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Developments in the Law Concerning Stored-Value Cards and Other Electronic Payments Products

By Sarah Jane Hughes, Stephen T. Middlebrook, and Broox W. Peterson*

Stored-value and other electronic and Internet payments products are joining credit and debit cards in replacing a significant number of cash transactions in the economy.¹ Wal-Mart's announcement in June 2007 that it plans to offer reloadable prepaid or stored-value cards using technology and services from Green Dot MoneyPack and GE Money Bank could be a dramatic step in that direction.² In addition, Wal-Mart plans to allow individuals to load and reload their paychecks onto

* Members of the Electronic Payments Working Group, Committee on Cyberspace Law, Section of Business Law, American Bar Association. The Working Group thanks the Indiana University School of Law-Bloomington and three members of the class of 2007—Kevin M. Halter, Jennifer Rodibaugh, and Robert Van Wert—for research support for this Survey.

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The authors invite readers to direct questions on each part of this Survey to the individual author named above as being primarily responsible for its content. Copies of many of the documents cited in this Survey may be found on the Electronic Payments Working Group's web page at http://www.abanet.org/dch/committee.cfm?com_CL320040.

1. See Robert J. Samuelson, *The Vanishing Greenback*, NEWSWEEK, June 25, 2007, at 35.

2. Marc Hochstein & William Launder, *Green Dot To Reload New Wal-Mart Card*, AM. BANKER, June 8, 2007, <http://www.americanbanker.com/article.html?id=200706072H318PM1>. The article reports that Green Dot's MoneyPak technology is sold at more than 40,000 retail locations in the United States. *Id.*

new Wal-Mart card products for a one-time fee of \$8.94, which buys the card.³ An additional monthly service fee of \$4.94 will apply in any month in which the cardholder fails to place \$1,000 or more on the card.⁴ Reloads accomplished through check cashing at Wal-Mart or direct deposit are free of charge, but reloads accomplished by other means will cost \$4.64 each.⁵ As one commentator summed it up, “there is no supply chain, product chain or merchandise management issue there. It is just cash and digital cash. There’s money to be made in money.”⁶ Indeed, it is probable that Wal-Mart can make more money selling prepaid cards than in selling low-price consumer products.⁷ Issuers expect that prepaid cards will increase in popularity, in part because approximately 28 million people in the United States—or nine percent of the population—do not maintain bank accounts.⁸ Wal-Mart’s inexpensive, reloadable stored-value cards will offer a widely available alternative to the conventional deposit account.

In last year’s Survey (“2006 Survey”), we presented developments in the law pertaining to stored-value cards and other prepaid products from 2002 through roughly May 31, 2006.⁹ This year, we have expanded the scope of our Survey to encompass developments in Internet payments, other non-paper based payments such as “demand drafts,” and e-gold transfers. Despite the fact that only one year has passed since our 2006 Survey on stored-value cards, there have been significant developments in each of the subject areas it covered. Our goals for this Survey are much the same as for the 2006 Survey: we want to present salient developments in a fashion that will be helpful to general practitioners as well as specialists who want to stay abreast of developments in payments and e-commerce.

Readers of the 2006 Survey will recall that we discussed the Federal Deposit Insurance Corporation’s extension of deposit insurance to payroll and gift cards.¹⁰ We also covered the Federal Reserve Board’s extension of Regulation E to cover payroll cards.¹¹ The second part of the 2006 Survey discussed recent state laws and regulations covering the terms and conditions of gift cards and the use of payroll cards to discharge wage and salary obligations.¹² It also gave a comprehensive listing of state laws pertaining to gift cards, payroll cards, and a brief update on Anita

3. Ylan Q. Mui, *Wal-Mart Expands Banking Services*, WASH. POST, June 21, 2007, at D1.

4. *Id.*

5. *Id.*

6. *Wal-Mart’s Digital Money Card*, DIGITAL MONEY WORLD, June 12, 2007, <http://www.digitalmoney-world.com/wal-marts-digital-money-card/> (quoting bbcamerican.blogspot.com).

7. Posting of Ron Galloway to The Huffington Post, The Blogs, http://www.huffingtonpost.com/ron-galloway/how-walmart-got-its-bank_b_54530.html (July 1, 2007, 4:24 PM EST).

8. Kathy Chu & Jayne O’Donnell, *Wal-Mart To Offer Payment Cards: Prepaid Visa-Branded Cards To Target Customers Who Don’t Have Bank Accounts*, USA TODAY, June 7, 2007, at A1 (citing statistic from the Federal Deposit Insurance Corporation).

9. See Sarah Jane Hughes, Stephen T. Middlebrook & Broox W. Peterson, *Developments in the Law Concerning Stored Value and Other Prepaid Payment Products*, 62 BUS. LAW. 229 (2006) [hereinafter “Hughes, Middlebrook & Peterson, 2006 Survey”].

10. *Id.* at 231–35.

11. *Id.* at 235–38.

12. *Id.* at 239–43.

Ramasastri's 2001 Survey of Cyberspace Law article on escheat statutes.¹³ The third part took on the task of describing the ongoing battles between the states and federal bank regulators over federal preemption and, more specifically, over who should regulate stored-value cards issued by or in conjunction with federally chartered depository institutions and their wholly owned subsidiaries.¹⁴

This year's Survey takes up some of these subjects, and adds a few new subjects as well. Part I addresses developments since our 2006 Survey in state gift and payroll card laws. Part II updates developments concerning the federal regulation of federally chartered financial institutions, particularly the U.S. Supreme Court's April 2007 ruling in *Watters v. Wachovia Bank, N.A.*,¹⁵ which favored federal preemption. The Supreme Court reaffirmed the precedent establishing that federal regulators of federally chartered financial institutions have exclusive visitorial rights—that is, rights to examine, supervise, and enforce both state and federal laws—over those institutions and their subsidiaries.¹⁶ The *Watters* opinion is directly relevant to the attempts by state regulators to apply their own states' consumer protection regulations to gift cards and other payments products offered by federally chartered depository institutions, their subsidiaries, and their business partners. *Watters* leaves a smaller number of depository and non-depository entities subject to state enforcement of the new laws regulating these products being enacted by state legislatures. Part III covers important developments involving other electronic payments systems including the federal prosecution of e-gold Ltd., which is a payments and stored-value provider; the U.S. Federal Trade Commission's action against and subsequent consent decree with Kmart and Darden Restaurants, Inc. over their gift card programs; and this year's developments in the federal injunction action against Payment Processing, LLC, a non-depository provider of payments processing to telemarketers. This part also covers other e-currency, Internet, and electronic payments issues, including (1) emerging concerns about the variable definitions of what constitutes a "money transmitter" for purposes of federal law, (2) enactment of the Federal Unlawful Internet Gambling Enforcement Act of 2006 (hereinafter "UIGEA") and developments subsequent to enactment, and (3) the Federal Reserve Board's decision to exempt debit card transactions of \$15 or less from the requirement in Regulation E to produce a paper receipt in an electronic funds transfers.

This Survey does not cover issues pertaining to potential money laundering through stored-value cards raised in the 2007 National Money Laundering Strategy issued jointly by the U.S. Departments of the Treasury, Justice, and Homeland Security.¹⁷ We consider it premature to comment prior to the publication of

13. *Id.* For Professor Ramasastri's article, see Anita Ramasastri, *State Escheat Statutes and Possible Treatment of Stored Value, Electronic Currency, and Other New Payment Mechanisms*, 57 *BUS. LAW.* 475 (2001).

14. Hughes, Middlebrook & Peterson, 2006 Survey, *supra* note 9, at 243–50.

15. 127 S. Ct. 1559, 1567 (2007).

16. *Id.*

17. UNITED STATES DEPARTMENT OF THE TREASURY, UNITED STATES DEPARTMENT OF JUSTICE & UNITED STATES DEPARTMENT OF HOMELAND SECURITY, 2007 NATIONAL MONEY LAUNDERING STRATEGY 39–42 (May 3, 2007), available at <http://www.treas.gov/press/releases/docs/nmls.pdf> (discussing prepaid cards).

any proposed regulations. We note, however, that government and industry panel members at the American Bar Association's Section of Business Law Spring Meeting program titled "Hype or Reality—Anti-Money Laundering Risks from Prepaid Payment Products and What Can Be Done About Them"¹⁸ unanimously agreed that the potential for laundering money through stored-value products was negligible. This Survey also does not cover antitrust implications of payment card systems.¹⁹

I. NEW STATE GIFT CARD AND PAYROLL CARD LEGISLATION

Thirty states now regulate gift cards and nine states regulate payroll cards in some manner through statutes or regulations.²⁰ The absolute number of new state gift and payroll card statutes since the 2006 Survey is smaller than the number of statutes that existed at the time of the 2006 Survey. Other states considered but failed to enact new gift or payroll card laws.²¹ The types of state laws described in the 2006 Survey continue with the new statutes. There is still a remarkable disparity in the treatment of substantive consumer protection issues and in the location and format of required disclosures. In the 2006 Survey, we summarized those issues on which state laws varied the most. This year, we will focus on presenting the newest gift and payroll card legislation.

A. RECENT STATE GIFT CARD LAWS: LOTS OF CONSUMER PROTECTION, LOTS OF DETAILS

Apart from applying their state escheat or "money transmitter"²² laws to stored-value cards, states continue to show interest in regulating the expiration, dormancy, fee disclosure, and other limitations relating to gift cards.²³ Since our 2006 Survey, three states—**North Carolina, Minnesota, and Utah**—have enacted new laws regulating gift cards in some respect.²⁴ States that previously had enacted

18. The materials from this program may be found on the Electronic Payments Working Group's web page at http://www.abanet.org/dch/committee.cfm?com_CL320040 (last visited Nov. 4, 2007). The audio from this program can be found at American Bar Association, Section of Business Law, <http://www.abanet.org/buslaw/apps/sentry/sentry.cfm?path=/buslaw/meetings/audio/2007/spring/&file=19.mp3> (last visited Nov. 4, 2007).

19. For the most recent discussion of the antitrust issues, see generally Pierre V.F. Bos, *International Scrutiny of Payment Card Systems*, 73 ANTITRUST L.J. 739 (2006).

20. This Survey does not discuss escheat issues in state regulation. For the most comprehensive work on state escheat laws and new payment mechanisms, see generally Ramasastry, *supra* note 13.

21. For a complete listing of all bills introduced in the 2007 legislative sessions, see *State Laws and Regulations*, PAYBEFORELEGAL.COM, May 17, 2007, at 7, paybeforelegal.com.

22. The regulation of stored-value card issuers and sellers as "money transmitters" or "money services businesses" is discussed briefly in Part III of this Survey. For a more comprehensive discussion of this subject, see generally Judith Rinearson, *Regulation of Electronic Stored Value Payment Products Issued by Non-Banks Under State "Money Transmitter" Licensing Laws*, 58 BUS. LAW. 317 (2002).

23. Some states that regulate prepaid products do not call these products "gift cards." See, e.g., HAW. REV. STAT. § 481B-13(e) (Supp. 2006).

24. 2007 N.C. Sess. Laws ch. 363 (S.B. 1517) (Aug. 17, 2007) (to be codified at N.C. GEN. STAT. § 66-67.5); 2007 Minn. Laws ch. 93 (S.B. 69) (May 21, 2007); 2007 Utah Laws ch. 19 (H.B. 261) (Feb. 27, 2007) (to be codified at UTAH CODE ANN. § 13-11-4).

laws governing gift cards in some manner include Arizona, California, Connecticut, Georgia, Hawaii, Illinois, Iowa, Kansas, Kentucky, Louisiana, Maryland, Massachusetts, Montana, Nebraska, Nevada, New Hampshire, New Jersey, North Carolina, North Dakota, Ohio, Oklahoma, Rhode Island, South Carolina, Tennessee, Texas, Vermont, Virginia, and Washington.²⁵ The most recent addition is in North Carolina, which added gift card-specific provisions to its existing coverage of gift cards under its abandoned property law.²⁶ This new law only applies to gift cards that are not issued by financial institutions or are not usable at multiple unaffiliated sellers of goods or services.²⁷

Lawyers who research state gift card laws should be aware that core consumer protection provisions in some states are found in “escheat” or “abandoned property” statutes or in amendments to earlier “gift certificate” statutes, rather than in freestanding consumer protection statutes with the words “gift card” in their titles.²⁸ This creates a challenge for lawyers as they research gift card laws for clients.

State gift card laws vary considerably with respect to compulsory disclosures and substantive requirements. Generally, limitations on or requirements for disclosures relate to dormancy fees and expiration dates, as well as to the location, form, and font sizes for disclosures. For a more extensive discussion of these variables, see our *2006 Survey*.²⁹

1. Utah’s New Law

One key feature of Utah’s new law is that it provides a limited exemption from some of the requirements for gift cards, instruments, and other records “useable at multiple, unaffiliated sellers of goods or services if an expiration date is printed on the gift certificate, instrument or other record.”³⁰ Otherwise, Utah’s law designates the failure to print in a readable manner any expiration date or information regarding fees to be charged against or deducted from the balance of the gift certificate, instrument, or record as a “deceptive act or practice.”³¹

2. Minnesota’s New Law

Minnesota’s new law makes unlawful the sale of gift certificates, including gift cards, subject to expiration or any service fees.³² Additionally, the law explicitly excludes from its scope gift cards issued by employers in recognition of services performed by employees (essentially as bonuses).³³ The law also excludes gift

25. See Hughes, Middlebrook & Peterson, *2006 Survey*, *supra* note 9, at 329 n.64.

26. 2007 N.C. Sess. Laws ch. 363 (S.B. 1517) (Aug. 17, 2007) (to be codified at N.C. GEN. STAT. § 66-67.5).

27. *Id.*

28. E.g., CONN. GEN. STAT. ANN. §§ 3-56(a), 42-460 (West 2000 & Supp. 2007).

29. Hughes, Middlebrook & Peterson, *2006 Survey*, at 239–40.

30. 2007 Utah Laws ch. 19 (H.B. 261) (Feb. 27, 2007) (to be codified at UTAH CODE ANN. § 13-11-4).

31. *Id.*

32. 2007 Minn. Laws ch. 93 (S.B. 69) (May 21, 2007).

33. *Id.*

certificates or cards issued by federally or state-chartered banks, thrifts, trust companies, or credit unions or any of their affiliates.³⁴ Finally, the Minnesota law excludes gift certificates and cards that can be used at more than one seller of goods or services, provided that the issuer discloses the expiration date and fees.³⁵

3. North Carolina's New Law

North Carolina was among the states reported in the 2006 Survey as having some law that pertained to gift cards. On August 17, 2007, the General Assembly adopted additional gift card-specific provisions that require disclosure of maintenance fees at the time of purchase, require that the disclosures be visible on the card itself, and prohibit imposition of service fees for the first 12 months after purchase.³⁶ The new law also provides that a seller or issuer who violates its requirements will commit an unfair trade practice under N.C. GEN. STAT. § 75-1.1 and be subject to a civil penalty in accordance with N.C. GEN. STAT. § 75-15.2.³⁷ These provisions do not apply to gift cards issued by financial institutions or their operating subsidiaries or to cards usable at multiple unaffiliated sellers of goods or services.³⁸

As the second part of our 2006 Survey explained, state regulations on gift cards contain varied requirements for and restrictions on the sale of gift cards.³⁹ Many regulations require certain disclosures as a precondition to charging fees or allowing expiration of the value stored.⁴⁰ To the extent that states continue to enact different regulatory requirements, the burden on depositary and non-depositary issuers and marketers of gift cards will increase and the pressure they may place on Congress or the states to adopt a uniform standard is likely to grow more intense.

B. NEW STATE PAYROLL CARD LEGISLATION: ALSO MORE PROTECTION AND LOTS OF DETAILS

Our 2006 Survey reported that seven states, including Michigan and Minnesota, have enacted laws or promulgated regulations governing the payment of wages by payroll cards, rather than by direct deposit or check, or have otherwise regulated the use of payroll cards.⁴¹ Among these seven states, two states have *regulations* as opposed to legislation on the use of payroll cards.⁴² Since the 2006 Survey,

34. *Id.*

35. *Id.* It is unclear whether this provision applies only to non-depositary issuers or also to depositary issuers.

36. 2007 N.C. Sess. Laws ch. 363 (S.B. 1517) (Aug. 17, 2007) (to be codified at N.C. GEN. STAT. § 66-67.5).

37. *Id.*

38. *Id.*

39. Hughes, Middlebrook & Peterson, 2006 Survey, *supra* note 9, at 240-41.

40. *Id.* at 240.

41. *Id.* at 241.

42. Delaware and Nevada have regulations on payroll cards. 65-400-013 DEL. CODE REGS. §§ 1-3 (2007); NEV. ADMIN. CODE § 608.135 (2007). This Survey does not discuss state escheat laws that apply to payroll cards.

Kansas and Maryland have joined the list of states regulating payroll cards, with Maryland's statute becoming effective on January 1, 2007.⁴³ In 2006, the **Commonwealth of Puerto Rico** included payroll cards on its legislative agenda to cut down on government expenses.⁴⁴ In addition, **Minnesota** has extended the expiration date of the law discussed in the 2006 Survey to May 31, 2008.⁴⁵ **Virginia** has enacted a law allowing the state comptroller to require either direct deposit of state employee wages or payment through payroll cards.⁴⁶

State law conditions regarding payroll cards differ substantially from state to state. Three features of state payroll card laws warrant special mention: (1) employee choice versus compulsory use, (2) full availability of wages, and (3) fee-free use of the compensation paid or pre-disclosed fee requirements for payroll paid by debit cards. These continue to be the primary issues addressed by the new state laws on payroll cards.

1. Wages in Stored-Value Form: Can Employees Still Choose?

The issue of mandatory versus voluntary acceptance of debit cards by employees remains a hot issue in state payroll card legislation. In states such as Minnesota,⁴⁷ employees have the *option* of being paid by electronic fund transfers to payroll card accounts.⁴⁸ Minnesota also requires that employees voluntarily consent in writing to the payroll card method of payment.⁴⁹

Recent Federal Reserve Board Regulation E amendments may have resolved the "choice" issue for payroll cards because of the Board's refusal to budge on the Electronic Fund Transfer Act's longstanding prohibition on compulsory use.⁵⁰ Despite the position taken by the Board of Governors on the "choice" issue, **Kansas's** new payroll card law added payroll cards to the optional means by which employers may pay wages and salaries,⁵¹ but it gives employers sole discretion to choose the means of payment.⁵² Kansas requires employers who elect to pay employees with payroll cards to provide "at least one means of fund access withdrawal per pay period at no cost to the employee for an amount up to and including the total amount of the employee's net wages. . . ."⁵³ A unique feature of the new Kansas law is its requirement that employers adopting direct deposit or payroll card payments either conduct

43. 2007 Kan. Sess. Laws ch. 132 (H.B. 2316) (Apr. 16, 2007) (amending Kan. Stat. Ann. § 44-314); 2006 Md. Laws ch. 458 (May 16, 2006) (H.B. 388) (amending MD. CODE ANN., LAB. & EMPL. § 3-502).

44. 2006 P.R. Laws ch. 103 (H.B. 2454) (May 26, 2006).

45. 2007 Minn. Laws ch. 87 (S.B. 1495) (May 18, 2007) (amending 2005 Minn. Laws ch. 158, § 4).

46. 2007 Va. Acts ch. 847 (H.B. 1650) (Apr. 4, 2007).

47. MINN. STAT. §§ 177.23, 177.255 (2006).

48. *Id.* § 177.255, subd. 5.

49. *Id.* § 177.255, subd. 6.

50. 12 C.F.R. § 205.10(e)(2) (2007) ("No financial institution or other person may require a consumer to establish an account for receipt of electronic funds transfers with a particular institution as a condition of employment or receipt of a government benefit.").

51. 2007 Kan. Sess. Laws ch. 132 (H.B. 2316) (Apr. 16, 2007) (amending Kan. Stat. Ann. § 44-314).

52. *Id.*

53. *Id.*

employee forums to educate employees or distribute educational materials not less than 30 days prior to implementing a payroll card or direct deposit program.⁵⁴

The **Commonwealth of Puerto Rico**, as part of a comprehensive cost-savings plan, authorized the government to “create incentives for development of technology by promoting that every disbursement of public funds be conducted through electronic means.” Puerto Rico also has authorized its Department of the Treasury to establish a mechanism for payment through “electronic cards” of wages for employees who do not “wish” to receive wages through deposits to personal bank accounts.⁵⁵

2. Full Availability of Wages Paid with Payroll Cards: Paying To Get Paid, or Not?

“Full availability” is the second issue. States such as Minnesota require that the “employee who chooses to be paid wages by electronic fund transfer to a payroll card account . . . be permitted to withdraw by a free transaction from the employee’s payroll card account[] an amount up to and including the total amount of the employee’s entire net pay, as stated on the employee’s earnings statement.”⁵⁶ This presents a potential problem for the employee who earned, for example, \$282.32 in a specific pay period because ATM machines only dispense amounts in round denominations of \$10 or, predominantly, \$20 bills. Thus, in a state such as Minnesota, an employee wishing to obtain all of his or her wages could do so by using the card in a retail transaction or by receiving cash back from a retailer, such as a grocery store, in a pin-based transaction. Alternatively, the employee could pay a fee to a depository institution in order to obtain the “total amount” of his or her net pay. Despite the availability of these options, Minnesota law does not address how an employee may obtain that last increment of his or her pay, \$2.32 in the above example, without encountering some inconvenience or possibly incurring a fee. Since our 2006 Survey, no state has clarified this issue and it remains unclear to us whether “full availability” of net pay is a serious problem or merely a theoretical concern. At least one new service offered since our 2006 Survey suggests that it is a real issue. Discover Financial Services and First Data Corp. have announced new payroll products with “pay-to-the-penny” payroll services.⁵⁷

3. “Fee-Free” Use of Payroll Cards: Getting It All, or Not?

The third issue is “free access to or use of” wages.⁵⁸ As we explained in our 2006 Survey, some states require that employees be able to get wages without incurring

54. *Id.*

55. 2006 P.R. Laws ch. 103 (H.B. 2454) (May 26, 2006).

56. MINN. STAT. § 177.255, subd. 4 (2006).

57. *Discover Financial Services Announces Agreement with First Data To Issue Discover Network Payroll Cards by Money Network*, BUSINESS WIRE, June 11, 2007, <http://www.businesswire.com>. The new system also allows check-writing capacity via Money Network Checks, access to a large ATM network, direct deposit, and money transfers from the United States to Mexico and Latin America. *Id.*

58. For more information on Regulation E’s prohibition on compulsory use, see Hughes, Middlebrook & Peterson, 2006 Survey, *supra* note 9, at 237–38 & nn. 56–58.

associated fees.⁵⁹ **Minnesota** prohibits employers from charging their employees fees for the “initiation, participation, loading, or [receipt of] wages in an electronic fund transfer to a payroll card account.”⁶⁰ Similarly, the 2007 **Kansas** law prohibits employers from charging “initiation, loading or other participation fees to receive wages payable in an electronic fund transfer to a payroll card account, with the exception of the cost required to replace a lost, stolen or damaged payroll card.”⁶¹ In comparison, **Maryland** does not prohibit fees but instead requires the employer to disclose any fees applicable to payroll debit cards or card accounts in writing in at least 12-point font.⁶²

The recent spate of new gift and payroll card laws signal that the states see the need for more gift and payroll card regulation. As the next part of this Survey explains, the reach of these new state laws is likely to be more limited than would appear on first reading.

II. FEDERAL PREEMPTION OF STATE CONSUMER PROTECTION REGULATION

The federal system established under the U.S. Constitution was an innovation in government that permits and encourages multiple levels of government, national and state.⁶³ Because of overlapping constituencies of state and federal jurisdictions with independent law-making authority,⁶⁴ conflict “is perpetually arising and will probably continue to arise, as long as our system exists.”⁶⁵ Our 2006 Survey discussed in some depth the attempts by states to regulate the gift card and other programs of federally chartered financial institutions, the litigation involving those attempts, and the federal regulatory response.⁶⁶ Following publication of our 2006 Survey, the U.S. Supreme Court ruled on the preemption issue and may have decided the issue as a legal matter, if not as a political one.⁶⁷ Additionally, there have been appeals in the U.S. Courts of Appeals for the First and Second Circuits from district court decisions in New Hampshire and Connecticut, respectively, involving attempts by the states to regulate co-branded prepaid card programs involving national banks and/or a federal savings association.⁶⁸

59. E.g., 65-400-013 DEL. CODE REGS. § 2.0 (2007). For employees who do not maintain their own bank accounts, Delaware also provides that the employer, upon a written request from the employee, may deposit funds into an individual bank account assigned to the employee, but requires that “[c]osts associated with accounts established for the unbanked employee who voluntarily participates in the payroll debit card individual account program must be under reasonable circumstances.” *Id.* § 3.0.

60. MINN. STAT. § 177.255, subd. 12 (2006).

61. 2007 Kan. Sess. Laws ch. 132 (H.B. 2316) (Apr. 16, 2007) (amending Kan. Stat. Ann. § 44-314).

62. MD. CODE ANN., LAB. & EMPL. § 3-502 (LexisNexis Supp. 2006).

63. Richard Briffault, *Federalism*, in THE OXFORD COMPANION TO AMERICAN LAW 299, 299 (Kermit L. Hall ed., 2002) (“Before 1787, political thinkers did not believe two governments could have direct authority over the same people.”).

64. *See id.*

65. *McCulloch v. Maryland*, 17 U.S. (4 Wheat.) 316, 405 (1819).

66. Hughes, Middlebrook & Peterson, 2006 Survey, *supra* note 9, at 243–50.

67. *Watters v. Wachovia Bank, N.A.*, 127 S. Ct. 1559 (2007).

68. *SPGGC, LLC v. Aoyotte*, No. 06-2326 (1st Cir. May 30, 2007); *SPGGC, Inc. v. Blumenthal*, 408 F. Supp. 2d 87 (D. Conn. 2006), *aff’d in part, vacated in part*, No. 05-4711 (2d Cir. Oct. 19, 2007).

Part II will discuss the background of the U.S. Supreme Court's decision in *Watters v. Wachovia Bank, N.A.*, as well as decisions in the First and Second Circuits pertaining to gift card programs⁶⁹ and the shift of the battlefield from the courts to Congress.

A. FEDERALISM—YES I CAN, NO YOU CAN'T

Preemption jurisprudence entangles the judiciary in the difficult task of ensuring the survival of two fundamental but inherently conflicting values embodied in the U.S. Constitution: how does the Constitution permit states, as sovereign powers, to regulate local conduct, but yet enable the national government to preempt parochial state regulation that harms the national interest?⁷⁰ In cases where preemption questions arise out of business regulation enacted by Congress, the role of the judiciary is eased considerably.⁷¹ Under the Commerce Clause,⁷² Congress has extensive power to enact federal legislation that supercedes state regulation,⁷³ although that power is limited in part by the Tenth Amendment, which reserves certain powers to the states.⁷⁴ In cases where Congress has enacted legislation in an area within its authority, the judiciary's task is to ascertain whether Congress intended to preempt state action in that area in accordance with the Supremacy Clause of the Constitution.⁷⁵ Because Congress does not address preemption in legislation very often, the answer is not always clear cut. If Congress has not explicitly addressed preemption, the judiciary is required to "determine congressional intent based on its analysis of the general purposes of the federal statute and the relationship between those general purposes and the state action at issue."⁷⁶ This effort is a

69. SPGGC, LLC v. Aytote, No. 06-2326 (1st Cir. May 30, 2007).

70. Richard J. Pierce, Jr., *Regulation, Deregulation, Federalism, and Administrative Law: Agency Power To Preempt State Regulation*, 46 U. PITT. L. REV. 607, 611 (1985).

71. In matters where Congress has not acted, the judiciary must employ the Dormant Commerce Clause analysis, an area beyond the scope of this Survey. For an excellent discussion of this topic, see *id.* at 614–21.

72. U.S. CONST. art. 1, § 8, cl. 3.

73. In 1995, the Rehnquist Court began to place limits on congressional exercise of powers that it felt stretched the Commerce Clause too far. These decisions were in cases where Congress regulated non-commercial matters. See, e.g., *United States v. Morrison*, 529 U.S. 598, 615–17 (2000) (striking down Congress's attempt to exercise its power under the Commerce Clause to provide federal remedies for violence against women); *United States v. Lopez*, 514 U.S. 549, 561–67 (1995) (striking down Congress's attempt to exercise its power under the Commerce Clause to prevent individuals from knowingly carrying weapons in school zones). This trend continued until 2002, but since then may have slowed. See Erwin Chemerinsky, *The Assumptions of Federalism*, 58 STAN. L. REV. 1763, 1763 (2006). However, nothing in these decisions tampered either with the assumption that Congress has broad powers under the Commerce Clause in the area of business regulation or with previous Supreme Court jurisprudence in this area. *Id.* at 1779–80; Briffault, *supra* note 63, at 301.

74. U.S. CONST. amend. X; see *Reno v. Condon*, 528 U.S. 141, 149 (2000) (noting that even where Congress has "legislative authority over the subject matter," Congress cannot act through statutes that "violate[] the principles of federalism contained in the Tenth Amendment"). See also *Alden v. Maine*, 527 U.S. 706, 712, 748 (1999) (holding that Congress cannot, in regulating commerce under Article I, make nonconsenting states subject to claims in state courts because doing so violates the sovereign immunity of the states); *New York v. United States*, 505 U.S. 144, 166 (1992) (holding that Congress cannot require states to enforce a federal regulatory scheme).

75. U.S. CONST. art. VI, cl. 2.

76. Pierce, Jr., *supra* note 70, at 621.

case-by-case matter. As a general rule, in the absence of an explicit congressional statement of preemptive intent, courts apply a presumption in favor of state powers, or federalism.⁷⁷ The presumption “is not triggered when the State regulates in an area where there has been a history of significant federal presence.”⁷⁸ The Supreme Court’s decisions finding preemption typically fall into three categories: those in which the Court finds congressional intent to preclude state regulation either by explicit statement or implicitly due to the pervasiveness of the federal regulatory scheme; those involving direct conflicts between the requirements of the state and federal laws; and those where the state’s regulatory action frustrates the policies underlying the federal regulation.⁷⁹

B. OCC PREEMPTION OF STATE REGULATION—CAN IT?

Congress often delegates to agencies the power to interpret federal legislation. The courts normally grant deference to the actions of regulatory agencies because of the superior expertise of agency officials.⁸⁰ However, courts do not always afford deference to an agency’s finding that state law has been preempted by federal legislation.⁸¹

For example, the Office of the Comptroller of the Currency (“OCC”) in 2004 adopted preempting regulations broadly denying states any role in regulating the banking activities of national banks or their operating subsidiaries.⁸² The OCC

77. “[B]ecause the States are independent sovereigns in our federal system, we have long presumed that Congress does not cavalierly pre-empt state-law causes of action. In all pre-emption cases, and particularly in those in which Congress has ‘legislated . . . in a field which the States have traditionally occupied,’ we ‘start with the assumption that the historic police powers of the States were not to be superseded by the Federal Act unless that was the clear and manifest purpose of Congress.’” *Medtronic, Inc. v. Lohr*, 518 U.S. 470, 485 (1996) (quoting *Rice v. Santa Fe Elevator Corp.*, 331 U.S. 218, 230 (1947); *Hillsborough County v. Automated Med. Labs., Inc.*, 471 U.S. 707, 715 (1985)).

78. *United States v. Locke*, 529 U.S. 89, 108 (2000). Regulation of federally chartered financial institutions has been once such area. *See, e.g., Wachovia Bank, N.A. v. Watters*, 431 F.3d 556, 560 n.3 (6th Cir. 2005) (noting that there is no presumption against preemption), *aff’d*, 127 S. Ct. 1559 (2007); *Nat’l City Bank v. Turnbaugh*, 463 F.3d 325, 330 (4th Cir. 2006) (deferring to agency interpretation even though agency erroneously thought that it should apply presumption against preemption); *Wachovia Bank, N.A. v. Burke*, 414 F.3d 305, 314–15 (2d Cir. 2005) (holding that presumption against federal preemption disappears upon judicial review in fields of regulation that have been “substantially occupied by federal authority for an extended period of time” such as with regard to the regulation of federally chartered banks), *cert. denied*, 127 S. Ct. 2093 (2007).

79. *Pierce, Jr.*, *supra* note 70, at 621–22.

80. *Chevron U.S.A., Inc. v. Natural Res. Def. Council, Inc.*, 467 U.S. 837, 844, 865 (1984) [hereinafter “*Chevron*”]; *United States v. Shimer*, 367 U.S. 374, 381–82 (1961) (“where Congress has committed to the head of a department certain duties requiring the exercise of judgment and discretion, his action thereon, whether it involves questions of law or fact, will not be reviewed by the courts unless he has exceeded his authority or . . . his action was clearly wrong” (internal quotations omitted)).

81. *See, e.g., Smiley v. Citibank (S.D.), N.A.*, 517 U.S. 735, 744 (1996) (noting in dicta that courts must always decide *de novo* whether federal agency regulation preempts state law); *Bankwest, Inc. v. Baker*, 411 F.3d 1289, 1300 (11th Cir.) (holding that agency decisions on preemption are not entitled to *Chevron* deference), *vacated*, 433 F.3d 1344 (11th Cir. 2005); *Colo. Pub. Util. Comm’n v. Harmon*, 951 F.2d 1571, 1579 (10th Cir. 1991) (“However, a preemption determination involves matters of law—an area more within the expertise of the courts than within the expertise of the Secretary of Transportation.”).

82. *Bank Activities and Operations; Real Estate Lending and Appraisals*, 69 Fed. Reg. 1904, 1917 (Dep’t of Treasury Jan. 13, 2004) (amending 12 C.F.R. pts. 7 & 34). This Survey covers the amendments

regulations preempted state laws to the extent they “obstruct, impair, or condition a national bank’s ability to fully exercise . . . powers”⁸³ granted to national banks in the National Bank Act.⁸⁴ The regulations were immediately challenged as overreaching.⁸⁵ In its supporting analysis that accompanied the final adoption of the rule, the OCC argued that it was merely restating the current state of the law in the area of National Bank Act preemption.⁸⁶ This contention, however, has been challenged by commentators on a number of grounds.⁸⁷

Our 2006 Survey discussed several cases in which one of the issues was the OCC’s ability to preempt state regulations applicable to prepaid card programs or mortgage-lending operations.⁸⁸ Since the publication of the 2006 Survey, several appeals from those decisions have been argued. A decision in the Supreme Court in one of these cases has swept aside many of the questions that have been raised about the authority of the OCC (and, with respect to federally chartered savings associations, the Office of Thrift Supervision or “OTS”) to preempt state regulation.

1. *Watters v. Wachovia Bank, N.A.*

From 1997 to 2003, Wachovia Mortgage was a subsidiary of Wachovia Corporation, a financial holding company, and was registered under Michigan’s Mortgage Brokers, Lenders and Servicers Licensing Act (“MBLSLA”).⁸⁹ In 2003, Wachovia

to Part 7, which address deposit taking, non-real estate lending, and other activities. Amendments to Part 34, which address real estate lending of national banks, are not addressed in this Survey.

83. 12 C.F.R. § 7.4009(b) (2007).

84. National Bank Act, ch. 106, 13 Stat. 99 (1864) (codified as amended in scattered sections of 12 U.S.C.).

85. See Hughes, Middlebrook & Peterson, 2006 Survey, *supra* note 9, at 244–50, for a discussion of the circumstances accompanying this adoption.

86. Bank Activities and Operations; Real Estate Lending and Appraisals, *supra* note 82, 69 Fed. Reg. at 1910–11.

87. Generally, the commentators contend that: (i) the OCC rules constitute “field” preemption, which is inconsistent with decisions of the U.S. Supreme Court and expressions by Congress that national banks are subject to state laws, except those that prevent or impair significantly (rather than merely add an additional regulatory layer onto) the exercise of powers granted to national banks; (ii) the effect of the OCC preemption rules will be to eliminate any meaningful state-chartered banking sector, as banks will seek national bank charters to escape state regulation, eliminating a source of innovation in banking that the dual-banking system has promoted; (iii) the OCC’s preemption determinations are inherently suspect as involving a conflict of interest since the effect is to increase the OCC’s importance as more banks seek federal charters and the protection of the OCC against the states; and (iv) this conflict of interest will also result in consumer harm as the OCC will be reluctant to take harsh enforcement action against the banks it regulates. See generally Arthur E. Wilmarth, Jr., *The OCC’s Preemption Rules Exceed the Agency’s Authority and Present a Serious Threat to the Dual Banking System and Consumer Protection*, 23 ANN. REV. BANKING & FIN. L. 225 (2004); Vincent DiLorenzo, *Federalism, Consumer Protection and Preemption: A Case for Heightened Judicial Review* (2007), <http://ssrn.com/abstract=796147>.

88. Hughes, Middlebrook & Peterson, 2006 Survey, *supra* note 9, at 245–48. The similar authority of the Office of Thrift Supervision with respect to federal savings associations was also at issue in some of these cases. See, e.g., SPGGC, LLC v. Ayoite, No. 06-2326 (1st Cir. May 30, 2007).

89. *Watters v. Wachovia Bank, N.A.*, 127 S. Ct. 1559, 1565 (2007). For the relevant Michigan law, see MICH. COMP. LAWS § 445.1651 (2006). This law was enacted in response to extensive predatory lending abuse in Michigan. Brief for the Petitioner at 5, *Watters v. Wachovia Bank, N.A.*, 127 S. Ct. 1559 (2007) (No. 05-1342). The registration requirement was a special provision for subsidiaries of financial institutions subject to federal regulation and did not require the background investigations,

Mortgage became a subsidiary of Wachovia Bank, N.A., and thereafter claimed exemption from the Michigan registration requirement on the ground that the state regulation was not applicable to an operating subsidiary of a national bank.⁹⁰ Michigan disagreed and tried to shut down Wachovia Mortgage for non-registration. In the ensuing litigation, the district court⁹¹ and the court of appeals⁹² agreed with Wachovia Bank that the Michigan law was preempted by OCC regulations.

Michigan filed a petition for writ of certiorari with the U.S. Supreme Court in which it argued that the OCC did not have the power under the National Bank Act to extend its preemption rule to operating subsidiaries, and that the lower courts should not have given deference to the OCC rules.⁹³ The essence of Michigan's argument was that section 484(1) of the National Bank Act expressly grants exclusive "visitorial" (e.g., regulatory, supervisory, and enforcement) rights to the OCC over national banks, but not to their affiliates, meaning that Congress had not intended to grant the OCC exclusive regulatory authority over operating subsidiaries.⁹⁴ Therefore, Michigan argued, the OCC's rules extending preemption to operating subsidiaries were not entitled to *Chevron* deference,⁹⁵ upon which both of the lower courts relied in upholding the OCC regulations, because "the Court must reject an agency interpretation of a statute that is contrary to the unambiguously expressed intent of Congress."⁹⁶ The Supreme Court granted Michigan's petition.⁹⁷

proofs of financial responsibility, minimum net worth requirements, annual examinations, or operational restrictions applicable to other types of licensees. The registration did give Michigan the power to investigate complaints against the registrant if it deemed that an investigation of the complaint by the federal regulator was inadequate. *Id.* at 7.

90. *Watters*, 127 S. Ct. at 1565. For the relevant federal regulation, see 12 C.F.R. § 7.4006 (2007) ("Unless otherwise provided by Federal law or OCC regulation, State laws apply to national bank operating subsidiaries to the same extent that those laws apply to the parent national bank.").

91. *Wachovia Bank, N.A. v. Watters*, 334 F. Supp. 2d 957, 965 (W.D. Mich. 2004).

92. *Wachovia Bank, N.A. v. Watters*, 431 F.3d 556, 563 (6th Cir. 2005).

93. Petition for Writ of Certiorari at 8–22, *Wachovia Bank, N.A. v. Watters*, 126 S. Ct. 2900 (2006) (No. 05-1342).

94. Michigan argued, among other things, that nowhere else in the National Bank Act does the term "national bank" include its affiliates, which are separately addressed in the statute, and that operating subsidiaries (a type of affiliate) that do not have national bank charters are therefore not included within the exclusive visitorial rights granted in § 484(a), and thus can be subject to state regulation. Petition for Writ of Certiorari, *supra* note 93, at 8–9. Michigan further argued that Congress has not modified the original language in § 484(a), despite several opportunities to do so, most recently in 1983. *Id.* at 13–14. For the relevant section of the U.S. Code, see 12 U.S.C. § 484(a) (2000) ("No national bank shall be subject to any visitorial powers except as authorized by Federal law . . .") (emphasis added).

95. See *supra* note 80 and accompanying text.

96. Petition for Writ of Certiorari, *supra* note 93, at 10 (citing *Chevron*, 467 U.S. at 843). Michigan also argued that, to the extent that the intent of Congress was deemed ambiguous, the lower courts did not apply the required presumption that state regulation was not intended to be preempted, or adhere to the U.S. Supreme Court's dicta that agency interpretations involving preemption decisions are subject to *de novo* judicial review. *Id.* at 16, 23. For the Supreme Court's dicta, see, for example, *Medtronic, Inc. v. Lohr*, 518 U.S. 470, 475, 484–85 (1996), and *Smiley v. Citibank (S.D.)*, N.A., 517 U.S. 735, 744 (1996). Michigan also argued that the OCC was prohibited from preempting state regulation under the Tenth Amendment to the U.S. Constitution, see Petition for Writ of Certiorari, *supra* note 93, at 22–25, but this argument was ultimately summarily rejected by the Supreme Court. *Watters*, 127 S. Ct. at 1573.

97. *Wachovia Bank, N.A. v. Watters*, 126 S. Ct. 2900 (2006).

Respondents Wachovia Bank and Wachovia Mortgage argued in their brief that preemption of Michigan's law derives from a different section of the National Bank Act, 12 U.S.C. § 24,⁹⁸ one that grants national banks, in addition to the specific powers enumerated in the Act, "all such incidental powers as shall be necessary to carry on the business of banking."⁹⁹ The OCC in 1966 specified that one of these incidental powers included the ability to use operating subsidiaries to engage in banking activities.¹⁰⁰ Wachovia argued that the OCC had the authority to make such a determination and furthermore that the determination was entitled to deference under *Chevron*.¹⁰¹ Therefore, Wachovia argued, Michigan's attempt to regulate Wachovia's operating subsidiary would be tantamount to regulating the exercise by the national bank of one of its enumerated powers under the National Banking Act. This, Wachovia maintained, could not be allowed because "[t]he Court has long 'interpret[ed] grants of both enumerated and incidental 'powers' to national banks as grants of authority not normally limited by, but rather ordinarily pre-empting, contrary state law.'¹⁰² Moreover, Wachovia argued, the regulation of national banks is an area where there is an extensive history of federal presence (going back as far as *McCulloch v. Maryland*,¹⁰³ decided in 1819).¹⁰⁴ Thus the presumption against preemption would not apply in cases involving national bank regulation,¹⁰⁵ and in fact *Barnett Bank, N.A. v. Nelson*¹⁰⁶ would require quite the opposite presumption.¹⁰⁷

Regarding Michigan's argument that section 484 of the National Bank Act does not expressly give the OCC exclusive visitorial authority over operating subsidiaries, Wachovia argued that the use of operating subsidiaries did not exist as an incidental power of national banks until 1966. Therefore, Congress's failure to mention them in various amendments to the National Bank Act before that date cannot be taken as evidence of congressional intent.¹⁰⁸ Further, Wachovia argued that Congress acknowledged the power of national banks to use operating subsidiaries "subject to the same terms and conditions that apply to such activities when conducted by the bank" in the Gramm-Leach-Bliley Act¹⁰⁹ enacted in 1999.¹¹⁰

98. 12 U.S.C. § 24 (2000).

99. Brief for the Respondents at 4, *Watters v. Wachovia Bank, N.A.*, 127 S. Ct. 1559 (2007) (No. 05-1342).

100. *See* Acquisition of Controlling Stock Interest in Subsidiary Operations Corporation, 31 Fed. Reg. 11459 (Dep't of Treasury Aug. 31, 1966) (amending 12 C.F.R. § 7.10).

101. *NationsBank, N.A. v. Variable Annuity Life Ins. Co.*, 513 U.S. 251, 258 n.2 (1995) (affording *Chevron* deference to an OCC determination).

102. Brief for the Respondents, *supra* note 99, at 21 (quoting *Barnett Bank, N.A. v. Nelson*, 517 U.S. 25, 32 (1996)).

103. 17 U.S. (4 Wheat.) 316, 438 (1819).

104. *Id.* at 21-24.

105. *See* *U.S. v. Locke*, 529 U.S. 89, 108 (2000).

106. 517 U.S. at 34.

107. Brief for the Respondents, *supra* note 99, at 24.

108. *Id.* at 28-29.

109. Gramm-Leach-Bliley Act, Pub. L. No. 106-102, § 301, 113 Stat. 1338, 1407 (1999) (codified at 15 U.S.C. § 6711 (2000)).

110. Brief for the Respondents, *supra* note 99, at 18-20.

The Supreme Court sided with Wachovia and upheld the lower courts in a 5–3 decision.¹¹¹ The Supreme Court agreed that the use of operating subsidiaries is an incidental power of national banks under 12 U.S.C. § 24 and that, under *Barnett*,¹¹² the Michigan law was an impermissible restraint on the exercise of that power and therefore preempted.¹¹³ The Court held, “[s]tates are permitted to regulate the activities of national banks where doing so does not prevent or significantly interfere with the national bank’s or the national bank regulator’s exercise of its powers. But when state prescriptions significantly impair the exercise of authority, enumerated or incidental under the NBA, the State’s regulations must give way.”¹¹⁴ The Supreme Court adopted and agreed with most of the respondents’ other arguments, although it did not address the issue of the validity of the OCC regulations or any required deference to them under *Chevron*, since it found that preemption of Michigan law was required under the National Bank Act and applicable authority, regardless of the OCC regulations.¹¹⁵

2. State Prepaid Card Regulation

The U.S. Court of Appeals for the First Circuit has issued a decision in *SPGGC, LLC v. Ayotte*,¹¹⁶ a case involving an attempt by a state, this time New Hampshire, to argue that federalism principles should permit state consumer regulation of gift cards issued by a national bank (U.S. Bank) and a federally chartered savings association (Metabank) but sold through a mall operator (Simon Property Group). In some ways reminiscent of Michigan’s argument in *Watters*, New Hampshire argued to the First Circuit that the mall operator was not a national bank or federal savings association, but at best an agent of those entities, and thus the mall operator was subject to the New Hampshire gift card regulations.¹¹⁷ The OCC filed an amicus brief on behalf of U.S. Bank, arguing that the use of agents to market and distribute products was an incidental power of national banks subject to exclusive OCC supervision, that the features of the products that New Hampshire claimed violated state law were permitted for national bank products under OCC rules, and thus New Hampshire’s law was preempted under *Barnett*.¹¹⁸ Metabank argued for the same result, although it did so under a different and much more direct

111. “In accord with the Courts of Appeals that have addressed the issue, we hold that Wachovia’s mortgage business, whether conducted by the bank itself or through the bank’s operating subsidiary, is subject to OCC’s superintendence, and not to the licensing, reporting, and visitorial regimes of the several States in which the subsidiary operates.” *Watters*, 127 S. Ct. at 1564–65.

112. Brief for the Respondents, *supra* note 99, at 11.

113. *Id.*

114. *Id.* at 1567 (citing *Barnett Bank, N.A.*, 517 U.S. at 32–34; *Franklin Nat’l Bank v. New York*, 347 U.S. 373, 377–79 (1954)).

115. See *Watters*, 127 S. Ct. at 1572 n.13.

116. *SPGGC, LLC v. Ayotte*, No. 06-2326 (1st Cir. May 30, 2007).

117. Brief for Appellant at 12–21, *SPGGC, LLC v. Ayotte*, No. 06-2326 (1st Cir. May 30, 2007). For more discussion of the history and issues of this case in the lower courts, see Hughes, Middlebrook & Peterson, 2006 Survey, *supra* note 9, at 246–49.

118. Brief for the Office of the Comptroller of the Currency as Amicus Curiae Supporting Respondents at 13–16, *SPGGC, LLC v. Ayotte*, No. 06-2326 (1st Cir. May 30, 2007).

statutory and regulatory scheme administered by the Office of Thrift Supervision.¹¹⁹ The First Circuit found that the New Hampshire law restricted the exercise of the power of both the national bank and the federal savings association to use agents to sell gift cards, and thus was preempted.¹²⁰

On October 19, 2007, the U.S. Court of Appeals for the Second Circuit decided the appeal in *SPGGC, Inc. v. Blumenthal*.¹²¹ In this decision, the Second Circuit found that certain Connecticut gift card regulations (similar to the New Hampshire laws that were involved in *Ayotte*) were not preempted with respect to gift cards issued by Bank of America on behalf of Simon Property Group ("Simon") in Connecticut, although the court did find a valid claim of preemption of a Connecticut law prohibiting expiration dates.¹²² The *Ayotte* and *Blumenthal* decisions are easily reconciled. As the Second Circuit noted, the *Ayotte* decision involved gift cards issued by financial institutions that set the policies and collected the fees that were alleged to have violated New Hampshire law, whereas in the gift card program before the Second Circuit in *Blumenthal*, Simon Property Group set and collected the fees that violated Connecticut law, not Bank of America.¹²³ The Second Circuit found that application of the Connecticut gift card regulations to the gift card program fees did not have any impact on the exercise of national bank powers by Bank of America.¹²⁴ The court found that while the Connecticut regulations did have an impact on Simon, the regulations were not preempted as to Simon because Simon's conduct "is neither protected under federal law nor subject to the OCC's exclusive oversight."¹²⁵ Interestingly, the Second Circuit noted several times that the OCC had in an amicus brief urged the court to reach that conclusion.¹²⁶ On the other hand, since the Connecticut prohibition on expiration dates for gift cards would have prevented Bank of America from being able to issue gift cards at all in Connecticut,¹²⁷

119. Brief for Metabank at 25–28, *SPGGC, LLC v. Ayotte*, No. 06-2326 (1st Cir. May 30, 2007). The Office of Thrift Supervision ("OTS") is authorized under 12 U.S.C. § 1463 (2000) to provide for the safe and sound operation of federal savings associations, and has plenary authority to regulate all aspects of their operations. This regulatory control wholly preempts the field against state regulation. *Conf. of Fed. Sav. & Loan Ass'ns v. Stein*, 604 F.2d 1256, 1260 (9th Cir. 1979), *aff'd*, 445 U.S. 921 (1980). The OTS in an opinion letter issued in 2006 expressly preempted state gift card laws in their application to federal savings associations, mentioning specifically New Hampshire's. John E. Bowman, Chief Counsel, Office of Thrift Supervision, United States Department of Treasury, P-2006-3 (June 9, 2006), available at <http://164.109.59.122/docs/5/56218.pdf> (discussing preemption of state gift card restrictions). OTS regulations also specifically authorize federal savings associations to "market and sell, or participate with others to market and sell, electronic capacities and by-products" to third parties. 12 C.F.R. § 555.200(b) (2007).

120. *SPGGC, LLC v. Ayotte*, No. 06-2326, slip op. at 14–20, 22–24 (1st Cir. May 30, 2007).

121. *SPGGC, Inc. v. Blumenthal*, No. 05-4711 (2d Cir. Oct. 19, 2007).

122. *Blumenthal*, No. 05-4771, slip op. at 11–12.

123. *Id.* at 11.

124. *Id.*

125. *Id.* at 11–12. The Second Circuit further stated, "We do not address whether we would reach a different conclusion were the fees in question collected and established by the issuing bank rather than by SPGGC." *Id.* at 12.

126. *Id.* at 10–11.

127. These cards were issued under license from Visa U.S.A., Inc., which requires expiration dates on all cards for fraud control purposes. *Id.* at 4.

the Second Circuit remanded the preemption question on that specific issue to the district court for further consideration.¹²⁸

C. FEDERALISM AND FEDERALLY CHARTED FINANCIAL INSTITUTIONS

The effort by Michigan in *Watters* to assert a role for state consumer protection regulation of national bank activities failed, probably inevitably given the history surrounding the enactment of the National Bank Act and subsequent jurisprudence. The National Bank Act was enacted in the context of state hostility to previous attempts to create a national bank,¹²⁹ and during congressional debates it was clear on all sides of the issue that the intent of the Act was to create a class of banks exclusively under the control of the federal government and immune from unfriendly state regulation.¹³⁰ The Supreme Court early on called these banks “national favorites,”¹³¹ and in its opinion in *Watters* stated, “[i]n the years since the NBA’s enactment, we have repeatedly made clear that federal control shields national banking from unduly burdensome and duplicative state regulation.”¹³²

Given the expansive possibilities of the incidental powers clause of the National Bank Act,¹³³ the OCC’s aggressiveness in its interpretation,¹³⁴ and the Supreme Court’s history of backing the OCC, it is hard to imagine a case in which the states could prevail in an argument that their consumer protection regulation should apply to national banks under federalism principles. The same conclusion seems applicable to federal savings associations as well.¹³⁵ Because the powers of the OCC and the OTS are derived from Congress, the remedy for the states in their federalism concerns would seem to be in Congress, and it is to Congress where the battle has shifted.

House Financial Services Committee Chairman Barney Frank and House Energy and Commerce Committee Chairman John Dingell on May 11, 2007 wrote to members of the Federal Reserve Board, the Office of Thrift Supervision, the Federal Trade Commission, the Office of the Comptroller of the Currency, and

128. *Blumenthal*, No. 05-4711, slip op. at 12–13.

129. Brief of American Bankers Association et al. as Amici Curiae in Support of Respondents at 8–12, *Watters v. Wachovia Bank, N.A.*, 127 S. Ct. 1559 (No. 05-1342).

130. *Id.* at 9. “The NBA would establish a banking system ‘made to operate directly upon the people independently of State boundaries or State sovereignty,’ and ‘wholly independent of State authority.’” CONG. GLOBE, 37th Cong., 3d Sess. 1115 (1863) (statement of Rep. Spaulding).

131. *Tiffany v. Nat’l Bank*, 85 U.S. (18 Wall.) 409, 413 (1873).

132. *Watters*, 127 S. Ct. at 1566–67.

133. 12 U.S.C. § 24, Seventh (2000).

134. The OCC’s regulatory responsibility is a heavy one given the systemic and financial risk of a national bank failure, so aggressiveness is probably justifiable caution.

135. There could be another preemption battle looming over nascent state attempts to regulate the relationship of financial institutions, including federally chartered ones, with merchants accepting credit, prepaid, and debit cards. There are bills introduced in at least seven states that attempt to cap interchange rates, prohibit the charging of discount or processing fees on the sales tax portion of a transaction, and/or require disclosure to merchants or consumers of the existence and amount of interchange fees. See *Unfair Credit Card Fees.com*, Interchange Legislation in the United States, 2007, http://www.unfaircreditcardfees.com/uploads/State-by-State_Interchange_Activity.pdf (last visited June 3, 2007).

the Federal Deposit Insurance Corporation calling for stronger federal-level consumer protection and enforcement.¹³⁶ On June 13, 2007, the House Financial Services Committee held hearings at which it asked federal and state regulators and enforcement officials to provide testimony concerning how to better protect consumers from problems such as predatory lending and credit card marketing abuse.¹³⁷ At least one federal regulator took pains in his testimony to explain and defend the use of regular and comprehensive examinations of federally chartered financial institutions to nip in the bud potential consumer abuses, with enforcement actions taken only when that (infrequently) fails.¹³⁸

Recent accords between the states and federal financial institution regulators to share consumer complaints and to cooperate in ensuring resolution received prominent discussion in testimony by state and federal representatives.¹³⁹ State representatives asked Congress for uniform federal legislation that would accord the states a role in enforcement against national financial institutions: "because of our greater collective resources and experience handling consumer complaints, we believe we can handle consumer complaints more quickly and efficiently than can the OCC and other federal financial regulators."¹⁴⁰ The OCC, however, undoubtedly reflected the outlook of other federal regulators with this observation:

It is counterproductive for state officials to focus their finite supervisory and enforcement resources on national banks and their subsidiaries when those institutions are already extensively supervised by the OCC, and when there are other entities—many of which answer only to state authorities—that are demonstrably the source of problems. Returning to the metaphor, you can indeed have too many cops on the same beat if it means leaving other, more dangerous parts of the neighborhood unprotected.¹⁴¹

As we said before, federalism can be messy.

III. RECENT FEDERAL DEVELOPMENTS—A YEAR OF ENFORCEMENT ACTIONS, REGULATORY RELIEF, AND THE UNLAWFUL INTERNET GAMBLING ENFORCEMENT ACT OF 2006

In addition to the state and judicial developments that have occurred since our 2006 Survey, there have been important actions from Congress, the regulatory

136. Press Release, House Committee on Financial Services, Chairmen Dingell and Frank Call for Increased Consumer Protection (May 11, 2007), http://www.house.gov/apps/list/press/financialsvcs_dem/press051107.shtml.

137. *Improving Federal Consumer Protection in Financial Services: Hearing before the H. Comm. on Fin. Servs.*, 110th Cong. (2007), available at http://www.house.gov/apps/list/hearing/financialsvcs_dem/ht061307.shtml.

138. *Id.* (statement of John C. Dugan, Comptroller of the Currency, Office of the Comptroller of the Currency).

139. *Id.*

140. *See, e.g., id.* (statement of Thomas J. Miller, Attorney General of Iowa).

141. *Id.* (statement of John C. Dugan, Comptroller of the Currency, Office of the Comptroller of the Currency).

agencies, and federal prosecutors. In this part of the Article, we discuss recent enforcement actions and prosecutions, a decision by the Board of Governors of the Federal Reserve System to provide regulatory relief for issuers of small dollar value gift cards, and the Unlawful Internet Gambling Enforcement Act of 2006.

A. BIG FEDERAL ENFORCEMENT ACTIONS—THREE KINDS OF NEW PAYMENTS PRODUCTS ATTRACT GOVERNMENT ATTENTION

This year, the federal government pursued actions against providers of three different stored-value or other new electronic payment products. These enforcement actions reveal different approaches that federal prosecutors and regulatory agencies may take when dealing with alleged instances of violations of federal criminal and consumer protection laws.

1. The Prosecution of E-gold Ltd. and the Definition of Money Transmitter

In early 2007, the federal government charged e-gold Ltd. and its owners with violating federal and state laws regarding “money transmission” services. This part of the Survey describes the e-gold Ltd. business model and the charges made against the company, and then discusses certain ambiguities in the law pertaining to “money transmission” businesses.

a. *E-gold Ltd. Builds a Successful Business Facilitating Internet Payments*

E-gold Ltd. is an Internet-based system that allows individuals to make domestic and international payments not in dollars or pounds or euros, but rather in precious metals.¹⁴² Or more accurately, it allows individuals to settle debts by transferring book entry title to units of a precious metal held in trust by a corporate affiliate of e-gold.¹⁴³ Users are given an account dominated in grams of gold¹⁴⁴ and backed (or “purportedly backed” as the government asserts¹⁴⁵) by actual gold held in trust.¹⁴⁶ Users may pay for purchases by initiating an exchange between two e-gold accounts.¹⁴⁷ “E-gold appeals to . . . people who invest in the precious metal and believe money ought to be anchored to it.”¹⁴⁸ E-gold Ltd. describes its

142. See E-gold Ltd., <http://www.e-gold.com> (last visited Sept. 6, 2007).

143. *Id.*

144. Individuals with more eclectic tastes may also purchase e-silver, e-platinum, and e-palladium. The current exchange rates are available at E-gold Ltd., Exchange Rates, <http://www.e-gold.com/currentexchange.html> (last visited Sept. 6, 2007).

145. Indictment at 2, United States v. E-Gold Limited, Gold & Silver Reserve, Inc., Douglas L. Jackson, Barry K. Downey, and Reid A. Jackson, Crim. No. 07-109 (D.D.C. Apr. 24, 2007), available at <http://www.usdoj.gov/criminal/ceos/Press%20Releases/DC%20egold%20indictment.pdf> [hereinafter “Indictment”].

146. See E-gold Ltd., <http://www.e-gold.com> (last visited Sept. 6, 2007).

147. *See id.*

148. Brian Grow, *Gold Rush: Online Payment Systems like E-gold Ltd. Are Becoming the Currency of Choice for Cybercrooks*, Bus. Wk., Jan. 9, 2006, at 68.

product as “the world’s first electronic currency designed for borderless, electronic business transactions over the Internet.”¹⁴⁹ According to the e-gold Ltd. web site:

The target market for e-gold is simply people who use money. How do you presently use money? Chances are any of these activities would benefit from the increased soundness, security, efficiency, and lower cost of e-gold. Here are some examples of how e-gold is presently used:

- e-commerce
- Business-to-business payments
- Point of service sales
- Person-to-person payments
- Payroll
- Bill payments
- Charitable donations¹⁵⁰

E-gold’s promotional materials state that its product is unique because “every ounce is secured by actual gold bullion held in allocated storage at repositories certified by the London Bullion Market Association.”¹⁵¹ Title to the bullion is held by the E-gold Bullion Reserve Special Purpose Trust for the exclusive benefit of holders of e-gold, e-silver, e-platinum, and e-palladium (collectively “e-metal”).¹⁵² E-gold notes in its pleadings that a routine audit of all of the e-metal belonging to the special purpose trust that took place in April 2007 concluded that the e-metal issued by defendants was fully backed by bullion in allocated storage.¹⁵³

In 1999, the *Financial Times* described e-gold as “the only electronic currency that has achieved critical mass on the web. . . . For merchants, eGold has a further bonus: unlike credit cards, which are liable to chargebacks, the system guarantees payment once ordered.”¹⁵⁴ Early write-ups in magazines such as *Barrons*¹⁵⁵

149. Defendants’ Status Report and Notice of Compliance with This Court’s Seizure Warrants and Post-Indictment Restraining Order at 5, *United States v. E-Gold Limited, Gold & Silver Reserve, Inc., Douglas L. Jackson, Barry K. Downey, and Reid A. Jackson*, Crim. No. 07-109 (D.D.C. May 17, 2007) [hereinafter “May Status Report”].

150. E-gold Ltd., Better Money, <http://www.e-gold.com/unsecure/qanda.html> (last visited Sept. 6, 2007).

151. May Status Report, *supra* note 149, at 6.

152. Hildeberto S. de Frias & Michael J. Mello, Mello, Jones, Hollis & Martin, Barristers & Attorneys, Declaration of Trust Constituting the E-gold Bullion Reserve Special Purpose Trust § 4.1 (March 31, 2000), <http://www.e-gold.com/contracts/egold-spt-111899.htm>.

153. Notice of Filing of Accounting “of all Precious Metals Held” as Required by the Post-Indictment Restraining Order Entered in This Case at 4–5, *United States v. E-Gold Limited, Gold & Silver Reserve, Inc., Douglas L. Jackson, Barry K. Downey, and Reid A. Jackson*, Crim. No. 07-109 (D.D.C. May 9, 2007).

154. Tim Jackson, *When Gold Makes Cents: It May Sound Crazy, but the eGold Payment Mechanism Based on Deposits of Precious Metal, Is Cheap, Efficient and Easy*, *FIN. TIMES*, July 13, 1999, at 18.

155. “With the global explosion of the Internet and e-commerce, the world needs a new type of currency. It needs an asset-backed, high-tech money standard, without the political machinations that hobble the euro, the dollar, the yen and all other traditional currencies. . . . One company, E-gold, already allows online users to settle payments using its currency, which is 100% backed by gold.” Jack White & Doug Ramsey, *Making New Money*, *BARRON’S*, April 23, 2001, at 59.

and *Wired*¹⁵⁶ gave e-gold both visibility and credibility. Numerous other Internet-based payment systems came and went while e-gold survived.¹⁵⁷

Digital currencies in general, and e-gold in particular, however, developed poor reputations in some circles and one commentator called the payment systems “at best, lax on financial crime.”¹⁵⁸ Criticism of these new payment options was often harsh:

Skeptics, though, charge that efforts to create currency based on the value of metals seem designed to skirt standard banking and money-transfer rules while providing few customer protections and inadequate checks of account-holder identities. They also point to high fees typically charged by third party companies that support pre-paid card programs and that exchange gold value for traditional currencies.¹⁵⁹

For better or worse, e-gold’s novel business model attracted a lot of attention.

b. *E-gold Is Indicted for Money Laundering and Other Offenses*

On April 24, 2007, a federal grand jury in the District of Columbia handed down a four-count indictment against e-gold Ltd; its affiliate Gold & Silver Reserve, Inc.; and their owners, Dr. Douglas L. Jackson, Reid Jackson, and Barry K. Downey.¹⁶⁰ The government charged each of the defendants with one count of conspiracy to launder monetary instruments, one count of conspiracy to operate an unlicensed money transmitting business, one count of operating an unlicensed money transmitting business under federal law, and one count of money transmission without a license under D.C. law.¹⁶¹ The government alleged that “E-gold has been a highly favored method of payment by operators of investment scams, credit card and identity fraud, and sellers of online child pornography” and that e-gold facilitated payments “knowing that the funds involved were the proceeds of unlawful activity”¹⁶² If found guilty, the defendants could face up to 35 years in prison.¹⁶³

156. “[I]nvulnerable to government manipulation and subject to the kinds of market forces only a worldwide, 24/7 open-ended network can bring to bear, e-gold promises not simply better money but the best: a money supply kept so straight and narrow that it has room for neither bubbles nor crashes.” Julian Dibbel, *In Gold We Trust*, *WIRED*, Jan. 2002, at 3, <http://www.wired.com/wired/archive/10.01/egold.html>.

157. “DigiCash, the most innovative and best-publicized digital cash scheme, sought bankruptcy protection in 1998. CyberCash, a competitor, followed that route in 2001, the same year Beenz and Flooz, two rivals, closed their doors and left holders of their currencies high and dry.” Michael Mandel, *Money Ain’t What It Used To Be*, *Bus. Wk.*, Jan. 9, 2006, at 74.

158. Nadia Oehlsen, *U.S. Law Enforcers Are Cold on Gold*, *CARDS & PAYMENTS*, Apr. 2006, at 45.

159. *Id.* at 46.

160. Indictment, *supra* note 145, at 1, 26.

161. *Id.* at 9, 18, 25, 26.

162. Press Release, United States Department of Justice, *Digital Currency Business E-gold Indicted for Money Laundering and Illegal Money Transmitting* (Apr. 27, 2007), http://www.usdoj.gov/criminal/ceos/Press%20Releases/DC%20egold%20indict%20PR_042707.pdf [hereinafter “DOJ Press Release”].

163. Larry Greenemeier & Sharon Gaudin, *Law Abiding... or Criminal Enabler?*, *INFORMATIONWEEK*, May 7, 2007, at 20.

Count One of the indictment charges the defendants with transmitting monetary instruments or funds involving the proceeds of illegal activity with the intent of promoting that illegal activity, while knowing that the transactions were designed to conceal the source of the proceeds of the illegal activity.¹⁶⁴ At issue are transfers of e-gold from one account to another that the government alleges facilitated the sale of child pornography, stolen credit and debit card information, and various types of investment fraud, such as ponzi schemes and illegal high-yield investment programs.¹⁶⁵ The indictment identifies 36 specific e-gold transactions taking place between August 2000 and December 2005 with dollar values ranging from \$40 to \$725,000 that the government asserts were made in support of such illegal activity.¹⁶⁶

The remaining three counts of the indictment allege that e-gold operated as a money transmitter without an appropriate state license, failed to comply with federal money transmitter regulations, and transmitted funds known to have been derived from a criminal offense.¹⁶⁷ According to the government, e-gold failed to obtain a money transmitter's license in the District of Columbia¹⁶⁸ as is required by law.¹⁶⁹ Prosecutors further allege that e-gold ignored federal requirements to implement an anti-money laundering program¹⁷⁰ and to file reports of suspicious transactions (so-called "Suspicious Activity Reports" or "SARs") with the U.S. Department of the Treasury.¹⁷¹ The indictment alleges that e-gold failed to verify the identity of its customers, allowed accounts with obviously bogus names such as "Mickey Mouse" and "Anonymous Man," hired employees with no experience in financial services and provided them with little or no training, allowed transactions with suspicious notations such as "child porn" and "CC fraud," and did little or nothing to stop transactions tied to illegal behavior.¹⁷² As well as being independent violations of the law, these offenses constitute a criminal offense under 18 U.S.C. § 1960.¹⁷³

Although as of August 2007, the criminal prosecution of e-gold is in its early stages, the government has already won one significant victory. The court ordered

164. Indictment, *supra* note 145, at 9–10.

165. *Id.* at 7–8.

166. *Id.* at 14–18.

167. *Id.* at 18–19.

168. *Id.* at 22.

169. *Id.* at 26 (citing D.C. CODE ANN. § 26-1001(10) (LexisNexis 2001)).

170. *Id.* at 5 (citing 31 U.S.C. § 5318(h) (Supp. IV 2004) and its implementing regulations (31 C.F.R. § 103.125 (2007))).

171. *Id.* (citing 31 U.S.C. § 5318(g) (Supp. IV 2004) and its implementing regulations (31 C.F.R. § 103.20 (2007))).

172. *Id.* at 7, 11–12.

173. "Whoever knowingly conducts, controls, manages, supervises, directs, or owns all or part of an unlicensed money transmitting business, shall be fined in accordance with this title or imprisoned not more than 5 years, or both." 18 U.S.C. § 1960(a) (Supp. V 2005). Section 1960 was amended in 2001 with an effective date of October 1, 2004, and those amendments may terminate upon an appropriate joint resolution of Congress. *Id.* Given that some of the actions alleged in support of the indictment occurred before the effective date of the amendment, it is unclear to what degree section 1960 is applicable to defendants' alleged conduct.

the seizure of all of the assets of e-gold, including bank accounts, precious metals, and accounts receivable both in the United States and abroad.¹⁷⁴ The order stated it should not be construed “as limiting the e-gold operation’s ability to use its existing funds to satisfy requests from its customers to exchange e-gold into national currency, or its ability to sell precious metals to accomplish the same once approval has been received.”¹⁷⁵ Defendants complain, however, that the seizure order is so broad it has swept up all of their assets, and as a result “they simply do not have money with which to operate their businesses, pay attorneys’ fees, and pay for reasonable operating and living expenses.”¹⁷⁶ They asked the court to modify the terms of the warrants,¹⁷⁷ but the court denied their request.¹⁷⁸ Defendants have appealed that decision to the U.S. Court of Appeals for the D.C. Circuit.¹⁷⁹

c. *E-gold Defends Itself*

The e-gold defendants have asserted their innocence:

This is not a story of common criminals operating surreptitiously in a netherworld to launder money and commit crimes. Rather this is a case about three respected individuals—Douglas L. Jackson, M.D., a talented medical doctor; Barry K. Downey, a prominent lawyer; and Reid A. Jackson, a gifted systems analyst—who took seriously the rights and liberties guaranteed to them by the Constitution and laws of the United States and created an alternative global currency and payment system for the betterment of mankind. They did so forthrightly and openly, meeting at conferences with world bankers and representatives of international monetary funds, working hand-in-hand with various agencies of the United States government and even testifying on Capitol Hill about the nature of their business enterprise. They believed—and continue to believe—that they complied with all laws and regulations applicable to their business.

174. More specifically, the court ordered the seizure of:

All the assets, including without limitation, equipment, inventory, accounts receivable and bank accounts of E_GOLD, LTD. [sic], and GOLD & SILVER RESERVE, INC., whether titled in those names or not, including, but not limited to all precious metals, including gold, silver, platinum, and palladium, that “back” the e-metal electronic currency of the E_Gold [sic] operation, wherever located.

Post-Indictment Restraining Order at 4, *United States v. E-Gold Limited, Gold & Silver Reserve, Inc.*, Douglas L. Jackson, Brian K. Downey, and Reid A. Jackson, Crim. No. 07-109 (D.D.C. May 23, 2007).

175. *Id.*

176. Defendants’ Motion To Vacate Seizure Warrant and To Modify Restraining Order and Request for an Evidentiary Hearing at 1, *United States v. E-Gold Limited, Gold & Silver Reserve, Inc.*, Douglas L. Jackson, Barry K. Downey, and Reid A. Jackson, Crim. No. 07-109 (D.D.C. June 1, 2007).

177. *Id.*

178. Minute Entry Order at 1, *United States v. E-Gold Limited, Gold & Silver Reserve, Inc.*, Douglas L. Jackson, Barry K. Downey, and Reid A. Jackson, Crim. No. 07-109 (D.D.C. June 22, 2007).

179. Defendants’ Notice of Appeal and Request for Expedited Consideration at 1–2, *United States v. E-Gold Limited, Gold & Silver Reserve, Inc.*, Douglas L. Jackson, Barry K. Downey, and Reid A. Jackson, Crim. No. 07-109 (D.D.C. June 29, 2007), *appeal docketed*, No. 07-3074 (D.C. Cir. July 9, 2007). This appeal is fully briefed and oral argument has been scheduled for October 26, 2007. *United States v. E-Gold, Ltd.*, No. 07-3074 (D.C. Cir. Sept. 5, 2007) (order setting oral argument).

e-gold Ltd and G&SR, which represent an innovative new approach to exchanging value over the Internet in a global economy, are not subject to existing statutes and regulations drafted in an earlier day to govern "money transmitting businesses."¹⁸⁰

According to e-gold, not only do existing money transmitter laws not apply to it, several government officials and members of law enforcement concur in that opinion.¹⁸¹

One supporter has taken the initiative to create a short video extolling the innocence of e-gold and to post it on the Internet.¹⁸²

d. The Proper Application of Money Transmitter Laws to Cutting-Edge Payment Systems like E-gold Is Less than Clear

Based on the indictment, it appears that the government's theory of this case is that e-gold constitutes a money transmitter under 18 U.S.C. § 1960, and that fact triggers compliance obligations with money transmitter requirements found in 31 U.S.C. §§ 5330, 5318(g) and (h), and 31 C.F.R. part 103.¹⁸³ E-gold's position is that it is not a money transmitter under any definition and thus is not subject to any of these requirements.¹⁸⁴ Resolution of the debate is hampered by the fact that sections 1960, 5318, 5330, and 31 C.F.R. part 103 all contain different definitions of "money transmitter." The concept in each of the laws is similar, but the details are not the same. Because e-gold is operating outside the traditional realm of money transmitters, it is necessary to explore the nuances of the statutory definitions in order to determine whether the laws encompass e-gold. The inconsistencies in the statutes, coupled with potential criminal penalties in section 1960(a),¹⁸⁵ make advising clients who want to implement novel new payment mechanisms a difficult task.

As defined in 18 U.S.C. § 1960(b)(2), "money transmitting" includes "transferring funds on behalf of the public by any and all means including but not limited to transfers within this country or to locations abroad by wire, check, draft, facsimile, or courier."¹⁸⁶ E-gold asserts that it is not a money transmitter because it does not facilitate transfers of funds but rather allows users to trade precious metals.¹⁸⁷ If, however, e-gold is held to fall within the definition in section 1960(b)(2), then under section 1960(b)(1)(B), it also must comply with the requirements of 31 U.S.C. § 5330. On its face, section 5330 applies to a similar but different category of entities than section 1960, namely any business that:

180. May Status Report, *supra* note 149, at 1–2.

181. *E.g.*, May Status Report, *supra* note 149, at 3.

182. See You Tube, E-gold Digital Currency Testimony, <http://www.youtube.com/watch?v=Pvj-Px-C5ReY> (last visited Sept. 6, 2007), and Part 2: E-gold Digital Currency Testimony [sic], <http://www.youtube.com?v=bU9s97cUAAw> (last visited Sept. 6, 2007).

183. See Indictment, *supra* note 145, at 4–5.

184. See May Status Report, *supra* note 149, at 6–8.

185. "Whoever knowingly conducts, controls, manages, supervises, directs, or owns" an illegal money transmitting business may be fined or imprisoned for not more than 5 years. 18 U.S.C. § 1960(a) (Supp. V 2005).

186. 18 U.S.C. § 1960(b)(2) (Supp. V 2005).

187. See May Status Report, *supra* note 149, at 6–8.

- (A) provides check cashing, currency exchange, or money transmitting or remittance services, or issues or redeems money orders, travelers' checks, and other similar instruments or any other person who engages as a business in the transmission of funds, including any person who engages as a business in an informal money transfer system or any network of people who engage as a business in facilitating the transfer of money domestically or internationally outside of the conventional financial institutions system;
- (B) is required to file reports under section 5313; and
- (C) is not a depository institution (as defined in section 5313(g)).¹⁸⁸

E-gold denies that its activities fall within this definition.¹⁸⁹ The indictment explicitly alleges that e-gold operates as a "money transmitting business" as defined in section 1960(b)(2),¹⁹⁰ thus suggesting that the government will argue that it is the controlling definition.

The indictment also asserts that e-gold is required but has failed to implement an anti-money laundering program under 31 U.S.C. § 5318(h), which would include filing SARs when appropriate.¹⁹¹ Subsections 5318(g) and (h), however, only apply to "financial institutions" as that term is defined in 31 U.S.C. § 5312(a)(2).¹⁹² The latter subsection divides "financial institutions" into 26 categories, one of which is:

a licensed sender of money or any other person who engages as a business in the transmission of funds, including any person who engages as a business in an informal money transfer system or any network of people who engage as a business in facilitating the transfer of money domestically or internationally outside of the conventional financial institutions system.¹⁹³

To further complicate matters, the regulations implementing subsections 5318(g) and (h) classify "money transmitter" as one type of "money services business" or "MSB."¹⁹⁴ Under the MSB rules, a money transmitter is:

- (A) Any person, whether or not licensed or required to be licensed, who engages as a business in accepting currency, or funds denominated in currency, and transmits the currency or funds, or the value of the currency or funds, by any means through a financial agency or institution, a Federal Reserve Bank or other facility of one or more Federal Reserve Banks, the Board of Governors of the Federal Reserve System, or both, or an electronic funds transfer network; or
- (B) Any other person engaged as a business in the transfer of funds.¹⁹⁵

188. 31 U.S.C. § 5330(d)(1) (2000 & Supp. IV 2004).

189. See May Status Report, *supra* note 149, at 6–8.

190. Indictment, *supra* note 145, at 19.

191. *Id.* at 5.

192. 31 U.S.C. §§ 5318(g), (h) (2000 & Supp. IV 2004).

193. 31 U.S.C. § 5312(a)(2)(R) (Supp. IV 2004).

194. 31 C.F.R. § 103.11(uu) (2007). The other MSB categories are currency dealer or exchanger; check casher; issuer of traveler's checks, money orders, or stored value; seller or redeemer of traveler's checks, money orders, or stored value; and the U.S. Postal Service. *Id.*

195. 31 C.F.R. § 103.11(uu)(5)(i) (2007).

The regulations, however, note that the determination of whether a person qualifies as a money transmitter will depend on the specific facts and circumstances:

Generally, the acceptance and transmission of funds as an integral part of the execution and settlement of a transaction other than the funds transmission itself (for example, in connection with a bona fide sale of securities or other property), will not cause a person to be a money transmitter within the meaning of [this rule].¹⁹⁶

The MSB regulations suggest that if a business were to operate a legitimate online electronic commodity exchange dealing in precious metals, the fact that funds transmissions were made in order to settle the commodity transactions would not turn the enterprise into a money transmitter. Given that e-gold has already described itself as “the world’s first electronic currency designed for borderless, electronic business transactions over the Internet,”¹⁹⁷ it is unlikely that e-Gold could successfully make use of this defense.

E-Gold is being prosecuted, it appears, on an amalgam of all four laws. Because 18 U.S.C. § 1960 exposes individuals to criminal as opposed to civil liability for the business decisions of their companies, resolution of the ambiguities is essential for the market of electronic payment products to mature. At a technical level, failure to clarify the scope of the “money transmitter” laws—all four of them—coupled with criminal prosecution of businesses and their owners who run afoul of these laws will likely stifle the development of new electronic money products or raise compliance costs for new businesses.

2. The FTC Consent Decrees with Kmart and Darden Restaurants, Inc. for Their Gift Card Programs

Since our 2006 Survey, the Federal Trade Commission (“FTC”) has brought its first two enforcement actions against issuers and marketers of gift cards for practices related to the card terms—*In the Matter of Kmart Corporation, Kmart Services Corporation, and Kmart Promotions, LLC, corporations*¹⁹⁸ and *In the Matter of Darden Restaurants, Inc., GMRI, Inc., and Darden GC Group, Corp., corporations*.¹⁹⁹ The FTC made the consent decree with Darden Restaurants, Inc. final on May 7, 2007.²⁰⁰ Violations of the consent decrees carry possible civil penalties of \$11,000 per violation.²⁰¹

196. 31 C.F.R. § 103.11(uu)(5)(ii) (2007).

197. May Status Report, *supra* note 149, at 5.

198. Press Release, Federal Trade Commission, Kmart Settles with FTC over Gift Card Sales Practices (Mar. 12, 2007), <http://www.ftc.gov/opa/2007/03/kmart.shtm>.

199. Press Release, Federal Trade Commission, National Restaurant Company Settles FTC Charges for Deceptive Gift Card Sales (Apr. 3, 2007), <http://www.ftc.gov/opa/2007/04/darden.shtm>. Darden Restaurants, Inc. owns restaurant chains Olive Garden, Red Lobster, Smokey Bones, and Bahama Breeze. *Id.*

200. The comment period for the proposed Kmart consent decree ended April 10, 2007, and for the proposed Darden consent decree on May 2, 2007. See *supra* notes 198 and 199.

201. Press Release, Federal Trade Commission, Kmart Settles with FTC over Gift Card Sales Practices (Mar. 12, 2007), <http://www.ftc.gov/opa/2007/03/kmart.shtm>.

a. *Kmart*

The FTC charged that Kmart had promoted the cash-equivalent features of its gift cards but did not disclose fees it assessed after two years of non-use and also misrepresented that cards would not expire.²⁰² The proposed consent decree requires Kmart not to advertise or sell gift cards without disclosing clearly and prominently expiration dates or fees in all advertising and on the front of the gift cards.²⁰³ In addition, Kmart must disclose at the point of sale and prior to purchase all material terms and conditions of any expiration date or fee.²⁰⁴ Kmart also will be required to have a refund program to repay the dormancy fees it charged without disclosure and to publicize it.²⁰⁵

b. *Darden Restaurants, Inc.*

The FTC action against Darden Restaurants, Inc. is similar to that against Kmart. Darden promised that cards could be redeemed for their face value but did not disclose that dormancy fees would be deducted after a period of time depending on the individual cards' sale dates.²⁰⁶ Under the consent decree, Darden agrees to restore to each card the dormancy fees it assessed and to publicize the restoration program on its web site for two years.²⁰⁷ The FTC finally accepted the consent decree on May 7, 2007.²⁰⁸

3. The Federal Injunction Action Against Payment Processing, LLC

The term "demand drafts" refers to *orders to pay* ("drafts") that are (1) created by someone other than the person whose deposit account will be debited and (2) not signed by the person whose account will be debited.²⁰⁹ Demand drafts also are known as "telephone checks" or "remotely created checks."²¹⁰ Demand

202. *Id.*

203. *Id.*

204. *Id.*

205. *Id.*

206. Press Release, Federal Trade Commission, National Restaurant Company Settles FTC Charges for Deceptive Gift Card Sales (Apr. 3, 2007), <http://www.ftc.gov/opa/2007/04/darden.shtm>.

207. *Id.*

208. *In re* Darden Restaurants, Inc., GMRI, Inc., and Darden GC Group, Corp., corporations, Decision and Order, Docket No. C-4189 (FTC May 7, 2007), available at <http://www.ftc.gov/os/caselist/0623112/index.shtm>.

209. The type of "demand draft" described in this part does not include the category of drafts commonly used in letter-of-credit transactions, which present very different issues. For more information about "demand drafts" or "remotely created checks," see Collection of Checks and Other Items by Federal Reserve Banks and Funds Transfers Through Fedwire and Availability of Funds and Collection of Checks, 70 Fed. Reg. 71218 (Nov. 28, 2005) (to be codified at 12 C.F.R. pts. 210 & 229) [hereinafter "Collection of Checks"]; Press Release, Federal Trade Commission, Magazine Telemarketers Agree To Settle FTC Charges of Debiting Consumers' Checking Accounts Without Authorization (Oct. 18, 1996), <http://www.ftc.gov/opa/1996/10/genisis.shtm>; Press Release, Federal Trade Commission, Magazine Telemarketers Agree To Settle FTC Charges of Debiting Consumers' Checking Accounts Without Authorization (Oct. 21, 1996), <http://www.ftc.gov/opa/1996/10/diverse2.shtm>.

210. Collection of Checks, *supra* note 209, 70 Fed. Reg. at 71218.

drafts operate like conventional “checks” in the United States as instructions to depository institutions to pay a specified third party. Consumers use demand drafts or remotely created checks to pay credit card companies and merchants across the country for convenience and to avoid the risk of late payment charges from mail delays.²¹¹ Consumers also may give information about their bank accounts to creditors or marketing companies that contact them directly and that invite payment from the consumer’s checking account.²¹² Demand drafts, thus, are used by debt collectors and by telemarketers of many kinds of products.²¹³ They also help consumers who do not have credit cards make remote payments quickly.²¹⁴

“Demand drafts” have been in the news and on the minds of regulators and state legislatures for a decade. Demand drafts that start life as *paper-based* obligations are subject to special rules in Federal Reserve Board Regulation CC,²¹⁵ new “transfer” and “presentment” warranties in Articles 3 and 4 of the Uniform Commercial Code enacted by some states,²¹⁶ and a subset of the FTC’s Telemarketing Sales Rule.²¹⁷ The House Financial Services Committee Chairman Barney Frank has indicated that demand drafts are on the agenda for possible congressional legislation.²¹⁸ In adopting its Telemarketing Sales Rule, the FTC observed that telemarketers turned to demand drafts to obtain payments from consumers when credit card companies imposed stricter standards on credit card payments to telemarketing firms.²¹⁹ So, in a move contrary to other payment trends of the past decade or so, paper obligations replaced electronic obligations. However, some demand drafts

211. *Id.* at 71218–19.

212. *See id.* at 71218.

213. *See id.* at 71218–19.

214. *See id.*

215. *Id.* at 71221–23 (defining “remotely created checks” and warranties created by remotely created checks). Regulation CC covers only those demand drafts or “remotely created checks” that start life with the creation of a paper draft. *See id.* at 71219. Remotely created “orders” not originally in paper form would be subject to the Electronic Fund Transfer Act, Pub. L. No. 90-321, 82 Stat. 146 (1968) (codified as amended at 15 U.S.C. §§ 1601–1693 (2000 & Supp. V 2005)) and Regulation E, 12 C.F.R. pt. 205 (2007), on the theory that the deposit account number serves as the “access device” to the account, or the order is arguably not otherwise subject to any federal or state law.

216. Collection of Checks, 70 Fed. Reg. at 71219–20 & n.12.

217. For more information about the “demand draft” provisions of the Telemarketing Sales Rule, see Press Release, Federal Trade Commission, New Telemarketing Sales Rule “Strong New Weapon” Against Demand Draft Fraud, FTC Says (Apr. 15, 1996), <http://www.ftc.gov/opa/1996/04/jbsteest.shtm>. The Rule itself is codified at 6 C.F.R. pt. 310 (2007).

218. Stacy Kaper, *Check Fraud Query Made*, AM. BANKER, June 12, 2007, at 19 (noting that Congressman Edward Markey joined Chairman Frank in asking federal bank regulators to outline what they propose to do with remotely created checks including (a) how fraud involving remotely created checks compares with other bank products, (b) who bears the risk, and (c) what fraud prevention has been attempted, including records of related enforcement actions). For the letter from Chairman Frank and Representative Markey, see Press Release, House Committee on Financial Services, Markey and Frank Press Banking Regulators on Loophole Used by Fraudsters (June 11, 2007), http://www.house.gov/apps/list/press/financialsvcs_dem/press061107.shtml. The letter asked for a response by July 2, 2007. *Id.*

219. 16 C.F.R. pt. 310 (2007) (implementing the Telemarketing and Consumer Fraud and Abuse Prevention Act of 1994, Pub. L. No. 103-297, 108 Stat. 1545 (codified as amended at 15 U.S.C. §§ 6101–6108 (2000 & Supp. V 2005))).

now start as electronic obligations—hence, the reason for their mention in this Survey—as they start to move through automated clearing houses and become subject to different rules for electronic transactions.

There is a pending federal prosecution of Payment Processing, LLC, a non-depository processor of payments located in suburban Philadelphia.²²⁰ The U.S. Department of Justice has alleged that Payment Processing, LLC processed “demand drafts” on behalf of telemarketers who were engaged in fraudulent telemarketing campaigns. The multi-count indictment’s charges include alleged violations of federal mail and wire fraud statutes, 18 U.S.C. §§ 1341 and 1343, and bank fraud allegations pursuant to 18 U.S.C. § 3322(d).²²¹ In addition, the U.S. Department of Justice sought injunctive relief to freeze assets of the defendant pursuant to the Federal Anti-Fraud Injunction Statute, which is a civil action.²²² In November, 2006, in a related civil proceeding over the right to sums held by one of the depository banks in which Payment Processing Center, LLC held funds, the court held that credits in Payment Processing Center’s accounts with Wachovia had become “final” and no longer were susceptible to “chargeback” by the depository bank.²²³ Accordingly, the United States was entitled to restrain more than \$1 million in contested funds that *belonged to the defendant*, not to the bank.²²⁴

Because this is the first enforcement action against a *payments processor*, lawyers advising companies taking payments by demand drafts or remotely created checks should follow the proceeding. Lawyers also should be aware that, as mentioned earlier, Chairman Frank has expressed interest in new legislation pertaining to the use of demand drafts in consumer transactions as well as in clarification from the Federal Reserve Board about the potential applicability of either Regulation CC or Regulation E to these payment mechanisms.²²⁵

B. REGULATORY RELIEF: THE FEDERAL RESERVE BOARD EXEMPTS ISSUERS OF LOW-DOLLAR DEBIT CARD TRANSACTIONS FROM REGULATION E’S PAPER RECEIPT REQUIREMENTS

The Federal Reserve Board announced on June 28, 2007 that it had approved amendments to Regulation E²²⁶ to exempt transactions of \$15 or less from the

220. Complaint, *United States v. Payment Processing Center, LLC*, No. 06-725 (E.D. Pa. July 6, 2006), available at <http://www.usdoj.gov/usao/pae/News/Pr/2007/feb/Amended%20Complaint.pdf> [hereinafter “Complaint”]. The author of this part of the Survey has been retained as a potential expert in this proceeding. In an ancillary proceeding, the court determined the ownership of deposits held by depository institutions in the name of Payment Processing Center, LLC by reference to whether “final payment” had been made so as to preclude the depository banks’ exercise of “chargeback” pursuant to § 4-214 of the Uniform Commercial Code. For the most recent decision in this proceeding, see *United States v. Payment Processing Center, LLC*, 461 F. Supp. 2d 319 (E.D. Pa. 2006).

221. Complaint, *supra* note 220, at 1.

222. See *id.* at 1–2.

223. *Payment Processing Center, LLC*, 461 F. Supp. 2d at 326.

224. *Id.*

225. Press Release, House Committee on Financial Services, Markey and Frank Press Banking Regulators on Loophole Used by Fraudsters (June 11, 2007), http://www.house.gov/apps/list/press/financialsvcs_dem/press061107.shtml.

226. 12 C.F.R. pt. 205 (2007).

requirement that receipts be made available to consumers for transactions initiated at an electronic terminal.²²⁷ The exemption aims to facilitate consumers' ability to use debit cards in retail transactions where making receipts available may not be practical or cost effective.²²⁸ The amendments became effective on August 6, 2007.²²⁹

C. THE FEDERAL UNLAWFUL INTERNET GAMBLING ENFORCEMENT ACT OF 2006

Congress passed the Unlawful Internet Gambling Enforcement Act of 2006 ("UIGEA" or the "Act")²³⁰ on September 29, 2006. The Act establishes sanctions including civil or criminal penalties and imprisonment for up to five years, and prohibits gambling operations from taking payments by nearly all means currently available in the United States, including the proceeds of loan transactions, except cash. The Act has a substantial number of exemptions, such as for state lotteries, state-run casinos, horse racing, and fantasy sports.²³¹ The four primary provisions of the Act provide that:

No person engaged in the business of betting or wagering may knowingly accept, in connection with the participation of another person in unlawful Internet gambling—

- (1) credit, or the proceeds of credit, extended to or on behalf of such other person (including credit extended through the use of a credit card);
- (2) an electronic fund transfer, or funds transmitted . . . through a money transmitting business, or the proceeds of an electronic funds transfer . . . ;
- (3) any check . . . or similar instrument which is drawn on or payable at or through any financial institution; or
- (4) the proceeds of any other form of financial transaction, as the Secretary . . . and Federal Reserve may jointly prescribe by regulation. . . .²³²

Further, the Act:

- defines unlawful Internet gambling as "to place, receive, or otherwise knowingly transmit a bet or wager by any means which involves the use . . . of the Internet where such bet or wager is unlawful under any applicable Federal or State law in the State . . . in which the bet is . . . made";²³³
- provides that "the Secretary and the Board of Governors of the Federal Reserve System, in consultation with the Attorney General, shall prescribe

227. Electronic Fund Transfers, 72 Fed. Reg. 36589, 36590 (July 5, 2007) (codified at 12 C.F.R. pt. 205) [hereinafter "Electronic Fund Transfers"]. The announcement also is available at <http://www.federalreserve.gov/boarddocs/press/bcreg/2007/20070629/default.htm>.

228. Electronic Fund Transfers, *supra* note 227, 72 Fed. Reg. at 36590.

229. *Id.* at 36589.

230. Pub. L. No. 109-347, 120 Stat. 1952 (codified at 31 U.S.C.A. §§ 5361–5367 (West Supp. 2007)) [hereinafter "UIGEA"].

231. UIGEA, *supra* note 230, § 802(a), 120 Stat. at 1953 (codified at 31 U.S.C.A. § 5362 (West Supp. 2007)).

232. UIGEA, *supra* note 230, § 802(a), 120 Stat. at 1957 (codified at 31 U.S.C.A. § 5363 (West Supp. 2007)).

233. UIGEA, *supra* note 230, § 802(a), 120 Stat. at 1953 (codified at 31 U.S.C.A. § 5362(10) (West Supp. 2007)).

regulations . . . requiring each designated payment system, and all participants therein, to identify and block or otherwise prevent or prohibit restricted transactions through the establishment of policies and procedures reasonably designed to identify and block . . . the acceptance of restricted transactions”²³⁴

- provides that “[t]he United States, acting through the Attorney General, may institute proceedings . . . to prevent or restrain a restricted transaction . . . ,” and a state attorney general may obtain a “temporary restraining order, a preliminary injunction, or an injunction against any person to prevent or restrain a restricted transaction” However, “no provision of [the] subchapter shall be construed as authorizing the Attorney General of the United States, or the attorney general . . . of any State to institute proceedings . . . against any financial transaction provider”;²³⁵ and
- provides that “[a]ny person who violates section 5363 shall be fined . . . [and] imprisoned for not more than 5 years, or both,” and that “upon conviction . . . the court may enter a permanent injunction enjoining such person from placing, receiving, or otherwise making bets or wagers”²³⁶

Among the more controversial aspects of the Act is its extraterritorial effect over non-U.S. operators of Internet gambling operations.²³⁷ Regulations to implement the Act, to be proposed jointly by the Secretary of the Treasury and Board of Governors of the Federal Reserve System in consultation with the U.S. Department of Justice, were to be ready nine months after enactment—or on about July 10, 2007.²³⁸ As of August 30, 2007, no regulations have been promulgated.

Although the Act requires the *identification, coding, and blocking* of financial transactions to pay for unlawful Internet gambling, financial service providers obtained two types of protections from the Act’s harsh sanctions. First, financial institutions are not covered by the UIGEA if they do not own or control or are not owned or controlled by an entity in the business of betting or wagering.²³⁹ Second, financial services providers can comply by following the regulations that will be enacted pursuant to section 5364 of Title 31. Because so many payments in satisfaction of Internet gambling debts will be made of necessity in some electronic form, readers advising financial services providers and Internet gambling operators should follow developments and the forthcoming regulations carefully.²⁴⁰

234. UIGEA, *supra* note 230, § 802(a), 120 Stat. at 1958 (codified at 31 U.S.C.A. § 5364(a) (West Supp. 2007)).

235. UIGEA, *supra* note 230, § 802(a), 120 Stat. at 1959 (codified at 31 U.S.C.A. §§ 5365(b)(1), 5365(b)(2), 5365(d) (West Supp. 2007)).

236. UIGEA, *supra* note 230, § 802(a), 120 Stat. at 1961 (codified at 31 U.S.C.A. §§ 5366(a), (b) (West Supp. 2007)).

237. UIGEA, *supra* note 230, § 802(a), 120 Stat. at 1961 (codified at 31 U.S.C.A. § 5366(b) (West Supp. 2007)).

238. UIGEA, *supra* note 230, § 802(a), 120 Stat. at 1958 (codified at 31 U.S.C.A. § 5364(a) (West Supp. 2007)).

239. UIGEA, *supra* note 230, § 802(a), 120 Stat. at 1953 (codified at 31 U.S.C.A. § 5362 (West Supp. 2007)).

240. For more discussion of the UIGEA, see Anthony Cabot, *Keeping Current: Legislation—All Internet Bets Are Off, Offshore*, Bus. LAW TODAY, Mar./Apr. 2007, at 61.

In June 2007, the Interactive Media Entertainment & Gaming Association (“iMEGA”) sought an injunction to restrain the United States from enforcing the UIGEA arguing that the UIGEA “infringes on basic constitutional rights and sets a dangerous precedent for I-commerce by criminalizing the transmission of money” for activity that might be illegal in some locations.²⁴¹

CONCLUSION

Developments over the past year, and particularly the Supreme Court’s April 2007 decision in *Watters v. Wachovia Bank, N.A.*,²⁴² suggest that the laws pertaining to stored-value and other emerging electronic payment products, and their enforcement, will continue to develop along two distinct tracks. The Supreme Court has clarified that “visitorial” authority over payment providers that are federally chartered depository institutions or their subsidiaries is reserved to federal regulators of those entities.²⁴³ *Watters* has already been cited by a court that found preemption of state regulation of agents of federally chartered financial institutions,²⁴⁴ and by a court that found preemption of state law usury claims against a state-chartered, but federally insured bank.²⁴⁵ The states—and the FTC—will continue to have authority over issuance and marketing of stored-value cards in which federally chartered depository institutions have no involvement. This will lead, as noted last year, to increasing pressure on Congress to provide a national standard governing gift cards because of the increasingly interstate nature of the merchants issuing and marketing proprietary gift cards. Readers should stay aware of activity in Congress responding to the *Watters* decision, and should keep an eye on the House Financial Services Committee because Chairman Frank has announced his intention of finding a means for state roles in enforcing state laws against federally chartered banks and savings and loan associations.²⁴⁶

Congress also has shown through the enactment of the UIGEA a continued interest in regulating the use of the Internet and other electronic payment products. Congress passed the UIGEA despite the risk of eliciting protests from other members of the World Trade Organization and suits from payments providers and trade associations against its enforcement.²⁴⁷ Congress also has shown new interest in

241. See Press Release, iMEGA Corporation, iMEGA Files Lawsuit v. US Attorney General, FTC & Federal Reserve (June 5, 2007), <http://www.imega.org/2007/06/06/imega-files-lawsuit-against-attorney-general-alberto-gonzales-the-federal-trade-commission-and-the-federal-reserve-system/>. The complaint is available at <http://www.imega.org> (last visited Sept. 6, 2007).

242. *Watters v. Wachovia Bank, N.A.*, 127 S. Ct. 1559 (2007).

243. *Id.* at 1565.

244. *SPGGC, LLC v. Ayotte*, No. 06-2326, slip op. at 15 (1st Cir. May 30, 2007).

245. *Discover Bank v. Vaden*, 489 F.3d 594, 605 n.11, 606 (4th Cir. 2007) (citing 12 U.S.C.A. § 1831(d) (2000)).

246. See *Supreme Court Shuts Down Range of State Banking Laws in Gift to Predatory Lenders*, STATE-SIDE DISPATCH, Apr. 19, 2007, <http://www.progressivestates.org/content/596/washington-poised-to-be-second-paid-parental-leave-state>.

247. Tom Jones, *World Trade Organization Weakened by Internet Gambling Case*, CASINO GAMBLING WEB, May 30, 2007, http://www.casinogamblingweb.com/gambling_news/gambling-law/world_trade_organization_weakened_by_internet_gambling_case_46324.html; Warren Giles, *U.S. Ban on Web Gambling Rejected*, WASH. POST, Mar. 31, 2007, at D1. The government of Antigua and Barbuda filed

consumer protection for electronic payment transactions, even if the shape of potential regulation is not known at this time.

The Board of Governors of the Federal Reserve Board has shown a desire to clarify the scope of Regulation E²⁴⁸ to facilitate use of debit cards in low-dollar-value transactions by eliminating the requirements for paper receipts for transactions initiated at electronic terminals.

Federal prosecutors have pursued violations of the law by e-gold Ltd.²⁴⁹ and have prosecuted one payment intermediary²⁵⁰ that processed “demand drafts” or “remotely created checks” without obtaining a signature of the account holder or using a special access device, such as an ATM card.²⁵¹ Prosecutors are suing to enforce UIGEA, and the major trade association for the Internet gambling industry, iMEGA, has sued the U.S. Attorney General, the FTC, and the Board of Governors of the Federal Reserve System to prevent enforcement of that Act.²⁵² Finally, on May 7, 2007, the FTC made final its consent order with Darden Restaurants, Inc. pertaining to its gift card policies, requiring, among other things, restoration of fees collected prior to the settlement date and notice to consumers about the restoration of fees.²⁵³ Its earlier proposed consent decree with Kmart Corporation was pending as of July 7, 2007.

States continue to introduce and enact laws governing the terms and conditions of the issuance, sale, and redemption of gift and payroll cards. In the arena of payroll cards, as opposed to gift cards, the states may be able to exert more control over the terms on which cards are offered for a while longer because of the large role the states traditionally have played in the regulation of employers’ payment of wages and salaries to employees. States’ ability to enforce their new laws is at odds with the decision in *Watters*, as previously explained.

Looking forward, there are signals that the U.S. Department of the Treasury is interested in deterring the use of stored-value cards by money launderers, despite the absence of evidence to this point of any such use. The hypothesis that money launderers will find stored-value and other electronic payment products useful in their quest to evade detection by worldwide law enforcement officials remains a potent force in Treasury’s plans to thwart money laundering and terrorism finance globally. How Treasury proposes to proceed may be clearer as *next year’s* Survey of Cyberspace Law goes to print.

WTO compensation requests against the United States seeking \$3.4 billion a year from the United States for its failure to comply with the WHO ruling that U.S. Internet gambling restrictions are illegal. Lorraine Woellert, *A Web Gambling Fight Could Harm Free Trade*, *Bus. Wk.*, Aug. 13, 2007, at 43.

248. Electronic Fund Transfers, *supra* note 227, 71 Fed. Reg. 69430.

249. *See supra* notes 142–97 and accompanying text.

250. *See supra* notes 220–25 and accompanying text.

251. *Id.*

252. *See* Press Release, iMEGA Corporation, iMEGA Files Lawsuit v. US Attorney General, FTC & Federal Reserve (June 5, 2007), <http://www.imega.org/2007/06/06/imega-files-lawsuit-against-attorney-general-alberto-gonzales-the-federal-trade-commission-and-the-federal-reserve-system/>.

253. *In re* Darden Restaurants, Inc., GMRI, Inc., and Darden GC Group, Corp., corporations, Decision and Order, Docket No. C-4189 (FTC May 7, 2007), available at <http://www.ftc.gov/os/caselist/0623112/index.shtm>.

