National Consumer Law Center
Consumer Federation of America
Center for Responsible Lending
Consumer Action
Consumers Union
National Association of Consumer Advocates
National Consumers League
U.S. PIRG

October 9, 2015

By email to mbondoc@nacha.org
Maribel Bondoc
Manager, Network Rules
NACHA – The Electronic Payments Association
2550 Wasser Terrace, Suite 400
Herndon, VA 20171

Re: Comments on Third-Party Sender Registration Proposal

Dear Ms. Bondoc,

The National Consumer Law Center (on behalf of its low income clients), Consumer Federation of America, Center for Responsible Lending, Consumer Action, Consumers Union, National Association of Consumer Advocates, National Consumers League, and U.S. PIRG appreciate the opportunity to comment on NACHA's proposal to require registration of Third-Party Senders. We support the proposal and urge NACHA to strengthen it. We also urge NACHA to undertake other efforts to ensure that Third-Party Senders do not facilitate payment fraud.

Our organizations work on behalf of consumers and have a strong interest in efforts to stop fraud.[1] With the increasing role of electronic commerce as well as the alarming escalation of data breaches, stronger efforts to deter, detect and remedy fraud are needed.

Third-Party Senders Often Play a Critical Role in Enabling Fraud

Third-Party Senders (also called payment processors) play a critical role in many fraudulent schemes by enabling scammers to take unauthorized and fraudulent charges from consumers' accounts. These schemes can take various forms, including some that involve identity theft and some that focus on fraud in the inducement. While many third-party senders play a wholly legitimate role in helping merchants to process payments for lawful purposes, there are some that give fraudsters access to consumers' bank accounts and help those fraudsters launder payments and avoid detection.

Here are just a few recent examples of frauds that were enabled by third party senders. Some scams use ACH transactions, some charge debit and credit cards, and some create remotely created checks. But all show the pivotal role of the third party sender.

[1] Organizational descriptions are found in the attachment to these comments.

1. Global Client Solutions paid $6 million to settle charges by the Consumer Financial Protection Bureau that it violated the Telemarketing Sales Rule by making it possible for debt-settlement companies to charge consumers illegal upfront fees.[2] Global Client Solutions processed tens of millions of dollars in illegal advance fees from tens of thousands of consumers on behalf of hundreds of debt relief companies across the country. Debt settlement companies often promise to reduce consumers' debt but in fact leave them worse off.

2. The Federal Trade Commission cracked down on Process America, a payment processing operation that enabled "Google Money Tree" scammers to charge consumers $15 million in unauthorized charges.[3] Process America ignored plainly deceptive statements on merchant websites, chronically excessive chargeback rates from suspect merchants, and notices that the merchant should be placed in programs to monitor excessive chargebacks. The processor engaged in tactics that were designed to evade fraud monitoring programs, including submitting merchant applications containing false information and "load balancing" – distributing transaction volume among numerous merchant accounts so that the lower dollar amounts were less likely to trigger detection.

3. The Third Circuit Court of Appeals recently overturned the denial of class certification in a case brought against Zions National Bank and its payment processor for enabling scammers to use bank account information obtained from seniors to debit their accounts for unauthorized charges.[4] Last year, the lead attorney on the case, Howard Langer, submitted testimony before Congress explaining how the frauds were able to migrate from bank to bank:

> "The very same persons who operated the NHS fraud through Zions had operated a similar fraud through Wachovia. Several of the frauds involved in the T-Bank and First Bank of Delaware cases had simply migrated to Zions. Had the banks engaged in the most rudimentary due diligence they would have turned up these migrating frauds. Wachovia and Zions both obtained the fraudulent customers through what are known as account brokers. The account broker who brought PPC to Wachovia testified that four other banks had refused to open accounts for PPC before Wachovia accepted it. The perpetrator of the NHS fraud testified that he was approached by an account broker who brought his account to Zions within twenty-four hours of losing his prior access to the banking system, through a court order freezing PPC's accounts at Wachovia."[5]

4. Earlier this year, in a case brought by the Department of Justice through Operation Choke Point,Neil Godfrey pleaded guilty to criminal charges that he used Check Site Inc., a payment

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[2] CFPB, Press Release, "CFPB Takes Action Against Global Client Solutions for Processing Illegal Debt-Settlement Fees" (Aug. 25, 2014), http://www.consumerfinance.gov/newsroom/cfpb-takes-action-against-global-client-solutions-for-processing-illegal-debt-settlement-fees/.

[3] FTC, Press Release, "FTC Settlements Crack Down on Payment Processing Operation that Enabled 'Google Money Tree' Scammers to Charge Consumers $15 Million in Hidden Fees" (Nov. 18, 2013), http://www.ftc.gov/news-events/press-releases/2013/11/ftc-settlements-crack-down-payment-processing-operation-enabled.

[4] Reyes v. Netdeposit, LLC, --- F.3d ----, 2015 WL 5131287 (Sept. 2, 2015).

[5] Written testimony of Howard Langer to members of U.S. House Judiciary Committee re Operation Choke Point, (July 15, 2014), http://www.nclc.org/images/pdf/banking_and_payment_systems/payment-fraud/letter-howard-lange-bachus-johnson.pdf.

processor, to help scammers take millions of dollars from consumers.[6] Purported payday loan websites were actually a ruse to harvest bank account information. In addition to helping scammers find banks that were willing to ignore red flags, Godfrey helped the fraudulent merchants stay off the radar of other banks and regulators so that the fraud could continue. For example, Godfrey advised merchants how to change the names of their companies and set up the facade of a legitimate company to defeat banks' attempts at due diligence. In an email message quoted in the information, Godfrey advised a fraudulent merchant:

> [T]he lesson we have learned is that we must trick the [bank] folk. It means you need to set up some type of website front. What we need to do is set up a legitimate website selling anything you can think of – that is what you get approved on. It is irrelevant if anything is ever sold there – just so it exists. . . . In the mean time we set up false credit card approval etcetera. It is this we use to run the transactions. Yes, there will be a lot of returns, but what we do is send through transactions over the next few weeks that don't have high returns. They stop looking and then we can run the regular stuff. . . . [A]fter several months we junk that company and go to another company.[7]

Third-Party Sender Registration Will Help NACHA and ODFIs to Mitigate the Risk of Fraud

We support the proposal to require Originating Depository Financial Institutions (ODFIs) to register their third-party senders with NACHA and to apprise NACHA of any changes, including termination of an account. It is critical that these registration requirements will also include third-party senders who do not have a direct relationship with the ODFI but instead submit payments through another third-party sender ("nested" third-party senders). As the FDIC has explained:

> [F]inancial institutions and examiners should be alert for payment processors that use more than one financial institution to process merchant client payments, or nested arrangements where a payment processor's merchant client is also doing third-party payment processing. Spreading the activity among several institutions may allow processors that engage in inappropriate activity to avoid detection. For example, a single institution may not detect high levels of returned items if they are spread among several financial institutions. Payment processors also may use multiple financial institutions in case one or more of the relationships is terminated as a result of suspicious activity."[8]

The new reporting obligations, as well as the registry and associated enforcement tools, will help NACHA and ODFIs to improve know-your-customer (KYC) due diligence, detect patterns, and prevent fraud. Improved monitoring will enhance the ability to spot third-party senders who have been terminated for fraud and are attempting to move to another institution, who are spreading fraudulent payments among several institutions to avoid detection, and who are laundering fraudulent payments through nesting relationships.

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[6] U.S. DOJ, Press Release, "California Payment Processing Company Owner Pleads Guilty to Fraud" (July 16, 2015), http://www.justice.gov/opa/pr/california-payment-processing-company-operator-pleads-guilty-fraud.

[7] *Id.*

[8] Michael Benardo et al., Fed. Deposit Ins. Corp., Managing Risks in Third-Party Payment Processor Relationships, Supervisory Insights, at 8–9 (Summer 2011).

We also support the proposal to require ODFIs who have third-party sender customers to pay a registration fee, rather than spreading the costs of the registry among all ACH participants. It is appropriate that those ODFIs who profit from third-party sender customers should bear the costs of monitoring the risks that those customers pose.

The Proposal Should Be Strengthened to Improve the Ability to Detect Fraud

While we support the proposal, we urge that NACHA strengthen it in several respects.

First, we urge NACHA to require all of the information listed in proposed Section 2.17.3(f)-(j), rather than obtaining that information only upon request. Knowing doing-business-as names, the identity of the principals, and the approximate number of originators, along with the other information, will help NACHA to connect the dots when problems at one ODFI or third-party sender should raise red flags at others. NACHA should be proactively looking for these connections, not waiting for the connections to become apparent.

Second, some of the registry information should be visible to parties beyond NACHA. ODFIs should be able to see whether their customers also have relationships with other financial institutions or with other third-party senders. That information can help the ODFI to assess whether the third-party sender could be spreading fraudulent payments among various institutions to avoid detection. Moreover, the information in the registry should be available to government regulators and enforcement authorities, who can also help to detect patterns.

Third, proposed Section 2.15.1 should be modified to require third-party senders to identify their originators to ODFIs and not simply to provide that information upon request. NACHA should also require ODFIs to check the NACHA watch lists to ensure that the originator is not in NACHA's Terminated Originator Database and to adopt strict monitoring if the originator is on the Originator Watch List. ODFIs cannot do this due diligence if they do not have the names of the originators.

Finally, NACHA should go beyond compiling a list of third-party senders and should work towards aggregating the return rates of third-party senders and their originators across institutions. No amount of due diligence on the part of ODFIs will help if a fraudster is able to conceal the fraud by keeping return rates at any one institution below levels of suspicion. NACHA should consider required reporting of return rates below the levels currently required. While these lower return rates would not trigger the same obligations as higher return rates do, NACHA could aggregate them with returns reported by other ODFIs to identify if certain third-party senders or originators need closer examination.

For example, currently, ODFIs have reporting obligations if unauthorized returns for an originator exceed 0.5 percent. That rate is more than 16 times the average return rate (indeed, the trigger rate should be reduced to 0.3, 10 times the average). There is no reason for any originator to have more than de minimis unauthorized returns. If ODFIs (and, in turn, their third-party senders) were required to report returns that exceed twice the average return rate, NACHA could aggregate those returns to see whether there are patterns that bear investigation. Greater reporting and scrutiny could be especially helpful for nested third-party senders.

* * *

Thank you for the opportunity to submit these comments and for your efforts to improve risk monitoring in the ACH system.

Yours very truly,

National Consumer Law Center (on behalf of its low income client)
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APPENDIX: Organizational Biographies

Since 1969, the nonprofit **National Consumer Law Center® (NCLC®)** has used its expertise in consumer law and energy policy to work for consumer justice and economic security for low-income and other disadvantaged people, including older adults, in the United States. NCLC's expertise includes policy analysis and advocacy; consumer law and energy publications; litigation; expert witness services, and training and advice for advocates. NCLC works with nonprofit and legal services organizations, private attorneys, policymakers, and federal and state government and courts across the nation to stop exploitive practices, help financially stressed families build and retain wealth, and advance economic fairness.

The **Center for Responsible Lending (CRL**) is a nonprofit, non-partisan research and policy organization dedicated to protecting homeownership and family wealth by working to eliminate abusive financial practices. CRL is an affiliate of Self-Help, a nonprofit community development financial institution. For 30 years, Self-Help has focused on creating asset building opportunities for low-income, rural, women-headed, and minority families, primarily through financing safe, affordable home loans.

The **Consumer Federation of America** is an association of nearly 300 nonprofit consumer groups that was established in 1968 to advance the consumer interest through research, advocacy and education.

Consumer Action has been a champion of underrepresented consumers nationwide since 1971. A nonprofit 501(c)3 organization, Consumer Action focuses on financial education that empowers low to moderate income and limited-English-speaking consumers to financially prosper. It also advocates for consumers in the media and before lawmakers to advance consumer rights and promote industry-wide change. By providing financial education materials in multiple languages, a free national hotline and regular financial product surveys, Consumer Action helps consumers assert their rights in the marketplace and make financially savvy choices. More than 8,000 community and grassroots organizations benefit annually from its extensive outreach programs, training materials, and support.

Consumers Union is the public policy and advocacy division of Consumer Reports. Consumers Union works for telecommunications reform, health reform, food and product safety, financial reform, and other consumer issues. Consumer Reports is the world's largest independent product-testing organization. Using its more than 50 labs, auto test center, and survey research center, the nonprofit rates thousands of products and services annually. Founded in 1936, Consumer Reports has over 8 million subscribers to its magazine, website, and other publications. The National Association of Consumer Advocates (NACA) is a non-profit corporation whose members are private and public sector attorneys, legal services attorneys, law professors, and law students, whose primary focus involves the protection and representation of consumers. NACA's mission is to promote justice for all consumers.

National Consumers League, founded in 1899, is the nation's pioneering consumer organization. Our non-profit mission is to protect and promote social and economic justice for consumers and workers in the United States and abroad.

U.S. Public Interest Research Group (U.S. PIRG) serves as the Federation of State PIRGs, which are non-profit, non-partisan public interest advocacy organizations that take on powerful interests on behalf of their members. For years, U.S. PIRG's consumer program has designated a fair financial marketplace as a priority. Our advocacy work has focused on issues including credit and debit cards, deposit accounts, payday lending and rent-to-own, credit reporting and credit scoring and opposition to preemption of strong state laws and enforcement.