

To the Point!



Summary of CFPB Proposed Rule for Prepaid Products

The Consumer Financial Protection Bureau (“CFPB”) has issued a proposed rule that would bring prepaid products under the Electronic Fund Transfer Act (“EFTA”) and make the protections currently afforded to credit cardholders under Regulation Z applicable when credit features are obtained in connection with a prepaid account (the “Proposed Rule”). The Proposed Rule would apply to traditional plastic prepaid cards as well as mobile and electronic prepaid accounts, payroll cards, tax refund cards, student financial aid disbursement cards, peer-to-peer payment products, and certain government benefit cards such as those used to distribute unemployment insurance, child support payments and pension payments. The protections under the Proposed Rule would be triggered upon the consumer’s registration of the prepaid product with the institution that provided it.

Under the Proposed Rule, consumers who obtain prepaid products would be subject to the protections of the EFTA including error resolution rights, fraud and lost-card protection including limited liability for unauthorized charges, and either periodic statements or access to their account information online for free. The Proposed Rule also includes new “Know Before You Owe” disclosure requirements, including both a long and a short-form disclosure, which must be accessible to consumers before acquiring the prepaid product. In addition, the Proposed Rule would require prepaid account issuers to post their account agreements on their websites and to submit those agreements to the CFPB to be posted on its website.

When consumers use a credit feature in connection with their prepaid account, the protections for credit cardholders under Regulation Z would apply. This means financial institutions that offer prepaid products must assess the consumer’s ability to repay before approving a credit feature, provide a monthly credit billing statement, and allow consumers 21 days to repay before charging a late fee. The fee and interest charge limitations applicable to credit cards would also be applicable to prepaid product credit features, including notice of any interest rate increase 45 days in advance and a limit on the total fees that can be charged during the first year to 25 percent of the credit limit.

The Proposed Rule also included some additional protections to ensure that credit features are separate and distinct from the prepaid account. Prepaid product issuers would not be permitted to offer credit features to prepaid account holders until 30 days after the consumer registers their prepaid account with the institution, and would be prohibited from automatically taking funds from the prepaid account to repay a credit balance unless the consumer has affirmatively elected this repayment option. In that case, the issuer would only be able to take funds from the prepaid account once per calendar month and could not require repayment of the credit sooner than 21 days after mailing the billing statement.

In his prepared remarks on the Proposed Rule, CFPB Director Richard Cordray pointed out that prepaid product users are disproportionately unbanked and under-banked households and tend to be economically vulnerable thus the CFPB views it as crucial to close the gaps in the regulation of prepaid products and ensure that these consumers have strong protections under the law. Although Director Cordray noted that most prepaid cards do not currently have credit features, the CFPB is concerned that credit features offered in connection with prepaid products will lead to consumer abuses particularly where consumers have chosen a prepaid product to avoid incurring debt or have lost a bank account because of the same.

Financial institutions that offer prepaid products should familiarize themselves with the Proposed Rule and the proposed “Know Before You Owe” disclosures. The enactment of the Proposed Rule would bring comprehensive regulation into an area that has been largely unregulated to this point and represent a sea change for those institutions that are not already familiar with the

requirements of EFTA and Regulation Z. The CFPB will be accepting comments on the Proposed Rule for 90 days following the date it is published in the Federal Register, and we encourage financial institutions to review and comment on the Proposed Rule.

Chapman and Cutler LLP

Attorneys at Law • Focused on Finance®

To the Point! is a summary of items of interest and current issues for financial institutions with primary focus on regulatory, consumer, and corporate issues. Chapman maintains a dedicated practice group with the experience to counsel on these issues and other enterprise risk management matters facing financial institutions. If you would like to discuss any of the items contained in these briefings or other legal, regulatory, or compliance issues facing your institution, please contact one of the partners in our Bank Regulatory Group:

Marc Franson • 312.845.2988

Scott Fryzel • 312.845.3784

Heather Hansche • 312.845.3714

Doug Hoffman • 312.845.3794

John Martin • 312.845.3474

Dianne Rist • 312.845.3404

Judy Chen • 312.845.3716

Lindsay Henry • 312.845.3869

This document has been prepared by Chapman and Cutler LLP attorneys for informational purposes only. It is general in nature and based on authorities that are subject to change. It is not intended as legal advice. Accordingly, readers should consult with, and seek the advice of, their own counsel with respect to any individual situation that involves the material contained in this document, the application of such material to their specific circumstances, or any questions relating to their own affairs that may be raised by such material.

To the extent that any part of this summary is interpreted to provide tax advice, (i) no taxpayer may rely upon this summary for the purposes of avoiding penalties, (ii) this summary may be interpreted for tax purposes as being prepared in connection with the promotion of the transactions described, and (iii) taxpayers should consult independent tax advisors.

© 2014 Chapman and Cutler LLP. All rights reserved.

Attorney Advertising Material.