Comments of

Americans for Financial Reform
Arkansans Against Abusive Payday Lending
Consumer Action
Consumer Federation of America
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National Association of Consumer Advocates
National Consumer Law Center (on behalf of its low income clients)
Public Justice Center (Baltimore)
Reinvestment Partners
Woodstock Institute

submitted to the
Federal Reserve Board

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Regulatory Paperwork Reduction Act of 1996

FRB Docket No. R–1510

Regulation II (interchange fees and prepaid cards)
12 CFR Part 235

March 22, 2016

The undersigned consumer organizations and legal experts submit these comments on improvements needed to modernize Regulation II regarding debit card interchange fees.[1] We urge the Federal Reserve Board (FRB) to revisit the unnecessary limitations on the prepaid card accounts that are eligible for an exemption from Regulation II. As a result of Regulation II, many prepaid card accounts offered by larger financial institutions do not permit links to savings accounts or access to the bank's online bill payment page, features that are especially important for consumers who lack access to safe bank accounts. With the CFPB about to finalize rules to define prepaid accounts and cover those accounts under Regulation E, the FRB should adopt the CFPB's definition and eliminate the Regulation II limitations that restrict prepaid cards to second class accounts.

Regulation II implements the "Durbin Amendment" to the Dodd-Frank Wall Street Reform and Consumer Protection Act. The Durbin Amendment caps the interchange fees that may be charged on debit cards issued by financial institutions with assets over $10 billion. However, in order to protect the availability of prepaid cards for lower income consumers, the statute has an exemption for prepaid cards. That is, the interchange fees on prepaid cards are not limited as long as they meet two conditions in the statute: They may not charge overdraft fees, and they must provide at least one free ATM withdrawal per month.

[1] Organizational descriptions are attached at the end of these comments.

Like the statute, Regulation II exempts prepaid cards that meet certain conditions. Two of these conditions are in the statute: no overdraft fees and one free ATM withdrawal. However, the regulation adds another condition not in the statute: the card must be the sole means of accessing the account. That is, the funds on the prepaid account may not be accessible in any other way, such as by transferring funds to a savings account, by using the bank's online bill payment feature, or through money orders or pre-funded checks that come with the account.[2] These limitations were not in the proposed rule and were adopted in the final rule without any opportunity for notice or comment.

The Regulation II conditions on the prepaid card exemption inhibit the functionality of accounts intended for consumers who need that functionality the most. These consumers are not allowed to link savings accounts to their prepaid cards or to participate in automated savings programs. They cannot use a prepaid card's online bill payment feature or a pre-funded check to pay landlords who do not accept cards. They also cannot use their prepaid accounts to send money to family members.

The FRB adopted these limitations in order to prevent evasions of the interchange fee rules. However, the limitations are not necessary to prevent evasions, because none of the prohibited functions (bill payment, transfers to savings, person-to-person transfers) generates interchange fees. Ironically, Regulation II permits banks to allow consumers to transfer funds from an interchange fee-capped debit card account and spend those funds through an uncapped prepaid card – which could be a form of evasion. Yet banks cannot permit consumers to spend or access prepaid card funds through methods that would be very useful for lower income consumers and that do ***not*** generate interchange fees.

Because of the perverse incentives created by Regulation II, many major banks do not offer fully featured prepaid card accounts. The prepaid cards offered by larger banks mostly have limited functionality. For example, the BBVA Compass ClearSpend Card, the Commerce Bank mySpending Card, the PNC SmartAccess Prepaid Visa Card, the Regions Now Visa prepaid Card, the TD Bank Connect Reloadable Card, the U.S. Bank Convenient Cash Card, and the Wells Fargo Prepaid Card all lack online bill payment on the bank's website or the capacity to make transfers to a savings account.[3]

These accounts lack the features that smaller banks like Green Dot Bank and MetaBank can offer. The Regulation II limitations may become even more problematic if major prepaid card issuing banks grow large enough to be covered by the regulation.

The profit margins on general use reloadable prepaid cards are quite thin. Prepaid card users who use the prepaid accounts as checking account substitutes have lower incomes than the general population and are more likely than checking account holders to earn less than $25,000.[4] Prepaid accounts tend to

[2] A pre-funded check is a check that may not be used until the consumer contacts the financial institution and segregates the funds necessary to cover that check. Once activated, a pre-funded check is essentially a money order.

[3] Source: Survey by the Center for Financial Services Innovation (CFSI), conducted for Thea Garon, James Latta, CFSI, 2016 Prepaid Industry Scorecard (March 15, 2016), available at http://www.cfsinnovation.com/Document-Library/2016-Prepaid-Scorecard.

[4] Pew Charitable Trusts, "Why Americans Use Prepaid Cards" at 3-4 (Feb. 2014), http://www.pewstates.org/uploadedFiles/PCS_Assets/2014/Prepaid-Cards-Survey-Report.pdf. The vast majority of new Chase Liquid customers had no bureau score or a score below 660 when they opened their Chase Liquid accounts. Presentation by Jon Wilk, Chase, to FDIC Committee on Economic Inclusion, http://www.fdic.gov/about/comein/2013/2013-05-16_presentation_wilk.pdf.

have a shorter life than checking accounts. Full interchange revenue may be critical to making these accounts viable and to encourage more banks to offer them.

Banks' inability to generate more interchange revenue on fully functional prepaid accounts may be contributing to the lack of those accounts or banks' failure to aggressively market them.[5] In a recent review by the Consumer Financial Protection Bureau of the top retail banking websites, the CFPB found that nearly half do not appear to offer any deposit account that ensures consumers cannot overdraft.[6] The CFPB also expressed concerned that, even when banks have no-overdraft accounts available, the accounts are not marketed prominently and consumers may not know about them.[7]

The only functionality limits that a prepaid card account should have in order to be exempt from Regulation II are those directly related to the inherent nature of a prepaid card and the overdraft fee ban in the statute. In other words, the account should not have overdraft fees, nonsufficient funds fees, or checks that can bounce. However, pre-funded checks (which effectively become money orders) should be permitted. Distinguishing prepaid cards from checking accounts based on the presence or lack of checks and overdraft fees is consistent with the statute as well as the defining difference between checking and prepaid card accounts.

Thus, the FRB should re-define "prepaid card" in Regulation II as any account that:

- Is offered through a master-subaccount arrangement;
- Is covered by the CFPB's prepaid card rules;
- Lacks overdraft and nonsufficient funds fees; and
- Does not have un-funded checks.

If the FRB still fears evasions, it could put a cap on the amount of regular direct deposits or average balance that an exempt prepaid card account may have in order to prevent the exemption from covering accounts used as bank accounts by wealthier individuals.[8] The FRB could also prevent evasions by prohibiting financial institutions that allow funds to be transferred from an account with capped interchange from offering rewards for spending on prepaid accounts.

Policymakers across the country are working to promote financial inclusion of the millions of underserved consumers. The FRB should eliminate the outdated and burdensome restrictions on prepaid accounts that hinder those efforts at inclusion.

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[5] While Chase recently gave up its Durbin exemption in order to offer more features on its Liquid Card, the bank suffered a heavy cost when doing so. Chase may be less likely to promote its prepaid card account when it can make so much more money off putting a subprime consumer into a traditional checking account where the consumer may incur overdraft fees.

[6] CFPB, Press Release, "Consumer Financial Protection Bureau Takes Steps To Improve Checking Account Access" (Feb. 3, 2016), http://www.consumerfinance.gov/newsroom/cfpb-takes-steps-to-improve-checking-account-access/.

[7] *Id.*

[8] The FRB should permit occasional exceptions in order to permit lower income consumers to receive tax refunds, back payments of public benefits, and other one-time payments. The consumer could be required to spend those funds or transfer them to another account within a reasonable period of time.

If you have any questions, please contact Lauren Saunders at the National Consumer Law Center, (202) 595-7845, lsaunders@nclc.org. Thank you for considering these comments.

Respectfully submitted,

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Attachment: Organizational Descriptions

Americans for Financial Reform is an unprecedented coalition of over 250 national, state and local groups who have come together to reform the financial industry. Members of our coalition include consumer, civil rights, investor, retiree, community, labor, faith based and business groups.

Arkansans Against Abusive Payday Lending is a broad-based coalition of non-profit, consumer, community, civic, military and faith-based organizations dedicated to ridding our community of the abuses of payday lending. Payday lending tends to prey on low-to-moderate income families, college students, military personnel and the elderly.

Consumer Action has been a champion of underrepresented consumers since 1971. A national, nonprofit 501(c)3 organization, Consumer Action focuses on financial education that empowers low to moderate income and limited-English-speaking consumers to financially prosper. It also advocates for consumers in the media and before lawmakers to advance consumer rights and promote industry-wide change particularly in the fields of consumer protection, credit, banking, housing, privacy, insurance and utilities. www.consumer-action.org

The **Consumer Federation of America** is an association of nearly 300 nonprofit consumer groups that was established in 1968 to advance the consumer interest through research, advocacy and education.

The **National Association of Consumer Advocates (NACA**) is a nonprofit association of more than 1,500 consumer advocates and attorney members who represent hundreds of thousands of consumers victimized by fraudulent, abusive and predatory business practices. As an organization fully committed to promoting justice for consumers, NACA's members and their clients are actively engaged in promoting a fair and open marketplace that forcefully protects the rights of consumers, particularly those of modest means.

Since 1969, the nonprofit **National Consumer Law Center® (NCLC®)** has worked for consumer justice and economic security for low-income and other disadvantaged people, including older adults, in the U.S. through its expertise in policy analysis and advocacy, publications, litigation, expert witness services, and training.

The **Public Justice Center** works with people and communities to confront the laws, practices, and institutions that cause injustice, poverty, and discrimination. We advocate in the courts, legislatures, and government agencies, educate the public, and build coalitions, all to advance our mission of "pursuing systemic change to build a just society."

The **Reinvestment Partners'** mission is to advocate for economic justice and opportunity. We advocate for change in the lending practices of financial institutions to promote wealth building of underserved communities and to end predatory lending practices that strip wealth.

Woodstock Institute is a leading nonprofit research and policy organization in the areas of fair lending, wealth creation, and financial systems reform. Woodstock Institute works locally and nationally to create a financial system in which lower-wealth persons and communities of color can safely borrow, save, and build wealth so that they can achieve economic security and community prosperity. Our key tools include: applied research; policy development; coalition building; and technical assistance. Woodstock Institute has been a recognized economic justice leader and bridge-builder between communities and policymakers in this field since it was founded in 1973 near Woodstock, Illinois. Now based in Chicago, we work with community and philanthropic groups, financial institutions, and policymakers. Funded by foundation grants, consulting fees, and charitable donations, we conduct research on financial products and practices, promote effective state and federal policies, convene a coalition of community investment stakeholders working to improve access to credit, and help people use our work to understand the issues and develop and implement solutions.