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Statement by

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Board of Governors of the Federal Reserve System

before the

Subcommittee on Consumer Affairs

of the

Committee on Banking, Finance and Urban Affairs

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It is a pleasure for me to appear before this Subcommittee. I have been designated to chair the Board committee that has responsibility for consumer affairs, and look forward to working with you.

Section 1 of H.R. 3552 would make a written notification of the loss or theft of an EFT card effective when mailed by the consumer. The Board's Regulation E currently takes a different position. The regulation provides that a written notification is effective upon receipt by the financial institution or at the expiration of the time it normally takes for mail delivery, whichever is earlier. This provision was modeled on an identical section in the Truth in Lending Act and Regulation Z and was designed to encourage telephone notification.

Given the vagaries of the U.S. mail, it is likely that sending a written notice will create a "risk period" during which losses may continue to occur. The approach taken by H.R. 3552 would shift losses that occur during this period from the consumer to the financial institution. Neither the regulation nor the bill as presently drafted would reduce the losses--losses that ultimately will be passed on to consumers as higher costs. A better approach--one that could effectively reduce potential losses to everyone concerned--might be to allow financial institutions to require oral notice and to provide a 24-hour telephone line for this purpose. This would

coincide with the way consumers normally act, would speed up notification, and would reduce losses to everyone.

Section 2 of H.R. 3552 would change the effective date of most of the remaining provisions of the Electronic Fund Transfer Act from May 10, 1980, to September 10, 1979. The Board recommends against adoption of this amendment. While we recognize the need for prompt implementation of the Act, changing the effective date to September 10 would not leave sufficient time to accomplish this task effectively. It would require the Board to issue regulations without the degree of public participation that is essential for orderly implementation of this important new law.

The Board's present schedule for implementing the remainder of the Act is as follows: we are publishing a proposed regulation this week, with a 60-day comment period ending July 2 and public hearings on June 18 and 19. We are allowing 60 days for analyzing any complexities that may be uncovered by the comments and for redrafting the regulation. We plan to publish a revised regulation for a second 60-day period, running from September 1 through October 31. Analysis of those comments and redrafting will be completed in mid-December. The final regulations should be published by the end of December.

We believe this is a realistic schedule that demonstrates the Board's commitment to speedy and responsible implementation of the Act. Meeting it will require considerable effort by the Board and

its staff. Based on our experience in implementing consumer protection legislation, we believe that a shorter rulewriting timetable would not be in the public interest.

We could shorten the timetable by allowing 30 days instead of 60 days for public comment. We are concerned, however, that a 30-day period would not allow all interested parties to express their views adequately as has happened in the past. The Board has adopted a policy, in accordance with the spirit of Executive Order 12044, of allowing at least 60 days for public comment on regulations that implement a new law. We feel that adequate time for public comment is especially important in the case of a law, such as the Electronic Fund Transfer Act, that is highly technical and that confers significant consumer rights.

Our experience with implementation of other legislation also indicates that 60 days is essential for analysis of public comments, redrafting the regulations, and bringing them back for the Board's consideration. In 1976, when the amended Equal Credit Opportunity regulations were issued, the Board received about 650 comments on the first proposal and 500 comments on the second. More recently, the Board and the other financial supervisory agencies received almost 1,000 comments on the Community Reinvestment Act regulations. There is great public interest in the EFT Act. I think we can expect to receive at least several hundred comments on proposed Regulation E.

The Board's timetable calls for two public comment periods. I wish I could say that one comment period will suffice, but, again, our experience indicates otherwise. When new regulations are drafted, the first proposal may overlook important issues and some of the provisions may not be workable. Indeed, that is the purpose of public comment--to expose regulations to the critical gaze of the financial institutions and consumers who must live with them. Having two comment periods allows the public to comment on significant changes before regulations go into effect and thereby reduces the possibility that the regulations will have to be amended later. As a result of the comments received, significant changes were made to the regulation implementing §§ 909 and 911 earlier this year. Those changes were republished for public comment.

If the Act's effective date were changed to September 1979, the Board's regular procedures could not be followed. Even if we were to have only one comment period, there is a real risk that the law would take effect before implementing regulations could be issued in final form.

I would like to point out that the EFT Act imposes major new responsibilities on financial institutions. They will be required to prepare and print new disclosures, establish new error resolution and stop payment procedures, program computers to generate periodic statements, and, of course, train their personnel. Our experience

with other laws, including the Equal Credit Opportunity Act, suggests that the quality of compliance is enhanced and the cost of compliance reduced by providing a lead time of several months between the issuance of regulations in final form and the effective date of a statute.

I am also seriously concerned about making regulations effective before financial institutions have developed the procedures necessary to implement them. There is a real risk that consumers will be misled into thinking they have rights that, for all practical purposes, are not yet available to them.

I also want to express the Board's strong concern about some of the substantive provisions contained in the current EFT Act. In the course of drafting the regulations, it has become clear to us that unless Congress acts promptly, consumers and financial institutions will face different rules under the EFT Act and Truth in Lending. In the Board's view, these differences will create unnecessary confusion.

As things now stand, for example, different rules regarding liability and dispute resolution procedures will apply depending on whether the plastic card issued to a consumer is a credit card or a debit card. Different rules may even apply to the same piece of plastic, in the case of a combined credit-debit card. In some cases, the rule will depend on whether a card is used to obtain credit by electronic or non-electronic means. In other words, when something goes wrong, both the consumer and the issuer of the card will have to figure

out what category the transaction falls into, in order to know what rules apply and what has to be done.

The Board believes that, to minimize confusion, the EFT and Truth in Lending Acts should be amended to provide a single set of rules to govern credit and electronic fund transfer transactions, except where compelling policy considerations may dictate different treatment. We believe the rules should be simple and straightforward, so that both the industry and the consumers that use these services can understand them. The Board has a number of specific recommendations:

1. The Truth in Lending Act imposes a flat $50 limit on the liability of a credit card holder when a card is lost or stolen. The Electronic Fund Transfer Act has a $50, $500, and unlimited liability structure. A majority of the Board believes consumers' potential exposure under the EFT Act is too great, although there may be instances in which the consumer should bear some liability for carelessness. The structure of the liability provisions is unduly complicated, and the benefit to the industry of the escalating liability limits may ultimately be illusory rather than real. The Board favors the Truth in Lending approach of a single liability limit for unauthorized use. We also believe it will make electronic payment systems more acceptable to the public.

2. Under the Fair Credit Billing Act, a consumer must write to the creditor in order to take advantage of the dispute resolution rules of the Act. The Electronic Fund Transfer Act permits consumers to give oral notice, although an institution can require written confirmation. It is estimated that fewer than 1% of consumers with questions

about their bills follow the formal procedures of the Fair Credit Billing Act. Consumers usually telephone, and the lack of formality should not remove them from the protections of the Act. The Board therefore recommends that the Fair Credit Billing Act be amended to incorporate an oral notice provision.

3. When an error is alleged under the Electronic Fund Transfer Act, the institution has 10 business days in which to complete its investigation. If it needs more time, it must provisionally recredit the consumer's account within 10 business days. When an error allegation is received under the Fair Credit Billing Act, the creditor must either resolve the dispute or send an acknowledgment within 30 days. The Board recommends that the acts be amended to provide parallel timing requirements.

The maximum time limits for resolving disputes are 45 days under the Electronic Fund Transfer Act and two billing cycles (but not more than 90 days) under the Fair Credit Billing Act. The Board recommends that the Electronic Fund Transfer Act be amended to conform to the Fair Credit Billing Act, to require resolution within 90 calendar days. Lengthening the Electronic Fund Transfer Act limit will not harm consumers since an institution must have provisionally recredited within 10 business days in order to take advantage of the longer time period.

4. The Board recommends the elimination of the annual notice of rights under the Electronic Fund Transfer Act and the semiannual

notice of rights under the Fair Credit Billing Act. Since it is normally information on periodic statements which triggers a dispute, we believe that consumers are better served by a summary notice on periodic statements than they are by a lengthy explanation once or twice a year.

5. Finally, the Board's staff has received a number of inquiries asking whether the Fair Credit Billing Act permits creditors to impose charges for providing documentation or for investigating errors. In some cases, these charges are quite substantial, and in others they are open ended--for example, $5 per hour for an investigation. We anticipate that the same questions will arise regarding investigation of alleged errors in EFT transactions. The Board recommends that both the Fair Credit Billing Act and the Electronic Fund Transfer Act be amended to prohibit such charges. While Regulation Z already prohibits these charges where a customer's allegation of error proves correct, we believe that permitting these charges at all serves to discourage customers from exercising their right to assert errors.

It is essential that the legal relationship between electronic fund transfers and credit transactions be clarified. Consumers and the industry will both benefit from a rational, common-sense framework. The Board and its staff will be glad to work with you in developing the statutory language to implement these recommendations.

Finally, there are two other issues on which we would like to consider legislative or other remedies after we have a little more time to think them through. These issues arise because the consumer account used for EFT transactions will generally be the same account used for paper check transactions, and the account statement will cover both. The Act covers only transactions that are initiated electronically. But it is quite possible not only for there to be transactions that are wholly paper and others that are wholly carried out by means of EFT in the same account, but also for transactions to involve both paper and EFT elements, or to start as paper and to finish electronically.

One issue has to do with how the consumer is to be given an adequate disclosure of account terms and conditions when the account can be accessed by both EFT and conventional paper means. It is essential for consumers to know the terms and conditions of the entire account. Balance requirements, fees, usage limitations, and availability of funds are important facts that should be provided to consumers so that they can make educated decisions on which type of transfer most suits the consumer's needs. Under the Board's proposed regulations (and under most current practices) electronic deposits

are immediately available to the customer, while check deposits may be delayed for several days awaiting check clearance.

While the EFT Act requires disclosure of essential terms and conditions of an electronic fund transfer, it does not provide the Board with specific authority to require disclosure of all important terms of any account from which electronic fund transfers as well as other transfers may be made. Although we believe the Board has the authority to require disclosure of account terms generally, broadening the disclosure authority under the EFT Act for accounts subject to electronic fund transfers may be appropriate.

The second issue has to do with paper truncation and with how the consumer is to get adequate proof of payment on a transaction that begins with a paper check but in which the item is translated into an electronic impulse. This is the case with many credit union share drafts today--the customer only gets back a printout and not the actual paper itself. The present EFT Act protects the consumer only when the transaction is begun electronically; by law, the statement finally received by the consumer is proof of payment. If the transaction begins with a paper check and the check is not returned to the consumer, there is no such protection. Our reluctance to recommend

action at this time is based, in part, on the fact that check truncation is not yet widely developed for consumer payments (except for share drafts, and here the institution stands between the customer and the payee). Until we know more about the direction in which consumer check truncation is developing, we want to be cautious about suggesting consumer legislation. We believe that in both of these situations, consumers may need protection. We would like to give some further study to the technical problems involved, and will report to you when we have been able to develop recommendations. For now, we want to alert you that these problems are on the horizon and would be pleased to work with your staff in giving further consideration to these issues.