October 5, 2006

Mr. Steve Hanft
Legal Division
Federal Deposit Insurance Corporation
550 17th St NW
Washington, DC 20429

Re: Request for Comment on Proposed Study of Overdraft Protection Programs

Dear Mr. Hanft:

The National Community Reinvestment Coalition (NCRC) is pleased to respond to your request for comment on overdraft protection programs. NCRC is a trade association of 600 community organizations promoting equal access to credit and capital to traditionally underserved populations in the US.

We commend the Federal Deposit Insurance Corporation (FDIC) for its proposed survey on the overdraft protection programs of the institutions that it regulates. We believe that the collection of this information is absolutely necessary for the FDIC to determine the safety and soundness of basic checking accounts and compliance with consumer protection laws.

Overdraft protection, which was originally intended as a courtesy service for bank customers to avoid the embarrassment of a bounced check, has transformed into a high-priced loan program similar to payday lending, with expensive fees serving effectively as an interest rate. For example, an overdraft of $100 paid back in two weeks with a fee of $20 amounts to an annual percentage rate (APR) of 520 percent on the money borrowed. The application of overdraft protection to other transactions, such as ATM withdrawals and debit card transactions increases the likelihood that consumers will overdraw and incur more fees. Overdraft protection is the source of enormous fee income for banks, most of it usurped from unsuspecting consumers. Existing surveys carried out by consumer groups show that the key features of many overdraft protection programs often are poorly disclosed, so that the customer has very little information about the product.

Given that this product is an extension of credit, rather than a routine feature of a checking account, we believe that the FDIC's survey will conclude that overdraft protection must be regulated *not* under the Truth in Saving Act (TISA) as is presently the case, but rather under the Truth in Lending Act (TILA), which would require that banks include the proper lending disclosures.

In response to the FDIC's request for ways to enhance the quality and utility of the data collected in the survey, NCRC respectfully submits our suggestions for data collection under three categories: implementation, disclosure, and marketing. This letter will conclude with recommendations for regulation of overdraft protection.

Implementation. Many banks engage in questionable practices that raise the likelihood and frequency of overdrafts. Chief among these, the FDIC should survey the proportion of banks that apply their programs to electronic transactions; that is, transactions made by automated teller machines (ATMs) and at point-of-sale (that is, through debit cards). Most institutions do not decline customers who attempt to overdraw through an electronic transaction, or otherwise notify the consumer at the time of the transaction that the amount of the transaction is greater than the funds available. Further, this subverts the original intent of overdraft protection: consumers do not face embarrassment or merchant fees when denied by an ATM transaction and during many point-of-sale transactions.

Second, some institutions have taken to displaying a "cash available" number on bank statements and ATMs. This number includes the sum of the account's current balance and the consumer's overdraft limit (typically between $100 and $900). Thus, the consumer is misled into supposing that the account has more funds than is actually the case. Data about the prevalence of this "cash available" phenomenon is lacking and must be investigated by the FDIC's survey.

Third, the FDIC must consider the order in which a bank clears checks and electronic transactions: whether it orders them from highest amount to lowest amount, lowest amount or highest amount, or in some other fashion. Many banks order checks from highest to lowest, claiming that a consumer's most important charges (such as mortgage, rent, and insurance) are cleared first. However, this method also has the effect of increasing the number of transactions that bounce, thus increasing the bank's fee income.

Fourth, the FDIC should inquire if the bank purchases overdraft protection software from one of many third-party consultants. These consultants provide overdraft protection software to mid-size banks, as well as technical support. However, these vendors solicit business from banks by advertising that their overdraft protection services are a method for boosting fee income, as seen in their advertisements in bank trade magazines and on the internet.

Fifth, information is unclear on whether banks automatically apply overdraft protection or if the program is discretionary on the part of the bank. Oftentimes banks' advertisements all but assure consumers that the program will reliably apply to all transactions, yet in checking account booklets the bank often asserts that the program is discretionary. The FDIC should inquire into the specifics of how banks apply the product, and whether banks are making proper disclosures in compliance with consumer protection laws.

Last, the FDIC must consider how many institutions deny overdraft protection to repeat users. A study by East Carolina University economist Marc Fusaro discovered that the depositors who most often face these fees are the lowest income and youngest consumers in his sample. No data exist on how banks treat repeat users of overdraft protection, and whether banks have clear and fair procedures for terminating the program.

Marketing. Using data from recent surveys of large banks' programs, the marketing of overdraft protection falls into two categories: first, banks that encourage the use of overdraft protection as a short-term loan program rather than a final attempt to avoid a negative balance; and second, banks that make information on the product scarce, so that the consumer doesn't realize its deleterious effects until after (s)he has used it. Both of these are questionable practices.

In regard to banks whose marketing encourages overdrafts, the FDIC should survey language in advertisements and other materials that encourage consumers to overdraw their accounts. For example, a survey conducted by the Consumer Federation of America found these examples of such language: "Have you ever had unplanned expenses between paydays? There is no need to worry! With [our] Powerdraft Plan, you will be covered without the embarrassment of a returned check!" Another states: "Did that last check catch you off-guard? Don't worry, we've got you covered."

In regard to banks that poorly disclose information about their overdraft protection programs, the FDIC should question how the program is disclosed. A survey by the Woodstock Institute in 2004 showed that this information is often difficult for the consumer to understand. That is, mention of the program might be in one section of the checking account's disclosure booklet, and mention of the fees may be in another. Further, many banks implement a sustained overdraft system that is especially difficult to understand. For example, one institution in the Woodstock survey assesses a $33 fee at the time of the overdraft; then, when the account remains overdrawn for five consecutive banking days, a fee is assessed on the sixth day and then every four days thereafter as long as the account remains overdrawn.

Disclosure. Much of the above discussion has focused on how clearly the bank discloses the finer points of overdraft protection. Past surveys have shown that the features of overdraft protection are often unclear or missing from banks' disclosure booklets, violating the letter and spirit of consumer protection statutes. Further, some disclosures use vague or nonspecific language when mentioning their overdraft protection terms. Specifically, the FDIC should survey how clearly the following points are explained:

- **Application:** Are all types of checking accounts at a given institution eligible for overdraft protection? Does a consumer need to opt-in to the program? Does a consumer have the right to opt-out of the program?

- **Types of Transactions Covered:** As discussed above, what types of transactions are covered by overdraft protection? Does it apply to paper checks, ATM transactions, and POS transactions?

- **Alternative Overdraft Protection Programs:** Are consumers made aware of alternatives to overdraft protection, such a link to a savings account, a credit card account, or a line of credit?

- **Overdraft Limit:** Does the bank establish a limit? Does it increase or decrease upon certain criteria?

- **Order of Payments:** As discussed earlier, how well does the bank disclose how it processes payments – from highest to lowest amount, lowest to highest amount, or by some other method?

- **Notification of Overdraft:** How, if it all, does a bank notify a customer of an overdraft? Is it done by mail, email or phone? After how many days does it send notification? Does the bank then reiterate clearly how its overdraft program works?

- **Fee Schedule:** Does the bank have an initial charge for each overdraft, as well as a sustained charge if the account remains overdrawn? Further, does the bank add an additional surcharge for an account that has a history of overdrafts? In addition, does the bank charge a different amount to pay for a check, ATM transaction, or POS transaction?

Recommendations for Regulation. As the FDIC and other federal bank regulators have stated in the past, when an overdraft is paid, credit is extended. That is, overdraft protection constitutes credit, and the banks that offer it are creditors. We predict that, after the FDIC has conducted this survey, it will conclude that the product is more appropriately regulated under the Truth in Lending Act (TILA, 12 CFR § 226.5), rather than the Truth in Saving Act (TISA) as is presently the case. Coverage under TILA would require banks to state certain aspects of the program in a clear and conspicuous manner that TILA sets forth, including the APR of the product. If the FDIC deems coverage under TILA to be difficult, it ought to require a standardardized disclosure of some kind. Under current regulation, banks have made it exceedingly difficult for consumers to understand the product they are using, and furthermore make cost-shopping among institutions' accounts very difficult.

While NCRC is not opposed to overdraft protection, we feel that certain disclosures must be made clear so that consumers can understand the products they use. Again, NCRC applauds the FDIC on its proposed survey and hopes that the FDIC uses the survey to carefully and comprehensively assess overdraft protection programs. Thank you for your consideration on this matter. Please do not hesitate to contact myself or NCRC Research Analyst Tim Westrich at 202-628-8866 for more information.

Sincerely,

John Taylor
President and CEO