WASHINGTON — Industry groups are objecting to Consumer Financial Protection Bureau plans to regulate overdraft services in a pending rule on prepaid cards as well as to how the rule would treat virtual currencies.

Commenters weighing in on the agency’s proposed rule homed in on a provision that would treat overdraft protection available on a prepaid product essentially like a credit card — subject to tougher restrictions — and on the proposed scope of accounts covered by the rule.

"The proposal's overly prescriptive and complex rules for overdraft services would make offering such services for consumer short-term liquidity needs impracticable, if not impossible," Charles J. Harris, president of the prepaid card provider NetSpend, wrote in a March 23 comment letter.

The November proposal would include new protections for prepaid customers, ranging from error resolution rights to fraud and lost-card protection. Card providers would also have to follow "Know-Before-You-Owe" disclosure requirements, including the posting of account agreements on websites. Meanwhile, credit products related to a prepaid account would be subject to rules governing credit
cards under Regulation Z, including ability-to-repay requirements. Consumers would have to consent to an overdraft service first and be given at least 21 days to repay debt.

While providers and industry representatives, along with customers, expressed concern about the effects of the overdraft restrictions, some consumer advocates — in both interviews and comment letters — said the proposal would not go far enough.

"The rules will make credit more honest and affordable but we would like to see those overdraft features banned entirely," Lauren Saunders, associate director of the National Consumer Law Center, said in an interview.

"Although there are a number of protections in the proposal on overdraft charges, credit should be entirely separate so that consumers do not accidentally access it through overdraft when they would prefer to skip the purchase or pay in cash. For other credit features that are not accessed through overdraft, the proposal ensures that consumers can afford to repay the credit, but there are loopholes where institutions can evade the rule."

The comment letters, which numbered into the thousands, were due to the agency last month. The vast majority were short entries from prepaid card customers, explaining how they rely on overdraft protection for everyday purchases and would not want to see that option go away. For example, Lynn Wood, a prepaid card user, said, "I believe that I have the right to choose the overdraft protection. It allows my financial freedom and helps control my spending. Why should I be denied that option?"

While many observers say only a few prepaid card issuers offer overdraft features, industry representatives warn the added requirements in Regulation Z for those products could eliminate overdraft protection from the prepaid market. Basically, the cost of compliance would not be worth it, they said.

"We have serious concerns about many of the policy decisions made by the bureau such as the breadth of prepaid products covered by the proposed rule, the redundant disclosure requirements and the decision to place overdraft features under Regulation Z, which greatly threatens the continued viability of an increasingly popular consumer product," said Brad Fauss, interim executive director and general counsel at the Network Branded Prepaid Card Association.

Others groups, however, said the CFPB struck a good balance, particularly in addressing overdraft. The CFPB also proposed banning automatic withdrawals from a linked checking account — to repay debt associated with a prepaid card — without a consumer's consent, partly over concerns that overdraft fees could rack up in the process.

"The most important part is that this proposal tackles the problem of overdraft," said Thaddeus King, officer of the consumer banking project at The Pew Charitable Trusts. "In the proposal, the CFPB is treating overdraft as a credit, which is how it should be treated."

While the industry largely expected overdraft to be a part of the prepaid rule, one area that took many by surprise was how the CFPB included digital currencies within its definition of a "prepaid account."

Though the CFPB only mentions virtual currencies in the definition section of the proposal, observers said it could mean currencies like Bitcoin would now become subject to Electronic Fund Transfer Act
requirements, known as Regulation E, which are included in the proposal.

The CFPB’s prior research on prepaid accounts “took two years and nowhere during that time was there any mention of virtual currencies,” Peter Van Valkenburgh, director of research at the Coin Center, a non-profit advocacy group for virtual currencies like Bitcoin, said in an interview. “While we expect regulators will study and address regulation on virtual currencies, I don’t think anyone suspected virtual currencies would be swept into rulemaking on prepaid products.”

He added, “We are concerned about the procedural fairness in the rulemaking and what the substantive requirements under Regulation E would mean for Bitcoin, and whether that’s a good fit in a prepaid card rule.”

Outside of virtual currencies, many in the industry argue that an overly broad CFPB definition for prepaid cards would simply destroy certain products offered by companies that could not afford the compliance obligation.

“A one-size-fits-all approach to regulating the more than 15 separate categories of prepaid card products could have the unintended consequence of eliminating entire product categories from the market, especially those products that cannot afford to bear the costs and heavy compliance burdens imposed by the proposed rule,” Fauss said.

However, consumer groups have largely agreed with the CFPB’s broad approach in defining a prepaid account.

"The CFPB is being prudent by not limiting its definition of prepaid accounts based on the market structure that is most common today, which is a card-based product issued through an insured financial institution," Pew said in its 21-page letter. "There are already products on the market that are not based on a card — such as PayPal and Google Wallet — that allow for the storage of funds and can be used in many different ways, very similarly to traditional [general purpose reloadable] prepaid cards."

Pew, along with many other consumer groups, also continued to push the CFPB to include a requirement that prepaid accounts be federally insured. The CFPB did not include this in its proposal.

Yet consumer and industry groups agreed that the agency’s proposed disclosure requirements need revisions. The CFPB is considering requiring that prepaid card issuers disclose certain fees in two forms: a "short" form and a longer form providing additional details.

Some in the industry are calling for a simpler approach with just one form covering all the requirements. Consumer groups, meanwhile, say certain needed details would be missing under the CFPB proposal while other unnecessary information could be dropped.

Pew is suggesting that the final rule require more detail about a customer’s account balance on the short form, such as how quickly the cash will load and when direct deposits would be made available to consumers.

"People want to know how long it will take to get their money and the proposal didn't include that on the short form or the long form disclosures," said Susan Weinstock, director of the consumer banking
Other concerns include when the rule will become effective. The CFPB proposed to give the industry nine months from when the final rule is published to comply, but industry advocates want a longer period.

"Based on the number of changes required for card packaging and websites, the level of software development necessary to calculate transactions and fees in the manner described in the proposed rule … our members believe that between 18 and 24 months is a much more appropriate time frame to implement the required changes from such a broad sweeping new regulation," said the Network Branded Prepaid Card Association in its 94-page comment letter.