

COMMENTS
of the
CENTER FOR RESPONSIBLE LENDING

and

CONSUMER ACTION
CONSUMER FEDERATION OF AMERICA
CONSUMERS UNION
NATIONAL ASSOCIATION OF CONSUMER ADVOCATES
NATIONAL CONSUMER LAW CENTER (on behalf of its low-income clients)
U.S. PIRG

on

Regulation E
pursuant to
12 CFR Part 205
Docket No. R-1343

March 30, 2009

VIA ELECTRONIC SUBMISSION

Jennifer J. Johnson
Secretary
Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue, N.W.
Washington, DC 20551

The **Center for Responsible Lending**, along with **Consumer Action**,¹ **Consumer Federation of America**,² **Consumers Union**,³ **National Association of Consumer Advocates**,⁴ **National Consumer Law Center (on behalf of its low-income clients)**,⁵ and **U.S. PIRG**⁶ provide the following comments regarding the Federal Reserve Board's proposed rule to amend Regulation E pursuant to the Electronic Funds Transfer Act. While some discussion in this comment is specific to the Center for Responsible

¹ **Consumer Action** (www.consumer-action.org) is a national non-profit education and advocacy organization that has served consumers since 1971. Consumer Action (CA) serves consumers nationwide by advancing consumer rights in the fields of credit, banking, housing, privacy, insurance and utilities. CA offers many free services to consumers and communities. Consumer Action develops free consumer education modules and multi-lingual materials, for its network of more than 11,000 community based organizations. The modules include publications in Chinese, English, Korean, Spanish and Vietnamese.

² The **Consumer Federation of America** is a nonprofit association of over 280 pro-consumer groups, with a combined membership of 50 million people. CFA was founded in 1968 to advance consumers' interests through advocacy and education.

³ **Consumers Union** is a nonprofit membership organization chartered in 1936 under the laws of the state of New York to provide consumers with information, education and counsel about good, services, health and personal finance, and to initiate and cooperate with individual and group efforts to maintain and enhance the quality of life for consumers. Consumers Union's income is solely derived from the sale of Consumer Reports, its other publications and from noncommercial contributions, grants and fees. In addition to reports on Consumers Union's own product testing, Consumer Reports with more than 5 million paid circulation, regularly, carries articles on health, product safety, marketplace economics and legislative, judicial and regulatory actions which affect consumer welfare. Consumers Union's publications carry no advertising and receive no commercial support.

⁴ The **National Association of Consumer Advocates, Inc. (NACA)** is a nonprofit 501(c)(3) organization founded in 1994. NACA's mission is to provide legal assistance and education to victims of consumer abuse. NACA, through educational programs and outreach initiatives protects consumers, particularly low income consumers, from fraudulent, abusive and predatory business practices. NACA also trains and mentors a national network of over 1400 attorneys in representing consumers' rights.

⁵ The **National Consumer Law Center, Inc. (NCLC)** is a non-profit corporation, founded in 1969, specializing in low-income consumer issues, with an emphasis on consumer credit. On a daily basis, NCLC provides legal and technical consulting and assistance on consumer law issues to legal services, government, and private attorneys representing low-income consumers across the country. NCLC publishes and regularly updates a series of sixteen practice treatises and annual supplements on consumer credit laws, including Truth In Lending, Cost of Credit, Consumer Banking and Payments Law, Foreclosures, and Consumer Bankruptcy Law and Practice, as well as bimonthly newsletters on a range of topics related to consumer credit issues and low-income consumers. NCLC attorneys have written and advocated extensively on all aspects of consumer law affecting low income people, conducted training for tens of thousands of legal services and private attorneys on the law and litigation strategies to deal predatory lending and other consumer law problems, and provided extensive oral and written testimony to numerous Congressional committees on these topics. NCLC's attorneys have been closely involved with the enactment of the all federal laws affecting consumer credit since the 1970s, and regularly provide comprehensive comments to the federal agencies on the regulations under these laws.

⁶ The **U.S. Public Interest Research Group** serves as the federation of and federal advocacy office for the state PIRGs, which are non-profit, non-partisan public interest advocacy groups that take on powerful interests on behalf of their members.

Lending's affiliate, Self-Help Credit Union, all groups signing on to this comment concur in the policy recommendations provided.

The Center for Responsible Lending (CRL) is a not-for-profit, 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, which consists of a credit union and a non-profit loan fund.

For the past 28 years, Self-Help has focused on creating ownership opportunities for low-wealth families, primarily through financing home loans to low-income and minority families who otherwise might not have been able to purchase homes. Self-Help has provided over \$5 billion in financing to more than 60,000 low-wealth families, small businesses and nonprofit organizations in North Carolina and across the United States.

Self-Help has operated a North Carolina-chartered credit union since the early 1980s. Beginning in 2004, Self-Help Credit Union (SHCU) merged with three community credit unions that offer a full range of retail products,⁷ and it now services over 3,500 checking accounts and approximately 20,000 other deposit accounts.⁸ In 2008, Self-Help founded Self-Help Federal Credit Union to expand Self-Help's mission. SHCU complies with the National Credit Union Administration's (NCUA) regulations on overdraft practices, and it must do so as a relatively small provider of retail services. CRL has consulted with SHCU in formulating these recommendations. SHCU is already operating in accordance with some of these recommendations, and the rest would be operationally feasible.

SHCU does not offer a fee-based overdraft program, and it denies debit and ATM transactions when the customer does not have sufficient funds. It is currently converting its retail locations from batch processing—where all debit point-of-sale and ATM transactions are processed together twice daily—to on-line, real-time processing. It expects all locations to be converted by mid-2009. During this transition, if a debit card overdraft is inadvertently paid, SHCU does not charge the customer a fee for covering the payment.

SHCU customers can apply for an overdraft line of credit of up to \$500, carrying an interest rate of 16 percent. Customers may also link their checking account to their savings account, and SHCU charges a \$1 fee for each transfer from savings to checking. To avoid encouraging customers to purposefully use this overdraft coverage for short-term cash shortfalls, SHCU only allows customers' accounts to be overdrawn by checks and ACH transactions, and not by point-of-sale or ATM transactions, even with these lower cost overdraft options.

⁷ SHCU merged with Wilson Community Credit Union and Scotland Community Credit Union in 2004 and with Cape Fear Community Credit Union in 2006.

⁸ These include traditional savings accounts, money market accounts, certificates of deposits, and individual retirement accounts.

INTRODUCTION

We thank the Federal Reserve Board (the Board) for focusing its efforts on abusive overdraft practices in its Proposed Rule to Amend Regulation E (the Proposed Rule).⁹ While we continue to urge the Board to address abusive overdraft fees on all types of transactions, we thank the Board for considering an opt-in arrangement for debit card purchases and ATM withdrawals.

Overdraft fees on debit card and ATM transactions cost American families \$7.8 billion each year. Debit card transactions are the most common trigger of overdrafts¹⁰ and, relative to the cost of the overdraft, the most expensive.¹¹ Overdraft fees on these transactions are particularly harmful because consumers are often surprised to learn they can overdraft with their debit card, expecting purchases and ATM withdrawals to be denied if they lack sufficient funds.¹² These charges also often occur in clusters, as many consumers tend to use their cards for multiple small purchases within a short time. Some financial institutions maximize these fees by allowing overdrafts rather than denying them at the terminal and by manipulating the order in which they post transactions to deplete accounts as quickly as possible.

Institutions should not be allowed to charge consumers overdraft fees for debit card purchases and ATM withdrawals without their affirmative consent. When the Board makes a choice between its opt-in and opt-out alternatives, it will be determining the default arrangement. The default is critical because, as the Board acknowledges, a wide variety of economics research concludes that most account holders won't change the default. Two key facts compel the Board to set the default at no automatic enrollment:

- **The cost-benefit analysis indisputably favors no automatic coverage.** The cost of fee-based overdraft, particularly for debit purchases and ATM withdrawals, dramatically exceeds the benefit. *It's not a close call.*

⁹ 74 Fed. Reg. 5212 (Jan. 29, 2009).

¹⁰ Eric Halperin, Lisa James, and Peter Smith, *Debit Card Danger: Banks offer little warning and few choices as customers pay a high price for debit card overdrafts*, Center for Responsible Lending, at 24 (Jan. 25, 2007), available at <http://www.responsiblelending.org/pdfs/Debit-Card-Danger-report.pdf> [hereinafter *Debit Card Danger*]. See also FDIC Study of Bank Overdraft Programs (Nov. 2008) [hereinafter *FDIC Study*] (finding 41 percent of NSF-related transactions were triggered by point-of-sale/debit and another 7.8 percent by ATM transactions).

¹¹ *Debit Card Danger, Id.*, at 25.

¹² A recent nationally representative telephone poll addressing overdraft fees found that 39 percent of consumers expected their bank to deny a debit card transaction or cover it for no fee if they lacked sufficient funds. Forty-eight percent of consumers thought their withdrawal would be denied at an ATM, and another 10 percent thought they would not be charged a fee. Comments of Consumers Union on Regulation E: R-1343, at 3 (Mar. 12, 2009) [hereinafter *Consumers Union Comments*] (citing Financial Regulation Poll Final Report at 3, *Consumer Reports* National Research Center (Feb. 13, 2009)).

- **Consumer preferences indisputably favor no automatic coverage.** Statistically valid nationwide surveys have repeatedly found that consumers overwhelmingly don't want fee-based coverage of these transactions. *Again, it's not a close call.*

While we were disappointed that the Board's new rule does not address checks and ACH transactions, limiting the proposal to debit card and ATM transactions makes the arguments for an opt-in arrangement virtually impossible to credibly refute. Indeed, the only benefit derived from an opt-out arrangement will accrue to financial institutions' revenue streams. An opt-out arrangement would offer American families little more than an ostensible choice about an opaque system designed to charge them billions in fees in exchange for a "service" that offers them no benefit.

In response to the previously issued Proposed Rule on Unfair or Deceptive Acts or Practices (the UDAP Proposal),¹³ CRL submitted comments urging the Board to require an opt-in arrangement instead of an opt-out arrangement and addressing other issues in the proposal.¹⁴ CRL, along with CFA, NCLC and Consumers Union, also submitted comments in response to the previously issued Proposed Rule to Amend Regulation DD pursuant to the Truth in Savings Act,¹⁵ where we addressed the proposed opt-out disclosures and recommended an opt-in form. To avoid undue repetition, we will refer frequently to those two comments throughout this letter.

In our UDAP Comments, we discussed several recommendations related to overdraft fees that are not considered in the Board's current proposal:

- Subject fee-based overdraft loans to Regulation Z requirements under the Truth in Lending Act (TILA).
- Limit the number of overdraft fees that may be charged to four per year or, alternatively, one within a 60-day period.
- Prohibit overdraft fees for overdrafts caused solely by the lag time between the institution's receipt and posting of a deposit.

¹³ 73 Fed. Reg. 28904 (May 19, 2008).

¹⁴ Comments of the Center for Responsible Lending to Board of Governors of the Federal Reserve System, Office of Thrift Supervision and National Credit Union Administration on Proposed Rule Regarding Unfair and Deceptive Practices—Overdraft Practices (Aug. 4, 2008), *available at* <http://www.responsiblelending.org/pdfs/overdraft-comments-udap-final-as-submitted-w-appendices-080408-2.pdf> [hereinafter UDAP Comments].

¹⁵ Comments of the Center for Responsible Lending, along with Consumer Federation of America, Consumers Union and National Consumer Law Center, to Board of Governors of the Federal Reserve System on proposed amendments to Regulation DD, promulgated pursuant to the Truth in Savings Act, Docket No. R-1315 (July 18, 2008) *available at* <http://www.responsiblelending.org/pdfs/crl-reg-dd-comments-071808-w-appendices-as-submitted.pdf> [hereinafter Regulation DD Comments].

- Immediately prohibit manipulative clearing practices that maximize overdraft fees.

We will not repeat our discussions of those recommendations here; however, we continue to emphatically urge the Board to take immediate steps to implement them.

Summary of recommendations addressed herein:

- **Revisit the proposal to use the Board’s UDAP authority under FTC Act to require institutions to provide a choice about coverage for checks and ACH transactions.**
- **Require institutions to obtain account holders’ affirmative opt-in before charging them overdraft fees for debit card purchases and ATM withdrawals.**
- **Allow no exceptions that would result in a debit card purchase or ATM withdrawal triggering an overdraft fee for account holders who have not chosen coverage.** Instead, place the expectation on institutions, card processors, and merchants to resolve operational issues among themselves. If overdrafts are inadvertently covered, the account holder should not be charged a fee.
- **Prohibit institutions from treating checks and ACH transactions differently depending on whether a consumer chooses fee-based overdraft coverage for debit card purchases and ATM transactions.** Otherwise, account holders may be unduly discouraged from choosing to not have overdrafts from debit card purchases and ATM transactions covered.
- **Require institutions to offer checking accounts with identical terms, except for whether overdrafts from debit card purchases and ATM withdrawals are covered for a fee.** Otherwise, institutions may design accounts aimed to steer account holders into fee-based coverage.
- **Require notice of the right to opt-in/opt-out before existing account holders are charged their first overdraft fee following the effective date.**
- **Prohibit overdraft fees caused solely by debit holds under any circumstances.** The Board’s current proposal would continue to allow account holders who have not in fact overspent their accounts to be charged overdraft fees, which is simply unjustifiable.

I. Option to choose should apply to all transactions.

In our UDAP Comments, we urged the Board not to exclude checks and ACH transactions from the right to opt-in or opt-out.¹⁶ We ask the Board to reconsider using its UDAP authority under the FTC Act to provide, at a minimum, the right to opt-out of fee-based coverage of these transactions.

Nearly 90 percent of account holders want a choice about whether they have fee-based overdraft coverage.¹⁷ To deprive them of *any choice* about whether they are exposed to high-cost overdraft fees for checks and ACH transactions, which together account for 55 percent of all overdraft fees,¹⁸ is indeed an unfair and deceptive practice.

Even if coverage of a check or ACH transaction may benefit some account holders in the context of a single covered transaction, fee-based overdraft for these transactions ultimately harms account holders more than benefits them. For account holders who pay the majority of overdrafts, coverage causes repeat overdrafts that drive account holders deeper into debt and prevent them from meeting obligations they otherwise would have been able to pay. Public policy clearly supports giving account holders the option to select a cheaper alternative, like a line of credit, or no coverage at all, for all types of transactions. See UDAP Comments for further discussion.¹⁹

The Board based its decision to exclude checks and ACH transactions in part on its limited consumer testing.²⁰ This is problematic for several reasons. The Board's sample size of 18 consumers is an extremely small number on which to base national policy, especially when much larger surveys have found that consumers undoubtedly want a choice about overdraft coverage. In any event, the Board's testing found only that some consumers wanted coverage of their checks and ACH transactions—not that consumers should not be offered a choice about whether these transactions are covered. Moreover, it is unsurprising that some consumers would want these transactions covered by fee-based overdraft programs when they are given no adequate cost of credit disclosure and, as a

¹⁶ UDAP Comments, *Id.*, at 32-33.

¹⁷ A January 2008 CRL survey found that of consumers with a preference, 88 percent of all consumers, and 91 percent of respondents enrolled in a fee-based program, want a choice about whether or not a loan program is included with their account. The preference was even stronger—94 percent—among those who had overdrawn their account in the last six months. Leslie Parrish, *Consumers Want Informed Choice on Overdraft Fees and Banking Options*, CRL Research Brief (Apr. 16, 2008), available at <http://www.responsiblelending.org/pdfs/final-caravan-survey-4-16-08.pdf> [hereinafter 2008 CRL Research Brief].

¹⁸ *Debit Card Danger*, *supra* note 10, at 24 (noting that checks account for 27 percent and electronic transactions 28 percent of all transactions triggering overdrafts).

¹⁹ UDAP Comments, *supra* note 15, at 32-33.

²⁰ 74 Fed. Reg. 5216.

result, may not realize how expensive fee-based coverage is relative to alternative forms of overdraft coverage or other methods of payment.

II. Institutions should be required to obtain account holders’ affirmative consent before enrolling them in fee-based overdraft programs.

The reasoning favoring an opt-in arrangement for all transactions, as we presented in our UDAP Comments, is only stronger when applied strictly to debit card purchases and ATM transactions. In this section, we revisit that reasoning, applied only to debit card purchases and ATM transactions. Our previous argument is bolstered by recent consumer surveys tailored to determine consumer preferences about whether these transactions should be addressed through an opt-in or opt-out arrangement.

The default arrangement is critical because a wide range of evidence suggests that the vast majority of account holders will not alter the initial default status of the account. Therefore, it should be the arrangement that (1) causes consumers more benefit than harm and (2) better reflects consumer preferences.

(1) Fee-based overdraft on debit card purchases and ATM withdrawals indisputably causes account holders more harm than benefit, leaving them worse off than they would have been with lower cost alternatives or even with no overdraft coverage at all.

(2) Statistically valid surveys overwhelmingly indicate that consumers want a choice about whether their transactions are covered; would prefer to have their debit card denied than covered for a fee; and, in a survey recently conducted, 80 percent of people who want choice prefer opt-in over opt-out.

A. The default rule is critical because account holders are highly likely to stick with it.

The Board recognizes the power of the default in its Proposal: “Under an opt-out approach, consumers who may prefer to have ATM and debit card transactions declined if they would result in an overdraft may nonetheless incur overdraft fees simply because they fail to act on the notice.”²¹

The primary purpose of the Electronic Fund Transfer Act is to provide for “individual consumer rights” in the context of electronic fund transfer systems.²² The power of the default imparts responsibility upon the Board, as implementing agency for the statute, to

²¹ 74 Fed. Reg. 5224-25 (noting that “Various studies suggest that consumers are likely to adhere to the established default rule . . . even if the default rule may not always be in their best interest.”).

²² “It is the purpose of [the Act] to provide a basic framework establishing the rights, liabilities, and responsibilities of participants in electronic fund transfer systems. *The primary objective of this subchapter, however, is the provision of individual consumer rights.*” 15 U.S.C. 1693(b) (emphasis added).

select the default that maximizes consumer benefit. As we noted in our UDAP Comments, scholars have identified at least two approaches policymakers may take when designing a default: a cost-benefit analysis focused on welfare effects or an analysis of individuals’ preferences. Either approach, as demonstrated by the analyses below, compels the Board to set the default at no fee-based overdraft coverage for debit card purchases and ATM withdrawals. For a more complete discussion of the power of the default, including discussion of related behavioral economics research, *see* our UDAP Comments.²³

B. A cost/benefit analysis or an analysis of consumer preferences compels an opt-in arrangement.

1. *Cost/benefit analysis: Overdraft fees triggered by debit card/ATM transactions cause tremendous harm while offering no benefit.*

The harm of fee-based overdraft coverage on debit card/ATM transactions dramatically outweighs its potential benefits because (a) the cost of the fee is exorbitant, while the cost of having a transaction denied is zero; (b) the large majority of fees are paid by repeat overdrafters who are less able to quickly recover from them; and (c) as our case study demonstrates, fee-based overdraft leaves the most frequent account holders worse off than cheaper overdraft alternatives *or no overdraft coverage at all*.

(a) The cost far exceeds the benefit, especially because the cost of denial is zero.

Having debit card/ATM transactions covered offers no benefit of avoiding a denied transaction because the cost of a denied transaction is zero.²⁴ As the Board noted in its UDAP Proposal, if denied, “the consumer would be given the opportunity to provide other forms of payment without incurring any fees.”²⁵ Furthermore, there are no merchant or third party fees charged to the consumer if the transaction is denied.

Moreover, the average debit card overdraft is under \$17,²⁶ yet it triggers an average fee of \$34.²⁷ Account holders, then, are paying nearly \$2 in fees for every dollar of credit

²³ UDAP Comments, *supra* note 15, at 11-13.

²⁴ In its Proposal, the Board states: “the consequence of not having overdraft services for ATM and one-time debit card transactions is to have a transaction denied with no fees assessed.” 74 Fed. Reg. 5218. Currently, charging NSF fees for denied debit or ATM transactions is not a common practice. *See* UDAP Comments, *supra* note 15, at 18-19, for discussion of why this practice should be prohibited by the Board.

²⁵ 73 Fed. Reg. 28929.

²⁶ The average overdraft amount for debit card transactions is \$16.46. *Debit Card Danger*, *supra* note 10, at 25.

²⁷ *Id.*

extended through debit card overdrafts.²⁸ Americans aged 55 and older, despite less common debit card use, are still paying \$1.65 for every \$1 borrowed.²⁹

(b) The majority of overdraft fees are paid by a small group of account holders least able to recover from them.

The large majority of fees are paid by repeat overdrafters, who are also those least able to recover from them. The FDIC study, consistent with CRL’s previous research, found that account holders who overdraw their accounts five or more times per year paid 93 percent of all overdraft fees.³⁰ It also found that consumers living in lower-income areas bear the brunt of these fees.³¹ Seniors, young adults, military families, and the unemployed are also hit particularly hard.

- Seniors. Older Americans aged 55 and over pay \$4.5 billion in total overdraft fees annually and \$1.8 billion for debit card/ATM transactions alone.³² Those heavily dependent on Social Security pay nearly \$1 billion annually.³³
- Young adults. Young adults who earn relatively little as students or new members of the workforce pay nearly \$1 billion per year in overdraft fees.³⁴ Because they are far more likely to use a debit card for small transactions than older adults, they pay \$3 in fees for every \$1 borrowed

²⁸ Account holders pay \$1.94 in fees for every \$1 of credit extended for debit card overdrafts. *Id.*

²⁹ See Leslie Parrish and Peter Smith, *Shredded Security: Overdraft practices drain fees from older Americans*, Center for Responsible Lending, at 7 (June 18, 2008), available at <http://www.responsiblelending.org/pdfs/shredded-security.pdf>.

³⁰ FDIC Study, *supra* note 10, at iv.

³¹ *Id.* at v. Two CRL surveys, conducted in 2006 and 2008, found that 71 percent of overdraft fees were shouldered by only 16 percent of respondents who overdrafted, and those account holders were more likely to be lower income, non-white, single, and renters when compared to the general population. Respondents reporting the most overdraft incidents were those earning below \$50,000. CRL Research Brief, *supra* note 17. See UDAP Comments, *supra* note 15, at 19-21 for further discussion.

³² *Shredded Security*, *supra* note 29. The report found that these Americans pay \$4.5 billion per year in overdraft fees (p.2) and that debit card POS and ATM transactions account for 37.4 percent and 2.5 percent, respectively (p.7), which, when calculated, equals \$1.8 billion.

³³ *Id.* at 6, Table 1. “Heavily dependent” was defined as recipients who depended on Social Security for at least 50 percent of their total income.

³⁴ Leslie Parrish and Peter Smith, *Billion Dollar Deal: Banks swipe fees as young adults swipe debit cards, colleges play along*, Center for Responsible Lending, at 1 (Sept. 24, 2007), available at <http://www.responsiblelending.org/pdfs/billion-dollar-deal.pdf>. The FDIC Study found that young adults aged 18 to 25 were the most likely to overdraw their accounts, with 46 percent of all young adults overdrawing their accounts in the previous year. FDIC Study, *supra* note 10, at v.

for debit card overdrafts.³⁵ For discussion of how this situation is exacerbated by deals banks make with universities/debit cards, see our UDAP Comments.³⁶

- Military families. Military families, whom Congress has taken recent action to protect from payday and other predatory lending practices,³⁷ remain vulnerable to abusive fee-based overdraft practices. An executive vice president of one turnkey overdraft system vendor has been quoted as saying, “Areas of high unemployment . . . you typically have more activity If you happen to be a bank that’s on a military post, you’re probably doing twice as much activity as any other bank.”³⁸

One credit union whose customers are predominantly military families found that after implementation of an automated “privilege pay” system, the percentage of overdraft users considered “chronic overdrafters” increased from 37 percent to 65 percent.³⁹ One-quarter of its customers who used its “privilege pay” system were less than 25 years old.⁴⁰

- The unemployed. Some debit cards to which many states’ unemployment benefits are issued come with *automatic* fee-based overdraft coverage that costs the unemployed user as much as \$17 or more per overdraft transaction.⁴¹ The result is that the next benefit payment the unemployed person receives from the government will be automatically reduced by the

³⁵ Seven out of ten young adults would use a debit card for purchases costing less than \$2. *Billion Dollar Deal, Id.*, at 3. (citing Visa USA Generation P Survey, conducted July 24-27, 2006. Findings and discussion at <http://corporate.visa.com/md/nr/press638.jsp> (last visited Mar. 29, 2009)).

³⁶ UDAP Comments, *supra* note 15, at 20-21.

³⁷ In 2006, Congress passed the Talent-Nelson Amendment to the Defense Authorization Bill for 2007, capping loans to military borrowers at 36 percent APR, among other protections. Pub. L. No. 109-364, 120 Stat. 2266-2269.

³⁸ Alex Berenson, *Banks Encourage Overdrafts, Reaping Profit*, N.Y. Times, Jan. 22, 2003 (quoting Dick Gowdy, executive vice-president, Strunk & Associates).

³⁹ Testimony of Mary Cunningham, USA Federal Credit Union, on behalf of the Credit Union National Association, Before the Financial Institutions Subcommittee of the House Financial Services Committee (July 11, 2007), available at <http://financialservices.house.gov/hearing110/htcunningham071107.pdf> (last visited Mar. 27, 2009).

⁴⁰ Cunningham Testimony, *Id.*

⁴¹ See AP Impact: Jobless Hit with Bank Fees on Benefits, Christopher Leonard, AP Business Writer (Feb. 20, 2009) available at <http://abcnews.go.com/US/WireStory?id=6917758>; see disclosure of the \$17 overdraft fee at Oregon.gov, http://www.oregon.gov/EMPLOY/UI/ui_payment_options.shtml, and in a fact sheet issued by Ohio Job and Family Services promoting the card at http://jfs.ohio.gov/ouc/ReliaCard_FactSheet.pdf (cites last visited Mar. 29, 2009).

amount by which the card has already been overdrawn, plus \$17 for each overdraft transaction. The absurdity of this arrangement and its impact on the most vulnerable—an arrangement effectively blessed by the states that forge these agreements with the banks issuing the cards—is indefensible.

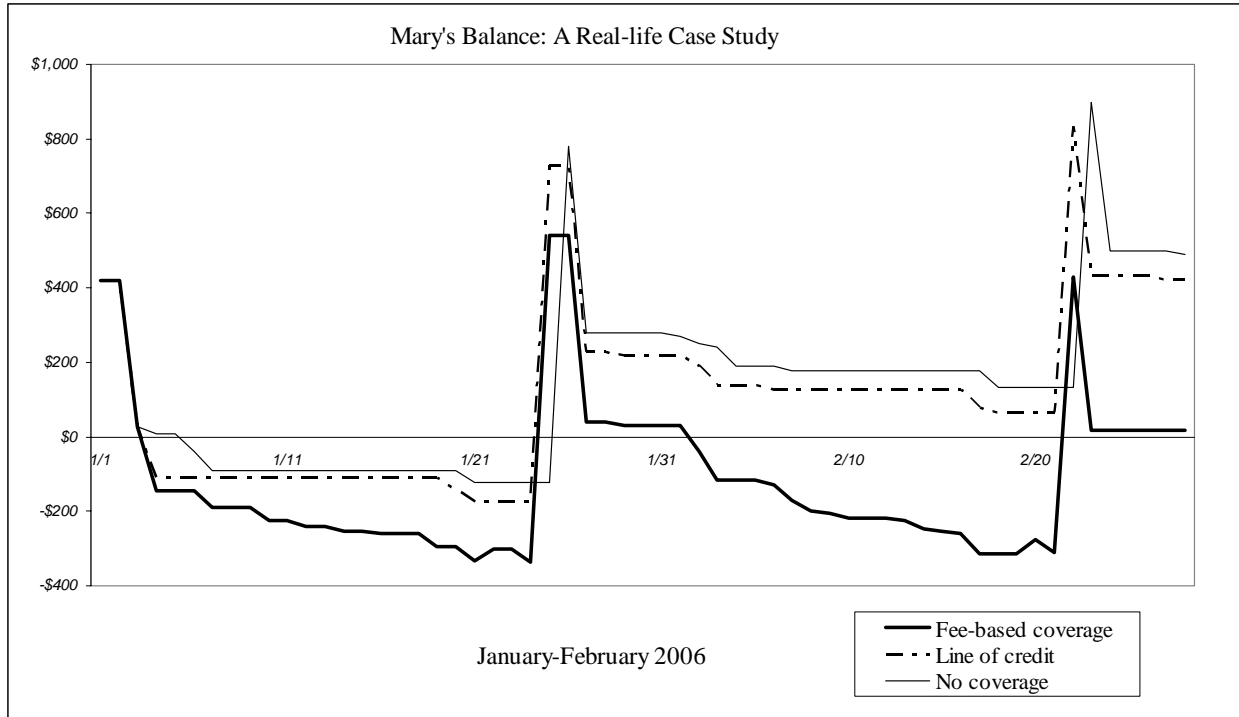
(c) Overdraft fees leave account holders worse off than lower cost coverage, or even no coverage at all.

Third, and critically, fee-based overdraft leaves account holders worse off than cheaper overdraft alternatives *or no overdraft coverage at all*. In our UDAP Comments, we included a real-life case study from our report on overdraft fees paid by older Americans. We include this study again below because its key findings bear repeating.

We graphed two months of actual checking account activity of one panelist from our database,⁴² whom we call Mary. Mary is an older American entirely dependent on Social Security for her income. We also graphed what her activity would have been with an overdraft line of credit. The two relevant pages from our report, including the graph, are attached to these comments as Appendix A.⁴³ We later added a third scenario to the graph: no fee-based coverage at all, reflected on the following page:

⁴² CRL analyzed 18 months of bank account transactions from participants in Lightspeed Research’s Ultimate Consumer Panel, from January 2005 to June 2006. For further discussion of our database and methodology, see Eric Halperin and Peter Smith, *Out of Balance: Consumers pay \$17.5 billion per year in fees for abusive overdraft loans*, at 13-14, Center for Responsible Lending (June 2007), available at <http://www.responsiblelending.org/issues/overdraft/reports/page.jsp?itemID=33341925>.

⁴³ *Shredded Security*, *supra* note 29, at 9-10.



During January and February of 2006, Mary overdraw her account several times and was charged \$448 in overdraft fees. At the end of February, she had \$18.48 in her account. She was trapped in a destructive cycle, using the bulk of her monthly income to repay costly overdraft fees.

With an overdraft line of credit at 18 percent, after two months, Mary would have paid about \$1 in total fees for her overdrafts and would have had \$420 in the bank.

Under the Fed's current proposal, if Mary's checks and ACH overdrafts were covered for a fee but her debit card and ATM transactions were denied, her ending balance would be \$402—again, a far better alternative to having all transactions types covered for a fee.

Critically, *even if Mary had had no overdraft coverage at all*, she would have been better off than she was with fee-based overdraft. Five of her transactions, totaling \$242, would have been denied—two point-of-sale transactions and three electronic transactions. She would have been charged no fee for the two point-of-sale transactions. She may or may not have been charged an NSF fee for each of the three denied electronic transactions. She also may have been charged late fees if any of the electronic transactions were bills. Assuming, conservatively, that she was charged an NSF fee and a late fee for each of the three transactions, as the chart illustrates, her ending balance still would have been \$489—plenty enough to cover the value of the denied transactions.

Mary's situation illustrates a problem common among the repeat overdrafters who pay the vast majority of the fees: Overdraft fees simply beget more overdraft fees.

Ultimately, fee-based overdraft coverage prevents account holders from being able to meet obligations they otherwise would have been able to meet. This reality makes it

impossible to justify fee-based overdraft, particularly for debit card/ATM transactions, as a program that causes account holders more benefit than harm.

2. Analysis of consumer preferences: Consumers want opt-in and would prefer their debit card transactions be denied than covered for a fee.

CRL's most recent survey explored consumer preferences related to the Board's current proposal.⁴⁴ The telephone survey started with 1,005 consumers, 56 of which said they did not have a bank account. The remaining 954 respondents were asked about their preferences on overdraft. Of the vast majority who wanted a choice about whether their debit card/ATM transactions were covered, 80 percent preferred opt-in over opt-out. The chances are 95 in 100 that the survey results do not vary from the preferences of the general population by more than 2 percent.⁴⁵

This result was unsurprising given prior stated consumer preferences about overdraft. An overwhelming percentage of account holders have said they would prefer to have their debit card transaction denied than covered for a fee.⁴⁶ This is true not only when the purchase is \$5 (80 percent prefer denial, as the Board cites in its Proposal), but also when the purchase is \$40 (77 percent prefer denial).⁴⁷

While the sample size of only eighteen individuals in the Board's consumer testing does not allow for broad-based conclusions about consumer preferences, we do note that "almost all" participants who were asked would want a debit purchase in a bookstore denied if there were insufficient funds.⁴⁸

We know of no research that has found either that consumers would prefer opt-out over opt-in for debit card/ATM transactions or that consumers would prefer to have their debit card transactions covered in exchange for the typical overdraft fee.

⁴⁴ CRL Research Brief, *Overdraft Fees and Opting In: A survey of consumer preferences*, Center for Responsible Lending (March 2009), available at <http://www.responsiblelending.org/pdfs/consumer-preference-opt-in.pdf>. This CARAVAN telephone survey was conducted by Macro International, Inc., March 12-15, 2009, of 1,005 adults in the continental U.S.

⁴⁵ *Id.* Eighty-three percent of consumers surveyed wanted a choice about whether the debit card and ATM transactions were covered. The results of the recent *Consumer Reports* Survey were consistent. Two-thirds of consumers said they would prefer to expressly authorize overdraft coverage so that there would be no overdraft loan fee unless and until they opted into the service. Consumers Union Comments, *supra* note 12 (citing Financial Regulation Poll, at 8).

⁴⁶ 2008 CRL Research Brief, *supra* note 17.

⁴⁷ *Id.* In its proposal, the Board cites the CRL Research Brief, noting consumers' preference when the purchase is \$5. 74 Fed. Reg. 5213, n.10.

⁴⁸ *Review and Testing of Overdraft Notices* at iii, Macro International (Dec. 8, 2008) [hereinafter Macro Report].

C. An opt-out arrangement does little to ensure account holders a meaningful choice.

The Board’s own explanation for why it has proposed an opt-in alternative reflects the weaknesses of an opt-out approach. The Board recognizes that under an opt-out arrangement, consumers may incur fees “for a service they did not request or were unaware they had.”⁴⁹

As we discuss in our UDAP Comments, the limitations of disclosure coupled with the incentives financial institutions have to keep consumers enrolled in fee-based overdraft make it unlikely that consumers will receive, read, understand, and act on an opt-out disclosure.

The Board’s recent consumer testing has reinforced this concern. The confusion consumers experienced about a number of issues—whether opting out for debit card/ATM meant their checks would not be covered;⁵⁰ whether opting out may save them money;⁵¹ the meaning of the phrase “opt-out;”⁵² how they could be charged a fee for circumstances outside the institutions’ control⁵³—raises substantial doubt about how well consumers will understand their right to opt out. Moreover, while we commend the Board’s effort to test the effectiveness of the forms and believe the testing resulted in improved forms in some respects, the predictive value of such testing is inherently limited. More consumers would choose to opt out, it would seem, while spending an hour with a form focused on their understanding of their right to opt out, than at an account opening when an institution has every incentive to ensure the customer pays no attention to the form.

⁴⁹ The Board notes that opt-in “would enable consumers to avoid fees for a service that they did not request or were unaware they had.” 74 Fed. Reg. 5225.

⁵⁰ Macro Report, *supra* note 48, at 14. In the second round, when opt-out was only offered for debit card purchases and ATM transactions, only three of seven participants understood that their checks would still be covered if they opted out.

⁵¹ *Id.* at 11. “At least two participants thought the sentence ‘You may save money by opting out’ meant that there was a charge for the overdraft coverage.”

⁵² *Id.* at 8: “At least two participants initially had difficulty understanding the term ‘opt out’. One did not know what the phrase meant; the other thought it meant to sign up for the program—the opposite of its actual meaning.”

⁵³ *Id.* at 10: “Both the long and short forms indicated that even if consumers opted out, they might still overdraft their account ‘under limited circumstances outside of our control.’ However, almost none of the participants initially noticed this phrase, and when it was pointed out to them, most did not understand what it meant.”

D. An opt-in arrangement allows competitive incentives that will benefit account holders.

We appreciate the Board’s recognition of the productive incentives an opt-in arrangement would offer.⁵⁴ Transparency fosters competition in the marketplace. Under an opt-in arrangement, institutions will want to enroll consumers in some kind of overdraft coverage, which will encourage them to compete by designing programs that benefit account holders. This incentive may benefit institutions as well: The founder of FindABetterBank.com estimates that that customers hit with multiple overdraft fees in a year are five percent more likely to select a new account when using the website than those who didn’t overdraft.⁵⁵

E. The Board’s justifications for why opt-in may not be optimal are not compelling.

The Board offers two reasons that opt-in may not be the optimal arrangement: (1) that those who occasionally overdraft may benefit having coverage, and (2) that opt-in could result in greater inefficiency for processing systems due to the potential increase in declined transactions.

1. The default rule should be designed to address the vast majority of circumstances, not the occasional one.

The Board notes that for consumers who rarely, if ever, overdraw their accounts, “occasional coverage of overdrafts . . . may be a positive benefit.” However, the examples the Board offers represent extraordinary scenarios: a consumer needing “emergency funds” from an ATM or a consumer needing to purchase essential groceries or medicine with no other means of credit. The Board notes that if these consumers have not opted in and have no other form of payment, they would not be able to complete the transactions. “Thus,” the Board concludes, “while an opt-in approach may benefit some consumers, it may not be the optimal outcome for others.”⁵⁶

This justification of fee-based overdraft is problematic for several reasons. First, this scenario represents the infrequent exception, not the rule. There is no evidence to suggest that the examples the Board cites comprise the majority of circumstances in which account holders overdraft. To the contrary, all available evidence suggests that these

⁵⁴ The Board notes: “[Opt-in would] provide an incentive for institutions to persuade consumers of the benefits of the overdraft service and enable the consumer to make an informed choice about the merits of the service before he or she incurs any overdraft fees.” 74 Fed. Reg. 5225.

⁵⁵ Anthony Malakian, “NSF Fees Pay the Bills But Make Customers Bolt,” *US Banker*, March 2009 (citing Robert Rubin, founder and chief executive of Facilitas, which runs the website). An analyst with the consultant Aite Group further found that 50 percent of people searching the site had overdrawn their account in the last year (as compared with only approximately 25 percent of all customers who had overdrawn in the last year according to the FDIC Study, *see* FDIC Study, *supra* note 10, at iv).

⁵⁶ 74 Fed. Reg. 5225.

transactions could comprise no more than a miniscule percentage of the transactions that cause overdrafts. We know that 93 percent of all overdraft fees are paid by consumers who overdraft repeatedly—not by the occasional overdrafter the Board refers to here.⁵⁷ Of the remaining seven percent of overdrafts, no evidence suggests that those triggered by debit cards are likely to be essential purchases. The FDIC Study found that the average debit card transaction triggering an overdraft was only \$20.⁵⁸ Moreover, the Board’s limited consumer testing in conjunction this proposal found that most participants used debit cards for less important, discretionary purposes.⁵⁹ The individuals that overdraft only rarely, the ones that the Board is concerned about, are likely to be higher income than repeat overdrafters.⁶⁰ As a result, these purchasers would likely have some alternative payment mechanism—a credit card or \$20 cash—if their debit card were declined. In the rare case that no other form of payment is available, there is, again, no data to support what portion of those remaining transactions would qualify as emergencies. There is, however, copious data that indicate that if these transactions do in fact exist at all, there are very few of them and people who rarely overdraft will have alternative means to pay for them.

It is clear, then, that the financial destruction caused by routine overdraft fees exceeds the speculative costs of the *exceptional* scenario. A set of rules governing a large universe of transactions simply should not be designed around the small minority of them, especially when there is non-anecdotal evidence supporting that these transactions do not occur in any substantial numbers. It is impossible for the Board to craft rules that work for any scenario that one could dream up; the result would be policy-paralysis. Instead, the Board should design a rule that best addresses the overwhelming majority of transactions.

Second, this justification ignores the reality that most account holders have dramatically cheaper alternatives to fee-based overdraft programs they are just not aware of, like overdraft lines of credit and automatic links to savings accounts, credit cards, or cash for small purchases. The dilemma is not a two-dimensional, either/or scenario—to have the transaction covered for an expensive fee or to have the transaction is denied. This limited choice is particularly unwarranted given the overwhelming percentage of institutions that offer cheaper alternatives.⁶¹

⁵⁷ *Supra*, note 30 (FDIC Study found that 93 percent of overdraft fees are paid by account holders who overdraw their accounts five or more times per year). As noted earlier, CRL’s survey found that 71 percent of overdraft fees are paid by only 16 percent of consumers who overdraft. *Supra*, note 31.

⁵⁸ FDIC Study, *supra* note 10, at v.

⁵⁹ 74 Fed. Reg. 5218: “[P]articipants indicated that they were more likely to pay important bills using checks and preauthorized EFTs, and to use debit cards for their discretionary purchases.”

⁶⁰ *See, supra*, note 31 and accompanying text.

⁶¹ Nearly 85 percent of 33 of the nation’s largest depository institutions surveyed in 2005 offered automatic links to savings accounts; nearly 82 percent offered overdraft lines of credit; and over 42 percent offered automatic links to a credit card. These alternatives were consistently significantly cheaper than the institutions’ fee-based “courtesy” programs. Jean Ann Fox, Patrick Woodall, Consumer Federation of America, *Overdrawn: Consumers Face Hidden Overdraft Charges from Nation’s Largest Banks*, 2 (June

Finally, and critically, this justification perpetuates the misconception that struggling Americans are better off with fee-based overdraft than they are with no coverage at all. Our real-life case study indisputably illustrates that allowing institutions to effectively slap a \$34 surcharge on many of these account holders' everyday purchases has substantial long-term costs.

2. An increase in denied transactions is not a compelling reason to reject opt-in.

The Board's second reason opt-in may not be optimal is that it could result in greater inefficiency for processing systems due to the potential increase in declined transactions.

First, no evidence that inefficiency would result has been presented.⁶² Second, any speculative inefficiencies are dwarfed by the benefit derived from consumers' avoidance of unwanted overdraft fees. If an increase in denials indeed occurs, it would be because most consumers are choosing the optimal outcome for themselves, and maximizing welfare in the aggregate, by not opting into coverage.

Less than a year ago, industry argued that *covered* overdrafts create inefficiency in the system: "Overdraft fees are meant as a deterrent. Overdrafts slow down our nation's efficient payment system and increase costs for everyone."⁶³ If inefficiencies will result whether a transaction is approved or denied, policymakers should choose the option that, consistent with the primary purpose of EFTA, maximizes consumer benefit.

III. Opt-In/Opt-Out Section-by-Section Analysis

A. Relation to other laws⁶⁴

The Board proposes to clarify that an overdraft fee-based program attached to an access device such as a debit or ATM card is covered under Regulation E instead of Regulation Z. As discussed in our UDAP Comments, we fundamentally disagree with this approach. Credit extended in conjunction with an overdraft program should be subject to the requirements of Regulation Z under the Truth in Lending Act. Debit cards that access overdraft credit should also be protected against unsolicited issuance and have the same dispute protections as credit cards. Under an opt-out arrangement, removing the

9, 2005), available at <http://www.consumerfed.org/pdfs/CFAOverdraftStudyJune2005.pdf> (last visited Mar. 29, 2009).

⁶² To the extent existing systems need to be updated in order to comply with the Board's new rule, they need to be updated whether the Board chooses opt-out or opt-in.

⁶³ Edward Yingling, President and CEO, American Bankers Association, *Opposing View: Fees are a deterrent—Banks offer several ways to keep customers from overdrawing*, USA Today, June 23, 2008.

⁶⁴ 74 Fed. Reg. 5216, § 205.12.

protections against unsolicited issuance is particularly unacceptable because a debit card with an overdraft program attached is essentially an unsolicited credit card. Under an opt-in arrangement, this arrangement may be more justifiable since the consumer would have requested the overdraft credit.

B. General rule and scope of opt-in/opt-out⁶⁵

1. Opt-in

(a) Required choice at account opening⁶⁶

The Board proposes that an institution be allowed to require choosing between an account that covers debit card/ATM overdrafts for a fee and one that doesn't as a necessary step to opening an account. We appreciate the Board's effort to enable consumers to make an engaged choice. We are concerned, however, that institutions will steer consumers into accounts that cover these overdrafts.

Requiring that a choice be made either way at account opening makes it particularly critical that the Board require institutions to offer accounts that are identical except for their treatment of debit card/ATM overdrafts. Otherwise, consumers will too likely be steered into an account that may appear cheaper but in reality wouldn't be. *See* Section D below for further discussion of product-level implementation.

(b) Written confirmation⁶⁷

We support the Board's proposal that institutions be required to provide written confirmation of the consumer's opt-in, "to help ensure that the consumer intended to opt in to the service."⁶⁸

2. Opt-out

(a) Required choice at account opening⁶⁹

The Proposal provides that an institution may require the consumer to decide whether to opt out as a necessary step to opening the account. Again, we support the Board's effort to ensure consumers have a choice but emphasize that identical accounts, with and without coverage of debit card/ATM transactions, must be offered. Moreover,

⁶⁵ 74 Fed. Reg. 5217, § 205.17(b)(1).

⁶⁶ 74 Fed. Reg. 5226, § 205.17(b)(1)(ii).

⁶⁷ 74 Fed. Reg. 5226, § 205.17(b)(1)(iii).

⁶⁸ 74 Fed. Reg. 5226.

⁶⁹ 74 Fed. Reg. 5218, § 205.17(b)(1)(ii).

institutions that require a choice at account opening must not be exempted from any other provisions requiring subsequent notice during the period a fee is incurred.

(b) 30-day safe harbor following initial notice⁷⁰

The Board proposes a 30-day safe harbor following initial notice of the right to opt out, during which the institution “generally” would be prohibited from charging an overdraft fee for a debit card purchase/ATM transaction.⁷¹ This is a reasonable timeframe. We only note that it is half as long as the period of time, under the proposed opt-in arrangement, that an institution would be allowed to continue to charge overdraft fees even without receiving a customer’s opt-in. This disparity is unwarranted. (*See* Section I below for further discussion of why 60 days under an opt-in arrangement is too long.)

(c) Provision of toll-free phone number⁷²

The Board should require that a toll-free number be provided, particularly in light of its consumer testing, which found that participants would prefer to opt out by calling their institution.

(d) Examples of what is not a reasonable opportunity to opt out⁷³

We commend the Board for clarifying what would not constitute a reasonable opportunity to opt out, such as suggesting that the consumer write a letter to the institution to opt out.

C. The Board should prohibit conditioning coverage of checks and ACH transactions on whether debit card/ATM transactions are covered.⁷⁴

The Board must not condition the account holder’s right to opt into or out of an overdraft program for debit card/ATM transactions on the account holder also opting out of overdraft service for checks, ACH, or other transactions. It must also prohibit an institution from declining to pay checks, ACH, or other transactions because the customer has opted out of the overdraft program for debit card/ATM transactions.

Account holders should be allowed to have their checks and ACH transactions covered without choosing to have debit card-triggered transactions covered. First, as the Board notes in its proposal, there may be a benefit to having a check or ACH transaction

⁷⁰ 74 Fed. Reg. 5218, § 205.17(b)(1)(ii).

⁷¹ 74 Fed. Reg. 5218.

⁷² 74 Fed. Reg. 5218, § 205.17(b)(1)(ii).

⁷³ 74 Fed. Reg. 5218, § 205.17(b)(1)(ii).

⁷⁴ 74 Fed. Reg. 5226-27, 5218-19, § 205.17(b)(2).

covered, but “[s]uch benefits are not evident, however, with regard to the payment of overdrafts for certain types of EFTs, specifically ATM withdrawals and one-time debit card transactions.”⁷⁵ Given the Board’s conclusion that a rational consumer may have very different feelings about the two groups of transactions,⁷⁶ it would be inappropriate for institutions to discourage consumers from making that choice.

Second, treating different types of transactions differently for overdraft purposes is clearly feasible. The FDIC Study found that of the institutions with automated overdraft programs, 81 percent of institutions applied them to debit card purchases and ATM withdrawals—indicating that 19 percent did not.⁷⁷ SHCU is one example of an institution that treats different transactions differently for overdraft purposes: For customers who have chosen either SHCU’s low-cost line of credit or to link a savings account, it allows overdrafts by checks or ACH transfers, but its policy is to decline overdrafts triggered by ATM or debit card purchases, even when the customer has a lower cost form of overdraft coverage.

D. The Board should require institutions to offer checking accounts with identical terms, except for whether debit card purchases and ATM withdrawals are covered.⁷⁸

The Board explains that an institution may choose to implement the right to opt-in/opt-out at either the account level—by programming the account so that overdrafts on ATM and one-time debit purchases are not covered, or at the product level—by offering a different type of account for which debit card purchases and ATM withdrawals are not covered.

The Board requests comment on two alternative ways in which opt-in/opt-out could be implemented if the institution chooses implementation at the product level: either by requiring an identical account except for whether debit card/ATM transactions are covered or by requiring an account with “the same or reasonably comparable terms” provided that the differences “are not so substantial that they would discourage a reasonable consumer” from exercising his or her right to opt in/opt out.

We appreciate the Board’s effort to ensure that allowing implementation at the product level does not result in a chilling effect on consumers’ exercising their right to opt-in/opt-out. The Board should choose the first alternative and require the institution to provide an account alike in all ways except for the treatment of ATM/one-time debit card

⁷⁵ 74 Fed. Reg. 5217.

⁷⁶ See, generally, the Board’s discussion of why it concluded concerns about overdraft programs may be appropriately addressed through Regulation E, covering only debit card purchases and ATM transactions, at 74 Fed. Reg. 5216-17.

⁷⁷ FDIC Study, *supra* note 10, at iii.

⁷⁸ 74 Fed. Reg. 5227, 5219, § 205.17(b)(3).

transactions. The second alternative, because of institutions’ incentives to discourage consumers from choosing not to have certain overdrafts covered, will not adequately ensure that customers are given the right to not have these overdrafts covered without being otherwise penalized. The first alternative is also a clear rule, which will be easier for the banks to comply with and easier for regulators to enforce, while the standard in the second alternative is more ambiguous.

We are concerned by the only example the Board provides of what would be “so substantial[ly different]” that it would not be allowed: an account that does not provide services for debit card or ATM transactions at all.⁷⁹ This example provides a great degree of wiggle room between a substantially different account and an otherwise identical account. There are many more subtle ways in which an institution could vary the characteristics of an account—other fees and interest rates paid on deposits, for example—that could certainly discourage the reasonable consumer from choosing not to have debit card/ATM transactions covered.

Requiring consumers to have more expensive checking accounts because they don’t want to be able to spend more than they have with their debit card is simply unfair. Moreover, as the Board has recognized, consumers tend to underestimate at account opening how often they may later overdraw their account.⁸⁰ As a result, when presented with two potential checking accounts, they are likely to pick the one that has even marginally cheaper fees or higher interest—particularly when the personnel assisting them with the account opening will have every incentive to ensure they choose the ostensibly “cheaper” account.

The more effective approach is to require that the accounts be identical in every way except for the opt-out/opt-in option. Allowing the accounts to differ on other terms could undermine the entire regulation.

E. The proposed exceptions to the notice and opt-in/opt-out requirement are appropriate.⁸¹

The Board proposes to exclude institutions from the requirement that they allow consumers to opt-in/opt-out and provide notice of such option if the institution has a policy and practice of declining debit card/ATM transactions for which authorization is requested, when the institution has a reasonable belief that the account lacks sufficient funds. The Board proposes an additional exception in the context of an opt-out arrangement for institutions that already require consumers’ affirmative opt-in to cover these transactions. These exceptions are appropriate, but *see* Section F below for

⁷⁹ 74 Fed. Reg. 5227.

⁸⁰ In its 2008 Regulation DD Proposal, the Board states, “[C]onsumers may not focus on the significance of the information at account opening because they may assume they will not overdraw the account,” noting that this behavior is referred to as “hyperbolic discounting.” 73 Fed. Reg. 28743.

⁸¹ 74 Fed. Reg. 5227, 5219-20, § 205.17(b)(4).

discussion of why even these institutions should not be allowed to charge an overdraft fee under any circumstances when the account holder has chosen not to be covered.

F. The fee prohibition should allow no exceptions.⁸²

The Board proposes two exceptions to the requirement that overdraft fees not be charged unless the consumer has opted in/not opted out. A fee would be allowed if (i) the institution had a reasonable belief that there were sufficient funds at the time of authorization; or (ii) a debit card transaction is presented by the merchant by paper-based means and the institution has not previously authorized the transaction.

We oppose both of these exceptions. When consumers don't opt in or they opt out, they will expect that they will not be charged overdraft fees for debit card purchases or ATM transactions, and they shouldn't be.

1. Reasonable belief exception

The Proposal offers four examples of situations that would fall under the reasonable belief exception: (i) where balances are not updated in real time, such as in a batch environment; (ii) where a previously deposited check has been returned; (iii) where the settlement amount exceeds the authorization amount; and (iv) where a “force pay” debit card transaction was authorized based on available funds but intervening transactions made funds unavailable at settlement.⁸³

The worst case for the institution in any of these situations is that it inadvertently covers an overdraft without charging a fee.⁸⁴ The institution will be immediately repaid upon the customer's next deposit, and the cost of funds for the few days it covered the overdraft will pale in comparison to what an overdraft fee would cost the consumer. Allowing institutions to charge overdraft fees in these situations only provides a disincentive for them to play an active role in making transaction processing speeds faster, which would prevent many of these inadvertently authorized overdrafts.

Situations (i), (iii), and (iv) are all attributable to operational issues among the merchant, the card processor, and the institution that should be worked out among themselves. They should not result in a consumer who has chosen not to have debit card/ATM overdrafts covered being charged a fee.

In the case of batch processing, while smaller institutions may be at a disadvantage when their systems do not have the capacity of larger institutions' systems, those smaller

⁸² 74 Fed. Reg. 5227, 5220-21, § 205.17(b)(5).

⁸³ *Id.*

⁸⁴ As the Board has pointed out, the opt-in/opt-out requirements do not prohibit institutions from covering overdrafts for debit card and ATM transactions; they only prohibit institutions from charging the customer a fee for covering them when that customer has not opted in or has opted out. 74 Fed. Reg. 5219, n.29.

institutions’ customers should not be any more vulnerable to unauthorized overdraft fees than customers of larger institutions.

As we noted in our UDAP Comments, SHCU is a relatively small institution that is still in the process of converting from batch to on-line processing. With batch processing, customers’ balances are updated only twice daily, allowing for the possibility that SHCU inadvertently covers an overdraft. When this occurs, SHCU does not charge an overdraft fee but is repaid the amount of the overdraft the next time the customer makes a deposit.

In situation (ii), the returned deposit scenario, institutions often charge consumers a returned item fee for depositing a check that goes unpaid by the issuing institution.⁸⁵ This fee more than covers the institution’s costs for dealing with the returned check. Again, institutions will be repaid the amount of any overdraft that occurs as a result, and they shouldn’t be able to unreasonably capitalize off the consumer who spent funds under the reasonable belief that they had access to them.

The Board offers two examples that would *not* fall under the reasonable belief exception: (i) where the merchant does not submit the transaction for authorization; and (ii) where a stand-in processor is used.⁸⁶

We strongly agree with the Board’s reasoning here, and there is no reason the same reasoning should not be applied to all the scenarios proposed to fall under the reasonable belief exception. In its discussion of the scenario where the merchant does not submit the transaction for authorization, the Board states: “From the perspective of the consumer who has opted out, it is reasonable to expect that the transaction would be declined if he or she did not have sufficient funds in the account.”⁸⁷ It further states that the merchant’s decision not to seek authorization “generally is not transparent to the consumer.”⁸⁸

Likewise, the Board’s explanation for why use of a stand-in processor would not allow an institution to charge a fee is “because a consumer who has opted out would reasonably expect the transaction to be declined if he or she did not have sufficient funds in the account.”⁸⁹

The same is true of all four scenarios the Board proposes to allow as exceptions. The Board’s consumer testing even found that “[m]ost participants,” despite disclosure to this

⁸⁵ The Government Accountability Office’s analysis of Moebs Services Data found the average returned item fee was \$12 in 2007, up from \$8 in 2000. *Bank Fees: Federal Banking Regulators Could Better Insure That Consumers Have Required Disclosure Documents Prior to Opening Checking or Savings Accounts*, GAO Report 08-291, at 68 (Jan. 2008).

⁸⁶ 74 Fed. Reg. 5221.

⁸⁷ *Id.*

⁸⁸ *Id.*

⁸⁹ *Id.*

effect, did not understand that after opting out, they could still be charged overdraft fees and “did not understand what might be meant by ‘circumstances outside of our [i.e., the bank’s] control.’”⁹⁰

2. Paper-based debit card transaction exception.

The Board justifies this exception by explaining that a consumer should be aware that a merchant processing a paper-based transaction is not obtaining authorization from the institution; therefore, the consumer should not be surprised if later charged an overdraft fee.⁹¹

The Board may be correct that some consumers will understand that the authorization process did not occur. However, many consumers will not understand that whether an authorization took place affects whether or not they are charged an overdraft fee. Many may reasonably assume that if an institution inadvertently covers an overdraft, they will not be charged a fee because they *did not choose such coverage*. As a result, the Board should prohibit overdraft fees under any circumstances when consumers have not opted in or have opted out.

G. Timing⁹²

1. Opt-in⁹³

(a) Existing account holders should be given the same protection as new account holders.

The Board has proposed requiring that an opt-in notice be sent to existing account holders either on or with the first periodic statement sent after the rule becomes effective or following the first assessment of an overdraft fee after the rule becomes effective. Following notice, the institution could continue charging overdraft fees for the next 60 days.

The notice should be required by the first statement or within 30 days after the rule becomes effective, whichever occurs first. Institutions should then be prohibited from charging overdraft fees on debit card/ATM transactions after a short period—say, 7 or 10 days—following such notice, unless the account holder has opted in.

We understand industry has cost concerns about notifying all existing customers of their right to opt-in. But these costs are modest when compared with both (1) the fee income

⁹⁰ Macro Report, *supra* note 48, at iv.

⁹¹ 74 Fed. Reg. 5227, 5221.

⁹² 74 Fed. Reg. 5227-28, 5221-22, § 205.17(c)

⁹³ 74 Fed. Reg. 5227-28.

generated by the product and (2) the cost to consumers of one additional fee before receiving notice. As Consumers Union illustrates in its comments on this proposal, account holders would pay an additional \$82 million in overdraft fees to one major institution alone if existing customers likely to overdraft are allowed to incur even one overdraft fee before being asked to opt-in.⁹⁴

The Board has also requested comment on whether a hybrid approach—opt-out for existing customers and opt-in for new customers—may be appropriate.⁹⁵ For the reasons noted throughout this comment, institutions should be required to obtain consumers’ affirmative consent before charging overdraft fees on debit card/ATM transactions, regardless of whether they open their account before or after the effective date of this rule. Requiring opt-in for existing customers is especially important in light of the relatively small number of existing customers who will open new accounts in the near future. A 2003 estimate from a financial institutions consulting firm found that only 14 percent of banks’ customers leave their bank each year;⁹⁶ it also found that consumers were 70 to 80 percent less likely to leave after they were set up on electronic bill payments,⁹⁷ indicating that attrition rates are likely decreasing as more consumers sign up for bill pay.

(b) Notice should be stand-alone.⁹⁸

The Board proposes, and we support, a requirement that the institution make the opt-in notice separate from other disclosures to ensure the account holder does not inadvertently opt in by signing a signature card or other account-opening document.

⁹⁴ Consumers Union Comments, *supra* note 12, at 12. By contrast, a study by the Board’s staff showed that the cost to implement all new disclosures required by TISA in the 1990s translated into only \$29,390 per bank or approximately \$337 million for all banks. Gregory Elliehausen and Barbara R. Lowery, Staff, Board of Governors of the Federal Reserve System, *The Cost of Implementing Consumer Financial Regulations: An Analysis of Experience with the Truth in Savings Act* (Dec. 1997). Thus, even if the cost is doubled to account for inflation, the cost to banks to make new TILA or TISA disclosures for overdraft loans translates to about \$60,000 per bank.

⁹⁵ 74 Fed. Reg. 5228.

⁹⁶ Michelle Higgins, *Direct Deposit, Online Billing Make Switching Banks Harder*, Wall Street Journal, Aug. 14, 2003 (citing estimates from Celent Communications); *see also* Bill Stoneman, *After Free . . . What Is There To Offer?*, Banking Strategies (May/June 2006) (citing Betty Cowell, Wachovia executive vice president and director of retail banking, noting that Wachovia enjoyed 11 percent household attrition versus an industry average of 14 percent).

⁹⁷ Michelle Higgins, *Id.* (citing Garter Inc.).

⁹⁸ 74 Fed. Reg. 5226.

(c) Notices should continue to be required even after account holders have opted in.

The Board proposes that institutions not be required to provide opt-out notices to account holders who have opted in.⁹⁹ We disagree. Given institutions' incentive to steer consumers to opt-in, many consumers may opt in and later wish to opt out but be unaware that they may. Continued notice of the right to opt out should be required during every period in which a consumer incurs a debit card/ATM overdraft fee.

2. Opt-out

(a) Existing account holders should be given the same protection as new account holders.

We continue to urge the Board to require that an opt-out notice be sent to all account holders at the time the rule is implemented. In the event the Board does allow institutions to charge an overdraft fee before initially notifying customers of their right to opt out, we urge the Board to clarify that the institution may only charge *only one single fee* for a debit card/ATM overdraft before the initial notice is sent (not, for example, three fees for three additional overdrafts incurred on the same day as the initial overdraft fee). For further discussion, *see* our UDAP Comments.¹⁰⁰

(b) Notice should be stand-alone.

As written, the Proposal would not require that an opt-out notice be separate from other disclosures; however, the Board requests comment on whether this notice should be required to be stand-alone.¹⁰¹ While the Board's concern about a consumer inadvertently opting in does not apply to opt-out—because we expect institutions will ensure no account holders inadvertently opt-out—we are concerned that a notice combined with other disclosures, such as within an account agreement at account opening, will go unnoticed by the consumer.

In its Regulation DD Final Rule, despite expressing concern about overemphasizing one type of fee in its Regulation DD Proposal,¹⁰² the Board concluded that placing emphasis on overdraft fees on the periodic statement was appropriate, in part because these fees are not as predictable as many other types of account fees.¹⁰³ The Board should require that a right to opt out of these overdraft fees be emphasized for the same reason.

⁹⁹ 74 Fed. Reg. 5228, § 205.17(c).

¹⁰⁰ *See* UDAP Comments, *supra* note 15, at 33-34.

¹⁰¹ 74 Fed. Reg. 5222, § 205.17(c)(1).

¹⁰² 73 Fed. Reg. 28742-43.

¹⁰³ 74 Fed. Reg. 5587.

Moreover, research strongly suggests that consumers will miss disclosures buried within a longer document.¹⁰⁴ Indeed, the Board’s own limited consumer testing does not appear to support its proposal. The study’s findings report that in the first round of testing, nearly all participants preferred a stand-alone notice, while in the second round, half of the participants preferred that the notice not be stand-alone.¹⁰⁵ This explanation of the findings would seem to indicate that a majority of the participants preferred a stand-alone notice.

Finally, there is precedent for requiring a disclosure to be on a separate document, including the Notice of the Right to Cancel under Regulation Z.¹⁰⁶ See our Regulation DD Comments for further discussion.¹⁰⁷

(c) Notice should be required immediately following an overdraft.

As noted in our Regulation DD Comments,¹⁰⁸ we agree with the Board that additional notice of opt-out should be required when the fee is more relevant. However, we disagree with the Board’s proposal that notice may be provided *either* immediately following an overdraft *or* on the periodic statement. Instead, it should be required *both* immediately after each day a consumer overdrafts—when the individual fees incurred are most relevant and so that consumers can more quickly avoid them by immediately opting out—and with the period statement, which allows consumers to see the aggregate impact of fee-based overdraft. If, however, the Board does not require disclosure at both times, it should require that the opt-out notice be provided immediately following an overdraft fee, accompanying notice of the fee itself, rather than on the periodic statement.

Consumers are more likely to notice a stand-alone document they receive only because they have just incurred a significant fee. Moreover, overdraft fees tend to occur in bunches, and not providing notice of an overdraft until month-end allows for substantial

¹⁰⁴ One recent study provided a three page consent form to 91 college students to see if they would read the form. The form included a provision in the fifth paragraph that required them to, among other things, administer electric shocks to other participants, even if the participant asked for medical assistance. An astounding 96 percent of the college students—87 of out 91—signed this consent form. The authors reported: “Very few read any provisions or even skimmed enough to get a vague idea of those provisions. The average time that these participants spent looking at the bogus consent form was 2.0 seconds.” Debra Poggrund Stark and Jessica M. Choplin, *A License to Deceive: Enforcing Contractual Myths Despite Consumer Psychological Realities*, NYU Journal of Law & Business, at 29-30 (Spring 2009).

¹⁰⁵ Macro Report, *supra* note 48, at iv.

¹⁰⁶ Regulation Z, 12 CFR §226.23(b)(1): “In a transaction subject to rescission, a creditor shall deliver 2 copies of the notice of the right to rescind to each consumer entitled to rescind. The notice shall be on a separate document that identifies the transaction and shall clearly and conspicuously disclose the following. . . .”

¹⁰⁷ Regulation DD Comments, *supra* note 15, at 18-19.

¹⁰⁸ See *id.* at 23 *et. seq.*

fees to be incurred that could have been avoided by an earlier notice. In addition, requiring only that *if* an institution chooses to provide prompt notification of an overdraft, *then* they must also provide the opt-out notice, would create a disincentive for institutions to provide notice of overdraft fees as they occur, even if they were doing so before issuance of the rule. Requiring the practice would put institutions on equal footing, while helping to ensure consumers have a reasonable opportunity to opt out.

(d) Notice should appear in close proximity to fees.

We commend the Board for requiring that notice provided on a periodic statement be placed in close proximity to any aggregate totals for overdraft fees.¹⁰⁹

The Board requests comment on whether institutions should be permitted to include the opt-out notice on a statement where no overdraft fees were incurred due to debit card/ATM transactions in order to better customize their statements.¹¹⁰ We appreciate the Board’s concern that customers may dismiss as boilerplate a disclosure they receive every month, even when it is not applicable. However, when counterbalanced with the possibility that by receiving the disclosure every month, consumers may be more likely to notice it even before they have incurred an overdraft fee and opt out, we would not oppose allowing institutions to include an opt-out notice on all periodic statements.

H. Content and format¹¹¹

As we noted in our Regulation DD Comments, the clarity of the Board’s proposed Opt-Out Form is inherently limited by the Board’s own resistance to making overdraft loans subject to Regulation Z under the Truth In Lending Act (TILA), and any recommendations we make to the forms below will not resolve this problem. *See* Regulation DD Comments for further discussion.¹¹²

1. Opt-in Form¹¹³

We make the following recommendations to the Board’s Opt-In Form:

- (a) Describe the alternatives as “less costly.” Alternative overdraft services are mentioned twice on the form. The first time, there is no comment on their cost. The second time, the form says they “may be less expensive.” In the prior version of the Opt-Out Form, these services were described as “less costly,” and rightfully

¹⁰⁹ 74 Fed. Reg. 5222, § 205.17(c)(2)(i).

¹¹⁰ 74 Fed. Reg. 5222.

¹¹¹ 74 Fed. Reg. 5228, 5223-24 § 205.17(d).

¹¹² Regulation DD Comments, *supra* note 15, at 11.

¹¹³ Model Form A-9, Alternative 2, 74 Fed. Reg. 5238.

- so. As the Board cites in its Proposal, the median overdraft fee per the FDIC’s study was \$27, compared to median fees of \$5 for using a line of credit or a transfer from savings.¹¹⁴ We see no reason to avoid calling them “less costly” other than to encourage account holders to select the most expensive option available: fee-based overdraft. We strongly urge the Board to make this change.
- (b) Do not emphasize the word “unless.” Underlining “unless” in the phrase “We will not pay your overdrafts for ATM withdrawals and debit card purchases . . . unless you tell us you want overdraft coverage for these transactions” comes across as a warning of sorts—as though not telling the bank to cover overdrafts carries some grave consequence—that may encourage account holders to opt in when they otherwise wouldn’t.
- (c) Move fee disclosure up. The form as written may sway consumers into opting in because the “Overdraft Fees” section does not appear until after the first three paragraphs. Account holders may read the first paragraph and jump to the bottom of the form to opt-in. We recommend that the fee section follow the first paragraph.
- (d) Require disclosure of minimum amount of overdraft that would trigger fee. The Board’s previously proposed version of the Opt-Out Form included the following statement: “We may charge you this fee even if your overdraft amount is as low as \$_.” The disclosure has since been removed from the form, but participants’ reaction to it in the Board’s consumer testing—they “reacted negatively” and found the practice “unfair”¹¹⁵—supports its staying on the form. This disclosure is important because it alerts consumers in a straightforward manner that they will be charged fees even on extremely small overdrafts.
- (e) Require an annual percentage rate disclosure. Currently, the form will provide account holders no way of comparing the cost of fee-based overdraft to other alternatives. In the past, we have urged the Board to require disclosure of an effective APR for overdraft fees, consistent with Regulation Z requirements for other open-end credit, since the effective APR included the impact of flat fees on the cost of credit. Since the Board eliminated the effective APR for most open-end credit in 2008, a decision that we vociferously opposed,¹¹⁶ we recommend instead a specific disclosure required under this proposed rulemaking for the Opt-In or Opt-Out Forms.

¹¹⁴ 74 Fed. Reg. 5223, n. 34 (citing FDIC Study at 15, 20, 23).

¹¹⁵ Macro Report, *supra* note 48, at iii and 7.

¹¹⁶ See Comments of the National Consumer Law Center, Center for Responsible Lending and other Consumer Groups Regarding Notice of Proposed Rulemaking Truth in Lending, Federal Reserve System, 12 CFR Part 226, Docket No. R-1286 at 52-57 (October 12, 2007).

Since an institution cannot determine the annual percentage rate of an overdraft fee before the fact because the term of the loan is not known, the Board should require a sample annual percentage rate on the form, as follows:

“Examples of the annual percent rate (APR) for overdraft coverage:

-[\$[maximum fee the institution charges] for a \$25 overdraft repaid in two weeks: x%

-[\$[maximum fee the institution charges] for a \$10 overdraft repaid in two weeks: x%”

Since this is a sample APR, it can be based on assumptions of a loan amount and time period. As such, the APRs can be calculated using the formula for a closed-end short term loan, such as a payday loan. In fact, such a disclosure would be the most beneficial because it will allow consumers to compare the cost of these loans to other forms of short term credit.¹¹⁷

- (f) Require an annual percentage rate disclosure for overdraft fees paid during the period on periodic statements.

As part of the notice that appears on periodic statements, the Board should require an APR disclosure for each overdrawn transaction using the formula in Section (e) above.

2. Opt-Out – Form at Account Opening¹¹⁸

We commend the Board for improving the Opt-Out Form by making notification of the right to opt out more prominent; mentioning alternatives earlier; avoiding labeling fee-based overdraft a “service;” requiring disclosure of an automatic link to savings account, when offered; and using more everyday language in the form.

We make the following recommendations to the Board’s revised Opt-Out Form at Account Opening:

- (a) Describe the alternatives as “less costly.” See discussion in part 1(a) above.
- (b) Improve the disclosure: “As a result [of opting out], you may pay fewer overdraft fees.” We understand from the Macros report that this language is used in part to allow institutions to continue to charge overdraft fees under the reasonable belief and paper-based means exceptions. However, this statement may also discourage

¹¹⁷ The sample APRs should be calculated as follows: The amount of the fee divided by the amount of the overdraft; divided by the number of days between when the overdraft occurred and when it was repaid; multiplied by 365 days; expressed as a percentage. Note that the two week assumption for repayment is very generous, since most overdraft loans are repaid within five days. However, at least it will provide consumers some idea of how costly these loans are.

¹¹⁸ Model Form A-9(A), Alternative 1, 74 Fed. Reg. 5237.

consumers from opting out because it offers no assurance they will pay fewer fees, so, they may wonder, “Why bother taking any action?” In practice, it is *highly likely* that opting out will result in fewer overdraft fees. The worst case is that it will result in the same amount of overdraft fees—if all a consumer’s debit card/ATM overdrafts were to fall under the Board’s two exceptions or if a consumer never overdrafts and incurs zero fees either way.

Ideally, the Board should rectify this problem by eliminating the two exceptions and requiring that the form state: “As a result [of opting out], you will not incur overdraft fees related to these types of transactions.” If the Board does not eliminate the two exceptions, it should develop a clear way to indicate that opting out will decrease the likelihood of incurring overdraft fees on these transaction types.

(c) Require an annual percentage rate disclosure. See section 1(e) above.

3. Opt-out – Form for Periodic Statements¹¹⁹

We make the following recommendations to the Board’s Opt-Out Form for Periodic Statements:

- (a) Mention line of credit as an alternative, in addition to linking an account. This disclosure should include both alternatives so that account holders who do not have another account with the institution will not be discouraged from contacting the bank for more information.
- (b) Describe the alternatives as “less costly.” See discussion in part 1(a) above.
- (c) Require an annual percentage rate disclosure for overdraft fees paid during the period on periodic statements. See section 1(f) above.

I. Time to comply with opt-in/time to implement opt-out¹²⁰

1. Opt-in

The Board has proposed that the institution may continue charging overdraft fees on debit card/ATM transactions until 60 days after the customer receives notice of the right to opt-in. As discussed in Section B.2.(b) above, such notice should be required immediately after the rule becomes effective, either on the next periodic statement or within 30 days, whichever is sooner.

¹¹⁹ Model Form A-9(B), Alternative 1, 74 Fed. Reg. 5237.

¹²⁰ 74 Fed. Reg. 5228, 5224, § 205.17(g).

If notice is not required until after the account holder incurs a fee, the period should be much shorter. We recommend 7-10 days. If the 60-day clock starts soon after a customer has incurred an overdraft fee, their account balance is more likely to be hovering around zero and they may be particularly vulnerable to overdraft fees in the following weeks. Yet they may continue incurring fees for the next *60 days*.

A likely justification offered for allowing 60 days is that consumers will be surprised to find that these transactions are being denied. However, our surveys support that even if customers are surprised, 80 percent of them will be *pleasantly* surprised. And if there is a small minority of individuals who will be disappointed that the institution has stopped covering debit card/ATM overdrafts after seven days, they may opt in at that time, or at any time thereafter. The time frame should be one that best suits the large majority, not the small minority, of account holders. So it should be short: 7-10 days.

2. Opt-out

The Board proposes that an institution be required to comply with an opt-out request “as soon as reasonably practicable after the institution receives it.”¹²¹ It requests comment on whether additional guidance is required. As we noted in our UDAP Comments, given the incentives institutions will have to delay implementation of opt-out requests, more guidance is necessary. We consulted with SHCU on this question, which advised that an institution should be able to comply within three days of receiving the notice from the account holder. *See* UDAP Comments for further discussion and specific language.¹²²

J. Other provisions

1. Joint relationships¹²³

We agree with the Board’s proposal that where one account holder on a joint account opts out, debit card and ATM overdrafts on that account should be denied. In an opt-in arrangement, where only one account holder opts in, ideally the other account holder should not be subjected to overdraft fees on debit card and ATM overdrafts; however, we understand that such a distinction would be difficult to implement.

2. Continuing right to opt-in/opt-out¹²⁴

We concur with the Board’s proposal that the right to opt-in or opt-out may be exercised at any time by the manner provided, subject to the recommendations we are making with respect to manner in Section 3 below.

¹²¹ 74 Fed. Reg. 5224.

¹²² UDAP Comments, *supra* note 15, at 35 *et. seq.*

¹²³ 74 Fed. Reg. 5228, 5224, § 205.17(e).

¹²⁴ 74 Fed. Reg. 5228, 5224, § 205.17(f).

3. Duration of opt-in/opt-out¹²⁵

(a) Opt-in

The Proposal provides that an account-holder's opt-in is effective until revoked by the consumer or until the financial institution decides for any reason to terminate coverage for the consumer. The Board did not limit or request comment on the means by which a consumer may revoke an opt-in. Because we are convinced that an institution will not have incentive to encourage consumers to revoke opt-ins, such revocations should be accepted by the institution in writing, electronically, over the phone or in person.

(b) Opt-out

The Proposal provides that a consumer's opt-out is effective until revoked by the consumer in writing or electronically and asks for comment on whether the consumer be allowed to revoke the opt-out by telephone or in person.

A consumer should not be able to revoke an opt-out by telephone or in person. Given the incentive institutions would have to encourage consumers to revoke their opt-outs, revocation should only be allowed through a means easily verifiable by a third party, in writing or electronically.

IV. Overdraft fees caused solely by debit holds should be prohibited under any circumstances.

A. Overdraft fees caused solely by debit holds should be prohibited under any circumstances.

We commend the Board's proposal to prohibit overdraft fees for overdrafts caused solely by debit holds.¹²⁶ We also appreciate the Board's continued efforts to address industry's concerns related to debit holds and its recognition that a disclosure-based approach would be ineffective.¹²⁷ We understand the issue is complicated and that with its new proposal, the Board has tried to strike a reasonable balance between protecting consumers from unnecessary fees and addressing industry concerns.

We are concerned, however, that the provisions limiting the prohibition on overdraft fees caused solely by debit holds in the Board's current proposal will not offer account

¹²⁵ 74 Fed. Reg. 5228, 5224, § 205.17(h).

¹²⁶ 74 Fed. Reg. 5229, § 205.19(a)

¹²⁷ 74 Fed. Reg. 5231.

holders sufficient protection from unwarranted overdraft fees. In short, consumers will continue to be charged overdraft fees when they *have not spent more than the funds in their account*. This is patently unfair.

The Board proposes to apply the rule only to those circumstances in which the actual transaction amount generally can be determined within a short period of time after authorization, such as pay-at-the-pump fuel purchases and restaurant purchases. We appreciate that according to one estimate these transactions make up the large majority of transactions in which the authorization amount and settlement amount do not match.

However, the rule would not apply to holds made by hotels or rental car companies—less numerous than gas and restaurant purchases, but generally much larger and generating much larger holds.

The rule is further limited in that it would only apply to overdraft fees triggered by holds that exceed the actual amount of the transaction.¹²⁸ This limitation would seem to allow overdraft fees in situations where the hold may be equal to or less than the transaction amount, but the institution does not release the hold when the actual transaction amount is debited, resulting in an unwarranted overdraft fee.¹²⁹

Operational challenges related to debit holds should be secondary to the broader point: transaction processing issues among merchants, card processors, and institutions should *never* result in account holders paying overdraft fees when they haven't spent more than the funds in their account. The rule should be crafted to prohibit charging a fee caused solely by a debit hold, *ever*; if an overdraft is inadvertently covered, the institution should not be allowed to charge a fee for it.

As we noted in our UDAP Comments, institutions should have all the necessary data points to program their systems to determine which overdrafts were caused solely by debit holds.¹³⁰ A clear rule such as this one would provide merchants, card processors and institutions every incentive to advance their systems to that these overdrafts occur much less frequently.

B. A safe harbor should not allow fees caused by debit holds.

The Board proposes that an institution may charge an overdraft fee for an overdraft caused solely by a debit hold so long as the institution has adopted procedures and

¹²⁸ 74 Fed. Reg. 5229.

¹²⁹ As noted in its comments on this proposal, Consumers Union received a complaint from a consumer who bought a \$20 meal at a restaurant, which generated a \$20 hold, and paid a \$5 tip on that transaction which generated an additional \$25 hold for the total transaction. The first \$20 hold was not released for three days, and she incurred overdraft fees in the meantime, even though she had sufficient funds for the meal. Consumers Union Comments, *supra* note 12, at 13.

¹³⁰ UDAP Comments, *supra* note 15, at 37.

practices designed to remove the hold within two hours.¹³¹ We oppose this provision for the reasons noted in Section A above.

The Board requests comment on whether other time periods may be more appropriate for the safe harbor in light of operational constraints at smaller institutions which may only receive authorization and settlement information periodically during the day. While we oppose the safe harbor, we discussed the issue with SHCU, a relatively small institution that still uses batch processing in some circumstances. SHCU acknowledged that requiring small institutions that use batch processing to reverse holds within two hours may result in their inadvertently covering more overdrafts than those institutions using real-time processing. However, it offered that the best way to address this challenge is not to lengthen the safe harbor or allow more overdraft fees to be charged, but to require merchants to submit transactions for settlement more quickly, as the Board suggests.

The Board requests comment on whether it should exercise its authority under Section 904 of EFTA to also require merchants (or their acquirers or processors) to promptly submit transactions covered by this rule for settlement. Specifically, the Board seeks comment on whether the final rule should also require merchants (or their acquirers or processors) to submit such transactions for settlement within the safe harbor period.¹³² This requirement would benefit account holders by resulting in fewer unwarranted overdraft fees caused by debit holds if the rule is finalized without eliminating the its limitations.

C. We support protection for account holders who have not opted-in/have opted out.

We note that the Proposal would not allow overdraft fees caused solely by debit holds for customers who have not opted in/opted out of coverage for debit card purchases/ATM transactions.¹³³ We agree strongly with this provision, and it indicates that it is indeed feasible for institutions to avoid *ever* charging a customer a fee caused solely by a debit hold.

D. Require prompt reversal of prohibited fees caused debit holds.

We appreciate the practical need for the Board’s provision clarifying that institutions have not violated the prohibition if they promptly waive or refund any overdraft fees caused by debit holds.¹³⁴ We commend the Board for further clarifying that the

¹³¹ 74 Fed. Reg. 5230, § 205.19(b). However, the safe harbor would not allow such fees for consumers who have not opted in or have opted out of overdraft coverage for debit card purchases/ATM transactions. *Id.*

¹³² 74 Fed. Reg. 5231.

¹³³ *Id.*

¹³⁴ 74 Fed. Reg. 5230.

institution may not require the customer to provide notice or other information demonstrating that an overdraft fee was caused by a debit hold in order to have the fees waived. This provision in fact makes any limitations to the substantive rule less necessary since, even if an institution inadvertently charges an overdraft fee for an overdraft caused solely by a debit hold, it would have the opportunity to reverse it without violating the regulation.

However, we are concerned that institutions may lack the incentive to ensure that all overdraft fees caused by debit holds are promptly reversed. We urge the Board to establish a more defined, enforceable time limit during which fees caused by debit holds must be waived—for example, within five business days—particularly since wrongly charged overdraft fees may trigger a spiral of additional wrongly charged overdraft fees that would also require reversal.

V. The Board should require implementation of the final rule as soon as reasonably practicable.

The Board states that to minimize cost impact on institutions, it “anticipates allowing substantial lead time for institutions to implement the necessary programming changes.”¹³⁵ We emphasize that minimization of cost and burden *for account holders* during the implementation period—to the tune of \$7.8 billion in overdraft fees on debit card and ATM transactions paid annually—should also be of great concern.

Many institutions, like SHCU, already have systems that can easily be programmed to prohibit overdraft fees on debit card and ATM transactions alone. But since the Board has proposed allowing institutions to implement the rule at the product level, the ability to treat different transactions differently on the same account may not even be necessary. Institutions can certainly set the allowed overdraft limit to zero, for all debit card/ATM transactions, on a specific type of account.

Even if the Board determines that implementation of the debit hold rules may take more time, this may not justify allowing the same length of time for implementation of the opt-in/opt-out provision.

Prompt implementation is particularly important in the current environment. Many families are struggling to meet daily obligations, which may subject them to more overdraft fees just when they are least able to recover from them.

Moreover, many financial institutions with abusive overdraft programs are receiving taxpayer assistance.¹³⁶ The government must ensure that those institutions are not

¹³⁵ 74 Fed. Reg. 5218.

¹³⁶ For example, since August 2008, Citigroup has increased its overdraft fee per item by 13 percent, from \$30 to \$34. *Survey of Sixteen Large Banks’ Overdraft Fees and Practices*, Consumer Federation of America (2009). Since October 2008, Citigroup has received \$45 billion in taxpayer dollars through the Troubled Asset Relief Program. David Enrich, *et. al.*, *U.S. Agrees to Rescue Struggling Citigroup*, Wall Street Journal (Nov. 24, 2008), available at <http://online.wsj.com/article/SB122747680752551447.html>.

engaging in unfair practices that affirmatively harm the very taxpayers who have helped prop them up.

We urge the Board to require implementation as soon as it determines is reasonably practicable.

CONCLUSION

We appreciate that the Board has devoted substantial attention to abusive overdraft practices. We strongly support an opt-in requirement for debit card purchases and ATM transactions. An opt-out arrangement would do little to alter the status quo. Because account holders are unlikely to alter the default, the Board must get the default right. The default should be the arrangement that wouldn't cause consumers more harm than benefit and that better reflects clear consumer preferences. *It's not a close call:* the only justifiable choice is opt-in. An opt-in arrangement would provide account holders a moment of affirmative choice, when they may select among lower cost alternatives or choose no coverage at all. Ultimately, it would provide account holders the greater control over their finances they deserve.

If the Board wishes to discuss these comments, please do not hesitate to contact us.

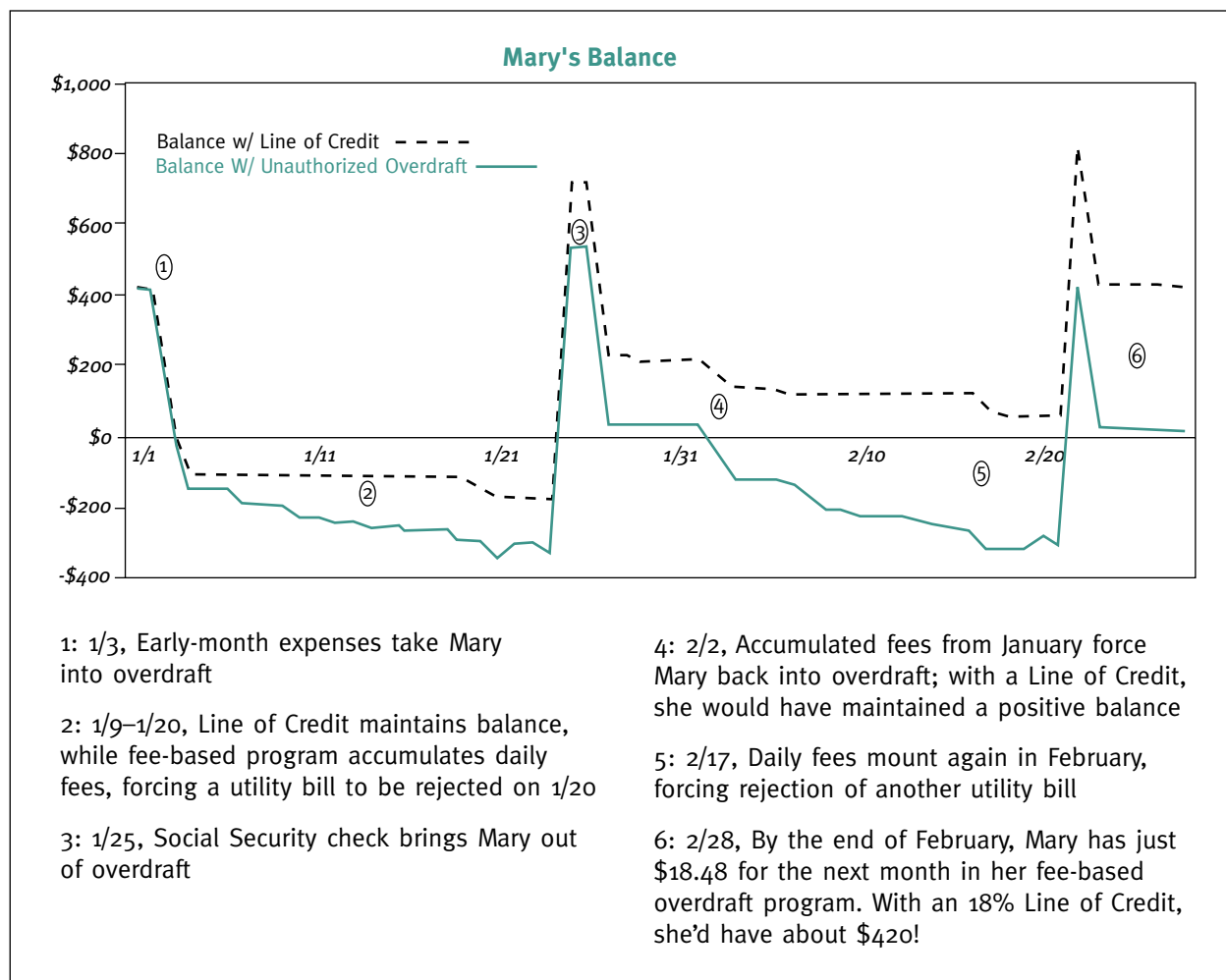
Appendix A

Real-Life Case Study

Case Study: A Social Security Recipient's Experience with Overdraft Fees

Our data allows us to recreate periods of time in a person's checking account activity, to provide snapshots of the broad trends in the data. Here, we track the checking account activity of a panelist (aka "Mary") entirely dependent on Social Security income for the months of January and February 2006.

Figure 3. Representation of account balance of panelist "Mary" January–February 2006



Mary begins the year 2006 with \$420.56 in her checking account, held at a large national bank. She makes a \$380 ATM withdrawal and several smaller point-of-sale purchases on January 3, comes up short, and is overdrawn by January 4. She incurs a \$34 overdraft fee for the initial overdraft. After two more purchases, and two more overdraft fees, she finds herself almost \$200 below zero on January 9.

For the next eleven days, Mary doesn't spend any money from her checking account, but her checking account loses money, nonetheless. Her bank charges her a fee of \$7 a day because of her ongoing negative balance. By the time a scheduled electronic withdrawal is made to pay a bill for \$32.38 on January 20, Mary's account is overdrawn by more than \$300, and the bank rejects the transaction. Her bill goes unpaid, although the bank continues to charge daily negative-balance fees.

Finally, on January 25, Mary receives her monthly Social Security check of \$904. However, her account is already \$335 overdrawn and she still has an additional \$500 in expenses for the month. Once these payments are made, Mary only has \$31.09 left to live on until her next Social Security check comes in late February. Because of this, Mary almost immediately has a negative checking account balance again, once she makes three small (\$20 or less) purchases on February 1. Over the next two days, Mary incurs two overdraft fees because of these purchases and conducts another transaction for \$50, which also results in an overdraft.

Mary does not make any more purchases between February 8 and February 17. However, the bank again continues to charge her a fee of \$7 a day because of her ongoing negative balance. On February 18, an automatic bill payment causes Mary's account to go even farther into the red—a transaction that the bank approves even though her account is already below zero and she cannot even repay the \$7 daily negative balance fee.

Once Mary's account dips to \$314.91 *below zero*, the bank finally begins to refuse additional transactions, rejecting a utility bill for another month. The \$7 daily negative balance fees continue to be assessed through February 21.

Finally, on February 22, Mary's Social Security check comes in, and the account balance ends up above \$400 once the bank subtracts the overdraft fees. Unfortunately, because Mary still has to pay her end of the month expenses totaling about \$410, she is left with only \$18.48 to tide her over until the end of March. This meager sum—even less than the \$31.09 she had to make ends meet after being charged for overdrafts in February—virtually guarantees that Mary will continue to remain trapped in a cycle of accumulating overdraft fees month after month.

In January and February, Mary paid \$448 in overdraft fees in return for receiving \$210.25 in credit from her bank, and was forced to live on \$20 from a Social Security check of nearly \$1,000. If Mary's bank had instead offered her an 18 percent APR line of credit to cover overdrafts, she would have only paid about \$1 in total fees for her overdrafts.

In the figure on page 9, Mary's account balance is shown in green, and her account balance had *she been enrolled in an 18 percent line of credit* is shown in black and dashed. By the end of the two months with a line of credit, Mary's balance would have been \$420, more than enough to meet her remaining expenses until the next Social Security check. In addition to this, her payments to the utility company would have been approved because her account would not have been over \$300 overdrawn, thus saving her non-sufficient funds fees and keeping her utility account current. Most importantly, the cycle of having the bulk of her monthly income stripped away to repay high overdraft fees, leaving little to use for the current month's bills—and therefore making Mary more vulnerable to incurring yet more overdrafts—would be broken.

If Mary's bank had instead offered her an 18 percent APR line of credit to cover overdrafts, she would have only paid about \$1 in total fees for her overdrafts.

The following graph is identical to the one on page 13 of these comments. It adds a third scenario—no overdraft coverage at all—to the graph discussed on the preceding two pages of this appendix.

