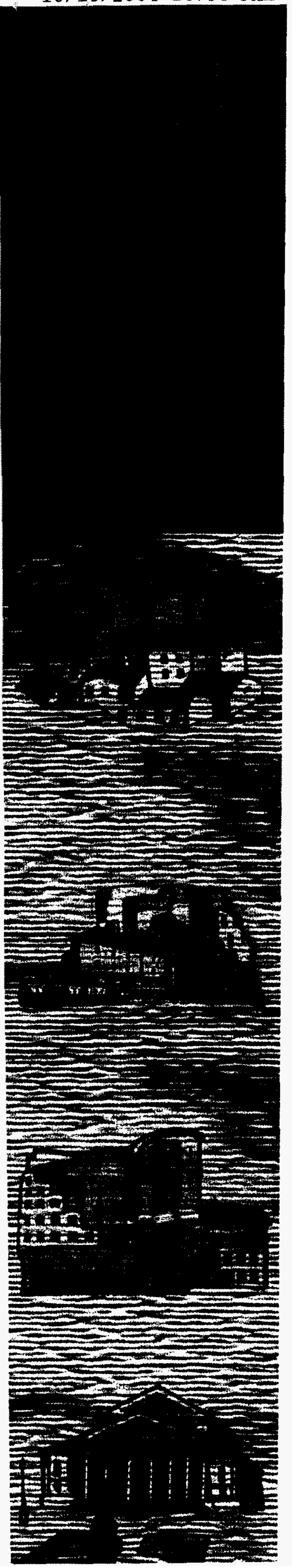

WILLIAM E. HULT
President

EDWARD F. MONCRIEF
Executive Director

Comments of:
Consumers Union of U.S., Inc.
Consumer Federation of America (pending)
National Consumer Law Center (pending)
U.S. PIRG (pending)

October 19,2004

Jennifer L. Johnson, Secretary
Board of Governors
Federal Reserve System
20th and Constitution Ave., N.W.
Washington, DC 20551

By email: regs.cornrnents@,federalreserve.gov
Or by fax: 202-452-3819

Re: Docket No. R-1210

Dear Ms. Johnson,

The consumer, community development, and civil rights groups making these comments strongly support the proposed amendment to federal Regulation E addressing payroll cards. The amendment would define a payroll card account directly or indirectly established by an employer to receive wages, salary, or other employee compensation on a recurring basis as an account which receives the consumer protections of the federal Electronic Fund Transfer Act. While we strongly support this amendment, it is too narrow. The amendment should be expanded to cover other kinds of stored value cards which hold funds important to consumers and families, including prepaid debit cards marketed or used as account substitutes, child support cards, unemployment cards and tax refund related cards.

These comments:

- Strongly support the amendment to expressly include payroll card accounts under the EFTA.

- Ask the Board to strengthen the amendment by covering all cards which deliver employee compensation, even if that compensation is not "recurring."

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- Ask the Board to expressly cover child support cards, unemployment cards, and tax refund or refund anticipation loan proceeds cards.
- Ask the Board to clarify that recurring payments into an account are not a precondition to meet the general "consumer asset account" standard set forth in Regulation E.

1. This Issue is Important

Consumer, community development, and other organizations serving low and moderate income consumers are deeply interested in consumer protections for payroll card holders and for consumers holding other types of stored value cards which consumers use as substitutes for bank accounts, or on which consumers receive important household funds. These cards, sometimes called "stored value cards," "prepaid debit cards" or "pooled debit cards" are increasingly being offered to and used by lower and moderate income consumers as a substitute for a traditional bank account. Lower-wage workers can be paid by payroll card, single-parent households may receive child support payments distributed by stored value card, persons may receive unemployment payments through a state benefits card, consumers may receive tax refunds or the proceeds of tax refund anticipation loans on a card, and a consumer may place funds needed to support his or her household on a prepaid debit card that the consumer purchases from a check casher, bank, or other entity. Consumers can even arrange for their wages to be directly deposited onto an individual prepaid debit card. These are the very households who can least afford to be deprived of funds, or to experience delayed access to funds, due to an error, a theft or an unauthorized transaction using the consumer's card or card number. The funds accessed through these cards are needed to pay rent or a mortgage, to buy food, and to pay bills.

On June 23,2004, twenty-six national and local consumer, community, and labor groups asked the Federal Reserve Board to act to clearly apply EFTA consumer protections to all payroll cards and to certain other types of stored value cards. We incorporate that letter by reference into these comments. It is posted at:
http://www.consumersunion.orcr;/pub/corefinancial_services/001205.html

A delay in access to funds or a loss of funds due to non-application of the protections of the federal Electronic Fund Transfer Act (EFTA) to a payroll card or to another kind of stored value card holding significant household funds could trigger eviction, a negative mark on a credit record, and hungry children. Lower-income and many middle-income families simply do not have the assets to cushion against even a temporary interruption of funds. In the year 2000, significant numbers of **U.S.** households had negative or zero net worth, including 27.6% of Hispanic households, 29.1% of Black households, and 11.3% of White Non-Hispanic households. An additional 6.7%; **7.3%;** and 4.7% of these households respectively had net worth ranging from $1 to $4,999 including equity in the family car. B. Robles, ***Economic Opportunity: Family Assets,*** June 2003, a report prepared for the Annie E. Casey Foundation, www.utexas.edu/lbj/faculty/robles/research. These families simply can't afford to be without access to their household funds because of a problem with a payroll card, child support card, unemployment benefits card, tax refund related card or a prepaid debit card.

It is essential that the federal consumer protections of the EFTA clearly apply to stored value cards that serve as account substitutes or that hold significant household funds. The proposed amendment accomplishes this for payroll cards. Without a clarifying amendment to Regulation E, the level of protection for consumers ranges from ambiguous to nonexistent, which leaves unbanked consumers in the position of being offered a significantly inferior product carrying significantly higher risks—an electronic payment mechanism that may lack the baseline consumer protections available to other debit-based electronic payment mechanisms.

2. The payroll card proposal has many positive aspects

For these reasons, we strongly support the proposed amendment to federal Regulation E to define a payroll card account as a type of account clearly covered by the EFTA. It is important that the proposed amendment would cover ***all*** employee compensation funds placed in any card account established by the employer if the account receives recurring employee compensation funds, including recurring commissions or wages. We also strongly support the language of the proposed amendment which covers all payroll card accounts regardless of whether they are operated and managed by a financial institution, employer, or other entity. We are also pleased to see that the proposed amendment treats payroll card accounts equally with other consumer accounts for all purposes under the EFTA, including the requirement for a periodic statement. Lower-paid workers need to know how much is left in their card accounts, and all cardholders need statements to monitor their accounts and to discover unauthorized use of their cards or card numbers.

3. The Board should strengthen the amendment in three ways

A. Eliminate or modify the restriction to "recurring" employee compensation

Despite our strong support for the proposed amendment, we ask the Board to strengthen it in three ways. The first concerns the restriction to payroll cards to which "recurring" employee compensation is paid. This appears to exclude an initial payment that is meant to be recurring if the job ends during the first pay period. It would also exclude wages for a short-term job which is begun and completed within a pay period. It would exclude a non-recurring bonus payment, even if that bonus is a significant percentage of the monthly or annual total wage. Non-recurring bonuses and payments for short-term jobs can be an important part of household income. A person who works for just one pay period and receives a payroll card might not qualify under the "recurring" payments language of the amendment, and yet that person needs security for his or her wages just as much as a person who is employed for a longer time. A person who works for a temporary agency might be given a new card every two weeks, circumventing the policy underlying the amendment.

Because short-term jobs can be an important income source for households, we respectfully request that the phrase "on a recurring basis" be deleted from the proposed amendment. If this change is not made; then in the alternative, the amendment should be modified to make it clear that payroll card accounts are covered when they contain funds from pay or from bonuses which may recur, whether or not there has yet been an actual recurrence. This would cover the first pay period, before it is known if there will be a recurrence, and would also cover bonuses that can occur on a periodic basis, even though those bonuses are not guaranteed. The staff interpretation could also make it clear that a card issued by a temporary agency is included even if the employee actually works only one pay period. The proposed change, if "recurring" is not simply eliminated, is to change the language of the proposed amendment from "are made on a recurring basis" to "are or may be made on a recurring basis."

B. Expand the amendment to cover stored value cards marketed or used as account substitutes

We **ask** that the amendment be augmented to apply Regulation E not only to payroll cards established directly or indirectly by an employer, but also for other kinds of stored value cards marketed or used as a substitute for a traditional bank account. Consumers may place hundreds or even thousands of dollars on these cards. These cards are marketed as account substitutes, and consumers are even invited to directly deposit wages or Social Security payments to some of these cards. See, for example, **https://www.rushcard.com/how.html.** If the reason that these cards are not included in the proposed amendment is that the Board believes that they are already covered by the EFTA, the official staff interpretations should be augmented to say so. If these cards are not already covered in all instances, then Regulation E should be amended to cover them.

We are concerned that the failure to clarify coverage for prepaid debit cards on which consumers place significant amounts of funds relative to household disposable income may place at a disadvantage those consumers who seek the convenience of a card-style account substitute but whose employers do not offer a payroll card. If the employer encourages, directs, or steers the employee to a third-party card for the direct deposit **of** wages, such conduct would constitute "indirect" establishment of the account by the employer, and so that account would be covered, However, if an employer simply does not offer a payroll card, a consumer may be marketed directly by a prepaid debit card offeror, induced to directly deposit his or her wages to the prepaid card account, and then find the offeror asserting that the card does not provide EFTA protections because it draws from a pooled account held or managed by the card issuer.

We suggest that all stored value cards which are marketed or used ***as account substitutes*** be expressly covered by Regulation E. This request does not extend to single-retailer **gift** cards or low dollar value general use cards. Those cards **are** not marketed or used **as** account substitutes. The reasoning provided by the Board's proposal for the amendment to define and cover payroll card accounts is equally applicable to other types of stored value cards which are offered as substitutes for traditional bank accounts. Cards which function as account substitutes are a mechanism for holding significant household income. Direct deposit of wages, Social Security payments, or other periodic payments onto a stored value card should be conclusive evidence that the card account is being used as an account substitute.

Households using stored value cards as account substitutes are the very households who can least afford to be deprived of funds, or to experience delayed access to funds, due to an error, a theft or an unauthorized transaction using the consumer's card or card number. The funds accessed through these cards are needed to pay rent or a mortgage, to buy food, and to pay bills.

The silence in the proposed regulation about coverage by the EFTA for stored value cards other than payroll cards does not exclude those cards if they meet the broad general definition of an account under 15 U.S. C. section 1693a(2). However, we are concerned that expressly defining payroll cards as one type an account while remaining silent on other, quite similar types of cards could suggest that these other types of card-linked accounts are not covered. We urge the Board to clarify, by amendment to Regulation E or by an addition to the official staff interpretations, that "account" includes all stored value card products which are marketed or used ***as account substitutes*** or which provide significant sources of income or assets to an individual or household.

C. Expand the amendment to cover stored value cards used to receive payments of significant household funds

The proposed amendment clarifies the application of Regulation E only for payroll cards. The amendment leaves important ambiguities for other kinds of stored value cards used to receive payments of funds which are essential for day to day family expenses. We urge the Board to expand the amendment to the definition of "account" to also cover other stored value cards holding funds which constitute a significant source of household income or assets. These other types of cards include unemployment payment cards, child support payment cards, and cards delivering tax refund funds or refund anticipation loan proceeds. The dollar amounts on child support and unemployment cards can be a key source of household income. The dollar amounts on tax refund-related cards can be very significant, particularly for households eligible for the Earned Income Tax Credit.

If the Board believes that government-sponsored cards such as child support and unemployment cards are already covered by the EFTA, so that no amendment to Regulation E is needed, then that interpretation should be specifically stated in the official staff interpretations. Parents receiving periodic child support or unemployment payments via a card, and persons receiving a tax refund via a card, are just as vulnerable to loss of funds from the card account as are workers using payroll cards. We ask that the protections for these consumers be clarified by expressly including all stored value cards carrying significant household assets in the definition of a consumer asset account under Regulation E.

D. Clarify that the "recurring" precondition on the definition of payroll cards has no effect on what other types of stored value cards qualify under the general definition of a "consumer asset account"

Finally, the proposal should make it clear that that any restriction on the definition of payroll card accounts to cards receiving "recurring" employee compensation payments does not impose a "recurring payments" precondition on the types of stored value cards that will be covered under the general Regulation E definition of a "consumer asset account.

4. So-called "zero liability" policies do not satisfy the need for EFTA consumer protections

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Companies marketing prepaid debit cards, that is, non-payroll card type stored value cards, sometimes cite the VISA or MasterCard "zero liability" policies as evidence of the safety of these cards for consumers. However, these policies do not give the same protections as the EFTA, even in the area of lost and stolen cards and unauthorized use.

Both the VISA and MasterCard "zero liability" policies have significant exceptions. They do not confer zero liability on cardholders in all cases. For example, Mastercard's posted policy says that it does not apply if there are two or more instances of theft or unauthorized use of a card in one year. MasterCard's policy also requires that the consumer have taken reasonable care to safeguard the card, and that the card account be in good standing. VISA's posted "zero liability'' policy does not apply when the card is used at an ATM. VISA's policy also does not protect the consumer if the card is used for a PIN-based transaction processed on another network. The consumer can't control whether a thief who gets the card and steals or guesses the PIN chooses to use this information at an ATM or a non-VISA network.

Application of a "voluntary" policy is never as good for consumers as a statutory protection because voluntary policies generally lack an effective means of enforcement. **A** statutory enforcement mechanism provides an incentive to more complete compliance and a remedy for the consumer in the event of non-compliance. Finally, a voluntary policy is subject to the risk of uneven application and to the discretion of employees about how and when to apply the policy, which may disadvantage consumers whose primary language is not English, who are less able to spend time on the phone with customer service due to the nature of their jobs, or who are less able to write a persuasive letter describing the problem – in many cases, the very consumers to whom stored value cards are being marketed as account substitutes.

5. The Board's proposed amendment to Regulation E is provides better treatment of payroll cards than a restriction to those payroll cards to which deposit insurance would apply under the FDIC proposal

The request for comments seeks views on whether the application of federal EFTA consumer protections should depend on the application of FDIC insurance. For payroll cards, it should not. The Board's proposed amendment to Regulation E is cleaner, simpler, and more comprehensive than any approach that is tied to whether or not there is FDIC insurance on the funds in a payroll card accounts. The FDIC deposit insurance proposal is very technical. It does not cover all payroll cards. A key difference between the scope of the FDIC's proposal and the preferable language proposed by the Board for payroll cards is that the Board's language would cover all payroll card accounts, regardless of whether those accounts are operated or maintained by the employer, a non-financial institution, or a financial institution. By contrast, FDIC insurance does not apply to funds held outside of a financial institution. Other actual and potential loopholes in the coverage outlined by the FDIC proposal are described in detail in a June **23,2004** letter submitted by national and local consumer, community, and labor organizations from eleven states and the District of Columbia. That letter can be found at:
http://www.consumersunion.org/pub/corefinancial_services/001376.html.

Here are some examples of ways in which to apply Regulation E protection only to payroll card funds eligible for FDIC issuance (if the FDIC proposal is adopted) would be weaker and

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less complete, for payroll cards, than the amendment proposed by the Board. First, under the FDIC proposal as issued for comment, only stored value cards that enable a cardholder to ***transfer*** funds would be covered. FDIC's proposed section 306.16(f). It would be possible to design a payroll card which could be used only to withdraw funds at ATMs, not to transfer funds to merchants. That card would not be covered by the FDIC proposal. Second, the FDIC proposal would exempt cards where there is no individual sub-accounting by the financial institution on a cardholder-by-cardholder basis. This exemption raises the possibility of a chip-based payroll card with no FDIC insurance protection.

A final example where the FDIC proposal may be less complete than the language proposed by the Board is the potential loophole for coverage created by subsection 303.16(c)(2). Unless modified by the FDIC before it is finalized, this provision appears to contemplate some situations where a consumer could purchase a stored value card directly from an insured depository institution and yet receive a product for which the underlying funds are not insured, due to the nature of the behind-the-scenes arrangement between the bank and the third-party processor under which the bank has prepaid the processor for a card which the bank then sells to the consumer.

We would support a modification to the Board's proposal which retains the specific amendment for payroll cards but also adds an additional specific inclusion in the definition of account for other types of stored value cards for which the underlying deposits are eligible for FDIC insurance.

6. The consumer protections of the EFTA should apply as soon as possible

The Board requested comment on a six month time period for full compliance with the amendment on payroll card coverage. We strongly suggest that the time period be no longer than six months for full compliance, but also that the substantive protections with respect to error resolution and the cardholder's liability for lost cards, stolen cards, and unauthorized transactions go into effect immediately upon adoption of the proposal. Even if financial institutions and others need time to develop and distribute notices, they should be able to act more quickly to provide error resolution and to change any policies that hold consumers liable for more losses than the consumer is liable for under the EFTA. Employees should not have to wait for the substantive protections of liability restrictions and error resolution guarantees for card accounts holding their wages and other employee compensation, even if they do have to wait for notices of these rights.

The payroll card market is growing too fast to subject to employees to any unnecessary delay. The OCC estimates that at the end of 2002, approximately one million families were using payroll cards. ***Payroll Cards: An Innovative Product for Reaching the Unbanked and Underbanked,*** OCC Community Development, October 2003. By May 2004, the Associated Press reported that 1,000 companies were using payroll cards in the **U.S.,** distributing $11 billion annually in payroll and $4 billion annually in employee incentive or commission payments. ***New Payroll Cards Sub for Paychecks,*** Associated Press Online, May 31, 2004. The Board's request for comment, section VII, estimates that there are 2,000 entities involved in providing payroll card accounts to consumers, including employers, financial institutions, and payroll card servicers.

7. Comments to the official staff interpretation on the consumer asset account definition

We suggest some changes to the proposed addition to the official staff interpretation which would exclude a "one-time EFT of salary-related payments." The comment excluding a one-time EFT for a salary-related payment should more clearly state that the exclusion applies only if the one-time payment was provided by a means which was designed so that it could provide ***only*** a one-time payment. In other words, an employer who issues or arranges for a payroll card and then terminates the employee after the first payment of wages has still provided a payroll card account, even though the payment was in fact a one-time payment. Similarly, issuing the employee a "bonus card" to receive **a** bonus plus any unearned future bonuses should still be treated a payroll card account despite for one-time nature of the first bonus. These effects could be clarified by adding "<u>of a type which may not recur</u>" after the first appearance of the phrase "one-time EFT of a salary-related payment." This kind of clarification is also needed to avoid creating an unintended loophole, such as a temporary agency or seasonal employer who might choose to use a new card for each pay period to attempt to avoid meeting of the definition of a payroll card.

We strongly support the rest of the interpretation, which clarifies that all funds in a payroll card account receive the same treatment. We also suggest that the reference in the explanatory material pointing out that card-based payments to seasonal workers are within the definition of a payroll card account be included in the official staff interpretation.

Conclusion

We deeply appreciate the efforts of the Board **of** Governors of the Federal Reserve to make the consumer protections of the EFTA more plainly applicable to payroll cards. We ask the Board to approve this aspect of the regulatory proposal and to extend that same clarity to other types of stored value cards which hold a significant source of household income or assets or which are marketed to or used by consumers as substitutes for bank accounts.

Very truly yours,

Edward F. Moncrie
Edward F. Moncrief
Neighborhood Housing Services Silicon Valley
San Jose, **CA**

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