

PUTTING STORED-VALUE CARDS IN THEIR PLACE

by
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This Essay explores the effects of stored-value cards on social welfare. We argue that stored-value cards, in general, are socially beneficial payment devices. Their burgeoning use benefits society in three main plains. First, by replacing paper-based instruments in market segments previously inaccessible to card-based payments, stored-value cards lower the private and public costs of payment transactions. Second, by extending the use of card-based payment systems towards lower- and middle-income households, stored-value cards foster inclusion of those households in the financial mainstream of our society. Third, by operating without an extension of credit, stored-value cards help to limit the uniquely American reutilization of credit transactions associated with the widespread use of credit-card borrowing.

We further identify several risks associated with the use of stored-value cards. First, as in many cases their issuers are not federal banks, stored-value cards expose consumers to the possibility of losing funds in the case of issuer's insolvency. Second, as their mechanism is vulnerable to data breaches, they expose consumers to unauthorized uses of their funds—as opposed to other payment cards where consumers enjoy regulatory protection on this matter. Third, they raise the issue of the unused funds remaining on the card after most of it has been depleted.

We recommend policies that will foster the use of stored-value cards, while adopting several rules that will confine their associated risks. We therefore call for adequate supervision that will assure the availability of deposits insurance to most stored-value cards; an extension of the current unauthorized use rules to stored-value cards; and a mechanism that will allow cash out of small unused funds associated with those cards. We also emphasize the need to exempt from regulation small stored-value cards programs in order to foster their beneficial use in contexts where the risks of harm are slight.

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INTRODUCTION

Stored-value cards are the latest innovation in the payment-card field. After the 1970s introduced consumers to credit cards and the 1990s to debit cards, stored-value cards are the latest product trying to lead consumers forward to a cashless society. The spread of stored-value cards is not limited to a specific country. Rather, in recent years consumers around the globe have started to include stored-value cards among the payment devices they hold in their wallets. In the United States, the cards were used for at least \$150 billion of transactions in 2012 and were projected to surpass \$200 billion in 2013.¹ Canada reported more than \$70 billion in stored-value card transactions in 2010.² Stored-value cards are also commonly used in Japan,³ Europe,⁴ and Russia.⁵ Even in the highly

¹ *Purchase Volume at Merchants on U.S. General Purpose Cards*, NILSON REP., May 2013, at 1, 1; BITS, *PREPAID ACCESS CARDS: OVERVIEW AND EMERGING RISKS 4* (July 2012), available at <http://www.bits.org/publications/fraud/PrepaidCardsRisksFinalJul2012.pdf>.

² TASK FORCE FOR THE PAYMENTS SYS. REVIEW, *SCENARIOS FOR THE FUTURE OF THE CANADIAN PAYMENT SYSTEM* 61, 63 (2011), available at http://www.viewpointlearning.com/wpcontent/uploads/2011/05/FINANCE_Viewpoint_Report_English.pdf (stating that the total transactions value in Canada in 2010 was \$7.2 trillion and that the portion of stored-value cards out of this value was 1%).

³ BANK OF JAPAN, *RECENT DEVELOPMENTS IN ELECTRONIC MONEY IN JAPAN* 4 (Dec. 2012), available at http://www.boj.or.jp/en/research/brp/ron_2012/data/ron121221a.pdf (stating that in June 2012 the value of transactions made with stored-value cards was JPY 198.1 billion).

⁴ BANK FOR INT'L SETTLEMENTS, *STATISTICS ON PAYMENT, CLEARING AND SETTLEMENT SYSTEMS IN THE CPSS COUNTRIES: FIGURES FOR 2011*, at 445 (Jan. 2013), available at <http://www.bis.org/cpmi/publ/d107.pdf> (stating that Italy reported

concentrated payment market of Israel, banks and merchants now offer several types of stored-value cards.⁶

Despite their apparent attractiveness to merchants and consumers, the cards have drawn withering and pervasive criticism from regulators and consumer advocates. Most obviously, stored-value cards are high on the list of products under scrutiny from the Consumer Financial Protection Bureau (CFPB). Among other things, the CFPB issued a 2012 notice of a general rulemaking regarding stored-value cards, generally expressing concern about the “lack of a comprehensive federal regulatory regime.”⁷ The following year, the CFPB issued an alert emphasizing concerns about employer compliance with regulations related to payroll cards.⁸ And it is not as if the CFPB is pursuing an agenda of its own in opposition to the will of Congress. To the contrary, leading legislators commonly press the CFPB to move even more vigorously.⁹ And, of course, stored-value cards are a common topic of proposed federal legislation.¹⁰ Nor is attention limited to the federal level. Rather, each of the 50 states has some form of statutory regulation of stored-value cards of one sort or another.¹¹

Although the great majority of the recent regulatory attention has focused on the problem of fees, the pervasive criticism of unduly high fees is fostering an atmosphere of general hostility to the basic product.

\$13.507 billion of stored-value-cards transactions in 2011, the Netherlands reported \$0.629 billion, and Germany reported \$0.174 billion).

⁵ *Id.* (stating that Russia had \$6.757 billion of stored-value-cards transactions in 2011).

⁶ Although credit cards continue to dominate the Israeli market, several of the central issuers now offer stored-value cards. For instance, Leumi Card is now offering a onetime closed-loop gift card in the amount of approximately \$250. Leumi also offers a new general-purpose reloadable open-loop card called “Leumi Card Cash,” available mainly for teenagers. See Press Release, Leumi, *Leumi Card CASH: Loaded Debit Card for Teens* (May 23, 2012), available at <http://www.leumi.co.il/Articles/26906>. Israel Post and C.A.L. (another large Israeli issuer) also offer an open-loop Visa stored-value card. See *Visa CAL Debit Card*, ISRAEL POST, <http://www.israelpost.co.il/postshirut.nsf/misparide/140?opendocument&L=EN>; *Loaded Visa Card*, CAL, <https://www.cal-online.co.il/he-IL/Cal/Cards/special/prepaid/Pages/welcome.aspx>.

⁷ Electronic Fund Transfers (Regulation E), 77 Fed. Reg. 30,923, 30,924 (proposed May 24, 2012) (to be codified at 12 C.F.R. pt. 1005).

⁸ CONSUMER FIN. PROTECTION BUREAU, CFPB BULLETIN 2013-10, at 1–4 (Sept. 12, 2013).

⁹ E.g., Letter to Richard Cordray, Director, CFPB & Seth Harris, Acting Sec’y, U.S. Dep’t Labor (July 11, 2013), reprinted in Press Release, U.S. Senator Richard Blumenthal, Blumenthal Urges CFPB, DOL to Protect Workers Paid with Predatory Payroll Cards (July 11, 2013), available at <http://www.blumenthal.senate.gov/newsroom/press/release/blumenthal-urges-cfpb-dol-to-protect-workers-paid-with-predatory-payroll-cards> (letter from 16 senators to CFPB urging more investigation and regulation of stored-value cards).

¹⁰ E.g., Prepaid Card Disclosure Act of 2014, S. 1903, 113th Cong. (2014).

¹¹ Heather Morton, *Gift Cards and Gift Certificates Statutes and Legislation*, NAT’L CONF. STATE LEGISLATORS (Jan. 17, 2014), <http://www.ncsl.org/research/financial-services-and-commerce/gift-cards-and-certificates-statutes-and-legis.aspx>.

With the CFPB poised for a general rulemaking about the product as a whole, it is important to situate the problems with fees in a broader context that considers not only the problematic attributes of some of the cards, but also the potential benefits of the product more generally.

In that vein, the purpose of this Essay is to urge a redirection of the regulatory and policy concerns related to stored-value cards. Without downplaying issues related to fees, protection for unauthorized payments, and the like, we contend that the narrow focus on what might be called the “traditional” regulatory issues pertaining to payment cards has obscured broad social benefits likely to accrue from broader use of the product. Among other things, the cards are likely to speed the transition to paperless transactions, foster democratization of the card market (because they are more useful for low- and moderate-income (LMI) households than credit cards and debit cards), and nudge consumers away from the routinized borrowing associated with the use of credit cards.

Collectively, we urge, those benefits are so important that they outweigh the minor regulatory issues that have preoccupied regulators and consumer advocates to date. We propose a set of simple and straightforward regulatory reforms designed to address the significant issues apparent from existing usage, without burdening the product so heavily as to stifle its deployment.

The first Part of the Essay describes the use of stored-value cards, their penetration of United States and global markets, and the legal frameworks that govern them. The second Part analyzes the principal factors that weigh for, and against, the use of stored-value cards. It emphasizes the substantial benefits of stored-value cards over other payment instruments, and concludes that the benefits justify policies that foster their spread. The third Part addresses the risks associated with stored-value cards. It considers not only the problem of fees, which has pervaded the existing discourse, but broader issues related to the product’s basic structure. We close briefly with a call for a broad-minded regulatory approach that takes care, lest well-meaning regulation deprive low- and moderate-income households of a product that can provide so much to them.

I. WHAT IS A “STORED-VALUE” CARD?

We start by describing the product in question. The “stored-value” card, often called a “prepaid” card, is a payment device that to the ordinary consumer looks exactly like a conventional credit card or debit card. What distinguishes the stored-value card from those older and more common products is that the stored-value card allows access to a balance previously associated with the card (“placed” or “deposited” on the card in the typical usage). Because the card has the same form as conventional credit and debit cards, and because the most commonly used ones bear Visa and MasterCard brands on their face, they can be used just as the more conventional cards: to withdraw funds from an ATM or to buy

products or services from merchants that accept Visa and MasterCard products.

Although it remains relatively unexamined in the academic literature, the stored-value card has been the most prominent innovation in the payment industry since the full-scale introduction of the debit card about fifteen years ago.¹² From essentially no market share in 2000, the cards have spread rapidly. In 2012, they were used for more than \$150 billion of retail purchase transactions, or 4% of all payment-card transactions.¹³ This may seem small compared to the totals for credit and debit cards (\$2.2 trillion and \$1.8 trillion, respectively), but it is still impressive for such a young device.¹⁴

Mechanically, the use of the card is no different from use of a conventional credit or debit card. The consumer decides to initiate a retail transaction with a merchant. If the consumer decides to use the stored-value card to pay for this transaction, the first step is verifying that the merchant accepts the particular stored-value card in the consumer's possession. If the card is a general-purpose one (with a Visa or MasterCard brand) then all merchants that accept credit cards will accept it.¹⁵ If the card bears a more limited-purpose brand, then the consumer would have to figure this out on a case-by-case basis; often the card will be good only at the merchant (or group of merchants) indicated on the card. If the merchant accepts the card (which essentially means that the merchant has an agreement with a financial institution that can retrieve funds from the card to pay for the transaction), then the consumer will, usually, swipe the card in the merchant's terminal. Alternatively, the consumer might choose to enter a PIN. Acting through the merchant's acquirer, the point-of-sale terminal would initiate a connection to a remote server that contains data regarding the stored-value card's balance. After confirming that a sufficient balance for the transaction exists, it would then reduce the stored-value card balance by that amount and credit the merchant with that amount (reduced by the applicable interchange and acquisition fees).¹⁶ Similarly, as with branded credit and debit cards, the

¹² Ronald J. Mann, *Information Technology and Non-Legal Sanctions in Financing Transactions*, 54 VAND. L. REV. 1627, 1634 (2001).

¹³ *Purchase Volume at Merchants on U.S. General Purpose Cards*, *supra* note 1, at 1, 9. This data surely understates actual usage because it accounts only for general-purpose stored-value cards (those with a Visa or MasterCard brand).

¹⁴ *Id.* The rapid uptake is particularly impressive given the traditional hurdles new payments products face in establishing critical masses of users and merchants at the same time. See generally DAVID S. EVANS, *PLATFORM ECONOMICS: ESSAYS ON MULTI-SIDED BUSINESSES* 282–374 (2011).

¹⁵ The Visa and MasterCard honor-all-cards rules compel this result. See Ronald J. Mann, Essay, *Making Sense of Payments Policy in the Information Age*, 93 GEO. L.J. 633, 655 (2005).

¹⁶ BENJAMIN GEVA, *THE LAW OF ELECTRONIC FUNDS TRANSFER* § 6.02 (2014); RONALD J. MANN, *PAYMENT SYSTEMS AND OTHER FINANCIAL TRANSACTIONS* 336–41 (5th ed. 2011).

consumer with such a card ordinarily can use it to withdraw funds from most ATMs; because the entities that operate those ATMs typically are members of the Visa and MasterCard network, they can route stored-value transactions through those networks just as they would route credit or debit transactions.¹⁷

As the discussion above suggests, all stored-value cards are not the same. Generally speaking, for functional purposes the cards fall into two main categories: open-loop and closed-loop cards. Open-loop cards typically carry a brand (like Visa or MasterCard) that is accepted at a wide variety of merchants. Those stored-value cards can be used at any merchant that previously has engaged the services of a processor who is a member of the stored-value card brand-payment network.¹⁸ Closed-loop cards, by contrast, normally can be used only at the specific merchant that issued them. In essence, then, the purchase of such a card is perceived as a prepayment for a later purchase at the merchant—hence the common term “prepaid” cards.¹⁹ By far the most important application for those cards is the gift card, redeemable only at the merchant (or group of merchants) that issued it.

It is also important to note whether the card is a “single-charge” card or a “reloadable” card. Most commonly, open-loop cards can be reloaded and spent in a continuous (endless) cycle; by contrast, closed-loop cards typically are good only for one use, the expenditure of the funds originally placed on the card.²⁰

Although the discussion above emphasizes the functional similarities of stored-value cards and conventional credit and debit cards, they are fundamentally different in the relation between the issuer and the cardholder. The credit card rests on the issuer’s individualized underwriting decision to extend a credit line to the cardholder; when the card is used, the transactions are posted to a revolving credit account which can be repaid in small payments in the ordinary course over the ensuing years.²¹ The debit card accesses a conventional demand-deposit account and thus is (with rare exceptions) issued by the bank where the consumer maintains such an account; for most consumers there is only one such bank. Transactions on that card are funded by immediate withdrawals from the

¹⁷ Mann, *supra* note 15, at 654–55.

¹⁸ Philip Keitel, *The Laws, Regulations, Guidelines, and Industry Practices That Protect Consumers Who Use Gift Cards* 16 (Fed. Reserve Bank of Phila., Discussion Paper, 2008), <http://www.philadelphiafed.org/consumer-credit-and-payments/payment-cards-center/publications/discussion-papers/2008/D2008JulyGiftCard.pdf>.

¹⁹ For a more elaborated review of closed-loop stored-value cards and their regulation, see PHILIP KEITEL, *FEDERAL REGULATION OF THE PREPAID CARD INDUSTRY: COSTS, BENEFITS, AND CHANGING INDUSTRY DYNAMICS* 12–16 (2010), *available at* <http://www.philadelphiafed.org/consumer-credit-and-payments/payment-cards-center/events/conferences/2011/C2011-Federal-Regulation-of-Prepaid-Card-Industry.pdf>.

²⁰ *Id.* at 13–14.

²¹ See MANN, *supra* note 16, at 151–58.

account; if a transaction exceeds the balance of funds already in the account, the bank can honor it under the ordinary procedures for authorizing overdrafts on the account.²²

The stored-value card, by contrast, requires no such relationship between the issuer and the cardholder. Transactions on those cards are paid out of balances previously provided to the issuer. If a purchase exceeds the balance on the card, the issuer will honor the transaction only by mistake. The issuance of the card is simple, because it requires only the transmission of funds to the issuer.

Finally, it warrants noting that the legal frameworks for the cards are entirely different. Because they involve the extension of credit, credit cards are regulated in many important ways by the Truth in Lending Act and Regulation Z.²³ Because they access an asset account electronically, debit cards are governed by the Electronic Fund Transfers Act and Regulation E.²⁴ Because stored-value cards conventionally have been regarded as doing neither of those things, they are, with limited exceptions, governed by neither of those bodies of law, and thus remain relatively unregulated.

II. THE SOCIAL AND ECONOMIC ROLE OF STORED-VALUE CARDS

Any sensible opinion about the appropriate policymaking response to the rise of stored-value cards must start from an informed sense of the role stored-value cards play in our society and economy. In our view, that role has the potential to be strongly positive: the benefits of stored-value cards, as compared to the payment instruments that they replace, are so substantial that they justify policies that foster and support the spread of the product. We make three main points. First, by replacing paper-based instruments in market segments previously inaccessible to card-based payments, they lower the private and public costs of payment transactions. Second, by extending the use of card-based payment systems by low- and moderate-income households, they foster inclusion of those households in the financial mainstream of our society. Third, because they operate without an extension of credit, they help to limit the uniquely American routinization of credit transactions associated with the widespread use of credit-card borrowing.

A. *Replacing Paper-Based Payment Systems*

The most startling thing about the systems used for payments in this country is that, even as we pass through the second decade of the twenty-

²² See *id.* at 200–05.

²³ Truth in Lending Act of 1968, 15 U.S.C. §§ 1601–1667f (2012); Truth in Lending (Regulation Z), 12 C.F.R. § 1026 (2013).

²⁴ Electronic Fund Transfer Act, 15 U.S.C. §§ 1693–1693r (2012); 12 C.F.R. §1005 (2014).

first century, so many consumers continue to use paper-based systems for payment. To get a sense for the continuing usage of paper-based payment systems, it is instructive to review current data from the Boston Federal Reserve's Survey of Consumer Payment Choice. With respect to cash, it is no surprise that substantially all consumers (99.8% as of 2009) are users;²⁵ what is more surprising is the share of retail payment transactions in which cash is used (still 25.2% as of 2009).²⁶ Although many readers of this Essay may not be among them, the same survey shows that 85.4% of consumers were still using checks in 2009; although check use has fallen substantially, checks were still used for 5.8% of retail transactions in 2009.²⁷

This is not just an amusing factoid about the Luddite behaviors of the typical American consumer. On the contrary, the costs of continued use of currency and checks—as compared to electronic payments—are an embarrassment to an economy struggling to modernize and compete efficiently on the global stage.

1. *Setting a Baseline: The Costs of Electronic Payments*

The starting point of our analysis is that the costs of processing are a deadweight social loss, the paradigmatic “cost of doing business.” All other things being equal, the optimal payment system is the payment system that moves money from payor to payee at the lowest cost. From that perspective, electronic payments plainly dominate paper-based payments. For one thing, although it is difficult to get a firm understanding of the precise level of costs, it is plain that the cost of processing a card-based electronic payment is already far less than the cost of any of the major paper-based systems. The best current estimates suggest that the “all-in” processing costs are substantially less than a dime per payment.²⁸ Importantly, aside from those processing costs, the merchants that receive the payments have only insubstantial expenses: they need not pay employees to handle, protect, or deposit the “electronic” funds as they do the paper-based systems discussed below. Reflecting that intuition, the best evidence of comparative costs suggests that credit-free payment cards like stored-value cards are the cheapest of all payment systems.²⁹

²⁵ Kevin Foster et al., *The 2009 Survey of Consumer Payment Choice* 60, 103 (Fed. Reserve Bank of Bos., Public Policy Discussion Papers, 2011), <http://www.bostonfed.org/economic/ppdp/2011/ppdp1101.pdf> (also stating that the incidence of the use of paper-based payment instruments in 2009 was 96.2%).

²⁶ *Id.* at 68 (the data include uses for retail, service, and person-to-person payments).

²⁷ *Id.* at 68, 103. The study also states that 25.1% of consumers reported using money orders. The incidence of using cash in 2009 was 92.2%, and the incidence of using checks was 76.1%. In comparison, the incidence of using debit cards was only 67.6%, and the incidence of using credit cards was 60.8%. *Id.* at 60.

²⁸ KEITEL, *supra* note 19, at 21 (suggesting that as of 2010, an electronic funds transfer (EFT) costs less than a dime).

²⁹ See Daniel D. Garcia Swartz, Robert W. Hahn & Anne Layne-Farrar, *The Move Toward a Cashless Society: A Closer Look at Payment Instrument Economics*, 5 REV. NETWORK

But whatever the costs presently might be, we can be sure that they will fall substantially in the years to come, both because of the steadily continuing decline in the costs of processing electronic information and because of the increasing scale and presumable cost-effectiveness of the electronic systems dedicated to this particular enterprise.³⁰ We can see this easily if we look overseas, where this area of technology has developed much faster than in the United States. Most obviously, the last few years have seen a steady rise in the usage of so-called “virtual stored-value cards,” especially in Japan, where the product is commonly integrated directly into mobile-phone hardware.³¹ Those products allow consumers to purchase and recharge a virtual card issued to them over the internet. That “card” is a purely electronic artifact, accessed through a code provided upon deposit of the funds to the associated account.³²

The baseline, then, is a rapid and inexpensive system, with no obvious external effects on those that do not use the system, the costs of which predictably will fall as the years go by. The story for paper-based systems is quite different.

2. *The Costs of Cash*

It is easy to understand the widespread continuing use of cash as a consumer payment system. Because it requires no evaluation of credit—either by the merchant or by any third-party network—cash comes closer to universal acceptance than any other payment system. Also, cash delivers a conclusively final payment at the moment of the transaction, a highly attractive feature (at least for those who receive it). But lest a romanticized view of cash carry us away, we should remember why we collectively are using cash much less frequently than we used to, and why almost all merchants have come to accept non-cash payments.

ECON. 175, 195 (2006) (ranking the overall cost of different payment card transactions from high to low as, cash, then credit card, then check, then debit card). As we mentioned before, payment cards’ costs have probably decreased rapidly in the last seven years due to economies of scale. The important point, however, is that without the additional costs associated with credit, payment cards are the cheapest of the readily available payment systems.

³⁰ On the importance of economies of scale to the development of payment card systems, see Ronald J. Mann, *Credit Cards and Debit Cards in the United States and Japan*, 55 VAND. L. REV. 1055, 1071 (2002).

³¹ Jean J. Luyat, Comment, *A Tale of Regulation in the European Union and Japan: Does Characterizing the Business of Stored-Value Cards as a Financial Activity Impact Its Development?*, 18 PAC. RIM L. & POL’Y J. 525, 530–34 (2009). For a general discussion of the reasons Japanese payment technology has developed differently from that in the United States, see Mann, *supra* note 30, at 1059–60; Stephanie M. Wilshusen et al., *Consumers’ Use of Prepaid Cards: A Transaction-Based Analysis* 63 (Fed. Reserve Bank of Phila., Discussion Paper, 2012), <http://www.phil.frb.org/consumer-credit-and-payments/payment-cards-center/publications/discussion-papers/2012/D-2012-August-Prepaid.pdf> (estimating at 10% the portion of web general-purpose reloadable cards out of the entire general-purpose reloadable-card market in the United States).

³² Luyat, *supra* note 31, at 530–34.

The first point is the surprisingly substantial cost of creating and replacing currency, a task that falls here (as in most countries) to the central bank. In this country, as of 2012, the Federal Reserve was spending between 5 and 10 cents on each bill³³ and between 2 and 11 cents on each coin that it produces.³⁴ Because neither notes nor coins last forever,³⁵ the government incurs those costs ceaselessly, and their volume steadily increases: as the size of the economy grows more rapidly than the use of cash decreases, the total amount of cash in circulation continues to increase from year to year.³⁶ Moreover, this discussion says nothing of the plainly substantial costs that the Federal Reserve incurs collecting and disposing of worn-out currency and coins.³⁷

The second point is the costs to the merchants that accept cash. Merchants that accept cash necessarily spend time counting and processing the currency, costs that apparently approximate 12 cents per retail transaction.³⁸ Moreover, because it is so much easier to “redeploy” stolen cash than any other payment instrument, merchants (like consumers) obviously experience a major risk whenever they are in possession of substantial amounts of cash. It should be no surprise that those who cannot avoid that risk incur substantial expenses to protect them-

³³ BD. OF GOVERNORS OF THE FED. RESERVE SYS., 2012 NEW CURRENCY BUDGET (Dec. 2011), *available at* <http://www.federalreserve.gov/foia/files/2012newcurrency.pdf>.

³⁴ U.S. MINT, DEP'T OF THE TREASURY, 2012 BIENNIAL REPORT TO THE CONGRESS ON THE CURRENT STATUS OF COIN PRODUCTION COSTS AND ANALYSIS OF ALTERNATIVE CONTENT 4 (Dec. 2012), *available at* http://www.usmint.gov/about_the_mint/pdfs/united_states_mint_report_2012_biennial_report_to_the_congress_on_the_current_status_of_coin_production_costs_and_analysis_of_alternative_content_december_2012.pdf (excluding dollar coins and not including distribution cost to the public).

³⁵ FAQs, U.S. MINT (2014), http://www.usmint.gov/faqs/circulating_coins/#anchor1000 (stating that the lifespan of a coin is 25 years); *How Long Is the Lifespan of U.S. Paper Money?*, BD. OF GOVERNORS OF THE FED. RESERVE SYS. (July 10, 2014), <http://www.federalreserve.gov/faqs/how-long-is-the-life-span-of-us-paper-money.htm> (stating that the lifespan of a note varied between 3.7 years to 15 years, depending on the type and value of the note).

³⁶ Bruce Bartlett, *America's Most Profitable Export Is Cash*, N.Y. TIMES ECONOMIX BLOG (Apr. 9, 2013), <http://economix.blogs.nytimes.com/2013/04/09/americas-most-profitable-export-is-cash>. The costs of producing bills have particularly frustrated the Federal Reserve, which has tried repeatedly to shift consumers to larger-valued coins that would parallel the Euro or to larger bills (like the ill-fated two-dollar bill). See Matthew Healey, *A Push for Dollar Coins, Using Presidential Fervor*, N.Y. TIMES, Feb. 15, 2007, at C3; Collen Curry, *Coins Could Replace Dollar Bills, Save US \$5.6 Billion*, ABC NEWS (Oct. 25, 2011), <http://abcnews.go.com/blogs/business/2011/10/coins-could-replace-dollar-bills-save-us-5-6-billion>.

³⁷ See James Bohn, Diana Hancock & Paul Bauer, *Estimates of Scale and Cost Efficiency for Federal Reserve Currency Operations*, ECON. REV. 2001 Q.4, at 2, 24 n.41 (estimating the costs of destroying unfit currency at \$4.6 million a year). Because currency demand increases each year, those costs also continue to increase.

³⁸ David B. Humphrey, *Replacement of Cash by Cards in U.S. Consumer Payments*, 56 J. ECON. & BUS. 211, 212 (2004) (stating that the “all-in” handling cost of such a bill for a merchant is 12 cents).

selves.³⁹ It is also not surprising, then, that scholars analyzing the comparative cost of different payment instruments readily conclude that cash is the most expensive of all, with an all-in marginal cost per transaction of approximately one dollar.⁴⁰

The third point is the broader social cost of routinized cash use. All informed observers agree that cash is uniquely suited for the facilitation of widespread criminal enterprise; most importantly, cash is by far the easiest vehicle for laundering the profits of crime and thus insulating them from retributive public scrutiny.⁴¹ The link to criminal activity is not chimerical; statistical analysis readily demonstrates that the risk of crime is greater for societies that depend on cash payments than for those that depend on card-based payments.⁴² A shift to the routinized use of more-traceable payment instruments makes the large-scale use of cash ever more conspicuous. Thus, to the extent stored-value cards shift routine transactions away from cash, they undermine the ease of illicit use of cash.⁴³

3. *The Social Costs of Checks*

The cost-based advantage of stored-value cards over checks is even more pronounced. Consider first the use of checks and cards in retail transactions. If a stored-value card transaction is only slightly less cumbersome than a cash transaction (the swipe is faster than counting out coins and change), check transactions afflict the merchant with delay of an entirely different order. Existing studies suggest a time savings of more than thirty seconds per transaction (comparing cards to checks), and given recent advances in the speed of card processing, the current figure doubtlessly exceeds a minute per transaction.⁴⁴ This improves the

³⁹ BD. OF GOVERNORS OF THE FED. RESERVE SYS., 2012 NEW CURRENCY BUDGET 8 (Dec. 2011), available at <http://www.federalreserve.gov/foia/files/2012newcurrency.pdf> (stating that the budget for currency transportation in 2012 was \$22.8 million).

⁴⁰ See Garcia Swartz, *supra* note 29, at 193; *supra* note 29 and accompanying text.

⁴¹ RONALD J. MANN, CHARGING AHEAD: THE GROWTH AND REGULATION OF PAYMENT CARD MARKETS 10 (2006); Keith McCarthy, *UK Part I: Laundering the Proceeds of Crime—Methodology?*, in INTERNATIONAL GUIDE TO MONEY LAUNDERING LAW AND PRACTICE 1, 2 (Mark Simpson et al. eds., 3d ed. 2010).

⁴² See MANN, *supra* note 41, at 102–05.

⁴³ To be sure, stored-value cards were vulnerable to such uses when they were originally introduced, largely because of regulatory gaps in applicable “know-your-customer” rules. By all accounts, the vigorous regulatory responses to that possibility have substantially resolved that problem. See generally Bank Secrecy Act Regulation; Definitions and Other Regulations Relating to Money Services Businesses, 76 Fed. Reg. 43,585 (July 21, 2011) (codified at 31 C.F.R. pts. 1010, 1021–22).

⁴⁴ See Elizabeth Klee, *Paper or Plastic? The Effect of Time on Check and Debit Card Use at Grocery Stores* 25, 27 (Fed. Reserve Bd., Fin. & Econ. Discussion Series No. 2006-02, 2006), <http://www.federalreserve.gov/pubs/feds/2006/200602/200602pap.pdf>. Klee’s study examines an era in which signatures were still ubiquitous at checkouts, and one in which much retail processing occurred using modems over conventional phone lines. Thus, while the speed of check processing at the point of sale has improved slightly, if at all, the time to complete a card-based payment transaction has shortened

retail process by sharply lowering labor costs for the merchant, but also by decreasing the net cost to the consumer of the purchase transaction; existing studies (of which retailers are well aware) document the importance to consumers of speedy checkout transactions.⁴⁵

The sector in which cost savings for stored-value cards as compared to checks are most conspicuous is in the payment of salaries. For decades, employers have struggled to avoid the high costs of issuing paper salary checks to their employees. On a per-employee basis, the cost of issuing the check is in the range of one dollar *for each check*, and apparently is still increasing.⁴⁶ By contrast, the cost to an employer of loading funds on to a stored-value card is already less than a dime,⁴⁷ and for the reasons discussed above, seems likely to decline steadily in the years to come; this suggests a savings of more than 90% of the transaction costs of payment from a simple switch to paying employees by stored-value card instead of check.

The total cost savings from such programs are staggering, especially for large payers, like the federal government, which has estimated savings from switching some of its outstanding paper payments to stored-value cards at \$60 million *per year*.⁴⁸ Even a relatively small employer has much to gain by switching to stored-value cards from checks. For example, a 2009 industry report estimated the annual savings for an employer with only 1,000 employees (and thus presumably many fewer check-receiving employees)⁴⁹ at \$11,880.⁵⁰

markedly, so that card-based payments plainly have become the speediest method of retail payment.

⁴⁵ *Id.* at 27.

⁴⁶ KEITEL, *supra* note 19, at 21 (stating that in 2010 check issuance costs were estimated at \$1.03 per check). The costs of processing lost payroll checks are even more staggering, in the range of \$8 to \$10 per item. Motivano, *White Paper: Payroll Cards Facts & Statistics* 5 (2009), <http://www.motivano.com/datasheets/SmartCashFactsAndStats.pdf> (stating data from the American payroll association). The rate of error for stored-value cards is likely to be much lower, and there is no reason to think that the costs of reloading cards will be any higher than the costs of the original loading.

⁴⁷ KEITEL, *supra* note 19, at 21.

⁴⁸ *Id.* (stating that the Treasury Department estimates savings from switching some of its outstanding paper payments to stored-value cards at \$300 million in five years). Similar data exists in other countries. For instance, the Canadian Task Force for the Payments System Review estimated that the social cost saving from Canada “going digital” will be \$7.7 billion for a year. See TASK FORCE FOR THE PAYMENTS SYSTEM REVIEW, GOING DIGITAL: TRANSITIONING TO DIGITAL PAYMENTS 17, *available at* http://paymentsystemreview.ca/wp-content/themes/psr-esp-hub/documents/r03_eng.pdf.

⁴⁹ Because the cheapest method of payment typically is for employers to pay their employees by an Automated Clearing House (ACH) transfer to the employees’ bank accounts, the switch from checks to stored-value cards generally applies only to the subgroup of employees who will not accept ACH transfers—generally speaking those without a demand-deposit account. The surprising number of those employees reflects the continuing difficulty in penetrating LMI households with mainstream financial services, a dominant theme of the following Section of this Essay. See Jesse

The most staggering costs of checks traditionally have come from the costs of processing them once they are written. Because traditional check processing involves the transportation of the paper item from the bank of first deposit to the bank on which the check is drawn,⁵¹ the process for years consumed a disproportionate share of social resources, much of it coming from the operations of the Federal Reserve banks (at least indirectly subsidized by federal tax dollars). Thus, as recently as a decade ago, the cost of processing checks, perhaps three dollars *per check*, amounted to about 0.5% of the entire gross domestic product of the country.⁵² To be fair, those processing costs surely have fallen markedly with the rise of Check 21,⁵³ which has substantially limited the amount of paper-based processing.⁵⁴

Those processing improvements, albeit important to the system, do nothing to remove the costs of issuing, delivering, and receiving the paper instrument, discussed above. It is the promise of saving those costs, ineradicably inherent in the initial use of a paper check, that so advantages stored-value cards as a consumer payment system.

B. Fostering Inclusion in the Financial Mainstream

Because the cost savings from the shift to stored-value cards for the most part accrue to the private businesses and individuals that use and accept those instruments, there is every reason to think that (absent legal and institutional obstacles) market forces would drive rapid adoption of the product without any affirmative governmental intervention. The point of this Section is to underscore a second benefit of the rise of stored-value cards: their potential to remedy our nation's persistent inability to extend the financial mainstream below the middle class. Because the broadening of the financial mainstream has social and societal benefits that accrue to the entire polity, the potential for stored-value cards to

Bricker et al., *Changes in U.S. Family Finances from 2007 to 2010: Evidence from the Survey of Consumer Finances*, FED. RES. BULL., June 2012, at 1, 32, available at <http://www.federalreserve.gov/Pubs/Bulletin/2012/PDF/scf12.pdf> (stating that 9.6% of United States households did not have a checking account in 2010).

⁵⁰ See Motivano, *supra* note 46, at 6.

⁵¹ MANN, *supra* note 16, at 95–96.

⁵² MANN, *supra* note 41, at 11.

⁵³ Check Clearing for the 21st Century Act (Check 21), 12 U.S.C. §§ 5001–5018 (2012); see also MANN, *supra* note 16, at 141–43.

⁵⁴ FED. RESERVE SYS., THE 2010 FEDERAL RESERVE PAYMENTS STUDY: NONCASH PAYMENT TRENDS IN THE UNITED STATES: 2006–2009, at 8 (Apr. 5, 2011), available at http://www.frb-services.org/files/communications/pdf/press/2010_payments_study.pdf (indicating that 97% of interbank checks were cleared electronically in 2009). Since 2003 the Federal Reserve Board has systematically closed check processing centers. See Press Release, Bd. of Governors of the Fed. Reserve Sys., Federal Reserve Banks Complete Check Processing Infrastructure Changes (Mar. 2, 2010), available at <http://www.federalreserve.gov/newsevents/press/other/20100302a.htm>.

bring those benefits would justify proactive steps to foster their use even apart from the cost savings discussed in the preceding Section.

Our discussion proceeds in three steps. First, we offer a brief summary of the nature and reasons for the limited penetration of mainstream financial products in low- and moderate-income households. Second, we discuss the social consequences of that problem—the commonplace transactions and interactions from which those households consequently are excluded. Finally, building on the discussion above, we explain why stored-value cards are so much more likely to erode this problem than existing mainstream payment systems.

1. *Understanding the Underbanked*

One of the most remarkable attributes of the American financial system in the twenty-first century is its persistent inability to deploy mainstream products to LMI households. Despite such forceful interventions as the Community Reinvestment Act⁵⁵ and intense attention by federal regulators to the placement of bank branches in under-served neighborhoods, the fact remains that the financial products used by middle- and upper-class Americans—demand-deposit accounts, credit cards, and debit cards—remain out of the reach of a large share of LMI households.

For example, data from the Federal Deposit Insurance Cooperation (FDIC) suggest that 1 in every 12 households still has no bank account.⁵⁶ For the most part, those households use a set of financial products—money orders, check-cashing services, and the like—completely separate from the products used by less impecunious households. For example, the FDIC reports that 38% of those without bank accounts used check cashers in 2011, and 25% used them within the last 30 days before the survey.⁵⁷ Use of money orders is similarly concentrated among LMI households.⁵⁸ Suffice it to say that the overwhelming majority of the readers of this Essay use those products rarely, if ever.⁵⁹

⁵⁵ Community Reinvestment Act of 1977, 12 U.S.C. §§ 2901–2908 (2012), *see* John Taylor, *CRA Modernization: A Critical Moment for Underserved Neighborhoods*, SHELTERFORCE, Fall/Winter 2009, *available at* http://shelterforce.org/article/cra_modernization_a_critical_moment_for_underserved_neighborhoods; John Taylor & Josh Silver, *The Community Reinvestment Act at 30: Looking Back and Looking to the Future*, 53 N.Y.L. SCH. L. REV. 203 (2008/09).

⁵⁶ SUSAN BURHOUSE & YAZMIN OSAKI, 2011 FDIC NATIONAL SURVEY OF UNBANKED AND UNDERBANKED HOUSEHOLDS 4 (Sept. 2012), *available at* https://www.fdic.gov/householdsurvey/2012_unbankedreport.pdf.

⁵⁷ *Id.* at 32.

⁵⁸ *Id.* (stating that 49.1% of unbanked consumers used money orders in 2011, and that 32.1% have done so in the last 30 days).

⁵⁹ Both of us regularly teach a course in payment systems; we have not during this century had a student who would admit to using a money order or check casher.

Penetration of credit cards into LMI households is much more substantial.⁶⁰ It seems plain from the limited transactional use of debit cards by LMI households, however, that this reflects the credit needs of these households more than it does the extension of a conventional middle-class product. As one of us has explained elsewhere, the use of credit cards by underbanked households is quite different from the use of credit cards by more affluent households. The cards are much more likely to involve long-term revolving credit that is much less likely ever to be repaid than the cards used by more affluent households. The last ones are likely to depend more on substantial annual fees and high charges for revolving account balances that periodically are paid off.⁶¹

The complex reasons for the limited penetration of mainstream financial products are largely beyond the scope of this Essay. Still, they warrant a brief discussion if only because their intractability underscores the social value of a product that can bypass them. The most obvious problem, apparent from Caskey's path-breaking work on the subject, is that the business models of mainstream financial products drive cost structures that make the products unattractive to LMI households: a dominant reason that the poor do not have bank accounts is that the costs of having bank accounts exceed the benefits to those households of maintaining them.⁶² The costs of alternative financial services—check cashers, pawnshops, car-title lenders, payday lenders, and the like—seem outlandish to the middle-class and elites, but only because mainstream financial products have cost structures designed to make those products attractive to them, not to the poor.⁶³

Again, data from the FDIC underscore the continuing relevance of these basic product-design issues. For example, the most popular justification for not having a checking account is the perception of the underbanked that they do not have enough money.⁶⁴ The same data indicate a preference for alternative, paper-based payment services based on

⁶⁰ Ronald J. Mann, *Patterns of Credit Card Use Among Low- and Moderate-Income Households*, in INSUFFICIENT FUNDS 257 (Rebecca M. Blank & Michael S. Barr eds., 2009).

⁶¹ Ronald J. Mann, *Bankruptcy Reform and the "Sweat Box" of Credit Card Debt*, 2007 U. ILL. L. REV. 375, 385–86; Mann, *supra* note 60, at 262. On the prohibitions of fee-harvesting with regard to credit-card use, see the Credit Card Accountability Responsibility and Disclosure Act of 2009 (CARD Act), § 105, 15 U.S.C. § 1637(d) (2012).

⁶² JOHN P. CASKEY, FRINGE BANKING: CHECK-CASHING OUTLETS, PAWNSHOPS, AND THE POOR 84–106 (1994); Ronald J. Mann, *After the Great Recession: Regulating Financial Services for Low- and Middle-Income Communities*, 69 WASH. & LEE L. REV. 729, 740–43 (2012).

⁶³ See Mann, *supra* note 62, at 741–42.

⁶⁴ BURHOUSE & OSAKI, *supra* note 56, at 27. This was the most popular answer among unbanked consumers (given by 32% to 33% of unbanked consumers) for not having a bank account.

convenience, speed, and fees.⁶⁵ Given the general importance of convenience and efficiency to consumer selection of payment services,⁶⁶ the relative failure of insured depository institutions to respond on those attributes—as compared to the marketing and service efforts of alternative financial-services providers—certainly must be regarded as a major cause of the disjunction.

It is plain, however, that costs and related product attributes are not the only source of the problem. Much of the abyss between the financial practices of LMI households and the mainstream rests on social and psychological factors—an aversion to banks rooted in something ranging from the discomfort of social distance to an affirmative distaste founded on explicit bad experiences. Thus, for example, a major justification for not having a bank account—offered by 26% of respondents without a bank account—is simply that they do not need or want one.⁶⁷ Another group (7.1%) offered the stronger perspective that they did not like dealing with banks or did not trust them.⁶⁸ Similar responses to the “cold” and “impersonal” nature of banks commonly justify preferences for alternative financial services.⁶⁹

2. *The Plight of the Underbanked*

The exclusion of the underbanked from the financial mainstream has important consequences for all sectors of society. This is not simply a function of the greater cost of the products that they use, though that certainly contributes to the increasingly high levels of income inequality in the United States.⁷⁰

⁶⁵ *Id.* at 38. For instance 51.8% of underbanked and 28.7% of unbanked stated that they used non-bank check cashing services because those were located in a more convenient place for them. 18.4% of underbanked and 11.3% of unbanked stated that they used the same service since it was a faster way to get money. And 3.4% of underbanked and 6.6% of unbanked mentioned that banks charge more to cash checks. See also CASKEY, *supra* note 62, at 75–76.

⁶⁶ SARAH GORDON, JENNIFER ROMICH & ERIC WAITHAKA, A TOOL FOR GETTING BY OR GETTING AHEAD?: CONSUMERS' VIEWS ON PREPAID CARDS 5–6 (2009), available at http://www.cfsinnovation.com/sites/default/files/imported/managed_documents/voc-prepaidfinal.pdf. See also Elizabeth K. Kiser, *Household Switching Behavior at Depository Institutions: Evidence from Survey Data 1* (Fed. Reserve Bd., Fin. & Econ. Discussion Series No. 2002-44, 2002), <http://www.federalreserve.gov/pubs/feds/2002/200244/200244pap.pdf> (listing household relocation, customer service, and price factors as most common reasons for changing banks).

⁶⁷ BURHOUSE & OSAKI, *supra* note 56, at 27.

⁶⁸ *Id.* (stating that 7.1% of consumers who never had a bank account mentioned that the reason was their distrust in banks and/or they disliked dealing with banks).

⁶⁹ CASKEY, *supra* note 62, at 74, 76 (stating that consumers feel more comfortable with non-bank check cashing outlets than with banks, and that 24% of those outlets' consumers stated that “[b]anks are too cold and impersonal with people like me” (internal quotation marks omitted)).

⁷⁰ Michael O'Higgins et al., *Income Distribution and Redistribution: A Microdata Analysis for Seven Countries*, in POVERTY, INEQUALITY AND INCOME DISTRIBUTION IN COMPARATIVE PERSPECTIVE 20, 33 (Timothy M. Smeeding et al. eds., 1990) (ranking the United States as one of the three countries with the highest degree of income

The problem is that the products used by the underbanked not only cost more than the products mainstream households use, they have a much more limited functionality. There are many transactions in our society that are simply unavailable to those without a mainstream branded payment card. It is all but impossible to rent a car. It is difficult, though certainly not impossible, to reserve a hotel room.⁷¹

More seriously, although it is not impossible, it is expensive and impractical to purchase from the internet-based merchants that middle- and upper-class households prefer without a branded payment card or a checking account.⁷² Exclusion from those merchants becomes ever more significant as their share of retail transactions grows so markedly from year to year.⁷³ Lest those types of transactions seem like luxuries that LMI households better might forgo, we should remember the primary reasons middle- and upper-class households use those retailers: a considered judgment that the service they provide is so markedly superior to available retail options.⁷⁴ There is no more reason LMI households should have to pay more for these products than they should have to pay more for financial services. It is also certainly distressing as a policy matter that the rise of internet commerce should spread the problems caused by financial-market segmentation into new sectors of retail commerce.⁷⁵

Taking the concern to its logical conclusion, we all benefit from a community of social cohesion, and we all suffer from a financially segmented community in which the products, goods, and services that define success and “making it” in our culture are beyond the reach of an

inequality); Liran Haim, *Rethinking Consumer Protection Policy in Financial Markets*, 32 J.L. & COM. 23, 46–48 (2013); see also Koen Caminada, Kess Goudswaard & Chen Wang, *Disentangling Income Inequality and the Redistributive Effect of Taxes and Transfers in 20 LIS Countries over Time*, at 12 (Lux. Income Study, Working Paper No. 581, 2012), available at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2168885 (stating that those results remain constant over time).

⁷¹ Ivan Daniel, *5 Things You Can't Quite Do Without a Credit Card*, GET.COM (Aug. 21, 2014), <https://get.com/blog/5-things-you-cant-do-without-a-credit-card>. See also Mary Pilon, *Life Without Credit Cards*, WALL ST. J. BLOG (June 18, 2009), <http://blogs.wsj.com/wallet/2009/06/18/life-without-credit-cards>.

⁷² See RONALD J. MANN, *ELECTRONIC COMMERCE* 707 (4th ed. 2011) (stating the main payment instruments used for distance selling are credit cards, debit cards, and ACH).

⁷³ U.S. *E-Commerce Sales, 2013–2017*, INTERNET RETAILER, <http://www.internetretailer.com/trends/sales/us-e-commerce-sales-2013-2017> (stating that online retail sales in the United States will grow in a compound annual rate of 9.5% from 2013 to 2018, and that by 2018 the web will account for 11% of United States retail sales).

⁷⁴ See CHRIS ANDERSON, *THE LONG TAIL: WHY THE FUTURE OF BUSINESS IS SELLING LESS OF MORE* 168–91 (2008).

⁷⁵ DAVID CAPLOVITZ, *THE POOR PAY MORE: CONSUMER PRACTICES OF LOW-INCOME FAMILIES* 12–31 (1967) (discussing adaptation to low-income consumers by durable-goods merchants). The real answer is that the Internet *could* mitigate the geographic segmentation that is such a large part of the reason that the poor pay more, but only if the poor could get the financial instruments to get to the internet.

identifiable and substantial part of the populace. A financial product that can make inroads on that problem provides value to us all.

3. Using Cards to Mainstream the Underbanked

The natural question, then, is why stored-value cards provide the “magic bullet” that can solve a problem that has festered, intractably, for much of the post-war era. The basic answer lies in the cost advantages discussed above: the steadily decreasing costs of electronic processing of information have lowered the costs of deploying payment cards that monitor balances in real time on a transaction-by-transaction basis. Therefore, it is now practical, at a fraction the costs of processing traditional paper-based payments, to deploy those products with little or no consideration of the individual creditworthiness of the end users. To put the point another way, the central cost advantage of stored-value cards is that they involve no extension of credit and thus avoid any costs to an issuer for collecting information about the creditworthiness or financial responsibility of the cardholder.⁷⁶

To be sure, the information-processing problem is one that would have been daunting only a decade ago. For example, the large payroll-card issuer must allocate every two weeks to each account the correct amount of salary disbursed to that employee. Then, when the employee uses the card, the issuer must identify the correct card account, check the balance, and account for the transaction, all in the fraction of a second typical for modern branded-card processing in this country. This is not at all unusual for the major card networks and acquirers in this country, but it is something that could not successfully have been done without the advances in information processing of the last few decades.

With those advances, however, we have the promise of a product that is ideally suited for deployment among the underbanked. Because the product often (especially in the payroll context) carries one of the major payment-card brands (Visa or MasterCard), the product is likely to be accepted at substantially all mainstream merchant outlets at which the users are likely to spend money. Because the product on its face is indistinguishable from the credit and debit cards middle- and upper-income households have preferred for decades, the product avoids the social stigma (and inconvenience) associated with food stamps and similar previous techniques for deploying financial assistance to LMI households.

⁷⁶ To be sure, as discussed above, the issuer does need to comply with know-your-customer rules designed to limit money laundering, but that is a simple question of verifying identity, which even for most LMI households is a much simpler (and cheaper) problem than collecting credit information: many poor households will often have very limited credit information, which makes it quite difficult to assess them under conventional “credit scoring” systems. However, they are still likely to have a driver’s license or other identity documentation indisputably adequate to support receipt of a stored-value card. That is particularly true in the employment context, where immigration rules will almost compel employers, at least those who pay a periodic salary, to have such documentation.

The fact is, the product works precisely the same as the mainstream debit card and has for all practical purposes the same cost structure to LMI households as the debit card has for mainstream households.⁷⁷

The most obvious reason to doubt the viability of the stored-value card based on that conceptual discussion is the “network” problem of payment networks: given the need for multi-party payment products to be simultaneously deployed by issuers and accepted by merchants, it traditionally has been quite difficult for new products to break into the market.⁷⁸

The stored-value card has avoided that problem for two distinct reasons. First, because the major products bear the Visa and MasterCard marks, and have been deployed through their networks, they feed into the existing dominant market structure of merchant outlets. The honor-all-cards rules of Visa and MasterCard effectively require merchants to take the new product simply because it bears the Visa and MasterCard marks.⁷⁹ Second, the widespread deployment of payroll cards by large employers and, most importantly, the federal government over the last decade has jumpstarted a market so abruptly that there is no longer a basis for doubting whether the product will succeed, only uncertainty as to how large it will grow. For instance, over 1.5 million LMI consumers already receive their monthly social-security payments by electronic transfers (assuming they have a bank account) or by stored-value cards.⁸⁰ Another 45 million consumers eligible for tax refunds can also now choose to get their payments in the same way.⁸¹

Perhaps the biggest problem with consumer adoption of stored-value cards is the perception that they have “negative float”—the value must be placed on the card at one point in time, and reside there until it can be used. This differs, at least in perception, from payment devices like cash and checks, where the consumer retains the funds until the consumer wishes to spend them. In truth, however, there is little practical difference as long as the consumer regards the funds on the card as still “in hand.” In practical effect, in a world in which demand-deposit accounts bear negative implicit interest rates, the “cost” of “putting (or holding) funds on a card” is unlikely to be any more than “holding” them in a bank account. So the difference between leaving funds in a bank account—sent there by an ACH transfer—and leaving funds on a general-

⁷⁷ There is the potential for adversely differential fee structures. We discuss proper responses to that problem in the policy discussion below. *See infra* Part III.(D).

⁷⁸ DAVID S. EVANS & RICHARD SCHMALENSEE, *PAYING WITH PLASTIC: THE DIGITAL REVOLUTION IN BUYING AND BORROWING* 159–212 (2d ed. 2005).

⁷⁹ Mann, *supra* note 15, at 655.

⁸⁰ KEITEL, *supra* note 19, at 21. *See also* Management of Federal Agency Disbursements, 75 Fed. Reg. 80,315 (Dec. 22, 2010) (codified at 31 C.F.R. pt. 208).

⁸¹ KEITEL, *supra* note 19, at 21, *see* Press Release, U.S. Dep’t of the Treasury, Treasury Launches Pilot Program of Prepaid Debit and Payroll Cards for Fast, Safe and Convenient Tax Refunds (Jan. 13, 2011), *available at* <http://www.treasury.gov/press-center/press-releases/pages/tg1021.aspx>.

purpose stored-value payroll card—sent there by an electronic fund transfer from the employer—seems so academic that it is unlikely to affect consumer use or perceptions.

C. *Routines of Credit and Debit*

The third and final benefit of stored-value cards draws directly on the credit-free nature of the product discussed in the preceding Section. Because routine use of stored-value cards, especially for households that have not previously used a mainstream payment card, will not involve the use of credit, deployment of those cards will limit the routine use of credit cards as the payment card of choice.

One of us has written extensively on the adverse social costs of the unusually high levels of routine credit-card use in this country.⁸² Essentially, the argument is that credit cards are associated with financial distress⁸³: analysis of time-series data at the national level suggests a substantial and statistically significant relation between the level of credit-card use in a country, on the one hand, and the rate of bankruptcy filings, on the other.⁸⁴ The reasons for that effect are difficult to discern. They doubtlessly relate in part to the ease of payment, which associates credit-card use with an increased rate of unreflective spending.⁸⁵ The effect also certainly relates to the ease of borrowing, attributable at least in part to the complex and confusing design of the product.⁸⁶

Whatever the underlying reason might be, that work argues that the countries that have avoided this problem successfully (such as Japan) have done so for the most part by developing card-based payment systems in which the extension of credit is not common.⁸⁷ It goes on to argue that the most salient public-policy response in this country would be to foster the routine use of payment cards that do not involve extensions of credit.⁸⁸

Against the backdrop of that work, the possibility that LMI households might enter the financial mainstream with stored-value cards seems like a godsend, too good to be true.⁸⁹ The set of households most at risk of financial distress, which traditionally have been the least well served by mainstream financial providers, could move directly into the financial

⁸² MANN, *supra* note 41, at 51–72; Mann, *supra* note 61, at 384–87.

⁸³ MANN, *supra* note 41, at 49–51.

⁸⁴ *Id.* at 60–72.

⁸⁵ *Id.* at 46–47; see Mann, *supra* note 61, at 403.

⁸⁶ See Mann, *supra* note 15, at 655–58 (stating that consumers will find it difficult to tell the difference between their debit card and their credit card due to product design).

⁸⁷ See Mann, *supra* note 30.

⁸⁸ See Mann, *supra* note 61, at 403; Mann, *supra* note 60, at 263 (stating that LMI households mainly use credit cards to receive revolving credit).

⁸⁹ See Mann, *supra* note 60, at 280 (summarizing high credit-card debt among LMI households).

mainstream with a product that avoids the risks of prolonged borrowing—risks that have afflicted so many of the relatively invulnerable households using the mainstream products in recent decades. On the scale of social benefits, this must count as a major benefit in favor of the deployment of the stored-value card.

III. SOCIAL RISK ASSOCIATED WITH STORED-VALUE CARDS

The analysis to this point unequivocally supports the development of public and private institutions to foster consumer use of stored-value cards. It does, however, ignore several obvious ways in which those cards expose consumers to risks greater than those associated with the more conventional credit and debit cards commonly used by middle- and upper-class consumers. This Part of the Essay considers the four most important risks—issuer insolvency, fraudulent transactions, escheat of unused funds and fees—and summarizes policies that can readily mitigate those risks.

At the outset, we emphasize our awareness of the risk that regulation specifying the content of the product can hinder market development by legislating a particular mix of product attributes that might not be optimal for all consumers. We discuss in the sections below regulatory options that respond to that problem, designed to blunt the likelihood that the policies we recommend might prevent consumers from obtaining the products that they actively seek.

A. *Issuer Insolvency*

The most salient risk unique to stored-value cards arises directly from the defining feature of the cards: the cardholder dedicates funds to the card *in advance* of the purchase transaction. By providing those funds in advance, the cardholder directly exposes himself or herself to the risk that the issuer will lose those funds so that they will be unavailable when the cardholder attempts to redeem them through use of the card. That could happen either through a failure to maintain the funds separately or through a general insolvency that would leave the issuer without funds sufficient to match the balances remaining on previously issued cards.

To be sure, debit cards expose the cardholder to a similar risk: that the issuer of the debit card may become insolvent, thus losing the funds previously deposited by the cardholder in the account that backs the card. In that case, however, because the issuer of the debit card is (for all practical purposes) always a depository institution, the risk of loss to the cardholder is minimized by federal deposit insurance. In the case of a stored-value card, the availability of federal insurance is much less certain. In the first place, there is nothing inherent in the stored-value card that requires it to be issued by a financial institution. Indeed, in the case of closed-loop cards, it is fair to assume that the great majority of cards are *not* issued by financial institutions. Moreover, even when the issuer of

the card is a financial institution, the availability of federal deposit insurance requires complex actions on the part of the issuer,⁹⁰ actions that are not required by any body of existing law. Thus, as the law stands now, there is no affirmative requirement that the issuer take any steps to ensure the availability of the funds deposited onto the card by the cardholder.⁹¹

Given the likelihood that consumers are not fully aware of these risks, the obvious response is to require the issuers of the cards to take the steps necessary to protect the cardholders. In the case of financial institutions, that is simple enough because of their ready ability to segregate the funds in accounts protected for the cardholders by deposit insurance.⁹² To be sure, there is no reason that stored-value cards must be issued by financial institutions, and it would be unfortunate if regulation unnecessarily tilted the field to prevent nonfinancial institutions from competing against banks. That is particularly important with respect to products that are of particular importance for LMI households, given the relative inability of banks to effectively reach those households.⁹³

A simple two-step response should be adequate to resolve that problem. Most obviously, at the first step, institutions that wish to issue stored-value cards can be obligated to place the funds received from their cardholders in accounts that qualify for customer-level deposit-insurance protection under the existing FDIC program. To be sure, that does not deal with the possibility that the non-depository issuing institutions might fail to maintain the appropriate balances in those accounts. On that point, however, the provisions of the Dodd-Frank Act that grant the CFPB regulatory authority over nonfinancial institutions that provide important consumer financial services⁹⁴ should allow the CFPB to monitor compli-

⁹⁰ Insurability of Funds Underlying Stored Value Cards and Other Nontraditional Access Mechanisms (General Counsel's Opinion No. 8), 73 Fed. Reg. 67,155 (Nov. 13, 2008). Generally speaking, that opinion establishes three steps an issuer must take for FDIC deposit insurance to extend to an account that holds funds deposited on stored-value cards: (1) the funds must be placed in an account under the cardholder's name or in an account that discloses the existence of the agency or custodial relationship; (2) the records of the insured depository institution or the issuer must disclose the identities of and amounts deposited by the cardholders; and (3) the cardholders (rather than the issuer) must be the owners of the card-associated account. *Id.* at 67,156.

⁹¹ For a conspicuous counterexample, see 31 C.F.R. § 210.5(b)(5)(i)(B) (2013) (requiring pass-through deposit insurance for a card to be eligible to receive federal payments).

⁹² According to General Counsel's Opinion No. 8, the easiest way for financial institutions to set up such an account would be to create it in the cardholder's name. General Counsel's Opinion No. 8, *supra* note 90.

⁹³ See Ronald J. Mann, *A Requiem for Sam's Bank*, 83 CHI.-KENT L. REV. 953, 967-72 (2008); Mann, *supra* note 62, at 743-44.

⁹⁴ Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, §§ 1001-1100H, 124 Stat. 1376, 1955-2113 (codified as amended in scattered sections of 12 U.S.C. and 15 U.S.C.). The regulatory authority directed

ance with that obligation and any other related issues of financial stability that might undermine the reliability of that protection.⁹⁵

At the second step, regulators might wish to consider the possibility of permitting the issuance of a card for which the stored values are not deposit protected. At first glance, the casual reader might wonder why *any* consumer would affirmatively select a card that did not include protection of funds on the card. The answer depends on context. In the context of particularly localized closed-loop programs, like those operated on university or corporate campuses, it might well be that the costs of establishing the accounts discussed above would dwarf the benefits of the program.⁹⁶ That suggests the propriety of a regulatory exception for those cards, which might be premised on (1) a limitation on the maximum amount to be stored on the card at any one time (presumably something less than \$250) together with a limitation on the program volume (to keep the exception limited for small, localized programs only); and (2) an emphatic branding requirement related to the lack of insurance. What we have in mind on the latter point is something like the phrase UNPROTECTED CARD in two lines of bold-face all-capital type about one inch high on the face of the card.

B. Unauthorized Use

The second risk uniquely associated with stored-value cards is the risk that the funds will be lost through unauthorized use. For credit cards and debit cards, federal law for decades has provided regulatory protection (under the TILA/Z and EFTA/E regimes, respectively) against unauthorized use.⁹⁷ However, as discussed above, neither of those regimes

specifically at nonbank financial-service providers appears in section 1024 of Dodd-Frank, codified at 12 U.S.C. § 5514 (2012).

⁹⁵ One such issue might include clarification that closed-loop issuers that deposit their cardholder funds in accordance with General Counsel's Opinion No. 8 would entitle their customers to pass-through deposit insurance in case of issuer insolvency. General Counsel's Opinion, *supra* note 90.

⁹⁶ That is particularly true where the cards are "unhosted," so that the only record of value resides on the card (the common mechanism for magnetic-stripe subway cards until recently). For those cards, given the absence of a record in the issuer's possession of the funds on the card at any given time, the insurance program would not be practical. To put it another way, such an exception would be necessary if the regulatory system is to tolerate the continued issuance of unhosted cards. See MANN, *supra* note 16, at 337–39 (discussing the mechanism of unhosted stored-value cards).

⁹⁷ TILA/Z refers to Regulation Z of the Truth in Lending Act, 12 C.F.R. pt. 1026 (2013); EFTA/E refers to Regulation E the Electronic Fund Transfers Act, 77 Fed. Reg. 30,923 (proposed May 24, 2012) (to be codified at 12 C.F.R. pt. 1005). That is not to say those protections are perfect. For suggestions of ways those regimes could be rationalized, see Mann, *supra* note 15, at 652–73.

applies for stored-value cards.⁹⁸ Accordingly, except for protections voluntarily provided by issuers, cardholders are exposed to the risk that if their cards are lost or stolen, third parties will dissipate the funds on the cards. A strong case could be made that cardholders bearing some of the risk of loss is appropriate to ensure that they are not negligent in protecting their cards.⁹⁹ Nevertheless, for all other card-based payment systems, our society has adopted a regime that reflects the sensible intuition that technological innovations by the issuers are the best way to limit such losses.¹⁰⁰ Even if that conclusion is debatable, it seems particularly perverse to single out for limited protection the card that is most likely to be used by LMI households, while requiring those protections for the credit and debit cards commonly used by middle- and upper-class households.

To be sure, Visa and MasterCard¹⁰¹ already provide protection against unauthorized transactions for their cards that in many cases¹⁰² is superior to that required by the TILA/Z and EFTA/E regimes. Although that suggests a market pressure towards a protective solution on this particular attribute, it does not in any way undermine the need for regulatory intervention. Most other issuers, in particular (so far as we know) most of the closed-loop issuers, provide no such protection; a loss of those cards is, for all intents and purposes, a loss of the funds.¹⁰³

A regulatory intervention would underscore the difference between the cards that provide those protections and those that do not.¹⁰⁴ The natural ensuing question is whether there is a basis here for a regulatory exception, parallel to the one discussed above for uninsured cards. We are inclined to think such an exception should exist for the small-volume programs discussed above, but it should be strictly limited to marked,

⁹⁸ Some specific types of open-loop stored-value cards have been included over the recent years under Regulation E protection. 12 C.F.R. §§ 205.2(b)(2) (discussing payroll cards), 205.15 (discussing EBT cards).

⁹⁹ Mann, *supra* note 15, at 638.

¹⁰⁰ *Id.*

¹⁰¹ American Express and Discover do have similar regimes, but given their relatively limited importance in the stored-value card market we refer here for convenience only to the Visa and MasterCard programs.

¹⁰² The Visa and MasterCard regimes are much more absolute in their protections, setting “zero-dollar” limits, where the TILA/Z and EFTA/E regimes have small-dollar “coinsurance” provisions. For the zero liability rule see: <http://usa.visa.com/personal/security/zero-liability.jsp> <http://www.mastercard.us/zero-liability.html>. For a discussion on the TILA/Z and EFTA/E rules see MANN, *supra* note 16, at 151–53, 209–10.

¹⁰³ For instance, the Starbucks stored-value card provides unauthorized use protection subject to online registration of the card. That protection, though, applies only to funds that were associated with the card at the time Starbucks was notified of its loss. See *Starbucks Card Terms & Conditions*, STARBUCKS (2014), <http://www.starbucks.com/card/card-terms-and-conditions>.

¹⁰⁴ The CFPB’s pending notice of proposed regulation suggests a likelihood that the CFPB is considering a regulation along these lines. See Regulation E, 77 Fed. Reg. 30,923 (proposed May 24, 2012) (to be codified at 12 C.F.R. pt. 1005).

unhosted cards (where it is not practical to provide the protection), and the maximum dollar amount that can be loaded on the unprotected cards should be strictly limited to something in the vicinity of \$250.

C. *Loss of Unused Funds*

The last salient risk uniquely associated with stored-value cards is the risk that the funds, if unspent, will be appropriated either to the issuer or the State through dormancy fees and escheat rules. This problem is uniquely associated with stored-value cards because they are the only cards where funds are associated directly with the card. Moreover, because the cards can be issued with only a limited relation between the issuer and the cardholder—a benefit in extending the market reach of the cards—it is particularly likely that the issuer will lose touch with the cardholder. Accordingly, and especially in the early days of stored-value cards, it has been common for value initially loaded on the cards to be appropriated by the issuer (through dormancy fees) or transferred to the State through escheat rules.¹⁰⁵

Some simple regulatory approaches here are apparent. First, the dormancy fees are a classic example of the kind of “shrouded” back-end fees that are a classic problem in card markets.¹⁰⁶ It would seem appropriate, then, to ban those fees in the first instance. The CARD Act¹⁰⁷ already has banned those fees, but only for gift cards.¹⁰⁸ That ban should be extended to cover all stored-value cards.¹⁰⁹ Although reasonable minds might differ, we see no reason to except the small, unhosted programs discussed above from that requirement; because the premise of the intervention is that consumers are unlikely to rationally price a probability this remote, it seems simpler to ban the dormancy fees and let issuers use upfront pricing (which is apparent to their customers) to make any necessary adjustments to their fee structures.

The second response is to mandate a practical mechanism for consumers to access the last remaining value on the card. One of the most likely reasons for residual unspent value will be the difficulty of spending precisely the amount loaded onto a card. This is seen most easily with a

¹⁰⁵ See Keitel, *supra* note 18, at 9 (stating that in the United States approximately 20 states require that unclaimed funds which are accessible by closed-loop stored-value cards be reported and reverted to the state under abandoned-property laws).

¹⁰⁶ See MANN, *supra* note 41, at 136–37; Haim, *supra* note 70, at 32; Ronald J. Mann, “Contracting” for Credit, 104 MICH. L. REV. 899, 912–13 (2006). See generally Xavier Gabaix & David Laibson, *Shrouded Attributes, Consumer Myopia, and Information Suppression in Competitive Markets*, 121 Q.J. ECON. 505 (2006) (detailed economic analysis of “shrouded” product attributes).

¹⁰⁷ § 105, 15 U.S.C. § 1637(d) (2012).

¹⁰⁸ Regulation E, 12 C.F.R. § 1005.20(a)(3)(i)–(ii) (2013).

¹⁰⁹ The CFPB’s authority to prevent unfair, deceptive, or abusive practices by financial firms should be more than adequate to extend to this situation. See 12 U.S.C. § 5531 (2012). The rulemaking notice discussed above suggests that the CFPB shares this view of its authority.

closed-loop gift card. Assume, for example, that the consumer receives a \$100 gift card from a merchant that the consumer does not frequent. If the consumer visits the merchant's store and tries to spend as much of the card as possible without going out of pocket—after all, who wants to pay to get a birthday present—it is almost inevitable that some small amount will remain unspent. Because this problem seems particularly acute for closed-loop cards, we recommend a regulatory requirement that consumers be permitted to cash out (without additional charges) a *de minimis* unspent amount on the a closed-loop card—perhaps the greater of five dollars or five percent of the total amount loaded on the card. This option should be available to the consumer at the merchant's business place or from the same platform through which the card was initially issued.

The third prong of responses on this point relates to escheat fees, traditionally the province of state (rather than federal) law.¹¹⁰ Here, we are indeed not sufficiently informed to be sure there is a problem that warrants intervention. At some point, we think it makes sense for funds to escheat to the State—imagine the polar case in which there has been no activity on a card for twenty years and the issuer has been unable to reach the cardholder despite reasonable efforts. Here, there seems no approach more sensible than escheat to the State. If a case could be made that state-escheat laws were taking funds with undue rapidity, at a point when cardholders reasonably might be located or might decide to spend the funds, then a case for federal regulatory intervention might be made out to establish a “floor” that must be satisfied before funds can be escheated. To date, however, we do not think that case has been made. Moreover, we expect that the “cashing-out” rule we recommend above would diminish considerably the small-dollar values left indefinitely on closed-loop cards.

D. *The Problem of Fees*

We turn in closing to the problem of fees, which we save for last in part because it has been such a prominent part of the existing discussion that a variety of proposals already are at hand. The case for regulation of fees has several prongs, all of which tend to suggest that consumers are not adequately pricing the fees in their calculations of whether it makes sense to acquire the cards. The main concern is that the fees are not adequately salient to consumers when they acquire the cards; they could be regarded, like the dormancy fees discussed above, as another example of the “shrouded” contract terms that Gabaix and Laibson decry.¹¹¹ Here, that problem is exacerbated by the likelihood that the cards are presented to their users, in many circumstances, as a non-negotiable proposition;

¹¹⁰ William S. King, Note, *A Bridge Too Far: Due Process Considerations in State Unclaimed-Property Law Enforcement*, 45 SUFFOLK U. L. REV. 1249, 1252–53 (2012).

¹¹¹ See *supra* note 106 and accompanying text.

this is particularly true in the payroll context. What this means is that the consumer has no opportunity to negotiate terms; the consumer's choice is to accept the card or accept some even-less-convenient method for receiving salary.¹¹² Three regulatory approaches are apparent: letting the market set the fees, requiring disclosure of the fees, or imposing substantive regulation of the amount of the fees.

The first question is whether regulation is appropriate at all. To the extent that consumers acquire the cards in a competitive market, there might seem little reason for the government to step in to set the "price" at which the payment services are sold. But, of course, the problem with that position is the premise of a competitive market in which card purchasers accurately "price" the fees. As suggested above, that is particularly unrealistic in the payroll-card context. Even in other contexts, such as gift cards, it seems unlikely that customers accurately price the fees when they price the cards. Can the consumer purchasing a gift card accurately assess the impact of future per-transaction or periodic fees? Perhaps, if the fee structures are well-disclosed and not unduly complicated. But it seems clear that the consumer could assess them more accurately if the issuer capitalized all necessary fees into a single charge included in the price of the card. The issuer, for example, might charge an extra five percent of the amount of a gift card up front, rather than a series of fees in the future; as the issuer is better placed than the purchaser to assess the likely total fees over the life of the card, the issuer could set that price more accurately than the consumer could predict the fees. At that point, there would be little concern about mispricing, because the fees would now be charged up-front.¹¹³

The issue is a little more problematic with respect to reloadable cards. In that situation, the fees for loading funds onto the cards could be regarded as metering the consumer's use of the card in transactions that in fact impose costs on the issuer—each act of loading the card requires the equivalent of an ACH transfer, and thus is likely to impose some costs on the issuer.¹¹⁴ Even here, though, a limit of the maximum loading fee to some multiple of likely costs seems reasonable enough. If the CFPB knew, for example, that the true costs of a transaction loading the card (including an allotment for the salary and rent of employees in

¹¹² In some cases, as in the federal government program, the recipient without a bank account has no choice but to accept the card—the government no longer disburses benefits payments by check or cash.

¹¹³ Issuers might be concerned that the absence of a per-transaction fee would expose them to undue processing costs from cardholders that use the cards for an unusually large number of unusually small transactions. Given the low per-transaction processing costs discussed above, that problem does not strike us as critical. If it did seem serious, regulations could permit issuers to require a minimum transaction amount for use of the card without a transaction fee. The ability of the federal Direct Express program (discussed below) to ban such fees suggests, however, that issuers in reality have no real need for such a fee.

¹¹⁴ See MANN, *supra* note 72, at 742.

the retail location loading the card) amounted to approximately 50 cents per transaction (an estimate that seems quite high to us), and if we knew that the present industry norm for loading fees is several multiples of those costs (two to five dollars), does it seem plausible that the market for those fees is functioning well?

In the end, then, we conclude that some form of fee regulation is appropriate. Turning to the form of the regulation, the most common proposal is for detailed disclosures. For example, the proposed Prepaid Card Disclosure Act of 2014 would require something like a “Schumer” box with a detailed disclosure of the various fee amounts.¹¹⁵ Recognizing that our views on this question are driven largely by a general skepticism of disclosure, and that this Essay is not the place to argue the merits (or demerits) of disclosure, we express a general doubt that the costs of those sorts of disclosures can justify the benefits they will bring.¹¹⁶ For the most part, we expect, the disclosures will do little or nothing to alter the understanding or product choices of the consumers that receive them. Accordingly, we think the costs of requiring them are largely unjustified.¹¹⁷

We turn then to the question of mandatory fee regulation. In our view, the question of fee regulation should be largely contextual. It is, accordingly, beyond the scope of this brief Essay to consider all the possible contexts. It is instructive, however, to consider how our mode of analysis applies to three of the most common contexts.

The first is the question of transaction and periodic fees for gift cards that are not reloadable. As suggested above, we think it is plain that the best solution here is to ban those fees entirely, requiring the issuers to charge those fees in the most transparent manner—including them as part of the up-front price of the card.

Also following from the discussion above is our view on fees related to reloading reloadable cards. Here, we believe the best approach is a cap set at several multiples of the true expected costs of the transaction. If we are correct in our sense that the “all-in” transaction costs are unlikely to exceed 50 cents per transaction, then it well might be reasonable to cap loading fees at \$1 (a figure much lower than the present industry norm but far exceeding any likely costs of the transaction, even for small issuers). Again, we suspect that any such cap would allow issuers to recover their variable costs related to loading transactions. If that fee were inadequate to cover more general costs, the simple (and transparent) remedy for the issuer would be to increase the up-front price of the card.

¹¹⁵ See Prepaid Card Disclosure Act of 2014, S. 1903, 113th Cong. (2014).

¹¹⁶ Haim, *supra* note 70, at 37–38.

¹¹⁷ *Id.* For a general criticism of disclosures, with which we largely agree, see OMRI BEN-SHAHAR & CARL E. SCHNEIDER, MORE THAN YOU WANTED TO KNOW: THE FAILURE OF MANDATED DISCLOSURE (2014).

The hardest problem relates to fees for payroll cards, which have generated by far the most scrutiny.¹¹⁸ The case for imposing costs on the cardholder is somewhat stronger here; the cardholder often benefits from the card because the costs of acquiring funds on the card are so much lower than the fees of other acquisition transactions (such as cashing a check at a third-party check casher). Still, we are inclined again to conclude that these fees probably should be banned, in favor of a model that internalizes the processing costs with the issuer.

For one thing, the issuer is far more likely to notice, and attempt to minimize, the costs of processing than the cardholder, who has little or no control over those costs; ordinary economic principles suggest that those costs will be managed most effectively if their burden is placed on the party in the best place to minimize them. In that model, the residual processing costs would be priced into the employee's salary structure; if the actual processing costs are far less than the alternatives available to the employer (as seems likely), then forced internalization should have no negative effect on the employers' salary structure.

We should add that our conclusion on this point is motivated primarily by the example of the federal government's Direct Express program (through which a wide variety of federal benefits are disbursed). It is a condition of participation in that program that issuers waive substantially all fees related to the cards.¹¹⁹ Thus, there can be no fees for loading benefits onto the cards, for purchases in the United States, or for withdrawing cash at purchases or from bank tellers or, once each pay period, from ATMs.¹²⁰ The only permitted fees relate to such things as multiple ATM withdrawals in a single pay period, insisting on paper statements, seeking more than one replacement card per year, or purchases from merchants outside the United States.

The existence, and success, of the Direct Express card shows that an issuer can execute a successful program without any substantial volume of back-end fees. In a way, this should come as no surprise. Unlike the credit card—where the issuer advances funds up-front and needs revenue after the fact to cover the cost of the funds and operating costs—the stored-value-card issuer receives funds up-front, and thus can rely on revenues from holding those funds to defray the operating costs of the system. With advances in the efficiency of electronic processing, it should

¹¹⁸ See, e.g., Herb Weisbaum, *Feds: Employers Can't Force Payroll Debit Cards on Workers*, TODAY (Oct. 2, 2013), <http://www.today.com/money/feds-employers-cant-force-payroll-debit-cards-workers-8C11312099>; Martha C. White, *Nickeled, Dimed, and Dollared to Death: Fee-Laden Payroll Cards Forced on Low-Wage Workers*, TIME (July 9, 2013), <http://business.time.com/2013/07/09/nickeled-dimed-and-dollared-to-death-fee-laden-payroll-cards-forced-on-low-wage-workers>.

¹¹⁹ *Frequently Asked Questions*, DIRECTEXPRESS, <https://www.usdirectexpress.com/edcfdtclient/docs/faq.html> (posting the permitted fee structure).

¹²⁰ With the slight exception that third-party ATM providers can charge surcharges (as they can for any withdrawals in the conventional-card market).

come as no surprise if the processing costs and overhead can largely be covered by revenues accruing to the issuer based on the balances it holds.

CONCLUSION

This Essay is a discursive attempt to analyze the impact of a relatively new payments innovation. In our view, the cards have the potential to solve one of the most persistently embarrassing problems in the provision of financial services in our country—the limited penetration of mainstream products to LMI households—and to forestall the extension into those households of the routinized credit use that plagues more affluent households in our economy. Accordingly, we believe that regulation should shift from a position of hostility, or even disinterest, toward a position of affirmative support. That is particularly true for the general-purpose reloadable cards that have the most direct potential to bring LMI households into the financial mainstream.

We summarize above a series of simple and straightforward regulatory approaches that should give LMI households access to financial products that are functionally similar to the products middle- and upper-income households have used for decades. If those products are confined so that they expose LMI households to no more risks than those that middle- and upper-income bear on their cards, this can signal movement forward in resolving a longstanding problem of central importance to LMI households.

We recognize that our analysis rests on assumptions and conjectures that might not be shared by all readers. We offer it primarily as a template for further discussion. Whatever the ultimate results, we are convinced that the burgeoning use of these cards should be welcomed and fostered whenever possible by regulators at all levels of government.