

To the Point!

legal, operations, and strategy briefs for financial institutions December 5, 2012



General Purpose Reloadable Pre-paid Cards

General purpose reloadable prepaid cards (“GPR cards”) are expanding in usage. GPR cards are offered for general retail use, are network branded and can receive direct deposits of government benefits. For these reasons GPR cards may be used by the unbanked or underbanked as a substitute for a checking account. While the consumer regulatory scheme that applies to deposit accounts accessed by a debit card does not apply, the warnings sent by the Consumer Financial Protection Bureau (“CFPB”) in recent enforcement actions assessing fines against certain card

issuers are a strong message that any consumer card product must be established on nothing less than clear terms. The CFPB, now responsible for rule-writing authority under Regulation E, issued an Advance Notice of Proposed Rulemaking (“ANPR”) soliciting comment from the public on GPR cards, noting that GPR cards are not yet subject to Regulation E and requesting input on how to ensure that consumers who use GPR cards are adequately protected. The FTC submitted a comment to the ANPR expressing concern regarding unfair and deceptive practices involving the sale of GPR cards, citing enforcement actions it had taken against companies involved in the marketing of GPR cards, and urging the CFPB to adopt consumer protections including limiting consumer liability for fraud and unauthorized use, imposing disclosure requirements and mandating error-resolution procedures. While the CFPB has not released its findings from the ANPR or proposed any rules, banks and other financial institutions that offer GPR cards to consumers should (1) consider implementing, as a matter of contract, product terms establishing liability limits for fraud and unauthorized use, dispute-resolution procedures, and (2) provide adequate disclosures to consumers concerning the cost of using the card, including ways to limit fees. This may help to avoid claims of unfair and deceptive trade practices and to minimize future compliance issues related to anticipated CFPB regulation.



“Commercially Reasonable” Online Banking Security Procedures

Financial institutions offering online banking products must comply with the FFIEC guidelines for Internet Banking Authentication and they must also offer “commercially reasonable” security procedures to their customers under the Uniform Commercial Code (“UCC”). While the UCC allows a bank to shift risk to its customers through contractual provisions, recent court cases have established that a court will scrutinize a bank’s security procedures and make the determination

whether the procedures offered are commercially reasonable as a matter of law. Following the FFIEC guidance alone may not be sufficient in the case of fraud for a court to find that, in fact, the bank’s security procedures were - as a matter of law - commercially reasonable if the bank has not offered and implemented available security procedures for its customers. The financial institution must use appropriate technology under the FFIEC guidance to authenticate customers and customer transactions, and its employees must use the technology to monitor those transactions and promptly use information identifying potential fraud to block transactions and inform clients. Financial institutions should review their agreements and the procedures that are provided to clients to evaluate whether the procedures are proper (i.e., commercially reasonable) for the type, size and frequency of transfers they originate. Finally, the financial institution should make certain that the procedures offered to clients are implemented correctly.



Servicemember's Civil Relief Act Updates

Protections for service members under the Servicemember's Civil Relief Act ("SCRA") have received continued attention in the media as well as scrutiny by federal regulators. Following the Interagency Guidance issued by the banking regulatory agencies on practices that may pose risks to homeowners who are serving in the military, recent changes to the SCRA and other protections for service members related to mortgage foreclosures are worth noting to ensure compliance by financial institutions and mortgage servicers. Effective February 2, 2013, sale, foreclosure or seizure of property proceedings are invalid for 12 months from the date the service member is released from active duty, extended from 9 months under the existing rule. Similarly, the postponement of foreclosure benefits will be extended to the surviving spouse if there is a service-related death. These enhanced protections are effective through December 31, 2014. Beginning January 1, 2015, the 12-month protections will change to 90 days. In addition, the Federal Housing Finance Agency ("FHFA") changed its short sale policies for mortgages owned or guaranteed by Fannie Mae or Freddie Mac. FHFA worked with Fannie Mae and Freddie Mac to merge four programs into one Standard Short Sale/HAFSA II. Fannie Mae and Freddie Mac issued standard short sale guidelines effective November 1, 2012. These changes are intended to simplify and streamline existing guidelines and increase efficiency to help more borrowers avoid foreclosure. Notably in the new short sale policies, active duty service members will not be asked to contribute cash or a promissory note toward a shortage if the home was purchased on or before June 30, 2012, and they will receive an affirmative deficiency waiver at closing. As a result of increased regulatory scrutiny and changes to law, financial institutions and mortgage servicers should review and update their policies and procedures and ensure that their internal controls operate effectively to achieve compliance. Financial institutions and mortgage servicers should always determine a borrower's military status prior to taking any action and research military status periodically to ensure continued compliance.

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To the Point! is a summary of items of interest and current issues for financial institutions with primary focus on regulatory, consumer, and corporate issues. Chapman and Cutler LLP maintains a dedicated practice group with expertise to counsel on these issues and other enterprise risk management matters facing financial institutions. If you would like to discuss any of the items contained in these briefings or other legal, regulatory, or compliance issues facing your institution, please contact one of the partners in our Bank Regulatory Group:

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