

# DON'T LOOK A GIFT CARD IN THE MOUTH: BEWARE OF LIABILITY UNDER THE ELECTRONIC FUND TRANSFERS ACT

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## Financial Institutions and Services Litigation Alert

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Many of us have had a similar experience. We receive a gift card, put it in a "safe" place with other gift cards, and forget it exists. Inevitably, we uncover the gift card and find ourselves asking questions such as: Does this card still have any value? Has it expired? Can it expire? Will I be charged a fee for use (or non-use)? Should I call the 800 number? The experience invariably ends by putting the card aside and promising to deal with it later. But, what really does happen to the value of those cards?

Gift cards issued by retailers and other merchants are prevalent throughout the United States. They are given and received by consumers for birthdays, holidays, and other events year-round. Retailers provide them as part of special promotions, in exchange for returns of merchandise, and for customer service purposes. The popularity and widespread use of gift cards continue to increase.

Reports indicate that in 2015, gift card sales in the United States alone totaled an estimated \$130 billion.<sup>[1]</sup> A survey by the National Retail Federation found that gift cards were "the most requested gift" during the holiday seasons for the past nine years in a row.<sup>[2]</sup> Moreover, a recent study conducted by the Wharton School Baker Retailing Center and the NPD Group found that gift cards are very popular with so-called "Millennials,"<sup>[3]</sup> who make up approximately one-third of the United States population and "are the largest and youngest shopper generation."<sup>[4]</sup> These reports highlight the importance of gift cards to retail merchants' businesses.

As an integral part of many merchants' businesses, assessing potential liability in developing and implementing gift card practices is critical and worthy of frequent review. While gift cards and related products are subject to a variety of state laws and regulations, this alert focuses primarily on the overarching provisions of federal law as codified in the Electronic Fund Transfers Act ("EFTA")<sup>[5]</sup> and Regulation E.<sup>[6]</sup>

## BACKGROUND

In May 2009, Congress passed the Credit Card Accountability Responsibility and Disclosure Act of 2009 (the "CARD Act").<sup>[7]</sup> The CARD Act, in relevant part, amended the EFTA<sup>[8]</sup> to add sections addressing and governing the use of gift cards.<sup>[9]</sup> Those amendments became effective on August 22, 2010,<sup>[10]</sup> and apply only to gift cards sold or provided to consumers on or after August 22, 2010.<sup>[11]</sup> Regulation E was later amended and new regulations promulgated to implement the gift card provisions of the EFTA.<sup>[12]</sup>

The EFTA applies to three separate, yet-related gift card products: "general-use prepaid cards," "gift certificates," and "store gift cards."<sup>[13]</sup>

First, "general-use prepaid cards" are cards, payment codes, or payment devices that are (1) "redeemable at multiple, unaffiliated merchants or service providers," (2) "issued in a requested amount, whether or not that amount may . . . be increased in value or reloaded," (3) "purchased or loaded on a prepaid basis," and (4) "honored . . . by merchants for goods or services."<sup>[14]</sup> These are also referred to as "open-loop" gift cards, and they tend to run on credit-card-based systems. The most common examples would be Visa or MasterCard prepaid gift cards.

Second, "gift certificates" are electronic promises that are (1) "redeemable at a single merchant or an affiliated group of merchants" (2) "issued in a specified amount that may not be increased or reloaded," (3) "purchased on a prepaid basis in exchange for payment," and (4) "honored . . . by such single merchant or affiliated group of merchants for goods or services."<sup>[15]</sup>

Third, "store gift cards" are electronic promises, plastic cards, or other payment codes or devices that are (1) "redeemable at a single merchant or an affiliated group of merchants," (2) "issued in a specified amount, whether or not that amount may be increased in value or reloaded," (3) "purchased on a prepaid basis in exchange for payment," and (4) "honored . . . by such single merchant or affiliated group of merchants for goods or services."<sup>[16]</sup>

Store gift cards and gift certificates are the traditional form of single retailer (or affiliate retailers) gift card, and are also known as "closed-loop" cards. While similar in most respects, the key distinctions are clear. Both a store gift card and a gift certificate are redeemable only at one merchant (or one family of affiliated merchants), whereas a general-use prepaid card is redeemable at multiple, unaffiliated merchants. However, consumers can increase the value of store gift cards and general-use prepaid cards, whereas the value of a gift certificate cannot be increased. We also note that open-loop, general-use, prepaid cards raise a number of practical and legal issues not directly confronted by the closed-loop cards. While those issues are not the subject of this alert, we will address these and other related subjects in future publications. Otherwise, these three products differ only in form and method of transmission.<sup>[17]</sup> We will refer to all three products collectively as "gift cards."

## RESTRICTIONS AND DISCLOSURES UNDER THE EFTA: DORMANCY FEES, SERVICE FEES, AND EXPIRATION DATES

The EFTA restricts three general practices concerning issuance of gift cards. Those are: (1) charging dormancy or inactivity fees; (2) charging service fees; and (3) setting expiration dates.<sup>[18]</sup> Each is discussed below.

### Dormancy, Inactivity, and Service Fees

The EFTA treats dormancy fees, inactivity fees, and service fees similarly. A dormancy or inactivity fee is defined as any "fee, charge, or penalty for non-use or inactivity of a" gift card.<sup>[19]</sup> A service fee is defined as "a periodic fee, charge, or penalty for holding or use of a" gift card.<sup>[20]</sup> The EFTA prohibits the assessment of either type of fee, except in limited circumstances.<sup>[21]</sup>

A merchant may charge a dormancy, inactivity, or service fee only where (1) the consumer has not used the gift card for at least a 12-month period, (2) the merchant has complied with the EFTA's disclosure requirements, (3) the merchant does not charge more than one fee in any given calendar month, and (4) the merchant complies with any additional requirements established by the Consumer Financial Protection Bureau ("CFPB").<sup>[22]</sup>

To satisfy the EFTA, a merchant must disclose the existence of such fees at least twice.<sup>[23]</sup> First, the gift card itself must "clearly and conspicuously" state that a fee may be charged, the amount of the fee, how often the fee may be charged, and that such fee is assessed for inactivity.<sup>[24]</sup> The gift card must also display a telephone number and, if maintained, a website, that a consumer may use to obtain information about any chargeable fees.<sup>[25]</sup> Second, the merchant must inform the purchaser of the potential charges and fees **before** the gift card is purchased, regardless of the manner of purchase (whether in person, over the Internet, or by telephone).<sup>[26]</sup>

To view the full alert, [click here](#).

#### Notes:

[1] See Denise Dahlhoff, *Gift Cards' Appeal to Millennials*, RETAILING TODAY.COM, Feb. 19, 2016, at 2 (available at <http://www.retailingtoday.com/article/gift-cards-appeal-millennials>).

[2] *Id.* (citing National Retail Federation Survey at <https://nrf.com/media/press-releases/early-promos-great-deals-put-traditional-gift-card-buyers-gift-wrapping-mode>).

[3] Millennials are roughly defined to include individuals born in the early 1980s through the early 2000s (*i.e.*, 1982-2004). See Wikipedia, at <https://en.wikipedia.org/wiki/Millennials>.

[4] Dahlhoff, *Gift Cards' Appeal to Millennials*, at 2; see also Denise Dahlhoff and Sarah Wittenborn, *Exploring Cross-Generational Buying Behavior at a Time of Complex Change in Retail Landscape*, A Joint Report by the NPD Group and the Baker Retailing Center at the Wharton School (February 2006), at 3-4 (available at <https://bakerretail.wharton.upenn.edu/research-publications/publications/consumer-studies/>).

[5] See 15 U.S.C. §§ 1693, *et seq.*

[6] See 12 C.F.R. §§ 1005.1, *et seq.* (regulations issued by the Consumer Financial Protection Bureau ("CFPB")); 12 C.F.R. §§ 205.1, *et seq.* (regulations issued by the Board of Governors of the Federal Reserve System). The two sets of regulations are substantively identical, and the subsections in each set of regulations match up closely. For ease of reference we will cite to the CFPB regulations herein.

[7] Credit Card Accountability Responsibility and Disclosure Act of 2009, Pub. L. No. 111-24, 123 Stat. 1734 (2009).

[8] The EFTA is a consumer protection statute that is designed to "provide a basic framework establishing the rights, liabilities, and responsibilities of participants in electronic fund and remittance transfer systems." 15 U.S.C. § 1693(b).

[9] See *id.* at 1751-1754, §§ 401-403.

[10] *Id.* at 1754, § 403 (the EFTA amendments become effective "15 months after the date of enactment" on May 22, 2009).

[11] 12 C.F.R. § 1005.20(g)(1) ("the requirements of this section apply to any gift certificate, store gift card, or general-use prepaid card sold to a consumer on or after August 22, 2010, or provided to a consumer as a replacement for such certificate or card").

[12] See *generally* 12 C.F.R. § 1005.20.

[13] See 15 U.S.C. § 1693l-1.

[14] *Id.* § 1693I-1(a)(2)(A).

[15] *Id.* § 1693I-1(a)(2)(B).

[16] *Id.* § 1693I-1(a)(2)(C).

[17] Notably, the EFTA expressly exempts from the definitions of "general-use prepaid cards," "gift certificates," and "store gift cards," a number of different categories of similar products, including, but not limited to, devices used solely for telephone services, reloadable cards not marketed or labeled as a gift card or gift certificate, and a loyalty, award, or promotional gift card. See 15 U.S.C. § 1693I-1(a)(2)(D). While exempted from the EFTA definitions, Regulation E provides for certain required disclosures for "loyalty, award, or promotional gift card[s]." See 12 C.F.R. § 1005.20(a)(4).

[18] See *generally* 15 U.S.C. § 1693I-1.

[19] *Id.* § 1693I-1(a)(1).

[20] *Id.* § 1693I-1(a)(3)(A). A "service fee" does not include "a one-time initial issuance fee" for a general-use prepaid card. *Id.* § 1693I-1(a)(3)(B).

[21] See *id.* § 1693I-1(b) ("Except as provided under [the EFTA], it shall be unlawful for any person to impose a dormancy fee, an inactivity charge or fee, or a service fee with respect to a gift certificate, store gift card, or general-use prepaid card.").

[22] *Id.* § 1693I-1(b)(2).

[23] 15 U.S.C. § 1693I-1(b)(3).

[24] *Id.* § 1693I-1(b)(3)(A).

[25] See 12 C.F.R. § 1005.20(f)(2). Notably, Regulation E also requires certain disclosures be contained on the gift card with respect to fees other than dormancy, inactivity, or service fees, including information regarding the type of fee, the amount of the fee or its method of calculation, and the conditions under which the fee may be assessed. See *id.*

[26] See 15 U.S.C. § 1693I-1(b)(3)(B).

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