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Washington, DC 20036

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Nessa Feddis
Senior Federal Counsel
Phone: 202-663-5433
Nfeddis@aba.com

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Ms. Jennifer J. Johnson
Secretary
Board of Governors
of the Federal Reserve System
20th Street and Constitution Avenue, NW
Washington, D.C. 205551

Re: Docket No. R1210
Regulation E
69 *Federal Register* 55996, 17 September 2004

Dear Ms. Johnson,

ABA is pleased to submit our comments to the Federal Reserve Board's ("Board") proposed changes to Regulation E (Electronic Fund Transfer Act) and its Commentary. Proposed revisions address coverage of electronic check conversion services and payroll cards. In addition, the proposal provides guidance on preauthorized transfers, additional electronic check conversion issues, error resolution, and ATM disclosures.

The ABA brings together all categories of banking institutions to best represent the interests of this rapidly changing industry. Its membership – which includes community, regional, and money center banks and holding companies, as well as savings associations, trust companies, and savings banks – makes ABA the largest banking trade association in the country.

Overall, ABA believes that the proposal is helpful and will clarify some important matters. We recommend that the Board make some changes including treating payroll cards as it treats electronic benefit transfers ("EBT") and modifying some of the proposed disclosures associated with electronic check conversion.

Section 202.2(b). Definition of Account to Include Payroll Accounts.

The proposal adds to the definition of "account" a payroll card account "directly or indirectly established by an employer on behalf of a consumer to which electronic fund transfers of the consumer's wages, salary, or other employee compensation are made on a recurring basis,

whether the account is operated or managed by the employer, a third-party payroll processor, or a depository institution.” The definition excludes gift cards and one-time transfers of salary-related payments. Thus, under the proposal, the initial disclosure, periodic statement, and error resolution provisions of Regulation E would apply to payroll cards.

ABA recommendation. We agree that Regulation E should cover payroll cards. It is important that payroll card holders receive information about the fees, terms, and conditions and that they enjoy other consumer protections that Regulation E affords. We also agree with the proposed exclusion of gift cards and one-time transfers of salary-related payments. The variations among the types of gift cards and one-time salary cards are numerous and vast and in most cases, adding Regulation E coverage would be inappropriate or may chill development of new, attractive products.

We recommend, however, that the Board treat payroll cards as it has treated EBT under Section 202.15 of the regulation and thereby permit an alternative to the periodic statement. Accordingly, the Board should adopt the EBT approach and not require a periodic statement if the consumer:

- 1) has access to the balance through a telephone line and at a terminal (such as by providing balance information at a balance-inquiry terminal or providing it, routinely or upon request, on a terminal receipt at the time of the electronic fund transfer), and
- 2) may obtain a written history of the consumer’s account transactions that is provided in response to a request that covers at least 60 days preceding the date of request.

We also recommend that payroll cards be covered under Section 202.15 which covers EBT or under their own separate section rather than including it under the definition of “account.”

Discussion. The alternative to periodic statements is appropriate for payroll cards for many of the same reasons it is appropriate for EBT. Transactions under both programs are limited: the holder cannot make deposits, write checks, or arrange direct debit. Thus, there are fewer transactions to track. In addition, payroll card holders, have shown that they are most interested in immediate, real-time information about their balance and recent transactions. If the EBT approach were adopted, such information would be conveniently available by the phone, terminals, and the internet. More frequent, real-time access permits holders to know their balance immediately. It also allows them to learn sooner whether there has been a mistake that needs to be corrected and provides information at a time when card holders are better able to recall recent activity. In contrast, a periodic statement, arriving days or even weeks after the last

transaction, offers little use as the balance has already changed and other transactions have occurred.

We believe that the alternative to the periodic statement is also appropriate because payroll cardholders tend to be more mobile than other customers. Banks offering payroll cards have found a much higher return rate for mail sent to payroll cardholders. A typical experience is that 10 to 15 percent of payroll mail is returned. While not all payroll cardholders may have access to internet, they generally have convenient access to card information through terminals and by telephone. EBT recipients have relied on these vehicles for years with little if any complaint.

Another reason that the Board should not require periodic statements for payroll cards is that doing so will add unnecessary costs that could 1) discourage banks from offering a valuable and needed product, and 2) increase costs for employers and payroll card holders.

Payroll cards are valuable and convenient to those who lack bank accounts. They allow safe and convenient access to wages to those who may be ineligible or uninterested in checking accounts. Seeing the value, both state and federal government agencies have expressed keen interest in providing payroll through such cards.

Requiring periodic statements will increase the price of the product. Periodic statements are an expensive aspect of bank products. One bank estimated that it costs \$6 a month to compile, print, and mail a periodic statement. (This does not include, for example, other costs such as handling returned statements.) The expense associated with providing periodic statements will be paid for either by the employer or the employee. In some cases, it will discourage banks from offering the product. Banks report that the business case for payroll card programs is already rather tenuous. For some banks, especially small ones that lack economies of scale, adding an expensive component that offers little benefit may break the business case.

We also suggest that the Board address payroll cards under its own separate section or under Section 202.15 which covers EBT rather than under the definition of "account." This will make the information easier to find in the Regulation and distinguish it from typical bank accounts. The Board itself in the Supplementary Information notes the parallels between EBT and payroll cards:

Much like the EBT products that fall within Regulation E's coverage, payroll products are assigned to an identifiable consumer, represent a stream of payment to the consumer, are replenished on a recurring basis and can be used in multiple locations for multiple

purpose and utilize the same kinds of access devices, electronic terminals, and networks as do other EFT services.

We also respectfully disagree with the Board that, “Payroll cards products are, in effect, designed, implemented, and marketed as substitutes for traditional check accounts at a financial institution.” They are not. As noted above, unlike checking accounts, payroll card programs basically limit the types of transactions to payroll and POS and ATM card transactions: the holder cannot make deposits, write checks, or arrange direct debit. For these reasons, we recommend that payroll cards be addressed in their own section or under the EBT section.

The Board has asked whether Regulation E coverage should be determined by whether a payroll account holds consumer funds that qualify as eligible deposits for purposes of FDIC insurance. We do not believe that it should. Although generally, consistent definitions are helpful in simplifying compliance and understanding rules, the reasons for defining “account” for Regulation E purposes and FDIC insurance purposes are unrelated.

The Board has also asked when a final rule should be effective. We suggest that the Board allow at least 12 months for banks to comply with the final rule. First, most banks use vendors to offer the product and the process of ensuring compliance under these circumstances takes longer because more parties are involved. Second, depending on when the final rule comes out, it may interfere with the typical end-of-the-year two to three month black-out for systems modifications or additions.

Section 205.3(b) Electronic Check Conversion.

The proposal addresses electronic check conversion, which is a means for using a check to initiate a one-time electronic fund transfer by scanning and capturing the MICR-encoding on the check and entering the amount to be debited from the account. Previously, the Board amended the Commentary to establish a bright line test for when such transactions are covered by Regulation E. The proposal adds further clarifications.

The proposal specifically requires that “the person that initiates a transfer shall provide notice” for each transfer. We agree. The person initiating the transfer is making the decision to convert the check and is in the best position to provide the notice. Accordingly, that person should be responsible. The bank holding the account has no control over whether its customer received notice of the conversion.

The proposal also adds a provision that notice to obtain a consumer authorization must be provided for each transfer. We agree with the addition. It will help ensure that consumers understand that their check is being converted. However, we request that the Board

grandfather existing loans that rely on coupon books instead of statements. Otherwise, to comply, creditors would have to replace the coupon books. Given the expense and that coupon books lacking the disclosure will with time be phased out, we think the exception is justified. Moreover, consumers still receive the initial notice.

The Board requests comment on whether merchants or other payees should be required to obtain the consumer's written signed authorization to convert checks received at point of sale ("POS"). We agree that at POS the consumer should sign a written authorization. This helps avoid disputes later that consumers were unaware of the authorization because they failed to notice a sign. However, we do not think that it is necessary to add a specific mandate to the regulation as NACHA rules already require the written authorization. Leaving the decision to NACHA will allow more flexibility to adjust as appropriate and in a timely fashion. For example, the written authorization may not be necessary at a later date as consumers become more accustomed to the conversion.

The proposal also adds a requirement to provide notice that "funds may be debited from the consumer's account quickly. . . and that the consumer check will not be returned by the financial institution holding the consumer's account." We strongly suggest deletion of "funds may be debited from the consumer's account quickly." We believe that it will be confusing and misleading to consumers as it suggests that the transaction will process more quickly than if it were to be processed as a check. However, in many cases, the funds will not be debited more quickly than if the transaction were processed as a check. Moreover, with Check 21, checks will be processed more and more quickly, possibly faster than through ACH. It may also make some customers reluctant to authorize conversion and thereby preserve the inefficiencies of the paper process.

The proposal adds to the Commentary that if an electronic fund transfer or check is returned unpaid due to insufficient funds, an electronic fund transfer from the consumer's account is covered by the regulation and must be authorized by the consumer. We agree that it is important for consumers to authorize such fees.

The proposal adds to the Commentary that if a payee obtains a consumer's authorization to use a check as a source document to initiate an electronic fund transfer, the payee cannot process the transaction as a check. In order to process the transaction as an electronic fund transfer, or alternatively as a check, the payee must obtain the consumer's clear authorization to do so. In addition, it adds, "A payee may specify the circumstances under which a check may not be converted to an EFT."

We agree with the proposal, but suggest that it make clear that the payee is not required to specify the circumstances when the check may

not be converted to an electronic fund transfer. As the Board notes in the Supplementary Information, there are occasions when a payee may intend to process a check as an electronic fund transfer, but then is unable to do so or finds a more efficient way to process the transaction. Payees should not be required to list the circumstances when the check will not be paid electronically. First, it is impossible to anticipate all the potential reasons that a transaction intended to be processed as an electronic fund transfer is legitimately later processed as a check. The reasons are numerous and constantly changing. The payee should not then be precluded from getting paid. Merchants and their banks need the flexibility to process an authorized transaction and to obtain payment. Second, listing all the reasons will not help consumers. In many cases the explanation will be incomprehensible to consumers. In addition, a lengthy disclosure will only clutter the notice, distracting them from more important information.

For these reasons, we also recommend that the Board delete proposed model form A-6(c).

Moreover, we do not believe that consumers will be confused about their rights. Many banks today separate check transactions from electronic fund transfers, placing the check conversions on the list with the electronic fund transfers. Furthermore, once the consumer contacts the bank about a dispute, the nature of the transaction will be able to determine which law applies and act accordingly or risk a violation.

Section 205.7 Initial Disclosures.

The proposal adds to Commentary a requirement that initial disclosures list one-time electronic funds transfers initiated using information from a check. The proposed Commentary also says that electronic check conversions are a new type of transfer requiring new disclosures. We agree with this addition and believe that most depository institutions already have adjusted their disclosures.

Section 205.5(b) Unsolicited Issuances.

The proposal adopts a provision to the Commentary that permits additional cards to be issued at renewal or as substitution, provided that the additional access device is not validated at the time it is issued. We agree with the proposal as it allows flexibility in providing additional access devices while appropriately protecting consumers by requiring validation.

205.10 Preauthorized Transfers.

Written Authorization for Preauthorized Transfers. The proposal deletes from the Commentary, “A tape recording of a telephone conversation with a consumer who agrees to preauthorized debits does not constitute written authorization.” We disagree with deletion of this

provision. It provides an important protection for consumers against unauthorized recurring debits to their checking accounts. Banks receive a lot of complaints from customers that they had authorized, understood, and intended only a one-time debit only to find it recurring. We believe that it is important to have clear evidence of the authorization to ensure that consumers understand what they are authorizing and that unscrupulous people do not take advantage of consumers and the regulation. Tape recordings have not proved to provide that clear evidence.

Bona fide error. The Board notes that debit cards, unlike credit cards, cannot be charged in recurring fashion without written authorization. The proposal adds to the Commentary that requesting that the consumer specify whether the card is a debit card or credit card is a reasonable procedure for obtaining authorization for recurring transactions. We agree that this is a reasonable addition as it is not always practical for the third party to determine whether the card is a debit or credit card.

205.10(d) Notice of Transfers Varying in Amount.

When a preauthorized electronic fund transfer from a consumer's account will vary in amount from the previous transfer or the preauthorized amount, the regulation requires that the consumer receive written notice of the amount and date of the transfer at least 10 days prior to the scheduled date of the transfer. Consumers have the option to only receive the notice when the transfer falls outside a specified range of amounts or only when a transfer differs from the most recent transfer by more than an agreed-upon amount. To add flexibility the proposal adds to the Commentary a provision that a financial institution need not give the consumer the option of receiving notice before providing a consumer a range of varying amount to an account of consumer held at another financial institution. However, the range must be an acceptable range that could be anticipated by the consumer, and the institution must notify the consumer of the range. We agree with this addition because it will in some cases eliminate the need for unnecessary notices without detriment to consumers.

205.11(b) Procedures for Resolving Errors.

The proposal adds to the Commentary a statement that institutions are not required to comply with the error resolution provision if the consumer notifies the institution later than 60 days from the date on which the periodic statement first reflecting the error is sent. However, institutions must comply with the provision related to liability for unauthorized institutions. We suggest that the Commentary note the exception for extenuating circumstances as provided in the regulation.

* * * *

The ABA appreciates the opportunity to comment on these important changes to Regulation E and its Commentary. We are happy to provide additional information.

Sincerely,

Nessa Eileen Feddis