Payments Pros – The Payments Law Podcast*: *2023 Payments Year in Review: Subscriptions, FedNow, and More!
Hosts: Keith Barnett, Carlin McCrory, Josh McBeain

Keith Barnett:

Welcome to another episode of *Payments Pros*, a Troutman Pepper podcast, focusing on the hi ghly regulated and ever evolving payment processing industry. This podcast features insights fr om members of our fintech at payments practice, as well as guest commentary from business l eaders and regulatory experts in the payments industry. My name is Keith Barnett, and I'm one of the hosts of the podcast.

Before we jump into today's episode, let me remind you to visit and subscribe to our blogs, ConsumerFinancialServicesLawMonitor.com and TroutmanPepperFinancialServices.com. Don't forget to check out our other podcasts on Troutman.com/Podcast. We have episodes that focus on trends that drive enforcement activity, digital assets, consumer financial services, and more. Make sure to subscribe to hear the latest episodes.

Today, I am joined by my co-hosts, Carlin McCrory and Josh McBeain for the final part of our two-part series that takes a look back on what we've seen in the payments landscape in 2023, and also, what we expect in 2024. As a reminder, if you haven't already, make sure to listen to part one of our series that discussed the CFPB's oversight of big tech and the war on fees. Today's episode will focus on subscriptions, FedNow, the Money Transmission Modernization Act, and Nacha. Carlin and Josh let's just jump right into today's topics.

Carlin McCrory:

Thanks so much, Keith. The first theme that Josh and I are going to cover today are canceling subscriptions. On January 19th of this past year, in its circular, the CFPB said that negative option subscription services might constitute unfair, or deceptive practices under the Consumer Financial Protection Act, when a seller does one of three things. The first of those three things are misrepresenting, or failing to clearly disclose the material terms of the program. The second is failing to obtain consumer’s informed consent. The third is misleading consumers who want to cancel, or creating unreasonable barriers to cancellation, or failing to honor cancellation requests.

A negative option subscription service generally refers to a situation where a seller may interpret a consumer's silence, failure to take an affirmative action to reject the service, or failure to cancel an agreement as acceptance of the subscription. You can think about this as any of those TV subscription services that companies offer falls within a negative option subscription most of the times.

The CFPB stated that its impetus for targeting these negative option subscriptions is in response to consumer complaints, and it's part of a bigger initiative by the bureau and the FTC to combat what they call dark patterns, or website design features allegedly used to trick, or trap consumers. I think, the ultimate thing to get out of this is if you offer a negative option subscription service, you have to be aware that there are both state and federal laws on the topic. One thing of note, particularly here, is that it has to be easy for the consumer to cancel the subscription, and ideally, it should be just as easy for the consumer to cancel the subscription as it was for them to initially enter into the agreement. Josh, do you want to go ahead and talk about what the FTC had to say about this?

Josh McBeain:

Absolutely. Thank you, Carlin. I'll just add, I'm going to talk about this more here in a moment that companies that rely on subscription programs to generate revenue should pay close attention to what the CFPB's done and what you just mentioned in the space, and also, the FTC rulemaking, because the final rule may impact their operations. Taking a step further, the FTC last year in March issued a notice of proposed rulemaking to amend its negative option rule, because the FTC actually has a negative option rule on the books now.

What the FTC describes as a negative option generally falls into four categories. First, a pre-notification plan. Second, continuity plans. Third, automatic renewals. And fourth, free trials. Now, pre-notification plans for the sale of goods are the only type of negative option covered by the FTC's current rule. They generally describe a situation where a seller may interpret a consumer's silence, or failure to take an affirmative action as an acceptance of goods, for example, a book of the month club.

The FTC's proposed rule would amend the current negative option rule in multiple ways. It would expand the scope of the current rule, because the proposed rule would apply to all forms of negative option marketing, including pre-notification plans, which are currently covered and they would still be covered, but would expand to the other three types, so continuity plans, automatic renewals, and free trial offers.

Second, the proposed rule would require disclosures. The proposed rule would require sellers to clearly and conspicuously disclose certain information outlined in the proposed rule prior to obtaining the consumer's billing information. It would also require sellers to obtain certain affirmative consents from consumers and refrain from including any information that interferes with, or detracts from the consumer's ability to provide informed consent, and sellers would have to maintain a record of the consumer's consent.

Finally, the proposed rule, and Carlin mentioned this and the CFPB has taken issue with this as well. The FTC's proposed rule attempts to make cancellations easier and it does us in multiple ways. The FTC's proposed rule requires sellers to provide a cancellation option through the same medium use to enroll the consumer, whether that be through the internet, telephone, mail, or in person. Also, under the FTC's proposed rule, before making pitches for additional offers, or modifications to save, or prevent cancellations, sort of making a sales pitch when someone has to cancel it to prevent that, under the proposed rule, the seller must first ask consumers whether they would like to hear those saves, or pitches for additional offers. If the consumer declines, the seller must immediately proceed to cancel the service.

Finally, to make cancellations easier, the proposal requires sellers to provide an annual reminder to consumers enrolled in negative option plans, involving anything other than physical goods. Such reminders must identify the product or service, the frequency, and amount of charges, and the means to cancel. Under the proposed rule, the reminder requirement does not apply to subscription services for physical goods, since, according to the FTC, each physical delivery serves as a reminder of the contract.

This proposed rule was published by the FTC in March of 2023. In June of 2023, the FTC concluded its 60-day public comment period. In response to the notice of proposed rulemaking, several commenters requested an informal hearing on the proposed rule. That informal hearing will be conducted virtually on January 16th, 2024. This is an ongoing issue that we're still tracking, and as Carlin mentioned, and I mentioned it before we started talking about the proposed rule, companies that have subscription services should really pay attention to what the CFPB and the FTC do in 2024, and we expect more activity in the space.

Keith Barnett:

Can I add something to that? Just a little bit more color from the litigation and enforcement perspective. Over the past several years, the FTC has filed several enforcement actions against payment processors and their merchants that use the negative option features, and they have sued under the telemarketing sales rule, ROSCA, and Section 5 of the FTC Act. Payment processors, money transmitters, and banks in the case of the CFPB must be aware of merchants who use these negative option features.

From the payments perspective, if you're a bank, payment processor, or money transmitter, if you receive a higher percentage of chargebacks, or unauthorized returns, the regulators will not only investigate your merchant if it becomes exceedingly high, especially if your merchant targets more of the lower income, or people who are more likely to take out subprime loans. But the regulators may also add the payment processor, or the bank in the case of the CFPB to that enforcement action for not stopping the payments from being affected.

The CFPB and the FTC have both the ledge in these lawsuits that unauthorized returns that are higher than the notchet threshold are warning signs, or flags. Be careful of that. It is a choke point type of argument that the regulators have been making over the past several years, and I believe they will continue to make it into 2024.

Carlin McCrory:

Keith, wasn't there some movement as well on sole proprietorships being treated as consumers under some of the litigation?

Keith Barnett:

Yeah, that's right. Also, in the litigation, something else to look out for 2024 is, and this has been the FTC, so not as much the CFPB, but if there is a bigger company that is in a business-to-business contract with a small mom and pop shop, and the FTC believes that that bigger company is taking advantage of the smaller mom and pop shop with respect to payments, anything, that smaller mom and pop shop is going to be treated as a consumer for the purpose of Section 5 of the FTC Act. That's definitely something to also look out for.

Josh McBeain:

That's great, Keith and Carlin. I think now, I'm going to kick it over to Carlin to speak about FedNow, which was a big development in 2023.

Carlin McCrory:

Yeah. Thanks, Josh. As he said, FedNow was a huge development in 2023 and very welcome development. We've already released two separate podcasts on FedNow, so please listen to those if you'd like further detail. Broadly speaking, FedNow is a service for instant payments built by the Federal Reserve, and it allows financial institutions to offer instant payment transfers for their customers.

FedNow also allows financial institutions to improve their customers' experience by granting them instant access to transfers of money without having to wait. As you can imagine, with instant transfers, or instant anything, this poses another avenue that fraudsters can pursue, and financial institutions have to be aware, at least, of the unique risks posed by a service like FedNow. Generally, it's our understanding that adoption of FedNow has been great, but maybe just a little bit slower than expected possibly, because some institutions want to see how this plays out and see how it works with other institutions who have adopted the service. Our understanding overall is that it's going really well, and we expect a host of financial institutions to adopt the service this year. Keith, you want to talk a little bit about the Money Transmission Modernization Act?

Keith Barnett:

Sure. Thanks, Carlin. By way of background, the Conference of State Banking Supervisors issued a model rule several years ago concerning money transmission. The CSBS had hoped that all of the states would adopt this model rule on money transmission in its entirety. That has not happened. For our clients, the most significant parts of the MTMA are the agent of the payee exemption, the agent of the bank exemption, and the express inclusion of payroll processors within the definition of money transmission. That had never happened before.

With respect to the year-end review in 2023, the states of Georgia, Iowa, Maryland, Minnesota, Nevada, North Dakota, Tennessee, Texas, and West Virginia adopted the MTMA pretty much as written by CSBS. Most significantly to our clients, these states have included agent of the payee, agent of the bank, and included payroll processing within the definition of money transmission.

There has not been precise uniformity as the CSBS had hoped, especially on bond requirements, whatever the bond is, the minimum and the maximum amounts, net worth requirements for actually being a money transmitter and getting a license, and also, whether or not financial statements will be required and whether or not they would be audited, or unaudited in how far back they would go.

Interestingly, Iowa placed a moratorium on the enforcement of the part of the law that affects payroll, and that moratorium will end in July of this year, 2024. Do not be surprised if Iowa decides that it will not include payroll within its final definition of money transmission after their state lawmakers meet this year. Also, important to recognize and note that Nevada had town hall meetings to discuss MTMA, but no substantive changes were made that affect any of our clients, or any of our listeners.

The other thing that I want to bring up is that Alaska, New Hampshire, Hawaii, and South Dakota all passed significant portions of the MTMA, like agent of the payee and agent of the bank, but these states did not include payroll within their definition of money transmission. I do know that New Hampshire has proposed to include payroll, but it does not look like that will pass in 2024. In any event, we will keep you posted throughout the year on MTMA as more states look to adopt bits and pieces of it. We expect to see a lot of action this year, but then the question is whether or not there ever will be uniformity, and I just don't see that based upon the way things have been going so far.

Then next, we have a Nacha update. Shameless self-promotion here, we did a podcast with Jordan Bennett, who is the Senior Director of Network Risk Management of Nacha. During that podcast, Jordan was extremely informative, and I recommend that all of you listen to that podcast, if you have not already done so, and listen again if you've already listened to it, as we might get closer and closer to the proposals becoming actual Nacha rules.

During that podcast, we did discuss Nacha's release of a new risk management framework for the era of credit push fraud. These are my words, not Jordan's, not Nacha's, but this is Nacha's response on dealing with the peer-to-peer fraud payments that have been increasing year over year. The objectives of the framework were to increase awareness of fraud schemes that utilize credit push payments. Secondly, they want to reduce the incidence of successful fraud attempts. Third, they want to improve the recovery of funds after frauds have occurred. Because when you had a case of what I will call friendly fraud, where an unwitting consumer provides their credentials to a fraudster under Reg E, it is difficult, if not impossible, for the consumer to receive their money back from the bank. They are just out of luck on that for the most part.

As a part of implementing the objectives, Nacha requested comment on seven proposals related to ACH credit risk management. These seven proposals were, first, expanding commercially reasonable fraud detection. Secondly, RDFI monitoring and receive credits. Third, the expanded use of return reason code R17. Fourth, expanded use of reversals for fraud recovery. Fifth, additional exemption from funds availability requirement. Sixth, a standard company entry descriptions. Seventh, standard use of individual name field.

Now, I'm not going to go into any details on these, because they are already in our prior podcast that you should listen to. Also, we have written about it as well. There are many avenues through which you can find out more information about this. Then the last thing that I do want to discuss about that particular Nacha update is that Nacha did request comment on two proposals related to ACH debt risk management. The comments were due, I believe, last summer. So, it's too late to get in a comment, but just wanted to remind you of that. Those comments related to the timing of a written statement of unauthorized debit, and the other comment related to whether the RDFI must properly return an unauthorized debit.

Then lastly, Nacha requested information on four additional topics. These four topics were, should the Nacha rules implement a new return threshold for ACH credit returns? Second, should the NACHA rules identify and define third-party receivers as a type of participant in the ACH network and apply rules accordingly? Third, should the Nacha rules require that when an RDFI provides early funds availability and must employ a risk-based approach in determining eligibility? Fourth, whether a new notification of change would be useful to identify when there's a mismatch between the SEC code and the account type.

A lot there to unravel with Nacha. We expect a lot more from Nacha this year with respect to proposed rulemaking and also, bulletins and things of that nature. We should be hearing a lot more from Nacha in April of this year, of 2024. Stay tuned to that, because we'll try to have Jordan, or someone else back on from Nacha, and we will definitely talk about these things. Josh, do you have anything to say about EWA?

Josh McBeain:

Yes. Thanks, Keith. It was a highly active space last year at the state level. Earn wage access, or EWA saw multiple state legislatures proposed legislation that would regulate this EWA products in one way or another. Some legislation actually passed in a few states. We also saw state legislatures issue proposed regulations and interpretive opinions on EWA. We recorded a full podcast episode that covers the state level EWA topics and provides an overview of what has happened with EWA products at the federal level over the past couple years. We would strongly encourage you, if you want to learn more about the current state of play and the EWA space to go listen to that episode. In 2024 already, we have seen multiple states issue proposed EWA legislation. Thus, we anticipate that the EWA will be an active space in 2024 and beyond.

Keith Barnett:

Thanks, Josh. Also, just to piggyback off of that with respect to EWA, you have some EWA fintech providers. EWA delves in through some of the things that Carlin talked about in our last episode with respect to larger participants. I mean, because theoretically, if you have EWA providers who have a sufficient client base, right? What are they, 5 million transactions? even if they are not touching the money, they're just providing the technology to facilitate EWA related transactions. That could unwittingly put some EWA providers within that larger participants group, if the law proposed by the CFPB stays the same. That's something else to look out for in 2024 and in later years.

All right. Well, Carlin and Josh, thank you for joining me today. Thank you to our audience for listening to today's episode. Do not forget to visit our blogs, ConsumerFinancialServicesLawMonitor.com and TroutmanPepperFinancialServices.com. Subscribe, so you can get the latest updates. Please, make sure to also subscribe to this podcast via Apple Podcasts, Google Play, Stitcher, or whatever platform you use. We look forward to the next time.