleased to address any questions.