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(1915-2014)

Ms. Monica Jackson
Office of the Executive Secretary
Consumer Financial Protection Bureau
1700 G Street NW.
Washington, DC 20552

March 23, 2015

RE: Prepaid Accounts Under the Electronic Fund Transfer Act (Regulation E)
and the Truth in Lending Act (Regulation Z)
Docket No. CFPB–2014–0031
RIN 3170–AA22

Dear Ms. Jackson,

Texas Appleseed supports the Bureau of Consumer Financial Protection’s (“the Bureau”) proposed amendments to amend Regulation E (implementing the Electronic Funds Transfer Act), Regulation Z (implementing the Truth in Lending Act (“TILA”)) and the official interpretations to the regulations to create comprehensive consumer protections for prepaid financial products. Prepaid debit cards are one of the fastest-growing types of payment instruments in the United States; bringing their regulation in line with that of other, more established payment instruments is a necessary step in making sure that this high-growth industry does not become defined by predatory fee-generating practices.

One of the most distinctive features of prepaid debit cards is their customer base. According to the 2014 Pew Survey cited in the Bureau’s proposed regulations, users of prepaid cards are often un- or underbanked. Many either do not have a checking account or would not be approved for one, and 41% of them have closed or lost a checking account due to overdraft fees.¹

Notably, a number of major national payday lending chains offer “co-branded” or jointly marketed prepaid debit cards alongside their loan products. For example, Ace Cash Express offers the Ace Elite card, a co-branded card with netSpend. Speedy Cash is the exclusive distributor of the Opt+ prepaid card and Advance America is part of the Purpose Visa prepaid card program. These arrangements have the potential to circumvent intended protections in the rules. Therefore, we urge you to close loopholes that currently leave open the

¹ Bureau of Consumer Financial Protection, 79 Fed. Reg. 77105, at 77105–06 (proposed December 23, 2014) (to be codified at 12 C.F.R. pt. 1005 and 1026) (hereinafter “CFPB Proposal”).

possibility for third parties to extend credit in connection with prepaid cards outside of the credit protections in the proposed rules, and to make other improvements to ensure that consumers do not get trapped in—or pulled back into—a cycle of debt. Specific issues that need to be addressed include potential negative outcomes for consumers related to:

1. Disbursement of payday loans onto prepaid cards;
2. “Linking” payday loans to prepaid debit cards through debit authorization; and
3. Current barriers to cancel pre-authorized debits.

We firmly believe that one of the roles of prepaid debit cards is to provide opportunities for people to regain access to financial services essential for basic payments and financial transactions. These cards should not represent another opportunity to extract fees from customers.

Local Case Study: Research Documents Offerings of Prepaid Debit Products at Payday Loan Businesses in Austin, Texas

During late February and early March of 2015, Texas Appleseed visited 11 payday loan businesses located in the Austin area to document payday loan and prepaid debit card offerings and pricing. Findings from the visits document potential loopholes around the credit protections in the proposed rules as they relate to co-branding or joint marketing of prepaid debit cards with third-party loan products.

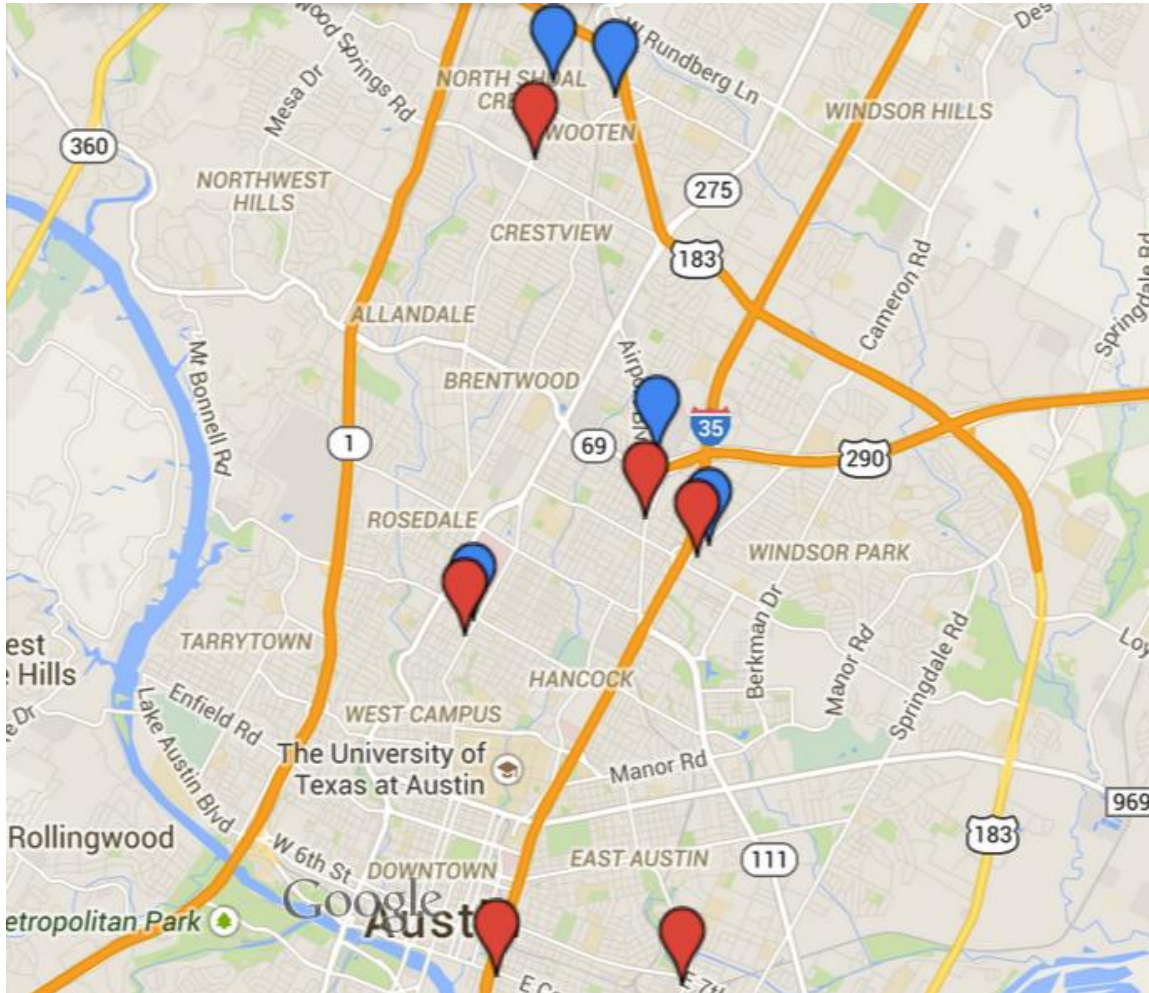
Of the 11 locations visited, five, representing three different chains, offered prepaid debit card products. Among the market practices observed in this study:

- Major national payday lending chains operating in Austin offer co-branded or jointly marketed prepaid debit card products, operated by third-party issuers;
- All three chains encouraged direct deposit of paychecks and other regular income onto their prepaid debit card, with two of the three offering discounts on transaction fees when setting up direct deposit;
- All offered to disburse loan proceeds onto their prepaid debit cards;
- At least one chain² offered to accept prepaid debit card authorization in place of checking account authorization when applying for a payday loan; and
- Loans offered at these locations ranged from a two-month to a six-month loan term with annual percentage rates between 537% and 750%.

² Ace Cash Express; other chains’ policy may vary between locations.

Map of Payday Loan Businesses Visited in Austin, Texas

Austin, Texas Payday Loan Business Survey, February 27-March 9, 2015



Red and blue markers indicate locations of payday loan stores. Blue markers indicate payday loan stores that offered prepaid debit card products alongside payday loan products.

Loan Charges and Prepaid Debit Card Fees

Austin, Texas Payday Loan Business Survey February 27-March 9, 2015

Business Name	Location	APR Payday Loan	Prepaid Cards Offered?	Sample Transaction Fees (Pay-as-you-go)	Sample Transaction Fees (Monthly Plan)	Sample Transaction Fees (Monthly with Direct Deposit)	Loans Disbursable onto Prepaid Cards?	Prepaid Card Authorization Accepted for Payday Loan Application?
Ace Cash Express	8728 Research Blvd., Austin, TX, 78758	750.43% (\$300 loan, 4-payment, bi-weekly)	Yes, co-branded only: Ace Elite netSpend card	\$0 monthly, \$1/signature transaction, \$2/debit transaction	\$9.95 monthly for unlimited signature and debit transactions	\$5.00 monthly for unlimited signature and debit transactions	Yes	Yes
Ace Cash Express	5341 Cameron Rd., Austin, TX 78723	750.43% (\$300 loan, 4-payment, bi-weekly)	Yes, co-branded only: Ace Elite netSpend card	\$0 monthly, \$1/signature transaction, \$2/debit transaction	\$9.95 monthly for unlimited signature and debit transactions	\$5.00 monthly for unlimited signature and debit transactions	Yes	Yes
Ace Cash Express	8501 Burnet Rd., Austin, TX, 78752	750.43% (\$300 loan, 4-payment, bi-weekly)	Yes, co-branded only: Ace Elite netSpend card	\$0 monthly, \$1/signature transaction, \$2/debit transaction	\$9.95 monthly for unlimited signature and debit transactions	\$5.00 monthly for unlimited signature and debit transactions	Yes	Yes
Speedy Cash	3706 Guadalupe St., Ste. D, Austin, TX, 78705	536.52% (\$500 loan, 12-payment, bi-weekly)	Yes, exclusive distributor of Opt+ Visa prepaid card	\$0 monthly, \$2/signature transaction, \$2/debit transaction	\$8.95 monthly for unlimited signature and debit transactions	\$5.95 monthly for unlimited signature and debit transactions	Yes	No
Advance America	5775 Airport Blvd., Ste. 600, Austin, TX, 78752	574.45% (\$500 loan, 12-payment, bi-weekly)	Yes, part of the Purpose Visa prepaid card program	\$0 monthly, \$1/signature transaction, \$2/debit transaction	\$7.98 monthly for unlimited signature and debit transaction	No monthly direct deposit discount; \$59.98 yearly for unlimited signature and debit transactions	Yes	No

Significance of Local Case Study Findings for the Bureau’s Proposed Regulations

In proposing the rules discussed here, “[t]he Bureau believes that many of these consumers lost their checking accounts because they could not handle repeated overdraft fees.”³

“[T]he Bureau also believes that many of these consumers . . . chose to purchase prepaid products because of their promise to allow consumers to control their spending.”⁴ To address these and other issues, the Bureau’s proposal aims “to ensure that credit products that are associated with prepaid accounts receive consistent treatment regardless of their particular structures,”⁵ and to help “consumers . . . understand when they are accessing credit using a prepaid account and . . . benefit from increased protections not available for checking accounts.”⁶ These considerations are important. For many prepaid card consumers, the card is their primary transaction account, yet they “may not fully grasp all of its fees and terms and how those fees and terms might impact [them] over time. In addition . . . , consumers may be offered these products in situations that make comparison shopping difficult.”⁷

Based on our findings regarding joint marketing and sales of prepaid cards by third-party businesses that offer high-cost credit, we believe that some of the current and potential issues and interests noted by the Bureau would be largely unaddressed by the current proposal. Offering payday loans with high APRs alongside co-branded or jointly marketed prepaid debit cards with elevated fees facilitates predatory fee-generating practices in ways largely unregulated by the Bureau’s proposal, and risks trapping consumers in the same cycles of debt that led to use of prepaid debit card products in the first place.

“Linking” a prepaid debit card to a payday loan via pre-authorization of lender withdrawals on default is particularly dangerous in this respect. Since payday loan businesses will automatically attempt to withdraw payment on a defaulted loan from any pre-authorized account, default could suddenly leave a linked customer without money for food, bills and other basic necessities. Such a scenario stands in stark contrast to the message broadcast by in-store marketing of prepaid debit card products: that prepaid debit cards are the responsible choice in taking control of personal finances.⁸

Our findings provide evidence that knowledgeable prepaid card issuers and program managers could circumvent a number of protections implemented in the rules as proposed, going against interests that, based on the intent of the rules and the realities of the marketplace, should be protected.

³ CFPB Proposal at 77211.

⁴ *Id.*

⁵ *Id.*

⁶ *Id.*

⁷ *Id.* at 77110.

⁸ *Id.* at 77211; confirmed by promotional materials displayed and/or gathered at Advance America and Ace Cash Express locations.

1. The Proposal Allows for Loading of Payday Loans onto Prepaid Cards

As part of its proposal to bring into TILA and Regulation Z credit services offered on prepaid accounts, the Bureau proposes to curtail the “comparable cash transaction” exception to finance charges by not applying carve-outs in the definition of “finance charge” when such charges are assessed on credit services associated with a prepaid account.⁹ These proposals would bring most overdraft-related fees on debit accounts within the definition of “finance charge,” making issuers “creditors” and the prepaid cards they issue “credit cards” subject to Regulation Z. The Bureau believes that these proposals would, among other benefits, aid consumers in “understanding the costs of credit transactions”¹⁰ by “[providing] a clear line about which fees that are imposed on the prepaid account are finance charges,”¹¹ in keeping with the Bureau’s general intent “to cover credit accessed by a prepaid card . . . as ‘open-end credit’ under Regulation Z.”¹² The Bureau notes that an ancillary benefit to this change would be “issuers . . . [waiving] certain transaction fees in connection with overdraft transactions” in order to fit within exceptions to the regime.¹³

However, distributing co-branded or jointly marketed prepaid debit cards via third-party payday loan businesses amounts to an end-run around this protection. When an issuer charges transaction fees for using a prepaid debit card that is loaded with a third-party’s payday loan proceeds, the issuer is effectively charging fees in connection with credit services, but is doing so in a way that keeps the activity out of Regulation Z: since the prepaid account itself has no associated credit service, the fees assessed by the issuer are not “finance charges,” the issuer is not a “creditor,” and the prepaid debit card is not a “credit card.” This approach also gives payday loan businesses an alternative way to generate fees on loans, since they receive a cut of any operating fees assessed on co-branded or jointly marketed prepaid debit cards—much like cutting a check for loan proceeds and then charging a check cashing fee.

Moreover, online payday loan applications could tie-in with online co-branded or jointly marketed prepaid debit card activation. Although the phenomenon has not yet been documented, prepaid debit card issuers could include the option to apply instantly for a payday loan when activating a co-branded or jointly marketed card. Such a mechanism could sharply accelerate the prevalence of prepaid debit card issuers assessing fees on credit—all without being subjected to Regulation Z. This scenario and the aforementioned mechanisms clearly frustrate the Bureau’s goals of providing consumers with easy ways to identify finance charges and understand the costs of credit transactions.

⁹ *Id.* at 77228.

¹⁰ *Id.* at 77229.

¹¹ *Id.*

¹² *Id.* at 77230.

¹³ *Id.* at 77229.

2. *The Proposal Allows for “Linking” Payday Loans to Prepaid Debit Cards*

Enhancing individual financial stability is another intended effect of the Bureau’s proposed rules that could be undermined by the overlap of payday loans and prepaid debit cards. For instance, the Bureau proposes to reinforce TILA’s restrictions on issuers’ setoff rights by limiting the frequency of setoff withdrawals from prepaid accounts to once a month, and by making security interests in prepaid accounts harder to obtain.¹⁴ These changes reflect the Bureau’s concern over issuers having undue leverage over the consumer by threatening to setoff debts against prepaid accounts, which are often used to pay for basic necessities such as food and utilities. In its own words, “the Bureau is concerned that . . . some card issuers may attempt to circumvent the prohibition on offsets by obtaining a consumer’s written authorization to deduct [a] cardholder’s credit card debt on a [basis corresponding to times when the issuer knows] the consumer is likely to be depositing funds.”¹⁵ In a similar vein, the Bureau proposes to provide “specific guidance on the term ‘agent’ for purposes of [Regulation Z’s definition of the term “card issuer”] where a credit plan offered by a third party is accessed by a prepaid card that is a credit card.”¹⁶ With this guidance, the Bureau intends to avoid situations where issuers “structure arrangements with third parties that offer open-end credit plans that are accessed directly by the prepaid card to avoid an agency relationship under state law.”¹⁷

Although the Bureau’s proposed solution appears adequate with respect to prepaid cards, it would not restrict “linking” payday loans to prepaid cards via debit pre-authorization. A typical payday loan contract pre-authorizes the lender to withdraw funds from an account (usually a traditional checking account) in case of loan default. As discussed above, at least one major payday lending chain accepts prepaid debit card authorization in place of standard bank account authorization when applying for a payday loan. When the pre-authorized account is a prepaid debit card account, the Bureau’s concerns are magnified.

Unlike a standard payday loan customer, who may continue to have access to a credit card or other bank account following default, many prepaid debit card users are un- or underbanked, lacking access to traditional financial services. Default on a linked payday loan could leave such customers unable to pay for anything, including basic necessities such as food and utilities. Since the linked payday loan is not a debt owed to the prepaid card issuer, pre-authorized withdrawals made by the payday loan business are not setoff activities of the type restricted by the Bureau’s proposed rules.

Furthermore, such withdrawals would not be restricted by the Bureau’s guidance on the term “agent.” The effect of finding a third party to be an “agent” of an issuer lies in making the agent a “card issuer” governed by Regulation Z.¹⁸ However, the Bureau’s guidance only provides that a “third party offering the credit plan that is [directly accessed or “pulled”] by the [prepaid] card would be considered an agent of the prepaid card

¹⁴ *Id.* at 77239.

¹⁵ *Id.*

¹⁶ *Id.* at 77216.

¹⁷ *Id.*

¹⁸ *Id.*

issuer....”¹⁹ The Bureau’s references to “credit plan” and “direct access” do not appear to cover situations where a payday loan business disburses a lump sum payout onto a card with no provision for further advances. Nevertheless, as discussed above, the consequences of default on a linked payday loan would look almost identical to the consequences of the type of arrangement contemplated by the Bureau’s proposal. Specifically, in both cases the consumer could be left with little or no funds to pay for necessities.

If wages are being direct deposited onto the prepaid debit card at the time of default, the linkage scenario becomes even more troublesome. Direct deposit of wages may seem attractive to many prepaid debit card users—most cards’ policies allow for wages to be received 2-3 days in advance when direct deposited, in addition to discounts on transaction fees. Anecdotal evidence suggests many lenders’ employees elect to receive their wages this way.²⁰ Yet default on a payday loan linked to a prepaid account into which wages are being direct deposited is apparently left unrestricted—despite being the type of scenario the Bureau’s proposed rules are meant to address.

3. The Proposal Does Not Address Barriers to Cancel Pre-Authorized Debits

Another issue of concern is the difficult and potentially expensive process to cancel pre-authorized debits from prepaid accounts, such as those associated with recurring bill payments. At least two of the prepaid cards surveyed that were co-branded or jointly marketed with major payday loan chains charge a significant fee for discontinuing pre-authorized debits unless the withdrawal is performed by directly contacting the business with the debit authorization, and require enough advance notice to make short-notice cancellations impracticable. For example, the prepaid card sold at Advance America locations includes a \$10 fee for this service, as does Ace Cash Express’ Ace Elite card. This reality goes against the stated goal of ensuring that funds for food, housing, and other necessities are not taken for debt repayment, as a result of the connection between the creditor or credit service provider and the prepaid card issuer.

Proposed Solutions

The gaps in the proposal’s coverage, discussed above, would allow card issuers opportunities to generate fees on “credit” without being subjected to the bulk of the Bureau’s proposed regulatory regime, undermining goals of transparency, stability, and control for consumers using prepaid debit cards.

While we support the Bureau’s proposed regulations as a much-needed step forward, additional measures could help forestall many of the current and potential problems discussed above. To this end, we suggest that the Bureau:

¹⁹ *Id.*

²⁰ Confirmed at the Burnet Road Ace Cash Express location (at least one employee), and at the Speedy Cash (all employees) and Advance America (at least one employee) locations visited.

- Limit the deposit of funds from a credit transaction only to cards that have been active for at least 90 days, and implement any other necessary protections to ensure that this mechanism does not operate as an end-run around the intended protections in the proposal;
- Prohibit prepaid card providers from marketing third-party credit products in conjunction with the prepaid card or any card interfaces (eg. Mobile app, website, or other marketing materials);
- Prohibit payment authorization for third-party credit payments from a prepaid card if the card is co-branded or jointly marketed with the credit or credit service provider or an affiliate of the credit or credit service provider or if there is any agreement between the prepaid card provider and credit or credit services provider related to the credit or credit services transaction;
- Reduce or eliminate fees to cancel an authorization for a third party to debit a prepaid card account, and shorten the required notice period to cancel a pre-authorized debit to the prepaid card provider to 24 hours in advance of the cancellation of the authorization.

Conclusion

In summary, Texas Appleseed's research shows that the Bureau's proposed regulations, while laudable, would not protect against certain potentially predatory practices stemming from relationships between prepaid debit card providers and high-cost third party credit providers. We believe that the proposed regulations should be amended to address the concerns raised in these comments. We appreciate the opportunity to share our concerns and proposed solutions.

Sincerely,



Ann Baddour
Director, Fair Financial Services Program