EXECUTIVE SUMMARY

Millions of underbanked Americans have found prepaid cards an effective way to meet their basic financial services needs. But functionality and ease of use are not the only important factors in the widespread adoption of prepaid cards. Consumers also need to be confident that the money stored on prepaid cards is secure, and they need to understand the exact costs of using them. As prepaid cards gain in popularity and are increasingly marketed and used as alternatives to bank accounts, it is time for formal consumer protections to be applied.

Most major prepaid card providers already offer basic consumer protections, such as deposit insurance, fraud and error resolution procedures, and account disclosures. But consumers need assurance that any general purpose reloadable (GPR) prepaid card account in the marketplace has these protections. Further, while the protections should be strong and clear, they should not make these products more difficult to obtain or restrict promising innovations to improve the value that they provide to underbanked consumers.

CFSI has been studying the evolution of the prepaid card industry since 2004. CFSI has supported the development of high-quality and affordable GPR prepaid card accounts as a valuable and necessary tool for the financially underserved. CFSI has analyzed the consumer protections applicable to GPR prepaid card accounts, as well as alternative payment mechanisms, and has consulted with a wide variety of stakeholders, including policymakers, consumer advocates, and industry representatives. As a result, CFSI recommends the following extensions of consumer protections to GPR prepaid card accounts:

1) Mandate FDIC pass-through insurance.
2) Extend Regulation E as it is applied to payroll cards and enhance the protections by:
   • Lengthening the period for which transaction history is available;
   • Enabling consumers to make a single request for ongoing paper statements; and
   • Studying and leveraging advances in technology and insights in financial capability to improve the delivery of account information.
3) Require a standardized fee-disclosure box and encourage additional disclosure tools for consumers, based on advances in technology and insights in financial capability.

These steps will ensure that all GPR prepaid card accounts have strong, basic consumer protections. They will also help to eliminate undesirable practices or fees associated with some products and improve the industry overall. Consumers will benefit by gaining a high-value, low-cost transaction account with the potential to access asset-building financial services that can ultimately help them achieve greater financial stability and prosperity.
THE EMERGENCE AND IMPORTANCE OF PREPAID CARDS

Over the past decade, an ever-growing array of financial services has become available for people who have traditionally been financially underserved. Previously, the 30 to 40 million American households who were unable to open a bank account or chose not to use one regularly were limited to cash, money orders, and check cashers for their basic banking needs. But technological innovations have given the underserved more and better options, such as prepaid cards. Although many varieties of prepaid cards exist, the one that typically has the most utility and relevance to the underbanked is the general purpose reloadable, or GPR, prepaid card account.

Like a bank account, a GPR prepaid card account can be used to make purchases, pay bills, access cash, monitor one’s finances, budget, save, and more. Unlike a bank account, however, a GPR prepaid card is typically easier and more convenient to open, and with the vast majority of cards, the consumer can spend only the money “loaded” or deposited into the account. For those living paycheck to paycheck, this feature helps with budgeting and, in most cases, protects against costly overdraft fees. Essentially electronic bank accounts without checks, GPR prepaid card accounts provide underbanked consumers with a safe, convenient means to manage their finances, with the additional potential to help them build assets.

The use of these products has taken off in recent years and is projected to grow even more rapidly in the near future. According to an industry research group, the funds loaded onto just GPR prepaid card accounts in 2008 totaled $8.7 billion and is projected to rise to over $118 billion by 2012. The total amount loaded onto all types of prepaid cards is estimated to double over the next three years to $672 billion in 2013.

1 The FDIC’s 2009 National Survey of Unbanked and Underbanked Households estimated that approximately 30 million households were underserved (http://economicinclusion.gov/about_survey.html). CFSI’s 2008 Underbanked Consumer Study estimated that approximately 40 million households were either unbanked or underbanked (http://cfsinnovation.com/publications/list/CFSIUnderbankedConsumerStudy). The two studies defined underbanked households slightly differently.

2 The Durbin Amendment to the Dodd-Frank Wall Street Reform and Consumer Protection Act required the Federal Reserve to develop new regulations regarding interchange fees that are scheduled to go into effect beginning on October 1, 2011. These new regulations will greatly reduce the fees charged by banks and payment card networks for debit interchange transactions. GPR prepaid card providers are exempted from the new regulations, but only if they meet certain criteria which include not charging overdraft fees or a fee for the first monthly withdrawal from an in-network ATM (http://www.federalreserve.gov/newsevents/press/bcreg/20110629a.htm).


THE NEED FOR STRONG CONSUMER PROTECTIONS

Increasingly, GPR prepaid card accounts are being marketed toward and used by consumers as alternatives to bank accounts. Currently, however, these products are not explicitly required by regulation to have many of the same consumer protections as bank accounts, such as FDIC insurance, fraud and error resolution procedures, and account disclosures. Although most major prepaid card providers already offer all or most of these consumer protections, consumers need to be confident that any GPR prepaid card account product in the marketplace includes the same strong protections.

The best way to extend these protections to GPR prepaid card accounts, however, is not simply to replicate the way they have been applied to bank accounts. Although the purpose and function of GPR prepaid card accounts are similar to those of bank accounts, their structure is fundamentally different. To ensure that GPR prepaid card accounts can continue to meet the unique needs and demands of underbanked consumers, protections must be thoughtfully applied in a manner that is both suitable for the consumer and feasible for prepaid providers. This paper recommends how regulators could address three key consumer protections: 1) FDIC pass-through insurance; 2) Federal Reserve Board Regulation E, concerning fraud and lost card protection and error resolution procedures (among other things); and 3) fee disclosures.

UNDERSTANDING THE BASICS OF PREPAID CARDS

Despite their growing popularity among underserved consumers, the financial services industry, and federal and state governments, prepaid cards are not well understood. This is both because prepaid cards are still emerging in the marketplace, and also because the term “prepaid card” is so broad. It can refer to a wide variety of products, including but not limited to gift cards, phone cards, healthcare cards, travel cards, rebate cards, payroll cards for directly depositing wages, federal and state benefit and payment cards (social security, income tax refunds, unemployment, welfare, food stamps, etc.), and general purpose reloadable (GPR) card accounts.

Each of these prepaid card products serves a different purpose and can function in a different manner. Generally, the cards fall into one of four categories, defined by two features. The first is whether money can be loaded on the card only once or multiple times (that is, whether it is reloadable). The second is whether the card can be used only at certain retailers or for specific goods, in which case it is called “closed loop,” or can be used at any retailer that accepts cards from payment networks such as Visa and MasterCard, in which case it is “open loop.” GPR prepaid card accounts are open loop and reloadable, making them similar in form and function to debit cards linked to bank accounts.

GPR prepaid card accounts look virtually identical to debit and credit cards. Like debit cards, they are issued by financial institutions and carry one of the major payment network brands (Visa, MasterCard, Discover, and American Express). Although they share many of the same functions and features as debit cards, GPR prepaid card accounts are typically easier to open and have no minimum balance requirements, credit history checks, or ChexSystems requirements. They also have greater restrictions than bank accounts such as maximum balance limits, no checks with the account, and are more difficult to overdraft. As with bank accounts, funds can be directly deposited into GPR prepaid card accounts. However, instead of depositing cash and checks at bank branches or ATMs, consumers typically add funds at check cashers, grocery stores, convenience stores, and other retailers.6

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THE CURRENT CONSUMER PROTECTION LANDSCAPE

A key difference between GPR prepaid card accounts and bank accounts is in the legal protections applied to protect the funds they hold. Deposits in bank accounts, for example, are typically insured for up to $250,000 per institution for each individual account owner. Funds loaded onto GPR prepaid card accounts are held at a bank, but they typically are held in a pooled account structure, which may not provide individual prepaid card cardholders with the same level of deposit insurance as a bank account.

Under the Electronic Funds Transfer Act (EFTA), which is implemented by Regulation E, with respect to bank accounts, depository institutions are required to follow certain procedures in cases of fraud or account errors; disclose to consumers the specific account terms and any changes in those terms; provide consumers different types of information about their accounts, such as statements; adhere to certain guidelines regarding overdraft coverage; and meet other related guidelines. Although most major GPR prepaid card account providers adhere to most or all Regulation E requirements, they are not legally required to do so.

A slightly modified form of Regulation E tailored specifically to electronic accounts was extended to payroll cards by the Federal Reserve in 2007. Payroll cards allow employers to offer their employees without bank accounts a way to directly deposit their wages and, like GPR prepaid card accounts, often serve as bank account substitutes. Then, at the end of 2010, the U.S. Treasury Department released an interim final rule requiring all prepaid cards that receive federal payments (income tax refunds, Social Security benefits, etc.), including GPR prepaid card accounts, to meet certain consumer protection criteria, including full FDIC deposit insurance and all requirements that apply to payroll cards under Regulation E. As a result, most major GPR prepaid card account providers are now formally offering these protections to their customers.

Additional consumer protections apply to other types of prepaid cards and credit cards. The Fair Credit Billing Act (FCBA) provides legal protections for credit cards concerning the correction of billing errors and dealing with fraud that are similar to those for bank accounts.

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5 ChexSystems is a consumer-reporting agency that banks turn to for information about consumers who may have had negative or suspicious banking activity in the past five years. Most banks will not open a deposit account for potential customers who are in the ChexSystems database.
6 For more detailed information on the basics of GPR prepaid cards, please see CFSI’s The Nonprofit’s Guide to Prepaid (September 2010), http://cfsinnovation.com/intelligence/nonprofitguide.

under the EFTA. Under the FCBA, consumer liability is limited to a maximum of $50 if they notify their credit card company within sixty days of the statement, with the error in question, being sent. Consumers are also allowed to dispute a broader range of billing errors with credit cards than debit cards, which include goods or services not accepted by the cardholder or not delivered as agreed. Last year, the Credit Card Accountability Responsibility and Disclosure Act, which contains regulations for prepaid gift cards, went into effect. Specifically, these regulations apply to both open and closed loop gift cards, but not to reloadable prepaid card accounts. The regulations prevent gift cards from expiring in less than five years and restrict charges for dormancy, inactivity, and service fees.

This disparity in consumer protections among various types of payment cards, coupled with the growth in GPR reloadable prepaid cards has begun to generate discussion in both the media and among policymakers about the need to extend consumer protections to GPR prepaid card accounts. Legislation to this effect was introduced in Congress at the end of 2010, and proposals have been floated by both industry and consumer groups. Effective July 21, 2011, the Consumer Financial Protection Bureau (CFPB) will have regulatory oversight of GPR prepaid card accounts.

CFSI has been studying the evolution of the prepaid card industry since 2004. CFSI has supported the development of high-quality and affordable GPR prepaid card accounts as a valuable and necessary tool for the financially underserved. CFSI has analyzed the consumer protections applicable to GPR prepaid card accounts, as well as alternative payment mechanisms, and has consulted with a wide variety of stakeholders, including policymakers, consumer advocates, and industry representatives. As a result, CFSI recommends the following extensions of consumer protections to GPR prepaid card accounts:

1) Mandate FDIC pass-through insurance.

2) Extend Regulation E as applied to payroll cards and enhance the protections by lengthening the period for which transaction history is available and enabling consumers to make a single request for ongoing paper statements.

3) Require a standardized fee-disclosure box.

Both the pass-through insurance and extension of payroll card Regulation E could be implemented quickly. While CFSI believes research concerning consumer comprehension and utility is needed to develop a standardized fee-disclosure box, as well as to confirm that the proposed Regulation E enhancements would be useful and cost-effective, that work should also start.

as soon as possible. In addition to taking these specific actions, regulators should establish an ongoing process to monitor developments in financial capability and in the prepaid card industry, including increased functionality and integration with mobile technologies. This will encourage responsible product development and a level of regulatory intervention that enhances consumer access to quality products. CFSI believes these recommendations provide strong and appropriate protections for consumers without dampening access to these products or innovations to better serve the underbanked.

1) Mandate FDIC Pass-Through Insurance

Deposit Insurance for Bank Accounts and GPR Prepaid Card Accounts

Deposit insurance is one of the most fundamental consumer financial protections. Created during the Great Depression, it ensures that if a bank fails, consumers do not lose everything in their accounts. The Federal Deposit Insurance Corporation (FDIC) insures deposits in bank accounts for up to $250,000, and the National Credit Union Association (NCUA) does the same for share accounts at credit unions. The many bank failures following the recent financial crisis serve as an important reminder of the necessity of this protection, particularly for lower-income consumers who are more likely to be vulnerable if they lose access to the funds in their deposit accounts.

Funds deposited or loaded onto GPR prepaid card accounts are held at a depository, even though that depository is typically not the financial institution providing or servicing the account. As a result, most GPR prepaid card accounts have some form of deposit insurance, at least indirectly. However, the extent to which individual holders of GPR prepaid card accounts are insured varies because GPR prepaid card accounts have a different basic structure than deposit accounts. Deposit accounts (whether demand accounts or savings accounts) are directly owned by individual or joint owners, and thus the deposit insurance directly protects the individual or joint owners. GPR prepaid card accounts, on the other hand, usually have a pooled account structure, with the funds of multiple cardholders (potentially thousands) held in a single account owned by the prepaid card provider. Individual GPR prepaid card account owners have subaccounts within this larger account.

This pooled account has deposit insurance if it is held at an FDIC-insured bank. Depending on the details of the account’s structure, however, each subaccount may be insured up to the full $250,000, like a traditional bank account, or only the pooled account may be insured up to $250,000, providing GPR prepaid account users with much less deposit insurance than a traditional bank account. In 2008, the FDIC General Counsel’s Office issued an opinion affirming that funds loaded onto GPR prepaid card accounts are in fact deposits if held at an FDIC-insured bank. They also issued guidelines to enable...
prepaid card companies and banks to ensure that each individual GPR prepaid card account holder is eligible for the full $250,000 in FDIC deposit insurance, also known as “pass-through” insurance.12 These guidelines dictate that the custodial nature of the account must be disclosed in the records at the depository; the identity of individual GPR prepaid card account owners and exact amount each owns must be recorded and disclosed; and there must be a clear agreement between the prepaid card company and the individual account holders that the individuals are the actual owners of the deposits.13

Recommendation: Mandate FDIC pass-through insurance.

In the current GPR prepaid card account marketplace, the availability of pass-through insurance is inconsistent. Some prepaid card providers do not offer deposit insurance at all, others claim to offer FDIC insurance but do not offer pass-through insurance, and others offer full FDIC pass-through insurance. To avoid confusion and ensure that the funds of all GPR prepaid card account holders have this basic consumer protection, all GPR prepaid card accounts should be required to have full FDIC insurance. Additionally, the FDIC logo should be displayed prominently on prepaid card providers’ websites and on the card packaging in retail locations so consumers can be aware that their funds are fully insured. GPR prepaid card accounts issued by credit unions should also be required to have full NCUA share insurance and display the NCUA logo in a similar manner.

For depositories and prepaid card providers who do not already provide it, pass-through insurance is relatively easy to offer. Its value to GPR prepaid card account holders, who tend to have lower incomes and be more risk averse concerning their finances, is much higher than the cost of compliance. Additionally, taking this step may well make the product more attractive to current users and draw in additional financially underserved consumers.

2) Extend Regulation E as Applied to Payroll Cards

Regulation E and the Current State of Protection

Regulation E implements the Electronic Fund Transfer Act (EFTA), which outlines the rights and liabilities of consumers and the responsibilities of financial institutions and other providers regarding electronic funds transfers. Most credits or debits from a consumer’s account that involve a computer, telephone, ATM, or other electronic device are classified as electronic funds transfers. Examples include payments made with a debit card, direct deposit, wire transfers, and direct debit payments. Some of the major consumer protection provisions in Regulation E include requirements for disclosures by financial institutions regarding account terms and conditions, consumer liability limits for errors or fraudulent transactions, rules for change-in-terms notices to consumers, required procedures for investigating and resolving errors and fraud, and rules relating to overdraft services. These are some of the most important and basic consumer protections for card-based payments.

As noted, Regulation E applies to debit cards linked to bank accounts, and a slightly modified version applies to payroll cards, but GPR prepaid cards are currently not explicitly subject to it. Many of the major prepaid card providers already adhere to most of the major provisions of the version of Regulation E that applies to payroll cards, and the U.S. Treasury Department also requires GPR prepaid card accounts that receive federal payments to adhere to Regulation E as it applies to payroll cards.

In addition, major payment networks such as Visa and MasterCard provide zero liability protection for fraudulent charges to GPR prepaid card accounts. Visa, for example, offers a provisional credit to cover any losses from unauthorized use within five businesses days after the loss is reported.14 However, these protections are limited. Both Visa and MasterCard’s zero liability protections apply only to signature transactions; they do not apply to PIN transactions. Visa’s policy also does not apply to ATM transactions. MasterCard’s policy does not apply if a cardholder has reported more than two unauthorized purchases in the last 12 months and in some cases if the card has not been registered beforehand.15

In contrast to this variety of protections, the liability protections under Regulation E are more consistent and comprehensive, applying to all types of electronic

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12 Most GPR prepaid card accounts have maximum balance limits much lower than $250,000. However, for simplicity’s sake, it makes the most sense to extend the same level of deposit insurance to GPR prepaid card accounts as is currently available for deposit accounts.
transfers. Under Regulation E, a consumer’s liability is capped at $50 if they report a lost or stolen card to their financial institution within two business days of learning of the occurrence. If the consumer takes longer than two business days to report the loss, the maximum liability is $500. If a consumer takes longer than 60 days to report a lost card or an unauthorized transaction on their statement, they could be responsible for all subsequent fraudulent transactions after that date until they notify the financial institution. If there are extenuating circumstances for a delay in reporting an incorrect charge, the deadlines must be extended. Once a consumer reports an unauthorized transaction, the financial institution has up to 10 business days to resolve the dispute or issue a provisional credit, so the consumer is not denied access to their funds for too long while the financial institution resolves the matter. Regulation E also offers a broader range of protections for consumers than just limits on liability and resolution procedures for unauthorized transfers.

### Regulation E for Payroll Cards Versus Regulation E for Debit Cards

There are two key differences in Regulation E requirements for payroll cards versus those for debit cards linked to checking accounts. The first pertains to account statements and information, and the second involves error resolution.

In the case of debit cards, Regulation E requires financial institutions to send regular account statements to customers detailing all their transactions, either by mail or, if consumers have given consent, by email. In the case of payroll cards, Regulation E does not require financial institutions to send account statements to consumers. Instead, card providers are required to deliver the same account information by making a telephone number available for consumers to call for their current account balance, and they must also provide an electronic history of account transactions from at least the past 60 days through a website or other electronic means. Consumers who prefer a paper account statement can still receive one on request.

The second key difference involves the error resolution process. As described above, under Regulation E a consumer’s liability for unauthorized transactions depends on how soon they report the unauthorized transactions to their financial institution. If a consumer takes longer than 60 days to report an unauthorized transaction, they could be responsible for all subsequent fraudulent transactions after that date until they notify the financial institution. For debit cards, this time period begins when the financial institution sends the account statement to the consumer, such as the mailing date. For payroll cards, the period begins when the consumer electronically accesses the account, by logging in on a website, for example—unless the consumer has requested a paper statement, in which case the same rule applies as for debit cards. The payroll card version of this rule allows consumers more time to respond, since they can potentially see the error the same day the reporting time period begins, by accessing the account online. For paper statements, the time between mailing and receipt cuts into the reporting time period. If a payroll card user does not access their account within 120 days of an unauthorized transaction, the financial institution is no longer required to limit the liability of the consumer for that transaction.

**Recommendation: Extend Regulation E as it applies to payroll cards to GPR prepaid card accounts.***

To ensure that all GPR prepaid card account holders have the same basic and comprehensive protections, Regulation E should be applied to all GPR prepaid card account products. Because payroll cards are the type of payment card most similar to GPR prepaid card accounts, it is appropriate to use the payroll card model for applying Regulation E to GPR prepaid card accounts. This would ensure that the application of Regulation E requirements is tailored to the consumers who use them, and that compliance by prepaid card providers and depositories is feasible and realistic.

Applying the payroll card version of Regulation E to GPR prepaid card accounts is also consistent with the application of those rules to prepaid card products created by the U.S. Treasury Department for the electronic delivery of Federal government benefits and payments. These programs include the Direct Express Debit MasterCard program that allows unbanked social security recipients to receive their benefits electronically, and the recently launched MyAccountCard Visa Prepaid Debit Card pilot program, which allows select low-income tax filers to sign up for a GPR prepaid card account to receive their income tax refunds electronically.16

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Consumers are increasingly using computers and mobile phones to check their bank account and GPR prepaid card account transactions. Not only is this often more convenient, but it also allows consumers to detect errors or fraudulent transactions without having to wait for monthly paper statements. Lower-income consumers—and GPR prepaid card account users tend to be among them—are no exception to this trend, even though they typically are less likely to use or have access to the internet. The electronic delivery of account information will only increase in importance and relevance as mobile phones and other access devices become more sophisticated and cheaper and Americans grow more comfortable and familiar with banking online. However, some consumers will always prefer paper statements, and this option should also be readily available at a reasonable cost when requested.

**Recommendation: Expand the 60 days of transaction records to one year.**

In addition to extending Regulation E as applied to payroll cards to GPR prepaid card accounts, we also recommend further improvements in Regulation E for both payroll cards and GPR prepaid card accounts. For example, given that the default means for consumers to access their transaction history is electronic and that they have at least 120 days to report an unauthorized transaction, it would be logical to extend the current minimum of 60 days of transaction records that financial institutions are required to make available to at least 120 days. That would give consumers more opportunity to detect errors. In fact, given that consumers are increasingly turning to GPR prepaid card accounts as bank account substitutes, it would be prudent to make transaction records available for even longer, such as six months or one year. This would enable consumers to see their transaction behavior over the long-term and allow better budgeting and more informed financial decisions. Given technological advances, the compliance cost to prepaid providers to store additional electronic records is also relatively small, and as long as the records are easily accessible for consumers, they could be stored in an active or archival format.

**Recommendation: Allow consumers who opt in for paper statements to choose to receive a single statement or ongoing paper statements.**

Under Regulation E for payroll cards, account transaction information is made available electronically, and consumers who want a paper copy must request it. Some prepaid providers give consumers the option of either receiving a one-time paper statement or regular monthly paper statements when they make their request. Others require consumers who want ongoing monthly paper statements to call or write each month. Consumers should be able to request either of these options with only one phone call, letter, or email, and at a reasonable cost. Additionally, consumers who request regular monthly paper statements should continue to receive them for each month there is financial activity in the account, until the account is either closed or the consumer requests no more paper statements.

**Recommendation: Regulators and industry should study and leverage advances in technology and insights in financial capability to improve the delivery of account information.**

Technological advances have created new and more effective means for financial institutions to inform consumers about their financial activity, alert them to potential unauthorized transactions, help them make more informed financial decisions, and encourage healthier financial behavior. For example, most major banks and prepaid card providers now give customers the option to receive text message or email alerts about their account activity. These alerts can often be customized for different situations, such as a low balance, direct deposit credit, or a large single transaction amount. This type of real-time information can help consumers budget better, avoid overdrafts, and quickly detect fraud. It is also a relatively easy and inexpensive service for most financial institutions to provide and may save them money in the long run by reducing the costs of fraud through early detection.

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17 According to a study by the Pew Internet & American Life Project, from 2009 to 2010, those with incomes below $30,000 a year were the fastest-growing income segment in terms of wireless internet use, either through a laptop or mobile phone, with 46 percent of that income segment reporting wireless use (The Pew Internet & American Life Project, "The current state of wireless internet use" (May 2010), http://www.pewinternet.org/Reports/2010/Mobile-Access-2010/Part-1/The-current-state-of-wireless-internet-use.aspx). According to another study by Pew, sixty-three percent of Americans with incomes below $30,000 a year use the internet in general (The Pew Internet & American Life Project, Demographics of internet users (May 2010), http://www.pewinternet.org/Trend-Data/Who’s-Online.aspx).

18 In 2010, CFSI and the Ready Credit Corporation conducted an experiment that provided targeted financial advice to a select group of Ready Credit customers via email to see whether it would positively impact their financial behavior. Overall, customers who opened the emails tended to show significant positive changes in the targeted behavior. The experiment was small and not designed as a formal study, but it does demonstrate the potential benefits that this type of financial communication and information can have on the financial health of consumers. See Can Email Alerts Change Behavior? An Experiment by Ready Credit Corporation (June 2010), http://cfsinnovation.com/node/440544.
This provides much greater utility to consumers than the paper statements currently required under Regulation E, which are not timely and can be easily overlooked.

Regulators such as the CFPB should monitor and foster industry innovations and developments like these through research. Eventually, if appropriate, and after weighing the cost and benefits to both consumers and financial institutions, they should also consider incorporating some of these developments into established consumer protection regulations, such as Regulation E, to guarantee that all consumers have access to them. Financial institutions should continue to innovate and use new technology to help customers be better informed about their account activity and make sound financial decisions.

3) Improved Fee Disclosure

Inadequate Fee Disclosure in the Current Marketplace

Another important area of consumer protection is fee disclosure. The number and types of fees associated with GPR prepaid card accounts and the amounts of these fees vary widely. Some cards have minimal fees and can be used so that very few fees are charged, while others impose fees for almost every individual feature or service. The extent of fees depends on the prepaid card company, the specific GPR prepaid card account product, and how the card is used. Recently the issue of GPR prepaid card account fees caught the attention of the national media when a card with excessive fees, endorsed by the celebrity Kardashian sisters and targeted toward youth, was introduced. After a backlash, the card was quickly pulled from the market. Policymakers also responded. U.S. Senator Robert Menendez (D-NJ) introduced legislation last year that would apply consumer protections to GPR prepaid card accounts, including greater fee disclosure.19

Despite the wide disparity in fees, the overall level and number of fees have continued to drop over time with market growth, competition, and innovation, and will most likely continue to do so. However, regardless of the current downward trend in fees, there are still some bad actors in the marketplace, and steps can be taken to improve fee disclosure. Regulation E contains guidelines for the disclosure of fees for both bank accounts and payroll cards. They are, however, often buried in several pages of terms and conditions, written in legal language, and largely overlooked by consumers. Consumers need to be able to determine more easily what the true cost of a product will be and how all the individual features and services available impact that cost. Furthermore, consumers often cannot obtain a comprehensive list of all the potential fees associated with a GPR prepaid card account before deciding which one to purchase. Even if they did obtain such a list, comparing all fees among different cards in an apples to apples manner would be almost impossible.

Recommendation: Require a standardized fee disclosure box for all GPR prepaid card accounts.

The most effective way to improve fee disclosure is by requiring all GPR prepaid card account providers to list all the fees for their products in a standardized and easy-to-understand box. This is similar to the Schumer Box, a standardized summary of all the major costs of a credit card, which is required by the Truth in Lending Act (TILA) to be included with every credit card offer.

To be effective, all the GPR prepaid card account fees would have to be listed in the box in a standardized format, so that consumers could easily compare total costs. The box would contain the name, amount, and a brief description of each fee. It would also be clearly displayed on the packaging of all GPR prepaid card accounts sold in retail locations and prominently displayed on the websites of prepaid card companies. Requiring GPR prepaid card account providers to list all their fees in this manner would force the industry to move toward less complex fee structures and fewer fees overall. By making the product clearer, more transparent, and easier for consumers to understand, this feature could spur greater competition among providers based on factors that provide the greatest value to consumers such as costs and features.

The key consideration in designing the box would be its format. Rather than just a list, fees should be organized by categories, such as type or setting, to make the box useful and easy to understand for consumers. For example, fees organized by type might include the following categories: Starter Fees (Activation and Personalized Card); Deposit Fees (Direct Deposit, Cash, and Check); Purchase/Withdrawal Fees (ATM, POS, Bill Pay); Information Fees (Customer Service, Paper Statements, and Balance Inquiry); Automatically Reoccurring Fees (Monthly and Credit Building); Penalty Fees (Overdraft and Replacement Card); International Fees (Currency Conversion); and Closing Fees (Cancellation). Organized by setting, fee categories might include: At the ATM, At the Store, On the Phone, Online (Mobile or Computer), Outside the U.S., and Standard or Reoccurring Fees.

Neither of these examples is a comprehensive list of categories or fees, but rather examples of how a fee box could be organized. The exact format of the box should be determined through consumer research and testing by the CFPB. This should include survey or focus group work with underserved consumers who use these products to find out which format best communicates their true cost. The CFPB should also consult with members of industry who have done work with fee disclosures to learn from their experiences. Many of the major prepaid card companies have already taken steps to put fee boxes or charts like these on their websites, but not all of them have, and it is not always easy to compare fee boxes from different companies.

For a box to be effective, there has to be a tradeoff between the amount of information it contains and its simplicity. But additional fee disclosure information could be available through different sources. The CFPB could provide further fee disclosures via its website. For example, the CFPB could calculate and post the average or median fees in various categories across the industry. Then consumers could see where the price for each service and feature falls for a specific product compared with the industry average or median.

Recommendation: Regulators and industry should study and leverage advances in technology and insights in financial capability to improve fee disclosure for GPR prepaid card accounts.

Another voluntary step that prepaid card companies could take to help consumers choose among GPR prepaid cards is to offer a fee calculator on their websites. This calculator could take multiple forms and is an area of potential innovation for prepaid card companies. A basic calculator could simply let consumers choose which services and features they use each month and how often they use them and then give a personalized average monthly cost for comparison purposes. A more sophisticated average monthly fee calculator might resemble an online interview process, similar to how online tax preparation services and retirement planning tools work. The calculator or service could take consumers through a brief series of questions...
about their financial service needs and habits to estimate their average monthly cost of using the product. It might also offer tips for saving money or avoiding certain fees.

Prepaid card companies could also move beyond pure disclosure and information and into the realm of financial capability. For example, to build on the text message alerts described above, they might send a message warning consumers about to make a withdrawal at a non-network ATM that they could avoid a fee by using an in-network ATM instead. As technology advances, this text message might provide the location of nearby in-network ATMs as well. This is just one example of how the principles and lessons of financial capability could be used to help consumers make more informed decisions when it comes to fees. Beyond issuing fee disclosure rules, the CFPB should also promote research and best practices in this area, and perhaps consider additional new regulations if warranted and after weighing the cost and benefits to both consumers and industry.

NEXT STEPS

GPR prepaid card accounts are becoming the primary transaction account for millions of Americans underserved by the traditional banking system. While the cards have to date largely been issued by non-banks, depository institutions are showing increasing interest in the product. It is important that consumers who use GPR prepaid card accounts have clear and consistent consumer protections. CFSI recommends that those protections be adopted in three phases:

• Within the next six months, the FDIC should require (through regulation or otherwise) that all GPR prepaid card accounts have full pass-through insurance and the CFPB should extend payroll card Regulation E to GPR prepaid card accounts.

• Also within the next six months, the CFPB should call for public comments on ways to improve fee disclosure for GPR prepaid card accounts. In a timely manner after receiving input from all the relevant stakeholders, conducting research, and careful consideration, they should issue final fee disclosure regulations, with a limited but reasonable implementation period.

• The CFPB, working with industry and consumer stakeholders, should continue to monitor developments and research in financial capability and GPR prepaid card accounts. They should ensure that consumer protection regulations keep pace with developments without hindering access to the products or continued innovation.

These steps will ensure that all GPR prepaid card accounts have strong, basic consumer protections. They will also help to eliminate undesirable practices or fees associated with some products and improve the industry overall. By creating certainty at a high level of quality, improved regulations will increase the value of GPR prepaid card accounts, enlarging the market and the number of underbanked consumers it serves. This is not just a matter of making payments easier and safer. Beyond providing a high value and low-cost transaction account to underbanked consumers, GPR prepaid card accounts have the potential to enable consumers to access important asset-building financial services, such as savings tools, thus putting consumers on the path to greater financial stability and prosperity.

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20 For more information on financial capability, please see Joshua Sledge, Jennifer Tescher, and Sarah Gordon, From Financial Education to Financial Capability: Opportunities for Innovation, CFSI (March 2010), http://cfsinnovation.com/node/440486.
SOURCES


About CFSI:

The Center for Financial Services Innovation is the nation’s leading authority on financial services for underbanked consumers. Through insights gained by producing original research; promoting cross sector collaboration; advising organizations and companies by offering specialized consulting services; shaping public policy; and investing in nonprofit organizations and start-ups, CFSI delivers a deeply interconnected suite of services benefiting underserved consumers. Since 2004, CFSI has worked with leaders and innovators in the business, government and nonprofit sectors to transform the financial services landscape. For more on CFSI, go to www.cfsinnovation.com

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