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July 23, 2012

Ms. Monica Jackson
Office of the Executive Secretary
Bureau of Consumer Financial Protection
1700 G Street, NW
Washington, DC 20552

RE: Docket No. CFPB-201200019

Dear Ms. Jackson:

The Pew Charitable Trusts' Financial Security Portfolio is pleased to provide comments in response to the Consumer Financial Protection Bureau's Advanced Notice of Proposed Rulemaking on General Purpose Reloadable Prepaid Cards. In December 2011 and January 2012, the Portfolio analyzed the account agreements, fee schedules, and other web pages for the 52 GPR prepaid cards that are available for purchase online from the American Express, MasterCard, and VISA websites. This sample, which represents at least 75 percent of the market, typifies the type of prepaid cards a consumer can choose. Pew's quantitative research report on these cards, *Loaded with Uncertainty: Are Prepaid Cards a Smart Alternative to Checking Accounts?*, will be published next month. Pew also conducted qualitative research using focus groups with consumers who purchase and use prepaid debit cards.[1] *Key Focus Group Findings on Prepaid Cards* provides details on the results of these discussions. Pew's comments herein are based on the data and analysis from both of these research projects.

Introduction

General purpose reloadable (GPR) prepaid cards are often thought of as an alternative to a checking account. They are a burgeoning product; in 2009, consumers loaded $28.6 billion onto these cards, and by 2013 that figure is expected to reach $116.9 billion.[2]

Given that prepaid cards can be used as a substitute for, as well as in addition to, a checking account, Pew compared the terms, fees, and conditions provided by GPR prepaid cards with those for checking accounts. Both products are used by consumers to receive deposits, make point-of-sale purchases, pay bills, and withdraw cash from ATMs. However, despite these shared purposes, significant differences exist between them. Most notably, the checking account has a fairly uniform fee structure, is federally regulated through mandated consumer protection laws, and carries up to $250,000 in federal insurance against bank failures. In contrast, the GPR prepaid card market is evolving, with an array of fee structures and services offered. The cards also currently lack meaningful federal consumer protection regulations and oversight.

GPR prepaid cards are marketed, sold, and maintained by companies that are known as "program managers." Most program managers are not banks, but rather keep funds in "pooled accounts" in banks. If a program manager follows the rules outlined by the Federal Deposit Insurance Corporation (FDIC) for insuring funds in a pooled account, these cards can be insured for up to $250,000.
Funds can be loaded and reloaded onto GPR prepaid cards through cash loads, direct deposit, and bank transfers. Of the 52 cards Pew studied, 98 percent allow for cash loads, 92 percent permit direct deposits, and 58 percent provide at least one way to add money from a bank account. When the card balance is depleted, it may be reloaded with additional funds.

A. Regulatory Coverage

Consumers often incorrectly assume that there is federal government oversight of the prepaid card market.

Laws like the Truth in Savings Act (TISA) and the Electronic Fund Transfer Act (EFTA) provide mandatory disclosures and protections to consumers with checking accounts. While GPR prepaid cards can fill the functions of these accounts, they are not afforded the same protections.

In addition, the non-bank program managers which offer these cards presently are not directly supervised by the CFPB or any other federal regulator. The GPR prepaid card market is currently operating without federal supervision and without basic protections for consumers against loss of funds or unfair, deceptive or abusive acts or practices (UDAAP). This lack of oversight could turn a potentially beneficial emerging product into a haven for predatory lenders and other unscrupulous actors.

Yet most of the participants in Pew's GPR prepaid focus groups assume that the federal government provides oversight of prepaid cards. They are unaware of consumer protection gaps and are troubled upon learning of them. A female participant from Chicago stated, "I feel like if you are going to take someone's money, there has to be some regulation. If there wasn't regulation, I could open up a business and say, 'Hey, give me your money because it's a prepaid card,' and then I could just disappear, and then all these prepaid cards don't work. There has to be regulation at all times for doing that."

The contractual protections from liability for unauthorized transfers currently provided by GPR prepaid card companies are not as comprehensive as the protections provided to checking accountholders under the Electronic Fund Transfer Act.

When a charge is placed on a checking account that was not authorized by the cardholder, EFTA provides certain mandatory protections, including requiring the financial institution to investigate the claim, limiting the liability of consumers, and requiring provisional credit to the account while the case is pending. Banks also are required under EFTA to provide customers with periodic paper statements so they can determine if any transactions were unauthorized.

In contrast, GPR prepaid cards do not have any regulatory protections against unauthorized use. Rather, those protections are provided on a discretionary basis by the program manager in the account agreement. Moreover, GPR prepaid cards are not required to provide customers with any periodic statements or any other access to information about past transactions.

All of the cards Pew studied included some form of contractual protection from liability for unauthorized transfers in their account agreement. However, the extent of the protection given to cardholders was generally not as favorable as the protections that are guaranteed to checking accountholders by EFTA. Additionally, because the protections are offered by the program manager at its discretion, they could be revoked at any time. All of the cards studied by Pew reserved the right to amend the cardholder agreement and therefore could remove the liability protection from the contract. Most disclosed they would notify customers of any changes.

Furthermore, many GPR prepaid cards do not provide customers with adequate information to determine if an unauthorized transaction has taken place. While 98 percent of GPR prepaid cards offer free online access to account balances and past transactions, only 48 percent of cards explicitly disclose that they provide at least a 60-day history of each customer's account. The other cardholder agreements either state that they only provide information about the last five charges on their websites or they are silent on the matter. Accordingly, GPR prepaid cardholders have a harder time detecting errors with their accounts and are thus more exposed to the effects of fraud.

The treatment of checking accountholders is monitored by federal agencies such as the CFPB, FDIC, Federal Reserve, Office of the Comptroller of the Currency, and the National Credit Union Administration. Several laws, such as the TISA and EFTA, provide mandatory disclosures and protections to consumers.[3] The Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act) gave the CFPB the ability to supervise larger participants of a market for consumer financial products or services. This means the CFPB has the authority not only to write rules pertaining to the GPR prepaid card market, but also to actively supervise the larger participants.

B. Product Fees and Disclosures

Disclosures on GPR prepaid cards are often unclear and their lack of uniformity hinders consumers' ability to compare the fees, terms and conditions of the cards.

Pew's examination of the 52 GPR prepaid cards that are available for purchase online at the websites for American Express, MasterCard and Visa found a wide range in the number of fees disclosed. Most GPR prepaid cards included between seven and 15 fees. Common fees for GPR prepaid cards include, but are not limited to, charges for card acquisition, monthly maintenance, point-of-sale signature and PIN transactions, withdrawals from ATMs, and speaking with a customer service representative. Given the number of fees included with these cards, it is essential that these be disclosed to the consumer up-front, when they are purchased.

The median cost for most service charges on the GPR prepaid cards Pew studied was less than three dollars. Of the GPR prepaid cards Pew studied, monthly or maintenance fees were very common – 90 percent charged this type of fee. All cards that disclosed information about out-of-network ATM fees stated that the program manager charged an extra fee along with any fee charged by the owner of the ATM. With regard to ATM withdrawals, seven cards provided all in-network withdrawals free of charge and two cards offered limited free ATM usage. More than half of the 52 cards charged a fee for speaking with a customer service representative via telephone. Nearly one in five charged a fee for all point of sale transactions. Almost two-thirds of the cards charged a fee for a declined ATM withdrawal, while less than one-quarter disclosed a fee for a failed point-of-sale transaction. Ten percent of cards disclosed either "negative balance" or "shortage fees."

Pew found that the disclosures do not allow a consumer to distinguish between a fee which is not charged versus a fee that is undisclosed. For example, 21 percent of the cards studied disclosed that live customer service calls were free while an equal number did not disclose any information about this fee. These disparities in disclosure make it very difficult for a consumer to comparison shop for this product.

Many of the cards Pew studied included a summary box of fees and terms in their disclosures. However, the ability to compare terms across cards is hindered by the lack of uniformity among the disclosure boxes currently in use. This is problematic when the fees associated with individual GPR prepaid cards and the services offered vary widely. Without any standardization in the summary boxes offered by GPR prepaid cards, consumers will continue to have difficulty comparing products and choosing the option that is best suited for them.

Most participants in Pew's focus groups are "very concerned" that prepaid card companies do not have the same obligation to disclose fees as banks have. A male participant in Houston stated, "That just highlights my point: most folks aren't going to read the fine print. I think the card company should take the responsibility to make sure that their customers are informed."

Funds loaded onto GPR prepaid card are not uniformly covered by federal deposit insurance throughout all channels of the market.

FDIC insurance provides a backstop to financial loss for checking accountholders. When a bank fails, the FDIC reimburses covered accountholders for losses up to $250,000. For many GPR prepaid cardholders, there may not be such a safety net. GPR prepaid cards, unlike traditional checking accounts, cannot be directly covered by FDIC insurance but can be more tenuously secured by pass-through insurance, which allows program managers to hold customers' funds in a single pooled account and facilitate up to $250,000 in federal insurance to each cardholder. However, because there is no federal supervision of GPR prepaid cards, there are no safeguards in place to ensure that the program managers' assertions of FDIC insurance are accurate.

There are many ways in which the funds on a GPR prepaid card could be uninsured. FDIC insurance is not required for GPR prepaid cards, so a program manager could choose not to provide it. In addition, GPR prepaid cards must be registered with the program manager before FDIC pass-through insurance will apply. This means that "temporary cards," which are commonly distributed to consumers when they purchase a GPR prepaid card at a retail store, are not FDIC insured.

FDIC insurance only applies to funds that are actually currently held in an insured bank account. However, the loading process for GPR prepaid cards creates situations in which funds are not under the control of a financial institution and are therefore uninsured. For example, when a customer uses a Green Dot MoneyPak to load funds, they are not insured. A MoneyPak is a credit that can be purchased at a retailer with cash that then can be used to load or reload funds onto any participating GPR prepaid card. Until the MoneyPak is used and Green Dot transfers the funds to the program manager, which then deposits the funds in an insured account, the money is not protected by the FDIC.

In addition, there are no supervisory safeguards to ensure that GPR prepaid card program managers that claim to hold customers' funds in an FDIC-insured account are in fact holding all of those funds in such an account. For example, a dishonest company might use customers' funds for high-risk investments. If a program manager goes out of business, any funds that are not actually being held in an insured account could potentially be lost.

Of the 52 cards Pew studied, only three indicated that they lacked FDIC insurance. Of the remaining 49 cards, 23 disclosed that the funds held on the card were FDIC insured. For the other 26 cards, the disclosures were unclear as to whether each individual would be insured up to $250,000. However, for cards managed by non-banks, the fact remains that FDIC insurance may not be in place to fully cover the cardholders. Claims of FDIC insurance in cases where portions of consumers' funds may in fact be uninsured could create a false sense of security to unsuspecting consumers.

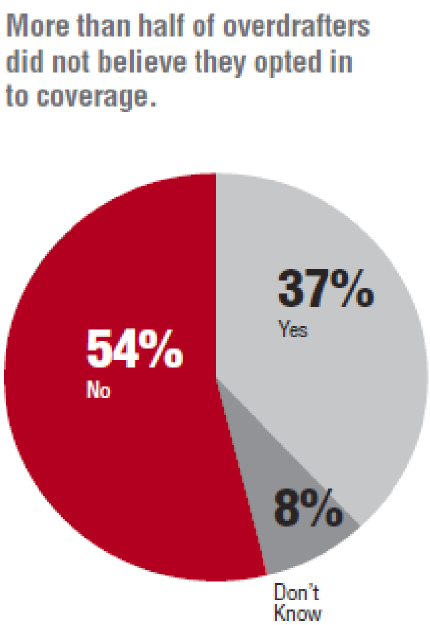
Most participants in Pew's focus groups were "very concerned" that not all cards have FDIC insurance. A male participant in Chicago stated, "Because I want my money back. Give me my money, and if I put it on your card, I deserve to get it back. I think they should be regulated by the FDIC."

C. Product Features

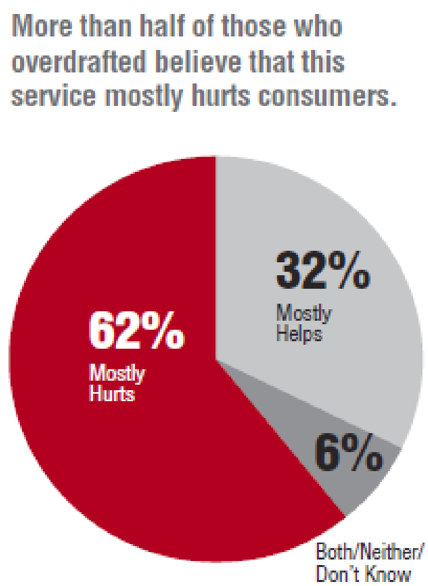
While most GPR prepaid cards do not currently include overdraft products, a prepaid card provider could enroll customers into such a service without getting affirmative consent as is required by Federal Reserve rules for debit card overdrafts.

Most GPR prepaid cards did not allow overdraft fees, which can keep costs for consumers low and ensure that "prepaid" cards remain just that. However, unlike consumers who use their debit cards for point of sale and ATM transactions, GPR prepaid cardholders are not protected from automatic enrollment into overdraft plans. In 2010, new Federal Reserve regulations required financial institutions to obtain affirmative consent from checking accountholders before they could be enrolled in overdraft penalty plans for debit point-of-sale and ATM transactions. Like other federal regulations implementing EFTA, this requirement to "opt-in" does not apply to GPR prepaid cards. Accordingly, should a prepaid card provider decide to offer overdraft services, unsuspecting consumers could be automatically enrolled into a costly plan.

In May, 2012, Pew published *Overdraft America: Confusion and Concerns about Bank Practices* which explored the understanding and attitudes of consumers who had overdrafted with their debit card on a point of sale or ATM transaction in the past year. The survey showed that these consumers struggle with bank overdraft policies and have strong concerns about these practices. Consumer difficulties with bank overdraft products are yet another reason to limit their availability on GPR prepaid cards, particularly since overdraft products undermine the very nature of the card itself.



As far as you know, did you choose to sign up for overdraft coverage, where you are charged a fee for each overdraft, or not?



Overall do you think that overdraft coverage for a fee mostly helps consumers like you or mostly hurts consumers like you?

Participants in Pew's focus groups stated that GPR prepaid cards allow them to limit their spending and avoid incurring unwanted debt. A female participant in Chicago stated, "You're not overdrafting, and what's on there is what's actually on there. If you have a prepaid card with $500, it's a $500 limit….If you have a credit card with $500, one you don't actually have $500. You just have this imaginary $500 that you have to pay back. Even though you say, 'Oh, it's fine. I'll just put X amount on each month and it will be gone.' That might have happened, and also now, you're into the interest rates and all these things, and you're not paying it, and they're mad at you. Now your credit would be down. If you have money on your prepaid card, you're not going to pay it off because it's already paid."

A female participant in Houston stated, "One of the things that I did was I got one of those debit cards, and I know that whatever is on it is the only thing that I can spend. I'm not using my real credit card where I can spend and pay a little bit a month. I know I'm only allowed to use what is on the card, and that actually limits me as well.

When asked, many focus group participants are uneasy with the idea of including credit options with GPR prepaid cards. While some say credit could be useful in an emergency, most express concern that it would undermine the perceived value of having a prepaid card – to budget and avoid overspending.

The vast majority of participants reject the idea of including overdraft options on prepaid cards. Many envision getting into the same spiral of trouble with overdraft fees on their prepaid cards that they have had with their checking accounts. A female participant in Houston stated, "For me, anyway, the reason I use a prepaid card and encourage my daughter to do that as well (is) you can't get into credit trouble."

Similarly, many borrowers seem uncomfortable with adding lines of credit or small dollar loans to prepaid cards. As one borrower in a Pew focus group in Chicago stated, "It defeats the purpose of a prepaid debit card because it is, like, it's a credit card. You can use money that you really don't have to pay back and I wouldn't want to do that because I know I'm just going to get myself into trouble." None of the 52 agreements and other disclosures Pew studied included any mention of short-term credit products. Even the cards that included information about overdraft plans and penalty fees did not clearly indicate that they would allow customers to spend more money than was on their cards.

Nonetheless, some GPR prepaid cards have been tied to potentially costly credit products such as small dollar loans. For instance, one GPR prepaid card, which was not available on any payment network website and was therefore not a part of Pew's study, allows consumers to take out short-term loans that are repaid after their subsequent deposits.[4]

Likewise, GPR prepaid cardholders can be targeted by outside third parties that offer expensive debt products that function like overdraft fees. Companies offering these services have begun to appear online and pose a serious risk to the ability of GPR prepaid cardholders to spend only the amount of money they have on their cards. One example is a third-party product that extends credit to GPR prepaid cardholders whose transactions would be declined because of insufficient funds.[5] In turn, the cardholder is required to repay the loan at the next deposit and is charged $1.60 for every $10 borrowed.

These types of credit products put GPR prepaid cards at risk of losing their status as an alternative to checking accounts that enable consumers to spend within their means. They also risk replicating a payday lending business model that is highly questionable. Pew recently published a report – *Payday Lending in America: Who Borrows, Where They Borrow, and Why* – which studied the use of small-dollar loans that require borrowers to repay in full on their next payday. The report concluded, in part, that:

> Payday loans are marketed as short-term credit products intended for emergency use, and they usually are depicted as a fix for an unexpected expense. However, Pew's first-of-its-kind survey reveals that seven in 10 borrowers use payday loans to deal with recurring expenses, while only one in six uses the loans for unexpected emergencies. Pews' analysis shows that the vast majority of borrowers use the loans on a long-term basis, not a temporary one. Thus it seems that the payday loan industry is selling a product that few people use as designed and that imposes debt that is consistently more costly and longer lasting than advertised.

Pew's findings strongly suggest that replicating the payday loan model on prepaid cards will lead to similar outcomes, with borrower experiences differing significantly from what they might expect based on how the loans are packaged and promoted. The CFPB should not condone the expansion of payday lending models to prepaid cards pending its full review of payday lending policy.

Focus Group Participants Welcome Savings Features But Not Necessarily Credit Building Features

The overwhelming majority of Pew focus group participants want a savings feature on their GPR prepaid cards. A female participant in Chicago stated, "It would help me to save more. It would, really, because if I just have just my checking it will be hard for me to just take money out and physically go put money in my savings or do it myself. If I have a feature to do it for me, I will save more."

With regard to credit building, about half of Pew's focus group participants support using prepaid cards to build credit history or repair damaged credit. Others strongly oppose it and have concerns about protecting their privacy. A female participant in Houston stated, "(I am) rebuilding and rebounding from the devastation of divorce….I have one line of credit and it's minimal. I'm penalized in my purchasing of large items because I don't have an active credit history now, even though I feel like I'm being very, very prudent with my spending and I'm a good credit risk. I have no proof of that because I operate on a cash basis or (with a) prepaid debit card."

Conclusion

GPR prepaid cards could potentially provide a valuable and needed substitute for consumers who are unable or unwilling to maintain a traditional checking account. While the fees for everyday services are generally higher for GPR prepaid cards than checking accounts, the trade off of a product that does not allow overspending may be beneficial to many consumers. However, at the moment, the unsupervised and unregulated status of the GPR prepaid card market creates many concerns about the terms, conditions, and fees that commonly accompany these cards.

Policy makers have recognized the importance of safety in consumer financial products, especially those that involve the holding of deposits for everyday use—most commonly the checking account. For all accounts held at financial institutions, federal regulators can ensure that accountholders are not being taken advantage of through their supervisory and UDAAP authority. Congress has given the CFPB the authority to supervise the larger participants in any financial services market, including GPR prepaid cards. Congress also has given the CFPB broad authority to regulate electronic fund transfers, which could be used to ensure that GPR prepaid cards are viable and safe options for consumers who want to avoid overspending and costly credit products that are commonly associated with checking accounts. Without better consumer protections, GPR prepaid cards will continue to put customers at risk.

Pew welcomes the opportunity to share our research on GPR prepaid cards with the CFPB. As always, we are available to discuss these comments or any other aspect of our work at any time.

Sincerely,

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[1]The two-hour sessions took place on November 14, 2011 in Houston, Texas and on November 17, 2011 in Chicago, Illinois. Two sessions were held in each city ; a total of 40 participants were included in the four discussions.
[2]Mercator Advisory Group, Prepaid Market Forecasts, 2011-2014, November, 2011.
[3] See Truth in Savings Act, 12 U.S.C. § 4301 et seq. (2012); Electronic Fund Transfer Act, 15 U.S.C. § 1693 et seq. (2012)
[4] Press Release, USA Cash Advance (Feb. 9, 2012), available at http://www.24-7pressrelease.com/press-release-rss/usa-cash-services-now-offers-debit-cards-to-complement-nevada-payday-loans-262208.php.
[5] Webpage of SureCashXtra, available at https://www.mysurecash.com/LearnMore.html#one.