

regulation other obligations of an insured depository institution to be deposit liabilities by general usage. The FDIC has not promulgated such a regulation.

Summary

In summary, in my opinion funds underlying Bank Primary—Customer Account Systems appear to be funds held by an institution, in the usual course of business, which remain credited to the customer's account until the payee makes a claim on the funds. Such funds would therefore appear to be deposits under section 3(l)(1) of the FDIA, 12 U.S.C. 1813(l)(1).

As a general matter, funds held by an institution to meet obligations under Bank Primary—Reserve Systems would appear not to be deposits under section 3(l)(1) of the FDIA, 12 U.S.C. 1813(l)(1), because the funds are not credited to or obligated to be credited to a commercial, checking, time, or thrift account.

It is my further opinion that the funds underlying Bank Primary—Reserve Systems are not deposits under section 3(l)(3) of the FDIA, 12 U.S.C. 1813(l)(3), because such funds are not held for a special or specific purpose. The examples of funds held for such purposes in the statute are all linked to one or more specific transactions. Conversely, the funds underlying stored value card transactions are not necessarily linked to a specific transaction.

In Bank Secondary—Pre-Acquisition Systems the funds underlying the stored value are, in my view, received or held by the third party, not the depository institution. Consequently, it appears that this requirement of section 3(l)(1) and (3) of the FDIA, 12 U.S.C. 1813(l)(1), (3), would not be satisfied in such systems.

The funds held by an institution in a Bank Secondary—Advance System would not create a deposit liability to the customer because the liability is owed to the third party for whom the institution is temporarily holding the funds. Such funds may create a deposit liability to the third party. The funds are held by the institution in the usual course of business prior to transferring such funds to the third party. The parties may or may not intend that the institution credit an account. Even if the institution is not obligated to credit such funds to an account, and thus such funds would not be a deposit under section 3(l)(1) of the FDIA, the funds may be deemed to be held for the specific purpose of transferring the funds to the third party and thus would be considered a deposit under section 3(l)(3) of the FDIA, 12 U.S.C. 1813(l)(3).

The fact that an institution may retain a contingent liability to redeem electronic value from consumers and merchants in Bank Secondary Systems does not meet the requirement of "money or its equivalent held by an institution" and therefore would not give rise to a deposit liability to the customer under either 3(l)(1) or (3) of the FDIA, 12 U.S.C. 1813(l)(1), (3).

With respect to the other provisions of section 3(l) of the FDIA, 12 U.S.C. 1813(l), the FDIC staff is not aware of stored value card systems in which funds will be held as trust funds. Thus, the funds underlying stored value cards would not be deposits under section 3(l)(2) of the FDIA, 12 U.S.C. 1813(l)(2). Similarly, while stored value cards have certain similarities to cashier's checks and money orders, they are not drafts drawn on the bank, nor are they negotiable instruments. Consequently, they cannot be considered deposits under section 3(l)(4) of the FDIA, 12 U.S.C. 1813(l)(4).

Notwithstanding the question of whether and under what circumstances stored value card obligations are deposits within the meaning of section 3(l)(1)–(4) of the FDIA, 12 U.S.C. 1813(l)(1)–(4), section 3(l)(5) of the FDIA, 12 U.S.C. 1813(l)(5), gives the Board of Directors the authority to find and prescribe by regulation that other obligations of an insured depository institution are deposit liabilities by general usage. The FDIC has not promulgated such a regulation.

This General Counsel Opinion only addresses the extent to which funds underlying stored value cards may constitute a deposit under 12 U.S.C. 1813(l). It is not intended to address the way in which FDIC would act in its role as receiver. In the event of an institution's failure, to the extent that any funds underlying stored value cards are recognized as deposits, there may be recordkeeping issues and other issues as to who may be entitled to deposit insurance and in what amount. See 12 C.F.R. Part 330.

Finally, the FDIC would expect that institutions clearly and conspicuously disclose to their customers the insured or non-insured status of their stored value products, as appropriate.

By order of the Board of Directors, dated at Washington, D.C., this 16th day of July, 1996.

Federal Deposit Insurance Corporation

Jerry L. Langley,

Executive Secretary.

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FEDERAL DEPOSIT INSURANCE CORPORATION

Stored Value Cards and Other Electronic Payment Systems

AGENCY: Federal Deposit Insurance Corporation (FDIC or Corporation).

ACTION: Notice; request for comment; public hearing.

SUMMARY: The FDIC is seeking comment on whether and under what circumstances the FDIC should take regulatory action with respect to finding that the funds underlying stored value cards or other similar electronic payment systems are deposit liabilities for purposes of the Federal Deposit Insurance Act. The FDIC is also seeking comment on types of proposed or existing stored value card systems, similar electronic payment systems, and the safety and soundness concerns raised by the emergence of these new technologies. This notice also sets forth the time and other particulars concerning a public hearing that the FDIC will conduct on this topic.

DATES: Written comments must be received by the FDIC on or before October 31, 1996. Requests to participate in the public hearing must be received by August 26, 1996. Each participant must submit a summary of his or her written testimony by September 3, 1996. The public hearing will be held on September 12, 1996 and possibly also on September 13, 1996, and other dates, depending upon the number of requests received to participate in the public hearing.

ADDRESSES: Written comments, requests to participate in the public hearing, and summaries of testimony are to be addressed to the Office of the Executive Secretary, Federal Deposit Insurance Corporation, 550 17th Street, N.W., Washington, D.C. 20429. Comments may be hand-delivered to Room F-400, 1776 F Street N.W., Washington, D.C. 20429, on business days between 8:30 a.m. and 5:00 p.m. (FAX number (202) 898-3838; Internet address: comments@FDIC.gov). Comments will be available for inspection and photocopying in Room 100, 801 17th Street, N.W., Washington, D.C. 20429, between 9:00 a.m. and 5:00 p.m. on business days.

Hearing location. Federal Deposit Insurance Corporation, Board of Directors' Room (6th Floor), 550 17th Street N.W., Washington, D.C. 20429

FOR FURTHER INFORMATION CONTACT: Sharon Powers Sivertsen, Director, Office of Policy Development, (202) 898-8710; Cary Hiner, Assistant Director, Policy Branch, Division of

Supervision (202) 898-6814; Marc J. Goldstrom, Counsel, Legal Division, (202) 898-8807, Federal Deposit Insurance Corporation, 550 17th Street, N.W., Washington, D.C., 20429.

SUPPLEMENTARY INFORMATION:

Background

Insured depository institutions are increasingly utilizing new technology to offer novel and innovative products to customers. One such product is the stored-value card. A stored value card stores information electronically on a magnetic stripe or computer chip and can be used to purchase goods or services. From the FDIC's perspective, the primary legal issue raised by the development of stored value card systems is whether and to what extent the funds, or obligations, underlying stored value cards constitute "deposits" within the meaning of section 3(l) of the Federal Deposit Insurance Act (FDIA) and are therefore assessable and qualify for deposit insurance. There has been a need for the FDIC to provide guidance on this issue. The FDIC has provided guidance with respect to this matter in General Counsel Opinion No. 8, published elsewhere in this issue of the Federal Register.

General Counsel Opinion No. 8 sets forth the Legal Division's views on whether and under what circumstances the funds underlying stored value cards may be considered deposits under sections 3(l)(1) through (4) of the FDIA, 12 U.S.C. 1813(l)(1)-(4). Notwithstanding the question of whether and under what circumstances the funds underlying stored value cards meet this statutory definition of deposit, the FDIC has the authority to find and prescribe by regulation that some or all stored value card obligations of a depository institution are deposit liabilities by general usage. 12 U.S.C. 1813(l)(5). The FDIC has not promulgated such a regulation and there are no current plans to propose a regulation on this matter. However, the FDIC wishes to solicit comments from the public as to the policy considerations concerning whether it should consider proposing such a rule at some point in the future. This request for comments is independent of and will in no way effect or undermine the analysis or conclusions in General Counsel Opinion No. 8.

In addition, General Counsel Opinion No. 8 is based generally on systems and technologies that have come to the attention of the staff. The FDIC is also soliciting comment with respect to whether there are other types of stored

value card systems in which depository institutions are involved.

Types of Stored Value Card Systems Discussed in General Counsel Opinion No. 8

General Counsel Opinion No. 8 identifies four types of stored value systems: (1) Bank Primary—Customer Account Systems; (2) Bank Primary—Reserve Systems; (3) Bank Secondary—Advance Systems; and (4) Bank Secondary—Pre-Acquisition Systems. These systems, as described below, represent a mechanism to generalize the circumstances under which the funds underlying stored value cards may or may not be considered deposits within the meaning of the FDIA.¹ The FDIC is soliciting comment with respect to whether there are other types of stored value card systems in which depository institutions are involved.

In Bank Primary—Customer Account Systems the funds underlying the stored value card could remain in a customer's account until the value is transferred to a merchant or other third party, who in turn collects the funds from the customer's bank.² In Bank Primary—Reserve Systems, as value is downloaded onto a card, funds are withdrawn from a customer's account (or paid directly by the customer) and paid into a reserve or general liability account held at the institution to pay merchants and other payees as they make claims for payments.

In the two types of Bank Secondary Systems, the electronic value is created by a third party and the funds underlying the electronic value are ultimately held by such third party. In such systems, depository institutions act as intermediaries in collecting funds from customers in exchange for electronic value. In Bank Secondary—Advance Systems, the electronic value is provided to the institution to have available for its customers. As

¹ We would also note that in its proposed amendment to Regulation E, 61 FR 19696 (May 2, 1996), the Board of Governors of the Federal Reserve System has distinguished between "off-line accountable", "off-line unaccountable", and "on-line" stored value systems in determining whether the regulation applies to various types of stored value systems. General Counsel Opinion No. 8 does not use these distinctions. This is not intended as a criticism or rejection of the Federal Reserve Board's classification system. Rather, it is indicative of the fact that these particular distinctions are not necessarily germane as to whether and under what circumstances the funds underlying a stored value card are "deposits" under the Federal Deposit Insurance Act (FDIA).

² Such a system would be similar to debit card systems, except that unlike a debit card, the information or value is on the card itself. The staff is not aware of any such system currently in development. It is our understanding, however, that such a system could be developed.

customers exchange funds for electronic value, the funds are held for a short period of time and then forwarded to the third party. In Bank Secondary—Pre-Acquisition Systems, the depository institution will exchange its own funds for electronic value from the third party and in turn exchange electronic value for funds with its customers.

In some Bank Secondary Systems, the depository institution may have a contingent liability to redeem the electronic value from consumers and merchants. As such electronic value is redeemed, the institution may in turn exchange the electronic value for funds with the third party.

Authority of the FDIC To Promulgate a Regulation Finding That Funds Underlying Stored Value Cards are Deposits

General Counsel Opinion No. 8 addresses the question of whether and under what circumstances stored value card obligations are deposits within the meaning of sections 3(l) (1)-(4) of the FDIA, 12 U.S.C. 1813(l) (1)-(4). Section 3(l)(5) of the FDIA, 12 U.S.C. 1813(l)(5), gives the Board of Directors the authority, after consultation with the Comptroller of the Currency, Director of the Office of Thrift Supervision, and the Board of Governors of the Federal Reserve System, to find and prescribe by regulation other obligations of an insured depository institution to be deposit liabilities by general usage.

In considering whether to promulgate such a regulation, the FDIC may wish to consider a number of policy issues. Through this notice and request for comment, and the related public hearing, the FDIC is inviting comment on any policy issues the FDIC should consider in determining whether to promulgate such a regulation. Some of these policy issues are discussed below. This discussion is intended to highlight the issues and does not represent the positions of either the Board of Directors or the staff.

While the discussion of policy considerations below focuses on stored value cards, the FDIC staff believes that such policy analysis would in general apply to a variety of electronic payment system issues, including concerns raised by Internet banking and the use of electronic cash. The FDIC is therefore also inviting comment on policy issues in connection with electronic payment systems.

Policy Considerations in Determining Whether To Promulgate a Regulation

Many industry participants are of the view that stored value cards and related products will eventually become a

significant element of the payment system and stream of commerce. By such reports, a significant portion of the payment system could be represented by stored value systems. As a result of the potential widespread use of such systems, it may be that the FDIC should determine that public confidence in these payment systems is critical to the safety and soundness of the banking system, such that deposit insurance is warranted.

Alternatively, it may be argued that the development of stored value technologies is in its very early stages. As such, stored value systems do not presently pose a threat to public confidence or the banking system, and therefore do not warrant deposit insurance coverage today.

Related to the public confidence issue are the expectations of depository institution customers. Consumers presently understand that if they open a checking or savings account with an institution, such accounts are insured up to applicable limits by the FDIC. It is possible that consumers could reasonably expect that deposit insurance protection is being obtained when they obtain stored value cards from institutions. The failure to provide deposit insurance in an instance where protection is reasonably expected by a consumer could, in the event of failure of an issuer, result in a loss of public confidence in these developing payment mechanisms.

Conversely, the staff would expect the relationship between a stored value card customer and the institution to be clearly and conspicuously stated on the disclosures and agreements accompanying the card. It is the staff's understanding that many of the stored value card systems in development intend to clearly and conspicuously inform customers that the card is to be treated like cash, and that if lost or stolen, it will not be replaced. Moreover, to the extent that stored value obligations do not otherwise constitute a deposit under sections 3(l)(1)–(4) of the FDIA, 12 U.S.C. 1813(l)(1)–(4), such disclosures and agreements should provide that the card does not constitute an account or deposit with the institution and that the funds underlying the card are not insured by the FDIC. Agreements and disclosures of this nature could influence consumer expectations as to deposit insurance with respect to stored value products.

It is also possible that consumer expectations regarding the existence of deposit insurance may differ depending upon the type of stored value card provided to the customer. Currently in development are both disposable and

reloadable stored value cards. The staff believes that this distinction is in large part irrelevant with respect to whether the funds underlying such cards constitute deposits within the meaning of sections 3(l)(1)–(4) of the FDIA, 12 U.S.C. 1813(l)(1)–(4). Nonetheless, such distinctions may be relevant with respect to consumer expectations and whether the FDIC should distinguish between the two if it decides to promulgate a regulation with respect to stored value cards.

A consumer may be more likely to believe that a reloadable card gives rise to an insured deposit. We understand that reloadable cards may contain information about the customer and may contain information about accounts the customer maintains with the institution. The customer may be required to provide name, address, and social security number to establish such a relationship. In addition, such stored value cards may allow the customer to transfer funds from existing insured accounts to a stored value component of the card.

On the other hand, if a consumer transfers funds in exchange for a disposable stored value card (which necessarily contemplates a transfer of value to an anonymous individual or entity, the only identifier being the card serial number), then a consumer could reasonably conclude that no deposit relationship has been established with the institution. Indeed, the consumer may not have been required to provide his name, address, telephone number, social security number, driver's license or other form of identification. After the transfer of funds by the customer, the institution may have no further relationship with him or her.

Another factor that may influence consumer expectations with respect to deposit insurance is whether the value on the card which has not been transferred is redeemable. If the value on the card is not redeemable, consumers may be less likely to expect deposit insurance associated with the product.

In addition to the issue of consumer expectations, the FDIC must consider whether insuring disposable/anonymous stored value cards is consistent with the statutory requirement that no more than \$100,000 in insurance coverage shall be provided to any one individual or entity. 12 U.S.C. 1821(a). Disposable/anonymous cards pose the possibility that an institution depositor, with \$100,000 in covered deposits, could transfer a disposable stored value card to another person in order to avoid the limit on deposit insurance coverage. In such a

case, the FDIC could have essentially unlimited liability for the total amount of stored value outstanding.

Another policy consideration is whether the FDIC should find that Bank Primary—Reserve System stored value cards are deposits based upon their similarity to cashier's checks, money orders, and traveler's checks on which an institution is primarily liable. As discussed in General Counsel Opinion No. 8, the differences between stored value cards and money orders, cashier's checks, and other drafts drawn on an institution, are such that they may not be included as one of the instruments listed in section 3(l)(4) of the FDIA, 12 U.S.C. 1813(l)(4). Similarly, inasmuch as stored value cards are not traveler's checks on which the institution is primarily liable, they may not come under this provision of section 3(l)(1) of the FDIA, 12 U.S.C. 1813(l)(1). Nonetheless, Bank Primary—Reserve System stored value cards resemble cashier's checks and money orders. The primary obligation of the institution reflected by a cashier's check, created in exchange for cash deposited in the general funds of the institution or transferred from a checking account, bears a resemblance to the obligation which appears to be established by stored value cards. Based upon the similarities, the FDIC could, by regulation, find that Bank Primary—Reserve System stored value card obligations are deposit liabilities.

In considering whether to promulgate a regulation, the FDIC is also concerned about competitive equity between depository institution issuers and other issuers of stored value products. If institutions pay deposit insurance assessments on the funds held in support of stored value, and non-banks do not, depository institutions could possibly be placed at a competitive disadvantage. If so, the question arises as to whether this disadvantage would be of such a magnitude that depository institutions would be prohibited entry into this new market for services. On the other hand, insurability could be a desirable feature of bank issued cards, such that consumers may be willing to pay a higher price for stored value products that are FDIC insured.

Finally, it is our understanding that, at least at the outset, many stored value cards will limit the amounts that may be loaded onto the cards to \$100 or \$200. Thus, it would appear that consumers will not be entrusting any significant or meaningful amount of money in exchange for the stored value card. Conversely, there is nothing preventing consumers from obtaining many stored value cards. Moreover, issuers may soon

allow cards to be loaded or issued in larger denominations. This issue may be considered by the FDIC in determining whether to find, by regulation, that certain stored value obligations are deposits.

In sum, notwithstanding the question of whether and under what circumstances stored value card obligations are deposits within the meaning of section 3(l) (1)–(4) of the FDIA, 12 U.S.C. 1813(l) (1)–(4), section 3(l)(5) of the FDIA, 12 U.S.C. 1813(l)(5), gives the Board of Directors the authority to find and prescribe by regulation that other obligations of an insured depository institution are deposit liabilities by general usage. In considering whether to promulgate such a regulation with respect to the stored value cards, the FDIC must consider a number of competing policy issues. Such policy issues include, but are not limited to, the level of public confidence in these new payment systems, consumer expectations, statutory limits with respect to “bearer” instruments, the similarities of stored value cards to other payment mechanisms which are deposits, competitive equity with non-bank issuers of stored value products, and the low denominations under which stored value cards will be issued.

Safety and Soundness Issues

The emergence of stored value cards and other electronic payment systems raises certain safety and soundness concerns for depository institutions and regulators. For example, institutions must take steps to ensure that the stored value or similar system in which they are participating has adequate safeguards to prevent counterfeiting or other fraudulent activities which could harm the institution, its customers, or other participants in the system. The FDIC is soliciting public comment on this and other safety and soundness issues in connection with stored value cards and other electronic payment systems.

Request for Comment

The FDIC is hereby requesting comment during a 90-day comment period on all aspects of this notice, including the following specific issues:

(1) General Counsel Opinion No. 8 is based generally on systems and technologies that have come to the attention of the staff. Are there other

stored value systems or technologies of which the staff may not be aware?

(2) Funds held by depository institutions to meet obligations arising under stored value card systems have been compared to funds held by an institution to meet letters of credit, which are deposits under section 3(l)(3) of the FDIA, 12 U.S.C. 1813(l)(3). In determining whether to promulgate a regulation, should funds held to meet obligations underlying stored value cards be distinguished from, or analogized to, funds held to meet letters of credit?

(3) Similarly, stored value cards have been compared to money orders or cashiers' checks drawn on an institution, which are considered deposits under section 3(l)(4) of the FDIA, 12 U.S.C. 1813(l)(4). In determining whether to promulgate a regulation, should stored value cards be distinguished from, or analogized to, such instruments?

(4) What are the expectations of consumers with respect to whether stored value cards are insured products? To what extent should consumer expectations be a factor in whether the FDIC finds by regulation that certain stored value products represent deposits?

(5) In determining whether to promulgate a regulation, should the FDIC distinguish between reloadable and disposable stored value cards or between single function and multiple function cards?

(6) Should the projected low dollar denominations for stored value cards be considered by the FDIC in determining whether to promulgate a regulation?

(7) What types of disclosure should the FDIC require with respect to the insured or non-insured status of these products? What types of disclosure would be most beneficial to consumers, while not overburdening depository institutions?

(8) If the funds underlying some or all stored value products issued by depository institutions are deemed by regulation to be deposits, to what extent would depository institutions be placed at a competitive advantage or disadvantage with respect to other issuers of stored value products?

(9) Should the FDIC ask Congress to amend section 3(l) of the FDIA, 12 U.S.C. 1813(l) to either include or exempt stored value cards from the definition of deposit?

(10) What safety and soundness concerns are raised by the development

of stored value cards and other electronic payment systems?

Public Hearing

The FDIC will hold a public hearing on all aspects of this notice on September 12, 1996 from 9:00 a.m. until 4:30 p.m. and possibly also on September 13, 1996, and other dates, depending upon the number of requests received to participate in the public hearing. The hearing will be held in the FDIC's Board of Directors' room which is located on the sixth floor of the FDIC's main building (550 17th Street NW, Washington, D.C.). At that hearing one or more members of the Board of Directors of the FDIC and other representatives of the FDIC will receive oral comments from all interested persons, who have been scheduled in advance to appear, on all aspects of this notice.

Persons wishing to participate in the hearing must send, or hand-deliver, a written request to participate in the hearing, so that it is received no later than August 26, 1996, to the Office of the Executive Secretary, 550 17th Street NW, Washington, DC 20429. All requests will be time and date stamped upon receipt. Participants will be limited to a 15 minute oral presentation and will be advised in writing of the time scheduled for their presentation. This procedure is necessary so that the hearing officers may adjust their schedules accordingly and so that alternative arrangements for the hearing may be made if more persons are expected to attend than the Board of Directors' room will accommodate. This deadline will also provide sufficient time to acknowledge receipt of the notices and inform participants of scheduling.

In addition, each participant must send, or hand-deliver, so that it is received no later than September 3, 1996 a written summary of his or her testimony to be given at the hearing, to the Office of the Executive Secretary, Federal Deposit Insurance Corporation, 550 17th Street NW, Washington, D.C. 20429.

By order of the Board of Directors, dated at Washington, D.C., this 16th day of July, 1996.

Federal Deposit Insurance Corporation
Jerry L. Langley,
Executive Secretary.

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