

What's in Store in Consumer Protection?

From the Editors

Welcome to the Summer 2021 edition of the *What's In Store* newsletter. In this issue, **Edward F. Glynn Jr.** and **Jeffrey C. Ankrom** at Locke Lord LLP explain the consequences of the AMG decision, in which the Supreme held that Section 13(b) does not give the FTC the authority to seek, or federal courts the authority to award, monetary relief. Edward F. Glynn Jr. and Jeffrey C. Ankrom review the history of Section 13(b), the consequences of the AMG decision and shares with us their thinking on FTC's pending cases and future possible strategies. Next, **Jenna Kramer** at Unilever shares her perspectives working as an in-house counsel and her learnings transitioning from external counsel to in-house counsel. Lastly, we would like to congratulate Rohena Rajbhandari (Boston College Law School '22) for winning the first place in the ABA's 2021 Consumer Protection Committee Law Student Essay Contest. The winning essay "Finding Venmo: Applying Consumer Protection Regulations to Peer-to-Peer Payment Platforms" addresses critical consumer abuses prevalent in peer-to-peer (P2P) payment platforms, such as Venmo.

Please contact any of the Editors to get more involved or submit an article for publication.

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The Future of FTC Redress Authority: Consequences of the AMG Decision

By Edward F. Glynn Jr. and Jeffrey C. Ankrom

Locke Lord LLP

Disclaimer: All answers and opinions shared by the authors are of their own.

In early summer, 1980, H. N. Singer, Inc. was selling fraudulent frozen pizza franchises for about \$25,000 apiece, cheating mostly retired people out of significant portions of their savings. When the “franchise” purchasers for “Hot Box Pizza” met their supposed customers, like bars and bowling alleys, their “customers” had never heard of them or their frozen pizza product. Because the franchise sellers used fake drivers’ licenses and disguises, the Federal Trade Commission was called to investigate the identities of the company’s principals and the banks where the victims’ money was initially deposited. One of the authors, then a lawyer in the FTC’s Office of General Counsel, was asked to put together a case that would freeze the funds before the gang could transfer them to an offshore account, and come up with a theory to obtain redress for the victims.

However, many of the purchasers were not covered by the FTC’s Franchise Rule; thus, Section 19 of the FTC Act, which specifically allows monetary recovery for violating the FTC’s rules, was unavailable. Instead, applying an implied redress theory established in the Securities and Exchange Commission’s cases, the FTC argued that the power in Section 13(b) to obtain a permanent injunction necessarily implied the authority of a federal court to grant full equitable relief, including redress. The Ninth Circuit upheld the order to freeze assets, stating that where Congress gave the authority to grant permanent injunctions under Section 13(b), that also “gave the district court authority to grant any ancillary relief necessary to accomplish complete justice” including ordering rescission of contracts and freezing assets. *FTC v. H. N. Singer, Inc.*, 668 F.2d 1107, 1113 (9th Cir. 1982).

The H. N. Singer case became a landmark decision that established the FTC’s authority to use Section 13(b) to seek equitable relief for consumers in the form of restitution, rescission of contracts, disgorgement of ill-gotten gains, and other forms of equitable monetary relief. Over the 40 years following the H. N. Singer case, the FTC used this interpretation of Section 13(b) to recover billions of dollars for consumers including \$483 million in 2020 alone.

1. The Supreme Court held that Section 13(b) does not allow the FTC to seek monetary relief

That 40-year history ended on April 22, 2021, when the Supreme Court unanimously held that Section 13(b) only provides for injunctive relief, not for recovery of damages. In *AMG Capital Management, LLC v. FTC*, No. 19-508, 2021 WL 1566607 (Apr. 22, 2021), the FTC sued a payday lender that advertised loan products online, but, the FTC alleged, misled consumers regarding the amount they had to repay. Unless consumers took affirmative steps to opt out, the loan would automatically renew, causing consumers to pay more than three times the amount of the loan. The FTC sued the lender and sought restitution under Section 13(b). However, the Supreme Court held that Section 13(b), by its terms, only granted authority to seek “a permanent injunction” in a court action where a person “is violating, or is about to violate” any law enforced by the FTC, not to remediate past violations. While the Supreme Court noted the 40-year enforcement history beginning with the H. N. Singer case, the Supreme Court struck down the FTC’s authority to seek restitution through Section 13(b).

The AMG decision was not unexpected. Several courts had criticized the FTC’s use of Section 13(b) in recent years. For example, the Third Circuit held that the authority to seek injunctive relief against future conduct does not allow for disgorgement of ill-gotten gains, because “[d]isgorgement deprives a wrongdoer of past gains,” not future conduct. *FTC v. AbbVie Inc.*, 976 F.3d 327, 376 (3d Cir. 2020). The Third Circuit previously held that the FTC can only bring actions under Section 13(b) to enjoin a violation of the law that “is” occurring or “is about to” occur, not for a past violation, for which it must use its administrative process under Section 5(b). *FTC v. Shire ViroPharma, Inc.*, 917 F.3d 147, 159 (3d Cir. 2019).

On this backdrop, the Supreme Court not only held that Section 13(b) only has prospective effect, but also held that the authority to seek injunctive relief does not also include broader



equitable remedies, such as restitution or disgorgement of assets.

2. What enforcement strategies will FTC use next?

Without the ability to seek monetary relief through Section 13(b), the FTC will likely increasingly coordinate its enforcement activities with state attorneys general who are empowered by their states' laws to seek restitution on behalf of consumers. On May 11, 2021, speaking with a panel of state attorneys general, the FTC's acting chair Rebecca Kelly Slaughter acknowledged the restrictions that the AMG decision placed on the FTC's ability to seek monetary relief for consumers and expressed that the FTC would partner more frequently with state attorneys' general who have authority pursuant to their states' statutes to seek monetary relief.

About a week later, the FTC joined with the attorneys general and enforcement officers of six states to file an action against Frontier Communications, alleging that it failed to deliver the maximum internet speeds that it advertised and sold to consumers. The FTC based its authority on Section 13(b) to seek injunctive relief only. However, the complaint also seeks restitution through the states' attorneys general based on their authority under state statutes like the California Unfair Competition Law.

Cooperating with state attorneys general enables the FTC to provide restitution to some consumers. The FTC has been coordinating enforcement actions with state attorneys general for decades. However, only those consumers who live in states whose attorneys general participated in the complaint will receive monetary relief in these actions. The complaint against Frontier Communications was only joined by the Attorneys General of Arizona, Indiana, Michigan, North Carolina, and Wisconsin, and for California by the District Attorneys of Los Angeles County and Riverside County. While there have certainly been cases involving a coordinated effort of a dozen or more states, such coordinated actions have never involved all 50 states' attorneys general to provide nationwide relief.

In addition to increased cooperation with state attorneys general, the FTC is likely to make greater use of its administrative remedies and other enforcement powers. In the AMG decision, while the Supreme Court struck down the FTC's use of Section 13(b) to obtain monetary relief, the Supreme Court noted that several other remedies that the FTC can use to prosecute unfair and deceptive practices and provide redress to consumers, including the following:

- a. The FTC can pursue an administrative hearing under Section 5 of the FTC Act, at which the

FTC can make findings of fact regarding the act or practice that is deemed to constitute an unfair method of competition or unfair or deceptive act or practice, and issue a final cease and desist order against the act or practice. After an appeal period, the findings of fact are conclusive in further proceedings. A final administrative order itself cannot include restitution or monetary relief, but the FTC can seek civil monetary penalties for a knowing violation of the final cease and desist order.

- b. The FTC can still seek injunctive relief under Section 13(b) against any person or entity that "is violating, or is about to violate, any provision of law enforced by the FTC." Using Section 13(b) as interpreted by the Supreme Court still provides the FTC with broad authority to seek temporary restraining orders, preliminary injunctions, or permanent injunctions, until the FTC can bring enforcement actions through the administrative process of Section 5.
- c. The FTC can also initiate civil actions under Section 19, for a violation of any FTC rule respecting unfair or deceptive acts or practices or for violating a final cease and desist order, if "a reasonable man would have known under the circumstances" that the act or practice "was dishonest or fraudulent." Under Section 19, a court can award "rescission or reformation of contracts, the refund of money or return of property, the payment of damages, and public notification respecting the rule violation or the unfair or deceptive act or practice," but not punitive damages.

So, while the AMG decision curtailed one powerful enforcement mechanism used by the FTC to seek restitution, the FTC is by no means toothless. As a result of the AMG decision, the FTC will likely shift its enforcement strategy to use one or more of these other remedies more frequently.

3. What happens to the FTC's currently pending cases?

The FTC had about 24 cases pending in federal courts that relied on Section 13(b) when the Supreme Court determined that it did not have authority to seek monetary relief under that statute. Likely, the FTC will have to amend those complaints



to seek only injunctive relief against future violations and commence administrative actions under Section 5 to issue cease and desist orders regarding past conduct.

In a notable pending action, Facebook, Inc. moved to dismiss the FTC’s complaint on the grounds that the FTC’s authority under Section 13(b) is limited to enjoining ongoing violations of the law, not past actions, relying on the Third Circuit cases cited above. The FTC’s complaint alleged that Facebook’s acquisition of Instagram in 2012 and What’s App in 2014 unfairly restricted competition. Facebook argued that the FTC’s complaint only concerned past practices, not ongoing practices. Facebook’s motion is pending, but similar arguments are likely to be raised in other actions the FTC has pending in federal court. In testimony before Congress, the FTC cited Facebook’s arguments as reasons that Section 13(b) needs to be amended to enable it to seek injunctions, and monetary relief, when an entity “has violated” the FTC Act, not just “is” or “is about to” violate.

4. Will Congress restore the FTC’s authority to seek monetary remedies under Section 13(b)?

Even before the Supreme Court issued the AMG decision the FTC asked Congress to amend Section 13(b) to “confirm” the FTC’s authority to seek restitution. A proposed legislation, H.R. 2668, introduced on April 20, 2021, may restore the FTC’s ability to seek monetary relief through a civil action under Section 13(b) and to do so for past violations. The House Committee on Energy and Commerce held a hearing on that same day (two days before the AMG decision), at which the FTC’s Acting Chair Slaughter testified that amending Section 13(b) to allow monetary relief for past violations was beneficial to consumers and necessary to adequately enforce the law.

However, the U.S. Chamber of Commerce presented a letter to the House Committee that argued against the proposed amendment to Section 13(b). The Chamber argued that Congress originally intended the FTC to enforce unfair and deceptive practices through its administrative process and only use a direct court action through Section 13(b) to enjoin ongoing commercial practices. The Chamber believed that the FTC abused Section 13(b) in a way that hindered law-abiding businesses. The Chamber was also concerned that the proposed legislative amendment would expand, not restore, the FTC’s authority, by allowing monetary relief for any unfair and deceptive practice, not just fraudulent and dishonest conduct when enforcing a final order under Section 19. The Chamber also advocated for a 3-year statute of limitation for actions under a revised Section 13(b) similar to the 3-year statute of limitations under Section 19.

On May 18, 2021, the FTC’s Acting Chair responded to the Chamber’s arguments and urged Congress to restore Section 13(b) in light of the Supreme Court’s devastating AMG decision. The FTC argued that Section 13(b) was not intended to apply only to certain types of cases, but rather applies to enjoin any unfair or deceptive act or practice. The FTC also argued that restricting Section 13(b) only to ongoing conduct drastically reduces any incentive to an entity to avoid fraudulent acts, when merely stopping the act or practice avoids any liability.

The House continues to evaluate the scope of the potential amendment to Section 13 (b). Some of the restrictions being considered by Congress include a 5- or 10-year statute of limitations on a restitution claim, a safe harbor provision for persons who relied on FTC guidance, and a requirement that the act or practice result in substantial harm to consumers.

Conclusion

Clearly, the AMG decision removed a major enforcement tool from the FTC, and until Congress acts, the FTC’s ability to recover on behalf of consumers will be limited. However, the FTC’s current limitations are not carte blanche to violate the law. The FTC remains an active enforcement authority with powers to seek injunctive orders, to coordinate with state attorneys’ general, to pursue administrative remedies, and to enforce its rules and regulations.



One Year as In-House Counsel

10 Lessons Learned

By Jenna L. Kramer

Unilever

Editor’s Note: Jenna Kramer works as a legal counsel at Unilever. Prior to joining Unilever in 2020, she worked at the Federal Court of Canada assisting the Honorable Justice Henry Brown and later at Fasken on issues related to mergers, advertising and marketing practices, abuse of dominance, and criminal cartel matters. Jenna received a J.D. from University of Windsor and a B.A. in Political Science from University of Regina.

A year ago, I left private practice for an exciting in-house opportunity with Unilever Canada. As legal counsel for a global CPG company, I advise on a wide range of consumer protection topics including marketing and advertising, contests and promotions, product, regulatory, and privacy and data security matters. I am often asked about the transition from private practice to in-house and have come to learn that the *raison d’être* of in-house counsel is very different from that of external counsel. As I strive to become a more strategic business and in-house legal partner, I’ve observed the following learnings.

1. **Scale, scale, scale**

Most in-house legal teams are lean, and all in-house legal teams are a cost-center. As such, legal resources must be used sparingly and efficiently. Investing time upfront in developing “self-help” documents, easy-to-use templates, and legal technology services such as a contract lifecycle management system will pay off in the long run. Speak with business leaders, identify their pain points, and swiftly implement legal solutions to increase service levels and deliver faster advice. Scaling leads to greater efficiency which leaves more time to focus on the complex and novel legal problems, rather than spending the day treading through an over-active email inbox.

2. **“Business issues comes first. Legal issues come second.”**

Allow this to serve as a mantra and it will inform your approach for nearly everything you do as in-house counsel. From assessing risk to determining annual objectives for the legal team, understanding the business goals – both long-term and immediate – must shape all legal considerations and recommendations.

3. **More listening, less talking (ask the right questions)**

The only way to understand the business’s priorities is to take the time to learn and listen:

- When speaking with colleagues regarding legal issues, ask open-ended questions. Resist the urge to formulate your response while a colleague is still speaking and limit how much talking you do.
- Avoid multitasking wherever possible. Consider silencing emailing notifications during meetings so as not to be distracted (especially while working from home).
- Book time with colleagues from different departments (operations, HR, finance, marketing, procurement, and communications) to learn about their respective roles within the broader organization. This is also a chance to promote the legal department internally and learn about potentially forthcoming legal issues.
- Know your company’s products (and this isn’t just an excuse for me to sample all of the Ben & Jerry’s flavours!).
- Follow company social media accounts and stay current on company-wide news.

4. **Fast and practical decision making**

The number of decisions to make in each day, and the speed at which those decisions need to be made is perhaps the most striking difference from private practice. Potential legal risk must be weighed against anticipated business upside to reach a practical, commercially-reasonable recommendation (which almost never involves a research memorandum).

5. Understanding trends and enforcement priorities is critical

Digitization is rapidly changing the way we conduct business and applicable laws related to privacy, data security and digital marketing are also evolving. As the first point of contact for legal matters, in-house counsel must remain extremely current on these legal developments. Areas of focus for 2021 are digital advertising including influencer marketing and consumer reviews, privacy law developments (including Bill C-11, Federal and Bill 64, Quebec), green marketing, and monthly subscriptions.

6. And not just the trends in your own jurisdiction – keep an eye across the border and abroad

As a Canadian lawyer, it is important to have a sense of consumer protection developments in other jurisdictions including the U.S., Europe and Australia. If you have legal colleagues in other jurisdictions, coordinate closely. Open lines of communication, resource-sharing and proactively cascading legal developments from your own jurisdiction will be beneficial for all.

7. Resourcefulness is a mindset

There is no need (or time) to do all of your own primary legal research. Along with subscribing to blogs and webinars authored and presented by external counsel, here are some of my go-to resources:

- The Competition Bureau Canada Twitter account (@CompBureau)
- Ad Standards Advisories and Interpretation Guidelines (<https://adstandards.ca/>)
- The International Consumer Protection and Enforcement Network “News” page (<https://icpen.org/node/44>)
- The BBB National Programs Newsroom (<https://bbbprograms.org/media-center/newsroom>)
- The Competition & Markets Authority Twitter account (@CMAgovUK)

8. Trust your team, your gut and when in doubt, external counsel

- Build trust with your business counterparts by being responsive and accountable. When legal issues transpire, the phrase, “I told you so” should never be used; the best way to gain confidence and trust is to be a supportive legal partner in the challenging moments. Trust must be mutual; once your business counterparts trust you, you too will have more confidence in them.
- Trusting your own gut takes practice and experience, but the best legal advice is based on the facts, the law and your intuition.
- Know when to consult specialized external counsel, weighing the anticipated costs and time savings.

9. Trade billable hours for other measurable KPIs

Even if you no longer track your day in 6-minute increments, there are other metrics that a legal department should measure to track the value of its contributions to the wider business. Start with broad topics such as: (i) budgeted vs. actual legal spending; (ii) number of contracts executed; (iii) litigation matters (including percentage successful); (iv) training and compliance; and (v) other legal department initiatives.

10. Ruthlessly promote the in-house legal team

My approach to marketing our legal team internally is to simply say “yes”. Provide an update on a discrete legal development at an upcoming company-wide meeting? Yes. Conduct training on a novel and complex topic? Absolutely. Join a leadership call to weigh-in on a non-legal issue? No problem. These are all opportunities to promote visibility of the legal department and to add value.

Finding Venmo: Applying Consumer Protection Regulations to Peer-to-Peer Payment Platforms

By Rohena Rajbhandari

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Introduction

In recent years, technological innovations have spurred new forms of mobile payment.¹ Nonbanks and technological firms have led this innovation, and consumers have flocked to these novel services.² Also known as Peer-to-Peer (P2P) payments, mobile applications such as Venmo, PayPal, and Cash App, are nonbanks that are not regulated by traditional banking laws.³ Although state and federal laws exist that regulate money transmission and electronic fund transfers, P2P payments employ a unique transaction structure that creates new, potential consumer protection harms to the customers that use these innovative payment platforms.⁴

P2P platforms facilitate the transfer of money from one individual to another through funds pulled from either a linked

payment method or a stored deposit on the sender's P2P account.⁵ Transfers process immediately and funds are usually delivered to the recipient within minutes, sometimes even before the funds have settled with the underlying payment method.⁶ Despite the benefits of this innovative payment platform, rapid transfers and P2P applications, as a whole, can lead to serious consumer protection risks.⁷ Consumers face at least three specific risks that currently lack sufficient legal protection.⁸ First, consumer deposits are not sufficiently insured against insolvency because P2P platforms do not have Federal Deposit Insurance Corporation insurance and state money transmitter laws are woefully inadequate in insuring against P2P insolvency.⁹ Second, transfers initiated by a user after being subject to fraud have no error resolution procedures under either state money transmitter laws or the federal Electronic Funds Transfer Act as they are neither unauthorized transfers nor transfers made in error.¹⁰ Finally, P2P platforms draw customers to their services by promising instantaneous payments, meaning that the platform often must front a payment to the recipient while the funds settle with the sender's linked payment method.¹¹ In this situation, the sender's account shows a negative balance until the payment is fulfilled.¹² The P2P platform will often attempt to collect on the money and may even send the debt to a collection agency even if the sender disputes the transaction due to being subject to fraud.¹³

This Article is the first to address concrete consumer problems in the P2P market, and to address these issues, I propose that the Consumer Financial Protection Bureau (CFPB) should take five specific actions.¹⁴ First, the CFPB should extend Regulation E, which implements the EFTA, to cover payments made in error to illegitimate recipients and from which the

¹ See NAT'L CONSUMER L. CTR., CONSUMER BANKING AND PAYMENTS LAW § 1.2.1 (6th ed. 2018), www.nclc.org/library.

² See U.S. DEP'T OF TREASURY, A FINANCIAL SYSTEM THAT CREATES ECONOMIC OPPORTUNITIES: NONBANK FINANCIALS, FINTECH, AND INNOVATION, at 25 (2018), <https://home.treasury.gov/sites/default/files/2018-07/A-Financial-System-that-Creates-Economic-Opportunities---Nonbank-Financi...pdf>; CONSUMER BANKING AND PAYMENTS LAW, *supra* note 1, § 1.2.1.

³ See CONSUMER BANKING AND PAYMENTS LAW, *supra* note 1, § 1.2.1.

⁴ See *infra* Parts III-IV.

⁵ See, e.g., *Venmo User Agreement*, VENMO, <https://venmo.com/legal/us-user-agreement> (last visited Nov. 28, 2020).

⁶ See Peter Rudegeair, *Even in a Pandemic, Venmo Tells Conned Customers to Pay Up*, WALL ST. J. (Sept. 24, 2020), <https://www.wsj.com/articles/even-in-a-pandemic-venmo-tells-conned-customers-to-pay-up-11600939826>.

⁷ See *infra* Parts I-IV.

⁸ See *infra* Part III.

⁹ See *infra* notes 184-196 and accompanying text.

¹⁰ See *infra* notes 197-227 and accompanying text.

¹¹ See *infra* notes 228-235 and accompanying text.

¹² See *id.*

¹³ See *id.*

¹⁴ See *infra* Parts I-IV. Although some scholars have discussed the separate solvency risk and systemic risk of P2P systems, no scholarly work has analyzed the market conduct risks, or, in other words, the consumer protection risks of P2P platforms. See Hilary J. Allen, *Payments Failure*, 62 B.C.L. REV. ____ (forthcoming 2021); Dan Awrey & Kristin Van Zwieten, *Mapping the Shadow Payment System* (Oct. 8, 2019) (available at <https://ssrn.com/abstract=3462351>).

sender receives no benefit.¹⁵ In that same vein, to identify legitimate recipients before a transfer is initiated, P2P platforms should add an additional recipient authentication factor such as a username, QR code, or phone number.¹⁶ Next, if a consumer invokes Regulation E's error resolution procedures, companies should be prohibited from collecting or attempting to collect on a debt.¹⁷ Lastly, the CFPB must educate consumers on the risks of conducting payments on P2P platforms.¹⁸ In an education campaign, the CFPB must caution customers of their limited legal rights in the event of fraudulent activity on their P2P accounts as well as the significantly limited protections against insolvency on stored deposits in their P2P accounts.¹⁹

This Article examines these arguments in four parts.²⁰ Part I provides an overview of the P2P payment market and explains how P2P transactions are distinctively processed.²¹ Part II examines state and federal consumer financial protection regulations that govern P2P payments.²² Part III identifies the unique consumer protection problems prevalent in P2P transactions and argues that the current legal structure does not provide adequate safeguards against those harms.²³ Finally, in Part IV, this Article offers solutions for the CFPB to resolve the identified consumer protection problems.²⁴

¹⁵ See *infra* notes 241-250 and accompanying text.

¹⁶ See *infra* notes 251-255 and accompanying text.

¹⁷ See *infra* notes 256-259 and accompanying text.

¹⁸ See *infra* notes 260-266 and accompanying text.

¹⁹ See *id.*

²⁰ See *infra* Parts I-IV.

²¹ See *infra* notes 25-57 and accompanying text.

²² See *infra* notes 58-176 and accompanying text.

²³ See *infra* notes 177-235 and accompanying text.

²⁴ See *infra* notes 236-276 and accompanying text.

²⁵ See Elizabeth Boise & Leo Tsao, *Money Moves: Following the Money Beyond the Banking System*, 67 DEP'T OF JUST. J. FED. L. & PRAC. 95, 99 (2019).

²⁶ See *id.*

²⁷ See A FINANCIAL SYSTEM THAT CREATES ECONOMIC OPPORTUNITIES: NONBANK FINANCIALS, FINTECH, AND INNOVATION, *supra* note 2, at 145.

²⁸ See CONSUMER BANKING AND PAYMENTS LAW, *supra* note 1, § 5.1.6.2; Boise & Tsao, *supra* note 25, at 99, 102; Spencer Tierney, *Wire Transfers: What Banks Charge*, NERDWALLET (Oct. 11, 2019), <https://www.nerdwallet.com/article/banking/wire-transfers-what-banks-charge>.

²⁹ See *Can Regulators Foster Financial Innovation and Preserve Consumer Protections*, PEW (Sept. 10, 2020), <https://www.pewtrusts.org/en/research-and-analysis/issue->

I. Overview of the Peer-to-Peer Payment Market

In the United States, four primary payment systems electronically transfer funds between financial institutions.²⁵ These payment systems include credit cards, debit cards, automated clearing house transfers, and wire transfers.²⁶ Prior to the entry of FinTech firms, wire transfers and ACH systems were used to electronically transfer funds between individuals.²⁷ Wire transfers and ACH systems, however, each presented challenges to consumers: wire transfers require high fees to transfer payments and ACH does not transfer payments in real-time.²⁸ Recent developments in the Peer-to-Peer payment market have reduced these barriers.²⁹

a. *The Layout of the P2P Market*

Driven by millennials seeking to split discrete payments, P2P payment platforms were created to efficiently transfer payments between individuals.³⁰ Through mobile applications, P2P payments are made seamlessly on smartphones, without the cumbersome exchange of cash or checks.³¹ In the past few years, these novel tools have become a part of the mainstream financial system, and for some demographics, the primary medium for making payments.³² In fact, market analysts predict that P2P payments will surpass \$396 billion by the end of 2020.³³ Moreover, due to the COVID-19 pandemic, P2P payments have become more

[briefs/2020/09/can-regulators-foster-financial-innovation-and-preserve-consumer-protections](https://www.pewtrusts.org/en/research-and-analysis/issue-briefs/2020/09/can-regulators-foster-financial-innovation-and-preserve-consumer-protections).

³⁰ See Melisande Mual, *Peer-to-Peer Payments May be the Next E-Commerce Trend in the US*, THE PAYPERS (Sept. 11, 2019), <https://thepaypers.com/expert-opinion/peer-to-peer-payments-may-be-the-next-ecommerce-trend-in-the-us--780590>. Millennials are expected to achieve far less levels of financial success than the preceding generations, and due to record levels of student loans and housing costs, they must often combine their resources and spend in groups. *Id.*

³¹ *Id.*

³² *Can Regulators Foster Financial Innovation and Preserve Consumer Protections*, *supra* note 29. Some consumers choose not to use mobile payments and insist they are satisfied with other payment methods. *Id.* Approximately, 30% of consumers said they do not use mobile payments to prevent loss of funds from theft, double billing, or disputes with merchants or app providers. *Id.*

³³ Jason Hoffman, *P2P Payment Statistics, Trends and Market Size for 2020*, WISDOM PLEXUS, <https://wisdomplexus.com/blogs/p2p-payment-statistics/>. In 2019, Venmo alone delivered over \$102 billion total payment volume and ended the year with over 52 million active accounts, whereas Cash App ended 2019 with \$106 billion in total payment volume and 30 million active accounts. David Curry, *Cash App Revenue and Usage Statistics (2020)*, BUSINESS OF APPS (Oct. 30, 2020), <https://www.businessofapps.com/data/cash-app-statistics/>.

prolific as consumers increasingly seek to exchange funds without physical contact.³⁴ Nowadays, P2P platforms can even accept government stimulus payments through direct deposit.³⁵

P2P platforms can be divided into two major categories: deposit holding platforms and non-deposit holding platforms, also known as pass-through platforms.³⁶ This Article focuses on deposit holding platforms such as Venmo, Square Cash, Google Pay, and PayPal.³⁷ Approximately 68% of mobile payment application users stated that they maintain a balance on their P2P payment application, and on average, they keep up to \$287 in their account before transferring those funds to a linked bank account.³⁸ The majority of P2P payment users make mobile payments at least weekly, and they primarily use these platforms to pay family members, friends, informal online sellers (e.g., Craigslist, Facebook Marketplace), and landlords.³⁹

b. *The Transactional Structure of P2P Payments*

To use any deposit holding P2P service, an individual must create a personal account on the P2P platform, which allows a

person to make payments using a linked credit card, debit card, bank account, or through funds held on the P2P account.⁴⁰ During enrollment, P2P platforms verify a user's identifying information through their name, physical address, date of birth, and social security or taxpayer identification number.⁴¹ All accounts are accessible through a mobile application; Cash App and PayPal also allow users to access their accounts through their respective websites.⁴²

Users can locate other users on the platform to either send or request payment via their registered email address, phone number, account name, or unique QR code.⁴³ To request money, a user must first send a payment request; after which, the recipient of the payment request can then accept the charge request before any money is transferred.⁴⁴ Once a sender has initiated payment, the P2P application first seeks to withdraw available funds from the sender's balance held on the platform if that balance can cover the full funds.⁴⁵ Because the funds are already held on the P2P platform, this transaction is instantaneous on both the recipient's and sender's ends, meaning the funds leave the sender's account and are deposited into the recipient's account immediately.⁴⁶ Alternatively, if the account balance cannot cover those funds, the P2P provider

³⁴ *How The Pandemic Has Helped Push P2P Payments Mainstream*, PYMNTS (June 12, 2020), <https://www.pymnts.com/news/payment-methods/2020/covid-19-pushes-p2p-payments-into-the-mainstream/>.

³⁵ See Bryan Derman, *The P2P Domain Gets Big COVID Push*, GLEN BROOK (June 18, 2020), <https://pv.glenbrook.com/the-p2p-domain-gets-a-big-covid-push/>.

³⁶ See Mual, *supra* note 30; Erin Fonte, *2017 U.S. Regulatory Overview of Mobile Wallets and Mobile Payments*, 17 WAKE FOREST J. BUS. & INTELLECTUAL PROP. L. 549 (2017).

³⁷ See *Additional Cash Terms of Service*, CASH APP (April 21, 2020) <https://cash.app/legal/us/en-us/tos>; *Learn About Google Pay Balance*, GOOGLE, <https://support.google.com/pay/answer/9039165?hl=en> (last visited Nov. 28, 2020); *PayPal User Agreement*, PAYPAL, <https://www.paypal.com/us/webapps/mpp/ua/useragreement-full> (last visited Nov. 28, 2020); *Venmo User Agreement*, *supra* note 5. PayPal is considered the pioneer in P2P payments. See Eric Pacifici, *Making PayPal Pay: Regulation E and Its Application to Alternative Payment Services*, 13 DUKE L. & TECH. REV. 89, 95-96 (2015) (referring to PayPal as “the granddaddy of internet payment systems” (citation omitted)). Non-deposit holding platforms include Zelle and Facebook Pay. See e.g., *Zelle Network Terms of Use*, ZELLE, <https://www.zellepay.com/terms-use> (last visited Nov. 30, 2020).

³⁸ Erin E. Issa, *Most Americans Go Mobile With Payment Apps – Here's How they Roll*, NERDWALLET (Feb. 26, 2020), <https://www.nerdwallet.com/article/banking/mobile-payment-app-survey>.

³⁹ *Id.*

⁴⁰ See *Additional Cash Terms of Service*, *supra* note 37; *Learn About Google Pay Balance*, *supra* note 37; *PayPal User Agreement*, *supra* note 37; *Venmo User Agreement*, *supra* note 5. Any payment sent via a P2P account balance or through an external bank account is not charged a fee. See, e.g., *Additional Cash Terms of Service*, *supra* note 22; *Google Pay About*, GOOGLE, <https://pay.google.com/about/> (last visited Nov. 29, 2020); *PayPal Consumer Fees*, PAYPAL, <https://www.paypal.com/us/webapps/mpp/paypal-fees#personal-fixed-fee> (last visited Nov. 28, 2020); *Venmo Fees*, VENMO, <https://venmo.com/about/fees> (last visited Nov. 28, 2020). If the underlying transaction originates from a debit or credit card, the mobile wallet will charge a fee, usually around 3%. See, e.g., *Additional Cash Terms of Service*, *supra* note 37; *Google Pay About*, *supra*; *PayPal Consumer Fees*, *supra*; *Venmo Fees*, *supra*. P2P providers do not charge a fee to add additional funds to a user's P2P account balance from a linked bank account. See *Additional Cash Terms of Service*, *supra* note 37; *Google Pay About*, *supra*; *PayPal Consumer Fees*, *supra*; *Venmo Fees*, *supra*.

⁴¹ See *Additional Cash Terms of Service*, *supra* note 37; *Google Pay About*, *supra* note 40; *PayPal User Agreement*, *supra* note 37; *Venmo User Agreement*, *supra* note 5.

⁴² See *Additional Cash Terms of Service*, *supra* note 37; *Google Pay About*, *supra* note 40; *PayPal User Agreement*, *supra* note 37; *Venmo User Agreement*, *supra* note 5.

⁴³ See, e.g., *Additional Cash Terms of Service*, *supra* note 37.

⁴⁴ See, e.g., *id.*

⁴⁵ See, e.g., *Venmo User Agreement*, *supra* note 5.

⁴⁶ See, e.g., *id.*

processes the full transaction through the user's preferred payment method, *i.e.* a bank account or credit card.⁴⁷ But it can take a day or more for the money to leave the sender's bank account or settle with the debit or credit card, so in the interim, the P2P platform fronts the transaction amount for immediate deposit into the recipient's account.⁴⁸ Generally, P2P platforms do not split payments between money held on a user's P2P account and the preferred linked payment method.⁴⁹ A user cannot stop a transfer once initiated.⁵⁰

Once a user receives money on their P2P account, the recipient can either leave the funds in their P2P account or separately transfer the funds from their P2P account to a linked bank account.⁵¹ If a user chooses to transfer those funds to their linked bank account, the mobile application processes the transfer within one to three business days for no additional cost.⁵² The user can also request an immediate transfer if they pay an additional fee, usually 1% to up to \$10.⁵³ Immediate transfers can be sent to an eligible debit card or linked bank account.⁵⁴

The user can also send money to an individual who does not have an account on the same platform, but in order to access those funds, the recipient must create an account and accept the payment.⁵⁵ In addition, users may add funds to their P2P

account by using the existing bank account linked to their P2P account or by setting up a direct deposit.⁵⁶ Aside from funds originating from direct deposits, which may qualify for Federal Deposit Insurance Corporation (FDIC) pass-through insurance, a balance held on a P2P account is not FDIC insured.⁵⁷

II. Federal and State Laws Applicable to Peer-to-Peer Payment Platforms

P2P platforms fall under the purview of multiple regulators, both state and federal, and no single regulatory framework governs their operations.⁵⁸ This Part will identify the applicable state regulations and federal consumer financial protection regulations and analyze whether those laws cover P2P payments.⁵⁹

a. State Money Transmitter Laws

State money transmitter laws regulate the business of transmitting money from one person or company to another.⁶⁰ These laws focus on protecting consumers by ensuring that money transmitters have sufficient resources to prevent the loss of consumers' funds.⁶¹ Money transmission typically involves an entity accepting funds from one person and

and the P2P provider will not use them for its operating expenses or other corporate purposes. *See, e.g., id.* Finally, they will not voluntarily make these funds available to their creditors in the event of bankruptcy. *See, e.g., id.*

⁵⁸ *See* Madison Thompson, *Money Transmitters Face Ambiguity in State, Federal Law*, LEXOLOGY, <https://www.lexology.com/library/detail.aspx?g=662f9314-4154-49f7-ab8e-39c321450d39> (last visited Nov. 28, 2020). If a P2P payment is funded by a linked payment source, that source is also subject to certain state and federal laws. *See* CONSUMER BANKING AND PAYMENTS LAW, *supra* note 1, § 5.14.1. This Article focuses on the second step of the process that occurs on the P2P platform.

⁵⁹ *See infra* notes 60-176 and accompanying text.

⁶⁰ CONSUMER BANKING AND PAYMENTS LAW, *supra* note 1, § 6.6.4.1. Money transmitters may also be referred to as a money service business (MSB). *Id.* States also regulate payments under the Uniform Commercial Code. *Id.* § 6.7.1. However, the UCC does not apply to a funds transfer if it is governed by the EFTA. U.C.C. § 4A-108. This Article will not discuss UCC protections due to space limitations. State regulators have also responded to the increase in P2P usage by establishing fintech "sandbox" programs which temporarily reduce licensing and regulatory requirements to help spur the development of novel financial products and technologies. *Can Regulators Foster Financial Innovation and Preserve Consumer Protections*, *supra* note 29. This is also outside the scope of this Article.

⁶¹ *See* Fonte, *supra* note 36, at 584; Kevin V. Tu, *Regulating the New Cashless World*, 65 ALA. L. REV. 77, 93 (2013).

⁴⁷ *See, e.g., id.*

⁴⁸ *See* Rudgegear, *supra* note 6; Telis Demos, *You Accidentally Sent \$149 to a Stranger on Venmo? Good Luck Getting It Back*, WALL ST. J. (July 12, 2018), https://www.wsj.com/articles/you-accidentally-venmoed-149-to-a-stranger-good-luck-getting-it-back-1531411133?mod=hp_featst_pos3.

⁴⁹ *See Additional Cash Terms of Service*, *supra* note 37; *Money in Your Venmo Account and Venmo Balance*, VENMO, <https://help.venmo.com/hc/en-us/articles/217042588-Money-in-Your-Venmo-Account-and-Venmo-Balance> (last visited Nov. 28, 2020).

⁵⁰ *See Additional Cash Terms of Service*, *supra* note 37; VENMO, <https://help.venmo.com/hc/en-us/articles/235171088-Cancel-Payment> (last visited Nov. 28, 2020)

⁵¹ *See, e.g., Additional Cash Terms of Service*, *supra* note 37.

⁵² *See, e.g., Additional Cash Terms of Service*, *supra* note 37.

⁵³ *See Additional Cash Terms of Service*, *supra* note 37; *PayPal Consumer Fees*, *supra* note 40; *Venmo Fees*, *supra* note 40.

⁵⁴ *See, e.g., Venmo Fees*, *supra* note 40.

⁵⁵ *See, e.g., Additional Cash Terms of Service*, *supra* note 37. If those funds are not claimed, the money will be refunded to the sender. *See, e.g., id.*

⁵⁶ *See, e.g., id.*

⁵⁷ *See, e.g., id.* Generally, P2P platforms take all of their customers' account funds and invest them in liquid investments. *See, e.g., PayPal User Agreement*, *supra* note 37. The platforms state that they own the interest or other earnings on these investments. *See, e.g., id.* They also confirm that these pooled amounts are held separately from the company's corporate funds,

transmitting those funds to another person.⁶² Although every state, except Montana, has a statute that governs money transmitters, state laws vary by jurisdiction, and there is no uniform legal definition of a money transmitter.⁶³ Though no law is the same, states usually define money transmission broadly with few constraints.⁶⁴ Ultimately, state laws require any person engaging in money transmission to obtain a license from the appropriate state regulator and comply with the licensing requirements imposed on money transmitters.⁶⁵

Licensed money transmitters may be charged an annual licensing fee and the costs of regulatory assessments and investigations.⁶⁶ They must comply with regulatory requirements, including obtaining surety bonds (or similar security device); maintaining minimum levels of permissible investments (e.g. government obligations and other low-risk investments); satisfying minimum net worth requirements; retaining specified business records for specific periods of time; and filing annual and periodic reports regarding the money transmitter's financial condition and any significant events.⁶⁷ Furthermore, licensed money transmitters are subject to audits and investigations by the state regulatory agency overseeing compliance.⁶⁸ If an examination or report indicates that the business is not performing its duties or is in danger of failing, the regulator can mandate corrective action or suspend or revoke the license.⁶⁹

Surety bonds must be held in trust for the benefit of the state and any individual to whom an obligation arises under state

law.⁷⁰ In other words, surety bonds protect the obligee (the depositor) if the bond principal (the money transmitter) becomes insolvent.⁷¹ Each state has its own cap on the bonds and securities, and those caps may not cover all consumers if a money transmitter becomes insolvent.⁷²

Most state statutes also permit exemptions from money transmitter law coverage.⁷³ Depository institutions, *i.e.* banks, are exempt from money transmitter licensing requirements because they are already covered by bank regulators and deposit insurance.⁷⁴ State laws may also exempt governmental entities and other entities that provide processing, clearing, or settlement services.⁷⁵ All states prohibit unlicensed money transmissions, and unless an exemption applies, operating as an unlicensed money transmitter can result in criminal and civil penalties.⁷⁶

Due to the fragmented nature of state money transmitter licensing for money transmitters that operate in multiple states, states have attempted to coordinate their supervision of money transmitters that operate in multiple states.⁷⁷ The Money Transmitter Regulators Association and Conference of State Bank Supervisors have developed some frameworks, including the Money Transmitter Regulatory Cooperative Agreement.⁷⁸ However, of the states that have adopted this agreement, all of them have different interpretations of the law.⁷⁹

⁶² Thompson, *supra* note 58.

⁶³ CONSUMER BANKING AND PAYMENTS LAW, *supra* note 1, § 6.6.4.1 (comparing the definition of money transmission in California, which includes selling or issuing payment instruments, selling or issuing stored value, or receiving money for transmission, with the definition of money transmission in New York, which includes all instruments sold or issued for the transmission or payment of money). Although there is no legislation in Montana regulating money service business, MSBs must still register as a business with the Montana Secretary of State. *Money Service Businesses*, MONTANA OFFICIAL STATE WEBSITE, <https://banking.mt.gov/moneytransmitters> (last visited Nov. 28, 2020).

⁶⁴ See Tu, *supra* note 61, at 87. For example, Arizona and Maryland both define money transmission to encompass not only the money transferred toward consumers but also the transmission of monetary value, which is considered a medium of exchange, regardless of whether it is redeemable in money. See *id.* at 87-88.

⁶⁵ CONSUMER BANKING AND PAYMENTS LAW, *supra* note 1, § 6.6.4.1. When applying for a money transmitter license, the applicant must supply personal, business, and fitness-related information regarding the applicant and the business. Tu, *supra* note 61, at 92. The state regulators then will approve or deny the application on the basis of: (1) the application, itself; (2) an

investigation into the applicant's financial condition, financial and business experience, competence, character, and general fitness; and (3) an on-site examination, in some cases. *Id.* An applicant must also submit an application fee. *Id.*

⁶⁶ Tu, *supra* note 61, at 92.

⁶⁷ *Id.* at 93.

⁶⁸ *Id.*

⁶⁹ *Id.*

⁷⁰ CONSUMER BANKING AND PAYMENTS LAW, *supra* note 1, § 6.6.4.5.

⁷¹ See *id.*

⁷² *Id.* For example, in California, only \$2 million in securities must be held for all accounts in the state, compared with Alabama where the maximum requirement is \$50,000 in surety bonds. *Id.*

⁷³ Tu, *supra* note 61, at 89.

⁷⁴ CONSUMER BANKING AND PAYMENTS LAW, *supra* note 1, § 6.6.4.1.

⁷⁵ *Id.*

⁷⁶ *Id.*

⁷⁷ Brian Knight, *Federalism and Federalization on the Fintech Frontier*, 20 VANDERBILT J. OF ENT. & TECH. L. 129, 157-58 (2017).

⁷⁸ *Id.* at 158.

⁷⁹ *Id.*

i. *Application of State Money Transmitter Laws to P2P Platforms*

Because P2P payment providers are nonbanks that accept funds from one person and transmit those funds to another person, they are generally considered nonbank money transmitters that are subject to state money transmitter laws in each state in which they operate.⁸⁰ Thus, P2P platforms must apply for a money transmitter license in each state in which they engage in money transmission.⁸¹ All of the P2P platforms considered in this Article, are subject to state money transmitter laws and, accordingly, have active state transmitter licenses across the United States.⁸²

b. *The Electronic Fund Transfer Act, The Truth in Lending Act, and the Prepaid Account Rule*

The Consumer Financial Protection Bureau (CFPB or the Bureau) enforces and regulates consumer financial services and products through the Electronic Fund Transfer Act (EFTA), implemented by Regulation E, and the Truth in Lending Act (TILA), implemented by Regulation Z.⁸³ The CFPB also recently amended Regulations E and Z to expand their coverage to prepaid cards, through the Prepaid Account

Rule.⁸⁴ This Section discusses the EFTA and TILA alongside their implementing regulations and the Prepaid Account Rule in relation to P2P payments.⁸⁵

i. *The Electronic Fund Transfer Act and Regulation E*

In 1978, Congress enacted the Electronic Fund Transfer Act (EFTA) to address the lack of clarity in consumer protection laws surrounding electronic fund transfers.⁸⁶ Presently, the CFPB administers and enforces Regulation E, which implements the EFTA and provides consumer safeguards for electronic fund transfers (EFTs).⁸⁷ An EFT is “any transfer of funds, other than a transaction originated by check, draft, or similar paper instrument, which is initiated through an electronic terminal, telephonic instrument, or computer or magnetic tape so as to order, instruct, or authorize a financial institution to debit or credit an account.”⁸⁸

Under the EFTA and Regulation E, financial institutions that process EFTs are subject to various requirements regarding disclosures to consumers, the issuance of access devices, periodic statements, records retention, resolution of errors procedures, and limitations on consumer liability for unauthorized transactions.⁸⁹ A “financial institution” is

⁸⁰ See CONSUMER BANKING AND PAYMENTS LAW, *supra* note 1, § 6.6.4.1; Fonte, *supra* note 36, at 585; Tu *supra* note 61, 87-88.
⁸¹ See Fonte, *supra* note 36, at 585; Tu, *supra* note 61, at 87.
⁸² See CONSUMER BANKING AND PAYMENTS LAW, *supra* note 1, § 6.6.4.1; Fonte, *supra* note 36, at 585; Google Payment Corp. Money Transmitter Licenses, GOOGLE, <https://support.google.com/pay/answer/7160765?hl=en> (last visited Nov. 28, 2020); PayPal State Licenses, PAYPAL, <https://www.paypal.com/us/webapps/mpp/licenses> (last visited Nov. 28, 2020); Square, Inc. Licenses, SQUARE, <https://squareup.com/us/en/legal/general/licenses> (last visited Nov. 28, 2020); Venmo State Licenses, VENMO, <https://venmo.com/legal/us-licenses> (last visited Nov. 28, 2020). These P2P platforms also hold a business license from Montana, in accordance with Montana’s laws. Google Payment Corp. Money Transmitter Licenses, *supra*; PayPal State Licenses, *supra*; Square, Inc. Licenses, *supra*; Venmo State Licenses, *supra*. While, at present, the major P2P players all have money state transmitter licenses in all fifty states, in the past some of them have failed to obtain these licenses in all states in which they operated. See Ingrid Lunden, Square Fined \$507K in Florida For Operating a Mobile Payment Service Without a Money Transmitter License, TECH CRUNCH (Aug. 16, 2013), <https://techcrunch.com/2013/08/16/square-fined-507k-in-florida-for-operating-a-mobile-payment-service-without-a-money-transmitter-license/>. States, in turn, have fined these businesses for failing to obtain the necessary licenses. See *id.*

⁸³ See generally Regulation E, Electronic Fund Transfer Act, 12 C.F.R. pt. 1005; Regulation Z, Truth in Lending Act, 12 C.F.R. pt.

1026.1. The FTC also has jurisdiction over consumer protection issues, but this Article will focus on the CFPB. See Thompson, *supra* note 58. The FTC, established through the Federal Trade Commission Act of 1914, outlaws unfair acts or practices that affect commerce. Dodd-Frank Act, 12 U.S.C. § 5511. The FTC has primarily regulated P2P players in relation to consumer privacy concerns and the availability of users’ funds. See Fonte, *supra* note 21, at 591. In 2018, PayPal settled with the FTC regarding Venmo’s default privacy settings, misrepresentations that it offered “bank-grade security systems,” and failure to disclose that transferred funds are still subject to review by the company. PayPal Settles FTC Charges That Venmo Failed to Disclose Information to Consumers About the Ability to Transfer Funds and Privacy Settings; Violated Gramm-Leach-Bliley Act, FTC (Feb. 27, 2018) <https://www.ftc.gov/news-events/press-releases/2018/02/paypal-settles-ftc-charges-venmo-failed-disclose-information>.

⁸⁴ See generally Federal Deposit Insurance Act, 12 U.S.C. § 1811.

⁸⁵ See *infra* notes 86-172 and accompanying text.

⁸⁶ Electronic Fund Transfer Act, Pub. L. 95-630, § 2001, 92 Stat. 3641, 3728 (1978) (codified at 15 U.S.C. § 1693); Pacifici, *supra* note 37, at 98.

⁸⁷ 12 U.S.C. § 5511(b); 15 U.S.C. § 1693; 12 C.F.R. pt. 1005.1.

⁸⁸ 15 U.S.C. § 1693a(7).

⁸⁹ See generally 15 U.S.C. § 1693; 12 C.F.R. pt. 1005. Regulation E clarifies that an access device is “a card, code, or other means of access to a consumer’s account, or any combination thereof, that may be used by the consumer to initiate EFTs.” 12 C.F.R. pt. 1005.2(a)(1).

defined as “a State or National bank, a State or Federal savings and loan association, a mutual savings bank, a State or Federal credit union, or any other person who, directly or indirectly, holds an account belonging to a consumer.”⁹⁰ The term “account” includes a consumer demand deposit, savings deposit, or other asset account held by a financial institution and “established primarily for personal, family, or household purposes.”⁹¹

Through the EFTA, consumers have legal recourse to resolve errors related to electronic fund transfers.⁹² The EFTA defines an error to include: “(1) an unauthorized electronic fund transfer; (2) an incorrect transfer to or from the consumer’s account; (3) the omission of a transfer from a periodic statement; (4) a computational error made by the financial institution relating to a transfer; (5) the consumer receipt of an incorrect amount of money from an electronic terminal; (6) a consumer’s request for additional information or clarification concerning an [EFT]...; (7) any other error described in regulations of the Bureau.”⁹³

Importantly, the EFTA places limitations on the amount of loss a consumer is liable for in the event of an unauthorized EFT, such as a loss associated with the theft of a debit or credit card.⁹⁴ An unauthorized EFT is defined as an EFT “from a consumer’s account initiated by a person other than the consumer without actual authority to initiate such transfer and from which the consumer receives no benefit.”⁹⁵ In contrast, the EFTA specifically excludes the following from the definition of an unauthorized transfer: (1) EFTs initiated by a

person to whom the consumer furnished the card code, or other means of access, unless the consumer has notified the financial institution that transfers by such person are no longer authorized; (2) EFTs initiated with fraudulent intent by the consumer or anyone acting together with the consumer; or (3) EFTs made in error by the financial institution.⁹⁶ An unauthorized transfer may also include a transfer that is initiated by someone who obtained an access device from the consumer through fraud or robbery or through an ATM transfer that the consumer was induced by force to make.⁹⁷ Regulation E adds that if the unauthorized EFT occurred through an access device, the financial institution must be able to identify the consumer to whom it was issued.⁹⁸ Depending on the timing of the consumer’s notice to the financial institution of the unauthorized EFT, the EFTA limits the consumer’s liability under various tiers.⁹⁹ Notice can be provided to the financial institution in any reasonable manner, such as in person, by telephone, or in writing.¹⁰⁰

In addition, the EFTA and Regulation E protect consumers in situations where loss or theft of an access device goes undetected and, subsequently, unreported until the consumer discovers the unauthorized EFT in a periodic statement.¹⁰¹ To avoid liability for subsequent transfers, the consumer has sixty days from the date the financial institution transmitted the account statement to report the unauthorized transfer; otherwise, the consumer will be fully liable for those transactions.¹⁰² Once a consumer provides the financial institution with notice, the financial institution has ten business

device, the consumer’s liability is limited to the lesser of \$50 or the amount of the unauthorized transfers that occurred before notice was given to the financial institution. 15 U.S.C. § 1693g(a); 12 C.F.R. pt. 1005.6(b)(1). If, however, the consumer notifies the financial institution after the two business days, then the consumer’s liability is capped at

“the lesser of \$500 or the sum of (i) \$50 or the amount of unauthorized transfers that occur within the two business days, whichever is less; and (ii) [t]he amount of unauthorized transfers that occur after the close of two business days and before notice to the institution, provided the institution establishes that these transfers would not have occurred had the consumer notified the institution within that two-day period.”

12 C.F.R. pt. 1005.6(b)(2); *see also* 15 U.S.C. § 1693g(a) (stating same).

¹⁰⁰ 15 U.S.C. § 1693f(a); 12 C.F.R. pt. 1005.6(b)(5). Constructive notice is established when a financial institution becomes “aware of circumstances leading to the reasonable belief that an unauthorized transfer to or from the consumer’s account...may [have been] made. 12 C.F.R. pt. 1005.6(b)(5)(iii).

¹⁰¹ *See* 15 U.S.C. § 1693g(a); 12 C.F.R. pt. 1005.6(b)(3).

¹⁰² 15 U.S.C. § 1693g(a); 12 C.F.R. pt. 1005.6(b)(3).

⁹⁰ 15 U.S.C. § 1693a(9).

⁹¹ § 1693a(2).

⁹² § 1693f. The EFTA also provides procedures for administrative enforcement if a financial institution violates any of the Act’s requirements. § 1693o. Separately, consumers may privately enforce their claims by bringing individual or class action claims in any United States District Court within one year of the alleged violation. § 1693m(a), (g).

⁹³ § 1693f(1)-(7). Regulation E specifies that routine inquiries about the consumer’s account balance, requests for information for tax or other recordkeeping services, and requests for duplicate copies of documentation are not considered to be errors that trigger the error resolution obligations. 12 C.F.R. pt. 1005.11(a)(2).

⁹⁴ *See* 15 U.S.C. §§ 1693a(12), 1693f, 1693g.

⁹⁵ § 1693a(12).

⁹⁶ *Id.*

⁹⁷ Regulation E, Official Interpretations, 12 C.F.R. pt. 1005.2(m)-3.

⁹⁸ 12 C.F.R. pt. 1005.6(a). An access device is a card, code, or other means of access to a consumer’s account that can be used to initiate an EFT. 12 C.F.R. pt. 1005.2(a)(1).

⁹⁹ 15 U.S.C. § 1693g(a); 12 C.F.R. pt. 1005.6(b). If the consumer provides the financial institution with a timely notice (within two business days) of learning of the loss or theft of his or her access

days to investigate.¹⁰³ After completing its investigation, the financial institution has three business days to report the results to the consumer and, if necessary, one business day to correct the error.¹⁰⁴

Expanding upon the EFTA's provisions, Regulation E may also apply to money transmitters that do not hold the consumer's depository account.¹⁰⁵ If a transmitter does not have an agreement with the depository institution that holds the customer's account, Regulation E will still apply if the transmitter issues an access device that the consumer can use to access the account.¹⁰⁶ Under Regulation E, these EFT providers must satisfy specific compliance requirements, including required disclosures and documentation, error resolution, and final resolution of investigation and transfer funds to or from the consumer's account for errors for which the consumer is not liable or has limited liability.¹⁰⁷

ii. *The Truth in Lending Act and Regulation Z*

The Truth in Lending Act (TILA), implemented by Regulation Z, establishes the rules regarding consumer credit so that consumers have the necessary information to better understand the available credit options as well as the costs of various credit lines.¹⁰⁸ The focus of TILA and Regulation Z is on the subject of credit, which is the right "to defer payment of debt or to

incur debt and defer its payment."¹⁰⁹ Generally, TILA and Regulation Z apply to creditors that offer or extend credit to consumers, including both open-end and closed-end credit products.¹¹⁰ Under TILA, creditors must provide customers with disclosures that describe various credit costs, including interest rates, billing rights, and dispute resolution procedures.¹¹¹

In 1974, Congress passed the Fair Credit Billing Act (FCBA) as an amendment to TILA, to protect consumers against inaccurate or fraudulent credit card charges and other billing errors on open-end credit accounts.¹¹² Under the FCBA, a billing error includes, but is not limited to: an extension of credit not made to the consumer or a credit extension made in an amount different from what was reflected on the statement; an unauthorized extension of credit, meaning an extension of credit to someone without actual, implied or apparent authority to use the credit card or account; an extension of credit that is not properly identified under the rules for transaction identification; and an extension of property or services not delivered to or not accepted by the consumer or consumer's designee as agreed.¹¹³

If a consumer submits a proper billing error notice,¹¹⁴ the creditor must conduct a reasonable investigation into whether such an error occurred.¹¹⁵ Prior to the resolution of the alleged

¹⁰³ 15 U.S.C. § 1693f(a); 12 C.F.R. pt. 1005.11(c)(1). While investigating the alleged error, the financial institution may provisionally credit the customer's account in the amount of the alleged error within ten business days of receiving the error notice. 15 U.S.C. § 1693f(c); 12 C.F.R. pt. 1005.11(c)(2)(ii).

¹⁰⁴ 15 U.S.C. § 1693f(b), (d); 12 C.F.R. pt. 1005.11(c)(1).

¹⁰⁵ See generally 12 C.F.R. pt. 1005.14.

¹⁰⁶ 12 C.F.R. pt. 1005.14(a)(1)-(2).

¹⁰⁷ 12 C.F.R. pt. 1005.14(b)(1)-(2).

¹⁰⁸ See 15 U.S.C. § 1601(a); 12 C.F.R. pt. 1026.1; Fonte, *supra* note 21, at 576.

¹⁰⁹ 15 U.S.C. § 1602(g); 12 C.F.R. pt. 1026.2(a)(14); see also Fonte, *supra* note 21, at 576 (explaining that the purpose of TILA is to protect consumers against inaccurate and unfair credit card practices).

¹¹⁰ 12 C.F.R. 1026.1(b)-(c). An open-end credit is "a plan under which the credit reasonably contemplates repeated transactions, which prescribes the terms of such transactions, and which provides for a finance charge which may be computed from time to time on the outstanding unpaid balance." 15 U.S.C. § 1602(j). Regulation Z elaborates on this definition and states that open-end credit means "consumer credit extended by a credit under a plan in which (1) [t]he credit reasonably contemplates repeated transactions; (2) [t]he creditor may impose a finance charge from time to time on an outstanding unpaid balance; and (3) [t]he amount of credit that may be extended to the consumer during the term of the plan...is

generally made available to the extent that any outstanding balance is unpaid." 12 C.F.R. pt. 1026.2(a)(20). A closed-end credit is defined as a consumer credit other than an open-end credit. 12 C.F.R. pt. 1026.2(a)(10).

¹¹¹ 15 U.S.C. § 1637a.

¹¹² Fair Credit Billing Act, Pub. L. No. 93-495, tit. III, §306, 88 Stat. 1512 (1974) (codified at 15 U.S.C. §§ 1666-1666j). In addition to the FCBA, state laws may also have billing error provisions that protect consumers. NAT'L CONSUMER L. CTR., TRUTH IN LENDING (10th ed. 2019), § 7.9, www.nclc.org/library. State billing error laws are beyond the scope of this Article.

¹¹³ 15 U.S.C. § 1666(b). The other listed billing errors are failure to include a payment or other credit to the account; computational error in the credit-related portion of the statement; an extension of credit for which the consumer requests additional clarification or documentation; and failure to send the periodic statement to the consumer in writing at least twenty days before the end of the billing cycle for the periodic statement. *Id.*

¹¹⁴ § 1666(a). An account holder who receives a statement with a billing error must dispute the charge in writing by sending a written notice to the creditor. *Id.* The creditor must receive the notice within 60 days of the statement date. *Id.*

¹¹⁵ § 1666(a)(3)(B). For example, if the billing error notice claims that the property or services were not delivered or not delivered as agreed, the creditor must determine whether the property was actually delivered as agreed or at least mailed or sent. Regulation

error, the creditor may not attempt to collect the amount in dispute or report or threaten to report the disputed amount to a credit agency or collection agency.¹¹⁶ As long as the consumer is disputing the amount in good faith, the creditor may not respond to a billing error notice by restricting or closing the consumer's account.¹¹⁷

The billing error dispute must be resolved within two complete billing cycles or ninety days, whichever is sooner.¹¹⁸ If the creditor determines that a billing error occurred, it must credit the consumer's account with any disputed amount and related charges.¹¹⁹ The creditor must also report the resolution of the billing error to any credit reporting agency if it notified any agency of the delinquency.¹²⁰ Conversely, if the creditor concludes that the consumer owes all or part of the disputed amount, the creditor must: notify the consumer in writing of the amount owed and time for payment; allow the consumer a grace period for payment of the amount; not report the disputed amount delinquent before the grace period ends or before ten days have passed since the consumer's receipt of the notice to pay, whichever time period is longer.¹²¹ During the grace period, if the consumer notifies the creditor in writing that they still dispute the charge, the creditor must report the amount as disputed if it reports it as delinquent.¹²²

When a specific type of billing error known as an unauthorized charge is made, TILA and Regulation Z limit a consumer's liability to the lesser of \$50 or the dollar amount of the unauthorized charges incurred prior to the cardholder notifying

the card issuer of the unauthorized use.¹²³ Unauthorized use means any "use of the credit card by a person, other than the cardholder, who does not have actual, implied, or apparent authority for such use, and from which the cardholder receives no benefit."¹²⁴ Once a consumer gives notice of an unauthorized use, the creditor has the burden of proving whether the charge was authorized.¹²⁵

iii. *The Prepaid Account Rule*

On April 1, 2019, the CFPB implemented the Prepaid Account Rule (Rule), which placed prepaid accounts within the scope of both Regulations E and Z.¹²⁶ Prepaid cards emerged in the 1990s, and these services are still among the fastest-growing segment of the financial payments industry.¹²⁷ Consumers use prepaid cards in a variety of situations such as for federal and state benefits, as an alternative to debit cards and bank accounts, for student aid through campus cards, and as inmate release prepaid cards.¹²⁸ Due to significant consumer issues arising with prepaid accounts, including unclear legal protections and remedies for lost or stolen cards, unauthorized charges, and errors, the CFPB enacted this new rule to address those issues.¹²⁹ Once a user registers their prepaid account in their name, the user has liability protection and may invoke error resolution provisions under the EFTA or TILA depending on the nature of the transaction.¹³⁰

The Prepaid Account Rule applies to the following groups of prepaid accounts: (1) payroll card accounts directly or

Z, Official Interpretations 12 C.F.R. pt. 1026.13(f)-3.ii. An investigation is not required if either the creditor chooses to correct the account as requested by the consumer or if the consumer withdraws the billing error notice. Regulation Z, Official Interpretations 12 C.F.R. pt. 1026.13(b)-1, (c)-2.

¹¹⁶ 15 U.S.C. §§ 1666(d), 1666a(a). The creditor may still report the amount as "in dispute." Regulation Z, Official Interpretations 12 C.F.R. pt. 1026.13(d)(2)-1.

¹¹⁷ 12 C.F.R. pt. 1026.13(d)(3). Taking any adverse action against a consumer for asserting FCBA rights also violates the consumer's rights under the Equal Credit Opportunity Act. 15 U.S.C. § 1691(e).

¹¹⁸ 15 U.S.C. § 1666(a)(B); 12 C.F.R. pt. 1026.13(c)(2).

¹¹⁹ 12 C.F.R. § 1026.13(e)(1).

¹²⁰ 15 U.S.C. § 1666a(c).

¹²¹ 12 C.F.R. pt. 1026.13(g). If the creditor determines that there was no billing error or a different error than that which the consumer complained of, the creditor must mail or deliver an explanation for its conclusion and it must provide the consumer with documentary evidence if requested. 15 U.S.C. § 1666(a)(3)(B)(ii); 12 C.F.R. pt. 1026.13(f).

¹²² 15 U.S.C. § 1666a(b).

¹²³ 15 U.S.C. § 1643(a)(1)(B); 12 C.F.R. pt. 1026.12(b)(1)(ii).

¹²⁴ 15 U.S.C. § 1602(p); 12 C.F.R. pt. 1026.12(b)(1)(i).

¹²⁵ 15 U.S.C. § 1643(b). No investigation is necessary if the creditor does not impose liability for the unauthorized use.

Regulation Z, Official Interpretations, 12 C.F.R. pt. 1026.12(b)-2.

¹²⁶ 12 C.F.R. pt. 1005.28; Prepaid Accounts Under the Electronic Fund Transfer Act (Regulation E) and the Truth In Lending Act (Regulation Z), 83 Fed. Reg. 6364, 6364 (Feb. 13, 2018) [hereinafter Prepaid Account Rule].

¹²⁷ See Lauren Saunders, *New CFPB Rule Provides Enforceable Protections for Prepaid Cards*, NAT'L CONSUMER L. CTR. (Apr. 16, 2019), <https://library.nclc.org/new-cfpb-rule-provides-enforceable-protections-prepaid-cards>; *A Brief History of Prepaid Cards*, UNIBUL'S MONEY BLOG, <http://blog.unibulmerchantservices.com/a-brief-history-of-prepaid-cards/> (last visited Nov. 28, 2020).

¹²⁸ Saunders, *supra* note 127.

¹²⁹ *Id.*

¹³⁰ See 12 C.F.R. pts. 1005.18(e)(3)(iii), 1026.61(a)(1)(i). A prepaid account is registered when the issuer successfully collects and verifies a consumer's identifying information as required by federal and state law. Official Interpretations of Regulation Z, pt. 1026.61(c)-1; see also Regulation E, Official Interpretations, 12 C.F.R. pt. 1005.18(e)-5 (explaining that collecting and verifying consumers' identifying information during enrollment satisfying the identification and verification process).

indirectly established through an employer and to which wages, salary, or other employee compensation are disbursed regularly; (2) government benefits accounts; (3) accounts labeled or marketed as “prepaid” and usable at unaffiliated merchants or at ATMs; and (4) accounts that are issued on a prepaid basis in a specified amount or not issued on a prepaid basis but can be loaded with funds thereafter and whose primary function is to conduct transactions with multiple unaffiliated merchants, at ATMs, or for person-to-person transfers.¹³¹ For the last two categories, the accounts must be accessible at unaffiliated merchants.¹³² This Rule does not apply to gift cards that are usable only at a particular store or group of stores, college cards that are usable only on campus, or transit cards.¹³³

In the CFPB’s Final Prepaid Account Rule, the Bureau listed “digital wallets” under the purview of the Prepaid Account Rule.¹³⁴ The CFPB described digital wallets as a way for consumers to electronically store one or more payment credentials.¹³⁵ According to the CFPB, these payment credentials may be accessed by the consumer through a website or mobile application, and some digital wallets may allow a consumer to store funds in them directly.¹³⁶ The Bureau further clarified that digital wallets may be used for P2P transfers and person-to-business transfers (*i.e.* to pay merchants).¹³⁷

In addition to extending general Regulation E protections, the Prepaid Account Rule requires the following: clear, uniform fee charts; a warning if funds are not FDIC insured; basic account information for free; and public and consumer access to account agreements and fee schedules.¹³⁸ Even if an entity is not covered by the Prepaid Rule specifically, it may still be subject to Regulation E if it is an EFT service provider that

does not hold a consumer’s account.¹³⁹ Under Regulation E, an EFT provider that does not hold a consumer’s account is subject to Regulation E if the provider issues an access device that the consumer can use to access the consumer’s account held by a financial institution and has no agreement with the account-holding institution regarding such access.¹⁴⁰

The Prepaid Account Rule also amended Regulation Z and expanded its coverage to credit features that a prepaid account may offer.¹⁴¹ Regulation Z has its own definition of a prepaid card, which is defined as “any card, code, or other device that can be used to access a prepaid account.”¹⁴² Nevertheless, the definition of a Prepaid Account is the same across both Regulations E and Z.¹⁴³ Through the Prepaid Account Rule, Regulation Z now regulates prepaid accounts that offer a credit feature in conjunction with a prepaid account where the credit feature is offered by the prepaid account issuer and that credit can be accessed in the course of a transaction conducted with the prepaid card to obtain goods or services, obtain cash, or transmit P2P transfers.¹⁴⁴ The Rule designates these prepaid accounts as “hybrid prepaid-credit cards.”¹⁴⁵ The credit feature on a hybrid prepaid-credit card must be separate from the asset portion of the prepaid account, and the user must be able to periodically access the credit feature.¹⁴⁶ The asset feature is defined as an asset account or asset subaccount of a prepaid account.¹⁴⁷ If the prepaid card qualifies as a hybrid prepaid-credit card, then the prepaid card is considered a credit card, and the account issuer is considered a card issuer under Regulation Z.¹⁴⁸ The CFPB has stated that hybrid-prepaid credit cards will generally satisfy the definition of an open-end credit.¹⁴⁹ So long as a consumer is contractually obligated to

¹³¹ 12 C.F.R. § 1005.2(b)(3)(i).

¹³² 12 C.F.R. § 1005.2(b)(3)(i)(C)-(D).

¹³³ 12 C.F.R. § 1005.2(b)(3)(ii)(D).

¹³⁴ Prepaid Account Rule, 83 Fed. Reg. 6364, 6364 (Feb. 13, 2018).

¹³⁵ *Id.*

¹³⁶ *Id.*

¹³⁷ *See id.* at 6421.

¹³⁸ *See generally* 12 C.F.R. pt. 1005.18(b)-(h). Regarding the fee schedule, the Prepaid Account Rule requires a short form disclosure that must include information about the periodic fee, per purchase fee, ATM withdrawal fees, cash reload fee, ATM balance inquiry fee, customer service fee, and an inactivity fee. 12 C.F.R. pt. 1005.18(b)(2). These fees must be disclosed regardless of whether they are charged by the issuer. Regulation E, Official Interpretations 12 C.F.R. pt. 1005.18(b)(2).1. The issuer must also disclose any other fees charged. 12 C.F.R. pt. (b)(2)(viii).

¹³⁹ *See* 12 C.F.R. pt. 1005.14(a)-(b).

¹⁴⁰ 12 C.F.R. pt. 1005.14(a).

¹⁴¹ Prepaid Account Rule, 83 Fed. Reg. 6364, 6364 (Feb. 13, 2018).

¹⁴² 12 C.F.R. 1026.61(a)(5)(vii). Confusingly, Regulation Z’s definition of a prepaid card is similar to Regulation E’s definition of an access device. *See* 12 C.F.R. § 1005.12(c).

¹⁴³ 12 C.F.R. pts. 1005.2(b)(3)(i), 1026.61(a)(5)(v).

¹⁴⁴ 12 C.F.R. pt. 1026.61(a).

¹⁴⁵ *Id.*

¹⁴⁶ 12 C.F.R. pt. 1026.61(a)(2)(i)(A). This is referred to as a “covered separate credit feature.” 12 C.F.R. pt. 1026.61(a)(2)(i). The CFPB had a dual purpose for instituting this structural requirement: (1) so consumers can better understand that they are accessing a credit; and (2) so creditors could implement Regulation Z’s requirements for hybrid-prepaid credit cards. Prepaid Account Rule, 81 Fed. Reg. 83,934, 84,264–84,265 (Nov. 22, 2016).

¹⁴⁷ 12 C.F.R. pt. 1026.61(a)(5)(ii).

¹⁴⁸ 12 C.F.R. pt. 1026.61(a)(1)(ii); Regulation Z, Official Interpretations, 12 C.F.R. pt. 1026.61(a)(3)(ii)-1.

¹⁴⁹ *See* 81 Fed. Reg. 83,934, 84,164, 84,190 (Nov. 22, 2016).

repay the credit, any credit issued by the prepaid account issuer constitutes a “plan” for the purposes of open-end credit.¹⁵⁰

Under the Prepaid Account Rule, structuring a credit feature as a negative balance on the asset feature of the prepaid account is a violation of Part 1026.61(b), which requires that any credit feature accessible by a hybrid prepaid-credit card be structured as a separate credit feature using either a credit subaccount or a separate credit account.¹⁵¹ Unless the prepaid card qualifies for the incidental overdraft exception, it will trigger coverage as a hybrid prepaid-credit card as long as it is a single device that can be used from time to time to access credit that can be extended through a negative balance on the asset feature, even though this is a violation of the Prepaid Account Rule.¹⁵²

The exception to the hybrid prepaid-credit card provision applies where the credit is incidental and the prepaid card issuer does not charge credit-related fees for that credit.¹⁵³ Specifically, a prepaid card that extends credit through a negative balance on the asset feature is not a hybrid prepaid credit card where: (1) the prepaid card cannot access credit from a covered separate credit feature that is offered by a prepaid account issuer or its affiliate, and (2) the prepaid card can only access credit extended through a negative balance on the asset feature under very limited circumstances.¹⁵⁴ The Rule qualifies that to satisfy the second criterion, the prepaid account issuer (1) must have an established policy and practice of either declining to authorize any transaction for which it reasonably believes the consumer has insufficient or unavailable funds in the asset feature of the prepaid account at the time the transaction is authorized or declining to authorize such transactions, except where the amount of the transaction will not take the account negative by more than \$10 or certain

transactions that are conducted while incoming deposits to the prepaid account are pending; and (2) must not impose any overdraft fees, fees for holding a negative balance, or fees for the availability of credit or other fees that are higher on cards with a credit feature.¹⁵⁵ Incoming deposits include cases where the prepaid account issuer has received a request from the consumer to load funds to the prepaid account from a separate asset account if there are insufficient funds in the asset feature of the prepaid account to fund the transaction.¹⁵⁶ The prepaid account must meet all of the listed factors to qualify for the exception for credit extended through a negative balance.¹⁵⁷ If a prepaid account qualifies for the exception and is thus not considered a hybrid-prepaid credit card, then the prepaid account is neither a “card issuer” nor a “creditor” under Regulation Z with respect to the incidental overdraft.¹⁵⁸

If a prepaid account triggers coverage as a hybrid prepaid-credit card, then it must follow timing requirements related to linking the credit product as set forth in Regulation Z.¹⁵⁹ For a hybrid prepaid-credit card, the nature of the transaction will determine whether Regulation Z billing error procedures apply or Regulation E error resolution procedures.¹⁶⁰ If the transaction is solely from the credit feature, then Regulation Z applies, but if the transaction is solely from the asset feature, then Regulation E applies.¹⁶¹ When a transaction is paid for by both the asset feature and the credit feature, then Regulation E primarily applies but Regulation Z applies to the credit portion of the transaction.¹⁶² If the transaction is paid by both the asset and credit features, then Regulation E error resolution procedures primarily apply, but certain Regulation Z provisions apply to the credit portion of the transaction.¹⁶³

¹⁵⁰ 12 C.F.R. § 1026.2(a)(20); Regulation Z, Official Interpretations, 12 C.F.R. pt. 1026.2(a)(20)(iv)-2.ii.

¹⁵¹ 12 C.F.R. pts. 1026.61(a)(3)(ii), 1026.61(b); *see also* pt. 1026.61(a)(5)(viii) (explaining that the term “separate credit feature” excludes a negative balance on the asset feature). A credit extension through a negative balance can occur during either the authorization phase or in later periods up to settlement. Regulation Z, Official Interpretations, 12 C.F.R. pt. 1026.61(a)(3)(i)-1.

¹⁵² 12 C.F.R. pt. 1026.61(a)(3); *see also* Regulation Z, Official Interpretations, 12 C.F.R. pt. 1026.61(a)(3)(i)-1.iii (illustrating an example of where a credit extension occurs during the course of authorizing a transaction and triggers the hybrid prepaid-credit card provision).

¹⁵³ 12 C.F.R. pt. 1026.61(a)(4).

¹⁵⁴ 12 C.F.R. pt. 1026.61(a)(4)(i)-(ii).

¹⁵⁵ 12 C.F.R. pt. 1026.61(a)(4)(ii)(A)-(B).

¹⁵⁶ 12 C.F.R. pt. 1026.61(a)(4)(ii)(A); Regulation Z, Official Interpretations, 12 C.F.R. pt. 1026.61(a)(4)(ii)(A)-3. Incoming deposits may also mean cases where the prepaid account issuer has received confirmation or instruction for an incoming EFT from a

separate asset account to load funds to the prepaid account, such as a direct deposit of salary or government benefits. Regulation Z, Official Interpretations, 12 C.F.R. pt. 1026.61(a)(4)(ii)(A)-3.

¹⁵⁷ 12 C.F.R. pt. 1026.61(a)(4).

¹⁵⁸ Regulation Z, Official Interpretations 12 C.F.R. pt. 1026.61(a)(4)-1.v.A.

¹⁵⁹ 12 C.F.R. 1026.61(c). Specifically, for a covered separate credit feature that is accessible by a hybrid-prepaid credit card, the issuer must wait thirty days after the registration of the prepaid account to (1) open a covered separate credit feature; (2) solicit or provide an application to open a separate credit feature; and (3) permit an existing credit feature opened by the customer to become a covered separate credit feature accessible by a hybrid prepaid-credit card. *Id.*

¹⁶⁰ *See* Regulation Z, Official Interpretations, 12 C.F.R. pt. 1026.13(i)-4.i to 4.2.

¹⁶¹ *Id.*

¹⁶² *Id.*

¹⁶³ Regulation Z, Official Interpretations, 12 C.F.R. pt. 1026.13(i)-4.iii (stating that Regulation E applies but certain Regulation Z

1. *The Prepaid Account Rule's Application to P2P Platforms*

Deposit holding P2P platforms are considered financial institutions under the Rule because they hold registered asset “accounts” and a user can initiate a payment through the mobile application which functions as an “access device.”¹⁶⁴ P2P accounts are registered and verified during the enrollment process.¹⁶⁵ Thus, the Rule requires deposit holding P2P platforms like PayPal, Venmo, Cash App, and Google Wallet to comply with Regulation E’s requirements for EFTs and Regulation Z’s requirements for any qualifying credit.¹⁶⁶

Although Regulation E’s application to P2P payments is straightforward, Regulation Z will only apply if the P2P platform qualifies as a hybrid prepaid-credit card.¹⁶⁷ Considering the payment structure of P2P platforms, the credit they extend through a negative balance on a user’s stored balance would qualify as an incidental overdraft exception to a hybrid prepaid-credit card.¹⁶⁸ First, this credit feature is not separate from the asset portion of the P2P account because the overdraft directly applies as a negative balance on the account’s stored funds.¹⁶⁹ Second, the P2P account only accesses this credit under limited circumstances where the P2P application extends this credit while an incoming deposit from the linked payment method is pending, specifically after the user has initiated a payment giving the P2P platform confirmation or instruction for an incoming EFT from the linked payment method.¹⁷⁰ Third, the P2P platform does not

provisions (*i.e.*, withholding payment, adverse credit reports, and the creditor’s duties after resolution) apply to the credit extension).

¹⁶⁴ See 12 C.F.R. pts. 1005.2(a)(1), (b)(3), 1005.18(e)(3)(iii); Regulation E, Official Interpretations, 12 C.F.R. pt. 1005.2(b)(3)(i)-6; *supra* note 26 and accompanying text (explaining that a new user’s identity is verified and the user is registered during the process to open a P2P account).

¹⁶⁵ See *supra* note 26 and accompanying text (explaining that a new user’s identity is verified and the user is registered during the process to open a P2P account); *see also* Regulation E, Official Interpretations, 12 C.F.R. pt. 1005.18(e)-5 (explaining that collecting and verifying consumers’ identifying information during enrollment satisfies the requisite identification and verification process). At a press conference, former CFPB Director Richard Cordray stated that “the new rule applies to traditional prepaid cards as well as mobile wallets, person-to-person payment products and other electronic accounts that can store funds.” Richard Cordray, *Prepared Remarks of CFPB Director Richard Cordray on the Prepaid Accounts Rule Press Call* (Oct. 5, 2016), <https://www.consumerfinance.gov/about-us/newsroom/prepared-remarks-cfpb-director-richard-cordray-prepaid-accounts-rule-press-call/>. P2P platforms that operate as a “pass-through” service that do not store deposits are not covered by this Rule. Regulation E, Official Interpretations, 12 C.F.R. pt. 1005.2(b)(3)(i)-6.

charge any fees in relation to extending a negative balance.¹⁷¹ Because the incidental overdraft qualifies for the exception to a hybrid prepaid-credit card, that credit will be subject to Regulation E and its applicable error resolution provision.¹⁷²

c. *Federal Deposit Insurance Corporation*

Federal Deposit Insurance Corporation (FDIC) insurance provides up to \$250,000 deposit insurance per customer account per insured financial institution in case of the institution’s failure.¹⁷³ Under the Federal Deposit Insurance Act, the FDIC considers the following factors when evaluating an application for deposit insurance: the institution’s financial history and condition; the adequacy of its capital structure; its future earnings prospects; the general character and fitness of its management; the risk presented by the institution to the Deposit Insurance Fund; the convenience and needs of the community to be served by the institution; and whether the institution’s corporate powers are consistent with the purposes of the FDI Act.¹⁷⁴ To obtain FDIC insurance, an institution must have either a bank or savings association charter from an appropriate state banking authority or the Office of the Comptroller of the Currency.¹⁷⁵ P2P providers are not required to obtain FDIC insurance, and generally, they do not have FDIC insurance on consumers’ account balances, except for direct deposits.¹⁷⁶

¹⁶⁶ See 12 C.F.R. pts. 1005.2(b)(3), 1005.18(e)(3); 12 C.F.R. § 1026.61(a)(1). Of the deposit holding P2P platforms, all include the EFTA’s error resolution procedures in their user agreements. *See, e.g., Additional Cash Terms of Service, supra* note 37.

¹⁶⁷ See 12 C.F.R. pts. 1005.2(b)(3), 1026.61(a)(1).

¹⁶⁸ See 12 C.F.R. pt. 1026.61(a)(4)(i)-(ii); *supra* notes 45-50 and accompanying text (explaining how P2P transactions are processed).

¹⁶⁹ See 12 C.F.R. pt. 1026.61(a)(4)(i); *supra* note 47-48 and accompanying text.

¹⁷⁰ See 12 C.F.R. pt. 1026.61(a)(4)(ii); Regulation Z, Official Interpretation 12 C.F.R. 1026.61(a)(4)(ii)(A)-3; *supra* note 32-33 and accompanying text.

¹⁷¹ See 12 C.F.R. pt. 1026.61(a)(4)(ii)(B); *see, e.g., Additional Cash Terms of Service, supra* note 37.

¹⁷² See 12 C.F.R. pts. 1005.18(a), 1026.61(a)(4).

¹⁷³ See generally Federal Deposit Insurance Act, 12 U.S.C. §§ 1818-31.

¹⁷⁴ 12 U.S.C. § 1816.

¹⁷⁵ FED. DEPOSIT INS. CORP., APPLYING FOR DEPOSIT INSURANCE, at 9 (2017),

<https://www.fdic.gov/regulations/applications/handbook.pdf>.

¹⁷⁶ See 12 U.S.C. § 1811(a); *supra* note 57 and accompanying text.

III. Consumer Protection Problems in the P2P Market

Consumers often seek out P2P platforms to transfer payments due to the convenient and instantaneous payment structures of these platforms.¹⁷⁷ Whereas a wire transfer may take days to settle, a P2P payment is deposited into the recipient's account within a few minutes.¹⁷⁸ Additionally, the ongoing pandemic has spurred increased P2P usage as consumers continually seek to transact in a contactless world.¹⁷⁹ Despite all of the benefits of mobile payments, the novelty of P2P platforms means consumers may potentially bear all risks of loss in the event of a P2P company's insolvency or if they send a payment to the wrong person or even if they fall victim to fraudulent activity.¹⁸⁰ Before the advent of P2P platforms, usually banks insured against consumers' loss of deposits through FDIC or assumed the risk of fraud under the Uniform Commercial Code in other payment scenarios.¹⁸¹ Without the heavy regulations imposed on banks, P2P platforms serve as fertile ground for consumer protection issues.¹⁸² This Part identifies some of the common P2P consumer protection issues under the current legal framework for mobile payments.¹⁸³

a. Protection of Consumer Deposits

As the volume of P2P transactions increases and users continue to store funds on their accounts, there are concerns about whether a consumer's stored balance is safe against the insolvency of the P2P payment provider.¹⁸⁴ Consumers often allow a balance to remain in their P2P accounts rather than transferring them to a linked bank account immediately because they assume that they will soon enough need that money to fund another payment.¹⁸⁵ Aside from requiring P2P

platforms to disclose whether users' account balances are FDIC insured, the Prepaid Account Rule does not provide any protection in the event of a P2P platform's insolvency.¹⁸⁶ Instead, FDIC insurance and state money transmitter licenses provide protection for consumers' stored deposits, yet P2P platforms are only required to obtain the weaker safeguard, state money transmitter licenses.¹⁸⁷

FDIC insurance offers the most robust protections for a consumer's stored balance, but because P2P platforms do not have FDIC insurance on P2P accounts, consumers cannot rely on this insurance protecting their funds in the event of a P2P provider's insolvency.¹⁸⁸ Rather, they must rely on state money transmitter laws, which to some extent ensure that the covered entities have sufficient resources to prevent the loss of consumers' funds.¹⁸⁹ Similar to the FDIC application, the state regulatory agency will approve or deny the money transmitter's license application based on the applicant's financial condition, competence, and general fitness.¹⁹⁰ These regulations also require the money transmitter to file annual and periodic reports regarding its financial condition.¹⁹¹ Most importantly, state money transmitter laws require money transmitters to obtain surety bonds which give consumers some level of protection against a P2P application's insolvency as the consumer can submit a claim against a surety bond which is held in trust for the benefit of claimants.¹⁹²

Nevertheless, surety bonds do not provide consumer protection to the extent that FDIC insurance does.¹⁹³ Each state has different caps on the bonds or securities held by licensees, and those caps may not cover all consumers.¹⁹⁴ In

¹⁷⁷ See Mual, *supra* note 30. In addition to consumer protection issues surrounding instantaneous P2P payments, privacy and security are also critical concerns in this area. See Fonte, *supra* note 36, at 591. Due to space constraints, this Article will not address those consumer protection concerns.

¹⁷⁸ See Mual, *supra* note 30; Justin Pritchard, *How Wire Transfers Work: Sending and Receiving Money*, THE BALANCE (May 19, 2020), <https://www.thebalance.com/bank-wire-transfer-basics-315444>.

¹⁷⁹ Bryne Hobart, *No One's Splitting the Bill, but Venmo is Surging*, MARKER (Sept. 9, 2020) <https://marker.medium.com/no-ones-splitting-the-bill-but-venmo-is-surging-47617013ebb0>.

¹⁸⁰ *Can Regulators Foster Financial Innovation and Preserve Consumer Protections*, *supra* note 29.

¹⁸¹ See 12 U.S.C. §§ 1818-31; CONSUMER BANKING AND PAYMENTS LAW, *supra* note 1, § 6.7.1.

¹⁸² See *Can Regulators Foster Financial Innovation and Preserve Consumer Protections*, *supra* note 29.

¹⁸³ See *infra* notes 184-235.

¹⁸⁴ See Issa, *supra* note 38; Lisa Rowan, *Don't Keep a Balance in Your Venmo Account*, LIFE HACKER (Feb. 26, 2020),

<https://twocents.lifehacker.com/dont-keep-a-balance-in-your-venmo-account-1841910098>.

¹⁸⁵ See Issa, *supra* note 38; Rowan, *supra* note 184.

¹⁸⁶ See 12 C.F.R. pt. 1005.18(b)(4)(iii). EFTA and TILA also do not protect consumers' deposits. See generally 15 U.S.C. §§ 1601, 1693.

¹⁸⁷ See generally Federal Deposit Insurance Act, 12 U.S.C. §§ 1818-31; Mual, *supra* note 30.

¹⁸⁸ See *supra* notes 173-176 and accompanying text (discussing what is FDIC insurance coverage and explaining that P2P providers do not have that coverage); see, e.g., *Venmo User Agreement*, *supra* note 5.

¹⁸⁹ Fonte, *supra* note 36, at 584; Tu, *supra* note 61, at 85, 93.

¹⁹⁰ See 12 U.S.C. § 1816; Tu, *supra* note 61, at 92.

¹⁹¹ Tu, *supra* note 61, at 93.

¹⁹² CONSUMER BANKING AND PAYMENTS LAW, *supra* note 1, § 6.6.4.5.

¹⁹³ See CONSUMER BANKING AND PAYMENTS LAW, *supra* note 1, § 6.6.4.5.

¹⁹⁴ *Id.*

contrast, FDIC insures each depositor per bank up to \$250,000.¹⁹⁵ Additionally, the procedure for submitting claims against a surety bond or security is often more cumbersome than the process of accessing funds through FDIC insurance, which allows consumers of covered accounts immediate access to their funds.¹⁹⁶

b. *Protections Against Fraudulent Transactions*

On P2P platforms, there are few limits to the types of fraudulent activities a consumer could experience.¹⁹⁷ For example, an individual or entity could hack into a user's account and transfer a payment.¹⁹⁸ Alternatively, a consumer may initiate payment and inadvertently direct it to an unintended recipient, such as someone with the same or similar name as the intended recipient, or a consumer may initiate a payment for a product or service through an informal marketplace like Craigslist or Facebook Marketplace not realizing that they were scammed.¹⁹⁹ Although the Prepaid Account Rule and EFTA limit a consumer's liability in scenarios where an unauthorized payment was made, a consumer's liability may not be limited where the consumer initiated payment, thereby disqualifying the transaction from error resolution procedures for unauthorized payments.²⁰⁰

While state money transmitter laws apply to mobile payment applications, these laws are inadequate in solving issues of fraud on the platforms as their primary purpose is to ensure that the covered entities have sufficient resources to prevent the loss of consumers' funds.²⁰¹ There are no requirements for investigating or remedying transfers made in error or unauthorized transfers.²⁰² Moreover, the fragmented nature of state money transmitter licensing laws makes it

difficult to regulate P2P transactions, which often cross state lines and must comply with licensing laws in all fifty states.²⁰³

In contrast, the EFTA and TILA both provide consumer protections through separate error resolution processes.²⁰⁴ Through the Prepaid Account Rule, P2P platforms are required to comply with robust error resolution procedures for EFT or credit billing errors, if it is a hybrid prepaid-credit card.²⁰⁵ Under those circumstances, if a consumer is a victim of an unauthorized payment, their liability for that transaction may be limited if they meet the notice and timing requirements.²⁰⁶ In contrast, the Prepaid Account Rule's application to transfers initiated by the consumer is murkier.²⁰⁷

Where a fraudulent transfer is initiated by a hacker, it qualifies as an unauthorized payment because it was initiated by a person other than the user who did not have actual authority to initiate that transfer, and the consumer received no benefit from it.²⁰⁸ Furthermore, even though the EFT occurred through an access device (the P2P application), the P2P platform can identify the user to whom the account was furnished, satisfying the Rule's additional requirement.²⁰⁹ So long as the user provides timely notice, their liability will be limited per the EFTA and Regulation E.²¹⁰

Conversely, for consumer initiated payments, P2P platforms' unique payment structure causes consumer problems that may not be resolved by the EFTA or Regulation E.²¹¹ Through the Prepaid Account Rule, payments funded by a user's P2P account balance or through a linked payment source would fall under the EFTA and Regulation E.²¹² For payments funded by a linked payment source which result in the P2P platform fronting a payment as the underlying transaction settles, although the user may be able to cancel the

¹⁹⁵ 12 U.S.C. § 1821(a)(1)(E).

¹⁹⁶ CONSUMER BANKING AND PAYMENTS LAW, *supra* note 1, § 6.6.4.5.

¹⁹⁷ See Waqas, *Everything You Must Know About Common Venmo Scams*, HACKREAD (July 1, 2020), <https://www.hackread.com/everything-you-must-know-about-common-venmo-scams/>.

¹⁹⁸ See Waqas, *supra* note 197.

¹⁹⁹ See Andrew Burnett, *Venmo Hacking Thieves Steal Thousands From Daniel Negreanu and Erik Seidel*, POKER TUBE (Nov. 26, 2020), <https://www.pokertube.com/article/venmo-hacking-thieves-steal-thousands-from-daniel-negreanu-and-erik-seidel>; Rudegeair, *supra* note 6.

²⁰⁰ See 12 C.F.R. pt. 1005.6(b).

²⁰¹ See Fonte, *supra* note 36, at 584.

²⁰² See Tu, *supra* note 61, at 92-93.

²⁰³ See Tu, *supra* note 61, at 93. In addition, applying for and complying with each state's money transmitter law can be costly and burdensome. See *id.* Licensees must both bear the costs of the license application and renewal as well as the costs of establishing a compliance program that encompasses all fifty states' laws. *Id.*

²⁰⁴ See generally 12 C.F.R. pts. 1005.11, 1026.13.

²⁰⁵ See generally 12 C.F.R. pts. 1005.11, 1026.13.

²⁰⁶ See 12 C.F.R. pt. 1005.6(b)

²⁰⁷ See 12 C.F.R. pts. 1005.11(a).

²⁰⁸ See 15 U.S.C. § 1693a(12).

²⁰⁹ 12 C.F.R. pts. 1005.2(a), 1005.18(e)(3)(iii); Official Interpretations, Regulation E, 12 C.F.R. pt. 1005.18(e)-5

²¹⁰ See 15 U.S.C. § 1693g(a); 12 C.F.R. pt. 1005.6(b)(1).

²¹¹ See 15 U.S.C. 1693f(f); 12 C.F.R. pt. 1005.11(a)(1).

²¹² See 12 C.F.R. pt. 1005.2(b)(3); see also *supra* notes 166-172 and accompanying text (explaining that Regulation E applies to deposit holding P2P platforms).

payment from being transferred out of their underlying payment method, the P2P platform will have already advanced the payment to the recipient, leaving the scammed sender's account with a negative balance that they must pay off.²¹³ Even though P2P platforms extend a line of credit that they seek to collect, this qualifies as an exception to a hybrid prepaid-credit card.²¹⁴ Accordingly, Regulation E applies to the overdraft credit.²¹⁵ Regulation E's error resolution processes do not provide safeguards for an incidental overdraft if it was not unauthorized, however.²¹⁶

Generally, in situations where a user is scammed or misdirects a payment, the consumer initiates the transfer, and only after realizing their error do they attempt to cancel that transfer.²¹⁷ Under the EFTA and Regulation E, this does not satisfy the definition of an unauthorized transfer because the transfer was initiated by a person who had the authority to initiate the transfer—even though the user received no benefit.²¹⁸ Nevertheless, it is unclear what an authorized transfer is since neither EFTA nor Regulation E defines what is an authorized transfer nor do they provide a right to revoke payment of a single EFT.²¹⁹ Instead, they define unauthorized transfers and state that an EFT error includes unauthorized EFTs and incorrect EFTs to or from the consumer's account.²²⁰ It is equally unclear what constitutes an incorrect EFT to or from a consumer's account.²²¹

In the absence of direct authority, P2P companies have placed all liability on consumers by treating payment initiation as a form of authorization.²²² Many companies in their disclosure statements place responsibility for consumer losses

on mobile carriers, phone manufacturers, or other parties, who are often not identified.²²³ Furthermore, these P2P companies do very little to inform customers about legal recourse in the event of a loss of funds through not authorized payments.²²⁴ Venmo, in particular, indicates on its FAQ page that the sender should first contact the recipient and request the latter return the funds to the sender.²²⁵ If that does not work, then the sender should contact Venmo who states that it cannot guarantee the money will be recovered.²²⁶ To prevent these unintended transaction issues, P2P platforms warn users that they should only send payments to those they know.²²⁷

c. *Protections Against Debt Collections from Fraudulent Payments*

As another byproduct of the P2P payment structure, users may end up with a negative balance even after successfully canceling their underlying payment, and as a result, P2P providers may send this “debt” to a collection agency to recoup the payment they advanced.²²⁸ Venmo, as an example, reports any money it “loaned” as a negative balance on the consumer's account if the sender's underlying payment account does not settle these funds.²²⁹ Venmo has communicated to some of its users who did not promptly pay off a negative balance that it would put this “debt” through a collection agency even if the sender was the victim of a scam.²³⁰

If the company puts this debt through a collection agency, it will negatively affect a consumer's credit report, which in turn impacts their ability to obtain loans, qualify for

²¹³ See Rudegeair, *supra* note 6.

²¹⁴ See 12 C.F.R. pt. 1026.61(a)(4)(i)-(ii); see also *supra* notes 168-172 and accompanying notes (discussing why P2P payment overdrafts qualify for the incidental overdraft exception to hybrid prepaid-credit card).

²¹⁵ See 12 C.F.R. pt. 1026.61(a)(4)(i)-(ii).

²¹⁶ See 12 C.F.R. pt. 1005.11(a)(1).

²¹⁷ See Demos, *supra* note 48.

²¹⁸ See 15 U.S.C. § 1693a(12); 12 C.F.R. pt. 1005.2(m).

²¹⁹ See generally 15 U.S.C. § 1693-1693r; 12 C.F.R. pt. 1005.1-1005.20. But see § 1693e (establishing that a preauthorized EFT must be authorized by the consumer in writing and a consumer may stop this payment by notifying the financial institution orally or in writing up to three business days preceding the scheduled transfer date).

²²⁰ 15 U.S.C. § 1693a(12), 1693f(f)(2); 12 C.F.R. 1005.2(m), 1005.11(a)(1)(ii).

²²¹ See 15 U.S.C. § 1693f(f)(2); 12 C.F.R. 1005.11(a)(1)(ii).

²²² See *Can Regulators Foster Financial Innovation and Preserve Consumer Protections*, *supra* note 14.

²²³ See *id.*

²²⁴ See *id.*

²²⁵ *I Paid The Wrong Person!*, VENMO, <https://help.venmo.com/hc/en-us/articles/209681208-I-paid-the-wrong-person-> (last visited Nov. 28, 2020).

²²⁶ *Id.*

²²⁷ See *id.*

²²⁸ See Rudegeair, *supra* note 6; Demos, *supra* note 48.

²²⁹ See Rudegeair, *supra* note 6.

²³⁰ *Id.*; see also *Venmo User Agreement*, *supra* note 5 (reserving the right to “engage in collection efforts to recover” any amounts owed to the company). According to a Venmo spokesperson, collecting on negative balances is a policy that Venmo carried over from PayPal. *Venmo Pursues Customers With Negative Balance*, PYMNTS (Mar. 25, 2019), <https://www.pymnts.com/news/payment-methods/2019/venmo-paypal-debt-collection-money-transfer/>. In contrast, Cash App has stated that as of its current policy, it does not report negative account balances to a collection agency. Rudegeair, *supra* note 6.

rental housing, get a job, etc.²³¹ A consumer is then left to either repay that debt and limit the impact on their credit score or dispute the debt.²³² The collection agency will often remove an inaccurate debt from a consumer's credit report.²³³ If the debt is accurate, however, then a consumer may not be able to negotiate the removal of this debt because credit reporting agencies themselves prohibit the removal of collection information, even if a consumer fully pays off the collection.²³⁴ Regulation E does not ban collecting debt resulting from fraudulent or misdirected transactions.²³⁵

IV. Proposal

Clear federal and state regulations guide financial institutions to track and prevent consumers' losses as a result of fraudulent activity or scams.²³⁶ For example, heavily regulated entities like banks and credit unions are strongly incentivized to prevent losses from fraudulent activities against their account holders because they are typically liable when payment is unauthorized or in the case of credit cards when payment is in error.²³⁷ The current legal framework surrounding P2P payments leaves many risks on P2P consumers with little incentive for P2P platforms to minimize harms.²³⁸ Therefore, regulations surrounding P2P payments should be adapted to induce the same effect on P2P payment platforms.²³⁹ In particular, the CFPB should expand the Prepaid Account Rule to properly account for the unique consumer harms arising from P2P payments, and concurrently, the Bureau should provide educational materials to consumers

to better inform them of the limited coverage on their stored funds if their P2P platform fails.²⁴⁰

While the Prepaid Account Rule extends EFTA and TILA protections to P2P platforms, the Rule does not account for the unique structure of P2P payments.²⁴¹ In fact, when formulating the current Rule, the CFPB refused to ban any type of overdraft on prepaid accounts because it understood this market as seldom offering credit services.²⁴² Whereas other prepaid cards may not often offer overdraft services, most P2P providers do in fact structure their transactions to offer overdraft services to facilitate immediate payments when a user's stored funds do not fully cover the transaction.²⁴³ Because P2P payment platforms' main draw is their instantaneous payments, it will not be possible to prohibit them from immediate payments.²⁴⁴ Considering this, the Rule should extend Regulation E's coverage by expanding the definition of an error, requiring additional authentication factors for fund transfers, and incorporating a stop on debt collection while a transaction is in dispute.²⁴⁵

First, to provide clarity and consistency for consumers and P2P platforms, the Rule should be amended to expand the definition of an error to include payments sent to illegitimate recipients.²⁴⁶ P2P companies have treated customer initiation of a payment as lawful authorization regardless of the legitimacy of the recipient.²⁴⁷ Therefore, a P2P transfer error should also include those where the sender initiates payment to an illegitimate recipient and from which the sender receives

²³¹ See Latoya Irby, *How Do Collection Accounts Affect You and Your Credit*, THE BALANCE (June 27, 2020), <https://www.thebalance.com/a-background-on-debt-collection-accounts-960569#:~:text=Your%20credit%20score%20will%20drop,or%20remains%20unpaid%20or%20both.&text=You%20can%20lessen%20the%20effects,score%20by%20paying%20it%20off>.

²³² See *id.*

²³³ See *id.*

²³⁴ See *id.*

²³⁵ See generally 12 C.F.R. pt. 1005.1-.18.

²³⁶ See *Can Regulators Foster Financial Innovation and Preserve Consumer Protections*, *supra* note 14.

²³⁷ See *id.*

²³⁸ See *supra* Part III.

²³⁹ See *Can Regulators Foster Financial Innovation and Preserve Consumer Protections*, *supra* note 14.

²⁴⁰ See *infra* notes 241-265 and accompanying text. Although outside the scope of this Article, PayPal's lawsuit against the CFPB on its Prepaid Account Rule offers interesting arguments against lumping together digital wallets with general purpose reloadable prepaid cards. See generally Complaint, *PayPal, Inc. v. CFPB*, CV No. 19-3700 (2019). PayPal's lawsuit challenges the Rule's short

form disclosures which allegedly require digital wallets to list fees they do not charge, thereby only further confusing consumers, and it challenges the Rule's imposition of a thirty-day ban on linking a credit card to a digital wallet. See generally *id.*

²⁴¹ See *supra* notes 197-235 and accompanying text.

²⁴² See Prepaid Account Rule, 81 Fed. Reg. 83,934, 84,161, 84,323 (Nov. 22, 2016).

²⁴³ See *supra* note 168-172 and accompanying text (arguing that the P2P payment structure gives rise to an incidental overdraft).

²⁴⁴ See Mual, *supra* note 30.

²⁴⁵ See *infra* notes 246-258 and accompanying text.

²⁴⁶ See *Can Regulators Foster Financial Innovation and Preserve Consumer Protections*, *supra* note 29; see also CONSUMER BANKING AND PAYMENTS LAW, *supra* note 1, § 5.3.1.1 (stating that Regulation E does not define what is an authorized payment). Because the user initiated payment, and the user automatically has actual authority to initiate the transfer, amending the definition of unauthorized use is likely not possible. See 15 U.S.C. § 1693a(12) (defining an unauthorized payment transfer as one initiated by a person other than the consumer without actual authority to initiate the transfer and from which the consumer does not benefit).

²⁴⁷ See *Can Regulators Foster Financial Innovation and Preserve Consumer Protections*, *supra* note 29.

no benefit.²⁴⁸ By stipulating that a sender cannot receive a benefit from a P2P payment error, the Rule can prevent senders who conspire with recipients in fraudulent transactions from benefiting from Regulation E's error resolution process.²⁴⁹ If a P2P transaction satisfies these requirements, the sender will be able to invoke Regulation E's error resolution procedures and potentially remedy any harm done to them.²⁵⁰

To meet the legitimate recipient factor, an amended Prepaid Account Rule should require P2P platforms to add an additional recipient authentication factor.²⁵¹ Specifically, the sender should have to verify the identity of the recipient through two of the following possible factors, a username, QR code, or phone number.²⁵² Because of this additional, but not overly burdensome obstacle, this two-factor authentication system will reduce the chances of a payment being directed to the wrong recipient.²⁵³ Recipients should also have to manually verify and accept the payment before it is deposited into their account.²⁵⁴ While this will not block all misdirected funds from entering the wrong accounts, this may provide some buffer time for the P2P platform to cancel or reverse a payment if a sender realizes they made a payment in error.²⁵⁵ And, in an ideal world, honest people will decline a payment that was accidentally sent to them.

²⁴⁸ See 12 C.F.R. pt. 1005.11(a)(1).

²⁴⁹ See 15 U.S.C. § 1693a(12) (excluding EFTs initiated with fraudulent intent by the consumer or anyone acting together with the consumer from the definition of an unauthorized transfer).

²⁵⁰ See generally 12 C.F.R. pt. 1005.11.

²⁵¹ See Tobie Stranger, *Why Apple Pay is the Highest-Rated Mobile P2P Payment Service*, CONSUMER REPORTS (Nov. 21, 2018) <https://www.consumerreports.org/digital-payments/mobile-p2p-payment-services-review/> (comparing the different P2P platforms' features).

²⁵² See *id.* This is analogous to the authenticating factors to send wire transfers, which require the sender to provide, at minimum, the recipient's name and address and the recipient's bank account number. See WELLS FARGO, *The Ins and outs of Wire Transfers*, <https://www.wellsfargo.com/financial-education/basic-finances/manage-money/payments/ins-outs-transfers/> (last visited Nov. 29, 2020).

²⁵³ See Stranger, *supra* note 251 (rating Apply Pay as the best P2P platform due, in part, to its additional payment authentication features).

²⁵⁴ Cf. *Send and Receive Money With Apply Pay*, APPLY, <https://support.apple.com/en-us/HT207875#:~:text=If%20you%20choose%20Manually%20Accept,the%20payment%20under%20Latest%20Transactions> (last visited Nov. 30, 2020). This would be modeled after Apply Pay's manual payment acceptance feature, where once a recipient receives money, they must manually accept it within seven days. *Id.*

Finally, P2P companies should be prohibited from collecting or attempting to collect on this debt once a consumer invokes Regulation E's error resolution procedures, akin to TILA preventing a card issuer from attempting to collect on a disputed charge while the investigation is pending.²⁵⁶ Even though the incidental overdraft does not qualify as a credit under TILA or even a hybrid prepaid-credit card under the Prepaid Account Rule, P2P companies still attempt to collect on the overdraft as though it were credit, including sending the debt to debt collectors.²⁵⁷ But the CFPB should not go further and extend TILA to cover incidental overdrafts. Doing so would be overly difficult because of its onerous requirements, such as ensuring that the consumer has the ability to repay the overdraft and waiting thirty days after the account is registered before offering to the consumer overdraft credit features.²⁵⁸ These requirements are excessive for a temporary extension of credit like an incidental overdraft.²⁵⁹

Along with amending regulation, the CFPB should seek to educate consumers in their financial decision-making process.²⁶⁰ As P2P payments rise, it would be beneficial to the public for the CFPB to undertake efforts to increase consumer education regarding safely using P2P payments as well as explaining their legal rights in the event of fraudulent activity on their P2P accounts.²⁶¹ Especially in the case of payments made through a stored balance, the CFPB should warn

Nonetheless, this feature is optional, and Apply Pay also allows its users to opt out and accept payments automatically. See *id.*

²⁵⁵ Cf. *Cancel Payment*, VENMO, <https://help.venmo.com/hc/en-us/articles/235171088-Cancel-Payment> (last visited Dec. 1, 2020) (stating that a sender may be able to cancel a payment if it is sent to a recipient that is not registered with Venmo, which indicates that the small buffer of time allows Venmo to cancel initiated payments).

²⁵⁶ See 15 U.S.C. §§ 1666(d), 1666a(a).

²⁵⁷ See Rudegeair, *supra* note 6; *supra* note 168 and accompanying text

²⁵⁸ See 12 C.F.R. pts. 1026.51(a)(1)(i), 1026.61(c)(1).

²⁵⁹ See Prepaid Account Rule, 83 Fed. Reg. 6364, 6390 (Feb. 13, 2018).

²⁶⁰ See *Consumer Education and External Affairs*, CONSUMER FIN. PROT. BUREAU, <https://www.consumerfinance.gov/about-us/the-bureau/bureau-structure/consumer-education-engagement/> (last visited Nov. 30, 2020) (stating that CFPB identifies and develops financial education materials to assist consumers); cf. *CFPB Launches Nationwide Education Campaign About New Mortgage Rules*, CONSUMER FIN. PROT. BUREAU (Dec. 18, 2013), <https://www.consumerfinance.gov/about-us/newsroom/cfpb-launches-nationwide-education-campaign-about-new-mortgage-rules/> (showing example of the CFPB's mortgage rule education campaign).

²⁶¹ See Hobart, *supra* note 179.

consumers that currently there is no legal recourse through the EFTA or TILA if a consumer initiates the payment, even if they were scammed.²⁶²

Although state money transmitter laws do not insure consumer funds to the same extent FDIC does, it is not feasible to require P2P platforms to obtain FDIC insurance because of the burdensome requirements involved in applying for this insurance, including the need to first obtain a state or OCC charter.²⁶³ Under the Prepaid Account Rule, P2P platforms are required to disclose that users' stored funds are not FDIC insured, but many consumers do not bother to read that fine print in the User Agreement.²⁶⁴ Thus, in an information campaign, CFPB should warn consumers that their stored funds, unless they are direct deposits, are not insured by FDIC, and although state laws provide some level of protection, they are not as strong safeguards against the loss of funds if the P2P provider files for bankruptcy.²⁶⁵ In that same vein, the CFPB should also encourage consumers to only maintain a minimal balance on a P2P account, and this minimal balance should be whatever the user can afford to lose.²⁶⁶

While increased regulation in the P2P sphere seems logical, it is necessary to address reasonable arguments against increased regulation.²⁶⁷ First, opponents of P2P regulation strongly argue that increased regulation will stifle innovation and limit the products and services provided by P2P platforms.²⁶⁸ Even though increased regulation adds additional burdens on companies that may diminish their capacity to innovate new products and services, it does not make sense to allow companies to continue operating in a manner that severely harms consumers.²⁶⁹ These harms have become especially prevalent during fraught times like this

ongoing pandemic.²⁷⁰ On balance, the proposed increased regulation is not too burdensome considering that some P2P platforms have already incorporated parts of the suggested solutions in their policies; given how prevalent consumer abuses have been, the benefit to consumers outweighs the burden to the companies.²⁷¹

Second, opponents of regulation argue that increased regulation will make it more difficult for unbanked and underbanked users to transact on P2P platforms.²⁷² Because these users either lack or have inadequate access to traditional banks, they may rely on P2P platforms to operate as a pseudo-bank.²⁷³ However, studies suggest that among the unbanked and underbanked, P2P usage is significantly lower compared with the broader population.²⁷⁴ This is likely due to a lack of access to the internet and cellular data services, as well as a higher reliance on cash.²⁷⁵ Therefore, increased P2P payment regulation likely will not harm unbanked or underbanked consumers.²⁷⁶

Conclusion

P2P platforms have significantly disrupted the payments industry by facilitating rapid fund transfers between individuals. Although their payment structure leads to many benefits for consumers, as a double-edged sword, it also enables substantial harm to consumers. The current legal framework provides some protection against consumer harm, but they do not effectively cover the P2P payment structure. Therefore, to combat some of these harms, the Consumer Financial Protection Bureau should amend existing regulations to properly account for P2P platforms' payment structure, and it should educate consumers on safely using these platforms.

²⁶² See *supra* notes 197-235 and accompanying text.

²⁶³ See APPLYING FOR DEPOSIT INSURANCE, *supra* note 179, at 9.

²⁶⁴ See 12 C.F.R. pt. 1005.18(b)(xi); Caroline Cakebread, *You're Not Alone, No One Reads Terms of Service Agreements*, BUSINESS INSIDER (Nov. 15, 2017), <https://www.businessinsider.com/deloitte-study-91-percent-agree-terms-of-service-without-reading-2017-11>.

²⁶⁵ See Rowan, *supra* note 184.

²⁶⁶ See *id.*

²⁶⁷ See A FINANCIAL SYSTEM THAT CREATES ECONOMIC OPPORTUNITIES: NONBANK FINANCIALS, FINTECH, AND INNOVATION, *supra* note 2, at 33; *Can Regulators Foster Financial Innovation and Preserve Consumer Protections*, *supra* note 29.

²⁶⁸ A FINANCIAL SYSTEM THAT CREATES ECONOMIC OPPORTUNITIES: NONBANK FINANCIALS, FINTECH, AND INNOVATION, *supra* note 2, at 18; Alan McQuinn, *Supporting Financial Innovation Through Flexible Regulation*, INFO. TECH. &

INNOVATION FOUND., at 2 (Nov. 2019), <https://itif.org/sites/default/files/2019-fintech-regulations.pdf>.

²⁶⁹ See Ben Bernanke, *Financial Innovation and Consumer Protection*, BD. OF GOVERNORS OF FED. RESRV. (April 17, 2009), <https://www.federalreserve.gov/newsevents/speech/bernanke20090417a.htm> (discussing the delicate balance between promoting financial innovation and managing risks to consumers).

²⁷⁰ See Rudegeair, *supra* note 6.

²⁷¹ See *id.* (stating that Cash App does not send a negative balance to a collection agency); Stranger, *supra* note 251 (illustrating how Apple's multi-factor authentication system works).

²⁷² See *Can Regulators Foster Financial Innovation and Preserve Consumer Protections*, *supra* note 29.

²⁷³ See *id.*

²⁷⁴ See *id.*

²⁷⁵ See *id.*

²⁷⁶ See *id.*