

FTC Input Likely To Propel Tougher Prepaid-Card Rules

By Allison Grande

Law360, New York (July 30, 2012, 9:02 PM ET) -- The Federal Trade Commission on Monday urged the federal government's consumer finance watchdog to push forward with its proposed regulation of a popular type of prepaid card, a move attorneys say will spur the implementation of stronger consumer protections for this product, mirroring those for checking accounts.

In public comments dated July 23, the FTC staff supported the Consumer Financial Protection Bureau's May 24 proposal to solicit information about the expense and benefits of enhancing protections related to the costs and terms of general-purpose reloadable cards, which consumers can fill up with money and spend almost anywhere.

While these cards function in much the same way as debit cards attached to checking accounts, the prepaid market is currently not subject to the same level of scrutiny as the issuers of traditional bank-account-linked products, a gap that the FTC — which has brought numerous actions against sellers such as VirtualWorks LLC and Swish Marketing Inc. alleging they duped consumers into buying the cards — believes should be narrowed.

“Although consumers who use GPR cards are protected from unfair and deceptive practices under the FTC Act, they have less protection under other federal laws regarding the cards' costs and terms than users of other types of payment cards,” the FTC's comments said. “Providing additional protections to consumers who use GPR cards may instill greater confidence in their use, fostering increased use and competition between GPR cards and other payment methods.”

The FTC's insistence that any regulation of this space establish protections for fraud and unauthorized-use liability limits, fee and expiration date disclosures, error resolution procedures, and recurrent payments — safeguards that are all typically applied to other payment cards — might provide the CFPB with the nudge it needs to implement stronger and more consumer-friendly protections in this space, according to attorneys.

“It's an important comment from the perspective that it's from another federal agency charged with consumer protection and bolsters the concerns that are expressed by the CFPB in its May 24 advance notice of proposed rulemaking,” Paul Hastings LLP partner Kevin Petrasic told Law360 on Monday. “Now we have the observations of two federal agencies charged with consumer protections that are looking to extend the types of protections for debit cards to general-purpose reloadable cards, and they're clearly moving forward in tandem.”

This support of a more expansive rule could also provide a boost to the rulemaking process by “encouraging the CFPB that it is on the right track,” according to Foley & Lardner LLP partner Christi Adams.

“The FTC is giving the CFPB guidance on what it, as the former regulator in a lot of these instances, would do if it were going to make these regulations,” she said.

Venable LLP of counsel Jonathan Pompan also pointed out that not only do the regulators agree on the approach to policing this space, consumer groups share their view.

In their own public comments, Americans for Financial Reform, the National Consumer Law Center, the Consumer Federation of America and two dozen other consumer advocates urged the CFPB to enact stronger consumer protections for prepaid cards, specifically requesting that the agency ban overdraft fees and payday loans on these products, the CFA announced.

“There's a consistency among these comments that would definitely give observers a very good sense of where consumer protection regulators would like to see this go,” Pompan said. “When all is said and done, there most likely won't be a large gap between what the FTC is supporting and what the CFPB will eventually propose.”

While the CFPB is likely to take an aggressive stance toward regulating this space, it remains vital that the agency take into account the unique challenges of the market, which differs from more traditional payment methods due to the issuers' more informal relationship with purchasers, who tend to be unbanked or underbanked consumers, according to attorneys.

For example, banks provide credit and debit cardholders with fee disclosures when they sign up for cards. But reloadable cards are often sold in small packages at retail locations where space is at a premium, making these disclosures more difficult, according to Morgan Lewis & Bockius LLP financial services litigation group co-chair Kenneth Kliebard.

“Issuers are unlikely to attach legal papers to these cards in a retail environment,” he said. “So that means we might see some type of online vehicle for making disclosures to consumers.”

Implementing error resolution and fraud protections can also be costly to the issuers of these cards, which may in turn affect the cards' availability to consumers, attorneys say.

Both the CFPB's proposal and the FTC's comments take this risk into consideration, Adams said.

“It seems like they don't want to put a rule into effect that prices the product out of consumer range,” she said. “They want to strike a balance between protecting consumers and freedom of choice for consumers.”

With the CFPB seeming to favor enforcement over enacting new rules in the early stages of its existence — the agency has an active investigation pending in all of the areas it has jurisdiction over, while it has rulemakings pending in only some of these areas, according to its semiannual report, released Monday — its reloadable-card initiative provides it with the opportunity to set its own standards without targeting a certain provider, Pompan added.

“It's significant that the CFPB has chosen to go down the regulatory path and not simply the investigation and enforcement path that it appears to be doing in other areas and that has also been the FTC's [strategy],” he said. “This may very well go down as one of its earliest regulatory moves.”

--Editing by Elizabeth Bowen and Cara Salvatore.

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