UNITED STATES OF AMERICA
FEDERAL TRADE COMMISSION
WASHINGTON, D.C. 20580

Office of the Secretary

February 4, 2005

Jennifer L. Johnson, Secretary
Board of Governors of the Federal Reserve System
20th and C Streets, N.W.
Washington, D.C. 20551

Re: Docket No. R-1210

Dear Ms. Johnson:

The Federal Trade Commission ("Commission" or "FTC") appreciates the opportunity to comment on amendments proposed by the Federal Reserve Board ("Board") to Regulation E, which implements the Electronic Fund Transfer Act ("EFTA"), and its Official Staff Commentary ("Commentary").[1]

The FTC has wide-ranging responsibilities concerning consumer financial issues for most nonbank segments of the economy that may be affected by this proposal, including diverse retail

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[1] The EFTA is at 15 U.S.C. § 1693 et seq.; Regulation E is at 12 C.F.R. § 205; the Commentary is at 12 C.F.R. § 205, Supp. 1. The EFTA provides a framework for the rights, liabilities, and responsibilities of participants in electronic fund transfer systems. See "Findings and Purpose" of the EFTA. 15 U.S.C. § 1693.

[2] The TILA is at 15 U.S.C. § 1601 et seq.; the FTC Act is at 15 U.S.C. § 41 et seq.

[3] Information regarding these activities is available at: http://www.ftc.gov.

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[8] Section 205.3(b)-1.v. and -3 of the Commentary. 12 C.F.R. § 205.3(b)-1.v. and -3, Supp.1.

[9] 69 Fed. Reg. at 55,997; proposed Sections 205.3(a) and (b)(2) of Regulation E, and proposed Section 205.3(b)(2)-1 of the Commentary. See 69 Fed. Reg. at 56,000.

[10] See Section 917(c) of the EFTA, 15 U.S.C. Section 1693o(c).

[11] The Board has proposed to cover merchants and other payees who use ECK in point-of-purchase and mail-in transactions. Because of the increasing use of one-time electronic debits in telephone and online transactions, in the future the Board also may wish to cover entities who use one-time electronic debits in these transactions. In telephone and online transactions, like point-of-purchase and mail-in transactions: 1) the transaction begins with a check; 2) source information from the check is used by the merchant/payee; 3) the information is processed as a single debit; and 4) the consumer's account is quickly debited.

The FTC has received complaints (including about unauthorized transactions) from consumers regarding one-time electronic debits in telephone and web purchases. Although, under Regulation E, some form of authorization is needed for all EFTs, the current absence of specific rules for telephone and online transactions means the mandate is vague and difficult to enforce. As a result, consumers may find it difficult to invoke protection under Regulation E to address fraud, including by using the unauthorized transfer rules and error resolution rules and by invoking their private right of action under the EFTA. See Sections 205.6 and 205.11 of Regulation E, 12 C.F.R. §§ 205.6 and 205.11 and Section 915 of the EFTA, 15 U.S.C. § 1693m.

[12] NACHA, the Electronic Payments Association (formerly, the National Automated Clearing House Association) is a private self-regulatory industry organization that establishes

standards, rules, and procedures for the automated clearinghouse ("ACH") network. ACH is an electronic funds transfer system that provides for interbank clearing of electronic payments by participating financial institutions. NACHA rules currently require merchants to obtain a written and signed or similarly authenticated authorization from the consumer for in-store ECK transactions. NACHA's rule, however, does not apply to mail-in transactions. See 69 Fed. Reg.

signs to provide the requisite notice. NACHA currently requires signed authorization.[15] The Commission agrees that signed written authorization generally is an appropriate and effective means of obtaining authorization.[16] The Commission has no specific data, however, on the costs or feasibility of requiring signed written authorization in every transaction. In addition, the Commission does not have sufficient grounds for concluding that other forms of notice, such as prominently placed in-store signs, could not be adequate.

As discussed below, the Commission also believes that the Board should elaborate on the "clear and conspicuous" requirement to ensure that ECK information is noticeable and understandable to consumers. The clear and conspicuous standard is particularly important for merchants' or other payees' in-store signs, which should be prominent, not hidden or obscured.

C. CLEAR AND CONSPICUOUS INFORMATION, AND CONSUMER RESEARCH

In general, the FTC supports the Board's use of notices and model forms to facilitate compliance and enhance consumer understanding of ECK. These disclosures, however, include technical information and pertain to relatively new electronic payment systems with which consumers may be less familiar than more longstanding options, such as paper checks, credit cards, and even debit cards. Therefore, the Board should provide additional explanation about what constitutes a clear and conspicuous notice in ECK transactions, including by providing examples. In addition, the Board may wish to consider whether the use of consumer research would be helpful in designing text and format for the disclosures envisioned by the proposal.

1. CLEAR AND CONSPICUOUS INFORMATION

The Board intends to make ECK authorization and notices provided to consumers subject to Regulation E's "clear and conspicuous" standard.[17] The Commission suggests that, to assist both consumers and businesses, the Board consider providing further explanation regarding the application of this standard to ECK, including by providing examples. Consumers who received ECK disclosures have complained to the FTC that the information was: 1) for mail-in transactions – buried in fine print and placed on the back of or in the middle of unrelated credit card information on periodic statements; and 2) for in-store transactions – hidden from view, obstructed by large ads for special discounts, or inconspicuously placed on the side of cash

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[15] See http://www.nacha.org. NACHA permits merchants to use "similar authentication" as well. Neither the NACHA rule, nor the Regulation E proposal, requires signed authorization for mail-in transactions.

[16] In a consumer's dispute regarding an unauthorized in-store transfer, a signed written authorization also may be helpful in determining whether the consumer, in fact, authorized the transaction.

[17] 69 Fed. Reg. at 56,000.

registers.[18] The Commission recommends that the Board clarify that these practices would not meet the "clear and conspicuous" standard.

Consumer information is also clearer if it avoids fine print and technical terms.[19] Adding language to the Commentary that adapts these concepts to ECK transactions could be useful to consumers, foster compliance, and facilitate enforcement. For example, the Commentary could emphasize the need for noticeability and understandability of information and note that use of fine print would not be sufficient. FTC publications discussing case law and other regulatory requirements[20] and other consumer financial laws provide additional guidance on this issue.[21]

2. CONSUMER RESEARCH

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[18] Some consumers reported receiving no explanation or an insufficient explanation from sales clerks who handed back checks, after ECK processing, that were stamped "void." Other consumers have reported not receiving any ECK disclosures, which they later learned should have been provided.

[19] See FEDERAL TRADE COMM'N, GETTING NOTICED: WRITING EFFECTIVE FINANCIAL PRIVACY NOTICES, at http://www.ftc.gov/bcp/online/pubs/buspubs/getnoticed.htm. Notices are more effective if they use plain language, avoid legal jargon, and recognize that customers may not be familiar with the applicable issues. Id. In determining what is "clear and conspicuous" for purposes of the Fair Credit Reporting Act, which does not define the term, a federal appellate court recently looked to other statutes, including the Uniform Commercial Code and Truth in Lending Act. It considered the following factors: "the location of the notice within the document, the type size used within the notice as well as the type size in comparison to the rest of the document . . . whether the notice is set off in any other way – spacing, font style, all capitals, etc. . . there must be something about the way that the notice is presented in the document such that the consumer's attention will be drawn to it." Cole v. U.S. Capital, Inc., No. 03-3331, 2004 U.S. App. LEXIS 24177, at *27 (7th Cir. Nov. 19, 2004).

[20] See FEDERAL TRADE COMM'N, DOT COM DISCLOSURES, at http://www.ftc.gov/bcp/online/pubs/buspubs/dotcom/index.html.

[21] For example, Regulation M's Commentary offers the following explanation of the "clear and conspicuous" standard for written disclosures: "disclosures must be presented in a way that does not obscure the relationship of the terms to each other . . . and . . . must be legible, whether typewritten, handwritten, or printed by computer." See Section 213.3(a)-2 of Regulation M's Commentary, 12 C.F.R. § 213.3(a)-2, Supp. 1. The Consumer Leasing Act amends the TILA; implementing Regulation M is at 12 C.F.R. § 213. Regulation M also provides the following explanation for advertising disclosures: "very fine print in a television advertisement or detailed and very rapidly stated information in a radio advertisement does not meet the clear-and-conspicuous standard if consumers cannot see and read or hear, and cannot comprehend, the information required to be disclosed." Section 213.7(b)-1 of Regulation M's Commentary, 12 C.F.R. § 213.7(b)-1, Supp. 1.

In the FTC's experience, it is possible that well-intentioned disclosures can be drafted in ways that inadvertently cause consumer confusion and result in unintended consumer impressions.[22]

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[22] See "The Effect of Mortgage Compensation Disclosures on Consumers and Competition: A Controlled Experiment," Federal Trade Commission Bureau of Economics Staff Report, by James M. Lacko and Janis K. Pappalardo (Feb. 2004). See also "The Effect of Mortgage Broker Compensation Disclosures on Consumers and Competition: A Controlled Experiment . . . or Why Disclosures are Tricky," presented by James M. Lacko and Janis K. Pappalardo, FTC Bureau of Economics at "Reflecting on Thirty-five Years of Consumer Disclosure Regulation" at Georgetown University Credit Research Center, Washington, D.C. (Oct. 5, 2004).

[23] See proposed Appendices A-2 and A-6.

[24] Consumer research and testing could help answer the following questions: How will consumers interpret and understand the particular disclosures? How will the disclosures affect consumer decisions? Would other text or formats be simpler and more suitable?

[25] The Board also has proposed alternative disclosures to allow merchants and payees to disclose that they may process a transaction as either an ECK or as an electronic check under Check 21. See 69 Fed. Reg. 56,001. See also note 14, above. The Board's proposed model forms for these disclosures use some technical terminology with which consumers may not be familiar. Because ECKs and electronic processing under Check 21 differ and because consumers may have less familiarity with these systems, testing on disclosures in this area could be especially useful.

[26] See

"free" trial offer, which automatically converted to mandatory payments unless the consumer canceled before the end of the trial period. In these cases, the sellers or telemarketers allegedly did not disclose adequately the terms of the negative option feature and failed to obtain affirmative authorization for recurrent charges that they made to consumers' deposit accounts.[30] The FTC continues to bring cases challenging these practices.[31]

In certain FTC investigations, companies have produced copies of tape recordings that highlight the problems inherent in using tape recordings to evidence consumer authorization for recurrent debits. These tape recordings have included: 1) taped portions of a telemarketing call containing a consumer's assent to something other than the recurrent transfers; 2) taped portions of calls that revealed ambiguous consumer comments intended as conversation fillers ("uh huh") or that failed to reveal a clear response to the solicitation (as the telemarketer rapidly delivers sales messages); 3) tape recordings that were manipulated or falsified to create the appearance of consumer authorization; and 4) confusing requests to consumers to punch numbers on a telephone keypad to authorize payment.[32]

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[30] See, e.g., U.S. v. Mantra Films, No. CV 03-9184 RSWL (MANx) (C.D. Cal. Aug. 4, 2004). In this case, the court entered a stipulated order containing injunctive relief, consumer redress and other relief to resolve various allegations, including that the defendants telemarketed videos and DVDs to consumers in a negative option program without disclosing material terms of that program and made recurrent debits without consumers' authorization. The complaint charged the defendants with, among other things, violating the EFTA and Section 5 of the FTC Act, 15 U.S.C. § 45. See also America Online, 125 F.T.C. 403 (1998); Prodigy Servs. Corp.,125 F.T.C. 430 (1998), and CompuServe, Inc., 125 F.T.C. 451 (1998) (alleging misrepresentations, failure to disclose material terms and conditions in connection with free trial offers of Internet service, and automatic debiting of checking accounts without obtaining consumers' prior written assent); United States v. Budget Marketing, Inc., No. 88-1698 E (S.D. Iowa Mar. 17, 1997) (consent decree settling charges that telemarketers selling magazine subscriptions failed to obtain written authorization from consumers for preauthorized transfers).

[31] The Commission's Telemarketing Sales Rule ("TSR") requires sellers and telemarketers that use previously obtained ("preacquired") consumer account information for billing purposes in "free-to-pay" transactions (transactions that involve a free trial offer that automatically converts to mandatory payments unless the consumer cancels before the conversion) to tape-record the entire transaction. See TSR, 16 C.F.R. § 310.4(a)(6)(i)(c). See also TSR Statement of Basis and Purpose, 68 Fed. Reg. at 4,621 (Jan. 29, 2003). Of course, the TSR only addresses certain telemarketing transactions and only applies to entities under FTC jurisdiction. Similar problems can occur in other contexts, however, including online or at point of sale.

[32] For example, the consumer can be instructed to "press 2 for yes and 3 for no." It is not always clear to what the "yes" and "no" apply, i.e., to the mailing of one item or repetitive mailings of items. Limited, unclear instructions may be provided for making the selection, and procedures may not exist for cancellation of the process if the consumer accidentally presses the wrong number or changes his or her decision.

should identify with specificity the account to be charged.[35] This language would help ensure that the consumer's clear and knowing authorization is obtained before his or her account is repeatedly accessed.

Fifth, in discussing the authorization standard in its Federal Register notice, the Board made various references to the standard's applicability to "institutions."[36] The authorization standard is highly relevant, however, to business entities that are not "institutions" within the meaning of Regulation E, such as telemarketers, traditional retail sellers, online sellers, creditors, and other payees.[37] Therefore, the Commission recommends that the Board revise the language in the final Federal Register notice to clarify its application to those entities, such as by substituting the term "merchants and other payees" or "payees" for "institutions."[38]

B. BONA FIDE ERROR

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[35] See TSR, 16 C.F.R. § 310.4(a)(6).

[36] 69 Fed. Reg. 56,003.

[37] "Financial institutions" under Regulation E hold an account belonging to a consumer or issue an access device and agree with a consumer to provide electronic fund transfer services. See Section 205.2(i) of Regulation E, 12 C.F.R. § 205.2(i).

[38] In addition, in its Federal Register notice, the Board states that authorization for preauthorized transfers must be readily identifiable "to the consumer" and the terms of the preauthorized debits must be clear and readily understandable "to the consumer," citing Section 205.10(b)-6 of the Commentary. See 69 Fed. Reg. at 56,003. In fact, this provision makes no reference "to the consumer." Accordingly, the FTC suggests including the terms "to the consumer" after each clause in the Commentary provision concerning authorization for preauthorized transfers. The resulting provision would read: "An authorization is valid if it is readily identifiable as such to the consumer, and the terms of the preauthorized transfer are clear and readily understandable to the consumer."

[39] Section 205.10(b)-7 of the Commentary, 12 C.F.R. § 205.10(b)-7, Supp. 1.

The Board has proposed to modify the Commentary so as to deem as a reasonable procedure to avoid errors a company's request to a consumer that she specify whether she is using a debit card or credit card. This modification would apply to telephone and online transactions. Under the Board's proposal, if the consumer indicates that she is using a credit card for a recurring payment (or that she is not using a debit card), the company may rely on that statement without seeking further information.

Because of the widespread use of debit cards in telemarketing and online transactions, the Commission agrees that companies in general should be permitted to rely on a customer's specification about the type of card he or she is using. However, the Commission recommends that the Board expressly require
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[40] The Board might include the following language: "If the payee learns that a pattern of problems may exist because, for example, numerous consumers have complained about unauthorized charges to debit cards, reasonable procedures would include investigation of the problem generally and related changes to its procedures."

[41] In addition, the Commission concurs with the Board's decision, in connection with the reasonable procedure rule, not to require, at this time, that merchants rely on or use BIN (bank identification number) tables to verify that a credit card or debit card is being used. See 69 Fed. Reg. at 56,003. The Commission notes, however, that the recent settlement with respect to Wal-Mart in In Re Visa Check/Mastermoney Antitrust Litigation, No. 96-CV-5238 (E.D.N.Y. Jan. 23, 2004) requires Visa and Master Card to make available to merchants lists of such numbers. Should this information become available in "real-time, online" form in the future, the Board should consider revisiting this issue.

[42] Section 205.11(c)(4) of Regulation E, 12 C.F.R. § 205.11(c)(4), and Section 205.11(c)(4) of the Commentary, Section 205.11(c)(4), Supp.1. An agreement authorizing the direct debit of a consumer's monthly utility payment from the consumer's bank account is an example of an

indicating that a particular merchant or other payee is experiencing a high chargeback rate, the institution should consider that information when evaluating a disputed transaction involving that entity. Otherwise, an institution may not give full consideration to reasonably available information

[47] For example, if an institution's subcontractor for consumer services experienced an error (such as an error with a processor) and, as a result, the system generated duplicate debiting of accounts, that problem should be included in the investigation.