Consumer Federation of America

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Testimony of

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On Behalf Of

Consumer Action
Consumers Union
National Association of Consumer Advocates (NACA)
National Consumer Law Center (on behalf of its low income clients)
US PIRG

Before
The Senate Committee on Banking, Housing, and Urban Affairs

Regarding
S. 1799, the FAIR Overdraft Coverage Act

November 17, 2009

Chairman Dodd, Ranking Member Shelby, and members of the Committee, I appreciate the opportunity to testify in support of the **FAIR Overdraft Coverage Act, S. 1799**, on behalf of the Consumer Federation of America[1], as well as Consumer Action,[2] Consumers Union,[3] USPIRG,[4] National Association of Consumer Advocates,[5] and the National Consumer Law Center (on behalf of its low income clients).[6] We also commend Chairman Dodd for the financial reform discussion draft he released last week, and in particular, his proposal for the creation of a Consumer Financial Protection Agency. This agency would not only implement the FAIR Overdraft Coverage Act, but also enforce the law and clamp down on other high cost loan abuses. The agency will monitor the marketplace both for evasions in current law and watch out for new products and services designed to trip and trap consumers.

We appreciate your interest in protecting consumers from unauthorized and extremely expensive overdraft loans, the banking equivalent of payday lending. Marketed as "overdraft protection" or "courtesy overdraft," fee-based overdraft programs protect the banks' ability to maximize fees while jeopardizing the financial stability of many of its customers. Rather than competing by offering lower cost and truly beneficial overdraft products and services, many financial institutions are hiding behind a smokescreen of misleading terms and opaque practices that promote costly overdrafts.

Without asking for their consent, banks and credit unions unilaterally permit most customers to borrow money from the bank by writing a check, withdrawing funds at an ATM, using a debit card at the point of sale, or preauthorizing an electronic payment that exceeds the funds available in a checking account. Instead of rejecting the debit card purchase or ATM withdrawal at no cost to the consumer, or returning the check unpaid with a bounced check fee, most institutions will now cover the overdraft and impose an expensive fee for each transaction.

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[1] The **Consumer Federation of America** is a nonprofit association of over 280 pro-consumer groups, founded in 1968 to advance consumers' interest through advocacy and education.

[2] **Consumer Action** (www.consumer-action.org) is a national nonprofit education and advocacy organization serving more than 9,000 community based organizations with training, educational modules, and multi-lingual consumer publications since 1971. Consumer Action's advocacy work centers on credit, banking, and housing issues.

[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 goods, services, health and person finance, and to initiate and cooperate with individual and group efforts to maintain and enhance the quality of life for consumers.

[4] The **U.S. Public Interest Research Group (USPIRG)** 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.

[5] The **National Association of Consumer Advocates**, Inc. 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.

[6] 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.

Consumers do not apply for this form of credit, do not receive information on the cost to borrow bank funds via overdrafts, are not warned when a transaction is about to initiate an overdraft, and are not given the choice of whether to borrow the funds at an exorbitant price or simply cancel the transaction. Banks are permitted by the Federal Reserve to make cash advances through overdraft loans without complying with Truth in Lending cost disclosure rules, denying consumers the ability to make informed decisions about whether to access credit, as well as comparison shop for the lowest cost overdraft program.

Overdraft loans are the bank equivalent of payday lending. Just as payday lenders use the borrower's personal check or debit authorization to insure priority payment, banks use their contractual right of set-off to collect the amount of the overdraft loan and the fee by taking money out of the next deposit into the borrower's checking account, even when the funds are Social Security or other exempt funds. Overdrafts are typically repaid within days, and the flat overdraft fees for very short-term extensions of credit result in outrageous interest rates.

Common banking practices, as confirmed by the FDIC's 2008 study of overdraft programs, now increase the number of overdrafts rather than minimize them—and can cost the account holder hundreds of dollars in a matter of hours, when they otherwise may have been overdrawn by just a few dollars for a few days or less.

Debit card overdrafts are now the single largest source of overdraft fees and are especially costly for account holders because they carry the same high flat fee but for much smaller loans. As recently as 2004, about 80 percent of banks rejected unfunded debit transactions without charging a fee. As consumers have switched to payment by debit instead of paper checks, banks have expanded overdraft programs that cover debits to make up for disappearing bounced check fees.

Abusive overdraft loans are costly for everyone, but are most destructive to people who are struggling to meet their financial obligations. The FDIC's study found that consumers most likely to be charged repeated overdraft fees are younger consumers and lower-income consumers. In a system hugely out of balance, our big financial institutions are collecting enormous fees from people who have nothing to spare, making them even less able to meet their obligations.

Banks continue to increase the dollar amount of fees, even as the recession makes consumers less able to pay ever higher fees for inadvertently overdrawing their accounts. Banks that received TARP funds from the public have not returned the favor. Indeed, the most recent CFA survey of the nation's sixteen largest banks found that overdraft fees continue their upward spiral, with the largest fee charged by big banks ranging from $34 at Citibank (up from $30 in the last year) to a maximum $39 charged by Citizens Bank. The median maximum overdraft fee for the largest banks is now $35. While major banks have announced changes to their overdraft programs in recent weeks, none of the largest banks have lowered the price for an overdraft.

We strongly support S. 1799 as a strong solution to the problem of overdraft lending. This legislation will help stop the abuse, without limiting the ability of financial institutions to provide genuine protection for their customers. While the Federal Reserve Board's new rule under the Electronic Fund Transfer Act is a good first step, the comprehensive protections in this legislation are essential to protecting consumers and making it safer for consumers of modest means to use mainstream banking.

In this testimony:

- We will describe the dysfunctional overdraft lending system that now dominates the market, the failure of bank regulatory agencies to protect consumers, and the vulnerable consumers most likely to use overdrafts. Our testimony also documents that consumers want to opt-in and have warning before triggering debit overdrafts and oppose manipulation of payment processing that drives up total fees.

- We will explain that abusive overdraft lending costs $24 billion per year and that nearly half of these fees come from overdrafts triggered by debit cards at the checkout counter or ATMs—overdrafts that could be prevented with a warning or if the transaction were simply declined. We will review overdraft fees and practices at the nation's largest banks, including recently announced voluntary "reforms".

- We will recommend that Congress enact S. 1799, a solution that will put real protection back into overdraft policy, and enact the Consumer Financial Protection Agency to enforce this law.

Abusive Overdraft Lending Systematically Strips Funds from Checking Accounts

Fee-based overdraft loans should not be confused with cheaper sources of back-up funds for checking accounts. Under traditional programs that link checking accounts to a savings account or line of credit, which are legitimate money management tools, funds are transferred in increments when the checking account is temporarily overdrawn. Financial institutions have offered such programs for decades. The largest banks charge a median $10 fee to transfer consumers' funds from savings accounts to cover overdrafts in their checking accounts. Banks with overdraft lines of credit generally charge around 18 percent per year and provide installment repayment arrangements.

Today, banks commonly automatically enroll their checking account holders in a high-cost fee-based system at the time they open a checking account or add this feature for existing customers without their consent. The FDIC reports that over three-fourths of the banks it surveyed automatically pay overdrafts for a fee and seventy-five percent of those banks automatically enroll their customers in overdraft programs without their permission.[7] If an account dips into a negative balance, the bank routinely covers the overdraft—a change from past practices—paying the shortfall with a loan from the banks' funds. When the account holder makes the next deposit,

[7] The FDIC Study found that 75 percent of banks surveyed automatically enrolled customers in automated overdraft programs. FDIC Study of Bank Overdraft Programs at iii (Nov. 2008) [hereinafter "FDIC Study"].

the bank debits the account in the amount of the loan plus a fee, which now averages $34.[8] At the largest banks, the median overdraft fee is $35.

Overdraft Loans Give Banks First Claim on Consumers' Pay or Benefits

The method in which overdraft loans are collected contributes to the harm they cause consumers. Banks, with the Federal Reserve's permission, currently treat overdraft loan "fees" as checking account fees under the Truth in Savings Act. As a result, banks can and do use set-off to pay themselves first out of the consumer's next deposit of pay or benefits. Consumers caught by overdraft loans do not get affordable installment repayment schedules. The full amount of the overdraft and the fees are due and payable immediately and the bank reserves the right to deduct full payment out of the next deposit of funds into the account, giving banks the first claim on a consumers' income.

For low-income account holders who have no cushion of cash in their bank account, repayment of the overdraft and the average $34 charge is difficult to make up before another debit hits their account, sending them further into the red, triggering another $34 fee, and accelerating a downward spiral of debt. As discussed below, a small percentage of customers end up paying enormous amounts for overdraft loans, and these consumers tend to be lower-income and minorities.

Consumers Trapped in Overdraft Loans Can Least Afford Astronomical Fees

Overdraft loans create a debt trap for a significant number of consumers. The FDIC examined individual transaction information from 39 banks to provide a snapshot of customers who overdrew their accounts on 22.5 million transactions. Nine percent of customers had ten or more insufficient fund transactions in one year. Consumers who overdrew ten to nineteen times in one year paid $451 in fees, while consumers who overdrew twenty times or more paid $1,610 in fees per year.[9]

Unfortunately, abusive overdraft fees have the greatest impact on those who can least afford them. In July of this year, 13 percent of a representative sample of 2000 adult Americans surveyed for CFA by Opinion Research Corporation said they had taken out a bank overdraft loan to cover a check or debit purchase or ATM withdrawal in the past year. Eighteen percent of those with incomes under $25,000 said they had used such a loan while 26 percent of African-Americans paid for overdrafts in the last year.[10] Two Center for Responsible Lending (CRL) surveys, conducted in 2006 and 2008, found that account holders who are repeatedly charged

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[8] 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 8 (Jan. 25, 2007), *available at* http://www.responsiblelending.org/pdfs/Debit-Card-Danger-report.pdf [hereinafter *Debit Card Danger*]. The FDIC study found that the median fee *charged* by surveyed institutions was $27. CRL's research reflects the average *paid* by account holders. It is not surprising that it is larger since larger institutions with more customers generally charge higher fees. Government Accountability Office report on bank fees, *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 16 (Jan. 2008) (noting larger institutions' average NSF and overdraft fees were higher than smaller institutions').
[9] FDIC Study. *Id.*
[10] ORCI Poll for CFA, July 2009.

abusive overdraft loan fees were more likely to be lower income, single, and non-white.[11] The FDIC study also found that customers living in low-income areas carry the brunt of overdraft fees.[12] This is not a recent development. CFA conducted a national opinion poll in 2004 which found that 28 percent of consumers say they overdrew their accounts which would trigger either insufficient funds or overdraft fees. Consumers who stated they overdrew their accounts and were most likely to pay overdraft and bounced check fees were moderate-income consumers with household incomes of $25,000 to $50,000 (37 percent). Those 25 to 44 years of age (36 percent) and African Americans (45 percent) were most likely to have bounced checks.[13]

Overdraft fees strip funds from Americans of all ages, but research indicates they hit America's oldest and youngest checking account holders—often the least financially stable—especially hard. Older Americans aged 55 and over paid $4.5 billion of the $17.5 billion total overdraft fees paid annually in 2006,[14] an especially alarming figure given that one in four retirees has no savings of any kind.[15] Those heavily dependent on Social Security pay nearly $1 billion,[16] while those entirely dependent on Social Security pay over $500 million.[17]

At the other end of the age spectrum, young adults who earn relatively little as students or new members of the workforce pay nearly $1 billion per year in overdraft fees.[18] CFA's 2009 ORCI poll found that 17 percent of those 18-34 years old had used overdraft loans in the last year, compared to 13 percent for the total sample. Because younger consumers are far more likely to use a debit card for small transactions than older adults,[19] they pay $3 in fees for every $1 borrowed for debit card overdrafts.[20] The situation is exacerbated by deals banks make with universities to provide school ID cards that double as debit cards. Banks pay the partner school for exclusive access to the student population and sometimes even split the fee revenue they collect on debit card transactions with the university.[21]

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[11] CRL Research Brief.

[12] FDIC Study at v. It further found that account holders who overdrew their accounts more than four times per year paid 93.4 percent of all overdraft fees. *Id.*

[13] ORCI Poll for Consumer Federation of America, 2004.

[14] See Shredded Security.

[15] Id. at 4 (citing 2008 Retirement Confidence Survey, Employee Benefit Research Institute (April 2008) finding that 28 percent of retirees have no savings). Shredded Security also notes that even those who do have savings are increasingly spending it on rising healthcare costs (citing Paul Fronstin, Savings Needed to Fund Health Insurance and Health Care Expenses in Retirement, Employee Benefit Research Institute (July 2006), projecting that retired couples will need between $300,000 and $550,000 to cover health expenses such as long-term care).

[16] *Shredded Security* at 6, Table 1. "Heavily dependent" was defined as recipients who depended on Social Security for at least 50 percent of their total income.

[17] *Id.*

[18] *See* 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) [hereinafter *Billion Dollar Deal*], *available at* http://www.responsiblelending.org/pdfs/billion-dollar-deal.pdf.

[19] Seven out of ten young adults would use a debit card for purchases costing less than $2. *Id.* (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. 15, 2009)).

[20] *Billion Dollar Deal*.

[21] *Id.* at 7 (citing *U.S. Bank Pays Campus for Access to Students*, Milwaukee Journal Sentinel, June 18, 2007 (noting the agreement between US Bank and the University of Wisconsin at Oshkosh prohibits all financial institutions other than US Bank and the college's own credit union from locating ATMs on campus); Amy

Banks Turn Debit Cards into High Cost "Credit Cards" When Overdrafts Are Permitted

Today, banks swipe a large portion of these fees when their account holders swipe debit cards at ATMs and checkout counters. A 2007 CRL report found, and the FDIC study confirmed, that debit card purchases are the most common trigger of overdraft fees.[22]

When debit cards first came into common use, they promised the convenience of a credit card without the cost, because debit card users were required to have the funds in their account to cover their purchase or withdraw cash. As recently as 2004, 80 percent of banks still declined ATM and debit card transactions without charging a fee when account holders did not have sufficient funds in their account.[23] But banks now routinely authorize payments or cash withdrawals when customers do not have enough money in their account to cover the transaction, so debit cards end up being very costly for many account holders. Among large banks, Citibank stands out for not permitting debit card transactions to overdraw its customers' bank accounts, protecting those consumers from unexpected high fees.

Banks and credit unions could prevent every dollar of debit card overdraft fee charges by simply notifying account holders when they are about to overdraw their accounts or by declining a transaction when there are insufficient funds available, as they did in the past. Indeed, consumers would appreciate the warning: 80 percent of consumers surveyed would rather have their debit transaction denied than covered for a fee, whether that transaction is $5 or $40.[24]

Institutions often claim that denial at the point of sale or ATM is not feasible, but it would be surprising if banks couldn't accomplish now technologically what they could in 2004. Furthermore, 7.9 percent of banks in the FDIC survey reported that they did inform customers at a debit card point of sale that funds were insufficient before transactions were completed, offering the customers an opportunity to cancel and avoid a fee, and 23.5 percent did the same at ATMs. It's difficult to believe that these banks have some sort of advanced technology unavailable to other banks.

Absent meaningful regulatory reform, banks will only increase their profits from overdraft fees as debit card transactions continue to skyrocket.[25] Debit card transactions will not only continue to grow as a percentage of all bank transactions, but they will continue to provide banks more transactions *overall* as more account holders use them in place of cash for small transactions.

Milshtein, *In the Cards*, College Planning & Management (Dec. 2005) (noting the fee-sharing deal Higher One has with partner universities)).

[22] *Debit Card Danger*. *See also* FDIC Study of Bank Overdraft Programs (Nov. 2008) (finding 41 percent of NSF-related transactions were triggered by point-of-sale/debit and another 7.8 percent by ATM transactions).

[23] Mark Fusaro, *Are "Bounced Check Loans" Really Loans?*, note 4, at 6 (Feb. 2007), *available at* http://personal.ecu.edu/fusarom/fusarobpintentional.pdf (last visited Mar. 15, 2009). *See also* Sujit Chakravorti and Timothy McHugh, *Why Do We Use So Many Checks?* Economic Perspectives, 3rd Quarter 2002, Federal Reserve Bank of Chicago, 44, 48 ("When using debit cards, consumers cannot overdraw their accounts unless previous credit lines have been established.")).

[24] 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 CRL Research Brief].

[25] Debit card transactions are increasing at a rate of 17.5 percent per year, while check payments are decreasing 6.4 percent annually. 2007 Federal Reserve Payments Study, Financial Services Policy Committee, *Federal Reserve Study Shows That More Than Two-Thirds of Noncash Payments Are Now Electronic* (Dec. 10, 2007), *available at* http://www.federalreserve.gov/newsevents/press/other/20071210a.htm (last visited Mar. 15, 2009).

Consumers Cannot Rely on Bank Overdraft Programs

Based on CFA's review of the largest banks' account disclosures and fine print in mid-2008, it is clear that consumers are unable to rely on their bank to honor overdrafts, are held responsible for immediately repaying the bank in many cases without notice or demand from the bank, and can have their overdraft "service" terminated at any time for any reason. Banks employ contract language making overdraft coverage a discretionary program. As a result, a consumer writing a check or paying by debit card never knows for sure whether the bank will honor or reject the overdraft. The consumer has no way of knowing whether any particular transaction will trigger merchant NSF fees, penalties for non-payment, or legal problems from writing an unfunded check.[26] Banks set internal but unannounced limits on the amount consumers can overdraw an account. Even if a bank provides fee-based overdraft programs, an individual consumer initiating a transaction for more funds than are on deposit cannot know with certainty that the transaction will be covered by the bank.

Banks make no promise to pay an overdraft while obligating consumers to immediately repay both the overdraft and the fee in a single balloon payment (often without notice or demand). The new Federal Reserve Reg E rules maintain the discretionary nature of overdraft coverage, even when consumers opt in to have debit card overdrafts paid for a fee. The Model disclosure form includes this statement: "We pay overdrafts at our discretion, which means we do not guarantee that we will always authorize and pay any type of transaction."[27] Banks use set-off to extract payment out of the next deposited funds, even when those funds are exempt federal benefits.[28]

Banks Speed Withdrawals but Not Deposits

In this age of fast-paced banking and electronic bill pay, anyone can temporarily slip into a negative balance. Check 21, passed in 2004, allows banks to debit accounts more quickly, while the rules for how long they can hold deposits before crediting accounts have not been updated in 20 years. In an age of 24/7 online banking and branches open six and seven days a week, the expedited funds rules defining a "business" day to exclude weekends result in consumers overdrawing when deposits could have covered the transactions. When banks hold deposited local checks until the permitted second business day, a paycheck drawn on a local bank and deposited on Friday afternoon can be held until Tuesday before money is available in the account to cover transactions. Fifth-day availability for deposited non-local checks means consumers may have to wait a whole week for deposits to become available, even when the check is drawn on the bank where it is deposited.

Banks Manipulate the Order of Processing Withdrawals and Drive Up Fee Revenue

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[26] The Indiana Department of Financial Institutions warned banks that "courtesy" overdraft programs arguably entice consumers to unwittingly commit a criminal offense. "Since the Program gives no assurance of coverage in the event of an overdraft, but leaves that to the discretion of the bank, a customer will never be certain that a bad check will be covered. This could make both the customer and the bank accountable under the criminal statute." Letter from J. Philip Goddard, Indiana Department of Financial Institutions, February 21, 2002.

[27] Federal Reserve Board, Model Consent Form for Overdraft Services (205.17), Regulation E: Docket No. R-1343, Final Rule, November 12, 2009.

[28] For examples of one-sided bank account contract terms, see CFA Comments to Federal Reserve Board, FRB Docket No. R-1314, August 4, 2008.

Financial institutions can manipulate the order in which withdrawals are posted in order to trigger more overdraft fees. Large institutions usually clear the largest transaction first, causing more transactions to overdraw the account. This practice generates more in overdraft revenues because the institution can charge an overdraft fee for each transaction once the account is below zero.

Consumers do not know the order in which items drawn on their account will be presented to their bank and are not likely to know the order in which their bank pays items. Banks bury the disclosures about the order in which they process transactions, and these disclosures provide the banks the widest possible latitude to engage in this behavior.[29] Even the Federal Reserve noted in adopting Truth in Savings regulations in 2005 that consumers who are aware that their account may be overdrawn are not likely to know the number of items that will bounce or the total fees they will be charged.[30]

Banks claim they do customers a favor by paying the largest, and presumably most important, items first to ensure those items get paid. But this argument is disingenuous when a bank has an overdraft loan program, *because the bank pays all of the transactions*, regardless of the order in which they are posted. So no matter what order the transactions are cleared in, all items get paid up to the bank's internal guidelines, and the only difference is how much the customer pays in overdraft fees. Legislation is necessary because bank regulatory agencies have failed to require banks to fairly treat their customers. (For a review of bank regulatory actions on processing order, please see Appendix C.)

Indeed, the FDIC's 2008 overdraft study found that over half of the large banks they surveyed process overdrafts from largest to smallest.[31] The survey further found, not surprisingly, that banks that engage in this abusive practice generate more overdraft fees than those that don't, but they also end up with more uncollectible debt related to overdraft loans.[32]

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[29] *See, e.g.*, US Bank's 26-page document, *Terms and Conditions for Deposit Accounts*, effective Feb. 1, 2005, *available at* https://fastapp.usbank.com/fastapp/en_us/termsAndConditions/TandC/LinkDepositAgreementCurrent.jsp (last visited Mar. 15, 2009): "If we get a batch of such items in a day (checks typically come in batches), and if one, some or all of them would overdraw the account if paid, we can pay or refuse to pay them, in any order, or no order . . . . We have all these options each time you might overdraw an account. What we do one time does not make that a rule you can rely on for the future"; Bank of America's 36-page document, *Deposit Agreement and Disclosures*, *available at* https://www1.bankofamerica.com/efulfillmentODAO/new_window_np.cfm?appURL=https://www1.bankofamerica.com/efulfillment/&showdaddoc=91-11-2000ED&daddoc2use=20081101&type=1&view=htm (last visited Mar. 15, 2009): "We may process and post items in any order we choose . . . . We may change categories and orders within categories at any time without notice. . . . [S]ome posting orders may result in more insufficient funds items and more fees than other orders. We may choose our processing and posting orders regardless of whether additional fees may result." Wachovia, *Deposit Agreement and Disclosures for Personal Accounts*, effective Feb. 8, 2008, *available at* http://www.wachovia.com/personal/online_services/disclosure/view/0,,7,00.html (last visited Mar. 15, 2009): "Although we generally pay larger items first, we are not obligated to do so and, without prior notice to you, we may change the order in which we generally pay items."

[30] Federal Reserve Board, Final Rule, Regulation DD, Docket No. R-1197, May 19, 2005, p. 4.

31 FDIC Study at iii (noting that 53.7% of large banks batched processed transactions by size, in order from largest to smallest).

32 FDIC Study at 62.

CFA's review of the largest banks' account agreements and customer information for comments filed in 2008 at the Federal Reserve found that fifteen banks disclose that they pay the largest transactions first or reserve the right to pay withdrawals in the order the bank chooses. There was insufficient information to determine payment order at one bank surveyed. Bank customer agreements typically reserve the bank's right to change the order of processing withdrawals without notice or consent from account holders.

The public wants banks to pay checks in the order they are received, as opposed to the current practice of allowing banks to routinely pay the largest first, which drains some accounts more quickly and increases bounced check fees. In a poll of 1018 people conducted by Caravan Opinion Research Corporation for CFA this summer, 70 percent supported (53 percent strongly supported) this requirement.[33] This confirms the finding of an older poll conducted for CFA which found that only 13 percent of the public support the bankers' claim that consumers want the largest transaction paid first.

Consumers Want To Decide Whether to Use Fee-Based Overdrafts

Most banks do not require customers to apply for and affirmatively choose to use fee-based overdraft coverage. Using either consultant-provided overdraft programs or internal bank policies, financial institutions decide which customers will be permitted to overdraw, the limit on the amount of overdrafts, and the fee or fees that will be charged. Banks do not contract or promise to cover overdrafts but claim this is a discretionary service that can be withdrawn at any time.

<u>Consumers Want Choice and Warning on Overdrafts</u>

Consumers think they should be provided the opportunity to affirmatively opt in to overdraft provisions of their checking accounts. CFA polled a representative sample of adult Americans in July 2009 and learned that 71 percent support requiring banks to gain the permission of customers before routinely providing loans to cover overdrafts. In CFA's 2004 ORCI poll, more than twice as many consumers thought it would be unfair for banks to permit overdrafts without obtaining their customers' consent (68 percent) rather than fair (29 percent).

The *Consumer Reports* National Research Center 2009 poll of a nationally representative sample of 679 people found that two-thirds of consumers prefer to expressly authorize overdraft coverage, so that there would be no overdraft loan – or fee – until they opted into the service. Likewise, two-thirds of consumers said that banks should deny a debit card or ATM transaction if the checking account balance is too low.

A 2009 Center for Responsible Lending survey found that 80 percent of consumers who wanted a choice about overdraft thought that their debit purchases and ATM withdrawals should only be covered for a fee if they affirmatively asked for overdraft coverage for those transactions. But the default arrangement for most institutions continues to be coverage—whether or not the account holder asked for it.

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33 CFA ORCI Poll, July 24-27, 2009.

In addition to wanting to opt-in for overdraft coverage, consumers want to be warned when ATM withdrawals will trigger an overdraft. CFA's 2009 ORCI poll found that 85 percent of adult Americans want banks to be required to disclose on the ATM screen when a withdrawal will overdraw an account. Seventy-three percent strongly supported that requirement. In a 2004 CFA poll, consumers by a wide margin said they are treated unfairly when banks permit them to overdraw at the ATM without warning. The 2004 ORCI survey also found that an overwhelming majority (82 percent) of consumers thought permitting overdrafts without any notice at the ATM was unfair, while 63 percent said it was "very unfair." Fewer than one in five (17 percent) people thought it was fair.

The *Consumer Reports* National Research Center poll also found that many consumers do not expect their bank to pay a debit card or ATM transaction that overdraws an account. Forty-eight percent of those polled thought an ATM card would not work if the account balance was too low and another ten percent thought they would not be assessed a fee if the bank allowed the overdraft. Thirty-nine percent of people thought their bank would either deny a debit transaction or allow it to proceed without charging a fee.[34]

A 2006 study by Forrester Research Group documented that consumers are "irked" by overdraft fees. While 65 percent of consumers with no overdraft fees said they were very satisfied with their banks, only 53 percent of consumers charged overdraft fees in the last few months reported being very satisfied.[35] By offering contractual overdraft protection by linked savings accounts, low cost lines of credit, and transfers to credit cards, banks can provide real protection at lower cost to consumers and avoid angering a large number of banking customers.

Overdraft Loans Are Credit but Don't Have Credit Protections

There is no question that overdrafts loans constitute a form of credit. Overdrafts are credit under the Truth in Lending Act (TILA), which defines "credit" as the right to "incur debt and defer its payment." See 15 U.S.C. §1602(e). When a bank permits a consumer to use the bank's funds to pay for an overdraft, and then requires the consumer to repay the bank, it is granting the right to incur a debt and defer its payment until the consumer's next deposit.

Involuntary Overdraft Credit

Overdraft loans are unique in that they are one of the few forms of *involuntary* credit. Banks impose this form of credit on consumers who have not requested it. Furthermore, some consumers may not be aware until they overdraw their account that they are accessing a high-cost credit product. This is especially true in the ATM or debit card context, where transactions that would overdraw an account were previously declined and did not incur a fee.

Indeed, we can recall only one time that consumers were sent loan products without their affirmative opt-in – when creditors sent unsolicited credit cards to consumers in the 1960s.[36] As

[34] *Consumer Reports* National Research Center, Financial Regulation Poll, as filed with the Federal Reserve Board in Reg E Docket R-1343, March 12, 2009.
[35] CUNA News: "Consumers ignore ATM fees, get irked at overdraft fees," January 17, 2006
[36] Note that a "stickiness" of default options was observed with respect to unsolicited credit cards, which is the same with unsolicited overdraft loans. When unsolicited credit cards were permitted, very few consumers opted out – only 1% returned the card. However, when prospective customers were asked whether they wanted to receive a

a result of the outcry over this practice, Congress stepped in, amending TILA in 1970 to ban unsolicited credit cards.[37] According to the Senate report that accompanied this TILA amendment, unsolicited credit cards encouraged consumers to incur unmanageable debt, and many consumers found them an unwarranted intrusion into their personal life.[38] These same problems cited by this Senate report nearly 40 years ago hold true today for unsolicited overdraft loans – they cause severe financial distress and represent an intrusion on the lives of consumers.

Note that in the case of unsolicited credit cards, the consumer at least has to affirmatively and knowingly take action to *use* the credit card, by making a purchase or taking a cash advance. In the case of overdraft loans, the consumer not only receives credit without requesting it, the consumer often unknowingly and involuntarily *uses* that credit when she triggers an overdraft, especially in the debit card situation where many consumers don't realize they can overdraw their accounts.

Thus, overdraft loans represent an even worse problem than unsolicited credit cards did nearly 40 years ago. S. 1799 would prohibit this "cramming" of overdraft loans on consumers by requiring banks to obtain specific written consumer consent before adding this feature to a bank account for debit purchases and ATM withdrawals.

<u>The Federal Reserve Board has Failed to Protect Consumers under Truth in Lending</u>

As discussed above, overdrafts are clearly "credit" under the federal Truth in Lending Act (TILA). The reason that overdraft loan programs do not require TILA disclosures is an exemption created by the Federal Reserve. Regulation Z, which implements TILA, excludes overdraft fees from the definition of a "finance charge." This exemption, written in 1969, was originally designed to exclude from TILA coverage the traditional banker's courtesy of occasionally paying overdrafts on an ad-hoc basis as a customer accommodation. However, banks exploited this exemption as a gaping loophole, creating and promoting predatory credit, extended on a routine basis without adequate disclosure – contrary to the clear statutory language and intent of TILA. The new Reg E rule maintains the special carve-out from TILA for the debit-card based overdrafts covered. As a result, S. 1799 would amend TILA itself to define an overdraft fee as a finance charge to ensure that institutions no longer benefit from a loophole to exploit account holders and that all short-term consumer lending operates by the same set of rules.

<u>Consumers Need "Truth" in Overdrafts to make Informed Decisions</u>

A requirement that banks comply with TILA and quote an effective APR for overdraft loans would be an eye-opener for the extreme high cost of these loans. In general, the fees for overdraft loans translate into APRs that are triple-digit or even higher. For example, consider a $100 overdraft loan that is repaid in two weeks, for which the bank charges a $20 fee. A comparable payday loan would have to disclose an APR of 520%. Instead of requiring TILA disclosures, the Board chose to regulate overdraft loans under the less effective Truth in Savings

card, only 0.7% said they would. Jack Metcalfe, *Who Needs Money*, New York Sunday News, Nov. 24, 1968, *reprinted in* 115 Cong. Rec. 1947, 1951 (Jan. 23, 1969).

[37] Pub. L. No. 91-508, 84 Stat. 1126-27 (Oct. 26, 1970).

[38] S. Rep. No. 91-739, at 2-44 (1970).

Act (TISA), simply requiring disclosure of the fee and a running tally. See Regulation DD, 12 C.F.R. Part 230.

Furthermore, most overdraft loans are paid much more quickly than two weeks – sometimes in a matter of days or hours – and sometimes the loan is only for a few dollars. The FDIC study gave a more realistic example of the extreme cost of fee-based overdraft. The typical $20 debit card overdraft with a $27 fee repaid in two weeks costs 3,520 percent APR if calculated as a closed-end loan. Bank overdraft loans are parallel to payday lending in that the high interest rates and short repayment time often trap marginally-banked consumers in a cycle of debt. Consumers should not have to pay triple or quadruple digit interest rates for either form of credit. (See Appendix D).

The failure of the Federal Reserve to require TILA disclosures and other protections for overdraft loans undermines the statute's key purpose of strengthening "competition among the various financial institutions and other firms engaged in the extension of consumer credit."[39] Without the uniform disclosure of the APR required by TILA, consumers have no way to compare overdraft loans to the cost of an overdraft line of credit or transfer from savings. Under the Fed's rules, the disclosed APR for a typical payday loan is 391% to 443%[40] but for an overdraft loan program the lender may disclose under TISA that the account is actually earning interest! Without apples to apples comparisons, there is no competition to reduce the cost of any of these products.

Legislation is needed because the Federal Reserve Board has failed to protect bank customers from abusive overdraft practices or to require financial institutions to comply with credit laws that apply to other forms of small lending or substitute products.

The new rule announced by the Federal Reserve last week amends Reg E and is substantially weaker than the provisions of S. 1799. The Board's rule does not recognize that overdrafts are extensions of credit that should require Truth in Lending disclosures, does not prohibit bank manipulation of the clearing of transactions to maximize overdraft fees, and places no limits on the number of overdraft fees banks can impose. The Federal Reserve's Reg E rule also does nothing to curb excessive fees. Industry calls for Congress to defer to a narrow Federal Reserve rule-making should be ignored. Opt-in alone is not sufficient protection. Consumers also get to "opt in" to using credit cards, but legislation was needed to curb abusive practices as well.

Overdraft Lending Cost Americans $24 Billion In 2008

Americans pay more in abusive overdraft loan fees than the amount of the loans themselves, paying almost $24 billion in fees in 2008 for only $21.3 billion in credit extended.[41] High fees,

[39] 15 U.S.C. § 1601(a)

[40] Keith Ernst, et al., *Quantifying the Economic Cost of Predatory Payday Lending*, Center for Responsible Lending (December 18, 2003), at 3.

[41] Eric Halperin and Peter Smith, *Out of Balance: Consumers pay $17.5 billion per year in fees for abusive overdraft loans*, Center for Responsible Lending, at 9 (June 2007), *available at* http://www.responsiblelending.org/issues/overdraft/reports/page.jsp?itemID=33341925 [hereinafter *Out of Balance*]. CRL analyzed 18 months of bank account transactions from participants in Lightspeed Research's

coupled with small overdrafts, result in consumers paying more to borrow from banks than the banks extend as credit.

Overdraft loan fees now make up 69 percent of all overdraft-related fees, while traditional NSF fees—generated when the paper check transaction is denied—make up only 31 percent.[42] The FDIC reports that all banks collected service charges on deposit accounts as of June 30, 2009 that totaled $21,796,013,000. Projected to a full-year, banks will take in almost $43.6 billion in bank account service charges. According to the FDIC report on overdrafts, about 74 percent of that line item on call reports is generated solely by insufficient fund fees and overdraft fees. If trends continue, consumers will pay banks $32.26 billion due to lack of sufficient funds to cover transactions. At 69 percent of that total, American consumers will pay banks alone almost $22.3 billion for overdraft loans in 2009. Credit union overdraft fees add to that total.

Small Dollar Overdrafts Trigger Steep Fees

The FDIC's report on bank overdraft loan programs, fees and practices, based on a detailed study of 462 FDIC-supervised banks and data on overdraft transactions from 39 banks, found that the typical debit card purchase overdraft was only $20 but cost an average $27 fee at FDIC banks. If repaid in two weeks, that overdraft costs 3,520 percent APR. The typical $60 ATM withdrawal on insufficient funds costs 1,173 percent APR. The median size check that overdraws an account is $66, an APR of 1,067 percent.[43] If the bank adds a "sustained overdraft fee" or requires repayment in less than two weeks, the APRs on these loans are even higher. Furthermore, because consumers often use their debit cards several times per day, multiple fees will be charged when an account is overdrawn.

CFA's 2009 survey of the nation's largest banks confirms that not only are multiple overdraft fees becoming more common, but the fee per transaction is getting larger. The maximum overdraft fee at this sample of banks is now $39, while the median fee is $35. Five of the largest banks use tiered fee schedules, with fees rapidly escalating when consumers incur more than a few overdrafts over a one-year period. US Bank charges $19 for the first overdraft, $35 for the second through fourth, and $37.50 thereafter. Fifth Third Bank switched to tiered fees in the last year, now charging from $25 to $37 per overdraft. Bank of America terminated its tiered fee structure and now charges $35 for each incidence.

Majority of Largest Banks Double Up on Overdraft Fees

Ten of the sixteen largest banks add sustained overdraft fees when consumers are unable to pay the overdraft and fee within a few days. On top of already high initial overdraft fees, SunTrust adds a $36 additional fee while Bank of America and Citizens Bank add a $35 fee when overdrafts are not repaid in less than a week. Chase Bank adds up to $25 per overdraft when an overdraft goes unpaid for five days. When initial overdraft fees and sustained overdraft fees are combined for overdrafts unpaid after seven days, consumers can be charged as much as $74 at Citizens Bank for a single overdraft. The combined cost at Bank of America is $70, at SunTrust $72, and at U.S. Bank $69.50. In recently announced changes to overdraft programs, six of the

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Ultimate Consumer Panel, from January 2005 to June 2006. For further discussion of CRL's database and methodology, *see Out of Balance* at 13-14.

[42] *Out of Balance* at 10.

[43] FDIC Study at v.

largest banks lowered or set a maximum on the number of overdraft fees charged on a single day. For banks with a limit on daily fees, the range is three to seven overdraft fees levied. (See Appendix B.)

Voluntary Bank Overdraft Changes are Too Little, Too Late

Recently announced changes in overdraft programs by some large banks are unlikely to significantly reduce costs to customers. Some banks have changed the threshold that triggers overdraft fees to a total of $5 to $10 in total overdrafts per day before fees are charged and some have lowered the total number of overdraft fees a consumer can be charged in one day. But none of the banks are lowering the fees charged for initial or sustained overdrafts.

While a few banks will soon permit consumers to opt-in for some forms of overdraft coverage, the norm is to permit current customers to opt-out and to only permit new customers to make choices about overdraft loans at those banks announcing changes. It has taken some of the largest banks in the country four years to get around to complying with the Interagency Guidelines for overdrafts, issued in 2005, that advised banks to at least provide an opt-out opportunity for consumers. Chase Bank plans to permit its existing and new customers to affirmatively sign up to use overdraft loans and will process payments as they come in during the day. In some cases, banks will permit only new customers to opt in to some forms of overdrafts in the future. In a change initiated in the last year without fanfare, Citibank does not permit its customers to incur overdrafts when using debit cards for purchases or at ATMs, although Citibank customers can incur four $34 overdraft fees per day for checks. Citibank does not charge sustained overdraft or tiered fees.

Other banks have also announced adjustments to their overdraft practices. For example, Capital One, starting in early 2010, will not charge fees if consumers overdraw their accounts by a total of $5 or less in a single day and will limit the number of overdraft fees to four per day. Capital One permits customers to opt out of having overdrafts paid for a fee. Starting mid-2010, Capital One will permit new account holders to decide whether to opt-in to overdrafts triggered by debit cards and at ATMs. (See Appendix A: Summary of Recent Bank Changes to Overdraft Programs.)

S. 1799 Protects Bank Account Customers

S. 1799, the FAIR Overdraft Coverage Act, will prevent abuses created by the relatively new system of unauthorized fee-based overdraft lending that is premised on generating fee revenue rather than protecting the funds of account holders. This important legislation places bank overdraft lending on the same legal playing field as other forms of small-dollar loans and provides consumers with information necessary to make an informed decision.

S. 1799 requires financial institutions to obtain account holders' specific written consent in order for financial institutions to enroll them in fee-based overdraft programs triggered by debit cards at point of purchase and ATM withdrawals. We also support requiring affirmative consent for overdraft coverage triggered by checks, preauthorized debits, and other ways funds are spent from consumers' accounts. This control over bank account credit features is what consumers expect and want to have.

S. 1799 requires banks and credit unions to warn account holders before making them a high-cost loan at the ATM or from a teller and permits them to terminate the withdrawal to avoid the fee. This warning is what consumers expect and want. A GAO study is mandated to explore the feasibility of point-of-sale warning and ability to terminate a debit purchase in the future.

S. 1799 prohibits manipulation of account activity if the result is to increase overdrafts. This should mean no debiting accounts with the highest dollar charge first in order to increase the number of overdraft fees an account holder is charged and no holding deposits before crediting accounts in order to create a negative balance and charge an overdraft fee. Bank manipulation of payment order is strongly opposed by consumers.

S. 1799 also clarifies that an overdraft fee is a finance charge subject to the Truth in Lending Act. This will confer TILA protections to overdraft loans and require cost-to-borrow disclosures as determined by the Federal Reserve. The Board will need to devise disclosures that provide consumers with comparable cost to borrow information.

S. 1799 requires the Federal Reserve Board to set "reasonable and proportional" bank overdraft fees, based on the cost to banks to cover these loans. Competition has had no impact on bank overdraft fees that continue to escalate even in a recession. This feature of S. 1799 is comparable to the CARD Act's requirement that the Board set the over-the-limit fee.

S. 1799 protects consumers from being buried in overdraft fees and requires banks to provide information on their less expensive and more appropriate products available to address overdrafts or extend small dollar loans. The bill applies the FDIC's payday loan suitability standard[44] as well as the over-the-limit policy in the CARD Act by limiting banks to one overdraft fee per month up to a total of six per year. The bill permits banks to cover more overdrafts without charging additional fees. Banks can and should reject debit card purchases or ATM withdrawals for which funds are not available, which was standard banking practice just a few years ago. A cap on the number of overdraft fees that can be charged is not an invitation for consumers to initiate numerous unfunded transactions. In fact, limiting banks to one fee per month gives banks a financial incentive to limit unfunded purchases and withdrawals.

S. 1799's one-fee-per-month limit will prevent banks from piling on sustained overdraft fees when consumers are unable to repay the overdraft and initial fee in just a few days. Not only will this limit protect frequent users of overdrafts, it will provide an incentive for financial institutions to market their more affordable and appropriate products such as overdraft lines of credit, transfers from savings, and small dollar loans.

We also urge the Senate to enact Senator Dodd's legislation to create the Consumer Financial Protection Agency to provide a strong consumer protection agency for financial services. The

[44] FDIC Guidelines for Payday Lending, 2005, Renewals/Rewrites amended the Retail Classification Policy, directing institutions to "Ensure that payday loans are not provided to customers who had payday loans outstanding at any lender for a total of three months during the previous 12 months…What a customer has used payday loans more than three months in the past 12 months, institutions should offer the customer, or refer the customer to, an alternative longer-term credit product that more appropriately suits the customer's needs. Whether or not an institution is able to provide a customer alternative credit products, an extension of a payday loan is not appropriate under such circumstances." See: www.fdic.gov/news/news/financial/2005/fill405a.html, viewed 3/2/2005. Since payday loans are typically two weeks in duration, a three month payday loan limit is equivalent to permitting six monthly overdraft fees per year.

CFPA will be assigned the job under Truth in Lending to write the rules that implement the FAIR Overdraft Protection Act, to supervise compliance with these new protections, and to provide consumer information. The Federal Reserve has failed to adequately exercise its authority to protect consumers from unfair and abusive overdraft loan practices.

CONCLUSION

Today, as many American families struggle to meet daily obligations in the worst economy since the Depression, the last thing they need is to be surprised by high-cost credit to which they never expressly consented. S. 1799 would benefit consumers by requiring financial institutions to get consumers' affirmative and informed consent to select fee-based overdraft programs for debit card purchases and ATM withdrawals; defining overdraft fees as a finance charge covered by Truth in Lending; capping fees based on Federal Reserve rules using reasonable and proportional costs to cover an overdraft; and limiting overdraft fees to one per month up to six per year. Overdraft loans are not a "convenience," but are dangerous high-cost loans that must be reined in, even for people who agree to use them. We urge this Committee to reverse the drain on vulnerable consumers' bank accounts and the current trend toward even greater overdraft abuses by supporting S. 1799.

Appendix A

Summary of Recent Changes to Bank Overdraft Practices and Prices

These descriptions of recent changes to bank overdraft programs are based on bank press releases, information posted on bank websites, and news stories.

Bank of America will not charge overdraft fees if the total amount overdrawn in a day is less than $10. The bank is reducing the total number of overdraft fees it can impose in a single day from the current ten to four. As recently as February of this year, however, Bank of America had limited the number of overdrafts to five per day.

When the changes took effect October 19th, a Bank of America customer who overdrew on four transactions that totaled $10 or more would be charged $35 for each overdraft for a total of $140. If that customer is unable to repay in five days, she will be charged another $35 sustained overdraft fee for each unpaid overdraft up to $140 for a total of $280 in fees for as little as $10 in overdrafts for less than a week of credit.

Next June, Bank of America will make it easier for customers to opt out of using overdraft loans and will permit only new customers to opt in for overdraft loans. Bank of America did not announce a change to its current practice of manipulating transaction order by paying largest transactions first, a practice that can increase the number of overdraft fees consumers pay.

BB&T is changing its overdraft practices for debit cards and ATM withdrawals starting the first quarter of 2010 and will not charge fees for overdrafts totaling $5 or less in a day. The bank, which currently has no limit on the number of fees it charges per day, will limit overdraft fees to four per day. The bank will start alerting ATM users when a withdrawal will overdraw the account. The bank currently permits customers to opt out of overdraft coverage.

BB&T charges $35 per overdraft and adds a $30 sustained overdraft fee if not repaid in seven days. When the changes take effect, the bank will be able to charge up to $140 per day for four overdrafts that total $5.01. If customers are not able to repay four overdrafts plus $140 in one week, the bank will charge another $120 in sustained fees for a total cost of $260 for as little as $5.01 in credit. BB&T is not providing its customers the right to affirmatively opt in to overdraft loans, but only permits customers to opt out.

Chase announced that it will give its 25 million current and new accountholders the right to opt in to overdrafts triggered by a debit card, but not for checks and other transfers. Debit card transactions and ATM withdrawals will be posted as they occur, which the bank expects will result in fewer fees. Chase will not charge its overdraft fee for overdrafts of $5 or less in a day and is reducing the maximum number of overdraft fees from six to three per day. Chase says that it denies ATM transactions that exceed the available funds in the account.

Chase has a tiered overdraft fee schedule, with the first overdraft in a year costing $25, the next three overdrafts at $32 each, and five or more overdrafts in a year at $35 each. Chase also adds a sustained overdraft fee if an overdraft is not fully repaid in five days. This second fee varies across the country, with a maximum of $25. As a result of the announced changes, a consumer who has three overdrafts in a day totaling $5.01 will owe the bank $89 if these are the first overdrafts in a year. If the customer has overdrawn at least four times in the past year, three overdrafts cost $105 with sustained fees adding another $75 for a total $180 for as little as $5.01 borrowed for less than a week.

Regions Bank is also setting a $5 total overdraft trigger for charging overdraft fees and limiting the number of overdraft fees per day to four, effective the first quarter of 2010. The bank permits customers to opt out of overdrafts and alerts ATM users that a withdrawal could create an overdraft. Regions Bank waives the first overdraft fee a customer triggers, then charges tiered fees for any subsequent overdrafts. The first fee in a year is $25, the next two overdrafts cost $33, and four or more overdrafts in a year's period cost $35 each. As a result of the announced changes, after the first overdraft in the customer's history with the bank, the bank will be able to charge a total of $126 for four overdrafts of $5.01 or more total in one day.

US Bank's changes as of the first quarter 2010 include a $10 threshold of total overdrafts per day to trigger an overdraft fee and a three overdraft fees per day limit. Currently, US Bank permits up to six overdraft fees to be charged in one day. US Bank charges tiered overdraft fees, starting at $19 for the first one, $35 for two to four, and $37.50 for five or more in a year, the highest fee charged by the sixteen largest banks surveyed by CFA in July. A customer with three overdrafts in a day will owe $89 for the first incident. If the customer has overdrawn four times in the past year, total fees for three overdrafts will be $112.50 for as little as $10.01 borrowed.

US Bank announced it would permit current customers to opt out of using overdraft loans and new customers the ability to opt in having overdrafts paid for a fee. The bank will set an annual unspecified cap on the total amount of overdraft fees that can be assessed on a single account and will evaluate its order of posting payments to accounts. Currently, the bank pays the largest transactions per day first, which can trigger more fees.

Wells Fargo and **Wachovia** customers will not be charged overdraft fees if the total amount overdrawn per day is $5 or less and will limit the total number of overdraft fees per day to four. Wells Fargo currently permits ten overdrafts per day and Wachovia has no maximum. Wells Fargo and Wachovia customers will get to opt out of having overdrafts paid for a fee, but do not get the right to opt in. Wells Fargo charges $35 per overdraft as does Wachovia as of July. As a result of the announced changes, bank customers can be charged $140 in overdraft fees for as little as $5.01 in four overdrawn transactions.

Appendix B

Update to CFA July 2009 Survey of Overdraft Fees

CFA issued a survey of overdraft fees as of late July. This survey is updated to show banks' announced overdraft program changes to these terms in **bold**.

Bank	OD Fee	Sustained OD Fee	Maximum Daily Fees
Bank of America	$35	$35 after 5 days	**4 per day**
BB&T	$35	$30 after 7 days	**4 per day**
Chase	$25 first OD $32 2 to 4 OD $35 5 or more	0 to $25 per OD after 5 days	**3 per day**
Citibank (Does not permit overdrafts by debit card)	$34	None	4 per day
Citizens Bank	$25 first OD $37 2nd OD day $39 3 or more	$35 after 6 days $35 2nd fee/ 10 days	No Max
Fifth Third Bank	$25 first OD $33 2 to 4 OD $37 5 or more	$8/day after 3 days	No Max
HSBC	$35	None	No Max
National City Bank	$30 to $36	None	No Max
PNC Bank	$31 1 to 3 OD $34 4 to 6 OD $36 7 or more	$7/day after 4 days Max $35 sustained	No Max
Regions Bank	$25 first OD	None	**4 per day**
SunTrust	$36	$36 on 7th day	No Max
TD Bank	$35	$20 on 10th day	6 OD and 6 NSF
US Bank	$19 first OD $35 2 to 4 $37.50 5 or more	$8/day after 3 days	**3 per day**
WAMU	1 free OD $34	None	7 OD
Wells Fargo/ Wachovia	$35	None	**4 per day**

Appendix C

Federal Bank Regulatory Agencies Failed to Stop Processing Order Manipulation

The Comptroller of the Currency permits national banks to rig the order in which debits are processed. When national banks began to face challenges in court to the practice of clearing debits according to the size of the debit -- from the largest to the smallest --rather than when the debit occurred or from smallest to largest check, the OCC issued guidelines that allow banks to use this dubious practice.

The OCC issued an Interpretive Letter allowing high-to-low check clearing when banks follow the OCC's considerations in adopting this policy. Those considerations include: the cost incurred by the bank in providing the service; the deterrence of misuse by customers of banking services; the enhancement of the competitive position of the bank in accordance with the bank's business plan and marketing strategy; and the maintenance of the safety and soundness of the institution.[45] None of the OCC's considerations relate to consumer protection.

The Office of Thrift Supervision (OTS) addressed manipulation of transaction-clearing rules in the Final Guidance on Thrift Overdraft Programs issued in 2005. The OTS, by contrast, advised thrifts that transaction-clearing rules (including check-clearing and batch debit processing) should not be administered unfairly or manipulated to inflate fees.[46]

The Guidelines issued by the other federal regulatory agencies merely urged banks and credit unions to explain the impact of their transaction clearing policies. The Interagency "Best Practices" state: "Clearly explain to consumers that transactions may not be processed in the order in which they occurred, and that the order in which transactions are received by the institution and processed can affect the total amount of overdraft fees incurred by the consumers."[47]

CFA and other national consumer groups wrote to the Comptroller and other federal bank regulators in 2005 regarding the unfair trade practice of banks ordering withdrawals from high-to-low, while at the same time unilaterally paying overdrafts for a fee. One of the OCC's "considerations" is that the overdraft policy should "deter misuse of bank services." Since banks deliberately program their computers to process withdrawals high-to-low and to permit customers to overdraw at the ATM and when making purchases with debit cards, there is no "misuse" to be deterred.

[45] 12 C.F.R. 7.4002(b).
[46] Office of Thrift Supervision, Guidance on Overdraft Protection Programs, February 14, 2005, p. 15.
[47] Dept. of Treasury, Joint Guidance on Overdraft Protection Programs, February 15, 2005, p. 13.

Appendix D

Bank Overdrafts are Payday Loans

Credit extended to consumers when banks pay transactions that overdraw accounts is very similar to loans made by payday lenders. Payday loans are small cash loans based on the lender holding the borrower's personal check for future deposit on the next payday. Parallels for these two forms of high-cost lending:

- Both require borrowers to have a bank account. Banks permit accountholders that meet threshold qualifications to use overdrafts. Payday lenders require borrowers to have a checking account and to show a recent bank statement in order to obtain a loan.

- Both are based on borrowers writing a check or authorizing a debit for more than the borrower has in the bank. Overdrafts are triggered when a consumer uses a debit card at a retailer, withdraws cash at an ATM, or has a check covered by the bank despite insufficient funds. Payday lenders hold the borrower's personal check or debit authorization as both security for the loan and the means of collecting payment.

- Both are due and payable within a few days. Payday loans are due in full on the borrower's next payday, generally 14 days. Overdraft loans are due and payable immediately. If not repaid within days, some banks add additional fees.

- Both require balloon payments of the full amount of the loan and the fees. If payday loan borrowers do not pay with cash on payday, the lender sends the check to the bank for collection. Banks demand immediate repayment and use set-off to withdraw payment for the overdraft and fees from the next funds deposited into the consumer's account.

- Both loans cost triple or quadruple-digit interest rates. The annual percentage rate for a one-week $200 payday loan at $17.50 per hundred is 910 percent, while a $200 overdraft loan repaid in one week for a $35 fee costs the same. The FDIC reported that a typical $20 debit overdraft, costing $27 fee, repaid in two weeks costs 3,520 percent APR.

- Both put borrowers in a debt trap. The typical payday loan borrower has 9 loans per year and ninety percent of the business is generated by borrowers with five or more loans per year. The FDIC reports that 84% of all insufficient funds and overdraft fees were paid by 8.9 percent of account holders who had ten or more overdrawn transactions in a year.

- Failure to immediately repay loans sets off a cascade of other fees. Payday lenders charge insufficient funds fees when checks are returned by the bank, plus the consumer's bank charges NSF fees each time. Bank collection through set-off may trigger more overdrafts when other payments are presented to the bank. Banks with sustained overdraft fees drive up the cost of the initial overdraft.

- Both products put consumers at risk for losing their bank accounts. Banks typically do not permit overdrawn customers to close accounts until the overdraft and fees are paid. Too many unpaid overdrafts or NSF fees can result in account closure. If the bank account is closed due to repeat overdrafts, this will be listed on credit reports which may prohibit consumers from opening a new bank account. A Harvard Business School study found that use of payday loans increases involuntary bank account closures.

Chart: The High Cost of Bank Overdraft "Payday" Loans

This chart illustrates what a $100 overdraft would cost when the overdraft remains unpaid for seven days, using the bank's maximum fee and the sustained overdraft fees that would be imposed over a seven-day time period. The APR is computed as if this were a closed-end one-week payday loan.

Bank	**Max OD Fee**	**Sustained OD Fee Times # of Days**	**Total**	**APR/7 days**
Bank of America	$35	$35	$70	3,640%
BB&T	$35	$30	$65	3,380%
Chase	$35	$12.50 (AZ)	$47.50	2,470%
Citibank	$34	0	$34	1,768%
Citizens	$39	$35	$74	3,848%
Fifth Third	$37	4x$8 = $32	$69	3,588%
HSBC	$35	0	$35	1,820%
National City	$36	4x$8 = $32	$68	3,536%
PNC	$36	3x$7 = $21	$57	2,964%
Regions	$35	0	$35	1,820%
SunTrust	$36	$36	$72	3,744%
TD Bank	$35	$20	$55	2,860%
U.S. Bank	$37.50	4x$8 = $32	$69.50	3,614%
Wachovia	$35	0	$35	1,820%
WaMu	$34	0	$34	1,768%
Wells Fargo	$35	0	$35	1.820%