

FEDERAL RESERVE PROPOSES RULES TO RESTRICT FEES AND EXPIRATION DATES ON GIFT CARDS

I. INTRODUCTION

On November 16, 2009, the Board of Governors of the Federal Reserve (Board) issued proposed rules (Proposed Rules) that would restrict the fees and expiration dates that may apply to gift certificates, store gift cards, and general-use prepaid cards that are marketed as gift cards (collectively, gift cards). The Proposed Rules would amend Regulation E, 12 C.F.R. Part 205, which implements the Electronic Fund Transfer Act (EFTA), 15 U.S.C. 1693 *et seq.* These amendments would implement the gift card provisions of the Credit Card Accountability Responsibility and Disclosure Act of 2009 (CARD Act), which was signed into law on May 22, 2009. The CARD Act requires the Board to adopt final rules implementing the gift card provisions within nine months of the date of enactment, or no later than February 22, 2010. The CARD Act and the Proposed Rules represent the latest federal actions in gift card restrictions since the Federal Trade Commission (FTC) in 2007 entered into settlement agreements with K-Mart¹ and Darden Restaurants² regarding their respective gift card practices.

II. SCOPE OF THE PROPOSED RULES

The Proposed Rules set limits on practices related to gift certificates, store gift cards, and general-use prepaid cards marketed as gift cards. These forms of stored value cards are defined within the Proposed Rules, and the scope of these definitions encompass physical cards, electronic codes, or any type of device that is issued to a consumer for a specified amount and redeemable for goods or services, or usable at automated teller machines. The Proposed Rules also define devices that are not included within the definition of a gift card, and thus are excluded from the Board's prohibitions. An excluded device has one or more of the following six characteristics:

1. **Useable solely for telephone services.** This exclusion includes prepaid calling cards for long-distance service, wireless service, and analogous calling services, such as voice over internet protocol (VoIP).
2. **Reloadable and not marketed or labeled as a gift card.** If anyone in the

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¹ <http://www.ftc.gov/os/caselist/0623088/0623088do.pdf>

² <http://www2.ftc.gov/os/caselist/0623112/070510do0623112c4189.pdf>

distribution chain markets or labels the device as a gift for another person, even seasonally, then this exclusion would not apply. Such marketing includes displaying a congratulatory message on the device, or incorporating imagery such as a bow, or ribbon, on the device or promotional materials. In addition, policies and procedures must be reasonably designed to avoid the marketing of the reloadable device as a gift. For a card issuer, this could mean taking actions to create two physically separate retail promotional displays, one for gift cards, and one for excluded reloadable general purpose cards.

3. **Not marketed to the general public.** Devices that are used exclusively for distribution of funds to a subset of consumers and not the general public are included within this exclusion. These non-marketed devices could include an employee reimbursement card, returned-item store credit, a tax refund card from a tax preparation company, or an insurance proceeds card that settles a policyholder's claim.
4. **Issued in paper form only.** This exclusion applies only to devices that were initially issued in paper form; electronic codes or cards that may be printed out onto a paper format are not included within this exclusion. If, however, an issuer replaces a lost paper device with an electronic device, then this exclusion would still apply.
5. **Redeemable solely for admission to events or venues.** This exclusion includes devices that allow a one-time admission into a venue such as an amusement park, or a durational admission to a venue such as a one-year gym membership. If the device also allows the purchase of goods and services *in conjunction* with the admission, then the exclusion still applies. However, if the device allows a consumer to either make purchases at a merchant *or alternatively* use the card for admission to the merchant's affiliated venue, then the exclusion would not apply.
6. **A loyalty, award, or promotional gift card.** Examples of this exclusion could include merchant programs that reward frequent consumers with redeemable cards, or

rebate cards provided in connection with a previous consumer purchase. The exclusion may apply regardless of whether a consumer received the device in exchange for payment. Unlike the other five exclusions, however, *the Board requires these devices to contain disclosures regarding any fees and expiration dates that may apply.* Disclosures regarding dormancy, inactivity, and service fees, as well as the expiration date, a toll-free number and, if one is maintained, a website, must be made on the device itself. Disclosures regarding other fees, such as one-time initial issuance fees and cash-out fees, may simply accompany the device.

III. RESTRICTIONS ON DORMANCY, INACTIVITY, AND SERVICE FEES

For gift cards covered by the Proposed Rules, fees such as transaction fees, dormancy fees, inactivity fees, maintenance fees, card reload fees, or balance inquiries fees, would be prohibited, unless the following three conditions are met:

1. there has been at least one year of inactivity on the card;
2. no more than one such fee is charged per month; and
3. the consumer is given clear and conspicuous disclosures about the amount and frequency of the fees, and that such fees may be assessed for inactivity.

The clear and conspicuous disclosures must be readily noticeable and understandable to consumers. The disclosures must also be provided prior to a gift card's purchase, as well as on the surface of the actual gift card. If additional fees, such as one-time initial issuance and cash-out fees are charged, then the type, amount, and conditions of that fee must also be disclosed on or with the card.

Additionally, the Proposed Rules require gift cards to include clear and conspicuous disclosures related to the terms and conditions of expiration of the underlying funds, including the expiration date of the device, and if applicable, a statement clarifying whether the underlying funds also expire on the card's expiration date; and a toll-free number and, if one is maintained, a website that a consumer may access for fee

information or replacement cards.

Prior to the purchase of the gift card, the disclosures may be provided in writing on the outside of the gift card's packaging, or orally if the volume and speed of the oral disclosure is sufficient for the consumer to hear and comprehend. The disclosures must also appear on the surface of the gift card. While the disclosures do not need to be on the front of the gift card, the print must be in a noticeable type size, and the font must contrast with the background on which it is printed. For non-physical gift cards, the disclosure must accompany the written or electronic document that is provided to the consumer. For example, an electronic code, or confirmation sent to a consumer through email must include the disclosures within the email.

IV. RESTRICTIONS ON EXPIRATION DATES

The Proposed Rules also would prohibit the sale or issuance of a gift card that has an expiration date of less than five years after the date of issuance, or the date the funds are last loaded onto the card. The Proposed Rules address the potential issue of a disparity between the stated expiration date of the gift card (card expiration date) and the date the underlying funds expire (funds expiration date). The funds expiration date may differ from the gift card expiration date because the funds expiration date, under the Proposed Rules, would depend on when the consumer purchases or adds funds to the gift card. Because the funds expiration date would adjust each time the consumer reloads the card, the funds may never expire. Also, no fee or charge may be imposed on a cardholder for replacing a gift card prior to the funds expiration date, unless such card has been lost or stolen.

The Board has proposed two alternatives to the expiration date restriction:

1. prohibiting a person from selling a gift card subject to an expiration date unless the gift card expiration date was at least five years after the date the gift card is sold or issued to a consumer; or
2. requiring entities involved in issuing, distributing, and

selling gift cards to adopt policies and procedures to ensure that a consumer will have a reasonable opportunity to purchase a gift card with at least five years remaining until the gift card expiration date. Under this alternative, a person would not be required to confirm that a gift card is in fact sold or issued to a consumer at least five years before its expiration date. This could lead to a disparity in the gift card expiration date and funds expiration date because the expiration date on some gift cards could be less than five years from the date of sale or issuance, but the consumer would still have access to the underlying funds for a minimum of five years from the date of sale or issuance. However, the first alternative could be very expensive, as card stocks with expiration dates are usually delivered well in advance of any sale.

V. BOARD'S REQUESTS FOR COMMENTS

The Board has requested comments on issues concerning the Proposed Rules including:

- whether it is appropriate to limit the scope of the final rule so that it does not apply to cards issued for business purposes;
- how issuers currently provide disclosures and how issuers comply with state laws that set forth disclosure requirements similar to those contained in the Proposed Rules;
- whether the Board should require issuers to automatically issue a replacement card to consumers prior to the expiration date of a reloadable card if the underlying funds will not expire until later;
- whether the Board should prescribe certain disclosure formatting standards, such as "in close proximity" and "equal prominence" standards, and whether it should prescribe a minimum type-size requirement; and
- whether to grandfather gift cards that are in the marketplace as of the effective date of the rule from

some or all of the requirements of the rule.

The Board has also requested comment on the following issues with respect to the exclusions in the Proposed Rules:

- whether the “usable solely for telephone services” exclusion should cover other prepaid cards that may be redeemed for services such as mobile broadband or Internet access time;
- whether additional guidance on marketing is necessary to provide clarity with respect to the activities that may trigger coverage under the rule and the activities that would not; and
- whether the Board has provided sufficient guidance regarding how an issuer, program manager, or other covered entity may comply with the exclusion for reloadable prepaid cards that are not marketed as gift cards, including whether there are any practical issues that may arise in the retail environment.

The Board also has indicated that the Proposed Rules would not impose on gift cards any of the other requirements that generally apply to accounts under the EFTA and Regulation E, such as periodic statement disclosures or error resolution obligations. The Board has reserved this issue for consideration in a broader rulemaking that covers prepaid cards generally to avoid any regulatory gaps or inconsistencies. The Proposed Rules also would not limit the amount of dormancy, inactivity, or service fees, or the balance below which such fees may be assessed, although the Board has indicated that it may address this issue at a later date.

Arnold & Porter LLP is available to respond to questions raised by the Proposed Rules or to provide any assistance in drafting comments. We also can assist in determining how these rule changes may affect your business and ensuring that your business is compliant when the Proposed Rules are finalized. For further information, please contact your Arnold & Porter attorney or:

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