Consumer protection

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U.S. CONSUMER PRODUCT SAFETY COMMISSION
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Date: 1/27/99 **Time:** 3:00 pm a.m./p.m.

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Pages (including cover sheet): 12

NOTE:

U.S. CONSUMER PRODUCT SAFETY COMMISSION

WASHINGTON, D.C. 20207

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CPSC's strategic plan calls for reducing injuries and deaths in five major areas: head injuries to children, childhood poisonings, fires, carbon monoxide poisonings, and electrocutions.

<u>Fires</u>

Each year, 1,000 children under age 15 die of fire-related causes, and over 600 of these deaths are to children under age 5.

To help reduce these numbers, CPSC is working on several product areas, including:

--Upholstered furniture fires ignited by small open flames kill 90 people per year.

--Mattresses and bedding fires ignited by small open flames kill 160 people per year.

--Kitchen ranges are a leading cause of residential fires. Cooking fires result in about 100 deaths and over 2,500 injuries each year.

--Smoke detectors need to have batteries changed annually. Approximately one-third of all smoke detectors in homes do not have working batteries. CPSC endorses the new 10-year "long life" batteries for smoke detectors.

<u>Head injuries</u>

Head injury is a leading cause of death and disability to children in the U.S. Each year, there are 800,000 product-related head injuries to children under 15 years old. To help reduce deaths and injuries, CPSC is:

--Working to improve safety straps (restraints) on infant and juvenile products to address over 25,000 injuries per year.

--Conducting a study on playground injuries (over 200,000 each year) to learn more about how to prevent them.

<u>Recalls</u>

Each year, CPSC announces the recall of approximately 300 hazardous products. In 1998, these recalls involved 36.6 million product units. CPSC's new "FAST TRACK" recall program cuts red tape for companies and speeds up corrective action for consumers, resulting in more effective recall rates. "FAST TRACK" recalls have an average 60 percent return rate while traditional recalls have an average 18 percent return rate.

CPSC does a good job getting recalled products off store shelves. It is much harder to get recalled products out of consumers' homes. To increase publicity to consumers about recalls, CPSC is:

--Adding thousands of people to CPSC's recall mailing list, e-mail list-server, and FAX list.
--Broadcasting video news releases for TV news reporters to use, reaching up to 40 million TV viewers for some recall notices.
--Providing recorded audio soundbites for radio stations to use in news programs about recalls.
--Conducting an annual "Recall Round-Up" with nationwide TV coverage and state/local assistance to find previously-recalled products.

Research

In the year 2000, CPSC is, for the first time, the Administration budget includes funding to conduct product safety research. Candidates under consideration include research on:

--Smoke Alarms: to stimulate development of new technology to enhance reliability and performance.

--Circuit Breakers: to reduce home fire hazards through safety improvements in design.

--Fire Sprinklers: to determine failure modes and recommend product improvements.

--Choking: to develop a three-dimensional computer model to better understand and evaluate choking hazards to children.

Data Collection

In 2000, CPSC, in cooperation with other federal agencies, plans to begin collecting data on all injuries, not just consumer product injuries, treated in hospital emergency rooms. This "All-Trauma" system will be based on CPSC's nationally recognized National Electronic Injury Surveillance System (NEISS) which collects injury data from a sample of the nations emergency rooms on a daily basis. This federal initiative recognizes CPSC's leadership in injury data collection.

Since CPSC came into existence in 1973, there has been a 30 percent decline in the rate of deaths and injuries related to consumer products. This new data collection effort by CPSC will provide a total picture of injuries nationwide and will help further reduce the injury and death rate.

IV. Annual Performance Goals for 2000 (by Strategic Goal)

KEEPING CHILDREN SAFE FROM HEAD INJURIES

STRATEGIC GOAL: The rate of head injury to children under 15 years old will be reduced by 15 percent from 1996 to 2006.

Total Budgeted Amount for this Goal[3]		
Fiscal Year	**FTEs**	**Amount (in millions)**
1999	55.6	$5.614
2000	61.0	$7.197

THE HAZARD

Head injury is a leading cause of death and disability to children in the United States. In 1997 alone, there were an estimated 650,000 product-related head injuries to children under 15 years old that were treated in hospital emergency rooms, or about 60 percent of all head injuries. Of these, about 360,000 were to children under 5 years old. Studies have shown that children have a higher risk of head injury than adults and that children's head injuries are often more severe than many other injuries and can have life-altering consequences.

In 1996, about 80 percent of the head injuries to children under 15 years old were diagnosed as concussions, fractures and internal head injuries, potentially the more serious head injuries. The types of consumer products under the Commission's jurisdiction that are most often associated with head injuries to children include bicycles, playground equipment, and other juvenile products. Participation in sports is also associated with high numbers of children's head injuries.

MEANS AND STRATEGIES

To reduce head injuries to children, in 2000, staff will: develop new proposals for voluntary standards for window guards and recreational helmets; develop and test passive restraint systems for a variety of children's products; and analyze hazard

[3] Estimates for 1998 are not available.

patterns for playground equipment. CPSC staff will also participate in the voluntary standards process with committees that received CPSC's recommendations for new or modified safety standards in 1998 and 1999. In 1998, recommendations were sent for high chairs, stationary activity centers, trampolines, and furniture (tipover), meeting the goals for these products a year early. In 1999, recommendations for baby swings and infant carriers will be sent to the committees.

Staff will also focus on those products with defects that may cause head injury, and when appropriate, conduct recalls, corrective actions, issue press releases, and warn the public about the hazards of bicycle-riding, All-Terrain Vehicles, older style baby walkers, infant carriers, the need for head protection for various recreational activities, the need for adequate protective surfacing around playground equipment, and the need to maintain that surfacing.

These projects and activities address over 127,000 head injuries to children under 15 years old treated in hospital emergency rooms, resulting in over $8 billion in societal costs. (Note: crosscutting goals with other agencies are described on pp. 47 to 49.)

ANNUAL GOALS FOR 2000

A. Program: *Hazard Assessment and Reduction*	1998 Estimated	1999 Proposed	2000 Proposed
A-1. Send recommendations to voluntary standards organizations	5	6	2
A-2. Complete testing/data collection/hazard analysis activities	6	2	3
A-3 Complete phase 1 on a head injury research study	--	--	1

A-1. Prepare and send to voluntary standards organizations recommendations to strengthen or develop two voluntary safety standards.

Window Guards

In cooperation with ASTM, develop a draft voluntary safety standard for window guards used on windows designed for emergency escape from fires.

Recreational Helmets

Develop a voluntary standards proposal for a helmet that could be used for one recreational activity such as skating, skateboarding or horseback riding to prevent head injuries from falls.

A-2. Complete three testing and data collection activities

Playground Equipment

Complete a hazard analysis to identify hazard patterns involved in playground injuries occurring in home, public and daycare locations.

Passive Child Restraint Systems

Develop and test passive restraint systems for effectiveness, ease of use, proper sizing and child-proofing to prevent falls from a variety of products such as high chairs, infant carriers, infant swings, strollers, changing tables, bicycle carriers, and baby jumpers. Also, complete a hazard analysis of death and injury scenarios.

Plastic Failures

Develop an engineering materials and design guide to address falls and asphyxiations from products with structural parts made of plastic that fail or break, such as plastic latching mechanisms on infant carriers and plastic hinges on high chair legs. The guide is intended to assist manufacturers in producing safer children's products.

A-3. Complete phase 1 of a head injury research study

Head Injury Study

Collect data to evaluate the adequacy of current safety performance criteria used to protect consumers from head injury. This research will help to ensure that head protection currently provided for children and adults in the design of helmets and other surfaces (e.g., playgrounds) is adequate to provide the protection needed.

B. Program: *Compliance*	**1998 Estimated**	**1999 Proposed**	**2000 Proposed**
B-1. Initiate recalls and corrective actions	14	15*	15*
B-2. Correct violations and initiate recalls	0	10*	10*
B-3. Monitor existing voluntary standards	0	2	2

* Projected goals

Identify and act on products that present a risk of head injury through:

B-1. *Recalls and Corrective Actions* — Pursue for recall or other corrective actions a projected 15 products that present a substantial risk of head injury.

B-2. *Violations and Recalls* — Identify and correct a projected 10 violations that fail mandatory safety standards that address head injury.

B-3. *Monitoring Voluntary Standards* — Monitor two existing voluntary standards likely to reduce head injuries to determine the number of firms in compliance.

C. Program: *Consumer Information*	1998 Estimated	1999 Proposed	2000 Proposed
C-1. Conduct public education efforts	2	4	4
C-2. Alert the public of recalls through press releases	24	15	15
C-3. Produce VNR for recalled product	3	1	1
C-4. Respond to consumer requests for publications	180,000	150,000	150,000

C-1. Issue four public alerts or warnings on:

Bicycles — Promote the use of bicycle helmets and safe bicycle-riding practices that prevent head injuries to children.

All-Terrain Vehicles (ATVs) — Warn teenagers, parents and other caregivers of ATV hazards and promote the use of helmets and safe riding practices that prevent head injuries to children.

Infant Products — Warn parents about the hazards of older style baby walkers and infant carriers and encourage the use of safer baby walkers and infant carriers.

Recreational Activities — Warn about the need for child head protection in recreational activities such as in-line skating.

Alert the public to the hazards of head injury through:

C-2. *Press Releases* — For recalled products presenting a substantial risk of head injury, initiate a projected 15 press releases to warn the public.

C-3. *Video News Release (VNR)* — For at least one recalled product, work with the manufacturer of the recalled product to produce a VNR.

C-4. *Publications* — Respond to consumer requests for a projected 100,000 checklists, booklets, and safety alerts warning about head injury hazards.

KEEPING FAMILIES SAFE FROM FIRE HAZARDS

STRATEGIC GOAL: The rate of death from fire-related causes will be reduced by 10 percent from 1995 to 2005.

Total Budgeted Amount for this Goal		
Fiscal Year	**FTEs**	**Amount (in millions)**
1999	112.9	$11.015
2000	112.1	$14.008

THE HAZARD

In 1996, about 3,700 people died and 19,000 were injured because of fires that started in their homes. These fires resulted in property losses of about $4.4 billion. Children are particularly vulnerable. Each year 1,000 children under the age of 15 die of fire-related causes and over 600 of these deaths are to children under the age of 5 years. In fact, children under age 5 have a fire death rate more than twice the national average. Children at increased risk are often those from low income and minority families who live in poorer urban and rural areas.

Most deaths occur from fires that start at night while families are asleep. Four times as many victims die of inhaling smoke and toxic gases than from burns. Products most often involved in fire deaths are upholstered furniture, mattresses and bedding, and heating equipment. These three products account for about 50 percent of the fire deaths.

MEANS AND STRATEGIES

In 2000, staff will focus on preparing for Commission consideration two candidates for final rulemaking or other alternatives. One of the candidates, upholstered furniture, has been deferred from final rulemaking consideration in 1999 due to chemical issues; the other candidate, wallcoverings, will begin in 1999. Staff will also prepare proposals to develop or modify four voluntary standards for: electrical reinspection, electrical switches, arc fault circuit interrupters and portable room air heaters and will complete data analyses and technical review activities for hazards related to mattresses and bedding; pellet stoves; fixed electric air heaters; portable electric fans, residential circuit breakers; and sprinklers.

These projects and activities address about 19,000 injuries, 3,700 deaths, and $4.4 billion in property damage resulting in $23.8 billion in societal costs. (Note: crosscutting goals with other agencies are described on pp. 47 - 49.)

ANNUAL FIRE-RELATED GOALS FOR 2000

A. Program: *Hazard Assessment and Reduction*	1998 Estimated	1999 Proposed	2000 Proposed
A-1. Provide candidates for rulemaking or other alternatives	0	1*	2
A-2. Send recommendations to voluntary standards organizations	7	6	3
A-3. Complete hazard analysis/data collection/technical feasibility studies	6	7	6
A-4. Complete two research studies	--	--	2

*The original 1999 Annual Plan proposed two rules. One has been deferred until 2000.

A-1. Prepare for Commission consideration two candidates for final rulemaking or other alternatives.

Upholstered Furniture

To address the risk of small open flame-ignited fires involving upholstered furniture, the Commission will: (a) continue the rulemaking process by issuing a final rule; (b) work with standards-setting groups to complete a voluntary safety standard; or (c) consider other alternatives. (A Commission decision planned for 1999 has been deferred to study the safety of flame retardant chemicals.)

Wallcoverings

To address the hazard of fires from wallcoverings, staff will provide an options package to the Commission for their consideration. (Over 200 people die each year in fires in which wallcoverings are the first item ignited.)

A-2. Prepare and send to voluntary standards organizations recommendations to strengthen or develop three voluntary standards:

Electrical Reinspection

To further address the problem of fires in older homes, develop and send recommendations to the Residential Electrical Maintenance Code to require smart arc fault circuit breakers and use of outlet testers and to expand the scope to include multi-family dwellings. Fires result from deterioration of the wiring in older homes leading to short circuits, arcing, and other fire hazard conditions. This includes inadequate amperage that results in fuses too large for the branch wiring or inadequate numbers of outlets that result in excessive use of extension cords.

Electrical Switches

To address the fire hazard in the switch components of appliances, complete a technical review of the safety standard; conduct laboratory testing and evaluation; and develop recommendations for voluntary safety standards. Appliance fires can start in switch components when the structural parts of switches become deformed through overheating.

Arc Fault Circuit Interrupters

Develop recommendations and support for expanded arc fault circuit interrupter (AFCI) coverage in new home construction and provide technical substantiation for new AFCI technology (e.g., digital enhancements). The 1999 National Electrical Code will require AFCIs in bedroom circuits of all new home construction, effective in 2002, meeting CPSC's annual goal for 1999 several months early.

A-3. Complete six data analysis and technical review activities to evaluate the need for, or adequacy of, voluntary standards.

Mattresses and Bedding

Evaluate an industry-sponsored study to assess the effectiveness of alternative fire-control strategies that could lead to the development of a voluntary or mandatory safety standard.

Pellet Stoves

Assess the causes of fires in the hoppers of stoves that use compressed materials, such as sawdust, for fuel. These fires occur in spite of the presence of sensors that detect overheating. Complete a data review and review product designs to develop recommendations for existing standard and code changes, if warranted.

Fixed Electric Air Heaters

Determine the role of component breakdown, insulation failure and dust accumulation in fires associated with fixed room air heaters. Complete a review of incident data, technical review of safety standards, and laboratory testing. (Prepare for possible voluntary safety standards recommendations in 2001.)

Portable Electric Fans

Determine the role of component or connection failures that result in fires originating in window-mount and oscillating types of portable electric fans. Complete a review of incident data, technical review of safety standards, and laboratory testing. (Possible voluntary safety standards recommendations in 2001.)

Residential Circuit Breakers

Assess the causes for failure at the circuit breaker plug-in connection that result in overheating and fires in the circuit breaker panel box. Complete a technical review of current and old production circuit breaker connections to determine the need for, or scope of, more extensive testing and analysis.

Sprinklers

Test and evaluate sprinklers to support voluntary standards recommendations on performance, design, installation, and maintenance. Problems could include: sprinkler designs that may not activate at lower pressures; installation problems resulting from contamination of water that cause seals to deteriorate and prevent sprinklers from operating; and determining the life of the product before replacement is recommended.

A-4. Conduct two research studies on fire-related hazards.

Circuit Breakers — Initiate a research study to evaluate the extent and the nature of the fire risks associated with residential circuit breakers. Laboratory and field studies will enable the Commission to determine what improvements are needed in circuit breakers to reduce the risk of fire. In 2000, staff will design the laboratory and field studies and begin data collection.

Smoke Detector Evaluation — Design a research study and collect data to evaluate the adequacy of smoke detector performance standards and technology, as well as new technology that is emerging for smoke detectors. Current standards are based on 30-year-old tests.

B. Program: *Compliance*	**1998 Estimated**	**1999 Proposed**	**2000 Proposed**
B-1. Initiate recalls and corrective actions	58	50*	50*
B-2. Correct violations and initiate recalls	387	350*	350*
B-3. Monitor existing voluntary standards	1	1	1
B-4. Conduct import surveillance	1	1	1

*Projected goals

Identify and act on products that present a risk of fire-related death through:

B-1. *Recalls and Corrective Actions* — Pursue for recall or other corrective actions a projected 50 products that present a substantial risk of fire-related death.

B-2. *Violations and Recalls* — Identify and correct a projected 350 violations that fail mandatory fire safety standards.

B-3. *Monitoring Voluntary Standard* — Monitor one existing voluntary standard likely to reduce fire-related deaths to determine the number of firms in compliance.

B-4. *Import Surveillance* — Conduct port-of-entry surveillance for at least one product for which fire safety standards are in effect.

C. Program: *Consumer Information*	1998 Estimated	1999 Proposed	2000 Proposed
C-1. Conduct public education efforts	4	6	5
C-2. Alert the public of recalls through press releases	43	35	35
C-3. Produce VNR for recalled product	6	2	2
C-4. Respond to consumer requests for publications	180,000	150,000	150,000
C-5. Implement a public safety campaign for smoke detectors	--	--	1

C-1. Issue five public alerts and warnings on:

Fireworks — Conduct the annual campaign for the Fourth of July holiday season to alert consumers to the common hazards associated with legal and illegal fireworks. The campaign will include a news conference to demonstrate the hazards; announcements of fireworks recalls; and publication of injury prevention tips.

Home Heating — Issue safety information designed to give consumers information related to home electrical system inspections; fuel-fired heating equipment; coal and woodstoves; and smoke detectors.

Halloween Hazards — Warn about the dangers of costumes catching on fire from children carrying candles or using matches and cigarette lighters.

Holiday Hazards — Warn about the risk of fire from decorative light strings and natural trees, as well as provide information on the safe use of candles and fireplaces.

Cigarette Lighters — Warn about the risk of fire from children under 5 years playing with cigarette lighters.

Alert the Public to Fire-Related Hazards through:

C-2. *Press Releases* — For recalled products presenting a substantial risk of fire-related deaths, initiate an estimated 35 press releases.

C-3. *Video News Releases (VNR)* — Complete two VNRs: (1) for at least one recalled product, work with the manufacturer of the product to produce a VNR; and (2) produce a VNR for the fireworks safety campaign.

C-4. *Publications* — Respond to consumer requests for an estimated 100,000 checklists, booklets, and safety alerts warning about fire-related hazards.

Consumer Safety

THE WHITE HOUSE

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DATE: 11-17-98 **PAGES TO FOLLOW:** 12

COMMENTS: Background info for 2:00 pm Consumer Fin mtg today in Room 239 OEOB. Thanks.

If this fax is incomplete or you need to give clearance information for a meeting, please call Sonyia Matthews at 456-5351. Thank you.

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MEMORANDUM FOR SARAH ROSEN

FROM: Gregory A. Baer
Deputy Assistant Secretary
Office of Financial Institutions Policy

SUBJECT: Options for ATM and other Bank Fee Disclosures

The Subcommittee on ATM and Other Bank Fee Disclosures has had several meetings to discuss options for gathering and disclosing information on such fees. This memorandum sets forth several options currently under consideration, including their pros and cons.

Option 1: **<u>Establish a Repository of Bank Fee Data</u>.**

All depository institutions are currently required by the Truth in Savings Act to maintain a schedule of the fees they charge, and present it to any person who asks for it. Conceivably, the Act could be amended to require banks to send the same information electronically to the Fed or any other central data repository, where it could be widely accessed via the Internet. Rough estimates of the cost of setting up such a website, assuming data could be obtained and accessed electronically, range from about $40,000 for a basic listing of banks and their fees to about $150,000 for a more useful interactive site. Consumer education in the use of the website and its information would be an additional cost.

We have spoken to the Fed, which did not deny the feasibility of this option, but did question its utility. Although banks must maintain a schedule of fees, different banks use different terms to describe the fees (bounced check fee v. insufficient funds fee) and list them in different order. Thus, ease of comparison would not be great.

<u>Pros</u>:

- This option would provide a reasonably comprehensive look at every consumer account in the banking system.

- Consumer groups, academics, and others could analyze the data and make recommendations to consumers.

<u>Cons</u>:

- *Since banks would be providing data on fees charged to their own customers, this option would not inform consumers about ATM surcharges,* *which are assessed against non-customers.* Even if a bank was required to list the surcharge it charged non-customers, this information would be of little utility to customers who do not pay the fee. (Ironically, consumers may rationally wish to choose a bank with *high* surcharges and many ATMs in the area, thereby gaining access to the maximum number of ATMs at the minimum cost.) Moreover, many surcharges are assessed by non-bank ATM owners.

- A website would be directly useful only to those who are technically equipped and sophisticated in accessing and manipulating data.

- Data would often be out of date, unless updated frequently at the institutions' and/or collecting entity's expense, and it may not be compared easily across institutions because of differences in definitions of various account terms and conditions.

- Institutions may object to providing data on identical accounts that have different fee schedules in distinct market areas, such as different states.

Option 2: Encourage Voluntary Posting of Bank Fee Data.

Under this option banks would be encouraged to post voluntarily their fees for various accounts, with an emphasis on low-cost, basic banking and ATM-fee accounts. The bank fee information could be collected and distributed electronically via a centralized database as in Option 1, or it might be collected and distributed in local markets via local entities, either electronically or in hard copy. For example, in Missouri, we gather that the state publishes a list of low-cost banking accounts and relies on the banks to provide the information voluntarily. Approximately 60 percent of banks do so.

We discussed this idea with representatives of the ABA, whose reactions ranged from indifference to hostility to suspicion. They promised to check on the Missouri experiment, but have not gotten back to us.

Pros:

- This option would create opportunities for "partnerships" between industry and consumer groups.

- Since institutions would be providing information on only a subset of their consumer accounts, the resulting database would not be as voluminous as in Option 1, and therefore could be made available to a broader range of consumers in paper form.

- Institutions with low or moderate ATM surcharges may be more willing to make this information available to consumers with voluntary posting than would be the case under comprehensive reporting as in Option 1.

- Institutions voluntarily providing account information to a central site for easy distribution to consumers would almost certainly view it as a marketing opportunity. This would better guarantee the accuracy and utility of the information provided, and it could pressure underperforming institutions to actively market competitive products.

Cons:

- Voluntary posting of bank fees would not provide the comprehensive database and analytical opportunities available under Option 1.

- Although voluntary posting of bank fee data would reward those institutions charging low fees, it would not directly highlight and punish those institutions charging the highest fees.

- Voluntary posting of account information may allow some institutions to undermine the utility of that information to consumers by posting accounts subject to inordinately unique conditions, terms, and definitions.

Option 3: Support ATM Surcharge Disclosure Legislation.

Under this option, legislation would be proposed to require the posting of ATM surcharge fees *both* at the terminal by signage and on the screen of the terminal before a transaction is irrevocably made. Currently, only one or the other is required.

Pros:

- Disclosure is consistent with the goal of relying on private market mechanisms to maximize consumer choice and convenience.

- *Ex-ante* disclosure of ATM surcharges would permit consumers to better understand and assess the costs of using ATMs not owned by their own bank.

- Improved disclosure of ATM surcharges may encourage consumers to "vote with their feet" by migrating to the use of ATMs owned and operated by no-surcharge alliances of institutions.

- Congress is already considering disclosure legislation of this type.

- The ABA's best argument against this option was concern about unjustified liability in the event that a strong wind or vandals removed the signage.

Cons:

- This may be viewed by consumers and consumer groups as a relatively minor federal response, since the major ATM networks already have moved to incorporate written and screen-based disclosures of surcharges.

MEMORANDUM FOR SARAH ROSEN

FROM: Gregory A. Baer
Deputy Assistant Secretary for Financial Institutions Policy

SUBJECT: Consumer Protection Options.

This memorandum sets forth several legislative and regulatory proposals the NEC may want to consider with respect to consumer protection in the financial services area.

1. CREDIT CARD DISCLOSURES AND OPTIONS

This section describes several ways to increase disclosure to consumers regarding credit card issues. These issues also were discussed in the context of bankruptcy legislation.

Option 1: **(1) Require the disclosures set forth in the Senate bankruptcy bill, including the amount of time it would take to pay back the debt balance if only the minimum amount were paid each month; the number of months it would take to pay the entire balance if the consumer pays only the required minimum and if no further advances are made; and the total cost to the consumer. (2) Require a credit worksheet.**

Pros:

- Would inform consumers of the full impact of only making minimum payments.
- The Administration has supported these requirements.

Cons:

- The proposal would add cost and regulatory burden if the requirement applied for all cardholders.
- Simply supplying a credit worksheet with no additional help may fall short of the intended benefits. A simple worksheet would not educate the consumer fully, and it is difficult to assure the consumer will pay attention. This effort would be better undertaken as part of a complete credit education initiative.

Option 2: **Support the reduced requirement in the House-Senate conference bill, requiring disclosure of: (1) a statement on minimum payments; (2) an example, based on minimum payments and APRs, of how long it would take to repay a**

$500 balance if the consumer made only the minimum payment and if no further advances were made, to be disclosed to the customer annually; and (3) a worksheet to assist the consumer in determining his or her debt obligations and income. Also require the Fed to conduct a study to determine adequacy of information, and to issue regulations requiring additional disclosures if it finds they are needed.

Pros:

- Using a hypothetical imposes less regulatory burden, but may still assist consumers in understanding minimum payments. Requiring a study by the Board and Board regulations based on its study would identify a true need for regulations.

Con:

- Board rulemaking will take years.
- The Administration has already supported the disclosures in the Senate bill.

2. DISCLOSURE OF MUTUAL FUND COSTS

In a widely reported May 15, 1998, speech to the Investment Company Institute, SEC Chairman Levitt criticized the investment company industry for not doing enough to educate individual investors who are pouring money into the funds. Less than half the investors know that fund expenses are deducted on an ongoing basis, according to the SEC. Only 8 percent say they completely understand the expenses that their funds charge.

The SEC staff recently sent the Investment Company Institute (the mutual fund industry's trade group) a letter warning them that they need to carefully consider, and sometimes more explicitly disclose, fees that investors ultimately bear when they hold funds that participate in the supermarket programs offered by Charles Schwab Corp., Fidelity Investments, and other financial firms. The letter says the SEC "will closely scrutinize any increases in a fund's investment advisory fee that appears to be for the purpose of compensating the fund's investment advisor for paying the fund's supermarket fee."

Option: Encourage the SEC's efforts to improve disclosure to mutual fund investors and question fees that may not be appropriate.

Pros:

- Should increase competition and protect investors.

- Disclosure empowers investors to avoid funds with questionable fees, thus pressuring those funds to change their fee structure.

Cons:

- Increases regulatory burden on the fund industry.

- Many investors do not read the disclosures they currently receive. Adding more could unnecessarily burden the fund industry and invite litigation without really helping investors.

- Evidence of problems is unclear -- the mutual fund industry may call on the administration to provide examples.

- Could be viewed as duplicative of the SEC's initiative without adding much additional value.

3. RENT-TO-OWN TRANSACTIONS ISSUES AND OPTIONS

In a rent-to-own transaction, the consumer rents an item with the understanding that after a specified number of rental payments, he or she becomes the owner of the item. Until that time, however, the consumer can return the item and walk away with no further obligation. Because rent-to-own transactions do not qualify as credit sales under the Truth in Lending Act (TILA), the consumer has none of the protections of federal consumer protection statutes.

Rent-to-own can be an accessible means of acquiring household items, but survey data and consumer complaints show abuses. For example, a 1997 survey by U.S. PIRG found that rent-to-own stores charged an average effective APR of 100% -- five times the prevailing credit card rate of 20%. The U.S. PIRG survey found that only 50% of labels disclosed the total actual cost to own in small print and that none disclosed an APR. Evidence also suggests that some in the industry have used abusive repossession techniques.

The FTC expects to complete a study on the rent-to-own industry practices in the Spring of 1999. One focus of the study is whether most customers are simply renting (in which case disclosures would be less important) or are truly renting to own. If the statute was amended, FTC would prefer that the Fed write the regulations, since it writes all related regs.

Option: **Propose authorizing the Fed to write appropriate disclosure requirements for rent-to-own transactions. Pending release of the FTC study, we would not**

wish to be too specific in stating what those disclosures are, but two are fairly obvious: whether the item is new or used, and the total cost of purchasing the item. (Calculating the implicit interest rate gets a little complicated, and needs further study.)

Pro: This is a simple way to give consumers the protection provided by federal consumer protection statutes for extensions of credit.

Con: Rent-to-own bills introduced in 1997, 1994, and 1993 failed in the face of strong industry opposition.

4. DEBIT CARD ISSUES AND OPTIONS

Over the past couple of years, card issuers have been marketing "offline" debit cards aggressively, encouraging consumers to use them in place of writing checks. Like credit cards, but unlike ATMs, these offline debit cards do not carry a security feature, such as a PIN, to protect against fraudulent use. Moreover, many institutions have automatically replaced their customers' existing ATM cards, previously usable only with PINs, with cards that can be used with a PIN at ATMs and electronic POS terminals, but *without* a PIN in the "offline" mode.

The problem here is that, by law, credit cards (without security features) carry legal protections against consumer loss (e.g., maximum liability of $50 if issuer is notified within 3 days), whereas offline debit cards do not. Thus, these cards carry neither the security protections of an ATM card nor the legal protections of a credit card -- yet because they are the same size and same plastic, and customers might not understand the difference.

In response to concerns about customer confusion and liability, VISA and MasterCard have entered into voluntary agreements with their member financial institutions that go beyond the consumer protections required under the Fed's Regulation E.

Option: **Support the Schumer-Gonzalez Bill , which would have: (1) limited a consumer's liability to $50 for a debit card that is not PIN-protected and does not use some other unique identifier (a signature is deemed not unique); (2) required card issuers, as a condition of imposing any liability on consumers, to disclose the importance of promptly reporting loss or theft of the card; and (3) prohibited issuing a debit card that can function without a PIN or other unique identifier unless the card is not activated when sent, certain disclosures accompany the card, and the card is activated only upon the consumer's request and after verification of the consumer's identity.**

Pro: The bill would make the industry's voluntary reforms a legal (and therefore permanent) requirement and ensure that they would apply to all issuers.

Cons: The proposal requires less protection than Visa and Mastercard voluntarily provide (for example, the proposal applies only to non-PIN-protected cards). It may be unnecessary in light of industry reforms, such as limited liability, provisional recrediting, and customer-requested activation. Fed staff has told us that the Board has not changed its September 1997 position that the voluntary industry actions appear adequate.

5. UNSOLICITED MAILINGS OF LOAN CHECKS

Loan checks are credit products for which the consumer need only sign and cash or deposit the check to obtain the loan. They also are referred to as "loans by mail" and "live checks." The amount of these loan checks is not limited by TILA or regulation Z and may be thousands of dollars. Federal law does not prohibit creditors from mailing unsolicited loan checks. TILA does mandate that full disclosure of credit terms, such as the annual percentage rate and the payment schedule, be included with any mailing so that consumers can make informed decisions about whether to accept the loan. Thus, our primary concern is not disclosure, but rather (1) the potential for theft and fraud and the consumer inconvenience of refuting a claim of liability, and (2) a paternalistic concern that consumers could indebt themselves too easily (though generally only the wealthier consumers are sent loan checks).

Note: in the closest parallel, unsolicited mailings of credit cards has long been prohibited, for the reasons set forth above.

An August 1998 GAO report, Live Loan Checks: Information on Unsolicited Consumer Loans for Preapproved Borrowers," said there had been little evidence of fraud, the American Financial Services Association has adopted voluntary standards including disclosure and no liability for theft or fraud, but possible problems were the burden of unwinding fraud and potential increases in defaults or bankruptcy. Fleet Bank reported that between 1995 and 1997 it experienced 68 cases of fraud, based on 4.35 million live loan checks mailed and approximately 155,000 borrowers cashing the checks.

The Fed has said it is mindful of the appearance that consumers are exposed to risks they have not voluntarily assumed, but as of 1997 it did not favor an outright prohibition against sending these checks. The issuance of unsolicited loan checks is not as prevalent as the issuance of unsolicited credit cards in the late 1960s that led to the TILA prohibition.

Option: Support the Hinchey-Gonzalez bill, which would have prohibited the unsolicited mailing of loan checks or other negotiable instruments. The bill also would have provided that if a check or other negotiable instrument is sent unsolicited, a consumer would not be liable for the debt unless the creditor could prove that the consumer received and negotiated the instrument. Whether or not the intended recipient received it, the creditor could not report any liability resulting from the unsolicited instrument to a consumer reporting agency.

Pros:

- Protects consumers from theft and fraud and the burden of unwinding forged transactions.

- Consistent with other relevant law.

Cons:

- May be addressing a problem that doesn't exist.

6. DISCLOSURE OF CUSTOMER COSTS OF ACQUIRING FINANCIAL PRODUCTS

The financial modernization bill approved by the House of Representatives (H.R. 10) contained a Dingell/LaFalce amendment that would have required the federal banking agencies, the SEC, CFTC, and their self-regulatory organizations to adopt rules improving disclosure of customer costs of acquiring financial products.

Option: Support standalone enactment of Dingell/LaFalce or some other disclosure scheme that runs across all industries

Pro:

- Makes intuitive sense: disclosures need to be more simple, and disclosure practices should really be the same regardless of whether the product is being purchased from a commercial bank or an investment bank.
- As financial services become more integrated, it becomes increasingly difficult for consumers to sort out the costs of acquiring financial products. This provision helps consumers better understand these costs and to comparison shop for better deals.
- Makes markets more competitive by alleviating confusion and better informing customers.

Cons:

- Exceedingly complicated to prescribe in statute; delegating rulemaking authority would postpone action for years and perhaps lead to little change.
- According to Senate Banking Committee staff, the banking industry strongly objected to the provision on the basis of regulatory burden, arguing that their fees changed so often that it would be difficult to continually update the disclosure. The bond marketing industry argued that markups are embedded, not consumer costs. The insurance industry agreed to allow the provision to be

dropped, and the Senate Banking Committee left it out of the bill that would have gone to the Senate floor.

7. NASD OVERSIGHT OF INVESTMENT ADVISERS

NASD staff has recently cited an increasing trend, whereby securities brokers (AKA registered representatives) are increasingly giving up their licenses and becoming registered investment advisors (RIAs). A recent Wall Street Journal article quoted a plaintiffs' lawyer as asserting that investment advisers are "the last refuge of scoundrels" and "an accident waiting to happen." Basically, becoming an RIA means giving up sales loads, but still allows one to recommend specific mutual funds to clients, accept custody of client funds, have customer trades executed through an affiliated broker, etc. Yet the RIA would no longer by subject to firm-wide supervision, reporting of customer complaints, standards for advertising and sales materials, training and qualification requirements, suitability rules, and other consumer protections. This trend is being facilitated by the exponential growth in mutual funds, by which the ability of a broker to execute trades on an exchange becomes less significant.

In response, NASD recently has expressed interest in regulating investment advisers. At a brokers' convention last September, Frank Zarb, the NASD's chairman, said he was talking with the SEC, which regulates investment advisers under the Investment Advisers Act of 1940, about whether the NASD should become a self-regulatory organization for investment advisers, as it is currently for broker-dealers.

OPTION: We are not ready to make a recommendation here, but do plan to meet with the head of NASD in the coming weeks to see whether she would be receptive to an Administration initiative. We would also need to run any proposal past the SEC.

Pros:

- Protects investors and promotes competition.

Cons:

- Industry would complain about increased regulatory burden.

- Congress has considered creating an SRO in the past, but the investment adviser reform legislation enacted two years ago did not include it.