

White Paper

Achieving Prepaid Compliance in a Financial Institution: Partnerships are Key



CONVENIENT CARDS

Contents

Executive Summary 1

Introduction: Prepaid and Compliance 1

The Compliance Challenge 2

The Argument for Partnership Dependability 2

The Convenient Cards Approach: Teamwork Without the Work 3

What Every Financial Institution Needs to Know 5

Conclusion 6



Executive Summary

With the rapid expansion of the prepaid market over the past decade, it is no surprise that consumers and corporate clients alike are increasingly expecting their financial institutions to provide prepaid solutions as extensions to their existing product portfolios. Just as with credit cards, ATM's, direct deposit, and online banking, prepaid products have become the next generation of peripheral offering. With humble roots in the simple products like gift cards, prepaid programs now serve a multitude of needs, such as payroll cards, general purpose reloadable cards, travel cards, corporate expense cards, and more. Consumers are using prepaid cards for everything from online shopping, to gift giving, to covering student expenses. Businesses are finding new efficiencies with the use of payroll cards to increase the adoption of electronic payroll and prepaid employee spending cards to reduce credit risk.

Financial institutions (FI's) have been quickly moving to keep product portfolios relevant, provide solutions that customers are expecting, and prevent large retail stores from enticing away entire segments (or generations) of their customer base. Add in the additional revenue streams and viable turn-down solutions, and it's difficult to see how a financial institution wouldn't benefit from having a robust suite of prepaid products at its disposal.

Despite all of the positives to adopting a quality prepaid program, some financial institutions have genuine concerns about the regulatory environment in which prepaid cards operate, and what the cost and risk is to maintaining such a program. After all, it's always good to serve customers well, but not at the expense of examiner complications. The unfortunate consequence is that compliance concerns have slowed some financial institutions from adopting prepaid, forcing customers to find desired prepaid solutions in the relatively unregulated and unmonitored retail world, instead of at well-regulated and safe financial institutions. Personal customer information such as names, addresses, and Social Security Numbers are being amassed by convenience stores and retail locations. These customers are losing the protections of sound banking practices. Retail clerks are not held to the same AML and KYC standards as the average employee at a financial institution.

The question then becomes, "What is the most efficient and reliable way to both serve consumers and business customers with products they are demanding, and provide them with the protections of the established practices of the financial services market, while maintaining a compliant program?" The solution rests in finding a prepaid card program provider that understands the environment in which financial institutions operate, keeps a vigilant watch on the laws and examiner expectations, and proactively keeps you informed. The Convenient Visa Prepaid Card Program is specifically designed for financial institutions, and manages most of the compliance burden, while providing current guidance and Best Practices for the elements that remain within the scope of its financial institution clients. With years of experience serving hundreds of financial institutions, Convenient Cards is uniquely positioned to serve as a trusted partner for high-quality, compliant prepaid solutions.

Introduction: Prepaid and Compliance

As prepaid cards have become mainstream financial service products, regulations and restrictions have grown in scope and are now similar to regulations and restrictions on more traditional financial service products. What can get a little complicated is that not all prepaid products follow the same rules. Laws and rules around prepaid often get applied to program categories, such as "gift cards" or "general purpose cards" or "payroll cards". Although there are some umbrella laws that are inherent to the sale of any negotiable instrument, each prepaid category has specific requirements that develop as a result of how each category is



used by the cardholder. For example, gift cards - with small balances, no cash access, and limited functionality - do not carry the same money laundering risk as General Purpose Reloadable (GPR) cards that have multiple reload networks, cash access, and online transfers. Accordingly, the money laundering requirements for gift cards are not as strict as those for General Purpose Reloadable (GPR) cards. This only makes sense. That doesn't mean that GPR cards are a risky product offering, but rather, it highlights the importance of understanding the rules and potential opportunities that apply to each card type.

In addition to the legal environment, good compliance standards also demand an understanding of contractual obligations. All the major card networks (Visa, MasterCard, and Discover) have rules that govern the proper marketing and use of products that belong to their brand. The network rules usually dictate the types of transactions allowed on different types of cards, how collateral (such as marketing materials, card plastic, and carriers) should be presented, card balance and cardholder registration requirements, and more.

As with the management of an inventory of any negotiable instrument, prepaid cards also have compliance and operational implications. Proper inventory management procedures, card load/reload system access, sensitive data management, and the like all need to be considered as part of the compliance arena. Disclosure requirements vary by product type, as established by regulations such as Reg. AA (Unfair or Deceptive Acts or Practices "UDAP") and Reg. E (Electronic Fund Transfer Act).

State laws add another layer of regulation on some prepaid card products that must also be considered. Most states have certain requirements for payroll cards defined in their payroll or wage statutes. A few states even have specific expectations defined for gift cards. It is critical to understand individual state laws and how they pertain to each card program.

The Compliance Challenge

Independently maintaining a compliant prepaid program can clearly be a costly and overwhelming task for small to mid-sized financial institutions (FI's), especially given the wide scope that "compliance" encompasses. At the same time, offering robust prepaid solutions is a necessity for any financial institution to remain relevant and survive in the rapidly-changing financial services landscape. In fact, many small to mid-sized financial institutions have been offering their customers prepaid cards for many years, despite the compliance complexity of prepaid card programs. And they have successfully navigated the compliance challenge. How have they done it? Clearly, the economics of smaller financial institutions don't allow them to have large staffs dedicated solely to mitigating prepaid card program compliance risk. The answer is simple: most have partnered with prepaid card program providers who both manage the majority of the compliance responsibility and provide support and guidance for the remaining tasks.

While financial institutions cannot offload the entire compliance burden, they can offload the prepaid-specific compliance to prepaid experts. At the same time, they can maintain responsibility for the types of compliance that they are already doing, such as BSA (Bank Secrecy Act) reporting and KYC (Know Your Customer) standards that will ultimately fall to the customer-facing staff that have the ability to have an effect on fraud and money laundering. When selecting a prepaid card program provider to be a partner in compliance, it is important to ensure that they not only have the prepaid expertise, but that they understand how financial institutions manage compliance in general. This will help to ensure that the prepaid card program compliance fits seamlessly into the organization.



The Argument for Partnership Dependability

There are several benefits to identifying and partnering with prepaid industry experts, and many of those benefits are related to compliance. With the correct prepaid partnership in place, compliance should be managed with very little effort, cost, or risk. It is important to note, however, that not all prepaid companies are focused on the same objective. Some companies have established an excellent reputation with consumers for the products they offer in a retail environment, but they have no experience offering those same prepaid cards in financial institutions. Other companies are well-known to offer a single product in financial institutions, but cannot provide their clients with a full suite of prepaid solutions to address the many different needs of consumer and corporate customers. Still other companies are known to serve financial institutions, but have an unfocused approach to compliance. So, it is not enough simply to have a prepaid partner. It is essential to partner with an organization that has experience and a solid reputation for addressing the organizational needs and goals at hand. Without exception, where compliance is concerned, focus and experience are two very critical elements to any successful partnership.

Once the correct prepaid partner has been identified, they can quickly help to implement a prepaid solution that fits the short- and long-term needs of their client financial institutions. Not all FI's operate the same, and so a "one-size fits all" approach rarely works. Each company has a different set of customer needs, and different experiences with examiners. Some FI's have experience with prepaid cards, and for others, this is an entirely new arena. It is the role of the prepaid partner to proactively identify each client's individual compliance strengths and weaknesses as they pertain to the prepaid products being offered. It is also the role of the prepaid partner to keep clients current on industry events, so that compliance can be addressed proactively, rather than reactively.

Finding an effective prepaid partner that can harness the experiences and feedback of a large financial institution client portfolio multiplies the compliance reliability for each one of the clients. For example, a prepaid program manager that works with three mid-sized financial institutions has a level of experience, and each of those three clients will benefit from the experiences of the other two, provided the program manager is properly disseminating that information. At the other end of the spectrum is the prepaid program manager that works with hundreds of financial institutions of varying sizes from coast to coast. Provided compliance is a priority for their business model, that program manager is now in a position to provide each individual client with the benefit of the compliance experiences of hundreds of other FI's. That's a powerful tool for the small to mid-sized financial institutions that are looking to roll out anything from a simple gift card program to a more complete prepaid portfolio addressing a variety of customer needs.

The Convenient Cards Approach: Teamwork Without the Work

After serving hundreds of financial institution clients for more than five years, Convenient Cards is uniquely positioned to offer clients a prepaid solution that emphasizes compliance and simplicity. The Convenient Visa Prepaid Card Program provides a full suite of prepaid products that financial institutions can use to strengthen existing customer relationships and develop new opportunities. It is the company's belief that the products are important, good service and support is vital, and compliance is essential. By fostering partnerships with clients, rather than simply building client rosters, Convenient Cards has been able to understand the unique compliance requirements facing financial institutions, and develop products, systems, and support materials that speak exclusively to this environment. A constant and proactive attention to the prepaid regulatory environment, keen appreciation for client and examiner feedback, and industry-leading business partnerships have allowed



the company to establish an excellent reputation for strict compliance and open client communication.

Regulation E – Over the years, Reg. E has become more and more applicable to the prepaid industry. This particular regulation has grown to impact different program categories (gift, GPR, payroll, etc.) differently. An entire section of Reg. E is devoted exclusively to gift cards. What fees can be charged, when they can be charged, expiration dates, and disclosures are all addressed in detail. Payroll cards have another section specifically discussing how the regulation applies to them. GPR cards that permit the electronic deposit of Government benefits have certain Reg. E protections. More recently, the Consumer Financial Protection Bureau (CFPB) began exploring a more universal application of the regulation to GPR cards. All of the cards offered by Convenient Cards are in full compliance with the applicable sections of Regulation E.

Reg. II – In April 2013, the prepaid card industry hit the compliance date requiring that all debit cards permit transactions to be processed on two unaffiliated networks. Many prepaid card program providers were in a panic, scrambling for solutions, and many did not make the deadline. Convenient Cards' prepaid card programs achieved full compliance by permitting transactions on both the Visa and Pulse networks.

The Federal Trade Commission Act – As with any financial service product, prepaid cards require full disclosure of program terms prior to the card sale. By partnering with clients and with the insight of FDIC examiners, Convenient Cards developed card carriers with a perforated "Statement of Acknowledgment", which cardholders sign. Clients can keep these signed statements, which prove to examiners that proper prior disclosures have been made, thus avoiding any Unfair and Deceptive Acts and Practices (UDAP) findings.

CIP and OFAC Screening – Only prepaid programs with certain functionality require CIP and OFAC verification of cardholders. The system (CC Studio) used to activate, load, and register cards in the Convenient Visa Prepaid Card Program automatically manages both cardholder verification and OFAC screening on the fly. Before the cardholder is even given their card, this process will be completed. Cardholder information is currently being verified against Experian. If the verification or OFAC query fails, the sale transaction will not be completed without contacting Convenient Cards for additional assistance. For an override to be processed (managed on a case-by-case basis), the issuing bank requires that Convenient Cards first obtains a scanned image of government-issued photo ID from the cardholder, and keeps that on file.

Card Inventory Management – With each shipment of cards, Convenient Cards sends an itemized detail of cards shipped. This provides a simple starting point to manage and audit inventories with a quick comparison to cards sold.

Remittance Transfers – The card programs in the suite of products offered by Convenient Cards limit functionality in such a manner as to render the new Remittance Transfer requirements inapplicable.

PCI Compliance – With the reloadable cards provided in the Convenient Visa Prepaid Card Program, the cards are registered with cardholder information at the time of sale. Undoubtedly, this level of customer information is very sensitive and needs to be properly protected using the most current IT security standards. Convenient Cards has partnered with an industry-leading processor that manages all cardholder data in accordance with these practices. They are PCI-certified and regularly verified by the major networks.

The cards offered as part of the Convenient Visa Prepaid Card Program are all issued by a



Federally regulated financial institution. That provides even further benefits to the cardholders, and increased compliance security for financial institution clients. All of the cards offered in the suite of products provide the cardholder with pass-through FDIC insurance. As the issuing bank for the cards is regulated by the Office of the Comptroller of the Currency (OCC), and subject to FDIC exam, the card programs, collateral, and business partners are always in full compliance with regulatory and industry requirements.

Another aspect of the Convenient Cards approach that aids FI clients in maintaining a compliant program is proactive communication. As information regarding prepaid industry or regulatory events becomes available, updates are issued to all clients. The easiest way to ensure full compliance is to know the rules. Again, by utilizing its extensive client portfolio, Convenient Cards is well-positioned to ensure program compliance on the back end, and keep clients on the front lines updated with any pertinent information they need to know for customers and examiners.

The role of a strong prepaid partner for financial institutions is not only to understand the rules governing prepaid cards, but also to help clients prepare for and respond to examiner inquiries. It's a partnership that is based on open communication, proactive attention, and a constant effort to stay current in the financial services industry. A partnership with Convenient Cards ensures this level of teamwork, without clients having to constantly ask for help and information. It's a partnership that brings the knowledge and experiences of hundreds of financial institutions across the United States together, and allows each client a level of prepaid expertise that would be unachievable alone, without enormous amounts of time, effort, and expense. That's the reason that compliance in the Convenient Visa Prepaid Card Program is all about teamwork without the work.

What Every Financial Institution Needs to Know

There are certain compliance responsibilities that any financial institution offering prepaid needs to consider, regardless of partnership. However, in all cases, with the right prepaid partner, these tasks should work seamlessly into existing policies and procedures. FI's will want to work prepaid into their operations manuals, but, rather than rewriting the book, should be able to add the program into existing sections.

Know Your Customer (KYC) – Tellers need to ensure that, if they are registering a card to Tom Smith, Tom Smith is standing in front of them with acceptable ID (or equivalent KYC standard). There isn't any new policy that needs to be developed for this. KYC is a basic principle to mitigating money laundering activities, and in most cases, many customers are known to branch staff from years of service. But KYC means more than just identification. Knowing the customer's intended uses for the cards and what their normal behavior would be are core competencies for customer-facing FI staff. This information is important to understanding any anomalous behavior, but it's also basic customer service to ensure the customer gets the correct card product for their need (gift, GPR, travel, etc.).

Bank Secrecy Act (BSA) Reporting – This is another existing policy/procedure at every FI in the United States. FinCEN (Financial Crimes Enforcement Network) already has established reporting requirements for high-currency or suspicious transactions. Reporting is the same for prepaid card sales and loads as for any other transaction which branch staff is to complete.

Card Inventory Management – It is advisable that financial institutions maintain an inventory log, which tracks card sales activity. The majority of FI's using this technique are currently tracking purchaser name, the type of card (gift, GPR, travel, etc.), the date of sale (or disposition), the method of payment (cash, account debit, etc.), and the person signing out



the card (dual-control is of course advisable). Although some of this information is already available through system-level reporting, the system only knows about transactions attempted. This independent log is intended to track inventory each time a card is added or removed from the supply, rather than only those cards that have actually been sold. This practice significantly reduces the risk of stray inventory, which may have fallen behind a drawer, or possibly a customer intended to buy a card but changed their mind. Keeping an accurate log certainly helps with inventory management, but also sales/account reconciliation, General Ledger (GL) balancing, teller differences, and BSA reporting.

Disclosure Practices – As with any item sold at a financial institution, full program disclosure must be made prior to the sale transaction. Examiners of course look for this, and it is absolutely good customer service to let customers know about products prior to making any commitment. Most prepaid programs simply provide disclosures which can be presented to customers to read prior to making a card purchase. As discussed earlier in this White Paper, The Convenient Visa Prepaid Card Program has specifically designed materials which aid in disclosure presentation, enhance customer understanding, and when necessary, provide a documented history of proper disclosure practices.

After reviewing the above list, it quickly becomes apparent that the essential compliance activities that cannot be removed from the purview of responsibility for financial institutions are very intuitive and easily managed. None of these items should present any FI with a new chapter in their policy manual. Each item is already inherent to sound banking practices and requires only the application to prepaid, rather than new adoption and rollout. However, it is worth noting that only by partnering with a reputable prepaid company that has solid experience serving FI's is it possible to limit the scope of compliance obligation to such a basic and manageable list. As levels of experience and reliability are stripped away from the prepaid partner, additional responsibilities must inevitably become the burden of the FI.

Conclusion

Prepaid card programs are becoming increasingly more important to businesses and consumers alike, and that trend shows no sign of slowing. The role of prepaid card programs varies depending upon the type of retailer that is offering them. Because of their consumer draw, non-traditional financial service provider retail locations are using them to lure in new customers and generate revenue. Financial institutions are using them to ensure their relevance to new generations of customers, generate revenue, keep product offerings current, and prevent retailers from tempting away their customers. The importance of prepaid card products to FI's and their customers is reflected in the rapid adoption of card programs amongst financial institutions and the explosive growth of cards being issued. Given the highly-regulated and monitored environment in which financial institutions operate, it is imperative that they select a reputable prepaid partner that is experienced in navigating their specific waters. Beyond experience though, it is also critical that the prepaid partner be focused not only on compliance of the card programs, but also the unique compliance needs of their financial services clients. With the Convenient Visa Prepaid Card Program, Convenient Cards has been serving this role for financial institutions since 2007. At the heart of the success of this program is a sound portfolio of products, outstanding client support and customer service, and the industry standard for compliance. Convenient Cards is uniquely positioned in the prepaid market to harness the compliance practices and experiences of hundreds of financial institutions, thus ensuring that each client benefits from the combined knowledge-base. Through strong partnerships like this, even small to mid-sized financial institutions can easily manage the compliance of a prepaid program, thus ensuring the benefits for them and their customers.