

Shredded Security:

Overdraft practices drain fees from older Americans

EXECUTIVE SUMMARY

Leslie Parrish and Peter Smith
Center for Responsible Lending

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About the Center for Responsible Lending

The Center for Responsible Lending is a nonprofit, nonpartisan research and policy organization dedicated to protecting homeownership and family wealth by working to eliminate abusive financial practices. CRL is affiliated with Self-Help, one of the nation's largest community development financial institutions.

Visit our website at www.responsiblelending.org.



North Carolina
302 West Main Street
Durham, NC 27701
Ph (919) 313-8500
Fax (919) 313-8595

District of Columbia
910 17th Street NW
Suite 500
Washington, DC 20006
Ph (202) 349-1850
Fax (202) 289-9009

California
1330 Broadway
Suite 604
Oakland, CA 94612
Ph (510) 379-5500
Fax (510) 893-9300

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As older Americans face a growing range of financial challenges, prevailing bank overdraft practices further threaten their security by draining income and social security benefits in the collection of excessive fees.

Typically, consumers are automatically enrolled in their bank or credit union's most expensive version of overdraft protection when they open a checking account. Under this system, the bank approves transactions that cause the customer's account to go below zero in return for a fee of around \$34 per incident. Because consumers are enrolled in these expensive overdraft programs without their consent and overdraft loans are made without the account holder's approval, we call these transactions "unauthorized overdrafts."

The largest share of unauthorized overdrafts is caused by debit card transactions, either at the ATM or checkout counter. Because these purchases are typically for very small amounts, the overdraft fee often greatly exceeds the amount of credit extended. Consumers making small purchases with their debit card at a variety of locations over the course of a day can easily find themselves owing hundreds of dollars in overdraft fees to their bank before they are aware of being overdrawn.

The Center for Responsible Lending analyzed a large, commercially-available database of personal bank account transactions. In the last 12 months, we have published findings that overdraft lending practices cost consumers \$17.5 billion per year by artificially increasing the incidence of overdrafts, which now trigger a fee averaging \$34 for all age groups. We found that young adults pay nearly a billion dollars of those fees.

In this report, we focus on account holders 55 years and older, and find that:

- Those relying heavily on Social Security income pay nearly \$1 billion in fees for unauthorized overdrafts. Overall, Americans 55 and older pay \$4.5 billion in overdraft fees.
- Debit card transactions are the most frequent trigger of unauthorized overdrafts for older adults, despite the fact that they are less likely to use debit cards than their younger counterparts. Account holders who overdraft using a debit card pay back far more in fees than they receive in credit.
- Survey respondents 55 and older overwhelmingly want the option to avoid unauthorized overdrafts and would rather be declined at the checkout if their debit card purchase would otherwise result in a fee averaging over \$30.

Recommendations

Prevailing overdraft practices have failed to protect the income of older Americans. Overdraft policies should be reformed so that they strengthen, rather than threaten, the financial security of older Americans.

- Federally-protected income from Social Security should not be permitted to be automatically taken to repay overdraft loans and bank fees;
- Banks and credit unions should be prohibited from manipulating the order in which charges clear and the time for which deposits are held to artificially increase overdraft fees;
- In addition, policymakers should take the following steps to protect consumers and provide them with choices and information regarding overdraft loans:
 - Require banks and credit unions to provide consumers with the choice to “opt-in” to overdraft loan programs, rather than automatically including it as an account feature;
 - Require banks and credit unions to comply with the Truth in Lending Act for high-cost overdraft loans by disclosing their cost in terms of an annual percentage rate;
 - To prevent consumers from falling into a cycle of debt, limit the number of high-cost overdraft loans a bank or credit union can make to a customer per year;
 - Require banks and credit unions to warn customers whenever an ATM withdrawal or debit card purchase will overdraw an account and give them a choice of whether to proceed or to cancel the transaction; and
 - Allow banks and credit unions to cover ATM and debit card POS overdrafts without warning only if the customer has elected, in writing, to participate in a lower-cost protection program that pays overdrafts from a linked savings account or line of credit.
- Finally, older adults should consider only doing business with banks that allow them to link their checking account to their savings account, or that offer them a less expensive line of credit for back-up funds so they can avoid unauthorized overdraft fees.

