

2008 Payments Conference

Payments Fraud: Perception versus Reality

Public and Private Responses to Payments Fraud:
Consumer Protection Laws

Judith Rinearson
Bryan Cave LLP



*A Broader Perspective*SM

Existing Legal Protections

- Credit Cards
- Debit Cards
- Stored Value / Prepaid
- Person to person

Credit Cards

- A payment card linked to a consumer's credit account
- The card is linked to one of the 4 major payment networks – American Express, Discover, MasterCard and Visa
- Consumers use the card to purchase goods/services, which are later billed and paid – 20-30 days later.
- Among the most mature payment products – usable globally

Credit Cards

- Subject to the Truth in Lending Act (TILA) and Regulation Z
- State consumer protection laws
- Card issuer policies and account agreements
- Card Network “zero liability” rules
- Card Network “merchant chargeback” rules

Debit Cards

- A payment card linked to an individual's bank account (usually checking or savings) so that purchases of goods/services or withdrawals of cash are immediately debited from that account.
- Can be issued either as a PIN-based debit (ATM) card or as a signature-based debit card from one of the bankcard associations.
- PIN-based: Works on EFT networks (STAR, Pulse, etc)
- Signature-based: Works on the bankcard association networks (Visa and MasterCard)

Debit Cards

- Subject to the Electronic Funds Transfer Act (EFTA) and Regulation E
- State consumer protection laws
- Bank issuer policies and account agreements
- Bank Payment Network “zero liability” rules
- Bank Payment Network “merchant chargeback” rules
- EFT Association Rules

Stored Value (or “Prepaid”) Cards

- A payment card associated with a specified amount of value in prepaid funds. The cards are NOT linked to an individual’s bank account. Instead the prepaid funds are usually held in a “pooled” account.
- When purchases of goods/services or withdrawals of cash are made, the electronic record associated with that card is immediately adjusted to reflect the decrease in the specified value associated with that Card.
- Most work on the four payment systems networks (Amex, Discover, MasterCard, Visa) similar to signature debit; some have PIN-based ATM access through an EFT network as well.

Stored Value (or “Prepaid”) Cards

- NOT subject to the Electronic Funds Transfer Act (EFTA) and Regulation E ***except for Payroll Cards***
- State consumer protection laws regarding expiration dates, fees, disclosures.
- Cardholder agreements
- Bankcard Association or Payment Network “zero liability” rules
- Some offer Bankcard Association or payment Network “merchant chargeback” rules
- State Unfair and Deceptive Acts & Practices (UDAP)

Person to Person (P2P) Payment Systems

- A “mediated” payment service in which both the payer and recipient of funds must open an online account to participate in the service.
- The payer funds the P2P account from a credit card or bank account.
- The payment service moves the funds from the payer to the recipient upon the payer’s verified instructions, usually given by email or by cell phone
- The system does not rely on Bank Association, EFT or other Payment Networks.

Person to Person (P2P) Payment Systems

- NOT subject to the Electronic Funds Transfer Act (EFTA) (No Consumer Asset Account) and Regulation E – Nor Reg Z – (except to the extent that the P2P account is loaded from a bank account transfer or credit card)
- State Unfair and Deceptive Acts & Practices (UDAP)
- Primary rules/protections arise from User agreements and payment system rules
- Secondary protections from state money transmitter laws.

Applying Existing Rules

Consumer claims based on fraudulent, unauthorized transactions.

Liability for Unauthorized Transactions - Fraud

- **Credit Cards**

- Revealed through Billing Statements**

- **Reg Z – Unauthorized fraudulent transactions - \$50 cap, regardless of consumer’s negligence and regardless of when the unauthorized transaction is reported; \$0 liability for mail, phone and internet charges**
 - **Network Zero Liability policies usually for 90 days. Many card issuers do not assess the \$50 permitted under Reg Z.**
 - **Contractual protections generally mirror Reg Z**

Liability for Unauthorized Transactions - Fraud

- **Debit Cards - Regulation E**

- Revealed through Bank Account statements**

- Limits liability to \$50 if consumer reports loss/theft within 2 days of learning and \$500 if consumer reports after 2 days but within 60 days of being sent statement reflecting fraudulent transaction. Consumer's own negligence is not a factor in assessing liability. Limits liability to \$0 for mail, phone, and Internet charges that are fraudulent.
 - Card Association Zero Liability Policies
 - Contractual protections

Liability for Unauthorized Transactions - Fraud

- **Stored Value –Network Branded Prepaid Cards Revealed through requested statements, online account information, or telephone requests**
 - No Federal Law protections – except for Payroll Cards
 - State laws don't address
 - But - Card Associations Zero liability policies
 - And - Cardholder agreements have contractual protections

Typical Prepaid Cardholder Protection Language

- Contact us at once if you believe your Card has been lost or stolen. Telephoning is the best way to minimize your possible losses. If you believe your Card has been stolen, or that someone has used your Card or made purchase transactions without your permission, call us toll free at 1-800-XXX-XXXX. **You will not be liable for unauthorized transactions on your Card if you notify us promptly and you are not grossly negligent or fraudulent in the handling of your Card.** If you fail to notify us promptly and you are grossly negligent or fraudulent in the handling of your Card, you could lose all the value available on your Card.
- Also, if you become aware of transactions that you did not make, tell us at once. **If you do not notify us within sixty (60) days after you became aware of the transactions, you may not get back any value you lost after the sixty (60) days if we can prove that we could have stopped someone from taking the value if you had notified us in time** and you are grossly negligent or fraudulent in the handling of your Card. If you notify us that your Card has been lost or stolen, we will close your Card Record to keep losses down.

Unauthorized Transactions - Fraud

- **Person to Person (P2P) Payment Systems
Revealed through online account review**
 - No Federal law protections
 - State laws don't address
 - But – Some Payment Network Zero liability policies apply
 - Contractual protections

P2P [Paypal]

User Agreement Language

- If you report and we verify that there has been an Improper Account Access related to your Account, we will reimburse you in full for all unauthorized transactions sent from your Account that occur within 60 Days of the time that you knew or should have known about the Improper Account Access. If you do not report the Improper Account Access to PayPal within 60 Days of the time that you knew or should have known about it, we will still reimburse you in full for all unauthorized transactions that took place within or before that 60-Day period, but you may be liable for all unauthorized transactions resulting from the Improper Account Access that occur on Day 61 and beyond (if we can demonstrate that we could have avoided any losses if you had notified us in a timely manner).

Summary

- Federal regulation for newer electronic payments is very limited.
- Nevertheless, most products provide protections for consumers with respect to
 - Unauthorized Transactions
 - Error resolution

Where no federal regulation exists, however, there is more discretion for banks and issuers

Qs & As

Judith Rinearson
Bryan Cave LLP
1290 Avenue of the Americas
New York, NY 10104
(212) 541-1135
Judith.rinearson@bryancave.com