

Payments Innovation and Consumer Protection – Revisiting the 2016 Prepaid Card Rule Amendments

by

Nancy K Brooks,

Partner,

Schuyler, Roche & Crisham

Chicago, Illinois

In November, 2016, the Bureau of Consumer Financial Protection (the “CFPB” or the “Bureau”) published final rules amending Regulations E and Z to incorporate sweeping changes for prepaid accounts.¹ These particular rule amendments became known as “the Final Prepaid Card Rules,” because the predominant focus of the rules, rule-making process, and related industry consternation, was impact to the prepaid card industry. And, as is highlighted in this article, the consumer protection provisions of the new rules also were designed based on the operation of the prepaid card industry in effect at that time. Some of those concerns included: many and varied fee structures and lack of ability for consumers to make “apples-to-apples” comparisons, and inconsistency and uncertainty regarding error resolution rights, limitations of liability, and related disclosures.

However, the Bureau also incorporated person-to-person (“P2P”) payments and digital wallets within the scope of “prepaid accounts” for purposes of Regulations E and Z in the Final Prepaid Card Rules. After postponement, the new rules will go into effect on April 1, 2019. So, it is timely to take a closer look at the protection that will be afforded to consumers for P2P electronic fund transfers and digital wallet accounts when the new rules become effective. This is particularly important because consumers are adopting electronic payment methods and digital/mobile banking at a rapid pace and this trend is likely to continue. Given the fundamentally different operation of these products and, in the case of a digital wallet, different services that may be offered to a consumer through a wallet account, it is questionable whether the consumer protection regime for traditional prepaid cards is appropriate for P2P electronic fund transfers and digital wallets. Innovation in this area continues at a rapid pace. It is time to re-visit the Final Prepaid Card Rules and adapt the consumer protections for evolving electronic fund transfers in a way that protects consumers in light of the risks attendant to the specific products, and their functions and operation, and still allows for future innovation.

A. The “Prepaid Card” Amendments to Regulation E

When the Bureau published the final rules amending Regulations E and Z in November, 2016 (the “Final Prepaid Card Rules”), the Bureau stated that it was “issuing this final rule to create **comprehensive consumer protections for prepaid accounts** under Regulation E which

¹ 81 Fed. Reg. 83943 (Nov. 22, 2016) (12 C.F.R. Parts 1005 and 1026).

implements the Electronic Fund Transfer Act; Regulation Z, which implements the Truth in Lending Act; and the official interpretations to those regulations.” (emphasis added)² When the Bureau published the Final Prepaid Card Rules, it culminated a several years-long rule-making and comment period process, as well as years of research by the Bureau. The Release that accompanies the Final Prepaid Card Rules provides a very detailed account of the rule-making process, proposals and comments received, as well as justifications for the Bureau’s ultimate rule-making decisions. The reader is directed to the thousand+ page release for further edification. The Final Prepaid Card Rules originally were due to go into effect in October, 2017, subject to a number of exceptions. That date has been extended, and the Final Prepaid Card Rules have since been amended, with a new effective date of April 1, 2019.

One of the changes incorporated into the Final Prepaid Card Rules that had not been included in the Advance Notice of Public Rulemaking on the prepaid card rule³ was the expansion of the definition of “prepaid account” to include accounts used for P2P transfers and digital wallets. While the words in amended Regulation E specifically refer to an account “[w]hose primary function is ... to conduct person-to-person transfers...,”⁴ the Bureau’s commentary to the Final Prepaid Card Rules make clear that this expanded definition of “prepaid account” also is intended to cover digital wallets.⁵

Reading the commentary to the Final Prepaid Card Rules, it appears that the Bureau’s primary justification for inclusion of digital wallets and P2P transfers within the scope of Regulation E and prepaid accounts was the recognition that digital/mobile banking and electronic transactions were increasingly being adopted by consumers and a desire to provide a regulatory framework of protection.⁶ Looking to the fundamental purposes of the Electronic Fund Transfer Act of 1978 (to establish “rights, liabilities, and responsibilities of participants in electronic fund and remittance transfer systems” and “provide individual consumer rights”),⁷ the Bureau sought to implement consumer protections for accounts within its purview under Regulation E.

Despite including digital wallets and P2P transaction accounts under the same rubric as other “prepaid accounts” subject to Regulation E, it is interesting to note that even the CFPB recognized in 2016 that those newer payment products were still evolving and were not represented by a “one size fits all” model and that the universe of transactions processed through a digital wallet might be much broader than traditional prepaid card transactions. In the Release to the Final Prepaid Card Rules, the CFPB stated “there may be significant variations in how funds are held in digital and mobile wallets and how payments are processed by such wallets.”⁸ The Bureau

² 81 Fed. Reg. 83943 (Nov. 22, 2016).

³ The prepaid card ANPR was issued in 2012. See 81 Fed. Reg. 83593 for a summary of the rule-making process.

⁴ 12 C.F.R. 1005.2(b)(3)[Effective April 1, 2019](i)(D).

⁵ “The Bureau is thus finalizing a definition of prepaid account that covers a range of products including GPR cards, as well as other products that may not be used as transaction account substitutes, such as certain non-reloadable accounts and digital wallets.” 81 Fed. Reg. 83968 (Nov. 22, 2016).

⁶ “Likewise, consumers increasingly use digital wallets to conduct daily financial transactions for which Regulation E protections are important.” *Id.*

⁷ 15 U.S.C. 1693 (b).

⁸ 81 Fed. Reg. 83943 (Nov. 22, 2016).

also recognized that “payment processing by digital and mobile wallets is evolving quickly” and that “the application of EFTA and Regulation E to digital and mobile wallets has been less clear than the application of the statute and the regulation to prepaid products.”⁹

B. P2P Payments, Digital Wallet Accounts, and Prepaid Cards

In order for the protections afforded consumers under the Final Prepaid Card Rules to address risks appropriately, presumably the risks attendant to the underlying accounts/products/services should be the same or comparable. I do not believe that is the case when comparing a prepaid card to a consumer-directed P2P electronic fund transfer or when comparing either of the foregoing to a digital wallet account. Similarities exist to the extent that each of these three electronic payment vehicles today usually relies on an account for purposes of effecting an electronic fund transfer. Beyond this one similarity, these products are fundamentally different and when assessing what protections are needed to protect consumers engaged in use of these products, those differences need to be considered. For example, the initiation of the fund transfer may be different, the “rails” for the transfer may be different, the intermediaries and regulatory status of intermediaries may be different, the dispute resolution and charge-back rights of the consumer may be different, and in the case of a digital wallet, there may be other electronic payment transactions affected through the account that have their own legal/regulatory implications. When the CFPB enacted the Final Prepaid Card Rules, the CFPB observed that, “[T]o the extent that [digital wallets] are used to access funds the consumer has deposited into the account in advance, the Bureau believes digital wallets operate very much like a prepaid account.”¹⁰ That statement may be true, as far as it applies to a consumer accessing funds in a deposit account. However, a digital wallet account also can offer much richer and varied functionality, such as access to other payment credentials (debit, credit, prepaid card products), electronic bill pay, P2P transfers, microloans, overdraft credit. All of which suggests consideration of a different consumer protection regime.

C. The Final Prepaid Card Rules and Consumer Protection

1. Disclosure Requirements

The amendments to Regulation E codified in the Final Prepaid Card Rules and subsequent amendments adopted by the CFPB contain, among other provisions, highly prescriptive pre-acquisition disclosure rules designed to enable a consumer to make an apples-to-apples comparison of prepaid card pricing. A laudable “know before you buy” goal. While one might argue about whether or not that particular goal is achieved in the categories of fees required to be disclosed on the “Short Form Fee Schedule” for a prepaid card, it is at least conceivable that a consumer might see many of the same types of fees listed on fee schedules for traditional general purpose reloadable prepaid cards.

Contrast that situation with a digital wallet/electronic banking solution that offers: a bank account with a linked debit, credit and/or prepaid payment card, electronic bill pay, P2P transfers, and maybe even overdraft credit. Following the highly prescriptive pre-acquisition disclosure rules

⁹ Id.

¹⁰ Id. at 83968.

designed to provide an apples-to-apples comparison of fees for a general purpose reloadable prepaid card program is doable, but some of the information simply will not be very meaningful or helpful to the consumer. And, a required statement directing the consumer to the CFPB website for more information on prepaid accounts likely will be confusing.

Missing from these highly prescriptive disclosures in the P2P context is any information alerting a consumer to the different rights that the consumer may, or may not, have with respect to a misdirected P2P transaction and underscoring the importance of verifying recipient information.

Zelle is an example of a P2P digital transfer platform where consumer-directed transfers are affected through bank account transfers. According to public press, over \$50 billion was transferred through Zelle last year. Zelle involves a credit/"push" payment initiated by a consumer with her bank/payment provider, authorizing payment to be made to an intended recipient, using an intended recipient's e-mail address or U.S. mobile number. But what happens if the payment doesn't get to the intended recipient? For example, what if the consumer mis-types the recipient's e-mail address or, unbeknownst to the consumer, the recipient has changed her mobile number? What if the payment was for the purchase of goods and the goods are never delivered? Unlike with a traditional credit or debit payment card purchase, Zelle does not offer the equivalent of charge-back rights. Recovery of a mis-directed payment occurring due to problems with an e-mail address or phone number will likely depend on individual bank policies and individual facts and circumstances, rather than Regulation E, because the consumer ostensibly authorized the transaction. (See "Error Resolution and Unauthorized Transaction Protection" below.)

Nowhere in the Final Prepaid Card Rules are any specific disclosures or warnings required to remind consumers to double-check the accuracy of recipient information for P2P payments, nor are there warnings about the lack of established means for recovering mis-directed payments. This is different than a payment card product, where the consumer might have recourse through her card issuer or financial institution. For an example of another country that has implemented a voluntary code with such requirements, see "Australia ePayments Code" below.

2. Error Resolution and Unauthorized Transaction Protection

Section 1005.11(a)(1) of Regulation E, defines an "error" to mean, among other things:

- i. an unauthorized electronic fund transfer; and
- ii. an incorrect electronic fund transfer to or from the consumer's account.¹¹

In the typical P2P transaction described above, the consumer-sender is the party that gives the direction for the payment to the consumer-recipient. That makes it challenging to see how the usual facts and circumstances of a mis-directed P2P payment will meet the definition of an "error" for purposes of Regulation E, leaving the consumer without the protection that the consumer would have for an electronic fund transfer made by her financial institution from her bank account based on a debit card or prepaid card transaction.

¹¹ 12 C.F.R. 1005.11(a)(1).

D. Australia ePayments Code

Australia has adopted the ePayments Code (formerly known as the Electronic Funds Transfer Code of Conduct; the “ePayments Code”). The Australian Securities and Investment Commission (“ASIC”) is responsible for the administration of the ePayments Code, including reviewing it regularly. The ePayments Code is a voluntary code of practice that has been adopted by banks, credits unions and other providers of electronic payment facilities to consumers who subscribe to it. According to the ASIC website, “Almost all banks, credit unions and building societies in Australia are subscribers to the ePayments Code. Other providers of consumer electronic payment facilities such as PayPal have also subscribed to the code.”

The ePayments Code provides consumer protections for “Pay Anyone” P2P transfers. “Pay Anyone” transfers are consumer-directed fund transfers from the consumer’s account to another consumer’s account at any Australian financial institution (bank, building society, credit union) account based on account details and payee identifying information (e.g., phone number or email address) provided by the sending consumer. Consumer protections provided under the ePayments Code include:

- On-screen warnings to consumers which clearly warn users about the importance of entering the correct identifier and the risks of mistaken Internet payments, including: (a) funds may be credited to the account of an unintended recipient if the identifier does not belong to the named recipient, and (b) it may not be possible to recover funds from an unintended recipient; and
- Rules for determining who pays for unauthorized transactions; and
- Process for recovering mistaken internet payments that includes the sending and receiving accountholders’ institutions.¹²

CONCLUSION

The evolution of electronic payment transactions has continued since the CFPB published the Final Prepaid Card Rules in November, 2016. The Bureau appropriately recognized at that time that large numbers of consumers were adopting digital and electronic payment products and funds transfer mechanisms and that consumers should be accorded protections when engaging in these banking services. We know more now, than we did then, about some of the different innovative technological and operation solutions that may power P2P payments and digital wallets and the different functionalities that might be offered through various solutions, and have begun to identify particular risks that may be posed to a consumer in some of these products.

Consumer-directed P2P fund transfers and digital wallet accounts that may operate as fulsome electronic banking solutions are fundamentally different than traditional prepaid cards and, understandably, the attendant risks are different. Therefore, it is time to re-visit the consumer protection regime in the Final Prepaid Card Rules for “prepaid accounts” to ensure that the protections accorded to consumers for P2P payments and digital wallets are tailored to these products. The Australia ePayments Code is an example of tailored disclosures and recourse for

¹² ePayments Code Chapter E, Sections 24-34.

mis-directed payments in a consumer-directed P2P payment. However, it is important to keep in mind that innovation in this area is continuing at a rapid pace. In order to protect consumers and still foster the innovation desired by consumers, it is important to adopt rules and principles with sufficient flexibility to adapt to different situations and models, rather than a set of highly prescriptive rules. Based on what we know today, I suggest that those general rules and principles include: warnings/information to consumers prior to engaging in consumer-directed P2P transfers about the need to verify recipient information; if finality of payment is involved, information/warnings about irreversibility; and some form of dispute resolution process to assist consumers with mis-directed payments. Protections for digital wallets should be tailored to the specific payment transaction involved, rather than simple focus on the digital wallet account that may be used as base for linked banking services and other functionality, such as P2P and other electronic payment transactions, linked payment card transaction processing, electronic bill pay, overdraft credit, and microloans.