Consumer Federation of America

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March 30, 2009

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

RE: FRB Docket No. R-1343

Dear Secretary Johnson:

Consumer Federation of America (CFA)[1] appreciates the opportunity to submit comments addressing overdraft transactions in the above referenced docket. We join the Center for Responsible Lending in their detailed comments in this docket and are adding these supplemental comments to share the results of our survey of large bank overdraft fees and practices.

We appreciate that the Federal Reserve Board (Board) is considering giving consumers the right to choose whether to use banks' overdraft loans. In prior comments, we have urged the Federal Reserve to require financial institutions to comply with the Truth in Lending Act when extending credit via bank overdraft loans.[2] CFA also filed comments regarding the Board's proposed rules under Reg AA to curb unfair trade practices by banks when transactions that exceed the balance in an account are covered and consumers are charged a fee.[3]

The current docket is narrowly focused on single use debit card purchases and ATM withdrawals that financial institutions permit to overdraw the consumer's account. We strongly urge the Board to give consumers affirmative control of their bank accounts by requiring financial institutions to only provide overdraft loans when consumers have

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[1] CFA is a nonprofit association of some 300 pro-consumer groups, with a combined membership of 50 million people. CFA was founded in 1968 to advance consumers' interests through research, advocacy and education. CFA has filed comments with the Federal Reserve Board on overdraft issues, testified before the House Financial Services Subcommittee on HR 946, and issued numerous reports on bank NSF and overdraft fees and practices. For more information, go to www.consumerfed.org.
[2] CFA, Comments, Federal Reserve System, 12 CFR Part 230 Docket No. R-1197, Proposed Amendments to Regulation DD, August 6, 2004 at http://www.consumerfed.org/pdfs/Document.pdf; CFA Comments, FRB Docket No. R-1136, January 27, 2003 at http://www.consumerfed.org/pdfs/frbcomments.pdf.
[3] CFA Comments Federal Reserve System, FRB Docket No. R-1314, August 4, 2008. At http://www.consumerfed.org/pdfs/OD_FRB_Comments.pdf

affirmatively chosen to use that credit product. Opt-in provides real consumer choice while requiring opt-out maintains the status quo. The opt-in requirement should apply to all types of payment devices that can overdraw a consumer's account. To accomplish that, we urge the Board to reopen the Reg AA docket to require opt-in for other forms of overdraft loans.

Currently most banks extend credit without authorization to customers by paying checks, debit card purchases, preauthorized payments, and ATM withdrawals despite insufficient funds in the account. The FDIC reports that over three-fourths of 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.[4] Banks charge a fee for each overdraft and collect payment for both the overdraft and the fee by set-off, unilaterally withdrawing payment from consumers' bank accounts. Some banks add additional sustained overdraft fees when accounts are not brought into balance immediately. According to the Center for Responsible Lending, consumers pay $17.5 billion a year to borrow $15.8 billion in unauthorized loans.[5]

Banks do not get consent from their customers to use overdraft programs, do not warn customers that a transaction will trigger an overdraft, do not provide cost of credit disclosures, and do not extend overdrafts under a firm agreement to pay overdrafts with clear terms. As a result, consumers pay billions to inadvertently borrow from banks without the benefit of consumer protections that apply to equivalent small loan products. As consumers switch to debit card purchases to avoid debt during this recession, they run the risk of inadvertently incurring extremely expensive debt through overdraft loans.

CFA's survey of the bank overdraft fees and practices that follows reveals that banks are increasing fees, removing their limits on the number of fees to be charged per day, and piling on sustained overdraft fees when consumers do not make immediate deposits to cover overdrafts. Competitive pressure on overdraft loan fees and terms would improve if the Federal Reserve requires opt in consent for fee-based overdrafts. A bank should have a hard time persuading a consumer to affirmatively choose to be charged $74 in overdraft and sustained overdraft fees for a single $20 debit card overdraft repaid in one week.

The proposals in this docket also do not address bank practices that maximize the number of transactions that overdraw and trigger a fee, such as clearing the largest transactions first. The FDIC's recent study found that over half of the large banks surveyed process overdrafts from largest to smallest.[6] The survey further found that banks that engage in this abusive practice generate more overdraft fees than those who don't while also ending up with more uncollectible debt related to overdraft items.[7] We

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[4] FDIC Study of Bank Overdraft Programs at iii (Nov. 2008)
[5] 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, July 11, 2007, page 11.
[6] FDIC Study at iii (noting that 53.7% of large banks batch processed transactions by size, in order from largest to smallest.)
[7] FDIC Study at 62

urge the Board to use its FTC Act authority to address the unfair practice of ordering withdrawals largest to smallest to maximize the number of overdraft fees charged.

We urge the Board to do the following:

- **Require banks to get consumers' affirmative consent to use overdraft loans** and prohibit banks from charging for paying an overdraft if the consumer has not affirmatively contracted for this form of credit. The Board's proposed option to continue the status quo by permitting banks to only offer an opt-out on just two forms of overdraft loans is inadequate consumer protection. If opt-in is not required, the Fed should ban overdraft loans through ATM and debit card transactions as patently unfair trade practices. We also urge the Board to reopen the Reg AA docket to provide consumer choice for overdraft loans based on all other payment methods from consumers' accounts.

- **Require banks to comply with Truth in Lending** cost disclosures and other TILA protections. The Federal Reserve should change the Reg Z provision and Official Staff Commentary sections that currently exempt banks from TILA cost disclosures as long as the bank does not contract to cover overdrafts and does not charge more for overdrafts than the bank charges as an insufficient funds fee.[8] Consumers need cost of credit information to make informed choices in deciding whether to opt-in for their banks' overdraft programs and to choose between alternate forms of credit including overdraft lines of credit.

- **Expand the proposal that limits overdraft fees caused by the merchant's hold placed on accounts when debit cards are used to also include overdrafts caused by deposit holds**. The Expedited Funds Availability Act time period for holding deposits has not been updated since it took effect in 1990. Although funds now move quickly due to Check 21 and electronic check conversion, banks can still hold a deposited check for days after the check has cleared, depriving consumers of access to their own money. It is a double hit on consumers to both be deprived of access to their funds and be charged an overdraft fee when a transaction that would have been paid overdraws the account. This protection should extend to insufficient funds fees triggered by debit and deposit holds as well.

- **Extend Overdraft Protections to Prepaid Debit Cards**

[8] Reg. Z § 226.4 (c)(3). Charges imposed by a financial institution for paying items that overdraw an account are not "finance charges" unless the payment of such items and the imposition of the charge were previously agreed upon in writing. Official Staff Commentary on this section states: "A charge on an overdraft balance computed by applying a rate of interest to the amount of the overdraft is not a finance charge, even though the consumer agrees to the charge in the account agreement, unless the financial institution agrees in writing that it will pay such items." Official Staff Commentary § 226.4(c). In addition, the Official Staff Commentary § 226.4(b)(2)-1 excludes a fee on a deposit account with a credit feature from being considered a finance charge if the fee does not exceed the charge for an account that does not include a credit feature.

The current proposal under the Electronic Fund Transfer Act and Reg E would not extend overdraft protections to prepaid cards not subject to that law, leaving unprotected those consumers who "bank" by stored value cards. This is an example of the two-track financial services market, where banked consumers and unbanked and usually lower-income consumers do not benefit from the same set of rules.[9] We urge the Board to extend all overdraft loan protections to prepaid debit cards that function as a bank account for families.

Applying overdraft loan protections to prepaid debit cards would also benefit Americans who receive unemployment benefits via cards. Recent news reports revealed that some state unemployment cards come with automatic fee-based overdraft coverage that costs the unemployed user as much as $17 or more per overdraft transaction.[10] Unemployed consumers who rely on benefits to make ends meet should not be exposed to exorbitantly expensive involuntary debt. Since these cards function as equivalent to bank accounts for individuals, the same protections should apply.

For Opt-In to Be Effective, Consumers Need TILA Cost Information

Consumers need comparative cost information to make an informed decision on whether to opt into borrowing from the bank to pay overdrafts. If overdraft loans were subject to TILA/Reg Z cost disclosure requirements, consumers would be given comparable price tags to use in deciding whether to borrow $50 from the bank at a cost of $35 which translates to the equivalent APR for a closed end loan of 3,640 percent if repaid in one week (and the bank did not also charge sustained overdraft fees). If banks were required to disclose the cost of borrowing via overdraft loans and had to obtain consumer consent ahead of time to provide this product, competitive pressures would have some impact on the cost and terms of borrowing money in this manner. Clear cost disclosures would likely motivate more consumers to apply for other forms of lower cost overdraft protection or choose other credit products.

Consumers Think the Current Overdraft Product is Unfair

Consumers by a wide margin believe they are treated unfairly when banks permit them to overdraw at the ATM without warning. A 2004 survey poll of a representative sample of 1,000 adult Americans conducted for CFA by Opinion Research Corporation

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[9] SVC overdraft loan fees are extremely expensive. See Testimony, Jean Ann Fox, CFA, Subcommittee on Social Security, Ways and Means Committee, "Hearing on Protecting Social Security Beneficiaries from Predatory Lending and Other Harmful Financial Institution Practices," June 24, 2008. http://www.consumerfed.org/pdfs/Jean_Ann_Fox_Testimony_Ways_and_Means_Social_Security_6-24-08.pdf

[10] See AP Impact: Jobless Hit with Bank Fees on Benefits, Christopher Leonard, AP Business Writer (Feb. 20, 2009) available at http://news.yahoo.com/s/ap/20090220/ap_on_bi_ge/bank_fees_jobless_benefits; 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.

International (ORCI) 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. Consumers think they should be provided the opportunity to affirmatively opt-in to overdraft provisions of their checking accounts. 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).

More recent consumer polling submitted by Consumers Union and the Center for Responsible Lending in this docket confirm that consumers want to be able to choose whether to use overdraft loans. Consumers want to be able to opt into using a bank's overdraft program.

CFA Survey Findings: Sixteen Largest Bank Overdraft Fees and Terms

In early 2009, CFA updated a survey of the largest banks that collected fee schedules, account agreements, and bank brochures from branches and websites at sixteen of the largest banks to learn more about current fees and overdraft terms and practices. This provides an update to a larger study conducted by CFA in 2005[11] and a 2008 survey for the Federal Reserve Reg AA docket comments.[12] In the 2005 study, CFA found that 80 percent of the 33 largest banks had contract terms that permitted non-contractual overdrafts. Current information from sixteen large banks indicates that all of them permit consumers to overdraw and all impose steep fees for those transactions. None of the largest banks provide consumers the opportunity to affirmatively sign up for overdraft loans.

Big Bank Overdraft Fees

Big bank fees for a first overdraft in a one-year period range from $19 for the first overdraft at US Bank to $36 at National City Bank. For some accounts, WAMU advertises that the first overdraft fee is waived. Some banks have tiered overdraft fees. The top maximum fee is $39 charged by Citizens Bank for the third or more overdrafts in a year. The median top fee charged by the largest banks is $35 per transaction that overdraws an account, regardless of the amount of credit extended. Nine of the banks charge $35 per overdraft.

Half of the largest banks have tiered overdraft fee schedules, charging higher fees for more than one overdraft over a rolling thirteen month time period. In 2005, only three major banks used tiered fees. For example, Regions Bank charges $25 for the first overdraft in a year, $33 for the next three overdrafts, and $35 each for four or more. US Bank charges $19 the first time, $35 for the second to fourth overdraft, and $37.50

[11] Jean Ann Fox and Patrick Woodall, "Overdrawn: Consumers Face Hidden Overdraft Charges from Nation's Largest Banks," Consumer Federation of America, June 2005
[12] Consumer Federation of America, Comments, FRB Docket No. R-1314; OTS-2008-0004; NCUA RIN 3133-AD47, Reg AA, August 4, 2008.

thereafter. Fifth Third Bank switched to tiered fees in the last year, previously charging a flat $33 per overdraft. Fifth Third now charges $25 for the first overdraft, $33 for the second to fourth, and $37 for five or more. In February, Bank of America dropped its $25 initial overdraft fee and now charges $35 for each overdraft.

In addition to per incident overdraft fees, nine banks charge sustained fees when overdrafts are not repaid within a few days. The sustained overdraft fees range from a flat $12.50 at Chase in Arizona after five days, $30 charged by BB&T after seven days, and $35 at Citizens and SunTrust after overdrafts remain unpaid for a week. Other banks charge a per day fee of $5 to $8 for overdrafts unpaid after a few days. This fee is going up, as well. PNC recently raised its sustained overdraft fee from $6 to $7 for a maximum of $35 over five days.

Despite the Agencies' Best Practices[13] recommendation that banks limit the number of overdraft fees charged per day, only three of sixteen large banks set maximum fees per day while the other thirteen banks charge an unlimited number of fees for a string of transactions that overdraw an account in one day. Citibank caps fees at four per day for a $136 total while WAMU limits its overdraft charges to seven per day ($238), up from five per day last year. US Bank limits total overdraft and NSF fees to 12 per day which would cost consumers up to $450 per day. Bank of America terminated its daily fee limit in February 2009 and now permits unlimited overdraft fees per day.

Bank	OD Fee	Sustained OD Fee	Maximum Fees
Bank of America	$35	No	No max
BB&T	$35	$30 after 7 days	
Chase	$25 first OD $32 2 to 4 OD $35 5 or more	$12.50 after 5 days in AZ, $5 to $25 per day	No max
Citibank	$34	No	4 fees per day
Citizens Bank	$25 first OD $37 2nd OD day $39 3 or more	$35 per contract	
Fifth Third Bank	$25 first OD $33 2 to 4 OD $37 5 or more	$6/day after 3 days	No max
HSBC	$35	No	No max
National City Bank	$30 to $36	$8/day after 3 days	No max

[13] Joint Guidance on Overdraft Protection Programs, 70 Fed. Reg. 9,127, 9,129-30 (Feb. 24, 2005)

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 $33 2 to 3 OD $35 4 or more	No	No max
SunTrust	$35	$35 on 7th day	No max
TD Bank	$35	No	No max
U.S. Bank	$19 first OD $35 2 to 4 $37.50 5 or more	$8/day after 3 days	6 OD and 6 NSF up to $450/day
Wachovia	$22 first OD $35	No	No max
WaMu	1 free OD $34	No	7 OD or $238/day
Wells Fargo	$22 first OD $35	$5/day after 3 days	No max

Big Bank Overdraft Loans are Extremely Expensive

The combination of the initial overdraft fee and sustained overdraft fees charged within a few days of the incident make bank overdraft loans extremely expensive for consumers. Since sustained overdraft fees can be applied even before consumers know that their account is overdrawn, it is difficult for consumers to avoid these extra fees.

A $100 overdraft repaid after seven days would cost fees ranging from $34 at Citibank to $74 at Citizens Bank, using the highest fees charged by these banks plus sustained overdraft fees. The annual percentage rates if these loans were subject to TILA closed-end credit cost disclosure requirements range from 1,768 percent to 3,640 percent APR. By comparison, payday loans for 7 days usually cost 780 percent to 1,560 percent APR if the finance charge is $15 or $30 per $100 borrowed. (See chart below.)

In requiring banks to provide information on the cost of their overdraft programs for either opt in or opt out arrangements, the Board should require banks to include both initial and sustained overdraft fees in disclosing the total cost of representative overdrafts. Otherwise consumers cannot make an informed decision.

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 payday loan.

Bank	Max OD Fee	Sustained OD Fee Times # of Days	Total	APR/7 days
Bank of America	$35	0	$35	1,820%
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$6=$24	$61	3,172%
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	$35	$35	$70	3,640%
TD Bank	$35	0	$35	1,820%
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	4x$5=$20 CA	$55	2,860%

Transaction Clearing Practices

All of the largest banks maximize overdraft and insufficient funds fees by ordering the sequence of withdrawals to pay the largest transaction first or reserving the right to process withdrawals in any order the bank chooses. Since banks that cover overdrafts for a fee pay all or most transactions that overdraw an account, the only purpose to order payments largest first is to maximize fee revenue. This should be an unfair trade practice under the FTC Act authority of the Board.

Conclusion

We appreciate the opportunity to comment on proposed additions to Reg E to apply the Electronic Fund Transfer Act to single debit card transactions and ATM withdrawals involving unauthorized overdraft loans. We urge the Board to require banks to get their customers' affirmative consent to be enrolled in the banks' most expensive credit product. The Federal Reserve should repeal the obsolete provision of Reg Z which exempts banks from providing Truth in Lending Act disclosures as long as overdrafts are discretionary on the bank's part and cost the same as bounced checks. The low and moderate-income cash-strapped families who pay most overdraft loans need opt-in control over their accounts when transactions exceed the available balance. As banks increase their fees and drop limits on the total number of fees charged per day, consumers are at increasing risk from unauthorized overdraft loans.

Sincerely,

Jean Ann Fox
Director of Financial Services
Consumer Federation of America