

March 23, 2015

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

Re: Prepaid Accounts Under the Electronic Fund Transfer Act (Regulation E) and the Truth in Lending Act (Regulation Z)
Docket No. CFPB-2014-0031 and RIN 3170-AA22¹

I. Introduction

The **Center for Responsible Lending** (CRL)² files this comment in response to the CFPB's proposed rule addressing prepaid accounts. We thank CFPB for its careful attention to prepaid cards, whose terms can have such a significant impact on the financial lives of the often unbanked and underbanked consumers who use them. Our comment letter addresses solely issues related to credit products associated with prepaid cards, with a particular focus on overdraft.

We strongly support much of what the Bureau has proposed regarding credit associated with prepaid cards. We strongly support its aim that any credit offered to prepaid cardholders be subject to Regulation Z's credit card rules. We strongly support its decision not to extend the flawed Regulation E "opt-in" overdraft regime to prepaid cards.

However, we strongly urge that the Bureau refuse to sanction overdraft charges on prepaid cards at all.

Context – as the Bureau recognizes throughout its proposal – matters. With respect to overdraft charges on prepaid cards, it could not matter more. As the Bureau recognizes, the context is that financial institution overdraft programs have driven many consumers out of the banking system, either voluntarily or involuntarily. The context is that many of those consumers, and others who have retained bank accounts despite negative experiences with overdraft fees, look to prepaid

¹ 79 Fed. Reg. 77102 (Dec. 24 2014).

² The Center for Responsible Lending (CRL) is a not-for-profit, non-partisan research and policy organization dedicated to protecting homeownership and family wealth by working to eliminate abusive financial practices. CRL is an affiliate of Self-Help, which consists of a state-chartered credit union (Self-Help Credit Union (SHCU)), a federally-chartered credit union (Self-Help Federal Credit Union (SHFCU)), and a non-profit loan fund. SHCU has operated a North Carolina-chartered credit union since the early 1980s. Beginning in 2004, SHCU began merging with community credit unions that offer a full range of retail products. In 2008, Self-Help founded SHFCU to expand Self-Help's mission.

cards as a way to avoid overspending, overdraft charges, or both. The context is that overdraft programs have a history of targeting financially vulnerable consumers and leaving them worse off. The context is that many prepaid card users share characteristics of consumers most likely to be targeted by any predatory financial practice. The context is also that overdraft fees have evolved, and thrived, as creatures of regulatory evasion, notorious now thanks to the shameless practices that have been employed to maximize them.

The context is also that the prepaid card market is almost free from overdraft today, but not entirely. And to the extent prepaid cards do carry overdraft fees, payday lenders are often the distribution channel. NetSpend is the largest prepaid card program manager that charges overdraft fees, and cards sold through payday lenders appear to be its largest source of revenue.³ Payday lenders distributing NetSpend's cards include ACE Cash Express,⁴ Advance America,⁵ Cash America,⁶ and Check 'n Go (CNG Financial);⁷ all of these cards carry overdraft fees. Another prepaid card manager that charges overdraft fees, Insight Card Services,⁸ distributes its cards through Approved Cash Advance⁹ and CheckSmart (Community Choice Financial).¹⁰ In addition, payday lenders have used overdraft functions on prepaid cards to evade credit laws before, and, if given the opportunity, likely will again.¹¹

³ Before its merger with TSYS, NetSpend disclosed that NetSpend's largest distributor was ACE Cash Express, with whom it had a long-term contract; that cards distributed through ACE accounted for 36.6% of NetSpend's total revenues in 2012; and that NetSpend's "long-term relationships" also included Advance America, Cash America International, and Check City. NetSpend Holdings, Inc., Form 10-K for the fiscal year ended December 31, 2012, SEC File No. 001-34915 at 7, <http://www.sec.gov/Archives/edgar/data/1496623/000104746913001507/a2212965z10-k.htm>.

⁴ *Id.*

⁵ See <https://www.advanceamerica.net/services/details/visa-prepaid-cards>.

⁶ See <http://www.cashamerica.com/FinancialServices/PrepaidVisa.aspx>.

⁷ See <https://www.checkngo.com/pre-paid-debit-card.aspx>.

⁸ See INSIGHT VISA® PREPAID RELOADABLE CARD CARDHOLDER AGREEMENT, https://www.insightcards.com/images/uploads/121221_TCs_v19a_REP_Final.pdf.

⁹ See <http://www.approvedcashadvance.com/visa-pre-paid-card.php>.

¹⁰ CheckSmart's main website, <http://www.checksmartstores.com/>, lists several different states where the prepaid card is available; one example is Arizona: <http://www.checksmartstores.com/arizona/prepaid-cards/>.

¹¹ The OCC took action against Insight Card's issuer, Urban Trust Bank, after noting "troubling" concerns about the line of credit and overdraft features on the cards that "have characteristics similar to predatory payday loans." Letter from Thomas J. Curry, Comptroller of the Currency, to the National Consumer Law Center (NCLC), CRL, and Consumer Federation of America (CFA) (Aug. 23, 2012), available at http://www.nclc.org/images/pdf/high_cost_small_loans/letter-occ-check-smart-urban-trust-bank.pdf. The payday lender CheckSmart had begun selling the Insight cards as a way to make 300% loans after Arizona voters upheld a 36% rate cap. See Comments of NCLC et al. to CFPB on Electronic Fund Transfers (Regulation E), Advance Notice of Proposed Rulemaking, Docket No. CFPB-20120019, RIN 3170-AA22 at 5 (submitted July 23, 2012), available at <http://www.nclc.org/images/pdf/rulemaking/cm-prepaid-card-july2012.pdf>.

Further, though the prepaid market is almost free from overdraft today, as the Bureau recognizes, it may not always be. The Bureau's regulation will provide far more regulatory clarity around overdraft on prepaid cards than there has been previously, and to some degree sanction it. This may result in a significant influx of overdraft into the prepaid market.

As context matters, so do the fundamental characteristics of financial products and services. Overdraft is a form of credit different from all others: On any given transaction, overdraft may be triggered without consciously accessing credit and on every transaction, overdraft is triggered only when funds are expended that exceed the funds in an associated asset account. Thus, virtually by definition, overdraft fees are felt most potently by those with little resources to spare. Prepaid cards, meanwhile, are an asset account different from all others in that, as the Bureau recognizes, they are typically marketed to and often used by consumers with fewer resources than the population at large, and because those consumers want to avoid overspending. They are marketed as "no credit check required," suggesting consumers suspect they would not qualify for the card if one were. And, typically, their name more than suggests – indeed, it promises – that they do not permit overspending, and whether or not the name "prepaid card" is used, the cards invariably emphasize the "control" they provide. Thus, overdraft and prepaid cards are each unique in ways that make combining them at best unnecessary, and at worst, very harmful.

This context, along with the fundamental nature of overdraft and prepaid cards, underlie why we believe the Truth in Lending Act and the Bureau's task to prohibit and prevent unfair, deceptive, and abusive acts and practices should compel it to prohibit overdraft charges on prepaid cards.

While our comments focus on overdraft, we also urge the CFPB to strengthen the credit card rules that would apply to any credit accessed through prepaid cards. Further, we strongly urge the CFPB to apply credit card laws to all credit transferred to a prepaid card (with some specified exceptions), regardless of whether the creditor has dictated that the credit be deposited to a particular card. The proposed "particular card" limitation risks undermining the entirety of the Bureau's proposed credit-related rules. While we discuss this issue very briefly at the end of these comments, the comments of the National Consumer Law Center (NCLC) submitted to this docket provide a longer discussion. We support that longer discussion, as well as the credit-related discussion and recommendations in NCLC's comment generally.

II. Summary of Recommendations

- A. Prohibit overdraft charges associated with prepaid card accounts, using TILA authority and authority to prohibit unfair, deceptive, and abusive acts and practices.**
- B. Short of prohibiting overdraft charges associated with prepaid card accounts, retain the general Regulation Z framework the Bureau has proposed but strengthen it to better prevent unfair, deceptive, and abusive acts and practices.**
 - 1. An ability-to-repay requirement should be applied but strengthened.**

2. **A limit on fees should be applied but strengthened, extending the 25%-of-credit-limit cap on fees to include pre-account opening fees and to apply to every year the account is opened.**
3. **Consumer control over repayment should be strengthened, including requiring that overdraft loans over a specified dollar amount be structured as installment loans (with an option to prepay).**
4. **A waiting period between registration and solicitation of credit should be imposed but lengthened to 90 days.**
5. **As proposed, terms and conditions should not be permitted to differ depending on whether a consumer has an overdraft or credit feature on the card.**

C. With respect to scope:

1. **The CFPB should include in the definition of “credit card” any card that accesses credit (with specified exceptions), even if the credit is not limited to a particular card.**
2. **The CFPB should support exclusion of prepaid cards falling under the definition of credit cards in this rule from the definition of credit cards covered under the Department of Defense’s pending rules under the Military Lending Act.**

D. Under Regulation E, as proposed, lenders should be prohibited from conditioning credit on preauthorized electronic transfers, but the Bureau should extend this prohibition to single-payment loans.

III. The Bureau’s proposal is not sufficient to prevent harmful overdraft practices on prepaid cards.

The Bureau’s proposal as it relates to overdraft would indeed impose restrictions currently lacking in the checking account space. It would apply Credit CARD Act protections to overdraft fees, requiring some consideration of the consumer’s ability to repay the overdraft and associated charges and limiting fees in the first year after account opening to 25 percent of the credit limit; prohibit requiring repayment more frequently than once per month; prohibit requiring automatic repayment; and prohibit attaching overdraft to the account until 30 days after registration of the account.

As the Bureau has found, the Credit CARD Act has been largely successful at curbing many of the most abusive practices credit card practices.¹² But most credit cards are not targeted at

¹² Consumer Financial Protection Bureau, *CARD Act Report: A review of the impact of the CARD Act on the consumer credit card market* at 4-7 (Oct. 1, 2013), available at http://files.consumerfinance.gov/f/201309_cfpb_card-act-report.pdf.

largely subprime consumers. Where subprime consumers are the target – with any financial product – aggressive, predatory practices tend to follow. Fee harvester credit cards that persist even in a post-Credit CARD Act market are clear evidence of this (for further discussion of these cards’ terms, see Section VI.D.2 below).¹³

Even while complying with the Credit CARD Act and the Bureau’s other proposed restrictions, a prepaid card issuer could:

- impose charges on overdrafts that the consumer was not conscious of, did not intend to occur, and would have preferred to avoid;
- make an ability-to-pay determination with no verification of a borrower’s income, debts or expenses and/or with no consideration of a borrower’s largest monthly costs, e.g., housing for a renter. For a largely subprime market, for an historically abusive product like overdraft, this ability-to-repay requirement is simply too weak (see Section VI.D below for further discussion);
- charge unlimited interest rates for overdraft;
- charge unlimited pre-account opening overdraft-related fees;
- charge unlimited overdraft fees after the account has been opened for one year; and
- require balloon repayment of principal, interest and fees.

In addition, though potentially inviting enforcement action, an issuer may aggressively and/or deceptively obtain consent to enrollment into an overdraft feature¹⁴ or consent to repay itself an entire lump sum via direct access to the prepaid card account.

These potential continuing abuses, in light of the context of overdraft programs generally (discussed in the following Part IV) and the prepaid card market, form the basis for our urging the Bureau to prohibit overdraft charges on prepaid cards altogether.

¹³ *Id.* at 77 (discussing fee harvesting credit cards as an ongoing concern).

¹⁴ The experience in the wake of “opt-in” for overdraft has shown all too clearly how aggressing and deceptive marketing can turn consent requirements on their head. See Leslie Parrish, *Banks Target, Mislead Consumers As Overdraft Deadline Nears*, Center for Responsible Lending (Aug. 5, 2010), available at <http://www.responsiblelending.org/overdraft-loans/research-analysis/Banks-Target-And-Mislead-Consumers-As-Overdraft-Deadline-Nears.pdf>; Center for Responsible Lending Research Brief, *Banks Collect Opt-Ins Through Misleading Marketing* (Apr. 2011), available at <http://www.responsiblelending.org/overdraft-loans/policy-legislation/regulators/banks-misleading-marketing.html>.

See also California Reinvestment Coalition, New Economy Project, Reinvestment Partners, and Woodstock Institute, *How Banks Sell Overdraft: Results of Overdraft Mystery Shopping in Four Key States* (July 2014), available at

<http://www.calreinvest.org/system/resources/W1siZiIsIjIwMTQvMDcvMzEvMTI0fNDBfNDdfODIxX0hvd19CYW5rc19TZWxsX092ZXJkcmFmdC5wZGYiXV0/How%20Banks%20Sell%20Overdraft.pdf>.

As further indication of consumer confusion, Pew found that more than half of consumers charged a debit card overdraft fee did not believe they were opted in. The Pew Charitable Trusts, *Overdrawn: Persistent Confusion and Concern About Bank Overdraft Practices* at 1 (June 2014), available at

http://www.pewtrusts.org/~media/Assets/2014/06/26/Safe_Checking_Overdraft_Survey_Report.pdf.

IV. Overdraft programs notoriously use unfair, deceptive and abusive practices that drive strapped consumers further into debt.

Overdraft programs provide a mechanism by which lenders easily and systematically reap outsized fees from consumers unable to keep up with ongoing expenses. In the checking account space, banks and credit unions have used these programs to strip tens if not hundreds of billions of dollars in fees from account holders, primarily from a relatively small subset of consumers who pay hundreds of dollars or more in fees annually.¹⁵

Overdraft programs have carried all the features of the worst forms of credit: no meaningful assessment of ability to repay, very high cost, very short term, balloon repayment, and first-in-line repayment directly from the consumer's next deposit. (As noted above and further in Part V below, the Bureau's proposal for prepaid cards would address some of these problems to some extent, but it would not address some of them sufficiently, if at all.) In addition to these fundamental design flaws, financial institutions have a history of shamelessly employing additional tactics to maximize overdraft fees further.

Most significantly, financial institutions extended fee-based overdraft to debit cards, despite no rational justification.¹⁶ The Federal Reserve later provided undeserved legitimacy to this practice by implementing an "opt-in" requirement for overdraft fees on non-recurring debit card and ATM transactions. Banks proceeded to undermine this requirement, engaging in aggressive, misleading marketing tactics aimed at deceiving the most frequent overdrafters into opting in.¹⁷ CRL's data show that, even following implementation of the "opt-in" rule, a large portion of overdraft fees are triggered by debit card transactions,¹⁸ and the Bureau's data show that the debit card transactions that trigger overdraft fees average far less than size of the fee itself.¹⁹

¹⁵ CRL's estimates of annual overdraft fees (not including non-sufficient funds fees) have been \$10 billion in 2004; \$17.5 billion in 2006; \$23.7 billion in 2008; \$16.7 billion in 2011. Rebecca Borné & Peter Smith, *The State of Lending in America & Its Impact on U.S. Households: High-Cost Overdraft Fees*, Center for Responsible Lending (July 2013), available at <http://www.responsiblelending.org/state-of-lending/overdrafts/> [CRL *State of Lending*]. Even conservatively assuming no increase in annual overdraft fees until a new annual estimate was derived, and not including any fees for 2012-2014, these estimates indicate \$142.8 billion in fees charged from 2004-2011 alone.

¹⁶ As recently as 2004, 80 percent of financial institutions declined debit card transactions that would have overdrawn a customer's account. Mark Fusaro, *Are "Bounced Checks" Really Loans?* (2007), available at <http://personal.ecu.edu/fusarom/fusarobpintentional>. As the Bureau's proposal discusses, overdraft programs began as ad hoc courtesy to prevent a paper check from bouncing. They later morphed into highly automated programs and were extended to debit card transactions. 79 Fed. Reg. 77118-19. But there is no non-sufficient funds fee on a declined debit card transaction, no merchant fee to the customer. There is also very little cost to the bank. (The CFPB's 2013 white paper noted that its study banks reported that charge-offs were the largest cost to banks of overdraft programs but that even those costs were relatively small compared to the revenue earned from the programs. CFPB, *CFPB Study of Overdraft Programs: A white paper of initial data findings at 19* (June 2013), available at http://files.consumerfinance.gov/f/201306_cfpb_whitepaper_overdraft-practices.pdf [CFPB *White Paper*]).

¹⁷ See note 14, *supra*.

¹⁸ CRL *State of Lending* at 5.

¹⁹ CFPB, *CFPB Data Point: Checking account overdraft* at 18 (July 2014), available at http://files.consumerfinance.gov/f/201403_cfpb_report_payday-lending.pdf [CFPB *Data Point*] (finding median

Financial institutions also have a history of manipulating transaction posting order, posting larger transactions first to deplete the account more quickly and thus maximize the number of overdraft fees charged. This practice continues today despite (1) many multi-million dollar settlements in lawsuits addressing this practice; (2) near universal recognition that there is no reason to post debit card transactions, which are “must-pay” items once they are authorized, in order from highest-to-lowest except to increase overdraft fees; and (3) regulatory guidance from the FDIC advising its supervisee banks not to post transactions in order from largest to smallest.

Banks also target university, and even high school, students with accounts that charge high and frequent overdraft fees, including on non-recurring debit card and ATM transactions.²⁰ One large bank’s high school checking account, for example, charges overdraft fees on non-recurring debit card and ATM transactions even as it requires that the account be linked to a parent or guardian’s checking account at the same bank. It would seem the bank could access that parent or guardian’s account if it wishes to cover overdrafts rather than charging a high school student \$34 per overdraft.²¹

These practices continue despite some regulatory efforts to rein them in. The FDIC’s 2010 guidance advised that charging more than six overdraft fees within a twelve-month period was excessive.²² But CRL’s analysis of 2011 checking account data found that two-thirds of overdraft fees – post-implementation of the opt-in rule – were charged to account holders paying more than six fees per year.²³ Similarly, the Bureau found that the 8% of account holders charged more than 10 fees per year pay 75% of overdraft fees.²⁴

Those incurring the large majority of overdraft fees – the individuals financial institutions target²⁵ – clearly cannot afford them. For those customers, overdraft fees leave them worse off and ultimately less able to make important payments than they would have been with no overdraft coverage at all. The following graph shows two months of actual checking account activity, including all overdraft fees charged, for one panelist (whom we call Mary) from our

debit card transaction triggering an overdraft was \$24). This is far less than the \$34 median overdraft fee among large banks. *CFPB White Paper* at 52.

²⁰ See Consumers Union, *Campus Banking Products: College Students Face Hurdles to Accessing Clear Information and Accounts that Meet Their Needs* (Aug. 2014), available at https://consumersunion.org/wp-content/uploads/2014/08/Campus_banking_products_report.pdf.

²¹ See https://www.chase.com/content/dam/chasecom/en/checking/documents/clear_simple_guide_highschool.pdf.

²² Federal Deposit Insurance Corporation, Supervisory Guidance for Overdraft Protection Programs and Consumer Protection, FIL-81-2010 (Nov. 24, 2010).

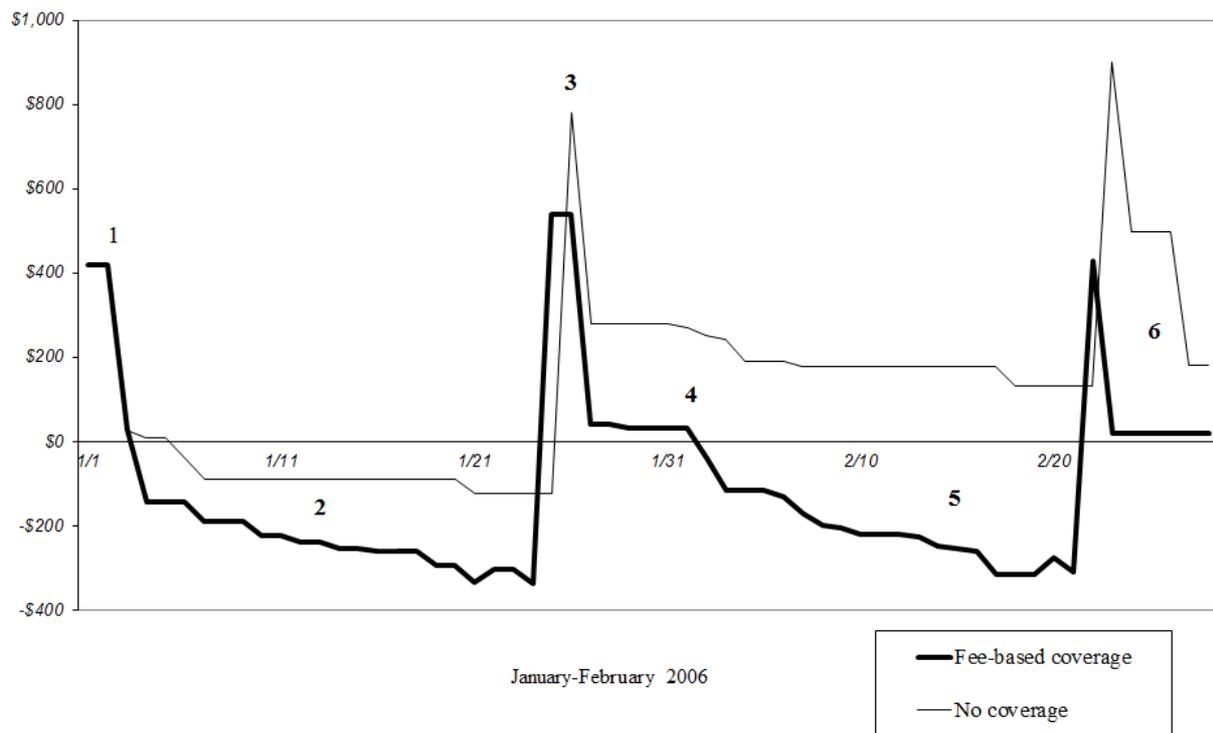
²³ CRL *State of Lending* at 12.

²⁴ *CFPB Data Point* at 11.

²⁵ See Leslie Parrish, *Banks Target, Mislead Consumers As Overdraft Deadline Nears*, Center for Responsible Lending at 3 (Aug. 5, 2010), available at <http://www.responsiblelending.org/overdraft-loans/research-analysis/Banks-Target-And-Mislead-Consumers-As-Overdraft-Dateline-Nears.pdf>.

database.²⁶ The graph also shows what Mary’s activity would have been with no overdraft coverage at all. Mary is an older American, entirely dependent on Social Security for her income.

Mary’s Balance: A Real-life Case Study



- 1 – 1/3 – Early-month expenses take Mary into overdraft.
- 2 – 1/9-20 – “No overdraft program” balance is constant here, while balance with overdraft accumulates daily fees, forcing a utility bill to be rejected on 1/20.
- 3 – 1/25 – Social Security check brings Mary out of overdraft.

- 4 – 2/2 – Accumulated fees from January force Mary back into overdraft; with no overdraft program, she would have maintained a positive balance.
- 5 – Daily fees mount again, forcing the rejection of another month’s utility bill.
- 6 – By the end of February, Mary has only \$18.48 in her account. She would have about \$200 with no overdraft program.

With fee-based overdraft, Mary ended up having two utility bills rejected anyway and ended up with only \$18.48 at the end of two months. With no overdraft program at all, she would have been better off than she was with fee-based overdraft. Five of her transactions, totaling \$242, would have been declined—two point-of-sale transactions and three electronic transactions. She would have been charged no fee for the two point-of-sale transactions. She may have been charged an insufficient funds (NSF) fee and a merchant fee (for a returned transaction) for each of the three declined electronic transactions. She also may have been charged late fees if any of

²⁶ CRL analyzed 18 months of bank account transactions, from January 2005 to June 2006, from participants in Lightspeed Research’s Ultimate Consumer Panel. For further discussion of this database, see Eric Halperin & Peter Smith, *Out of Balance: Consumers Pay \$17.5 Billion Per Year in Fees for Abusive Overdraft Loans* at 9, 13 (July 2007), available at <http://www.responsiblelending.org/overdraft-loans/research-analysis/out-of-balance-report-7-10-final.pdf>.

the electronic transactions were bills. Even if Mary had been charged an NSF fee, a merchant fee, and a late fee for each of the three electronic transactions, her ending balance, *after* payment of the declined transactions, would have been approximately \$200, far higher than the \$18.48 left in her account with fee-based overdraft.

Mary's situation illustrates a problem common among the account holders who pay the majority of the fees. Not only do overdraft programs fail to assess a borrower's ability to repay without having to re-borrow shortly thereafter, but overdraft loans are structured in a way likely to lead to repeat overdrafts by those least able to afford them. Over time, the repeated fees strip away consumers' cash assets, leaving them financially worse off than when they first overdrafted and unable to meet obligations they otherwise could have met even with no overdraft coverage at all. Former FDIC Chair Sheila Bair has noted that “[r]epet use of fee-based overdraft protection doesn't make sense for anyone.”²⁷

Ultimately, and particularly important in the context of prepaid cards, a significant portion of consumers paying large numbers of fees end up without bank accounts. Overdraft fees have been found to be the leading cause of involuntary bank closures.²⁸ The CFPB found that consumers whose debit cards could trigger overdraft fees were more than 2.5 times more likely to have their accounts involuntarily closed than those who were not “opted in” to debit card overdraft fees at several study banks.²⁹ As the Bureau's proposal notes, one study found that a full 41 percent of prepaid card users who had ever had a checking account either closed their account or had an account closed by the institution because of overdraft or bounced check fees.³⁰

As civil rights leaders have noted, overdraft fees “increase[] financial disenfranchisement”:

“Once a person is ejected from the mainstream financial system, it becomes difficult to reenter. And the unbanked and underbanked are more likely to end up with no choice except alternative financial services, which are often more expensive and less secure than a responsible mainstream checking account.”³¹

²⁷ Block, Sandra, *Bank overdraft fees: now it's up to the customer to accept*, USA Today, June 25, 2010, available at http://www.usatoday.com/money/industries/banking/2010-06-25-overdraft18_CV_N.htm.

²⁸ Dennis Campbell, Asis Martinez Jerez, and Peter Tufano, *Bouncing Out of the Banking System: An Empirical Analysis of Involuntary Bank Account Closures* at 6, (June 6, 2008), available at http://www.bostonfed.org/economic/cprc/conferences/2008/payment-choice/papers/campbell_jerez_tufano.pdf (noting that virtually all involuntary bank account closures, when the financial institution closes a consumer's account, occur because the customer overdrew the account an excessive number of times).

²⁹ CFPB White Paper 2013 at 34.

³⁰ 79 Fed. Reg. 77906 (citing The Pew Charitable Trusts, *Why Americans Use Prepaid Cards: A Survey of Cardholders' Motivations and Views*, at 7 (Feb. 2014)). Further, as the Bureau notes, Pew's survey found that 46 percent of respondents indicated that one of the major reasons they use prepaid cards is to “Avoid overdraft fees;” 51 percent of respondents said one of their major reasons is “Helping you not spend more money than you actually have.” *Id.*

³¹ Wade Henderson, President and CEO of The Leadership Conference on Civil and Human Rights, and Hilary Shelton, Washington Bureau Director for the NAACP, *Predatory Overdraft Practices Should Be Stopped*, The Hill,

V. Overdraft charges associated with prepaid cards should be prohibited.

This shameful history of overdraft programs in the checking account space – a history of targeting account holders to gain their consent, if nominal, to overdraft fees; of systematically draining them of what little resources they have; of resisting any efforts at reform despite legal and regulatory pressure – is the lens through which overdraft programs on prepaid cards should be viewed. We should not only be concerned that some issuers will take advantage of what may seem like a narrow window through which overdraft charges may be permitted, blow it wide open, and harm their customers; we should expect it.

The Bureau need look no further than its own proposed rule – its discussions of the relevant context and the defining features of both overdraft and prepaid cards – to find the bases on which it can, and should, prohibit overdraft charges on prepaid cards.

A. Prepaid cards, though increasingly similar to bank accounts in many ways, remain different from them in defining ways.

1. Prepaid cards are marketed as an account that offers consumers control and cannot be overspent.

As the Bureau notes, many prepaid cards are actively marketed as “safe” alternatives to checking accounts with overdraft.³² The Bureau cites the prepaid card trade association’s website, which notes:

“For many Americans, prepaid cards serve as a tool with which to more effectively budget their spending. With a prepaid card, consumers avoid the risk of over-spending or overdraft, thus avoiding the interest, fees and potential negative credit score implications of traditional credit cards. And for parents, prepaid cards provide tools to maintain control over their teens’ or college students’ spending.”³³

2. Prepaid cards are overwhelmingly marketed to, and largely used by, consumers who are more financially vulnerable.

As the Bureau notes, prepaid card issuers often promote their cards as requiring no credit check,³⁴ suggesting that a substantial portion of prepaid card users expect they would not qualify

Aug. 20, 2013, available at <http://thehill.com/blogs/congress-blog/economy-a-budget/317679-predatory-overdraft-practices-should-be-stopped>.

³² 79 Fed. Reg. 77111.

³³ *Id.* (citing Network Branded Prepaid Card Association’s website, *What are Prepaid Cards?* <http://www.nbpc.com/en/What-Are-Prepaid-Cards/Prepaid-Card-Benefits.aspx>).

³⁴ 79 Fed. Reg. 77210-11.

were credit checks required. Indeed, the Bureau notes that its sources have indicated that prepaid card users' average credit score is far below average.³⁵

Further, as the Bureau notes, prepaid card users are more likely than the general population to have sub-\$50,000 incomes, be young, single mothers, or disabled, and less likely to be homeowners, white, have a college degree, or be employed.³⁶ They are also often recipients of public benefits.³⁷ One study found that 84 percent of general purpose reloadable (GPR) prepaid cards had incomes below the nationwide median.³⁸

Prepaid card users are also disproportionately unbanked or underbanked.³⁹ On the same web page cited above, the prepaid card trade association notes that prepaid cards "open the doors to economic participation," stating:

"An estimated 100 million Americans are considered unbanked or underbanked. These are individuals who have no bank account or have limited or no access to credit. Many of these Americans are forced to rely on a combination of cash, money orders and pay-day loans. Network branded prepaid cards allow these Americans, many of whom are minorities, access to our increasingly card-based economy and provide an improved sense of control and empowerment."⁴⁰

3. Prepaid card customers are often those who have been harmed by overdraft fees in the past.

As the Bureau's proposal recognizes, many of the unbanked consumers using prepaid accounts were not always unbanked.⁴¹ Overdraft fees made them unbanked. As noted above, overdraft fees are the leading cause of involuntary account closures. One large survey found that 41 percent of prepaid card users who had ever had a checking account had the account closed or lost it due to overdraft fees.⁴²

³⁵ 79 Fed. Reg. 77211.

³⁶ 79 Fed. Reg. at 77106 (citing 2013 FDIC National Survey of Unbanked and Underbanked Households, Appendix at 46-47 (Oct. 2014)), available at <https://www.fdic.gov/householdsurvey/report.pdf>.

³⁷ 79 Fed. Reg. 77211.

³⁸ *Id.*

³⁹ *Id.*

⁴⁰ Network Branded Prepaid Card Association's website: <http://www.nbpca.com/en/What-Are-Prepaid-Cards/Prepaid-Card-Benefits.aspx>.

⁴¹ 79 Fed. Reg. 77111.

⁴² *Id.* (citing 2014 Pew Survey and also noting: "It appears that a desire to avoid fee-based overdraft services motivates a sizeable portion of consumers to choose prepaid products, such as GPR cards, over checking accounts . . . It also appears that many consumers specifically seek to acquire prepaid products that do not offer overdraft or credit features because they have had negative experiences with credit products, including checking accounts with overdraft features or want to avoid fees related to such products.")

And it is no coincidence that the profiles of prepaid card users discussed above closely resemble those of checking account customers who incur the large majority of fees. Indeed, two CRL surveys have found that account holders who overdraw frequently were more likely to be lower income, non-white, single, and renters when compared to the general population. Respondents reporting the most overdraft incidents were those earning below \$50,000.⁴³ In addition, the Bureau found that younger account holders were more likely to pay large numbers of overdraft fees than older ones.⁴⁴

4. Prepaid card customers often use them to avoid overdraft fees.

As the Bureau notes, many prepaid card customers use the cards to avoid overdraft fees. Citing its consumer testing, the Bureau states: “Indeed, many participants in the Bureau’s consumer testing emphasized control as a primary reason they used prepaid cards,” that they “did not want a product with overdraft services because they were afraid they would be tempted to use such a service and incur debt and fees beyond what they could control.”⁴⁵ The Bureau notes that other studies have found similar results, including that approximately three-fourths of prepaid users like that they cannot overspend on a prepaid card⁴⁶ and that the top two reasons consumers claim to use prepaid cards related to avoiding credit card debt (67 percent) and not spending more than they have (66 percent).⁴⁷

B. The Bureau’s reasoning supports prohibiting overdraft charges on prepaid cards altogether.

We support the Bureau’s refusal to extend the Regulation E opt-in regime to prepaid card transactions. We note, however, that the Bureau’s rationale in declining to extend the exemption from Regulation Z for overdraft fees on checking accounts to overdraft fees on prepaid cards should in fact compel the Bureau to prohibit overdraft charges on prepaid cards altogether.

First, the Bureau cites the purpose of TILA, including to “assure a meaningful disclosure of credit terms so that the consumer will be able to avoid the uninformed use of credit and to protect the consumer against inaccurate and unfair credit billing and credit card practices.”⁴⁸ Elsewhere the Bureau notes that TILA’s “stated purpose is tied to Congress’ finding that ‘economic stabilization would be enhanced and the competition among the various financial institutions and other firms engaged in the extension of consumer credit would be strengthened by the informed

⁴³ Leslie Parrish, Center for Responsible Lending, *Consumers Want Informed Choice on Overdraft Fees and Banking Options* (Ap. 16, 2008) [hereinafter CRL Research Brief, 2008], available at <http://www.responsiblelending.org/overdraft-loans/research-analysis/final-caravan-survey-4-16-08.pdf>

⁴⁴ CFPB Data Point 2014, at 14 (Table 4B).

⁴⁵ 77211, n.347 (internal citation omitted).

⁴⁶ 77211, n.348 (internal citations omitted).

⁴⁷ *Id.*

⁴⁸ 79 Fed. Reg. 77209.

use of credit.”⁴⁹ As we discuss in section C of this Part V below, this purpose, we believe, should compel the Bureau to prohibit overdraft charges on prepaid cards.

Second, the Bureau notes that the Board’s justification for the existing regulatory approach is “much less convincing as applied to prepaid accounts, both because the historical justification for checking account overdraft services does not apply to prepaid accounts and because there are notable differences between how prepaid accounts and checking accounts function.”⁵⁰ These, the Bureau notes, include avoiding the embarrassment and cost of bounced checks and that the program was ad hoc, neither of which is applicable in the case of an automated overdraft program on a prepaid card. But these were not only the rationale for why overdraft fees were originally exempted from Regulation Z; they were the rationale *for overdraft fees themselves*. Were there no embarrassment or cost to avoid, there would be no need for an overdraft fee, it would seem; were the overdraft fees routine and frequent rather than ad hoc and occasional, these fees would be clearly unreasonable. Thus, these factors do not so much distinguish non-credit-like overdraft from credit-like overdraft, but a rather distinguish a justification for overdraft from a lack of justification.

The Bureau continues: “[A] consumer using a prepaid account is less like the checking account customer that the Board focused on in creating the exemption for overdraft – a consumer being extended a courtesy in order to avoid potentially harsher repercussions – and instead is like any other consumer *using credit to purchase goods or services*.”⁵¹ Because prepaid cards are prepaid cards, marketed to offer control and to prevent overspending, the Bureau should not permit a prepaid card to become a credit card via overspending.

Third, the Bureau states that it believes that treating prepaid overdrafts as credit cards “would provide stronger protections that are more closely calibrated to how the industry has broadly marketed prepaid products to consumers and how consumers, in turn, expect to be able to use the products.”⁵² The Bureau then notes that financial institutions “deliberately market prepaid accounts to consumers as products that are safer and easier to use *than comparable products with credit features, in particular checking accounts with overdraft* . . . preventing overspending and the incurring of debt . . . requiring no credit checks, not reporting to credit bureaus unpaid debts (of which there are rarely any), and not including any credit features.”⁵³ The Bureau further notes that many industry commenters “repeatedly emphasized these unique features of prepaid products as a primary reason behind their growth in popularity.”⁵⁴ In addition, the Bureau notes that many consumers have chosen prepaid cards because the cards offer greater control and do

⁴⁹ 79 Fed. Reg. 77125 (internal citation omitted).

⁵⁰ 79 Fed. Reg. 77209-10.

⁵¹ 79 Fed. Reg. 77210 (emphasis added).

⁵² 79 Fed. Reg. 77210.

⁵³ *Id.*

⁵⁴ *Id.*

not typically offer overdraft services “of the same type as commonly found on checking accounts in particular.”⁵⁵

The Bureau’s proposed solution would formally make overdraft credit, but that only appropriately calls the overdraft what it is; it does not adequately address that a prepaid issuer, by imposing overdraft charges, is acting inconsistently with its pervasive representations by having the feature at all.

As the Bureau notes, “the prepaid industry has attracted a large number of both voluntary and involuntary former checking account customers who had their checking account closed. Many prepaid consumers previously had a checking account and either lost that account or gave up that account due to failure to repay debts or related issues. The Bureau believes that many of these consumers lost their checking accounts because they could not handle repeated overdraft fees Relatedly, the Bureau also believes that many of these consumers, and even many consumers who continue to maintain separate checking accounts, chose to purchase prepaid products because of their promise to allow consumers to control spending.”⁵⁶ The Bureau then cites its own consumer testing (consumers were “afraid they would be tempted to use [a credit service]) and other surveys finding three-fourths of prepaid consumers like not being able to overspend on a prepaid card and the top two reasons consumers claim to use prepaid cards related to avoiding credit card debt and not spending more than they have.

The Bureau then reasons that in order to “prevent erosion of what the Bureau believes is a clear distinction regarding overdraft services in the current market and in the minds of consumers between prepaid accounts and checking accounts that offer overdraft services, and to ensure that credit products that are associated with prepaid accounts receive consistent treatment regardless of their particular structures,”⁵⁷ the Bureau proposes to treat overdraft as an open-end credit product.

We appreciate the Bureau’s efforts to make what is permitted on cards more consistent with what is in consumers’ minds. However, it seems that the most appropriate response to the surveys the Bureau cites is to affirmatively prevent overdraft charges on a prepaid card rather than sanction them. The Bureau need not treat overdraft as consistent with other credit in all ways, in all contexts – because it is different. It is the only kind of credit exclusively triggered by overspending and, on any given transaction, potentially without intent.

Fourth, the Bureau notes that “there is evidence that a significant portion of consumers with prepaid accounts would particularly benefit from the stronger protections that Regulation Z provides,” notably to address “marketing dynamics” and because of negative overdraft experiences with checking accounts.⁵⁸ Here the Bureau notes prepaid consumers are

⁵⁵ *Id.*

⁵⁶ 79 Fed. Reg. 77211 (internal citation omitted).

⁵⁷ *Id.*

⁵⁸ *Id.*

“disproportionately unbanked or underbanked, often have limited education, and are unemployed or recipients of public benefits.”⁵⁹ The Bureau considers those prepaid users who may want to use “credit features” with their prepaid account and states that the proposal would “appropriately limit their credit exposure and reduce the risk of some of the harms that may be associated with using prepaid accounts for which an overdraft service is offered.”⁶⁰

The Bureau need not, and is not, banning any credit offered to prepaid cardholders, though it is appropriately requiring that credit only be offered subject to credit protections. But, again, overdraft is a particular kind of credit feature – it should not, in all ways, be treated consistently with other credit features, and certainly not on prepaid cards. It is distinct. It is *triggered by overspending*. The Bureau can and should do more than “reduce the risk of some of the harms.” It should – again, given the broader context – promulgate the rule that will prevent the harm.

Fifth, the Bureau notes that it “is proposing to regulate prepaid credit features on a largely blank slate,”⁶¹ in a market where very few prepaid products have overdraft or other credit features. But, the Bureau notes elsewhere that it believes additional providers may be considering credit features, “such as an overdraft service,” suggesting “there could be increased consumer access to these products in the future.”⁶² Rather than provide a regulatory framework that essentially offers a roadmap for how overdraft may be done, the Bureau should wipe the already nearly blank slate clean.

C. CFPB’s TILA and UDAAP authority should compel it to prohibit overdraft charges on prepaid cards.

As discussed in Part III above, though the proposed rule would change regulation of overdraft on prepaid cards in important ways, it nonetheless leaves potential for abusive overdraft charges and ensuing harm. TILA and UDAAP authority both support stronger rules to prevent abuses in this market.

Indeed, CFPB precedent demonstrates that in the context of subprime consumers, greater protections may be warranted. In its rules implementing the mortgages provisions of The Wall Street Reform Act, the Bureau determined that while some qualified mortgage loans should benefit from a safe harbor from ability-to-repay challenges, higher-priced mortgage loans should not, noting: “The subprime segment of the market is comprised of borrowers who tend to be less sophisticated and who have fewer options available to them, and thus are more susceptible to being victimized by predatory lending practices. The historical performance of subprime loans bears all this out. The Bureau concludes, therefore, that for subprime loans there is reason to impose heightened standards to protect consumers”⁶³

⁵⁹ 79 Fed. Reg. 77211 (internal citations omitted).

⁶⁰ 79 Fed. Reg. 77212.

⁶¹ *Id.*

⁶² 79 Fed. Reg. 77258.

⁶³ 74 Fed. Reg. 6511 (internal citations omitted). The Bureau also noted: “The Bureau believes that loans that fall within the rebuttable presumption category will be loans made to consumers who are more likely to be vulnerable

Both TILA and the Bureau's UDAAP authority should compel it to keep overdraft charges off of prepaid cards.

1. The Truth in Lending Act provides ample authority to prohibit overdraft charges on prepaid cards.

In its proposal, the Bureau notes the following regarding its authority under TILA (all emphases added):

TILA section 105(a). As amended by the Dodd-Frank Act, TILA section 105(a), 15 U.S.C. 1604(a), directs the Bureau to prescribe regulations to carry out the purposes of TILA, and provides that such **regulations may contain additional requirements**, classifications, differentiations, or other provisions, and may provide for such adjustments and exceptions for all or any class of transactions, that the Bureau judges are necessary or proper to effectuate the purposes of TILA, to prevent circumvention or evasion thereof, or to facilitate compliance. As discussed above, pursuant to TILA section 102(a), a purpose of TILA is “to assure a meaningful disclosure of credit terms so that the consumer will be able to compare more readily the various credit terms available to him **and avoid the uninformed use of credit.**” Moreover, this stated purpose is tied to Congress’ finding that “economic stabilization would be enhanced and the competition among the various financial institutions and other firms engaged in the extension of consumer credit would be strengthened by the informed use of credit[.]” TILA section 102(a). Thus, strengthened competition among financial institutions is a goal of TILA, achieved through the effectuation of TILA’s purposes.

Historically, TILA section 105(a) has served as a broad source of authority for **rules that promote the informed use of credit through** required disclosures and **substantive regulation** of certain practices. However, Dodd-Frank Act section 1100A clarified the Bureau’s section 105(a) authority by amending that section to **provide express authority to prescribe regulations that contain “additional requirements” that the Bureau finds are necessary or proper to effectuate the purposes of TILA, to prevent circumvention or evasion thereof, or to facilitate compliance.** This amendment clarified the authority to exercise TILA section 105(a) to **prescribe requirements beyond those specifically listed in the statute** that meet the standards outlined in section 105(a). Accordingly, as amended by the Dodd-Frank Act, TILA section 105(a) authority to make adjustments and exceptions to the requirements of TILA applies to all transactions subject to TILA, except [high-cost mortgages].

For the reasons discussed in this notice, the Bureau is proposing amendments to Regulation Z with respect to certain prepaid accounts that are associated with overdraft services or credit features to carry out TILA’s purposes and is proposing such **additional**

[fn cites 2008 FRB rule discussion along similar lines] so that, even if the loans satisfy the criteria for a qualified mortgage, those consumers should be provided the opportunity to prove that, in an individual case, the creditor did not have a reasonable belief that the loan would be affordable for that consumer.” 74 Fed. Reg. 6506.

requirements, adjustments, and exceptions as, in the Bureau’s judgment, are necessary and proper to carry out the purposes of TILA, prevent circumvention or evasion thereof, or to facilitate compliance. In developing these aspects of the proposal pursuant to its authority under TILA section 105(a), the Bureau has considered the purposes of TILA, including ensuring meaningful disclosures, **facilitating consumers’ ability to compare credit terms, and helping consumers avoid the uninformed use of credit,** and the findings of TILA, including strengthening competition among financial institutions and promoting economic stabilization.⁶⁴

In light of the context the Bureau provides above, it is clear that the Bureau’s “additional requirements” authority is extremely broad. (In its current proposal, the Bureau uses this authority to propose a 30-day gap between the registration of a card and solicitation for overdraft or other credit. We urge below that, should the Bureau keep the Regulation Z framework for overdraft, it lengthen this period to at least 90 days. The Bureau also proposes that repayment of credit associated with prepaid cards be required no more frequently than monthly.)

On any given transaction, overdraft may be an uninformed use of credit because, on any given transaction, the consumer may not know the consumer is using credit. On a prepaid card, where consumers typically not only do not expect to overdraft but often have the card *so that they will not*, this is only more true. Overdrafting on a prepaid card is thus strikingly different from using credit on, say, a traditional credit card, where consumers are clearly expecting to access credit and fully know, on every transaction, that they are doing so. TILA’s purposes include enabling consumers to decide between using credit and delaying consumption;⁶⁵ permitting overdraft charges on prepaid cards run directly counter to that purpose, particularly given that prepaid cards are largely marketed and used as a means to control spending.

The Bureau’s “additional requirements” authority may be used not only to further TILA’s purposes but to prevent evasion or circumvention of those purposes. Overdraft as we have known it is a creature of evasion. As one looks at the current prepaid card market, where a relatively small portion of cards have overdraft fees, it may seem as though greater protections than what CFPB has proposed are not needed. But the current prepaid market is not tomorrow’s prepaid market. As the prepaid card industry continues to grow and continues, as the Bureau notes, to be used by consumers seeking lower cost services, many of whom will continue to be more financially vulnerable than the population at large,⁶⁶ the CFPB should prohibit overdrafts

⁶⁴ 79 Fed. Reg. 77125 (emphases added).

⁶⁵ In connection with 1981 proposed comprehensive revisions to Regulation Z, the FRB prepared a “Regulatory Analysis of Proposed Revision of Regulation Z.” See Proposed Rule, Credit; Truth in Lending; Revision of Regulation Z, 46 Fed. Reg. 80648, 80731 (Dec. 5, 1980). This analysis included a table entitled “Goals of Truth in Lending” listing 39 TILA goals, which included seven “Goals Associated with Improving Consumer Decisionmaking.” These seven goals were to reduce credit search costs; simplify information processing; improve consumers’ ability to make comparisons; enable consumers to match products and needs; enable consumers to decide between using credit and delaying consumption; and show consumers where search can be beneficial. See *id.* at 80735.

⁶⁶ 79 Fed. Reg. 77211 (noting that it is likely that prepaid cards will continue to attract consumers who are new to the financial system).

charges on prepaid cards to prevent evasions of TILA’s purposes – particularly evasions that, based on the context underpinning the Bureau’s entire proposal, should be expected.

2. Overdraft charges on prepaid cards are unfair, deceptive, and abusive.

In addition to having authority under TILA to promote informed, conscious use of credit and prevent evasions of TILA’s purposes, CFPB’s UDAAP authority should also compel it to prohibit overdraft charges on prepaid cards.⁶⁷ Importantly, CFPB’s UDAAP authority includes rulemaking requirements aimed to *prevent* unfair, deceptive, and abusive acts and practices. And context, again, is critical. This context is the intersection of prepaid cards and overdraft – an intersection where we would expect to find the most vulnerable users of each. Precedent in the unfairness and deception contexts, and statutory language in the abusive context, make clear that the vulnerability of the potentially harmed consumer is a significant factor. The Bureau should thus use its UDAAP authority to prohibit overdraft charges on prepaid cards.

a. Overdraft charges on prepaid cards are unfair.

i. Significant harm

There is no question that overdraft fees, particularly for consumers with less means, cause substantial injury in the checking account space. In the prepaid card space as well, overdraft programs are currently designed in a manner likely to cause substantial harm to consumers struggling to maintain a positive balance.

On its general purpose reloadable (GPR) card, NetSpend charges up to three \$15 overdraft fees per month with a maximum negative balance of \$100, which includes any overdraft fees.⁶⁸ The program requires a direct deposit of only \$200 monthly to qualify.⁶⁹ NetSpend claims that its overdraft program is “responsible,” limiting fees as noted, providing a \$10 overdraft cushion and a 24-hour-grace period before a fee is imposed, and “cooling off” a customer for one month once the customer incurs \$180 in fees within a 12-month period. But it also reports that overdrafts are primarily used to meet recurring expenses rather than for one-time emergencies.⁷⁰ Where a consumer is routinely struggling to make ends meet, any “free” overdrafts the issuer extends often will not prevent the consumer from ultimately incurring \$45 in overdraft fees in a single month – a very substantial sum for a lower income consumer.

Other prepaid card programs are even harsher. NetSpend’s payroll card, Skylight, charges up to five \$25 overdraft fees per month, with a maximum negative balance of \$125, and up to \$450

⁶⁷ See 12 U.S.C. § 5531(b) (CFPB “may include requirements for the purpose of preventing such acts or practices.”)

⁶⁸ See <https://www.netspend.com/account/overdraftTerms.m>.

⁶⁹ *Id.*

⁷⁰ NetSpend has stated that most overdrafts are used for routine expenses. See Comments of the National Consumer Law Center (on behalf of its low-income clients) submitted to this Docket.

before a customer is “cooled off” for one month.⁷¹ Another payroll card, ReadyFUND\$, charges \$35 overdraft fees, up to two per month and 12 per year.⁷² Many workers being paid on this card likely earn the minimum wage;⁷³ as NCLC has noted, they would have to work three hours to recoup the value of a single overdraft fee. At another payroll company, the New York Attorney General found that the card manager’s accounts averaged \$77 per year in overdraft fees, including those accounts not “opted-in” to overdraft fees, which thus incurred none.⁷⁴

As noted above, even with the proposed limitations in place, prepaid card users may be targeted with overdraft features carrying these harmful characteristics: credit they do not intend to access, credit triggered only by overspending, back-end fees they cannot afford, lack of ability to repay, very high costs, repaid via balloon repayment.

ii. Harm not reasonably avoidable

The harm caused by overdraft on prepaid cards will not be reasonably avoidable for many vulnerable consumers incurring these fees. Though we appreciate the Bureau’s efforts to require that any overdraft function on prepaid cards be disclosed, disclosure does not sufficiently reduce risk of substantial harm, particularly in the context of economically vulnerable consumers like those typically targeted by overdraft programs.

There is ample precedent for finding that harm is not reasonably avoidable, even despite disclosure, based on the economic vulnerability of the targeted consumer. In 2009, when the Federal Reserve Board (the Board) limited upfront security deposit and fees on credit cards (in a precursor to the Credit CARD Act), it noted that subprime cards are typically targeted to “vulnerable consumers” without other credit options and cited the Credit Practices Rule’s suggestion that when nearly all of the credit offers received by a consumer have the same terms, they may not be reasonably avoidable.⁷⁵ In prohibiting raising interest rates on existing balances, the Board cited several sources indicating that loss of income, illness, or other factors outside the consumer’s control lead to delinquency.⁷⁶ In prohibiting as unfair payment allocation methods

⁷¹ See Comments of the National Consumer Law Center (on behalf of its low-income clients) submitted to this Docket.

⁷² See <http://www.readyfunds.net/assets/PDFs/ReadyFund-ODP-9.5.14.pdf>.

⁷³ See <http://www.readyfunds.net/partners/> (partners including McDonald’s and home health companies).

⁷⁴ Office of New York State Attorney General Eric T. Schneiderman, “Pinched by Plastic: The Impact of Payroll Cards on Low-Wage Workers” at 9 (June 12, 2014), available at <http://www.ag.ny.gov/pdfs/Pinched%20by%20Plastic.pdf>.

⁷⁵ Federal Reserve System, Dept. of Treasury--Office of Thrift Supervision, and National Credit Union Administration, Unfair and Deceptive Acts and Practices, Final Rule (Jan. 29, 2009) [2009 Credit Card UDAP Rule], 74 Fed. Reg. 5498, 5539 (“If 80 percent of creditors include a certain clause in their contracts, for example, even the consumer who examines contract[s] from three different sellers has a less than even chance of finding a contract without the clause.”).

⁷⁶ 2009 Credit Card UDAP Rule, 74 Fed. Reg. 5523. The Board cites the FTC Credit Practices Rule, which found “the majority [of defaults] are not reasonably avoidable by consumers” because of factors such as loss of income or illness; Bank of America testimony noting that falling behind on an account is likely due to circumstances outside

that were unfavorable to the consumer, the Board noted that “[a]lthough a consumer could avoid the injury by paying the balance in full every month, this may not be a reasonable expectation as many consumers are unable to do so.”⁷⁷

In 2010, in the OTS’s proposed guidance addressing overdraft practices, the agency noted that the harm caused by overdraft, particularly for those who overdraft frequently, may not be reasonably avoidable, even when it is not deceptively promoted: “Regardless of how overdraft protection is promoted, those who frequently overdraw accounts may simply not have other options in the market, as they may have credit histories and other characteristics that prevent them from obtaining less expensive services . . . when fees become excessive, consumers may have difficulty both repaying overdrafts and bringing accounts current, which may cause them to incur additional fees.”⁷⁸

In the mortgage context, in finding that harm caused by stripped equity from loan flipping was not reasonably avoidable, the Board noted the following potential factors:

- “borrowers’ own assessment of their repayment ability may be influenced by their belief that a lender would not provide credit to a consumer who did not have the capacity to repay.”⁷⁹
- even if the borrower considered the disclosures, urgently needing the cash for a household emergency;⁸⁰
- reasonably believing a more affordable loan may not be available.⁸¹

Case law also supports that a key factor in whether harm is reasonably avoidable is whether the consumer has reason to anticipate the harm.⁸² There are several reasons that a prepaid card

the customer’s control; and an economic journal finding conclusive evidence that unemployment is critical in determining delinquency. The Board acknowledged that the injury resulting from increases in the annual percentage rate “may be avoidable by some consumers under certain circumstances,” but it nonetheless concluded that “consumers cannot, as a general matter, reasonably avoid interest rate increases on existing balances.” 74 Fed. Reg. 5522.

⁷⁷ 2009 UDAP Credit Card Rule, 74 Fed. Reg. 5515.

⁷⁸ OTS, Supplemental Guidance on Overdraft Protection Programs, Docket ID OTS-2010-0008, 75 Fed. Reg. 22683, 22688 (Apr. 29, 2010). This guidance was never finalized, as the OTS was soon thereafter merged into the OCC.

⁷⁹ 74 Fed. Reg. 44542. The FRB continues: “Borrowers could reasonably infer from a lender’s approval of their applications that the lender had appropriately determined that they would be able to repay their loans. Borrowers operating under this impression may not independently assess their repayment ability to the extent necessary to protect themselves from taking on obligations they cannot repay.” *Id.*

⁸⁰ *Id.*

⁸¹ *Id.*

⁸² See, e.g., *National Ass’n of Mortgage Brokers v. Board of Governors*, 773 F. Supp. 2d 151 (D.D.C. 2011) (upholding the FRB’s finding that harm from mortgage yield-spread premiums was not reasonably avoidable, affirming the Board’s reasoning that the record showed that consumers were generally not aware of YSPs and that some borrowers reasonably expected brokers to be their trusted agents); two negative amortization mortgage cases: *Jordan v. Paul Fin. LLC* 745 F. Supp 2d 1084, 1100 (N.D. Cal. 2010) (refusing to dismiss claim that consumers

holder would not anticipate the harm caused by overdraft fees on prepaid cards. First, it would be abundantly reasonable for one to believe, even despite improved disclosures and consent requirements, that a prepaid card cannot be overdrawn. Second, overdraft fees are always back-end fees, triggered only by overspending the consumer may not be aware is occurring. Third, as behavioral economics has demonstrated and as the Board considered in its promulgation of the opt-in rule, consumers may be overly optimistic about their ability to avoiding overdrafting.⁸³ This is particularly important in the context of overdraft, where any consent is typically temporally disjoined from usage of the product, and where that use is often inadvertent. Fourth, consumers may not understand the cycle that may ensue, with the overdraft and associated charges creating a gap in the next month's pay and a need to overdraft again to make up that gap. And fifth, consumers may believe the prepaid card issuer would not authorize an overdraft the borrower cannot afford to repay. (As discussed in Section VI.D.1 below, the Credit CARD Act's provisions are not strong enough to ensure ability to repay among issuers eager to prey upon vulnerable consumers.)

Case law also indicates that the appropriate inquiry is whether a consumer could have *reasonably* avoided the injury, not whether it was *merely possible* for the consumer to avoid the injury.⁸⁴ Relatedly, the appropriate standard is a reasonable consumer, not a perfect consumer. The FTC deception standard explicitly requires consideration of the perspective of a "reasonable" consumer.⁸⁵ While the FTC does not appear to explicitly apply this to the unfairness standard, it follows that the same is true for this standard, particularly in light of the standard's language that the harm must be "reasonably avoidable." In addition, behavioral economics has indicated not only that consumers are not perfect or perfectly rational, but they often act in "irrational" ways

could not have reasonably avoided negative amortization); *Peel v. BrooksAmerica Mortgage Corp.*, 788 F. Supp. 2d 1149 (C.D. Ca 2011) ((denying motion to dismiss with similar reasoning); *Orkin Exterminating Co. v. Fed. Trade Comm'n*, 849 F.2d 1354, 1365 (11th Cir. 1988) (Orkin had offered lifetime guarantees to customers upon paying an annual fee each year stated in the original contract; it later raised the amount of that fee on existing customers. Courts upheld FTC's unfairness findings; the appellate court reiterated the FTC's reasoning from its order against Orkin: "Consumers may act to avoid injury before it occurs if they have reason to anticipate the impending harm and the means to avoid it. . . .").

⁸³ The FRB noted this concept, "hyperbolic discounting," in the context of its overdraft "opt-in" rule, 74 Fed. Reg. 59044 (Nov. 17, 2009) (citing, e.g. Shane Frederick, *et al.*, Time Discounting and Time Preference: A Critical Review, 40 J. Econ. Literature 351, 366–67 (2002) (reviewing the literature on hyperbolic discounting).

⁸⁴ *Jordan v. Paul Fin. LLC*, 745 F. Supp 2d 1084, 1100 (N.D. Cal. 2010) (refusing to dismiss unfairness claim, applying FTC 3-prong test to CA unfair competition law, of contract terms of payment option ARM with negative amortization, reasoning that while a sophisticated consumer might have reasoned from the loan documents that, at the teaser rate, negative amortization would indeed occur (rather than "could" occur, as the loan doc disclosed), "the fact that Defendant may have provided a technically accurate disclosure does not excuse the potentially inadequate or misleading character of other disclosures it provided or lessen the resulting potential for confusion" (internal cite omitted, emphasis added). Therefore, at issue is whether plaintiffs' allegations establish that they could have *reasonably avoided* the injury, not whether it was merely possible to avoid the injury"; *Peel v. BrooksAmerica Mortgage Corp.*, 788 F. Supp. 2d 1149 (C.D. Ca 2011) (similar case, noting the *Jordan* logic was persuasive and repeating it in reaching same conclusion).

⁸⁵ FTC Policy Statement on Deception, Oct. 14, 1983.

that are in fact predictable and expected.⁸⁶ Case law also supports that the standard is for a non-sophisticated consumer.⁸⁷

Finally, the FTC's 1980 Policy Statement on Unfairness discusses unfairness in the context of exercising undue influence over highly susceptible classes of purchasers, as by promoting fraudulent "cures" to seriously ill cancer patients.⁸⁸ In a case the FTC cites, "the special susceptibilities" of such patients were one reason for banning ads entirely rather than relying on the remedy of fuller disclosure.⁸⁹ This should be particularly true when a susceptible class is the same class that is targeted by a product, as has been the case with overdraft programs.⁹⁰ Notably, the FTC also contemplates that if "reasonably avoidable" is viewed narrowly enough, all injury can be avoided: "In some senses any injury can be avoided – for example, by hiring independent experts to test all products in advance, or by private legal actions for damages – but these courses may be too expensive to be practicable for individual consumers to pursue."⁹¹ This narrow reading, which the FTC rejects, may be likened to expecting a consumer never to obtain a prepaid card in the first place.

iii. Harm not outweighed by benefits to consumers or competition

Any benefit that may be derived by any relatively small portion of consumers who would like to be able to overdraw with their prepaid card is far outweighed by the harm it can cause to the targeted consumers most likely to incur overdraft charges on a prepaid card. Further, overdraft is notoriously anti-competitive, facilitating upfront "free checking" that is far from free for those customers paying most checking account fees through back-end overdraft fees.⁹² Prohibiting overdraft charges on prepaid cards would level the playing field so that issuers who desire to keep overdraft off of prepaid cards, and, consequently, have upfront pricing that reflects a lack of overdraft revenue, could more easily do so.

b. Overdraft charges on prepaid cards are deceptive.

⁸⁶ National Consumer Law Center, *Unfair and Deceptive Acts and Practices*, § 4.3.2.3.2 (citing, e.g., Dan Ariely, *Predictably Irrational: The Hidden Forces that Shape our Decisions* (HarperCollins 2008)).

⁸⁷ *Jordan v. Paul Fin. LLC*, 745 F. Supp 2d 1084, 1100 (N.D. Cal. 2010), *supra* note 84.

⁸⁸ FTC Policy Statement on Unfairness (Dec. 17, 1980).

⁸⁹ The FTC cites *Travel King, Inc.*, 86 F.T.C. 715, 774 (1975), *available here*: http://www.ftc.gov/sites/default/files/documents/commission_decision_volumes/volume-86/ftc_volume_decision_86_july_-_december_1975pages_715-825.pdf. This case involved the luring of ill people to the Philippines for "psychic healing."

⁹⁰ *See* Part IV, above.

⁹¹ FTC Policy Statement on Unfairness (Dec. 17, 1980).

⁹² 79 Fed. Reg. 77118.

As the CFPB’s Examination Manual notes, whether something is deceptive depends on “the context of the entire . . . course of dealing” and “the overall net impression.”⁹³ It further states: “Acts or practices that may be deceptive include . . . offering to provide a product or service that is not in fact available . . . [and] using bait-and-switch techniques.”⁹⁴

Overdraft on prepaid cards is both of these: The offered product, the prepaid card, is not in fact available because it is not prepaid, and routinely allowing a card originally offered as a prepaid card to overdraw is a bait-and-switch technique.

Further, the Bureau’s manual states that when practices “target a specific audience, such as . . . financially distressed consumers,” the relevant point of view is that of a “reasonable member of that group.”⁹⁵ In the prepaid card context, that group includes the many consumers the Bureau believes are selecting prepaid cards to control overspending or who have lost checking accounts due to overdraft. Many of these consumers would be the targeted audience of overdraft programs on prepaid cards, yet many of these individuals reasonably believe that there is no overdraft capability on a prepaid card⁹⁶ or that minimal protections like a 24-hour grace period will enable them to avoid overdraft charges.⁹⁷

c. Overdraft charges on prepaid cards are abusive.

Overdraft charges on prepaid cards are also abusive. They materially interfere with a consumer’s ability to understand what a prepaid card is. They take unreasonable advantage of consumers’ lack of understanding of the risks and costs of a prepaid card, which should not include overdraft charges; of the inability of a consumer to protect the interests of the consumer to obtain a product which indeed does not permit overspending; and the reasonable reliance by the consumer on the prepaid issuer that representations that this is a “safe” product that helps control overspending are legitimate.

VI. Short of prohibiting overdraft charges associated with prepaid card accounts, the CFPB should retain the general Regulation Z framework it has proposed but must strengthen it to better prevent unfair, deceptive, and abusive acts and practices.

Again, we thank the Bureau for refusing to extend the exemption from Regulation Z and the failed opt-in regime to prepaid cards. As the Bureau has concluded based on the extensive research it has done, the concerns the FDIC identified in 2008 based on data collected long before opt-in continue to persist now: “there remains a small but significant segment of

⁹³ CFPB Examination Manual v.2 (Oct. 2012), at UDAAP 5-6. *See also* FTC Policy Statement on Deception at 3 (“When evaluating the reasonableness of an interpretation, the FTC considers the sophistication and understanding of consumers in the group to whom the act or practice is targeted.”)

⁹⁴ *Id.*

⁹⁵ *Id.*

⁹⁶ 79 Fed. Reg. 77211.

⁹⁷ For many consumers routinely struggling to meet expenses, a 24-hour grace period will not allow them to avoid overdraft charges.

consumers at the banks participating in this study who continue to incur a large number of overdraft and NSF fees. These consumers are paying substantial sums to access this instant liquidity and maintain their checking accounts. Accounts with more moderate overdraft use may also pay hundreds of dollars in fees per year.”⁹⁸ It is clear that opt-in has not curbed consumer harm in the checking account arena, and given the targeting of those incurring the most fees that has occurred in that arena, it would be even less effective in the prepaid card arena.

If the CFPB decides to affirmatively permit overdraft charges on prepaid cards, it should indeed refuse to extend the exemption afforded overdraft on checking accounts to prepaid cards, and subject the cards to the card-related protections under Regulation Z. However, given the context discussed throughout this comment, even greater protections are necessary in order for the Bureau to *prevent* unfair, deceptive, and abusive practices.

Here, we discuss the key substantive overdraft-related provisions proposed and the manner in which we believe they must be strengthened in order to prevent abuses.

A. If the Bureau permits overdraft on prepaid cards, we support treating the fee as a finance charge under Regulation Z.

As the Bureau notes, Regulation Z generally defines “creditor” to be a person who regularly extends consumer credit that is subject to a finance charge or is payable by written agreement in more than four installments. The fee has been excluded from the definition of finance charge by virtue of the Board’s exclusion for “charges imposed by a financial institution for paying items that overdraw an account, unless the payment of such items and the imposition of the charge were previously agreed upon in writing.”⁹⁹ Thus, the Board created an exemption for overdraft with deposit accounts if the financial institution does not agree in writing to pay the items and does not structure the repayment of the credit by written agreement in more than four installments.¹⁰⁰

There is no question that overdraft is credit, as the Bureau recognizes and as has been recognized by the banking regulators for many years.¹⁰¹ As the Bureau notes, the statutory language does not exempt overdraft from TILA’s definition of “credit” or the fee from the definition of finance charge – “the sum of all charges, payable directly or indirectly by the person to whom the credit is extended, and imposed directly or indirectly by the creditor as an incident to the extension of credit.”¹⁰² Thus, we agree with the Bureau’s determination that charges levied for overdraft, such as “interest charges, transaction charges, service charges, and annual or other periodic charges to participate in the credit program” generally represent finance charges,¹⁰³ and we

⁹⁸ CFPB White Paper 2013 at 61.

⁹⁹ 79 Fed. Reg. 77206.

¹⁰⁰ *Id.*

¹⁰¹ *See, e.g.*, 2005 Joint Guidance on Overdraft Programs, 70 Fed. Reg. 9129 (“When overdrafts are paid, credit is extended.”)

¹⁰² 79 Fed. Reg. 77206.

¹⁰³ *Id.*

appreciate the Bureau’s statement that “overdraft service fees and charges on other credit features easily meet the general definition of finance charge.”¹⁰⁴

As discussed earlier, the exemption simply has no place with automated overdraft programs, and particularly not on debit cards. We further note that given the addition of Regulation E’s opt-in, the notion that there is not a written agreement whereby the institution agrees to pay the overdrafts is a fiction. In the language of the deception standard, surely many consumers are left with the “overall net impression” that they, as many marketing materials go so far as to say, are “covered.”¹⁰⁵ As the Bureau notes in its discussion of whether a “plan,” or contractual arrangement, exists in the context of an “open-end credit plan,” “simply labeling an overdraft service as discretionary is insufficient to negate the existence of a credit plan.”¹⁰⁶

B. A prepaid card with an overdraft feature would be appropriately deemed an open-end credit plan under the CARD Act.

We agree with the Bureau’s determination that overdraft programs are an open-end credit plan. First, they are a plan, even if, as the Bureau notes, the lender reserves discretion not to pay overdrafts. As the Bureau notes, “In practice, the Bureau believes that this discretion is typically limited; automated overdraft systems for prepaid accounts are typically programmed to approve all would-be overdrafts that are within a predetermined credit limit.”¹⁰⁷ We appreciate the Bureau’s noting that this is no different from credit card issuers’ standard practice of reserving discretion to decline a transaction without notice, even if a transaction is within a credit limit.¹⁰⁸

Next, with respect to the three prongs defining open-end credit, first, the creditor clearly contemplates repeat transactions. As the Bureau notes, this is particularly true when overdraft programs are automated.¹⁰⁹ We note that it is also true even were a prepaid issuer or financial institution to claim that the program is only for use as an occasional courtesy or limit the number of times it can be used. Second, the creditor may impose a finance charge from time to time on the outstanding balance, and there is no specific amount financed for the plan which may be calculated in advance. And third, the credit line, though it need not be specific or always be replenished to its original amount, will generally replenish to the extent that any outstanding balance is repaid.

¹⁰⁴ 79 Fed. Reg. 77207.

¹⁰⁵ See, e.g., Ready Fund\$, <http://www.readyfunds.net/assets/PDFs/ReadyFund-ODP-9.5.14.pdf>: “eZaccess Overdraft Privilege – a secure, smart solution It covers transactions that exceed the balance in your account, eliminating the inconvenience of rejected debit card or ATM transactions.”

¹⁰⁶ 79 Fed. Reg. 77207.

¹⁰⁷ *Id.*

¹⁰⁸ *Id.*

¹⁰⁹ *Id.* (“Indeed, every prepaid overdraft service that charges a fee of which the Bureau is aware contemplates and approves repeated transactions.”)

While we agree with the Bureau's analysis here, we have long expressed concern about lenders who claim their short-term, balloon repayment products are open-end primarily to skirt the scope of laws covering only closed-end products or to avoid effective APR disclosures.¹¹⁰ We urge the Bureau to continue to consider appropriate treatment for such products in the interest of preventing evasions of laws and regulations intended to apply to them.

C. Any overdraft feature on prepaid accounts should be captured under TILA's definition of credit card.

We agree with the Bureau's determination that the current exclusions from Credit CARD Act coverage of cards linked to overdraft lines of credit or other overdraft "services" should not be extended to prepaid accounts. As the Bureau notes, the commentary to Regulation Z's definition of "credit cards" today states that a debit card is not a credit card unless there is a credit feature or agreement to extend credit, even if the creditor occasionally honors an inadvertent overdraft.¹¹¹ Thus, debit cards with fee-based overdraft are excluded. Debit cards with overdraft lines of credit are "credit cards" under Regulation Z but are exempt from the Credit CARD Act provisions on the basis that overdraft lines of credit were not in wide use at that time and that creditors issuing such lines of credit generally did not engage in the practices addressed by the Credit CARD Act.¹¹²

The Bureau proposes including prepaid cards in the Regulation Z definition of credit card and in the cards subject to the Credit CARD Act protections if they access any credit feature, including any overdraft feature, for which a finance charge or fee, such as an application fee, late payment fee, over the credit limit fee or returned payment fee is charged (or repayment is expected in more than four installments).¹¹³ The unique nature of prepaid cards discussed by the Bureau and herein makes such treatment more than appropriate, and we support it. If application fees were not included, for example, issuers would easily be able to avoid the intended protections by charging large upfront "application" fees in exchange for an overdraft function.

D. TILA's credit card protections the Bureau proposes should be strengthened given the unique nature of prepaid cards and the more vulnerable consumers whom they target.

The Bureau recognizes it has the authority under TILA to impose additional substantive requirements pursuant to Sec. 105(a), as it proposes to prevent issuers from soliciting credit applications from a prepaid card holder until at least 30 days after the consumer has registered

¹¹⁰ See, generally, comments CRL submitted jointly with other groups on (1) the Department of Defense's proposed amendments to the Military Lending Act regulations in Dec. 2014 (http://www.responsiblelending.org/media-center/press-releases/pdf/mla_comments_12242014.pdf) and (2) the OCC and FDIC's proposed guidance addressing payday lending by banks in May 2013 (<http://www.responsiblelending.org/payday-lending/policy-legislation/regulators/advocates-support-proposed.html>).

¹¹¹ 79 Fed. Reg. 77208.

¹¹² *Id.* (citing 75 FR 7657, 7664 (Feb. 22, 2010); § 1026.2(a)(15)(ii)).

¹¹³ 79 Fed. Reg. 77206.

the prepaid account.¹¹⁴ Should the Bureau decide to permit overdraft charges on prepaid cards, we believe it must more fully use that authority in order to prevent abuses.

1. An ability-to-repay requirement should be applied but strengthened.

If overdraft on prepaid cards is permitted, we strongly support its being subjected to an ability-to-repay requirement. Indeed, this is the fundamental protection for any credit product. However, we are concerned that, given the largely subprime consumers who use prepaid cards, the Credit CARD Act's protections are not sufficient.¹¹⁵

As we understand it, issuers largely comply with the Credit CARD Act's requirement by relying on stated income and checking credit scores. In the traditional credit card market, most issuers will not extend credit to consumers whose extremely low credit scores and thick credit files suggest indicate inability to pay. But there is no guarantee that this discipline will extend to the prepaid card market, which is overwhelmingly made up of such consumers, or that the credit will be designed so that it is affordable, with smaller installment payments rather than lump sum repayments. Moreover, even in the credit card market today, some issuers offer cards to a "bad credit" target audience carrying predatory terms that together appear quite unaffordable. (*See* fee harvester card examples in section 2 below for examples of card terms that are surely unaffordable for many borrowers.) Thus, we are concerned that the Credit CARD Act's ability to repay standard will not provide adequate assurance that vulnerable consumers will be able to repay overdrafts plus associated charges.

The Bureau should enhance the ability-to-repay requirement by requiring that issuers make a reasonable determination of a borrower's ability to repay the overdraft credit plus associated charges based on either: (1) verification of income and debts, including, for renters, housing expense; or (2) a review of 90 days of the borrower's prepaid card account activity.

2. A limit on fees should be applied but strengthened significantly.

It is appropriate that any credit card be subject to the Credit CARD Act's limit on upfront fees, at 25% of the credit limit during the first year. But the Bureau should both include pre-account opening fees in that limit and apply the limit to every year the account is open. Again, such action is clearly justified, particularly given the generally more vulnerable consumers using prepaid cards. Failure to do so leaves an alarming loophole in the proposal.

¹¹⁴ 79 Fed. Reg. 77209. As the Bureau notes, it proposes adding "additional, unique protections to Regulation Z for prepaid accounts that are credit cards that access overdraft services or credit features."

¹¹⁵ The Credit CARD Act's general ability to repay rule requires that the card issuer "**consider**[] the ability of the consumer to make the required payments under the terms" Sec. 109; 15 USC 1665e (emphasis added), but not that the lender make a reasonable determination (as with the qualified mortgage requirements). The regulations for this provision allow wide latitude in how a creditor complies with this requirement, repeating the "consider" language. Procedurally, the commentary requires that the creditor have "reasonable written policies and procedures" requiring consideration of at least one of the following: the ratio of debt obligations to income; the ratio of debt obligations to assets; or the income the consumer will have after paying debt obligations. 1026.51(a)(1)(ii). The commentary goes on to further specifically authorize the creditor to rely on borrower self-certifications.

One fee harvester card charges a \$95 “processing fee” before the account is opened and a \$75 annual fee for a card with a \$300 credit limit.¹¹⁶ The fee harvester loophole allows the \$95 fee to be imposed, meaning that consumers may be charged \$170 in fees, more than half of their credit limit, before they make a single purchase. In subsequent years, when no fee cap applies, that same fee harvester card charges \$120 in annual and “monthly servicing” fees, on top of 36 percent interest, for a card with credit line of only \$300.¹¹⁷

Another fee harvester card, Continental Finance, the subject of a recent Bureau enforcement action, charges consumers with subprime credit scores \$75 in upfront fees on a \$300 credit line, in addition to an upfront security deposit and annualized interest. The Bureau noted the importance of context in this enforcement action: “These excessive fees are especially harmful because the cards were targeted to consumers with subprime credit who are often economically vulnerable. We will act to protect people who are wronged in this market.”¹¹⁸

Enforcement actions like this one are impactful and representative of the important enforcement work the Bureau has done on a range of issues impacting vulnerable consumers. In the prepaid card space, the Bureau has a “clean slate” opportunity to prevent holders of prepaid cards from suffering from the same practices in the first instance, and it should use it.

We support that under the Bureau’s proposal, any transaction fees, transfer fees or annual fees for an overdraft line of credit would be included in a limit. In the overdraft line of credit market today, annual fees tend to be in the \$25 range, while transfer fees can be as high as \$12.50 or more, even for small overdrafts.¹¹⁹

3. Consumer control over repayment should be strengthened.

As the Bureau proposes, consumers should be allowed at least 21 days following mailing of the bill to make a payment, and repayment should be required no more frequently than monthly.

And, as the Bureau proposes, lenders should be prohibited from repaying themselves immediately from incoming deposits. Typically this feature gives the depository or prepaid issuer a super-lien on a vulnerable consumer’s limited funds, disincenting responsible underwriting, and harming both the consumer and legitimate lenders and businesses who do not put themselves first-in-line. Prohibition of this practice should apply to all forms of credit in all

¹¹⁶ See https://www.premiercardoffer.net/CardDetails_Printable/EKOV1LVS1%200636OMI.

¹¹⁷ *Id.*

¹¹⁸ CFPB, Press Release, *CFPB Orders Subprime Credit Card Company to Refund \$2.7 Million for Charging Illegal Credit Card Fees: ‘Fee-Harvester’ Credit Cards Misrepresented Charges, Hit Consumers With Excessive Fees*, Feb. 4, 2015, available at <http://www.consumerfinance.gov/newsroom/cfpb-orders-subprime-credit-card-company-to-refund-2-7-million-for-charging-illegal-credit-card-fees/>.

¹¹⁹ See, e.g., M&T Bank charges \$12.50 up to once per day (<https://www.mtb.com/personal/loanscredit/OverdraftProtection/Pages/Index.aspx>).

contexts; it is especially important in the prepaid card space where so many consumers are on modest incomes.

In addition, as proposed, issuers should be required to offer consumers another manner to repay balances than through automatic repayment. Further, the Bureau should specify that consumer consent to automatic repayment may not be coerced through, for example, conditioning automatic receipt of funds on automatic repayment, or charging coercively higher rates or fees if the consumer does not opt-in.

Though improving borrower control over repayment, this proposal does not go far enough because it does not address balloon repayment. Balloon repayment is a central, typical element of unaffordable, predatory lending. For many prepaid card users, if they could not afford, for example, a \$100 payment a month ago, they cannot afford to repay that \$100 plus a fee in one lump sum the following month. The Bureau should require that overdraft loans over a specified dollar amount be structured as installment loans (with an option to prepay).

4. Additional requirements, as the Bureau has clear authority to impose, should also be imposed.

We support the Bureau's additional requirement that lenders wait some period of time between a consumer's registration of a prepaid account and solicitation/application for credit. However, we urge the Bureau to make this period 90 days rather than 30. While providing too little time for a consumer to become familiar with a card's features and fees, thirty days also does not give the issuer the needed transaction history to make a meaningful assessment of ability-to-repay.

VII. Scope of "Credit Card"

A. The CFPB should include in the definition of "credit card" any prepaid card that accesses credit (with specified exceptions), even if the credit is not limited to a particular card.

Though our comment focuses on overdraft, we nonetheless note a more general credit-related concern given its importance. The Bureau's proposal contains an alarming loophole for credit that is accessed through a prepaid card but can be accessed another way. The rules only apply to credit that can be directly deposited only to a particular prepaid card dictated by the lender. But lenders may design lines of credit that can be linked to any prepaid card a consumer chooses. Or, a credit feature could be designed for and work best when accessed through a particular prepaid card, but the lender could provide an alternative access point in order to evade the rules, such as the ability to transfer funds through the automated clearinghouse to any account, or even by a payment over the Visa or MasterCard network.

We are especially concerned about evasions by payday lenders, which, as noted earlier, often sell prepaid cards. Payday lenders are moving to lines of credit that help them evade payday loan laws. The payday lender could offer the option of accessing a line of credit through cash at the payday store, ACH deposit to any account the consumer chooses, or transfers to the payday lender-branded prepaid card. If the consumer chose to link the line of credit to the payday lender

prepaid card, the card would function in the same manner as the credit features that the CFPB has covered, but with none of the proposed protections. The payday lender could link the credit feature the same day that the consumer acquires the card and would not have to comply with the credit card ability to pay rules, limits on penalty fees, reasonable time to pay rules, or other protections.

The Bureau need not be concerned that this closing this loophole will result in an overbroad scope. It will, by definition, only bring in accounts that are structured as open-end lines of credit and only credit lines that can be deposited onto a prepaid card. In the small dollar loan market, with consumers who typically use prepaid cards, these are almost exclusively evasion products, poorly structured products that work much like closed-end credit but are structured as open-end to evade some state or federal (e.g., Military Lending Act) law.

We support the longer discussion of this issue in the comments of the National Consumer Law Center which include, among other things, suggested specified exceptions to this general recommendation.

B. Prepaid cards falling under the definition of credit cards should not be included in MLA's definition of credit cards.

As discussed in the comments we, together with other groups, submitted to the Department of Defense on the proposed amendments to the Military Lending Act regulations, prepaid cards with overdraft or other credit should be excluded from those regulations' definition of credit card.¹²⁰ Any MLA "bona fide" fee exemption should not apply to prepaid cards, as they are not traditional credit cards and could be used to evade the MLA.

VIII. Lenders should be prohibited from conditioning credit on preauthorized electronic transfers, including for single-payment loans.

We strongly support application of the EFTA's compulsory use provision to prohibit lenders from conditioning credit, including overdraft credit, on preauthorized electronic transfers. We also note that any open-end "plan" that is payable monthly contemplates payments at recurring intervals and thus fits within the EFTA's definition of preauthorized electronic fund transfer. Thus, any overdraft credit extended under the proposed rules would be subject to the compulsory use ban even if individual credit draws are repayable in a single lump sum. Further, we urge the Bureau to specify that tactics that effectively coerce preauthorized electronic transfers, like conditioning automatic receipt of funds on automatic repayment, or charging coercively higher rates or fees if the consumer does not authorize electronic transfer, are prohibited.

¹²⁰ Comments of Consumer Federation of America, CRL, *et al.*, on the Department of Defense's proposed amendments to the Military Lending Act's regulations at 17-19 (Dec. 2014), available at http://www.responsiblelending.org/media-center/press-releases/pdf/mla_comments_12242014.pdf.

IX. We also support the provision that terms and conditions may not differ depending on whether or not a consumer has an overdraft or credit feature on the card.

We support the Bureau's proposal that terms and conditions of a prepaid card may not differ depending on whether or not a consumer has an overdraft or credit feature on the card. Absent this protection, issuers could easily coerce consumers into accepting these features.

X. Conclusion

Thank you for consideration of our comments. We hope the Bureau will take full advantage of this opportunity to make the prepaid card market one where consumers are fully protected from unfair, deceptive, and abusive overdraft practices. We would be happy to discuss our comments further.