

November 19, 2004

Jennifer J. Johnson, Secretary
Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue, NW
Washington, DC 20551

Re: Docket No. R-1210; Federal Reserve Board Regulation E, 12 CFR § 205.10(b)

Dear Ms. Johnson:

The Electronic Retailing Association (ERA) appreciates the opportunity to comment on the agency's proposed rule that would make changes in Regulation E and in its official staff commentary, as announced in the *Federal Register* of September 13, 2004.

The ERA is a non-profit trade association representing the \$186 billion electronic retailing industry. ERA was founded in 1990 and is comprised of more than 400 member companies and subsidiaries worldwide that use the power of electronic retailing to sell goods and services directly to consumers via television, radio, internet, telephone and wireless media.

We write to support your adoption of proposed revisions to the Official Staff Interpretation to Regulation E as they relate to preauthorized transfers. The proposed rule would remove a barrier to implementing procedures that merchants believe are consistent with the E-Sign Act by deleting from the official staff commentary the sentence that says: "A tape recording of a telephone conversation with a consumer who agrees to preauthorized debits also does not constitute written authorization for purposes of this provision."

The proposal also clarifies the *bona fide* error rule: that a merchant is not in violation of the regulation if the merchant mistakenly treats a debit card as a credit card if the merchant has a procedure reasonably adapted to avoid such errors. The proposal would clarify that while reasonable procedures will vary with the circumstances, asking the consumer to specify whether the card to be used for the authorization is a debit card or is a credit card, using those terms, is a reasonable procedure. The proposal also clarifies that, in light of the difficulties in obtaining real time BIN tables, consulting such tables for new or existing transactions is not a requirement for a reasonable procedure.

We believe all of these changes are sensible and beneficial for the health of U.S. commerce and the payment system. The payment system in the United States is shifting from a paper to an electronic one. According to the first comprehensive studies of the payment systems by the Federal Reserve in more than 20 years, while check usage for non-cash payment has declined from 85% in 1979 to 60% in 2000, electronic payment systems, such as credit and debit cards have gained considerable ground, constituting approximately \$7 trillion in sales during 2000. According to Ms. Cathy E. Minehan, president of the Federal Reserve Bank of Boston, "Not only do we have a much better idea about the size of the total retail payments system, we clearly

see that electronic payments are taking a strong hold of the market and are poised for significant growth in the next few years.” Significantly, in passing 2003 amendments regarding payment term disclosures to its Telephone Sales Rule, 16 CFR Part 310, the Federal Trade Commission relied on the fact that consumers had become familiar enough with debit cards that they could be treated in the same manner of credit cards. See, 16 CFR 310.3(a)(3).

Payments that are subject to Regulation E are an increasing part of the payment industry. For example, the use of debit cards is growing at twice the rate of credit cards, and this trend is likely to escalate. VISA reported in 2002 that more than half of the payments processed using its cards were processed as debit card transactions. This year, VISA reported that not only the number of transactions but global debit sales volume exceeded that of global credit sales.

Consumers clearly appreciate the convenience that such payment mechanisms provide. Moreover, they provide additional benefits for users who operate on a cash rather than a credit basis, something that financial planners and consumer educators generally recommend, especially for those having difficulty managing their finances. The consumer receives a statement every month showing what he has spent. Consumers can live responsibly within their means rather than borrowing against his future. Banks and merchants also benefit from consumers using methods other than traditional checks, if only because the cost of processing is much less than that associated with checks.

Removing Barriers to Electronic Signatures

The proposed removal of the above sentence eliminates a substantial barrier to the use of mechanisms such as debit cards.

The Official Staff Interpretation to Regulation E already provides that the signature requirement can be satisfied by complying with the Electronic Signatures in Global and National Commerce Act, 15 U.S.C. 7001 (the “E-Sign Act”). While the E-Sign Act allows electronic writings to replace all hard-copy paper transactions and forbids any preference between different technologies, the Official Interpretation’s seeming prohibition on using recordings has generated considerable confusion about the relationship of Regulation E and the E-Sign Act. As a result, many merchants have concluded that they could engage in electronic transactions on the internet, but perhaps not by telephone. Such confusion has prevented realization of many of the benefits that the E-Sign Act was designed to provide.

The sentence of the Official Staff Interpretation also has led to the incongruous result that a merchant who obtained payment information from a consumer could tape an telephone authorization to support repeatedly submitting paper drafts to the merchant’s bank (“demand drafts” not subject to Regulation E) but was afraid that he could not submit recurring ACH transfers that are subject to Regulation E.

Ironically, as noted above, in its recent amendment of its Telemarketing Sales Rule, the Federal Trade Commission *required* merchants who engage in telephone sales to obtain the consumer’s

“express verifiable authorization” when using certain of the payment methods under Regulation E, including demand drafts. In some instances that authorization could be obtained only by recording the conversation with the consumer. As a result, again it has been seen as more feasible for merchants to accept orders involving recurring payments with a demand draft payment mechanism that provides fewer consumer protections than a debit card.

The proposed rule brings the two situations into a more rational conformity by removing unwarranted barriers to allowing consumers to adopt proper telephone authorizations, recorded electronically, as their electronic signatures. The superiority of the consumer protections of the EFTA over the scarce protections available with alternate mechanisms supports not driving merchants toward such alternatives because of confusion over the Staff Commentary’s apparent ban on telephone recordings.

The consumer continues to be protected by the requirement that the merchant provide the consumer with a copy of the terms of the authorization before making a pre-authorized transfer from the consumer’s account. By modifying the Official Staff Interpretation to eliminate the confusion about using tape recordings for electronic signatures, the Federal Reserve will serve the public interest by enabling banks and merchants to implement, and consumers to use, cost-effective alternatives to paper checks or demand drafts. The proposal facilitates a more effective payment system while furthering the Congressional purpose of supporting technological innovation reflected in the E-Sign Act. If merchants see no practical way to obtain compliant preauthorizations from the consumer for sales transactions governed by Regulation E, they will continue to favor less protective and less efficient methods. Such an outcome should be avoided by approving the proposed change to the Commentary.

Bona Fide Error

We also support the clarifications proposed regarding the *bona fide* error exception. Providing the proposed clarification, that asking the consumer to identify the nature of the card used is a reasonable procedure, and that obtaining and consulting BIN tables is not a requirement for a reasonable procedure, substantially reduces the risk of inadvertent regulatory non-compliance.

While we have not conducted a survey of all of our members, we have received anecdotal indications that the members who tried to get BIN table information faced substantial difficulties in obtaining archival data and were completely unable to obtain information that could be used on a real time basis. The difficulties were compounded by what seem to be reasonable privacy and proprietary concerns of the card associations, and their desire to work through their own members rather than providing such information directly to merchants, perhaps to contain their administrative expenses.

The procedure articulated in the proposed rule is as likely to avoid errors as consulting BIN tables, and at much lower cost. This will become even more true as the card associations implement their settlements of the litigation referred to in the proposal as the “Wal-Mart”

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settlement. In Re Visa Check/Mastermoney Antitrust Litigation, No. CV-96-5238 (E.D.N.Y.) Those settlement agreements provide that all new VISA and MasterCard debit cards issued after January 1, 2004 will have language (or a logo or other identifier) printed on their face that identifies the card as a debit card. VISA and MasterCard also promise to require all card issuers to convert all existing debit cards to the new format (through renewal of existing cards) by January 1, 2007. We understand that the card associations hope to complete implementation of these changes before 2007, so that very soon, there will be very little likelihood that a consumer will not know what type of card is being offered in payment.

We deeply appreciate the efforts of the Board of Governors of the Federal Reserve to make compliance with the consumer protections of the EFTA more feasible for electronic retailers. We ask the Board to approve these aspects of the regulatory proposal.

Sincerely,

Barbara Tulipane
President and Chief Executive Officer

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