WOODSTOCK INSTITUTE

Advancing Economic Security and Community Prosperity

June 25, 2018

Acting Director Mick Mulvaney
Consumer Financial Protection Bureau
1700 G Street NW
Washington, DC 20552

Re: Docket No. CFPB-2018-0012 -- Request for Information Regarding the Bureau's Inherited Regulations and Rulemaking

Dear Acting Director Mulvaney:

Woodstock Institute submits these comments in response to the Consumer Financial Protection Bureau (CFPB)'s Request for Information (RFI) regarding inherited regulations and rulemaking authorities. In general, we support the inherited regulations and urge the CFPB not to weaken them. We also urge the CFPB to use its inherited rulemaking authority to address areas, such as overdraft practices, that exact substantial harm on consumers.

1. About Woodstock Institute

Woodstock Institute is a leading nonprofit research and policy organization in the areas of equitable lending and investment, wealth creation and preservation, and access to safe and affordable financial products and services. We work 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.

In recent years, Woodstock played a leading role on reforms regarding payday and other high-cost lending, currency exchanges/check-cashers, debt collection, public fines and fees, children's savings accounts, and retirement savings programs for private sector workers. Woodstock also plays a leading role in helping to ensure banks invest in and provide safe and affordable services to low- and moderate-income communities, communities of color, and older people.

2. Objections to the CFPB's Request for Information Process

As we previously commented, the number of RFIs that you have issued and their frequency is overly burdensome to small not-for-profits like Woodstock. Industry, with its greater resources in terms of staff and otherwise, is far more capable than the consumer advocacy community in developing thorough responses to this flood of RFIs. The amount of time and attention required to try to address the RFIs has diverted scarce nonprofit resources that might otherwise be spent on other issues such as weakening the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (Dodd-Frank Act) or the multitude of Congressional efforts to repeal agency rulemakings through the Congressional Review Act.

The information provided through this RFI process will be inherently skewed in industry's favor simply because it has the necessary resources to create an official record reflecting its position. Accordingly, at the end of the day, the official record that will have been established through this process is not an accurate reflection of the variety and force of opinions on the many issues covered by the RFIs. We anticipate the need to raise objections insofar as this process is used to back off enforcement, lessen oversight, or gut the CFPB itself.

3. Develop Overdraft Protections

We disagree with the CFPB's announced decision to drop an overdraft fee rulemaking from the Bureau's regulatory agenda. The Bureau's research, consistent with research by third parties, has demonstrated the abusive nature of bank overdraft programs and the severe impact these fees—totaling an estimated $14 billion annually[1]—have on working families.

CFPB's research findings include the following:

- Nearly 80 percent of bank overdraft and non-sufficient funds (NSF) fees are borne by only nine percent of accounts, who tend to carry low balances—averaging $350—and have relatively low monthly deposits.
- Overdraft fees on debit cards (which can easily be declined at no cost when the account lacks sufficient funds), can lead to extremely high cumulative fees for consumers.
- Consumers whose debit cards could trigger overdrafts were more than 2.5 times more likely to have their accounts involuntarily closed than those who were not "opted in" to debit card overdraft at several study banks.

The diversion of cash needed for living expenses toward fees is devastating to a family living on the margins, but the consequences do not stop there. For some, overdraft fees prevent them from regaining their footing, marking a lasting economic setback. Overdrafts are the leading reason that consumers lose their checking accounts. The FDIC's 2013 survey of unbanked and underbanked households indicates that approximately 778,800 households, and well over a million adults, who once had bank accounts are currently unbanked primarily because of high or unpredictable fees. It is likely that in the majority of those cases, the fees at issue were overdraft/NSF fees, as they are both the largest fee and comprise the majority of checking account service charge revenue.

Once ejected from the banking system, the ejecting financial institution reports the account holder to a database, like ChexSystems or Early Warning Service—a blacklist, essentially, where the consumer's name remains for five years, often preventing the consumer from being offered a checking or savings account with another financial institution. While there are no national data on the number of consumers on bank account blacklists, millions of consumers are affected, with one software company estimating that 2.3 million online applicants were denied accounts based on their screening in 2012 alone;[2] the large majority of consumers blacklisted is blacklisted because of overdrafts.

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[1] Center for Responsible Lending, *Broken Banking: How Overdraft Fees Harm Consumers and Discourage Responsible Bank Products* (May 2016), https://www.responsiblelending.org/sites/default/files/nodes/files/research-publication/crl_broken_banking_may2016.pdf.

[2] National Consumer Law Center and Cities for Financial Empowerment Fund, *Account Screening Consumer Reporting Agencies: A Banking Access Perspective* (Oct. 2015) at 6, *available at*

The costs of exclusion from the banking system can be profound. A banking relationship is important to household financial stability and asset-building. A checking account protects funds from physical risk, offers a relatively low-cost and convenient way to conduct routine financial transactions, provides mechanisms for savings, and, for many families, is the gateway to a broader banking relationship that includes access to reasonably priced credit.

Furthermore, overdraft fees have fueled the development of a profoundly dysfunctional checking account market. When consumers shop for a bank account, they are likely to consider factors such as fixed monthly and annual costs of the account. Thus, they may choose an account that appears "free"—with no upfront monthly fee—but be unaware that they will pay more for the account due to overdraft charges than they would have on an account that has a modest monthly fee, but more responsible overdraft fee practices. Instead, overdraft charges operate as "back-end" or "gotcha" fees that undermine consumer choice and a healthy market and fuel aggressive, deceptive marketing efforts to convince people to "opt-in," rather than transparent upfront price tags.

Today, some overdraft practices vary significantly by institution, but often not in ways transparent to the consumer. For example, at some banks CFPB studied, "opt-in" rates on POS and ATM overdraft fees were 40 percent; at others, they were less than 10 percent. Further, for those customers that incur overdraft fees, some banks average annual overdraft fees nearly twice as large as overdraft fees at other banks.

A similar dynamic—low upfront costs, high back-end, hidden costs—was once at play in the credit card market, where interest rates were often low, but back-end penalty fees were unrestrained. The CARD Act reined in abusive fees and penalty rates, and the market shifted toward more transparent, upfront pricing.

More upfront pricing for checking accounts would provide incentive for financial institutions to have more responsible checking account models, rather than one that preys upon those with the least resources. Adopting an upfront pricing model would likely still permit many to maintain "free" checking accounts—banks often waive fees for those with direct deposit, or other features—but it would make the distribution of costs far more closely correspond to receipt of services.

The CFPB should restore plans to address overdraft fee abuses. In particular, CFPB should:

- **Regulate overdrafts as credit under Regulation Z, subject to an ability-to-repay assessment and repayment through installments.** Overdraft fees have long enjoyed a regulatory pass in many respects because banks have posited that overdraft is not being used as credit but merely as an occasional courtesy. Data showing that many consumers are charged numerous overdraft fees annually belie this argument, however. When financial institutions routinely pay a customer's transactions when the account lacks sufficient funds, the financial institution is clearly extending credit to that customer, and the product should be regulated as such. This means that credit should be extended only based on a determination that the customer has the ability to repay it, and payments should be repayable in manageable installments. Overdraft fees on debit card purchases and ATM transactions, in particular—which can easily be declined

http://www.nclc.org/images/pdf/pr-reports/Account-Screening-CRA-Agencies-BankingAccess101915.pdf (internal citations omitted).

at no cost to the customer—should be entirely prohibited unless they are covered under Regulation Z.

- **Rein in excessive fees.** The size of the overdraft fee is the engine that drives overdraft abuses. Typically, the size of the fee bears virtually no relation to the cost to the institution of covering the overdraft. The Credit CARD Act required that penalty fees on credit cards – including fees for exceeding the card's credit limit – be reasonable and proportional to the "violation." The Federal Reserve determined that this requirement included that the fee must be reasonable and proportional relative to the cost to the institution, and that the fee could not exceed the size of the violation. In the overdraft context, where overdrafts cost the institution very little, this would mean the fee should be significantly less than the average fee today, and should in no case exceed the size of the overdraft itself. Similarly, NSF fees are extraordinarily high given that processes are highly automated.

- **Limit overdraft fees to one fee per month, and six per year, and prohibit predatory posting practices.** Once an account has gone negative and the customer has incurred an overdraft fee, the customer should have sufficient time to bring the account back to positive before being charged additional fees. The CFPB should limit fees to one fee per month, and six per year; prohibit "sustained" or "extended" fees; and prohibit posting practices that result in unnecessary overdrafts and fees.

4. Protect the ban on compulsory use of electronic repayment as a condition of credit

The Electronic Funds Transfer Act (EFTA) and Regulation E prohibit creditors from conditioning credit on repayment by means of electronic fund transfers. This ban on compulsory use is critical for enabling consumers to maintain control over their funds and their deposit accounts. It also helps struggling consumers protect funds needed for necessities from lenders that attempt to take repayment off the top of an incoming deposit, leaving insufficient funds for food, rent, or medicine. The rule also gives lenders an incentive to underwrite for ability to repay.

Yet, the statutory ban on compulsory use of electronic repayment is widely evaded by lenders that obscure the fact that electronic repayment cannot be required or that impose coercive conditions on payments by other means. The CFPB should clarify Regulation E to make sure that consumers understand their choice of payment methods and do not effectively have their choice taken away by coercive conditions.

The CFPB should require that creditors disclose consumers' choice of payment methods in a clear and readily understandable manner before a choice is selected. The disclosure must make clear alternative payment methods.

Regulation E allows creditors to give consumers a reduced annual percentage rate (APR) or other cost-related incentive to choose electronic repayment. The CFPB should clarify that a discount must be modest, and that the cost of choosing another method of payment cannot be so great that no reasonable consumer would choose that method. Acceptable discounts include those offered by credit unions that, for small dollar loans, charge 21 percent APR without electronic repayment and 19 percent APR with electronic repayment. For larger loans, such as mortgages or student loans, some lenders offer a reasonable discount of 0.25 percent. Charges such as a $100 fee or large increases in the interest rate are coercive and deprive reasonable consumers of a real choice.

As the current Regulation E interpretation provides, the incentive should be "cost-related."[3] A modest increase in cost should be related to the risk to the lender of not receiving payment automatically, and should not discourage consumers from choosing a different method of payment.

Lenders should not be allowed to artificially and deliberately slow down funding of a loan for a consumer who chooses not to repay electronically. For example, some high-cost online lenders deliver funds electronically immediately if electronic repayment is chosen, but send a paper check that will not arrive for 7 to 10 days if the consumer chooses another means. Sending payment through the mail when the normal delivery method is electronic is merely a means of coercing the consumer. Slowing down funds delivery is especially coercive for lenders that cater to consumers who are likely to need funds quickly.

5. Prevent liability for fraudulent transfers in new, faster payments ("push payments")

In these days of increasing data breaches and identity theft, the protection provided to consumers by the EFTA and Regulation E against liability for unauthorized transfers is more important than ever. The CFPB should clarify and strengthen Regulation E to ensure that consumers can maintain confidence in existing and new electronic transfer systems and receive the protection mandated by Congress.

A number of new, faster payment systems have been launched or are under development. These systems may have security improvements over older payment methods and may make fraud and unauthorized charges less likely. One advantage of many of these systems is that they may require the consumer to take action to initiate ("push") a payment and may not allow an entity to debit ("pull") a payment from the consumer's account based only on a purported authorization.

While push payments can increase security, they do not eliminate the potential for fraudulent and unauthorized payments and, in some cases, may increase those risks. Today, telemarketing scammers may have to convince a consumer to visit a store in order to pay through an unusual payment method, such as a prepaid reload pack, gift card, or wire transfer. This can impede fraud and raise red flags. But with faster payments, an imposter or other criminal can simply tell the consumer to pay quickly through a method that that consumer already uses from the convenience of her home.

We have already seen how faster payment systems can result in more widespread and faster fraud.[4] As one article noted, Zelle's national advertising campaign "sets an expectation that Zelle can be used like a credit card, and scammers have figured out how to exploit this trust."[5]

The mere fact that the consumer pushed a payment does not mean that the payment is authorized. If that purported authorization is obtained through fraud – such as by claiming that the recipient is the IRS, is a grandson, or is the electric company – the authorization is invalid just as it would be if the

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[3] Reg. E, Official Interpretations § 1005.10(e)(1).

[4] Stacy Cowley, New York Times, "Zelle, the Banks' Answer to Venmo, Proves Vulnerable to Fraud" (Apr. 22, 2018), https://www.nytimes.com/2018/04/22/business/zelle-banks-fraud.html; Lauren Saunders, American Banker, "Will faster electronic payments mean faster fraud?"(Sept. 17, 2015), https://www.americanbanker.com/opinion/will-faster-electronic-payments-mean-faster-fraud.

[5] Kate Fitzgerald, Payment Source, "Are banks doing enough to protect Zelle users?" (Feb. 22, 2018), https://www.paymentssource.com/news/are-banks-doing-enough-to-protect-zelle-users-from-fraud.

consumer provided his bank account and routing number to the scammer (on the telephone or through the internet) for an ACH debit (pull) transaction. Moreover, in some faster payment systems, even if the payment must be pushed, it can sometimes be pushed in response to a request for payment, which may be fraudulent.

The CFPB should clarify that consumers are protected if a purported authorization is obtained through fraud, regardless of the manner in which the purported authorization is obtained or manifested. This is consistent with the EFTA's mandate that "the burden of proof is upon the financial institution to show that the electronic fund transfer was authorized."[6]

Consumers should be able to assert their protection against unauthorized push payments in the logical place: against their own institution – the institution that holds the account that was unlawfully accessed. The consumer's institution should, of course, be entitled to recover against the institution that received the payment and enabled the scammer, directly or indirectly, to access the payment system.

Clarifying protection against unauthorized push payments is not only consistent with the mandate of Regulation E, it also will lead to better fraud prevention efforts by giving incentives to the players who are in the best position to design safe payment systems, and will encourage financial institutions to better authenticate users of those systems.

Relying on warnings to consumers is an old-fashioned and ineffective fraud prevention method that cannot be relied on to protect consumers in faster payment systems. Certainly, consumers should be warned to push payments only to entities or persons whom they know and trust, but scammers can be incredibly deceptive and convincing.

Putting fraud prevention incentives with financial institutions and service providers – both the consumer's institution and the receiving institution(s) – is far more likely to result in improving methods of preventing fraud. These institutions can aggregate and share data, spot patterns and red flags, develop braking mechanisms in suspicious cases, and develop a variety of other practices all along the payment chain to prevent, spot, and remedy fraud.

The payments industry is also far more able than a consumer to absorb the loss of a given fraudulent payment. If the fraud is widespread, then the problem goes far beyond the consumer to the entities that allowed a scammer access to the payment system.

More information about fraudulent actors will also be available to everyone in the system if consumers have an incentive to report fraudulent push payments. If the answer from the consumer's bank is "Sorry, you authorized it," then the information will stop there and the receiving institution and payment system will not be able to spot bad actors and identify patterns.

Consumers will have more confidence in new, faster payment systems – which will benefit everyone who provides or uses those systems – if consumers know that they are protected from all types of fraud. Faster payment systems will suffer if they develop a reputation as hotbeds of fraud. Similar

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[6] 15 U.S.C. § 1693g(b).

considerations have led to changes in Great Britain's faster payments system to allow scam victims to recover their money more easily.[7]

Robust protection against unauthorized charges has worked well to give consumers confidence in credit and debit cards. Today, the card networks are continually improving fraud detection and often spot fraudulent charges long before the consumer even realizes that fraud has occurred. This strong protection has been critical to preventing consumers from losing faith in cards with increasing news of data breaches and identity theft.

6. Reject calls to create a consumer negligence standard that is not in the EFTA.

Some in the payments industry have called for Regulation E to be amended to impose consumer liability for unauthorized charges if the consumer was purportedly negligent. That change would directly counter the rule of Regulation E today and would impose a standard that has no basis in the statute.

Regulation E makes clear that consumers still have protection even if they could be deemed negligent, such as by writing a PIN number on a debit card.[8] The official interpretation of Regulation E correctly states that, under the EFTA, the extent of the consumer's liability is determined solely by the consumer's promptness in notifying the financial institution.[9] The CFPB is correct that "[o]ther factors may not be used as a basis to hold consumers liable."[10]

There is nothing in the EFTA that would support a contrary standard. The statute contains no qualifiers on the consumer's protection against unauthorized charges beyond (1) deadlines for reporting those charges, (2) an exception if the consumer authorized a person to use the access device (discussed below), and (3) an exception if the consumer benefited from the charge (making it less likely that the charge was truly unauthorized). The statute makes clear when consumers lose their protection, and it would be outside the CFPB's authority to open up a gaping hole for purportedly negligent transactions. To the contrary, the primary purpose of the EFTA is the creation of consumer rights and the statute is clear that protections cannot be waived.

Unauthorized transfers are far more likely to occur as a result of negligence on the part of financial institutions, merchants, and other companies than by consumers. Data breaches, inadequate security and authentication systems, and lax protection of consumer's sensitive personal information can lead to fraud on a widespread basis in far greater numbers than trivial one-by-one losses due to consumers writing their PIN numbers on their cards and then losing them without reporting the loss promptly.

Moreover, a negligence standard would be abused and asserted against consumers even when no negligence occurred. Even today, financial institutions at times resist addressing unauthorized transfers by claiming that the consumer authorized the transfer, at times in ludicrous situations. For example, one bank refused to credit the account of a senior who was in a residential rehabilitation hospital when a

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[7] Vicky Shaw, Independent, "Bank transfer scam victims could get money back more easily under new plans" (Nov. 7, 2017), https://www.independent.co.uk/news/business/news/bank-transfer-scam-victims-could-get-money-back-more-easily-under-new-plans-a8041366.html.
[8] 15 U.S.C. § 1693g; Reg. E, Official Interpretations § 1005.6(b)-2.
[9] 15 U.S.C. § 1693g; Reg. E, Official Interpretations § 1005.6(b)-3.
[10] Consumer Fin. Prot. Bureau, CFPB Consumer Laws and Regulations: Electronic Fund Transfer ACT 23 (Oct. 2013), available at www.consumerfinance.gov (CFPB Supervision and Examination Manual; original emphasis).

card was used at bar and ATM across the country. On another occasion, a bank rejected the claim of a 74-year-old senior whose account number was used on an online gaming site after the senior's data was subject to a data breach that she reported to the bank. Ordinary consumers who cannot file a lawsuit over small charges (and, most likely, are restricted by forced arbitration clauses) are powerless when banks reject their claims, and these problems would increase if banks could claim negligence by the consumer.

7. Protect Consumers from Deceptive Offers

Regulation DD implements the Truth in Savings Act, which governs disclosures and periodic statements for bank accounts, including checking and savings accounts. As discussed above, we urge the CFPB to restore plans to address overdraft fees abuses. As part of that effort, the CFPB should update the provisions of Regulation DD that govern advertising of "free checking." Regulation DD prohibits misleading or inaccurate advertisements, and prohibits advertisements that refer to an account as "free" or "no cost" if any maintenance or activity fee may be imposed. Banks that advertise "free checking," but derive substantial revenue from overdraft fees are engaging in misleading and inaccurate advertising. Banks should be prohibited from advertising "free checking" if the bank charges overdraft or otherwise encourages consumers to incur overdraft fees.

The CFPB should prohibit banks from charging monthly or inactivity fees on savings accounts. Those fees make any disclosures inherently deceptive. Regulation DD sets out the method of calculating and disclosing the interest rate, reflected as an annual percentage yield (APY). The APY disclosures are based entirely on the interest rates paid and do not account for fees charged. Yet some banks charge monthly fees on savings accounts. In this low interest rate environment, when balances are low, those fees can easily exceed any interest earnings. Not only does this make the APY deceptive, but it even makes the term "savings" misleading, as consumers can actually lose money if they put their funds in a savings account. This is exacerbated by the fact that some banks charge inactivity fees as well. Consumers – especially those who struggle to, but should be encouraged to, save – should not be misled about the usefulness of a savings account.

8. Protect Consumers Who Dispute Medical Debt Due to Billing Errors or Insurance Disputes

Medical debt can have a significant impact on a consumer's credit history. The Bureau's own research found that over half (52.1 percent) of debt collection entries on consumer credit reports was for medical debt and that nearly one in five consumers with credit reports had an entry for medical debt.[11]

Many times, a medical bill is sent to a debt collector as a result of a billing error or an insurance dispute (e.g., wrong code, inadequate documentation), which can be of extended duration. Some providers automatically refer a bill to a debt collector in as little as 60 or 30 days, even though the bills are ultimately paid by insurers.[12] This damages the consumer's credit history and credit score even after the bill is paid, as an account reported as a collection matter may remain on a credit report even after the balance is paid off.[13] These types of debt collection items say nothing about the consumer's creditworthiness.

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[11] Consumer Fin. Prot. Bureau, Consumer credit reports: A study of medical and non-medical collections, at 5, Dec. 11, 2014.
[12] *Id.* at 26.
[13] National Consumer Law Center, Collection Actions § 9.3.5.1 (4th ed. 2017), *updated at* www.nclc.org/library.

Thus, we recommend that, if a consumer disputes a collection item on his or her credit report because it is the result of a billing error or insurance dispute, that debt should be specially marked as such with a specific code of "insurance/medical billing dispute." Furthermore, the CFPB should require that such debts be excluded from any credit score and not be considered by lenders. The CFPB has authority to adopt such a rule under Section 604(g)(2) of the Fair Credit Reporting Act, 15 USC § 1681b(g)(2), which prohibits creditors from using medical information in considering a consumer's eligibility for credit unless permitted by Regulation V.

Currently, Regulation V permits the consideration of medical debt. The CFPB has the authority, however, to amend Regulation V, and to exclude consideration of medical debt that is the subject of provider-insurer billing errors and disputes. Permitting the consideration of this type of disputed debt, particularly when the dispute has nothing to do with credit worthiness, amounts to punishing a consumer for having a medical condition.

Thank you for considering these comments.

Respectfully submitted,

WOODSTOCK INSTITUTE