THE OVERDRAFT PROTECTION ACT OF 2009

HEARING

BEFORE THE

COMMITTEE ON FINANCIAL SERVICES

U.S. HOUSE OF REPRESENTATIVES

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THE OVERDRAFT PROTECTION ACT OF 2009

Friday, October 30, 2009

U.S. HOUSE OF REPRESENTATIVES,
COMMITTEE ON FINANCIAL SERVICES,
Washington, D.C.

The committee met, pursuant to notice, at 9:41 a.m., in room 2128, Rayburn House Office Building, Hon. Barney Frank [chairman of the committee] presiding.

Members present: Representatives Frank, Maloney, Green, Cleaver, Ellison, Perlmutter, Himes; Bachus, Royce, and Posey.

The CHAIRMAN. There is a very plausible reason that I am late: I am getting forgetful. And I am sorry. I got engrossed in something else. I apologize.

You honor us by coming here on a Friday. I feel badly and I am sorry.

We will begin with our opening statements. We will have 10 minutes on each side. And I recognize the gentlewoman from New York, Mrs. Maloney, the main author of this legislation, and so many other consumer protections, for 5 minutes.

Mrs. MALONEY. Thank you so much, Mr. Chairman, for your support and leadership on this important issue. And thank you for having this hearing on H.R. 3904, the Overdraft Protection Act of 2009.

The overdraft problem is significant and getting worse because the quantity of debit card transactions now exceeds the quantity of credit card transactions. Just yesterday, a headline in the American Banker Newspaper read, "Dependence on debit is the new norm."

The Center for Responsible Lending has found that overdraft fees have increased 35 percent in the last 2 years, and they estimate that 27 million Americans overdrew their checking account more than 5 times in a 12-month period.

From start to finish, the consumer is too often kept in the dark, not allowed to choose how he or she spends their own money. This bill brings sunshine and permission into the process, restricting deceptive practices and empowering consumers to manage their own lives and their own financial accounts.

Let me briefly explain the overdraft cycle. As a consumer opens an account, according to a study by the FDIC, most banks, 75 percent of banks, automatically enroll them in an automated overdraft program which charges a fee from $10 to $38 for each overdraft and, sometimes, another fee if an account stays at a negative balance, even though the consumer does not even know it is in a negative balance.

So what this bill does is give consumers more tools to better make their own decisions about how to manage their own money. Then, consumers begin to use their debit card just as they have advertised: for groceries, for gas, for a cup of coffee and movie tickets, to run a Sunday's worth of errands, and many people use their debit card at a point of sale half a dozen times or more. And because they were enrolled automatically in overdraft protection and are using ATMs or point-of-sale terminals, they don't or cannot tell if a transaction is about to drive them into a negative balance and they incur a fee.

Consumers often do not know that they have even incurred overdraft fees until they get the bills, sometimes as much as $300 to $600 for overdraft fees for one weekend.

What the consumer does not know, unless they keep very strict track of their balance after each and every transaction, is that they could have racked up half a dozen or more overdraft fees in just a single day. So that $5 cup of coffee, an extravagance in its own right, then turns into a $35 cup of coffee because of the overdraft fee.

What is more, the consumer does not find out about the fee that was automatically charged until later, because the overwhelming majority of banks, 81 percent according to the FDIC, will allow an overdraft to occur at an ATM or point of sale but only notify the consumer after the transaction has been completed and the overdraft fee has been charged.

Finally, the overdraft problem culminates when the transactions are posted to accounts back at the bank. You might think that the transactions would be posted in chronological order, but you would be wrong. They are usually posted by size, from the largest amount spent to the smallest, driving people into overdraft fees quicker, which means that the transaction fee has the effect of driving the account into a negative balance faster, and each smaller transaction that occurs while the account is in a negative balance incurs a new, separate overdraft fee.

The FDIC study reports that 53.7 percent of large banks process overdraft fees in large-to-small fashion, therefore driving up the cost to the individual.

The bill that Chairman Frank and Chairwoman Waters and I have introduced meets the overdraft problem head on from start to finish. First, this is a bipartisan effort; Walter Jones joined us in the introduction of this bill—it brings automated overdraft plans under the Truth in Lending Act, requiring financial institutions to obtain permission of consumers before enrolling them in the overdraft program.

It requires that ATMs notify the consumer if the cash withdrawal would incur an overdraft fee, and allows the consumer to reject the withdrawal before the fee is incurred, thereby giving the consumer more control over their own finances. It limits overdrafts at the source, the financial institution, to no more than 1 per month or 6 per year. It prohibits the manipulation—

The CHAIRMAN. The gentlewoman is recognized for an additional minute.

Mrs. MALONEY. Oh, my goodness.

I feel strongly about this. Let me just say that it requires that overdraft fees be proportional to actual harm, so that a $5 cup of coffee isn't charged what amounts to a 700 percent interest rate in the form of a $35 fee.

And I want to applaud the efforts of some of the large banks that have worked to address this problem by voluntarily limiting the fees. But we feel that overdraft protections must be extended to all customers of all financial institutions. Even some of the banks which have dialed back overdrafts still permit up to 4 overdrafts per day.

As the FDIC study has shown, the problem is so wide and so deep, encompassing the majority of banks and affecting tens of millions of consumers, Congress must address this problem across-the-board systemically.

The bill is the largest—my latest version of my legislation on this issue; I have introduced it in several other Congresses. And I thank the chairman for sponsoring it and for having this hearing.

I also want to welcome all of the witnesses. I believe this is the largest panel in the history of the Banking Committee—the Financial Services Committee, showing the deep concern and attention, so I thank you all for being here.

The CHAIRMAN. I thank the gentlewoman.

I appreciate—I thought it was best to do it this way, there being a small number of members. I will say we had originally contemplated our being in session today, but I don't mind that because I think we will be able to focus with the small amount of members.

But if we have unanimous consent—I have checked with the ranking member—each member will have 10 minutes rather than 5 to question, to accommodate. There aren't that many people here, so that way we will be able to accommodate that; and we will have a 10-minute question period—I am afraid we can't get used to that, given the size of this committee—and we might even be able to do a second round. So I do want to take up for that.

And the gentleman from Alabama is now recognized for 10 minutes.

Mr. BACHUS. Thank you, Mr. Chairman.

I will just touch on some brief thoughts. I am interested in hearing from the panel, because this is obviously an issue that I think all of us are interested in.

As far as an alternative, if you don't have overdraft fees, what do you have? And what I have is a line of credit, and I think that is a far wiser and sounder money management tool. And I am not sure; I think one approach would be if the banks—and I think with the financial literacy, if we said to people there is a better alternative than overdraft fees.

I would be interested in you—maybe either in the questions or addressing why aren't there more lines of credit or are people not aware of that.

I will say, one other alternative to overdraft fees is not a good alternative, and that is issuing a worthless check charge, which is a criminal charge. When I started practicing law in the mid-1970's, you had to take a certain number of appointed cases, and about a third of the docket in criminal court were people issuing worthless checks. You would go to a municipal court and you would find that was sort of the predominant charge. There were just people even in small towns who for one reason or another wrote a bad check. And I don't think any of us want to return to that.

The fees, I think all bank fees, we all know that over the past 10 years those fees have—all fees have either doubled or tripled. I think that is pretty much a given. And maybe that is not true. I would like to hear if I am wrong about that.

And the other thing about the overdraft fees is they are all $35. I think that seems to be the general charge. And every time the fee at every bank is $35, you wonder why that is. And maybe that is close to the cost.

The ATM or point—either a debit card when you go in a grocery store, it is my understanding from some of the banks that you have a problem at that point telling people that they are overdrafting. I am certainly interested in that. Obviously, if you could tell them, I think it would be a good thing.

Now, at the ATM machines it is also my impression that you can tell them there. And I really can't see anything wrong with a requirement that you tell them that they are overdrafting when they use their ATM card. But I think some of the smaller banks may have more difficulty, or the credit unions, with this because of technology.

And the last thing I would ask is, how do we address this? The banks that are making money today are the old investment banks. They are making money trading, they are making money speculating, which can be a dangerous thing.

The commercial banks are losing money. They may have a good quarter, but they are apparently not making a lot of money on lending even though the cost of money from the Fed is awfully cheap.

But if they are losing money, where do they make that up? And that is—so the timing of all this is a challenge, particularly when so many of our banks are losing money. Yes, they may be charging $35, and we may think that is too much, but we don't want to put all our banks out of business.

So, Mr. Chairman, I do appreciate you having this hearing, and I look forward to hearing from the witnesses. And I personally am more in just a listening mode and would be interested in your comments.

But I want to go right back to what I started with, and that is that I still remember in the late 1970's when I would be representing somebody on an appointed case, and they would have all these bad checks and a lot of times they would actually be in jail. And I don't think you see any of that, I don't think you see that like you used to. Now, I could be wrong. I would be interested in if some of the consumer groups, particularly whether you have sort of taken a look at that, and whether one unintended consequence of not having some safety net would result in people going to jail.

And particularly college kids who can't seem to—many of them can't seem to manage their money; you certainly don't want a criminal record, and issuing a worthless check is a criminal record, which actually in many cases would disqualify them from jobs. So $35 fees are one thing; a charge that disqualifies you from an occupation is a much more serious alternative.

So, with that, thank you, Mr. Chairman.

I thank the witnesses.

The CHAIRMAN. I just want to announce there had been some discussion of scheduling a markup of this bill on Tuesday. That will not happen now because we have the New York, Virginia, and New Jersey elections on Tuesday, and those are all within easy commuting distance of here, so a number of the members from the committee will be working that day. And the gentlewoman from New York, in particular, is very important obviously to this bill.

So we will not be marking this bill up next week, which means we won't be marking it up, people for their own calendars should know, for at least a couple of weeks, because the week after it being Veterans Day coming in the middle of the week, we are very unlikely to be in.

So we will proceed.

I will just recognize myself for a brief comment, which is, I would urge my friends in the Banking Committee—we wouldn't, I believe, be in a situation where we are talking about legislation if you would have had an opt-in regime from the beginning. I guess I would make it a general rule that I have learned in politics: Don't do people favors without asking them.

Early on in my career as a Member of Congress, I received a phone call from a woman who said her daughter was about to be married—this is a true story—and her husband-to-be was in the military, and he was about to be shipped out, and could I get that date postponed so that the wedding could take place before he was shipped out.

And being new at this, I tried to do that, whereupon I got a phone call from the groom-to-be that said, "Mind your own business; don't do me a favor without asking me." I would urge that on you.

I have to say, I am skeptical. People say, oh, we have to give them this overdraft without asking them. It is in their interest. That is another I have had as a Member of Congress. When people come to me to argue for something that benefits them, which is entirely legitimate, that is what people ought to be doing, we need to know how what we do affects people.

But when we go to the next step and say, this is not only good for me, this is good for the people who will be paying me to do it, my answer is now invariably, when they come and tell me that, I will believe that. But unless you have a signed proxy form in which you are empowered to tell me that it would be a good thing for them to pay you, I am skeptical.

So I really urge you to do this a lot. And part of it is it is human nature. It is not simply a question of how much money it is. It is indignation. It is the sense that people's integrity and autonomy has been impaired when you do this to them and then tell them you did it for them.

So I would just urge you on all of this, have an opt-in, have it in clear language.

I continue to get two types of mail from banks: solicitations to do things that will bring them money in very large type; and explanations of conditions that apply to things I do in very much smaller type. It is a very old joke and a very bad one.

So you can save yourselves a lot of problems by that, and I would encourage you to do that going forward.

With that, we will begin with the witnesses. And, as I said, we will have 10 minutes to question. I do have one preliminary question for Mr. Menzies, whom we welcome back, having been here yesterday.

Who is running the bank, Mr. Menzies? We have you down here all week.

Mr. MENZIES. Thank you, Mr. Chairman. We have a very strong little community bank.

The CHAIRMAN. We appreciate you. You have been a good witness, and we are glad to have you freed up for that.

Let's begin with Ms. Fox.

STATEMENT OF JEAN ANN FOX, DIRECTOR OF FINANCIAL SERVICES, CONSUMER FEDERATION OF AMERICA (CFA)

Ms. FOX. Thank you, Mr. Chairman, Ranking Member Bachus, and members of the committee. I am Jean Ann Fox, director of financial services for the Consumer Federation of America. I am testifying today on behalf of the national consumer groups listed on my testimony. We are here to express enthusiastic support for Representative Maloney's H.R. 3904, the Overdraft Protection Act of 2009.

Banks extend credit when they cover an overdraft and then charge a fee. Instead of denying a debit purchase, banks are permitting it to go through and then are charging about $35 for each occurrence. Banks pay overdrafts on paper checks, on point-of-sale debit purchases, ATM withdrawals, automated clearinghouse transactions to pay bills. And due to Federal Reserve action on this, consumers are not protected under the Truth in Lending Act.

These are very small loans. The FDIC study says that the typical debit card purchase is just $20, so consumers are paying $35 to borrow $20 for just a few days. The largest of overdrafts is just $78 for an ACH payment.

So these are very small loans, and they are very expensive. In our most recent look at the largest banks' overdraft fees practices, the top fee was $39 for the initial overdraft, the lowest was $34. The typical fee is $35. Ten of the largest banks charge a second fee if consumers don't pay the overdraft back in as little as 3 days.

The sustained overdraft fees are either one-time fees—for example, Bank of America started this June charging a second $35 fee if the overdraft was not repaid in 5 business days. Some banks charge $8 a day after a few days if the overdraft has not been repaid. This makes a single mistake, a single overdraft, turn into a financial disaster for consumers.

These are very short-term loans. The bank takes payment out of the next deposit into your bank account to repay your loan if you haven't come down with cash to pay them off right away. And, as Representative Maloney noted, consumers do not affirmatively sign up for this program. This is the only form of involuntary credit that we know of that is so widespread.

And, of course, the largest banks process payments large to small, or reserve the right to do that, which means that if they don't process payments out of your account as they come in, they wait a couple of days to have lots of little debits and one pretty good-sized check. You can wipe out the balance very quickly and then charge people a fee for each one of the smaller payments that overdraw.

This is not what consumers want to have happen.

CFA commissioned a poll by ORCI this past July and asked what consumers thought banks should be doing: 71 percent support that banks should get permission before they pay an overdraft; 85 percent say that banks should be required to disclose on the ATM screen that a withdrawal will overdraw the account and trigger a fee; 70 percent say that banks should be required to pay checks in the order they receive them; and 53 percent strongly support that position.

Your bill meets what consumers want to have happen.

And the folks who are harmed by this are the folks who can least afford to pay the highest cost for overdraft coverage of any bank products. These are low-income consumers, these are young people, these are folks who are renters and likely to be single.

In the polls that we did this summer, twice as many people who said they paid for an overdraft were African American, compared to the sample as a whole.

So this impacts a fraction of bank customers. According to the FDIC study, about a fourth of Americans are paying this $24-billion-a-year tab for credit they did not request, did not know they had, or were unable to make informed decisions.

Your bill adds protections that consumers need.

In addition to consent, which should be a given—that consumers should give consent to be able to borrow from their banks, the other protections help keep overdrafts from becoming a debt trap for unwary consumers—banks would have to comply with Truth in Lending and treat this fee as a finance charge.

There would be a ban on manipulating the order of processing payments. Banks have a lot of different tactics that result in more fees, and they are instructed to use those in order to maximize income.

Your bill provides a cap on fees so that a bank can't charge more than once a month if they have covered an overdraft, with a limit of 6 per year. This implements the safety and soundness guidelines that the FDIC provided a few years ago when banks were making a similar type of very short-term, very high-cost credit to consumers.

Thank you, Mr. Chairman.

[The prepared statement of Ms. Fox can be found on page 114 of the appendix.]

The CHAIRMAN. Our next witness is Nessa Feddis, who is vice president and senior counsel of the Center for Regulatory Compliance, American Bankers Association.

STATEMENT OF NESSA FEDDIS, VICE PRESIDENT AND SENIOR COUNSEL, CENTER FOR REGULATORY COMPLIANCE, AMERICAN BANKERS ASSOCIATION (ABA)

Ms. FEDDIS. Thank you, Chairman Frank, Ranking Member Bachus. My name is Nessa Feddis, and I appreciate the opportunity to testify on behalf of the American Bankers Association.

Americans enjoy the most affordable, accessible banking system of any country in the world. They have access to full service checking accounts at little or no cost.

Now, in the best of all worlds, people would only make payments when they have money in their accounts to cover the transaction. But this isn't a perfect world. When inadvertent overdrafts occur, most consumers value institutions paying their overdrafts, and they have come to expect it. Indeed, 96 percent of consumers who had an overdraft paid were glad that it had been paid.

Similar studies by the Federal Reserve found most participants expect and value coverage. Payment rejection means embarrassment, inconvenience, merchant fees, and other adverse consequences. Rejection means payment recipients refusing their checks or electronic payments in the future, or having negative information put into a credit report.

Customers also often want their debit card transactions to go through, whether it is for groceries already selected and bagged, a meal already eaten, emergency purchases, or a bill they want to pay through a debit card.

Overdraft fees are easy to avoid, and most consumers avoid them. In fact, in a survey of 1,000 bank customers, 82 percent said they hadn't paid one in the past 12 months.

For customers who find it challenging to manage their accounts and avoid overdraft, there are many options available, including keeping a little extra money in the account or linking their account to a savings account or a line of credit. And, as the FDIC found, most institutions permit customers to decline overdraft services.

ABA is very concerned about the potential unintended consequences of H.R. 3904. It presents significant challenges for all banks and will mean a complete redesign of checking account features and pricing. The result would be more hassle and cost for customers who find payments returned or rejected and will have significant unintended consequences on the availability of services and cost to all checking account customers.

For example, the bill limits overdraft fees to those that are reasonable and proportional to the cost of processing the transaction. Such an approach misses critical elements of the pricing.

First, the cost of pricing ignores the deterrent value of overdrafts. Just like a parking or speeding ticket, overdrafts are meant to be a deterrent. Like any penalty, they are designed to get the person's attention in a way that a nominal fee does not.

Second, the cost of processing does not reflect the risk of loss nor the lost income earned from balances which help pay for the cost of providing the account. This lost income makes it more expensive to offer accounts and means that those who manage their accounts well absorb those costs in the form of higher fees.

Another provision which limits monthly and yearly overdrafts limits consumer choice by prohibiting overdrafts they want paid from being paid. Banks would reject overdraft transactions once the maximum fee has been met or just reject all. This means consumers suffer the consequences discussed earlier: the hassle, inconvenience, cost and embarrassment of rejected items, the very reasons that consumer testing has found people value and want this service. Such artificial limitations would lead to significant unintended consequences. As history has shown, government price fixing does not work and ends up hurting the people it is intended to help.

H.R. 3904 also appears to require an APR calculation. As explained in greater detail in my written testimony and as government testing supports, calculating an APR for overdrafts would mislead and confuse consumers. The shorter the repayment period, the greater the APR will appear in instances involving a fixed fee. This means that the sooner the consumer repays, the greater the APR—a difficult concept to explain as it appears that paying earlier increases the cost and it is better to delay repayment; or the greater the overdraft, the less costly it is because, of course, the APR is going to be lower.

In summary, ABA believes that overdraft protection services provide a valuable service. The bill will mean a complete redesign of checking accounts, more hassle and costs for customers who find payments rejected, less access to checking account services for some, and higher prices. Because of these and other unintended consequences, ABA opposes the bill in its current form.

We are ready to work with this committee to address ways to improve the bill. Thank you.

[The prepared statement of Ms. Feddis can be found on page 105 of the appendix.]

The CHAIRMAN. Next, Mr. Eric Halperin, who is the director of the Washington office of the Center for Responsible Lending.

STATEMENT OF ERIC HALPERIN, DIRECTOR, WASHINGTON OFFICE, CENTER FOR RESPONSIBLE LENDING

Mr. HALPERIN. Good morning, Chairman Frank, Ranking Member Bachus, and other members of the committee. Thank you for inviting me to testify on H.R. 3904, the Overdraft Protection Act of 2009. The Center for Responsible Lending enthusiastically supports this bill as it will provide important protections for consumers from abusive overdraft fees.

The Center for Responsible Lending is a nonprofit research and policy organization dedicated to protecting family wealth. We also are affiliated with Self-Help, which is a nonprofit loan fund and a credit union. Self-Help does not charge overdraft fees and routinely denies debit card and ATM transactions that would overdraw the account for no fee.

In the midst of a recession, abusive overdraft practices are making the dire financial situation of families even worse. Banks are making loans that consumers never asked for at astronomical prices. In 2008, consumers paid nearly $24 billion in overdraft fees. This represented a 35 percent increase over the number of fees paid in 2006 and is now more than consumers spend on many basic household staples.

The effect of overdraft fees is widespread. An estimated 50 million people will overdraft their account at least once each year, and 27 million people will overdraw their account at least 5 times each year.

To understand the growth of overdraft fees over the last 5 years, it is important to understand the growth of debit card transactions which were key to this increase. Debit card transactions now account for nearly 50 percent of all transactions that trigger an overdraft, and they are growing every year as debit card transactions become more common.

Checks, on the other hand, account for only about a quarter of all transactions that lead to an overdraft. And the number of checks written each year is shrinking, especially among the younger demographic.

Debit card overdrafts are particularly indefensible because financial institutions could deny those transactions without charging their customers a fee. And this is, in fact, what most financial institutions did just 5 years ago. In 2004, 80 percent of financial institutions routinely denied transactions that would overdraw the account that originated through a debit card. The FDIC found that in 2008, 81 percent of institutions now routinely approve those transactions.

Debit card overdrafts are also more likely to be small-dollar transactions. On the average, a debit card overdraft results in a $17 loan, the average fee paid is $34, and that loan is paid back in 3 days. You pay your bank $34 to loan you $17 for 3 days. It is an expensive and unsustainable way to get credit.

When the debit card first came onto the market, we told consumers that this was an excellent tool to manage your finances; it is a way to make your purchases without going into debt on a credit card. But because of the widespread prevalence of debit card overdraft programs, we have turned that debit card into the most expensive credit card on the market although it lacks the basic consumer protections that we have for a credit card.

Debit card transactions drive overdraft fees in every demographic including those consumers 55 and older. It is the leading cause of overdrafts for those consumers. People 55 and over, on all types of transactions, paid $6.2 billion in overdraft fees. But, most importantly, $1.4 billion in overdraft fees is paid by seniors who are heavily dependent on Social Security for their income. People who worked hard their entire lives and paid into the system are seeing $1.5 billion taken out of their Social Security check by their financial institutions.

Overdraft programs are structured to encourage rather than discourage use. Their high fees and short repayment time often trigger a debt cycle for people who overdraft repeatedly, where overdraft fees simply beget more overdraft fees, because once the fees and the loan amounts are taken out of their check, they are left with less money to make it to the next payday.

H.R. 3904 contains important protections that go beyond the baseline of consent that you must consent to participate in the credit program. Reasonable and proportional fees will ensure that we will not have any more $35 fees for $5 overdrafts.

The six overdraft limit, as Ms. Fox testified, is analogous to what the FDIC did in the payday lending context where they determined that providing high-cost, short-term credit for long-term credit needs is an unsafe and unsound banking practice.

Certainly, we have learned over the last several years that providing high-cost, unsustainable credit is not just bad for consumers; it is bad for the financial institutions and bad for our economy in general.

Both a reasonable, proportional requirement and the limit have precedent in the CARD Act, recently passed by this committee, where we provided protections to credit card recipients.

At their best, banks and credit unions provide Americans valuable services and access to credit on fair and appropriate terms. We want to encourage people to enter the banking system, but they need to have confidence that those accounts are safe. The Overdraft Protection Act will ensure fair and transparent pricing for overdraft coverage and save Americans billions of dollars that is currently being taken from their hard-earned paychecks.

Thank you. I look forward to your questions.

[The prepared statement of Mr. Halperin can be found on page 136 of the appendix.]

Mrs. MALONEY. [presiding] Thank you very much.

Next, Mr. Rod Staatz, president and chief executive officer of the SECU Credit Union in Maryland; and he is speaking on behalf of the Credit Union National Association.

Welcome.

STATEMENT OF RODNEY STAATZ, PRESIDENT AND CHIEF EXECUTIVE OFFICER, STATE EMPLOYEES CREDIT UNION OF MARYLAND (SECU), ON BEHALF OF THE CREDIT UNION NATIONAL ASSOCIATION (CUNA)

Mr. STAATZ. Thank you. Madam Chairwoman, Ranking Member Bachus, and members of the committee, thank you very much for having me today. As you said, I am Rod Staatz, president and CEO of State Employees Credit Union of Maryland. I am also a member of CUNA's board of directors.

CUNA strongly supports the ability of credit unions to offer overdraft protection plans as a means to help their members resolve short-term financial problems. While the terms of the credit union overdraft protection programs may vary, they are structured to help pay rather than return nonsufficient funds transactions in exchange for fees that are similar to those charged for returned items. This spares the members the embarrassment of returned checks as well as additional fees charged by merchants.

Such programs, when used appropriately by consumers, serve as a valuable alternative to overdrawing checking accounts or relying on payday lenders or check cashing businesses and are fully consistent with the philosophy and principles of the credit union system.

CUNA recognizes there is a considerable interest in Congress in enacting a law to address abusive practices. However, we are convinced that H.R. 3904, as drafted, particularly the provisions that limit the number of overdraft fees, would simply end these programs.

If the bill were law, consumers would incur more NSF fees and none of the benefits of having the transactions honored. They would pay more merchant return check fees and have more bad checks reported to credit bureaus. Inevitably, other adjustments will have to be made in checking account services and maintenance fees that will impact a wide range of account holders.

I am very concerned that all consumers will lose under this scenario. We believe most credit unions approach overdraft protection in a manner that is in the best interest of the participating member as well as the overall membership of the credit union.

Several years ago, CUNA adopted a policy calling on credit unions offering overdraft protection service to adopt standards that emphasize the credit unions' consumer orientation. This policy is included in my written testimony.

Madam Chairwoman, my credit union offers an overdraft protection service which is similar to overdraft protection programs used by credit unions throughout the country. The objective of this program is to permit members on an occasional basis to have transactions completed even when they temporarily lack sufficient funds in their checking accounts or to spare them from merchant and collection agency fees incurred for return checks.

A member can prearrange to have funds drawn from a selected savings account or establish a line of credit. And if he or she writes a check without enough funds in his checking account, the necessary funds are withdrawn from the other account or line of credit.

There is no fee—zero—for these transfers. Our overdraft program allows SECU to pay an item after all funds in a member's accounts have been exhausted or a prearrangement transfer plan has not been established.

However, SECU does not allow members to draw their balance into the negative at the teller line, through ATMs, or through their debit card. Our program only pertains to written checks and preapproved ACH transactions.

The member's checking account is debited in the amount of the overdraft plus a $27 fee. The member is sent a nonsufficient funds notice explaining the account is negative and a deposit is required to bring the account into a positive status. If the account is not positive within 30 days, all future items will be returned NSF with the $27 fee.

SECU does not market overdraft protection because we do not want to encourage members to live beyond their means. Knowing this is an option to cover overdrafts may lead some members to view it as available funds.

If a specific member contacts SECU for a refund, we review the account and consider the specific circumstances. Also, we refer many of our customers to free counseling services. Those members who demonstrate repeated overdraft behavior will have progressive notification from warnings to account closure for overuse. In 2008, we had to close almost 500 checking accounts for overuse and abuse of the overdraft privilege.

While we strongly agree overdraft abuses should be addressed, H.R. 3904 will have a dire unintended consequence which will result in harming consumers.

As addressed in my written statement, some of the provisions of the legislation are positive and we would welcome the opportunity to work with you on them. We also think that the Federal regulatory system, which allows for a notice and comment process, should play a leading role to protect consumers from unintended consequences of Federal restrictions on overdraft programs.

In addition to our strong objection to the limits on overdraft transactions that this legislation would impose, we have several additional concerns regarding the bill, which are described in my written testimony.

Madam Chairwoman, you will hear horror stories about how bad overdraft protection is, and you will also hear many heartwarming stories about how it has helped many credit union members. I encourage you to do an independent, unbiased survey of consumers. Go to the people who are really affected by this and ask them what they really think about overdraft protection.

Thank you for the opportunity to testify today, and I look forward to answering any of the committee's questions.

[The prepared statement of Mr. Staatz can be found on page 176 of the appendix.]

Mrs. MALONEY. Thank you very much.

Next, Mr. Oliver Ireland, who is a partner at Morrison & Foerster.

Thank you for being here.

STATEMENT OF OLIVER I. IRELAND, PARTNER, MORRISON & FOERSTER LLP

Mr. IRELAND. Thank you, Madam Chairwoman, Ranking Member Bachus, and members of the committee. I am a partner in the financial services practice of Morrison & Foerster, and I worked for the Federal Reserve System for 26 years, 15 as Associate General Counsel of the Board in Washington. I am pleased to be here today to discuss H.R. 3904 concerning paying of overdraft fees.

While paying overdrafts enables consumers to meet unexpected expenses and avoid failing to make timely payments, overdraft programs have been criticized as costly and unfair, particularly for small debit card transactions. H.R. 3904 would amend the Truth in Lending Act to require that consumers opt-in to overdraft programs, limit overdraft fees to 1 per month and 6 per year, require that overdraft fees relate to the actual cost of processing the overdraft, prohibit charges for ATM and debit card transactions that are declined, and regulate the order in which transactions are paid.

The Federal Reserve Board has proposed to address overdrafts at ATM and debit card transactions, but H.R. 3904 would go well beyond the Board's proposal.

Applying the Truth in Lending Act to overdrafts is likely to be confusing to consumers, however. When checks result in an overdraft, the consumer would have Truth in Lending billing error rights and UCC rights; but when the check didn't result in an overdraft, only the UCC would apply. A similar problem would occur for debit card transactions.

In addition, it is not clear how the Truth in Lending Act disclosures would apply before an overdraft, and disclosing an annual percentage rate after an overdraft would be similar to the historical annual percentage rate that has been eliminated for credit cards because consumer testing found that it was not effective.

H.R. 3904 applies the opt-in and the limitation on fees to check and ACH transactions as well as ATM and debit card transactions. The limitations on fees should not apply to check and ACH transactions. Businesses receiving these transactions typically charge significant fees for returned checks and ACH transactions that, when added to the NSF fees, lead to costs that significantly exceed overdraft fees. In addition, failure to make bill payments on time due to a returned transaction may lead to other costs or the inability to obtain some services.

H.R. 3904 would prohibit overdraft fees due to debit holds. This practice has been an issue with respect to pay-at-the-pump gas station transactions. Although there has been progress in addressing debit holds such as the VISA real-time clearing program, if fees for overdrafts due to debit holds are prohibited, merchants should have a duty to submit transactions promptly to help avoid these overdrafts.

H.R. 3904 would require overdraft fees be reasonable and proportional to the cost of processing the transaction. Overdraft fees should be reasonable if the consumer has chosen to opt-into them, I would think, and in any event should reflect the credit risk inherent in these transactions as well as the processing costs.

In addition, the limitation on fees in H.R. 3904 may prevent the payment of overdrafts that some consumers want paid. At a minimum, a limit should not apply to ATM transactions where the consumer proceeds with the transaction after the notice that the transaction will cause an overdraft.

Finally, overdraft fees are an important source of revenue to both large and small banks and credit unions. Loss of overdraft revenue is likely to lead to the repricing of checking account services in the form of lower interest rates, more and higher account maintenance fees, and perhaps even per-transaction fees. In addition, consumers will need to manage their account balances more carefully and perhaps maintain higher balances to avoid timing errors.

Thank you for the opportunity to be here today. I would be happy to address any questions that members of the committee may have.

[The prepared statement of Mr. Ireland can be found on page 158 of the appendix.]

Mrs. MALONEY. Thank you for your testimony.

Our next witness is Mr. Jim Blaine, president of the North Carolina State Employees Credit Union.

STATEMENT OF JIM BLAINE, PRESIDENT, NORTH CAROLINA STATE EMPLOYEES CREDIT UNION

Mr. BLAINE. Thank you, Madam Chairwoman. I appreciate the opportunity to testify today. I will not use your valuable time to read the testimony already submitted, but I would like to make a few brief comments about the need and importance of this bill and several of its provisions.

As to the need for limits and the potential for abuse, personally I believe the overdraft protection service, such as Courtesy Pay, should be entirely banned, not because this service does not do some good, but because I am convinced the harm caused by the product far exceeds any good achieved.

Having said that, this bill offers a compromise which seeks to retain the good of overdraft while controlling for that potential abuse. I would note that all members of this panel in their testimony acknowledged that abuse does exist in this product. This is why limits and proportional costs are so important in this regulation.

As to opt-in, since this august panel has great difficulty in agreeing on just what this product is—disagrees on its definitions, disagrees on its impact, and disagrees on the best course forward, since this experienced professional panel cannot agree—we can all hopefully agree that it is very, very likely that the consumer has no idea about this product and has no understanding of it. Therefore, there is a definite need for consumer opt-in into this product.

The consumer needs to make an informed choice. That can best be achieved by a chance to review options and have the product clearly explained by their institution.

As to coming under Truth in Lending, this product is alone, and no sleight of hand, no semantics nor any Federal Reserve regulatory reluctance can ever alter that fact.

As financial institutions, we will further damage our credibility by refusing to tell the consumer the blunt truth about this product. It is a loan. Truth in Lending is an established, well-understood regulation, and placing overdraft protection within that existing regulation, within that legal framework, will reduce that much-dreaded increase in potential regulatory burden. Let's use the existing legal regulatory framework of Truth in Lending to manage this product in the future.

As to personal financial responsibility, I am all for it, and I hope we all are—but the product being offered is discretionary at the whim of the lender. The lender when offering this product accepts no responsibility to the consumer. There is no contract for this product, no listing of rights, no listing of duties by either party. Absent those contracts and those agreements, there is an absence of transparency, there is an absence of disclosure.

Lack of acknowledgement of responsibility by either party on this product is financially, commercially, and legally insane. In this economic environment, the banking industry might find that citizens of this country consider their pontification on personal and financial responsibility not only rings hollow, but sounds hysterically absurd.

Lessening of service, higher banking costs. Can they get any more expensive than what we are dealing with now? Our organization serves as an example that institutions can thrive and can prosper without offering the overdraft service product.

Representative Bachus, we also have indicated several initiatives we will take later next year to try to eliminate those NSF charges.

Claimants for the demise of free checking, the free market, and perhaps the entire free world, may be a bit overstated if this product is reduced in the future. It is worrisome that some panelists indicate that the survival of their institution hinges on the income from this product. Why is it a concern? It is a concern because their institutions' fate hinges on the future misbehavior of their customers and members.

Lastly, wealth and earnings achieved through the misfortune and the misery of others should always be highly suspect, if not held in outright contempt.

I look forward to your comments and questions.

[The prepared statement of Mr. Blaine can be found on page 54 of the appendix.]

Mrs. MALONEY. Thank you for your really remarkable testimony.

Mr. Dennis Dollar from Dollar Associates, LLC.

STATEMENT OF DENNIS DOLLAR, PRINCIPAL PARTNER, DOLLAR ASSOCIATES, LLC

Mr. DOLLAR. Good morning, Madam Chairwoman. My name is Dennis Dollar. I served as a member of the National Credit Union Administration board from 1997 to 2004. I have been before this committee before, and it is a pleasure to be invited back.

I also was the chairman of the National Credit Union Administration from 2001 to 2004. Prior to that appointment, I was president and CEO of the Gulfport VA Federal Credit Union, a relatively small—at that time—$32 million credit union with approximately 12,000 members in Gulfport, Mississippi.

Since leaving NCUA, I formed a consultancy that works with credit unions and other financial service entities in their strategic initiatives. I guess you could say, from my experience, I have had the opportunity, Madam Chairwoman, to view the overdraft protection issue—as Judy Collins famously sang in the 1960's—"from both sides now."

Today, I have been asked by Ranking Member Bachus to come before you representing no particular group or organization, only as a former credit union CEO and a former regulator who now sees overdraft programs in action on a daily basis and whose experience indicates that while there are always ways in which such programs can be structured better for the consumers and the financial institutions they do business with, in my opinion, it would not be good public policy to completely eliminate them from the marketplace, as H.R. 3904 might effectively do.

During my years in credit union management, there was no overdraft protection program in place, Madam Chairwoman. If a member wrote a bad check, we charged an NSF fee, and we returned the item. Needless to say, the members who, like all consumers, are always opposed to any user fees imposed on them, didn't like this fee arrangement. They not only faced our NSF fee, but they were also charged with an additional returned check fee by the merchant to whom they wrote the item. Often, they faced late charges if the returned item was for their rent or their insurance.

But these folks weren't slugs or deadbeats. They were good, hard-working members who, on occasion, ran out of money before they ran out of month. It was for these members that the overdraft protection programs we are here today to discuss were originally developed to assist.

Rather than being charged an NSF fee, the member would be charged an identical fee. And it is important to recognize here, Madam Chairwoman, that, if structured properly, an overdraft fee is not an additional fee above and beyond an NSF fee. It is an identical fee that they would be charged otherwise to honor the overdrawn item up to a specific fully disclosed limit, and that the item then must be settled within, according to credit union regulations, 45 days, or it has to be written off and formal collection efforts begun.

Credit union members, as did many bank customers, saw value in these programs because they were able to realize those additional cost savings associated with avoiding the merchant fees and the late charges, the cancellation of service, and even possible prosecution, Mr. Bachus.

A well-structured—and, again, I use that term because there certainly is abuse, and we have all seen those documented examples where there was manipulation of item clearance solely to maximize profits, or assessing the $35 in overdraft fees on a $5 debit purchase of a venti cup of latte at Starbucks.

Those exceptions should be corrected and appropriately regulated. But overdraft programs, if done right—they can be done right and they should be done right—consumers and financial institutions benefit.

There are standards that I provided in my written testimony that outline the way most responsible financial institutions, and certainly the credit unions that I work with, handle their overdraft programs today. Now, because some institutions don't follow these best practices doesn't, in my view, make a case to overregulate those who do with punitive or burdensome legislation that will result in many of their consumers losing their checking accounts and many institutions forced to transfer the cost of overdrafts from the consumers who use the program to the vast majority that do not.

Now, my regulatory experience, Madam Chairwoman, does give me some pause about the potential impact on the long-term safety and soundness of some institutions that could come from effectively eliminating this source of earnings, but that is not why I am here today. My primary reason for supporting these types of programs is the benefit to the consumer that I saw taken away under the old, antiquated days of the NSF fee and legal prosecution in return to get their check or debit honored up to a clearly defined, clearly disclosed—and if institutions would do their jobs in financial education and making sure that the disclosures are appropriate and the members understood how this program is used, we would probably would not be sitting here today.

But we do have to remember this: If there is no deterrent in the system, bad check writing will grow. A half century of NSF fees, often increasing in amount, proved to us that the number of overdrafts wouldn't be lowered simply by charging fees. Overdraft programs with the proper disclosures and a financial education commitment as a part of the program offering can provide greater consumer value and, in my opinion, I think that it could enable us to avoid having to return to those dark days of the costly NSF fees.

There is a way that a balanced regulatory approach, handled through the regulatory agencies without a statutory mandate, can keep consumers within the traditional finance institutions, but yet ensure that these programs are fully understood and transparent.

That is what we would like to see.

[The prepared statement of Mr. Dollar can be found on page 99 of the appendix.]

Mrs. MALONEY. Thank you very much for your testimony.

The next witness is Ms. Ellen Bloom, director of the Washington Office and Federal Policy, Consumers Union.

Welcome.

STATEMENT OF ELLEN BLOOM, DIRECTOR, FEDERAL POLICY AND WASHINGTON OFFICE, CONSUMERS UNION

Ms. BLOOM. Thank you, Madam Chairwoman, Ranking Member Bachus, and members of the committee. I am Ellen Bloom, director of Federal policy in the Washington Office of Consumers Union, which is the nonprofit, independent publisher of Consumer Reports magazine. Our organization strongly supports H.R. 3904, the Overdraft Protection Act of 2009. We appreciate the chance to add our perspective on the impact current fee-based overdraft programs are having on consumers.

First, I would like to briefly touch on telephone poll results from a nationally representative survey conducted by Consumer Reports National Research Center in February. This poll underscores two points: Consumers are often unaware of the consequences of overdrawing their accounts. When asked, however, they express a very strong desire to have more decision-making control over these fee-based overdraft programs. Here are just a few of the findings:

Only 52 percent of those surveyed who use debit cards had a correct understanding that a bank typically allows the transaction to proceed, covers the shortage from the next deposit, and charges a fee for doing so.

According to our poll, consumers appear even more misinformed about ATM overdrafts. Only 31 percent know that the bank will permit a transaction, subsequently dock the account and charge for the loan. It was clear that many consumers simply didn't expect to be charged a fee when they overdraft their account. To us it seemed clear, consumers would be unlikely to opt-out of a program of which they are unaware. And that is why CU strongly supports the opt-in language in H.R. 3904.

At the same time, our poll reveals that consumers overwhelmingly want choice when it comes to their bank accounts. Two-thirds of consumers polled said they would prefer to expressly authorize overdraft coverage so that there would be no overdraft loan or fee unless they opted-in to the service. Two-thirds also said that banks should deny a credit card or an ATM transaction if the checking account balance is too low. In addition to our polling, we have had consumers share their frustrations with us about automatic overdraft programs. I have attached a compilation of these stories to my written testimony.

I will highlight three now. Rachel from North Carolina explained to us that her bank manipulates the order in which they clear transactions in order to maximize the number of times she overdraws her account. A married mother of three, Rachel at one time found 7 overdraft charges for debit card transactions. Each of these was for purchases of less than $20, and at least half were under $10. One charge was even for a $1 beverage at a gas station. However, each of these transactions was penalized with a $35 fee. As Rachel explained to us, "They cleared the largest amounts first because they want to charge the fee on the $1 purchase." Rachel went on to tell us, when you are taking $300 from us in 2 weeks, we get behind on other expenses. It literally took us 2 months to catch up.

Justin from New York told us why he believes it is important to place strong limits on the number of times an institution can charge a fee for covering an overdraft. Justin told us that he was charged $385 for 11 overdrafts over a 10-day period. Some of these transactions were for less than $10. All but 2 were worth less than $50. Eventually, after multiple calls to the bank, Justin was refunded $100 of his $385 total overdraft fees. Justin told us that he wishes he could just choose whether the bank covers the transactions when they overdraw his account.

Don from Ohio described the snowball effect of overdraft fees. Don and his wife rely on a limited income, the paycheck from his part-time job, and the Social Security payment his wife receives for disability. Don checks his account balances regularly, but he was recently hit with a flurry of overdraft fees. One year ago this month, Don used his debit card and overdrafted his checking account by 35 cents. Before the bank had opened the next day, Don deposited $30 at the ATM to cover the 85-cent overdraft. A day later, he discovered he had incurred two overdraft fees, one for the 85 cents, and the other because the $30 deposit had not covered the deficit caused by the first fee. The second overdraft even triggered another overdraft fee and an additional $5 per day fee for each was added. After haggling with his bank, Don reached a compromise and only paid for one of the $35 overdraft fees, but it was grueling.

Mr. Chairman, members of the committee, the Overdraft Protection Act will go a long way to stop the abusive practices experienced by Rachel and Justin and Don and thousands of other consumers across the Nation. We applaud its introduction and urge its prompt passage. Thank you.

[The prepared statement of Ms. Bloom can be found on page 58 of the appendix.]

Mrs. MALONEY. Thank you very much for your testimony.

Our next panelist is Mark A. Colley, president and chief executive officer of the Tulsa Postal and Community Federal Credit Union, on behalf of the National Association of Federal Credit Unions.

STATEMENT OF MARK A. COLLEY, PRESIDENT AND CHIEF EXECUTIVE OFFICER, TULSA POSTAL & COMMUNITY FEDERAL CREDIT UNION, ON BEHALF OF THE NATIONAL ASSOCIATION OF FEDERAL CREDIT UNIONS (NAFCU)

Mr. COLLEY. Good morning, Madam Chairwoman, Ranking Member Bachus, and members of the committee. My name is Mark Colley and I am here today to testify on behalf of the National Association of Federal Credit Unions, or NAFCU. I am the president and chief executive officer of the Tulsa Postal & Community Federal Credit Union, headquartered in Tulsa, Oklahoma.

Tulsa Postal was chartered in 1923, making us the oldest credit union in the State of Oklahoma. We are a small credit union with 11 full-time employees and approximately $23.6 million in assets. U.S. Postal Service employees and retirees, as well as their family members, make up most of our membership base. The rest of our members are people who live, work, or worship in Tulsa County and are classified as underserved.

Most credit union members welcome and appreciate the opportunity to benefit from a courtesy pay or an overdraft protection program and consider it useful and a convenient service. Overdraft programs can prevent high fees and penalties that result from bounced checks, and provide important financial coverage in unexpected circumstances when members may need it the most. At Tulsa Postal, we currently offer courtesy pay programs to 936 of our 1,440 checking accounts. Only 2 of the 936 members have chosen to opt-out of our courtesy pay program.

In order to be enrolled in the program, a member must first select a transfer from another deposit account as the first overdraft coverage option. Courtesy pay is not triggered until all transfer options have been exhausted. We have several casinos in our area, and if we notice frequent casino activity, we shut off the debit cards and the courtesy pay program to them. We also do not report any of our overdraft protection balances to ATM or debit networks.

If a member comes to us, concerned that they have overdrafted their account because of an error, we refund 100 percent of the courtesy pay fee they were charged. If this happens multiple times, we ask them to come in so we can educate them about the proper use of the program.

I have read the stories about individuals who have been charged $35 for spending just a few dollars more than they have in their accounts. At my credit union, we refund these fees, provided the member does not abuse the privilege. We have never had a single member complain about our courtesy pay program.

NAFCU appreciates the Overdraft Protection Act's efforts to address our concerns regarding the credit union usury ceiling. We believe the bill is well-intended. H.R. 3904 is still problematic from a credit union perspective, and NAFCU maintains several significant concerns with this legislation.

First, the current opt-in provision would impose a considerable regulatory burden on credit unions and create consumer confusion among those who believe they already have this particular product. NAFCU would support language establishing an opt-out requirement instead, allowing existing members who are currently covered by overdraft protection programs to deny the coverage if they wish. We could also support an opt-in requirement for new members or customer accounts.

NAFCU is also concerned about provisions in the bill limiting NSF fees for debit and ATM transactions. These types of transactions are covered by financial institutions when made, even if there are insufficient funds in the account when cleared. Since the transaction is authorized by the merchant at the time it takes place, the credit union is contractually liable to post the payment, even though the funds are not available in the consumer's account to cover it.

Many merchants do not verify balances in real time. This provision therefore appears impractical and impossible to comply with. The limitation to one overdraft fee per month is highly problematic for the vast majority of credit unions that receive transactions not processed by merchants in real time. Further, providing same-day notification to members who have overdrawn their accounts would be another considerable burden for credit unions, as they may not learn that an overdraft has taken place until all transactions clear at the end of the day. NAFCU could support a more reasonable notification time frame.

NAFCU is also concerned about the bill's limitation on the number of overdraft coverage fees. We believe that the restriction to 1 overdraft fee per month and 6 per year would significantly limit consumer choice. An alternative would be to require financial institutions to send a notification to consumers who have overdrafted several times during the course of the month, listing the options available to them.

In conclusion, I would urge the committee to keep in mind that consumers can avoid overdraft fees, no matter what the law is, in one simple way, by managing the funds in their accounts. Increased focus on financial education funds and literacy to teach consumers this personal responsibility would make the need for overdraft protection moot.

We urge the committee to take these concerns into account and make significant changes to the legislation before it moves forward. I thank you for the opportunity to testify and the privilege of being here today, and I welcome any questions that you may have. Thank you.

[The prepared statement of Mr. Colley can be found on page 85 of the appendix.]

Mrs. MALONEY. Thank you very much.

Next, Mr. Richard Hunt, president of the Consumer Bankers Association.

STATEMENT OF RICHARD HUNT, PRESIDENT, CONSUMER BANKERS ASSOCIATION (CBA)

Mr. HUNT. And a very good morning, Madam Chairwoman, Ranking Member Bachus, and members of the committee. My name is Richard Hunt and, like many Americans, I too have overdrafted.

I am president of the Consumer Bankers Association and it is indeed an honor to appear here today representing retail bankers.

For more than 90 years, CBA has served as the voice of the retail banking industry, which provides banking services to meet the needs of consumers and small businesses. Our members are regional and supercommunity banks, as well as bank holding companies. I appreciate the opportunity to appear before you.

I want to provide a little bit of an insight about the services Americans may not be receiving from the media and the industry critics. Courtesy overdraft services are just that, a courtesy that banks have traditionally offered as a service to their customers. Our members report and statistics show the vast majority of customers manage their checking accounts in an appropriate manner, but even the most responsible consumer can overdraw an account every once in a while. When this occurs, the bank has one or two options. It can bounce the check, or deny the debit card transaction, or it can honor the check for the debit card purchase and assume that risk.

If the bank does indeed deny these transactions, which we believe will occur at a more frequent rate if this legislation is enacted, several things will happen to the consumer. They will pay a fee to the bank; they will find themselves at a register, possibly the Rayburn Cafeteria, with a plate full of salad and no possible way to purchase that salad. They will surely face late payment fees and delinquencies from a merchant or creditor, and as previously mentioned, the consumer may also be at risk of violating State laws pertaining to bad checks.

With this in mind, it is easy to understand why bank customers overwhelmingly prefer the bank to honor overdraft transactions, even when they result in overdraft fees. It is an important benefit thousands of banks provide to millions of customers.

Although it may seem reasonable to expect that a bank customer will not overdraft an account, more than once a month or 6 times a year, as this legislation mandates, I can tell you this is not always the case, even for the most responsible customers. For example, a consumer can write several checks, not realizing their spouse also recently made transactions, whether it was an ATM machine or a check. If a bank is not allowed to charge an overdraft fee when those checks bounce, the bank simply may not honor these charges. Indeed it may not be a safe or sound banking practice to honor the transactions without charging a fee. The bank is paying money with the risk of not being paid back.

Yes, there are anecdotes of a $39 cup of coffee resulting from an overdraft debit card transaction. These are abnormal cases. They do not reflect how the vast majority of bank customers manage their accounts. Congress ought not legislate based on anecdotes, especially when the legislation will harm a far greater number of customers than it helps.

In closing, Madam Chairwoman, my own personal experience with overdraft protection was a relief. Despite having numerous ways to access my account balance, I simply had one transaction too many. Had it not been for the courtesy extended to me by my bank, I would have had more hassle and more cost. I paid the fee and was grateful the service was there. That allowed me to continue with my life without interruption.

I appreciate the opportunity and look forward to any questions you may have.

[The prepared statement of Mr. Hunt can be found on page 150 of the appendix.]

Mrs. MALONEY. Thank you very much for your testimony.

Our last panelist is Mr. R. Michael Menzies. He is the president and chief executive officer of Easton Bank and Trust, and he is testifying today on behalf of the Independent Community Bankers of America. Thank you. And he is a former New Yorker, so welcome.

STATEMENT OF R. MICHAEL S. MENZIES, SR., PRESIDENT AND CHIEF EXECUTIVE OFFICER, EASTON BANK AND TRUST COMPANY, ON BEHALF OF THE INDEPENDENT COMMUNITY BANKERS OF AMERICA (ICBA)

Mr. MENZIES. Thank you, Madam Chairwoman. It is an honor to be back with you and Ranking Member Bachus and this distinguished committee today. I am truly proud to represent the Independent Community Bankers of America on this important legislation, and I am beyond thrilled that Mr. Hunt has introduced the notion that the elimination of overdraft protection could produce divorce. I hadn't thought of that one.

There are 8,000 community banks in this country, most of which are at or below $10 billion in total assets. The only thing my peers and I can do to compete in this industry, the only thing we can do is to serve our customers better than the competition, and that includes with the quality and fairness of the overdraft services we offer.

Three-quarters of community banks provide some form of overdraft protection, and all of those do so fairly and in a way that best meets the needs of their customers. However, community bank customers understand that when they spend money that does not belong to them, there are consequences and costs. While community banks always seek to treat customers honestly, the same expectations must hold true in reverse. Customers should not, and generally do not, expect a free pass when they overdraw their accounts.

The alternatives for a customer include merchant returned check fees, possible credit report and bad check database blemishes, collection hassles, embarrassment, and the list goes on and on, as the panelists have suggested. These alternatives are far worse than incurring an overdraft fee.

ICBA supports provisions of H.R. 3904 and improved disclosures for consumers, and restrict deceptive advertising, and encourage excessive use of overdraft programs. These efforts will go far in preventing unscrupulous providers of these services from taking advantage of consumers.

However, we are very concerned with other provisions of the bill. I outlined all of these concerns in my written statement, but I would like to discuss three of them in my oral statement.

First and most important, this legislation fails to distinguish clearly between discretionary overdraft coverage and automated programs that have drawn the ire of many for the so-called $35 cup of coffee. Discretionary coverage involves a banker, not a third party vendor or program, evaluating specific overdrafts on a case-by-case basis. These usually involve most important consumer bills, like a mortgage payment, a car payment, the utility bill, paid by a check or an ACH. It is these situations that demonstrate the strength and importance of the relationship-driven model of community banking and how overdraft coverage can be the most personal service a banker can provide. In fact, the Federal Reserve has acknowledged that these services should not be lumped into regulation along with automated overdraft programs.

Second, we are strongly opposed to placing arbitrary price caps and limits on overdrafts, especially when tied to the cost of processing versus the amount overdrawn. If caps were imposed, community banks who are proven risk managers must find other ways to manage that risk. This could include elimination of popular checking account features, cutting off debit cards for overdraft-prone customers, and, more likely, closing accounts. An unintended consequence of this clearly could be expanding the ranks of the unbanked.

Third, while we appreciate that the legislation calls for a study on the feasibility of point-of-sale overdraft for consumers, the fact remains that even for ATMs and branch tellers, the means do not exist to verify with 100 percent certainty that a transaction at a given time will not lead to an overdraft situation shortly thereafter. Not all banks and merchants process debit and ATM transactions in the same manner or at the same time. And banks that use a daily ledger balance, rather than real-time ledger balances, won't be able to comply with any real-time requirements.

In conclusion, we are very concerned that this legislation attempts to restrict the supply of overdraft coverage while ignoring the fact that community bankers offer these programs to meet our customers' demand. In a perfect world, consumers would never find themselves facing an overdraft situation. But given what we know of consumer behavior, community banks need to be able to provide all types of overdraft coverage to our customers, while also receiving a competitive fee for the cost and risk of paying transactions for customers with the bank's own funds. Furthermore, any legislation that increases the number of returned checks and debit transactions, as I believe this legislation will as currently drafted, is not good for consumers.

Thank you so much and I look forward to answering your questions.

[The prepared statement of Mr. Menzies can be found on page 167 of the appendix.]

Mrs. MALONEY. I would like to thank everybody for their testimony, and I would like to yield first to Mr. Ellison who has a conflict with another important meeting. I yield Mr. Ellison 5 minutes.

Mr. ELLISON. And let me thank the chairwoman who has distinguished herself in many ways on behalf of the participants of the American economy at large, including American consumers. Thank you, Madam Chairwoman, for this hearing today.

My first question is to Mr. Halperin. How much does it cost, to the best of our knowledge, to process an overdraft transaction—an overdraft? How much does it cost, everything?

Mr. HALPERIN. The processing costs alone for an overdraft are fairly minimal. At this point, if there is an automated program, often those things can be handled without human intervention in terms of the decision to cover the overdraft. And then if it is a discretionary program, there will be some staff time.

Mr. ELLISON. Okay. If we could from the best that we know—and I want to ask this of everybody, don't give me a long answer because I only have a few minutes—is it more than a dollar to process an overdraft? Let's start with you, Mr. Halperin. Is it more than a dollar?

Mr. HALPERIN. If it is more, I don't have a precise number. If it is more than a dollar, it is not much more than a dollar.

Mr. ELLISON. Is it more than $2?

Mr. HALPERIN. I imagine it would be somewhere in that range.

Mr. ELLISON. Ms. Feddis, I am reading your body language. Is it more than $2?

Ms. FEDDIS. Sir, we don't—

Mr. ELLISON. Now, don't give me a long answer, because I will cut you off if you do.

Ms. FEDDIS. I think you have to go beyond just processing. I don't know what that number is. I suspect it probably is more than $2, but you have to go beyond just processing. There are other costs associated with having an overdraft, whether it is lost income, because you can't earn interest on a zero balance. It is much more—

Mr. ELLISON. Ms. Feddis, of course, I am very sensitive to who you represent and why you're here, and that is fine with me. I think we need everybody in this economy, everybody. But I am just trying to get information. Is it $5 to transact an overdraft fee? How much does it really cost?

Ms. FEDDIS. I don't know, but there are more costs than just the electronic blip.

Mr. ELLISON. $5?

Ms. FEDDIS. It is probably more.

Mr. ELLISON. $7?

Ms. FEDDIS. It is probably higher.

Mr. ELLISON. I have a feeling that if I said it was $100, you would say it is probably higher.

Ms. FEDDIS. No, I wouldn't say that. I don't know, but I have talked to one analyst who suspected it was more; it was certainly over $10.

Mr. ELLISON. Let's say it is $10; let's just say that. Mr. Halperin says no way; you say $10. Can we all say $10 is in the neighborhood—

Ms. FEDDIS. I don't know.

Mr. ELLISON. Okay. Well, if you don't know, then you don't know.

Ms. FEDDIS. Well, that is what I said.

Mr. ELLISON. Okay, fair enough. But you did say—

Ms. FEDDIS. No, I said I heard from one analyst.

Mr. ELLISON. Let's just say it is $11, okay, just so we can talk about what we are here to talk about. If it is $11, Ms. Fox, how do they end up with $37, $39—how do they—even if it is $11, how do they end up with $39?

Mr. FOX. Because they can. Banks put their fee information in the fine print, as the GAO found when they did their survey of banks. It is hard for consumers to get that information before they open an account. So you don't have competitive pressure on the size of the fee, and consumers don't think they are going to incur it.

Mr. ELLISON. Thank you.

Mr. Ireland, I appreciated your comments. Why can't Ms. Feddis' organization and other folks who represent the banking industry support at least the opt-in provision that is contained in the bill?

Mr. IRELAND. I can't speak for Ms. Feddis.

Mr. ELLISON. I am not asking you to speak for her. Why can't the banking industry say, okay, we will support the opt-in; we are not for everything, but we are for the opt-in.

Mr. IRELAND. In my testimony, I didn't argue with the opt-in.

Mr. ELLISON. Okay, I know you didn't. And the reason I am asking you is because it seemed to me, as I read your piece, that you sort of were looking at both sides of this thing.

Mr. IRELAND. It seems to me you are going to do an opt-in, and why don't we talk about—

Mr. ELLISON. But what I am asking you is, how does it harm industry for an opt-in—or do you agree that it doesn't?

Mr. IRELAND. I think there will be a revenue impact of an opt-in that will lead to some repricing of the account.

Mr. ELLISON. So what is wrong the opt-in, Ms. Feddis?

Ms. FEDDIS. The ABA does support choice, we have always supported choice. Most banks, as the FDIC found—

Mr. ELLISON. Remember, 5 minutes. If I had 20 minutes, I would let you talk as long as you wanted.

Ms. FEDDIS. Oh, I am trying to answer the question. I'm sorry.

Mrs. MALONEY. I grant the gentleman 2 additional minutes so the lady can answer the question.

Mr. ELLISON. Thank you.

Ms. FEDDIS. Thank you, Madam Chairwoman. We do support consumers having choice. As the FDIC found, 86 percent of banks do offer the choice, opt-in or opt-out. Generally—

Mr. ELLISON. Thank you very much. And so, I think I am out of time and I want to thank the chairman again. I want to thank everyone on the panel, because I think we are all here trying to get to the right answer. Thank you very much.

Mrs. MALONEY. Reclaiming our time, I grant the gentleman, Ranking Member Bachus, 5 minutes.

Mr. BACHUS. I thank the gentlelady. Opt-in, there seems to be quite a bit of confusion over whether the banks and credit unions can do this. Are you saying, Ms. Feddis that 80 percent of the banking institutions allow opt-in?

Ms. FEDDIS. No. They allow choice, either opt-in or opt-out. Most of them allow opt-out. About 11 percent, according to the FDIC numbers, which only represents the banks surveyed, about 11 percent provided opt-in and 75 percent opt-out.

Mr. BACHUS. All right.

Ms. FEDDIS. I am not sure that, as I said, we support opt-out, because the consumer testing has found that most people want overdrafts covered and that the default should be for the preference of most people. But opt-in is certainly something we would consider.

Mr. BACHUS. Something what?

Ms. FEDDIS. Something the industry would consider. And some institutions are already moving toward opt-in. Some even large institutions don't allow any sort of debit card overdrafts, but that is something we would consider.

Mr. BACHUS. Mr. Colley, you said that it is a problem, opt-in; is that right?

Mr. COLLEY. Yes, I did. For our current members who are on the program, it would be a really large regulatory burden to try to get in touch with them, and also lead to more confusion for them to sign up for something that they perceive that they already have.

Mr. BACHUS. What if there were opt-ins for new consumers?

Mr. COLLEY. NAFCU does not have a problem with that, sir, and neither do I personally as a CEO.

Mr. BACHUS. What about Mr. Hunt?

Mr. HUNT. Mr. Bachus, we think it would lead to mass confusion for consumers if you required current customers to opt-in.

Mr. BACHUS. No, I'm talking about new customers.

Mr. HUNT. Sure, that is a viable option. Many of our banks are in fact doing that. They are opting-in for new customers. We think it is better for current customers to have the ability to opt-out of overdraft fees.

Mr. BACHUS. No, I'm talking about new customers.

Mr. HUNT. Yes. Many of our banks are already going that direction, and we think that is a viable alternative.

Mr. BACHUS. I know there still—I am trying to maybe get some things that we could agree on.

Now the debit cards, I think we all would agree that if the technology was there, we would deny those at the point of sale; is that basically right? Mr. Ireland?

Mr. IRELAND. There is—many banks find that if they check the balance when the transaction goes through at the point of sale and there is not money there at the time the debit card is used, there is money there when the debit settles a day or 2 later. And so there is a lack of precision—you could deny the transaction, but you would deny a lot of transactions that now actually get paid.

Mr. BACHUS. But what I am thinking, let's just assume a decision was made from a policy standpoint that they were going to deny it if they checked at that time.

Mr. IRELAND. They could do that.

Mr. BACHUS. Can the small banks—Mr. Menzies, you were telling me that some of the community banks, some of those don't have that ability?

Mr. MENZIES. Absolutely true, Congressman. Many banks process these items differently and we don't have real-time capacity, because we are focused on serving our customers, not just on buying the most expensive technology of the day.

Mr. BACHUS. Mr. Halperin—and I don't want to put words—the larger banks are—they have that ability, right?

Mr. HALPERIN. Mr. Bachus, all banks have the ability to deny. Our affiliated credit union is quite a small credit union and we deny transactions. We currently have a real-time system, but even when we had a posting system, we denied those transactions that would overdraft the account. We have heard other people on the panel today who also have testified that they deny debit card transactions from smaller institutions. But there is one very large institution, Citibank, that says its policy is to deny debit card transactions—

Mr. BACHUS. And you like that policy; is that correct?

Mr. HALPERIN. Yes, we think debit card overdrafts, as the Federal Reserve found, often provide very little or no benefit to the consumer; there is no avoidance of a fee, which I know is one of your concerns in your opening remarks over the NSF fee and the bad check issue. That simply is not present in the debit card context. So we think a denied debit card transaction, unless the consumer has chosen a line of credit or another method to have that covered, is the preferable outcome.

Mr. BACHUS. I think everyone agreed that a line of credit is a better alternative. And if you did start denying debit card transactions at the point of sale, that would encourage people to come in and open a line of credit, I would think. Ms. Fox?

Mr. FOX. Yes, one of the important side benefits of requiring opt-in in limiting this problem of overdrafts is that banks will have an incentive to promote their much more affordable, more appropriate products. Their line of credit simply costs about 18 percent a year, and consumers get to pay it back in installments. Banks have transfer services. If they have to get you to sign up, they have to offer all their products. People are likely to get a cheaper option.

Mr. BACHUS. Now ATM—can all institutions tell them, when they use their ATM card, whether or not it will overdraft their account?

Mr. IRELAND. Some institutions can tell on their own ATM. I am not aware of anybody who has an arrangement that, if you use another institution's ATM, that they have that communication facility at this time.

Mr. BACHUS. Would we all agree that if you can tell them that you shouldn't overdraft their account, does ABA agree with that?

Ms. FEDDIS. We would support providing the option to proceed with the transaction at the ATM's—for ATMs owned by that institution. As Mr. Ireland points out, it is not possible with today's systems to do it at the point of sale, to give the option at the point of sale or at another ATM.

Mr. BACHUS. Because I do think that if you approach your ATM—and you used to, but I think the banks have stopped doing this, but I thought—for a while I think there was actually—and I think this is very misleading, the balance would include the overdraft, their ability to overdraft, even the line of credit, which—

Ms. FEDDIS. The regulation now prohibits that.

Mr. BACHUS. It now prohibits that?

Ms. FEDDIS. The Federal Reserve did address that.

Mr. BACHUS. So if it can be done.

Now, Mr. Menzies, can the small banks let people know at the ATM, if it is there—obviously, can we agree if it is their bank's ATM—

Mrs. MALONEY. I grant the gentleman an additional 2 minutes. He is well over his time.

Mr. MENZIES. Congressman, we do not show our overdraft privilege customers being available at the ATM, because we don't want that, quite frankly. We want it there for protection for checks and debits. But your question was—-

Mr. BACHUS. When they use their ATM, if it would overdraw that account, do you know—do they get that note—

Mr. MENZIES. They don't have access to the funds at the ATM, at our ATM. They are not allowed to go to the ATM and use the debit card and access their privilege account at the ATM.

Mr. BACHUS. Oh.

Mr. MENZIES. We don't want them using it at the ATM for a cash fund because the purpose of it is to protect against bounced checks and debits.

Mr. BACHUS. All right. Do the banking institutions have a problem with processing checks in the order they come in? I would ask the American Bankers Association.

Ms. FEDDIS. Well, I guess under this bill it probably isn't necessary to address the posting because it is capped at one per month, so it doesn't matter what the posting order under this bill. It wouldn't be necessary to address it.

Mr. BACHUS. I am not talking about under this bill.

Ms. FEDDIS. It is a very complicated and much litigated issue.

Mr. BACHUS. No, no. But what I am asking is, do you object to processing them in the order they come in, is that—

Ms. FEDDIS. Well, I can't give you a straight answer because it is very complicated, the payment order. In fact, Mr. Ireland has actually studied it.

Mr. BACHUS. My bank processes them in—they used to process them in a different order. And I actually asked them, I said you hear all this stuff about how they take the large ones so they can get—and my bank, which is a large bank, actually said they quit doing that because they didn't think it was fair to their customers.

Ms. FEDDIS. Well, a lot of times people do want—and the consumer testing has found this—people want important payments made and they tend to be large—the mortgage, the rent—and so if they want those paid—and so that is why some institutions have done that. According to the FDIC, about half of the banks actually process small to large, about 24 percent under their survey found that it was—

Mr. BACHUS. Okay.

Ms. FEDDIS. The banks have been sued for both. One large institution was sued for paying low to high. And what people really want is—

Mr. BACHUS. At least we clarified it, right?

Mrs. MALONEY. The gentleman's time has expired.

The Chair grants herself 5 minutes. One of the purposes of the bill is what the gentleman is trying to clarify; more information to the consumer will help them, particularly during this extreme financial time, to better manage their own money. And the bill does have in it a specific prohibition to having financial institutions list on ATMs more money than what the consumer has. If it includes a line of credit, if it includes other access to capital, people are misled. They think they have money they don't have. It is one reason that we worked very hard to have this under the Truth in Lending provision so that consumers will have more understanding of what is happening.

I would like to ask Ms. Feddis and Mr. Hunt and others from financial institutions if you could explain why overdraft plans are the only financial product now where in essence you take the consumer's money without the consumer's permission? Why is that the only service that you have this means of operating? Mr. Hunt?

Mr. HUNT. Thank you, Madam Chairwoman. I want to tell you, we want to make sure our customers are always happy. We know in this time that if a customer is not happy with the services we provide in this day in time, they can quite frankly go to their terminal and open an account at another bank to do that.

When a person does sign up for a deposit account, there is a deposit agreement they do sign, that says we have the opportunity to offer services for a fee. And that is what we do. As we have stated many times before, this is a very popular program we offer to our consumers. We do not like overdraft fees. We do not want someone to overdraft. That is why when a person signs up, we tell them about lines of credit, lines of credit to their savings account, their checking account, and everything else.

Mrs. MALONEY. Mr. Hunt, what we are hearing from consumers is, why are they paying for a service that they don't want? These consumers are telling me that they would prefer for their debit card to be declined, for their check to be declined, as opposed to being charged the $35 fee for—many times it is an incidental.

I would like to ask you, how is this action any different from a Burger King charging you for a hamburger you don't even want? In that case, it would be called a robbery, taking someone's money for a product they don't even want. What we are told is that consumers go to their banks and say, we don't even want the fee, we don't want the protection, we don't want the service. And some financial institutions are forcing them into a program they don't even want.

But I would like to ask you, what if Burger King were to take your money for a product without asking for it? Wouldn't you be a little disturbed? That is why we have an opt-in so people can decide what they want. And how is what some financial institutions are doing different from McDonalds or Burger King, automatically charging you for fries or a burger that you don't even want and you are charged for something that you would prefer not to have? How is that fair?

Mr. HUNT. Madam Chairwoman, I appreciate the question, and I will tell you this: If a customer does not want any overdraft protection, it is very simple. You go to the bank and you tell them, I want to opt-out. The bank will adhere to your wishes.

I will also tell you, the mention of the $35 fee that everybody keeps mentioning, that is the maximum fee that a bank imposes. Most of the time when you an accidental overdraft, a person who may overdraft 1 time a year, the fee is lower than that, roughly $10 or $15. And I will tell you, Madam Chairwoman, if you go to your—

Mrs. MALONEY. Again, sir, that may be your institution.The average we are reporting is $35. And sometimes it can be $35 for each transaction. I have had consumers come to me and tell me that at the end of the weekend, they were charged $300 or $600 because they didn't know that the pack of gum, the carton of milk, the sandwich, the cup of coffee, with each purchase incurred a $35 fee.

So I would like now to ask some of the consumer groups on this opt-in and opt-out situation. I would like them to expand on opt-in and opt-out. And isn't it better to let consumers make a choice about what products they want?

Mr. Halperin, Ms. Fox, Ms. Bloom, if you could expand please? The opt-in, opt-out is a big issue, and I would like you to expand on why you prefer the opt-in over the opt-out.

Mr. HALPERIN. Madam Chairwoman.

Ms. FOX. You go first.

Mr. HALPERIN. The opt-in will create a critical moment of choice where consumers can be given all their options and choose that cheaper, contractually obligated option, the one that will always be there, the line of credit or another option.

One thing consumers experience repeatedly is that they cannot opt-out of their bank's overdraft programs, especially at larger financial institutions. There have been some recent changes announced by large financial institutions where some are moving towards an opt-out, and we are happy to hear that. But repeatedly, we hear from consumers that they can't get out of their program. Opt-in is critical because it creates that moment of choice.

Ms. FOX. And the interesting thing is that back in 2005, the bank regulatory agencies issued some guidelines, and they said banks should get consumers to opt-in to their overdraft program. And failing that, they should at least let them opt-out. And as the FDIC survey found, a significant portion of banks won't even let you opt-out. So what happens is banks also won't let you close your account or freeze your account when you owe them an overdraft fee. And that causes a real burden as well.

Mrs. MALONEY. Well, if I could just comment, in the 1960's, some creditors sent unsolicited credit cards to consumers and there was an absolute outcry, and Congress had to step in to stop that and ban that practice. Isn't this basically the same thing, where they are giving you something you don't want that actually costs you money?

Mr. FOX. That is right. This is the only form of involuntary credit we know about. Banks mail out debit cards to their customers that can be used as credit cards. These were sold to people as a substitute for cash. People don't know, they don't think that they can get into debt by using their debit card. They think their bank will reject it if they don't have enough money to cover it. That is what the system should do. This is not a credit instrument. It should be a payment instrument, and banks should not be permitted to mail out live debit cards that can trigger debt.

Mrs. MALONEY. Thank you. Mr. Posey from Florida is recognized for 5 minutes.

Mr. POSEY. Thank you, Madam Chairwoman. I want to thank everyone on the panel for some spectacular testimony. Some of it was a little conflicting, but I think it was all sincere from your perspective and very enlightening to us. I wish we weren't here to even have to talk about overdraft, and there wasn't a need for such a thing, and that there could be no abuse by the borrower or the lender, but that we know in reality and in commerce that is going to be necessary occasionally. And we know that ultimately at the end of the day, there is, or at least one would think there should be, some consequences for not paying obligations that you promised to pay. I hate to use that term, it scares a lot of people, it is called personal responsibility.

And sometimes, I wonder if more government and more regulation and less personal freedom also means less personal responsibility; if at the end of day, we don't really hurt people more than we help them. And what I want to make sure is the unintended consequences of what we are looking at don't go too far overboard. I know the $1 Coke really hit my nerve, it seemed pretty outrageous. It reminded me of the last time I was 1 minute late for getting my dime in a parking meter, and it was a lot more than $35, and they do that to poor people and rich people, it really doesn't matter. The parking meter doesn't do an analysis on how much it costs City Hall to collect that thing, whether we think it is fair or not fair. That is the cost of parking there, and if you don't want to pay a huge fine, make sure you get your nickel or quarter in there on time. Again, it is personal responsibility.

I wonder, from any of the consumer organizations, and just respond if you know this for a fact, has there been a survey that has just been straight up: Would you prefer overdraft protection at $35 a crack, or would you prefer nonsufficient funds at $35 a crack, and possible legal liability? Has anyone asked their respondees that question and framed it just like that in this polling? I would like to hear from you if you have.

Mr. HALPERIN. Congressman—

Mr. POSEY. If you haven't asked that exact question.

Mr. HALPERIN. That exact question, worded that way? We have not asked the question worded in that fashion.

Mr. POSEY. Because I think that is the bottom line for most of my people back home. I know I would not want to pay a $35 fee for an overdraft, but I would much less want to pay a $35 nonsufficient funds fee and have my check bounced.

Mr. HALPERIN. Congressman, we did ask—as I mentioned in my opening remarks, debit card transactions are driving the overdraft volume—the analogous question for debit cards, which is: Would you rather have it declined or have the transaction processed and pay the fee? And for debit cards, the numbers were 80 percent of the consumers would rather have it declined; 75 percent of consumers who had overdrafted in the last 6 months would prefer to have it declined in the debit card context.

Mr. POSEY. Okay, the next question. A lot of times I think it is perceived that we are looking at huge banks exploiting people in the marketplace, day in and day out up here. But we have representation here from a lot of community banks and credit unions. And I would interested in knowing from them what the unintended consequences might be of this: If we regulate this to a $10 charge, and if people opt-in and say, look, for $10 a transaction, we will pay all the bad checks that you ever want us to pay, what that could mean at the end of the day?

I know Congress used to have a program something like that and they had to completely eliminate their overdraft protection because it was so badly abused. Does anybody in the marketplace want to weigh in on that?

Mr. STAATZ. We are concerned, Congressman, that there would be abuse and that abuse would be even higher than some of it is today, and the number of overdrafts would increase. And we really don't want that to happen.

Mr. POSEY. We haven't heard today about the loss ratio either when they do an overdraft protection or an overdraft notice. How often is that money ultimately recovered? Does anybody know that, or are there some loses that are sustained, that are not repaid, that go into that $35 fee?

Mr. STAATZ. Absolutely, yes. I don't have the numbers for you, we could probably get that, but some of those are fairly substantial, depending on the institution.

Mr. DOLLAR. Congressman, most of the credit unions that I work with reserve 6 to 7, perhaps at much as 8 percent, of the total amount for potential losses.

Mr. POSEY. I think, as the lady pointed out before, the processing fee probably should be quantified generally. And I think these things need to be quantified, too, to give us a full picture of what all is involved in this. It is not just taking $35 and it is all 100 percent pure bottom-line profit. That is the feeling you get when you hear one side of the equation, until you hear the other side of the equation. It doesn't seem to focus as much in the middle.

I would like in the future when we have these discussions, if we could just get more information like that.

Mrs. MALONEY. The gentleman's time has expired. But I would like to note in Mr. Blaine's testimony earlier, he said his institution charges $12 for nonsufficient funds and 50 cents for a transfer from another account, which is the equivalent of an overdraft.

The Chair recognizes Mr. Green for 5 minutes.

Mr. GREEN. Thank you, Madam Chairwoman. I thank the witnesses for appearing today. And Mr. Blaine, I must tell you that you have completely destroyed my line of questioning.

Mr. BLAINE. Is that good or bad?

Mr. GREEN. I am concerned about you, Mr. Blaine. You used terms that we don't hear a lot of from people in your industry; "fair choice," you used the term "socially conscious," "socially responsible." You indicate that credit unions ought to wear white hats. And then you conclude with "do the right thing."

I will tell you that I read it, I heard it, and I was impressed that someone who is so closely aligned with the industry would use this type of terminology. And I am impressed because I think the American public is currently concerned about what they perceive banking to be all about. I think that the American public is of the opinion that banks don't have a social conscience, that they are not fair, that they are not being responsible at a time when responsibility would be helpful to the public. And I think that they don't believe and perceive banks to be the wearers of whites hats.

Having said that, I will tell you that I don't find overdraft fees, per se, invidious. I think that there may be a means by which they can be utilized and I think that is what we are trying to do today, to ascertain how we do this fairly. And so your testimony was a little bit unusual, given your line of work and given that I rarely hear it here at Congress. And so I thank you for your testimony. It meant something to me personally.

I think that this notion that when you do a person a favor and you charge a fee, and then you want to appear to be the Good Samaritan is a bit much. The Good Samaritan did not charge when he stepped across the street to help the person who had been beset upon by culprits.

It is a rare thing for me to accept the notion that you do me a favor. I come up to the gas pump and you say, let me pump your gas—this happens to all of us I am sure—and once you pump my gas, you say, by the way, that will be $5, but you were doing me a favor. And the question becomes, if you are going to do me this favor and appreciate overdraft protection, I have overdraft protection, can you at least give me notice that you are about to accord me a favor? That doesn't seem unreasonable, to tell me that you are about to do a favor that is going to cost me, by the way. It just seems fair.

I can use my credit card almost anywhere in the world. And to say to me that you can't tell me that when I'm about to go into overdraft, because it is not an electronic device that your company placed in the marketplace, if that device cannot say to me, by way of written word electronically that I am about to go into overdraft—as a matter of fact, it can even talk to me. We have the technology for it to literally say, "Al, you are about to go into overdraft." That technology exists. The question is: Do we want to spend the money on it? And I understand that can be expensive.

But let's talk about a much more empirical experience that I have had, because I think that intent is measured by your overt manifestations, so I am still talking about notice. I want to tell you about a personal experience with notice. I went to the bank and handed a check to the teller. Yes, the check went into overdraft; thank God I had the protection on my credit line. But the teller never said to me, "You are a few dollars over with the check, do you want this to go into overdraft and do you want to pay this fee, which will be more than your actual amount that we are depositing into your account?" Now that kind of notice I just believe a bank can give.

I am not going to say the name of the bank, but this is an actual experience. When the teller would not bother to tell the person who is standing right there in the presence of the teller, you have gone—this will take you into overdraft. It just seems fair to borrow Mr. Blaine's terminology to say to people we are about to do this. The technology exists. I think it can be done.

May I get 1 additional minute, Madam Chairwoman?

Mrs. MALONEY. The gentleman's time has expired. I will grant an additional minute for the panel to respond to your question of why they are not providing that service.

Mr. GREEN. May I pose the question?

Mrs. MALONEY. Sure.

Mr. GREEN. The question is just one of the fairness issue that Mr. Blaine has raised. Is it fair to tell people that you are about to charge an overdraft fee? And I will just start with Ms. Fox and you can go right down the line and be as terse and laconic as possible.

Ms. FOX. Absolutely.

Ms. FEDDIS. Yes.

Mr. HALPERIN. Yes.

Mr. STAATZ. Yes.

Mr. IRELAND. Yes.

Mr. BLAINE. To have a fee market, you must have a free and fair—

Mr. GREEN. Mr. Ireland, could your just speak a little louder?

Mr. IRELAND. Yes.

Mr. GREEN. Okay, thank you.

Mr. BLAINE. To have a free market, it must be free and fair. You can't have one without the other.

Mr. GREEN. I take it that is a "yes?"

Mr. DOLLAR. Disclosure is the key, yes.

Ms. BLOOM. Yes, absolutely.

Mr. COLLEY. Yes, sir. And if you were a member of my credit union and did that, we would tell you that it was going to cause you an overdraft.

Mr. HUNT. Yes, sir, we concur.

Mr. MENZIES. Yes, sir, our members know what our fees are.

Mr. GREEN. Thank you, Madam Chairwoman.

Mrs. MALONEY. Mr. Royce is recognized for 5 minutes.

Mr. ROYCE. Madam Chairwoman, I would like to yield to the gentleman from Alabama for a question.

Mr. BACHUS. I thank Mr. Royce. I wish I could submit a question you all would have said yes to. You were talking about overdraft privileges. It suddenly occurred to me that I think that is what the Federal Reserve Board and the Treasury have given to the "too-big-to-fail" banks. That is one overdraft privilege I wish they had not given. And it is the taxpayers who pay for that when they overdraft.

My first question maybe sounds like a legal question, but I do think it has some ramifications. I will ask Mr. Ireland, and then if any of you want to comment. But this is a legal question, it is not a policy question of what it should be. Is an overdraft charge a loan or a penalty?

Now, let me tell you why I am asking that question. Truth in Lending covers loans, the Truth in Savings Act covers penalties. So it makes a difference.

Mr. IRELAND. Under the Truth in Lending Act, an overdraft fee, as it is implemented by every banking institution I have seen, is not considered credit under Truth in Lending.

Mr. BACHUS. So it is not considered a loan?

Mr. IRELAND. It is not considered a loan under Truth in Lending.

Mr. BACHUS. Is it considered a penalty under Truth in Saving.

Mr. IRELAND. It would be a fee under Truth in Saving. It would be required to be disclosed under Truth in Savings.

Mr. BACHUS. As a fee in the nature of a penalty, I guess.

Mr. IRELAND. I don't know that they have a separate classification for fees that are penalties.

Mr. BACHUS. Ms. Feddis?

Ms. FEDDIS. Well, what they do, Regulation DD as of January 1st will require in every statement for NSF and overdraft fees to be disclosed, some for the month, and then total for the year in every periodic statement. So they will be segregated, but they are not identified necessarily as a penalty. They are identified as overdraft.

Mr. HALPERIN. Mr. Bachus, if I can provide some clarity to Mr. Ireland's statement, the banking regulators have said clearly that when an overdraft is paid, credit is extended. But they said it isn't a finance charge under the Truth in Lending Act because of various restrictions. So it has been called credit, but not a finance charge, which means it is not credit under the Truth in Lending Act, as Mr. Ireland said.

Mr. BACHUS. So it is sort of an in-between type.

Mr. IRELAND. They have called it credit for the purpose of the credit discrimination laws.

Mr. BACHUS. All right. Let me say this. One of the problems that I am having, and I don't speak for anyone else, is there seems to be some confusion on the part of the industry on what happens today and what your capacity is, whether or not you can tell people at the point of sale. And is may depend on the agencies. But I think that is a problem that we are having.

Ms. FEDDIS. Congressman, there is a distinction between opting out as a general opt-out, telling the bank, I don't want you to pay any of my overdrafts. There is another distinction between declining a debit card transaction at a point of sale, just straight-line decline, yes, no. And then there is a third option, which is at the point of sale, to say proceeding with this transaction will cause an overdraft; would you like to proceed? And I think that is what you are talking about.

GAO has looked at this in a study that came out, and it has been suggested. Technically, you can do it, I suppose you can do anything, but it would be a huge cost. Every point of sale—

Mr. BACHUS. Well, yes. I think there is a difference in it being a cost and it not being possible.

Ms. FEDDIS. The New York subway is a lovely system and everything, but if you are—

Mr. BACHUS. I understand. Because of our—and this is, obviously, as all you on the panel know, we lack the expertise that you have.

Ms. FEDDIS. I would never say that.

Mr. BACHUS. Well, I can. It is true. Let me say this, when we passed the credit card bill, some of us knew there would be some consequences, that in a few months, people would get notices that their interest rates are going up or their credit limit is going down. And it is a good thing in some respects. It stops some practices that probably should have been stopped.

But there is always a negative. And I will tell you this when, let me close with this. There is going to be—and the consumer groups and I am convinced you have the public interest at heart. And I do believe the banks and the credit unions—the banks are different from the credit union; there are for-profit institutions. So I think there is a difference, although some of the credit unions do make quite a good profit.

But no matter whether you are a consumer group or a financial institution, I can tell you that having overdraft privileges, not having them and bouncing a check is infinitely a worse consequence that I am not sure that most people appreciate. For people who have money, it is an embarrassment, and it has negative consequences. But for people who are short on cash, it can land them in jail.

Mrs. MALONEY. The gentleman's time has expired.

Mr. BACHUS. Let me just have an additional 30 seconds with unanimous consent.

Mrs. MALONEY. You have taken over a minute-and-a-half. And so I grant you another 30 seconds. That is now 2 minutes over.

Mr. BACHUS. Let me just say—you issue a worthless check, you get a warrant issued against you. It goes on your record. There are some pretty severe ramifications. And I am not sure that the general public realizes that because they have had overdraft privileges. I am not saying that it was very costly—it encouraged a lot of—that it was to their benefit but to issue worthless checks has terrible ramifications.

Mrs. MALONEY. The gentleman's time has expired.

And certainly the intent of the legislation is not to take away any services from consumers but allowing them to decide which services they want. For example, there could be alternatives, such as a line of credit. Some people may decide that they would like the overdraft protection, but others do not.

I would say that one of my bills, which was very hotly contested by the industry at one point, was merely a notice at ATM machines that there was going to be a charge, $1.50 charge or whatever the charge was, so that consumers would opt-in and say, yes, I want that service. And it now is the law, and at every ATM machine, they let the consumer know that they will be charged for the service if it is not their home bank. I very gladly pay this fee when I am in Washington so that I can access my bank.

We are just saying, for the services that you provide, let the consumers know and let them decide whether or not they want the service. And if they want to pay $35 for every overdraft, then let them opt-into the program for the service.

Mr. Cleaver is recognized for 5 minutes.

Mr. CLEAVER. Thank you, Madam Chairwoman.

Let me just start off with this. Will all of you who support this legislation just raise your hands? Okay. Let me just, before Thanksgiving, express appreciation to all of you who oppose the legislation. Those who oppose the legislation are really helping me, and I appreciate it.

The banks right now are preventing the Nation's ire from falling on Members of Congress. I think as long as you can continue to do this, it helps us. Thank you. You successfully bypassed us as the most hated group in America, and I think that just personally, I want to express appreciation.

Do those of you who oppose the legislation believe that what is going on, what the overdraft policy is, is the morally right thing to do?

Excuse me?

Mr. MENZIES. Could you restate your question? Did you ask, Congressman, if we believe that it is immoral to offer overdraft protection services to our customers?

Mr. CLEAVER. Yes, I guess you can rephrase it that way.

Mr. MENZIES. I would respond to you that it is not only not immoral; it is fair, reasonable, responsible relationship customer-driven, based on taking risks with people whom we know and we live with and we see in our bank every single day.

Mr. HUNT. And I do believe it is the right thing to do, to do everything we can to make sure a person is able to pay their house note, to pay their car note, to purchase food at Burger King using a debit card.

Mr. CLEAVER. So you are able in realtime to tell a person whether or not he or she has money in the bank and give them the opportunity to withdraw their transaction, but you don't do it because you make money, and that is the right thing to do?

Mr. HUNT. That is not—being able to tell someone's balance in realtime is not entirely correct. There is only one person who knows how much money you have in your account, how many checks you have written, how many items you have actually purchased. Just because a person is authorized to purchase an item, it doesn't mean they actually purchased it. And we try and provide technology so you have the right information, possibly on your Blackberry right now, you can find out your account balance.

Mr. CLEAVER. So when someone uses a debit card at Macy's, and Macy's runs the check through the machine, you are saying that the machine cannot tell Macy's whether or not the person seeking the transaction does in fact have money in the bank?

Mr. HUNT. What that machine would tell the merchant is that this person is authorized to make a transaction.

Mr. CLEAVER. That is not what—no.

Mr. HUNT. The answer to your question is "no."

Mr. CLEAVER. No, you didn't. You answered somebody else's question because the question I am asking is—the bank has the ability in realtime to say whether or not there is money in the bank, right?

Mr. HUNT. The bank has the ability with—if the merchant has the technology—that is another thing we haven't discussed. We don't know if the merchant has the technology. It is not a one—

Mr. CLEAVER. I know you think you are answering my question, and I don't like to—

Mr. HUNT. I am just trying to answer.

Mr. CLEAVER. And you are a nice person. What I am saying is, you are not answering the question. Let me just—if I am walking into Macy's and write a check, and they run it through the machine, will the merchant see that I have money to make the purchase?

Mr. HUNT. Not at all times, no, sir. They don't. Sorry.

Mr. CLEAVER. What do they see?

Mr. HUNT. They run the debit card through their machine.

Mr. CLEAVER. What do they see?

Mr. HUNT. They don't see anything. They just look at the cash register and see if you are approved or not approved for this transaction. They don't see that you have $123.

Mr. CLEAVER. No. Okay. But what does the bank see?

Mr. HUNT. The bank sees a request from the merchant for a certain amount of money. The bank has already basically predetermined whether you are going to be eligible to make a purchase or not.

Mr. CLEAVER. So the bank doesn't pay any attention to what your balance is? They make a predetermination that whatever comes through here, we are going to pay?

Mr. HUNT. Here is what the bank has done. The bank has looked at your history. They have looked when you are going to get paid again, and they are going to see if you are a good customer of the bank. And if they have seen, sir—

Mr. CLEAVER. In a matter of 5 or 10 seconds, the bank is going to look at your history, look at whether you treat your dogs nicely? All of this?

Mr. HUNT. We do that every day, sir, every day.

Mr. CLEAVER. In 5 seconds?

Mr. HUNT. Sir, they do it all the time based upon your records.

Mr. CLEAVER. I would love to take some cameras from news agencies, go in the bank with you, and see that happen.

Mr. HUNT. Sir, we would love to host you in your district to show you what a bank goes through every day.

Mr. CLEAVER. Would you host me and some national television cameras to come in the bank and do that? I think we can solve this problem and kill Mrs. Maloney's bill. All we have to do—let me have somebody in Macy's. I am with you and the cameras and we are on TV right now—we have a chance right now to fix this deal. We are going to fix it. Do we have an agreement?

Mr. HUNT. Oh, yes, sir, we have an agreement.

Mr. CLEAVER. We have an agreement. I am through—I am going to work this out.

Mrs. MALONEY. Mr. Perlmutter is recognized for 5 minutes.

Mr. PERLMUTTER. I am not sure how to follow that. I think—and I agree with Mr. Posey. I just appreciate the panel's testimony today.

There have been different opinions, some very strong terminology, strong feelings, strong ideas.

And the underpinnings of all of this are, allow business to engage in commerce, expect people to act as adults and have personal responsibility.

But then within the Constitution, we understand there are limits to that, and we have the bankruptcy section of the powers given to the Congress, and we have no involuntary servitude. So there is an understanding by the Founding Fathers and Mothers that people can overdo it, too, that they don't—they are not going to become indentured servants.

So what we have here is really a benefit, and Mr. Bachus and I were talking about it, which is to cover overdrafts so that people don't get bounced checks, don't get treble damages, don't get potential warrants, don't get denied in bankruptcy to try to get rid of that particular debt.

But on the other hand, these things get to be very seductive and can really run up—Ms. Bloom, I think you gave some anecdotes.

And Mr. Hunt, I know you objected to anecdotes.

The trouble is, Mr. Bachus says we may not have much expertise, but I can tell you we have a lot of experience. And my experience with my daughters—I have my nephew here today. Now, thank goodness, he can do a little better than at least one of my daughters has done. But the anecdotes there are a $6.50 cup of coffee at Starbuck's. She had $4.50, apparently, in her account; $2 overdraft, $35 charge. And if it had only happened a few times, that would be great. So we said, no more of this; you have to be on a cash and carry.

My youngest daughter, she is cash and carry. It has been very successful for her. My middle one, though, we went back and said, can we get a line of credit for $1,000 so that this doesn't happen? They said, no, she doesn't qualify for a $1,000 line of credit, but we will give her an $8,000 credit card. Okay?

So we have to watch the practices here. And I guess my question really does come back to point of sale, because it seems to me that debit cards really are becoming the convenience, but people are paying for that convenience. What started out as a courtesy becomes a profit center. And this happens in all kinds of businesses, not just banking. But we have to watch so that the Abby Perlmutters of the world aren't always paying that $35 fee and can never catch up.

So, Ms. Feddis, I appreciated your testimony. I think really Mr. Cleaver's questions about, can we address this—let us say, in my family, we say, no, if you don't have any money, boom, that debit card, it just stops; you are going to be embarrassed. Or at that point of sale, yes, you are going to overdraw, and you are going to pay a fee; do you really want to do that? I want to know, do we have the capacity? Is the technology there to do that?

Ms. FEDDIS. Certainly, the capacity to opt-in when you open the account or at some point, that is certainly something that is doable.

With regard to giving somebody the option at the point of sale, that technology, as the GAO found as a practical matter, isn't really available. It would require upgrading or replacing every point at the millions of point of sale terminals. It would require going into the networks and creating extra tracks. I am not an operations person, but you would have to do something to be able to carry—to have the capacity to carry that extra information.

In your case, it is probably just better if that person opts out and says, I don't want to ever have my debit card turned down. To the degree the bank knows that there are insufficient funds, even with debit cards, it is not a realtime situation. There will still be debit card transactions that will overdraw the account that the bank can't stop.

Part of that is the exact sort of transaction you are talking about. Small dollar transactions, a lot of times the merchants, to save time and money, they swipe the card to ensure that it is a good card, but they don't actually take that extra step to ensure—to get an authorization from the bank, and the bank doesn't learn that you have drunk that coffee until the next day. And as a practical matter, they can't return it at that time.

So those—but you could still—the bank could say, no, to the degree we stop them, and we just won't charge you, that is probably what your daughter should do, is just opt-out of the whole thing. Doing it each transaction is probably as a practical matter just not doable. GAO did look into that.

Mrs. MALONEY. The gentleman's time has expired.

And within the bill, there is another study required to look at point of sale and how the technology is progressing to allow us to do that. At one point, they did not have the point of notification on the ATM machines. Of course, now, they do. So we will look at it and go forward. Mr. Royce is recognized for 5 minutes.

Mr. ROYCE. Yes, thank you, Madam Chairwoman.

I would like to go to Mr. Dollar because he is the former chairman of the National Credit Union Administration. So he would know something about how regulators look at this situation of having customers who routinely commit over—who are basically underwater or creating risk. If it is the case that the regulator forces the institutions to set aside 60 percent in these cases to handle those accounts, to handle individuals with this proclivity to overdraft their accounts, wouldn't that imply that there is some risk involved for the institution?

Mr. DOLLAR. There is no question, Congressman, that there is risk. And that is the reason why the regulators allow the institutions to be able to not only charge the fee, but require them to reserve 6, 7—not 60, but 6, 7 or 8 percent, somewhere—

Mr. ROYCE. So it is 6, 7 or 8 percent.

Mr. DOLLAR. On average, some as little as 5 percent. Perhaps some as much as 10 percent. But, yes, there is risk there in answer to your question. And that is why the regulators do require that. And as I said in my testimony, perhaps it is because I am a former regulator, but I believe that the best arena to deal with abuse in this issue is through the regulatory arena, rather than statutorily. I think that it is able to reflect—the regulations are able to reflect the changes in the marketplace, the changes in technology, the changes in just the consumer perceptions of these issues as they move forward. I think the Federal Reserve and the Federal Financial Institutions Examination Council have taken the lead on this. They are taking it seriously, and I think that their new rules and guidelines, their regulatory requirements should be allowed to work.

Mr. ROYCE. I guess the question—if the credit union is only going to be able to pass on the cost of processing the transaction and if you have an 8 percent cost in terms of the risk, why would they ever offer the overdraft protection? Because they would be bearing the risk that a customer will not settle their balance, basically 8 percent of the time on average, and they can't be compensated for assuming that risk. So they would be better served by ending the overdraft protection under that scenario.

Mr. DOLLAR. I think that for many of those members who were mostly to take a loss, they would simply close their accounts. So there would be a ramification for them.

But another point here quickly on bringing this under Truth in Lending that has not been discussed today is that federally chartered credit unions have a statutory, again, a problem of the statutory requirement, rather than leaving it regulatory, have a statutory 18 percent usury cap. Therefore, if you were to place overdraft protection under Truth in Lending, every Federal credit union in the United States of America would not be able to approve 6 per year as the law indicates. When they approved the first one, they would be in violation of the Federal usury laws. So there are unintended consequences that I think have to be taken into consideration with this legislation.

Ms. FOX. Mr. Royce, may I add to that?

This bill specifically excludes the credit union usury cap for coverage under this bill. The bill requires the Federal Reserve to take into consideration what it costs for a financial institution to pay an overdraft when they set the guidelines for what is a reasonable fee.

Mr. ROYCE. Right. And I am looking at the risk element of this, and I am wondering, at the end of the day, why would banks and why would credit unions really continue to offer these programs if on the risk side, you are not able to be compensated for assuming that risk? And I guess the thought I have in this is, what is likely downstream? If you do have that action out of banks, credit unions, then the loser is going to be the type of individual who would most be likely to utilize routinely overdraft protection; who would be the type of individual who might not notice the accelerator clause in his mortgage, and suddenly he doesn't have that overdraft protection anymore, and now he has been late on his mortgage check, or he is the type of individual who is going to end up being dinged not by only the merchant and the bank but, in the most egregious cases, by the district attorney as well. He is going to have all of these charges to bear because we have created a scenario where the banks and the credit unions are not going to offer the overdraft protection or are going to close the account.

Mr. Dollar?

Mr. DOLLAR. The regulators see the benefit. They also see the risk. That is why they are regulating it. They are regulating it, I think, very well. There is certainly some additional scrutiny that should come. We have discussed some of those aberrations here. They are, however, the exception rather than the rule. But there is risk. There is moral hazard in not finding a way to discourage the writing of bad checks, and there are the additional costs that you have mentioned, Congressman, that are very real.

And that is the reason why there is some disconnect when folks say that consumers do not like this product, but yet the financial institutions are making a lot of money on it. Some way or another, there must be some consumers seeing some value in this product or else they would not be the earnings that there is. The answer, again, is disclosure and making sure those members know, through financial education and through proper disclosure, how this program works and have the right to opt-out of it if they do not agree.

Mr. ROYCE. Thank you, Madam Chairwoman.

Mrs. MALONEY. Mr. Himes, for 5 minutes.

Mr. HIMES. Thank you, Madam Chairwoman. I want to follow up on something Congressman Perlmutter said, the sort of concept of the profit center. I think we have four CEOs, presidents of banks and credit unions. Could I ask you each to quickly give me a sense for what the profitability of the overdraft business in fact is? And I am happy to take an answer in terms of return on invested capital or margin or whatever makes sense. I am also happy to take an estimate. Can we just start with Mr. Staatz, I guess?

Mr. STAATZ. I don't have those numbers with me here today, but a part of our—in our charge is not to cover costs; it is also somewhat of a penalty to try to discourage people from using it.

Mr. HIMES. Mr. Blaine?

Mr. BLAINE. Congressman, the profits are obscene. And I will give you an example. If these fees were correctly disclosed under Truth in Lending, everybody agrees that their interest rate would be at about 300 percent. Even with a 10 percent write-off, as Mr. Dollar just mentioned, the return to the banks and credit unions is 270 percent. This is a no-lose proposition for the banks; a definite loss for consumers.

Mr. HIMES. Mr. Colley, do you have a margin or return on investment capital number for me?

Mr. COLLEY. I don't have that information with me, sir. I would be happy to get it to you later.

Mr. HIMES. Thank you.

Mr. Menzies?

Mr. MENZIES. Congressman, we measure profit based on return of total relationship, not just of the payor overdraft protection programs, the total relationship. All loans, all deposits, the total relationship.

Mr. HIMES. But surely you break these businesses out, you need to be able to evaluate their relative profitability. You break them out, no?

Mr. MENZIES. I hate to admit, at a $150 million bank, we don't run ROE, ROA returns on specific products. I am sure we should, but we don't. We look at the relationship, the total profitability of the relationship.

Mr. HIMES. I am really not trying to make a point here. I was just curious about the profitability. I think if the four of you would be willing to follow up with just your best estimate of how profitable a business this is within your institutions, it would be, I think, very helpful to us.

Look, philosophically, I tend to believe that if you have good disclosure and smart choices being made, that we should be very light-handed with respect to what products are offered. This is a special case, though, because it represents a moment in which a household or an individual transitions from having assets to having liabilities. And we had a pretty unenlightening discussion down here and in the media about what caused the meltdown we are in right now.

Everybody blames it on CRAs, Fannie Mae, or the investment banks. And there is a grain of truth in much of that. And the reality is, of course, we have all sorts of factors. What we don't talk nearly enough about is the incredible increase in leverage in the American household. You know the numbers. The last 20 years, most households moving from net asset positions to very substantial leverage. And that makes all the difference as we go into one of these things.

And again, I appreciate that if you have—Mr. Dollar, you say if you have good disclosure and good decisionmaking and conscious decision making in the face of perfect information, fine. But here is the moment where somebody's account goes below zero, and they are now going into debt. So I think we have a public interest, given how important the leveraging of the American household, the irresponsible behavior—I am not blaming you—the irresponsible behavior of many American households in accumulating a lot of debt, using homes as ATM machines, etc.

These products can facilitate that. And so despite my philosophical leanings, I do want to look hard here. And my question is, why not an opt-in? Let us give everybody perfect information and let them make an affirmative choice, and if they have gotten that information, good disclosure, make an affirmative choice. I don't get the opposition to that because opt-out we all know. We all live enormously busy lives. We all know that moment very rarely presents itself where you say, from 10:30 to 11:00, today, I will read my agreement with my bank, and I will make an affirmative choice. That just doesn't happen. Why the opposition to opt-in?

Mr. STAATZ. Congressman, we don't have opposition to opt-in. Certainly on a go-forward basis. As a matter of fact, it would merely put into place what most credit unions do anyway.

Mr. HIMES. Does anybody oppose opt-in? I saw in the testimony here.

Mr. DOLLAR. Congressman, I contacted and have over the last several months when all this publicity came, about a number of the credit unions that I work with, and there is not a credit union that I had spoken with that has a problem with opt-in going forward and a very well disclosed opt-out option for existing accounts. I think that opt-in going forward would be very well received by responsible financial institutions.

Mr. BLAINE. Congressman, our organization manages 800,000 checking accounts for individuals. We offer only opt-in. We have for over 25 years; 80 percent of our members are covered by overdraft by their choice. They are allowed to use their other savings, other checking, money markets, CDs, credit card, line of credit, whatever.

Every one of those choices is wildly less expensive than overdraft that is being proposed. And the only people that we cannot qualify for reasonable overdraft protection are those who are not credit worthy. And those are the people who are most often taken advantage of by courtesy pay.

Mrs. MALONEY. The gentleman's time has expired.

Some members have asked for a second round, so I am recognizing myself for 5 minutes.

And I would like to ask Jim Blaine—I am really struck and fascinated by your fee structure for your credit union. In your testimony, you note that you charge 50 cents to transfer funds for overdraft protection. And in the Overdraft Protection Act, there is language that says that financial institutions can only charge fees that are reasonable and proportional to the cost of processing the transaction; 50 cents seems to me to be very reasonable compared to a $35 fee that many financial institutions charge for the same service. Can you tell us how your credit union arrived at the 50 cent figure?

Mr. BLAINE. Madam Chairwoman, it is a sophisticated process that we employ. Actually, it is a nuisance fee. We would rather that our members do it for free by going online, so we have very conservative, careful members, and believe it or not, many of them will do it themselves to avoid that 50 cent fee. But in an automated world, the incremental cost of doing those transfers is a matter of pennies. It covers our costs easily.

Mrs. MALONEY. Well, thank you.

Then the difference between a 50 cent fee and a $35 fee is obviously very, very striking. So why do you think there is such a huge difference between the credit union practice and one that serves its customers very well—you said you had 800,000 customers you said or 800,000 customers—and the practice of larger banks to charge an average of $35 fees?

Why do you think there is such a large discrepancy, Mr. Blaine?

Mr. BLAINE. Madam Chairwoman, I believe that is why we are here today.

Mrs. MALONEY. That is why we are here today.

Mr. BLAINE. But I would say, going back to a previous question, if they offered courtesy overdraft at Burger King, I think the question would be, where is the beef?

Mrs. MALONEY. Okay. I would like maybe Ms. Feddis to answer or Ms. Fox.

Ms. FEDDIS. I think I might be confused. The 50 cent fee isn't for the overdraft. Is that correct? Or is it for transferring money from a savings account, which is very different? Many banks do that for free. Usually, it is $5 or $10. You can pay somebody to make your coffee, or you can make your coffee yourself. So with the banks in terms of transferring funds from the savings account to the checking account, sometimes that is for free in some banks; sometimes it is $5 or $10.

Mr. BLAINE. Madam Chairwoman, Ms. Feddis has caught me. The 50 cents is a transaction fee. The cost of the overdraft is zero.

Mrs. MALONEY. The cost of the overdraft is zero. Okay. It is a transaction fee. The cost of the overdraft is zero. So there is a big difference between a zero and a $35 fee.

Ms. Fox, would you like to comment on it? Or Mr. Staatz and others?

Ms. FOX. The larger banks charge $10 to transfer your own money from your savings account into your checking account to cover an overdraft and if I recall correctly, your bill would have the Federal Reserve look at whether that fee is also reasonable and proportional because that makes even covering your overdraft with your own money still a fairly expensive transaction.

Mrs. MALONEY. Mr. Staatz?

Mr. STAATZ. I wanted to just clarify, for example, we don't charge anything when you are transferring your own money. And as others—some of the credit unions—as Mr. Blaine does, may charge 50 cents or a little bit more, but we don't charge anything for your own money.

Mrs. MALONEY. For your own money.

Mr. Menzies or Mr. Hunt, would you like to—

Mr. HUNT. Sure, I would, Madam Chairwoman.

Mrs. MALONEY. Why is there such a large difference, a discrepancy between a 50 cent transfer, a $10 transfer, a $35 overdraft fee?

Mr. HUNT. Sure, Madam Chairwoman. I will also tell you that I have never heard of any of our banks charging you money to transfer your own money from one account to another. I am a little bit confused by the gentleman to my right about whether that is a line-of-credit fee or a strict overdraft fee. Same thing here. If you do have a line of credit with one of our CBA bankers tied to your savings account, we charge a minimal fee of probably $3. Many of our banks charge zero if you have that line of credit.

Mrs. MALONEY. Would you like to clarify for him, Mr. Blaine?

Mr. BLAINE. I am not certain what the question is. The only overdraft or NSF fee we have is a $12 NSF fee that has been the same fee for over 20 years. And it is more than sufficient to cover not only our processing costs but all the fraud and other losses that are incurred in our 800,000 unit checking program.

Mrs. MALONEY. There seems to be a huge discrepancy between some institutions and others. And I thank you very much for your service to your customers, Mr. Blaine.

The Chair recognizes Mr. Green for 5 minutes. My time has expired. Excuse me. Mr. Posey.

Mr. POSEY. Thank you, Madam Chairwoman. There is definitely some good stuff in this well-intentioned legislation that is being proposed and worthy of further consideration for sure. But some of this stuff that gives me reason for pause, for example, is, under Part J, a depository institution may charge not more than 1 overdraft coverage fee in any single calendar month and not more than 6 overdraft coverage fees in any single calendar year per transaction account. You wonder what would happen then if somebody had 12 overdrafts in a year, 6 of them were free; would they take that maybe as an inference that they don't need to pay it or they shouldn't be responsible for it?

And the question that begs for an answer is, who would, even if the fee was exactly matched to the loss and to the administrative cost, who would then pay for the abuse, the 6 abuses that were not allowed to be charged back to this customer? And I am afraid the answer is the 99 percent of the customers who do not abuse the privilege of having a checking account.

Stealing is still stealing. I hope Congress is not trying to change that fundamental right. When you tell somebody, you give me this and I will pay you for it, and if you don't do it, that is called theft. If it happens at McDonald's or Burger King or anywhere else, you make an obligation; there is a moral obligation, I think we all believe, to hold up your end of the bargain.

And if I get you to loan me money and then say that I am going to pay you back and I don't in fact do it; if I give you a bad check, that is stealing. And there have been penalties for that, I am sure, in every State and severe penalties where the amounts are severe. So I hope that Congress is not trying to and cannot minimize the necessity of having responsibility to pay your debts.

And I hope that we are not trying to, by lowering the consequences in the interest of consumer protection, we are not trying to lower the consequences of bad behavior, which is what caused us to be in the major economic recession that we are in now. Sometimes, the cure is worse than a disease, and I wonder if some components here are not a cure in search of a disease.

It is laudatory that Mr. Blaine has 80 percent of his customers signed up for overdraft protection. That leads me to suspect that most consumers enjoy knowing that if they should inadvertently—hopefully—make a mistake and can't cover their last check, that there will be an opportunity for the institution to step up. I would be interested in knowing how often you have to exercise that overdraft protection.

Mr. BLAINE. Congressman, I agree with you.

The essence of our program is, it is an opt-in, and as you say, if you give the consumer a choice, they will make the right decision. But giving them the choice is very, very important. We have about 9,000 potential overdrafts every day. So it is a very, very large number, and if you would multiple that by $35, then you understand what is at risk in terms of income to institutions, why there is such a strong discussion.

One other point, in terms of the number of once per month or 6 per year, as I understand this legislation, you are trying to strike a balance between the number and the proportional fee, and the truth is somewhere in between. But you have to keep the two together when you do the legislation to make it more reasonable.

Mr. HALPERIN. Congressman, if I could add, under the legislation, there is no requirement that institutions continue to cover any transactions after the sixth limit. So in response to your question about whether institutions would be forced to cover transactions without a fee, the legislation would allow institutions then to deny those transactions, which I think is a more effective deterrent and a more effective encouragement for personal responsibility, which you have called for today, than allowing transactions to go forward without a fee.

The most effective deterrent is denying the transactions. And at six—under the current system, there seems to be a misunderstanding that the current system actually covers all payments. In fact, even under the current e-based overdraft system, people do get denied if they reach their maximum limit on a negative. For example, some banks have a negative $500. And that could just as easily be your mortgage payment or your rent payment or that important thing, and you were driven down there by your small debit card. So we are not in a world now where everything gets paid. But just to be clear, the bill certainly does not require institutions to continue to pay and not charge a fee.

Mr. BLAINE. Congressman, we very much support personal responsibility, too. We are all fully behind it. One of the innovations we are adding later next year is we all have mobile phones now, cell phones, smart phones, and we will actually text our members early in the morning. We process at night. And we know if there is a potential overdraft, and we will contact you if you are a member and say you need to come see us before 5:30 to give them a second chance because it is a very busy world, and most folks will do the right thing and come in and avoid those fees. If not, we have no compunction about punishing them severely.

Mr. POSEY. Do you find competitors following your business model?

Mrs. MALONEY. The gentleman's time has expired, and he is granted an additional 30 seconds for Mr. Blaine to respond.

Mr. BLAINE. I think banks and credit unions are good people, and they do want to serve their customers and members well, and as these technologies become available, they will try to help their customers and members.

Mrs. MALONEY. Thank you very much.

And Mr. Green is recognized for 5 minutes.

Mr. GREEN. Thank you, Madam Chairwoman.

I concur with Mr. Blaine. I think that banks and their employees are good people, and I sincerely do believe that you want to serve your customers well.

I do note, however, that the interests and fees that were at one time charged on one check, as I understand it, perhaps one, and correct me if I am not correct, at one time you would pay not only the fee but the money that was placed in your account, you paid interest on that as well. Is this true?

Ms. FOX. In the way the big bank fee-based overdraft works, if they permit an overdraft—

Mr. GREEN. Excuse me. Let me intercede because time is of the essence. I believe Ms. Feddis broached the issue when she explained that the Fed no longer allows that.

Is this true, Ms. Feddis?

Ms. FEDDIS. No longer allows what, sir?

Mr. GREEN. No longer allows a fee as well as interest on an overdraft.

Ms. FEDDIS. I didn't say that, sir.

Mr. GREEN. You did not? What did you say? I am sorry then.

Ms. FEDDIS. I have said a lot. I often repeat myself.

Mr. GREEN. I know you did, but let us just focus on this one area.

Ms. FEDDIS. Can you ask the question again? I am not sure what you are talking about.

Mr. GREEN. Let me ask the question. If you have an overdraft and there is a fee paid, let us say $35, and "X" number of dollars are placed in the account, do you get interest on the "X" number of dollars as well as the $35 fee?

Ms. FEDDIS. Interest on the $35 fee.

Mr. GREEN. The money that is placed into the account to cover the overdraft.

Ms. FEDDIS. At that point, it would be just to bring the balance to zero. So there wouldn't be any interest paid.

Ms. FOX. No. It is just a fee. But a lot of the banks charge a second fee if you have not paid for the overdraft and the overdraft fee in 3 to 5 days.

Mr. GREEN. Let us take this example. This will help. Let us assume that you—that $100 is required to go into your account to cover the overdraft amount. A fee of $35 is imposed. On that $100, do you pay interest?

Ms. FOX. No. No, sir.

Mr. GREEN. Did you ever pay interest? Did banks ever have the option of charging interest on the $100?

Ms. FEDDIS. That is in the checking account?

Ms. FOX. Only if they had an overdraft line of credit where they were charging interest on the amount that you borrowed. And typically banks charge about 18 percent annual interest if you cover an overdraft with a line of credit.

Mr. GREEN. Ms. Feddis, you were about to—

Ms. FEDDIS. I think we are getting there. The line of credit, if that is used to cover the overdraft, interest will be charged on that line of credit. If it is covered by an overdraft with an overdraft fee, there wouldn't be interest charged.

Mr. GREEN. And there has never been an instance or circumstance at any point when banks were charging both the fee and the interest?

Ms. FEDDIS. Not that I am aware of, if I understand the question.

Ms. FOX. There are a few banks that charge a transfer fee for you to access your line of credit, and in that case, you would pay a flat dollar fee plus the 18 percent interest.

Mr. GREEN. So you pay the transfer fee?

Ms. FOX. But it is not as big a fee. It is just a transfer fee.

Ms. FEDDIS. That is also, again, the line of credit, not the overdraft. We are talking about two different products.

Mr. GREEN. Right. If you have a line of credit, the line of credit charges you, and then you pay the overdraft fee as well.

Ms. FOX. No. Transfer fee.

Mr. GREEN. Transfer fee. How much is a transfer fee versus the overdraft fee?

Ms. FOX. For the largest banks, transfer fees start around $10, and the overdraft fees are $35 for the initial overdraft; at some banks, $35 in another few days.

Mr. GREEN. Mr. Blaine, if I may, you charge 50 cents for your transfer fee?

Mr. BLAINE. That is correct. And to finish out your thought, it may go to our members' Visa card with the credit union on which we charge 9.7 percent. So we do not charge an overdraft fee because we are charging interest on the line of credit.

Mr. GREEN. Somebody else wants to speak.

Mr. HUNT. We have to make this point very clear. If you have a line of credit, you do not pay an overdraft fee. That is why you have the line of credit. That is the beauty of a line of credit; there is no overdraft fee. So some banks do charge anywhere from $3 to $10.

Mr. GREEN. Can I just intercede? The lack of beauty is that you charge a transfer fee when you are charging me to take money out of one account that I have and place it in another account that I have. Do you find beauty in that as well?

Mr. HUNT. I do in the fact that it is better than paying the $35 fee in that we had to set that up for you and there was expenses behind the initial setup.

Mr. GREEN. So you—

Mr. HUNT. The beauty would be if you transferred money before you had an overdraft. That would be the beauty and there would be no charge for that.

Mr. GREEN. That would be the beauty it of. But then if I am not aware, and I should be—I guess sometimes you don't know when you need the help and you render the help. But—

Mr. HUNT. And I have needed help before.

Mr. GREEN. So have I. So have I.

To close, let me share this with you. I don't find overdraft fees to be repugnant, per se. My concern is that you don't give the consumer the notice. I think notice is important to consumers, and if we can get the notice—notice—assuming that I am about to go into overdraft, if you can give me the notice at that point—remember the statement about being in a bank also with the electronic devices. We can give consumers notice so that they can opt-out at that point and say, well, look, I really don't want to pay that overdraft fee at this point. I happen to have money in my pocket and I will cover it. There are all sorts of options available once you know what the consequences are. And I find that to be an acceptable solution.

The final comment would be this. With reference to the manipulating of the order of the transactions, do you agree that it would be fair not to manipulate the order of transactions in an invidious way, such that people find themselves, if the order had been in a different fashion, wouldn't pay as much?

Mrs. MALONEY. The gentleman's time has expired, but he is granted an additional 30 seconds for Ms. Fox to respond.

Ms. FOX. Absolutely. Consumers think it is just outrageous for their banks to order withdrawals in a way that maximizes the number of fees. That is viewed as extremely unfair.

Mrs. MALONEY. Thank you. The gentleman's time has expired.

Reverend Cleaver is recognized for 5 minutes.

Mr. CLEAVER. Ms. Feddis, are you familiar with a recent article in USA Today by a consultant advisor to large banks on credit cards, Mr. Brad Nickum, N-i-c-k-u-m. He wrote an article, and he said, "profits, not costs generally drive bank fees." Brad Nickum, consultant advisor to large banks on credit cards.

Ms. FEDDIS. I would suggest that, for any business, costs and profits drive fees. The point of a business is in basic business theory that income has to be higher than expenses.

Mr. CLEAVER. No. I am sorry. He is saying that profits from these fees, the profits from credit card—that—I am sorry—that banks charge on overdrafts is what drives—

Ms. FEDDIS. I am sorry. I misunderstood. The costs are certainly part of it. But part of the purpose of an overdraft fee is to serve as a penalty. And like any penalty fee, whether it is the IRS—

Mr. CLEAVER. Penalty of what?

Ms. FEDDIS. A penalty to encourage people, to get their attention and say, please, pay attention to your account.

Mr. CLEAVER. What about slow learners?

Ms. FEDDIS. That is a very good point. The vast majority of people manage their credit—their checking accounts very well.

Mr. CLEAVER. I am sorry. Mr. Blaine, did you say 9,000?

Mr. BLAINE. Per day. That is correct.

Mr. CLEAVER. That is a lot of folks. That is $315,000 a year; $35 per check would be—

Ms. FEDDIS. I am just getting to the point that the group you are talking about, which is the vulnerable group—most people manage it well.

Some people, as has been discussed today, are deliberately using the overdraft as their cash management, particularly small businesses because they can't get a loan or they don't want to get a loan. They are okay. There may be a vulnerable group. So, yes, we should protect them. But maybe we need to face the fact that some people maybe shouldn't have a full-service standard checking account. Maybe they need something else that is more suited to them.

Mr. CLEAVER. I agree with you. So why do you let them have the checking account and then charge them $35?

Ms. FEDDIS. I think what you need is something like a payroll card which is very popular with people. The only deposit allowed into it is the payroll. They only access it through a debit card. It is overseen by the employer. It is very popular.

Mr. CLEAVER. So it would work in realtime?

Ms. FEDDIS. Well, there will be overdrafts. It won't be for the reasons that I have discussed before. There can be because it is not possible for the bank to stop every overdraft, and it is not realtime, as you pointed out.

Ms. FOX. Mr. Cleaver, when a bank decides to lend money to consumers by letting a debit purchase go through that should have been denied for lack of funds, the fee is not a deterrent; it is a profit center. If the bank wanted to deter overdrafts, they would prohibit a debit card from overdrawing at the point of sale or at the ATM machine.

Mr. HALPERIN. Mr. Cleaver, if I can just add, we have that account, the account you are talking about. It was when the debit card didn't allow you to overdraft. So instead of driving people out of the banking system by charging high overdraft fees, why don't we bring back the debit card as the tool to only spend the money you have and give consumers the tool to be able to tell that debit card that it can't be turned into a credit card?

Ms. FEDDIS. But there are times when some people do want their debit cards—excuse me.

Mr. CLEAVER. No hitting, no hitting.

Ms. FEDDIS. It is okay. They do want their overdrafts paid. And give people the choice, as you point out, that, yes, in a perfect world, everybody would have enough money in their account, but sometimes they don't, and they need the medicine, or they want the groceries paid, or they want the meal that they just ate to be paid for. So give people the choice. And if there is another group that is a small group who is vulnerable, let us focus on them, but don't deny everybody else the choice.

Mr. CLEAVER. The choice to pay extra money?

Ms. FEDDIS. If it is their choice.

Mr. HUNT. To cover their bill, yes.

Mr. BLAINE. Representative Cleaver, I hope you have at least 8 spaces on your calculator, because 10,000 overdrafts times $35 is $350,000 a day. And that is just one of the advantages of participating in a credit union when you don't have to pay those kinds of fees.

Ms. BLOOM. If I might add, my experience with consumers is they get trapped in this cycle and that these—I mentioned some examples from stories we have heard, people just get into this cycle and it is 7, 8, 11 fees wrapped up within a 2-week period. So it is—and they don't really know until it is too late.

Mr. CLEAVER. I agree. Because it is similar to Johnnie's Check Cashing Company on the street corner.

Mrs. MALONEY. The gentleman's time has expired. I will grant him another minute for his closing question.

Mr. CLEAVER. Yes. What I think is difficult to explain is a report that appeared in a real estate group's publication where a customer with a $500 balance made 4 debits in the following order: $15, $10, $150, and $450. Three overdraft fees could be charged instead of one by posting the largest transaction first, right?

Mr. HUNT. Yes.

Mr. CLEAVER. Why doesn't that happen?

Mr. HUNT. Sir, I will tell you this. Of all the issues discussed in this bill and in all the meetings I have had across the country, the most challenging question that I get from retail bankers, especially retail branch managers is, what do they post first? If they pay the highest amount, then they get criticized for charging overdraft on the three lower amounts. If they take care of the three lower amounts but don't take care of the mortgage, they get criticized the same way. So it is a great question. No one has the solution to it. We do ask this of you, if this legislation is enacted, when you write the regulations, be crystal clear; what do you want the banks to do? Do you want the banks to go high-low or low-high?

Mrs. MALONEY. Thank you.

The gentleman's time has expired. And the bill is crystal clear; it says that the order of checks cannot be manipulated in order to get a higher overdraft fee. So it goes with higher to lower.

I would like to thank all of the witnesses. This has been incredibly interesting.

Many members were not able to be here because there are not votes today. They are invited to submit their questions in writing. And without objection, we will have an additional 30 days for members to submit questions to the witnesses and to place their responses in the record. Thank you again. This meeting is adjourned.

[Whereupon, at 12:33 p.m., the hearing was adjourned.]

A P P E N D I X

October 30, 2009

Testimony of Jim Blaine, CEO of State Employees' Credit Union
U.S. House of Representatives Committee on Financial Services
"The Overdraft Protection Act of 2009"

Good morning: My name is Jim Blaine, and I'm the president of the State Employees' Credit Union of North Carolina. Thank you for the opportunity to testify today in support of H.R. 3904, The Overdraft Protection Act of 2009. Our view of overdraft protection as currently offered to most consumers is that **enough is enough – it is past time for a switch to fairness.**

State Employees' Credit Union (North Carolina)

State Employees' Credit Union (SECU) is a member-owned, non-profit cooperative serving 1.5 million members in North Carolina. One out of six North Carolinians is a member-owner of SECU. The Credit Union was formed in 1937 with 17 members and $437 in assets during extremely difficult financial times to serve the consumer financial needs of North Carolina state employees, teachers, and their families. SECU has grown into a statewide organization with over 225 branches, and a proprietary *(CashPoints)* no-surcharge ATM network with 1,000+ locations in all 100 North Carolina counties. Assets now exceed $19 billion and we have approximately 800,000 checking accounts. SECU is well-capitalized, safe and sound.

Overdraft Protection

As currently and most frequently offered in the market place, **overdraft protection is neither a courtesy nor a privilege. It is a loan – a very, very expensive loan.** Despite claims by proponents to the contrary, overdraft protection is never the best nor the fairest choice for an accountholder – all other "choices" are, or can be, more beneficial and less expensive for the consumer. Credit unions, being member-owned cooperatives, are obligated by both philosophy and purpose to seek better financial solutions for their member-owners.

The following three fundamental changes in overdraft protection regulation proposed under HR 3904 will help ensure that credit union members and all consumers will make better choices when using an overdraft protection service:

1) Consumer "opt-in" to the overdraft service plan.

2) Limits on overdraft protection transactions and charges.

3) The requirement that fees be reasonable and proportional to the cost of handling overdraft protection.

SECU fully supports these consumer enhancements to overdraft protection services.

SECU's Approach to Overdraft Protection Services

SECU practices what it preaches. Overdraft protection is a service we offer our members to help reduce the possibility of checks/debits being returned because sufficient funds are not available in the account. All members can sign up for this safe, affordable service on an opt-in basis. Approximately 80% of all checking accountholders elect to have this overdraft protection. We do not charge overdraft fees.

Each checking account (protected account) can have up to two "protecting" accounts attached to it to provide protection. Attached accounts may be either other deposit or line of credit accounts. If an item is received on a protected checking account that does not have sufficient funds on deposit, then the overdraft protection program is activated to determine if the item will be paid or not. The member has pre-selected the order of accounts to be used for protection. Once the first account's available funds are transferred, then available funds in the second account will be used. Funds are transferred from the protecting account(s) to the checking account to provide sufficient funds in the checking account to pay the item. The fee for a transfer is 50¢. An average of 9,400 advances are made each day.

Available protecting accounts are:
- Another checking account
- Money Market Share Account (limited to 6 transfers per month)
- Regular share account (limited to 6 transfers per month)
- SECU issued VISA credit card
- SECU Open End Loan
- SECU Home Equity Loan

Transfer increments are $50 or full available balance (whichever is smaller), except for home equity coverage which has a minimum transfer of $500 or the available credit line (whichever is less). For credit card coverage accounts, we will transfer up to 110% of the approved credit line. When a member accesses their checking account via an ATM card or point of sale debit card, the transaction will be approved or denied based on the balance in the account plus the funds available in their protecting accounts.

If an item is presented for payment and the member does not have sufficient funds in the account or available through the overdraft protection system to transfer into the account, the item will be returned marked Non-Sufficient Funds. The NSF fee is $12.00. We average 6,100 items being returned each day.

If a member has had 6 or more NSFs in a 45 day period, the account holder automatically receives a letter (sent centrally) requesting the member visit a local branch to discuss any financial problems they may be experiencing and the proper handling of their checking account. It is never in the best interest of a member to continue to pay excessive fees for checking account services. Once the member receives the first letter, the branch receives notification to begin working with the member on proper management of the checking account. The account continues in an "alert" status for the branch to work with the member until problems are resolved or until the branch decides it is in the member's best interest to close the account. The branch will work with the member to transfer to a "cash" basis using their base share (savings) account as their primary operating account (payroll direct deposit, etc.). If the member continues to have excessive NSFs, two additional letters of warning are sent. After the third letter, the account is placed in a closed status. We contact approximately 2,000 checking account holders each month and have closed 328 accounts to date in 2009.

SECU 2010 – Coming Enhancements

SECU has plans for three new services in 2010 to further help our members manage their checking accounts.

1- **NSF FREE DAYS** –If the member has exhausted all available funds from their account (including the overdraft protection program) and items will be returned unpaid on the account, SECU will NOT charge any NSF fee for those returned items (regardless of number of items) up to two days during the calendar year. Although the item(s) will still be returned, the expense of the NSF fee(s) will not further decrease the member's account balance. There will be no fee for this service. There is no enrollment - all accounts are automatically enrolled. This program will begin January 1st.

2- **ANOTHER CHANCE PROGRAM** – If a member registers to receive text message notifications from SECU for this particular program, SECU will advise them early in the morning of potential NSF items. SECU will allow the member that full business day to make a deposit sufficient to pay the items instead of SECU automatically returning the items because of non-sufficient funds. This gives members "another chance" to cover the check/debit before SECU has to return the item and charge the NSF fee. There will be no fee for this service but members do have to register for it through our secure Member Access web service (which is also free). This program should be available by second quarter.

3- **CASHPOINTS GLOBAL** – This new program will be a controlled spending account that will be especially beneficial for our members who have had difficulty in managing checking accounts. No paper checks or ACH debits will be allowed on the account so there will be no NSF fees and no overdraft protection. The member will receive a VISA check card for point of sale purchases and ATM access. Electronic deposits (direct deposits, payroll deduction deposits, wire transfers and funds transfers) will be allowed as well as over-the-counter deposits. The member will be able to use the SECU BillPay service for paying bills electronically or by having SECU mail a cashier's check for the member. No interest will be paid on the account. E-statements will be required. The monthly fee for this account will be the same as our other checking account program - $1.00 (which 99% of our existing members donate to the SECU Foundation). This account will allow those members who cannot handle a checking account the convenience of a checking account without the possibility of mismanagement. All debit transactions will be pre-approved through the VISA check card or ATM networks or through our BillPay service. This account should also be ready by second quarter 2010.

Credit Unions: There is a Difference

Credit unions are different. No banks are non-profit by choice. Banks are not created to find new ways to leave more money in their customers' pockets. Banks are not challenged by philosophy, structure and purpose to put "people ahead of profits". The expectations of both Congress and the public should be higher for credit unions. Credit unions should set the standard, the benchmarks, the bar for socially conscious and socially responsible consumer financial services. Credit unions should wear "white hats" that are clean, brilliant and very, very apparent – in all credit union services and products.

For this reason, we do not support H.R. 3904's exclusion of overdraft fees from the interest rate cap applicable to federal credit unions. We believe all credit extended by credit unions should be subject to an interest rate cap.

While We're At It...

As Congress wrestles with alternatives to improve consumer financial services, SECU would ask consideration of the following issues:

1) Require that federally insured financial institutions honor, without fee or hold, all checks drawn on the institution. Employees should not have to pay to convert their wages from a check into cash.

2) Prohibit fixed rate mortgages with terms of greater than 15 years. The United States is the only modern economy which continues to permit – actually encourage – long-term, fixed rate mortgage lending. Such problems as subprime securitization, Fannie and Freddie, will cease to exist if long-term fixed-rate mortgages no longer are permitted in the market place.

3) Reinstitute a usury limit on all federally insured institutions. Credit unions, alone among federally insured institutions, continue to be subject to an 18% usury limit, and they remain a safe haven, safe harbor for consumer financial services.

Conclusion

The mission statement of SECU is: "Do the Right Thing!" We hope that Congress, through passage of HR 3904, The Overdraft Protection Act of 2009, will join us in that mission.

Thank you for the opportunity to testify today. I welcome your questions.

Consumers Union

Nonprofit Publisher
of Consumer Reports

Testimony of
Ellen Bloom

Director, Federal Policy and Washington Office
Consumers Union

Before the
House Financial Services Committee

On
H.R. 3904, the "Overdraft Protection Act of 2009"

October 30th, 2009

Consumers Union Testimony
regarding
H.R. 3904, the "Overdraft Protection Act of 2009"
House Financial Services Committee
October 30, 2009

Thank you, Chairman Frank, Ranking Member Bachus, Representative Maloney and other members of the Committee. Consumers Union, the non-profit, independent publisher of *Consumer Reports* magazine, strongly supports H.R. 3904, the "Overdraft Protection Act of 2009" and is pleased to cosign the testimony of Consumer Federation of America. We also appreciate the opportunity to offer the Committee our additional consumer perspective on the unfair and abusive practices used to trap consumers in fee-based overdraft programs without their affirmative consent.

First, we will share some of our polling results which underscore the confusion consumers have about overdraft loans and, how, when asked, they express a strong desire to have more decision-making control over these loans. Second, we would like to offer the Committee some real life examples of the problems people around the nation are enduring as a result of egregious overdraft programs.

In February of this year, *Consumer Reports* National Research Center conducted a nationally representative telephone poll about common bank policies involving overdraft fees. There were a few key findings:

Only half (52%) of those surveyed who used debit cards had a correct understanding that a bank typically allows the transaction to proceed, covers the shortage from the next deposit, and charges a fee for doing so. Consumers appear even more misinformed about ATM overdrafts. Only 31% correctly said that the bank will permit the transaction, subsequently dock the account and charge for the loan. Many consumers simply don't expect to be charged a fee when they overdraft their account. Therefore, consumers would be unlikely to opt out of a program of which they are unaware, and that is why CU strongly supports the opt-in language in H.R. 3904.

At the same time, when asked, consumers overwhelmingly want choice when it comes to their bank accounts. Two-thirds of consumers polled said they prefer to expressly authorize overdraft coverage, so that there would be no overdraft loan—or fee— unless and until they opted into the service. Similarly, two thirds of consumers said that banks should deny a debit card or ATM transaction if the checking account balance is low. A copy of our polling results is included with our written testimony as Appendix A.

Additionally, consumers from across the country have shared with us their frustrations with automatic overdraft programs. While we have attached as Appendix B a compilation of thirteen consumer stories regarding overdraft programs, I will highlight just three today.

Rachael from North Carolina explained to Consumers Union that her bank manipulates the order in which they clear transactions, to maximize the number of times she overdraws her account.

Rachael is a married mother of three, who finds it difficult to manage her household when overdraft fees pile up. At one point Rachael found 7 overdraft charges for debit card transactions. All of the purchases which caused Rachel's account to overdraft were for less than $20 each, and at least half of these were under $10. The smallest of these charges was for a $1 beverage purchased at a gas station; however, each of these transactions were penalized for a $35 fee.

In describing her bank's overdraft policy, Rachael explained, "they clear the largest amounts first because they want to charge the [$35] fee on the $1 purchase." The overdraft fees deducted from her account took away from the grocery money Rachael uses to feed her children – she describes: "When you're taking $300 from us in two weeks, we get behind on other expenses. It literally took us two months to catch up."

Justin from New York told us why he believes it is important to place strong limits on the number of times an institution can charge a fee for covering an overdraft. Justin knows firsthand why it is important to put in place strong monthly and annual limits on such fees, and why it will be extremely helpful to allow consumers the choice to opt-in to overdraft coverage.

Justin told Consumers Union that he was charged $385 for 11 overdrafts over a ten day period. Some of these transactions were for less than $10 – all but two were worth less than $50. Eventually, after multiple telephone calls to the bank, Justin was refunded $100 of his $385 total overdraft fees. Justin would rather have his debit card denied on transactions that would cause overdraft. He wishes that he could choose whether the bank should cover transactions which overdraw his account, and he feels that "to tack on fees and change policies to increase fee income is completely intolerable."

Don from Ohio shared with us his personal story about overdraft fees. He describes overdraft fees as, "a snowball effect, I couldn't get away from it –the more you put in the more they take out."

Don and his wife rely on a limited income—the paycheck from his part time job, and the social security payment she receives for disability. Don checks his account balances regularly, but has recently been hit with a flurry of overdraft fees because of his bank's overdraft policy.

In October 2008, Don used his debit card and overdrafted his checking account by 85 cents. Before the bank opened the next day, Don deposited $30 at the ATM thinking that this would cover the 85 cents overdraft. A day later he discovered he had incurred two overdraft fees, one for the 85 cents and the other because the $30 he had deposited did not cover the deficit caused by the first fee. The second overdraft triggered another overdraft fee and a $5 per day fee for each was also added. After haggling with his bank, Don reached a compromise where he only had to pay one of the $35 overdraft fees.

The Overdraft Protection Act will go long way to stop the abusive practices experienced by Rachael, Justin, Don and thousands of other consumers across the nation. The bill will require financial institutions to obtain consumers' affirmative consent before covering debit card, ATM and check-based transactions for a fee. Those offering overdraft protection will be required to educate their customers sufficiently about these programs to get customers to affirmatively sign up. For those who do choose to enroll, the legislation will:

- limit the number of overdraft fees financial institutions can charge to six per year;
- require fees to be reasonable and proportional to the cost to the financial institution; and
- Prohibit banks form manipulating the clearing of transaction in a way which maximizes fees.

We at Consumers Union wholeheartedly endorse this legislation as an important step in helping consumers avoid entering a cycle of debt because of unfair and abusive overdraft fees. We look forward to working with you as the bill moves forward.

Thank You

Appendix A

Final Report

Financial Regulation Poll

For Public Release

February 13, 2009
NRC #2009.07

Consumer Reports National Research Center

Methodology

- Telephone surveys were conducted among 1,001 random adults comprising 500 men and 501 women 18 years of age and older. Respondents were screened for possession of a checking account with either an ATM card or a debit card. The analysis is based on the 679 adults who reported having a checking account with ATM or debit card. Interviewing took place over February 5-8, 2009.

- The questionnaire was fielded via Opinion Research Corporation's Caravan twice-weekly national telephone omnibus survey. ORC used random digit dialing to achieve a nationally representative probability sample and weighted completed interviews by age, sex, geographic region and race.

- The results of this study are intended for external communications. Methodology statement for public release:

  The Consumer Reports National Research Center conducted a telephone survey using a nationally representative probability sample of telephone households. 679 interviews were completed among adults aged 18+ who reported having a checking account with an ATM card or a debit card. Interviewing took place over February 5-8, 2009. The sampling error is +/- 3.8% at a 95% confidence level.

Implications

- This study was commissioned to investigate consumers' beliefs about current bank policies involving overdraft fees, and how consumers prefer that banks handle overdrafts.

- Only qualified respondents participated in this telephone survey. Around 7 in 10 (69%) satisfied the two screening criteria—have a checking account and an ATM card or debit card—and were allowed to proceed (page 5).

- Our analysis indicates that many consumers are misinformed about common bank overdraft policies. They also expressed strong preferences for policies that are more favorable toward bank customers.

- Only half (52%) of respondents with a debit card had the correct impression of how banks commonly treat debit card overdrafts—namely, the bank allows the transaction to proceed, covers the shortage from the next deposit and also charges a fee. More young consumers aged 18-34 years (68%) expressed accurate knowledge of bank policy. In contrast, more than one-quarter (28%) erroneously thought that the bank would block an overdraft debit purchase, and 11% thought the bank would allow it to proceed and recover the difference later without charging a fee. Those aged 55+ years demonstrated the poorest understanding (page 6).

- Consumers are even more misinformed about ATM overdrafts. Only 31% correctly said that the bank will permit the transaction, subsequently dock the account and charge for the loan. In contrast, nearly half (48%) incorrectly said the ATM card would not work at all if the account balance were too low. Although 1 in 10 understood the first two components of the policy—the transaction proceeds, is covered later—they were unaware of the fee (page 7).

Implications (cont.)

- The majority of consumers prefer bank overdraft policies that are more favorable to them. Two-thirds said they want an opt-in policy, where banks cannot cover overdrafts—and charge for the service—unless a customer expressly authorizes the service. Only 27% preferred an opt-out policy, which allows banks to provide overdraft loans for a fee until the customer instructs otherwise (page 8).

- Moreover, two-thirds (65%) of consumers said that banks should deny a debit card or ATM transaction outright if it would overdraw the account. Young consumers, those with household income under $40,000 and women were most likely to express this viewpoint. Only one-third said the bank should permit the transaction, even if they incur a fee (page 9).

- Regardless of whether a bank follows an opt-in or opt-out policy for overdrafts, consumers don't want the notification buried in their regular bank statement. To the contrary, three-quarters (74%) said they should be notified in a separate letter (page 10).

- Consumers also don't want to be punished for declining the bank's overdraft service. Overall, 73% of respondents said they should receive the same type of bank account whether or not they agree to pay for an overdraft service. Young, female and low-income consumers had the strongest feelings about this (page 11).

- If the law were changed to require that banks follow an opt-in policy, overwhelmingly (90%) consumers want to receive notification before they incur additional fees (page 12).

- Overall, 14% of consumers recalled being assessed an ATM or debit card overdraft fee during the past six months (page 13).

Screening Criteria

- Consumers were screened to ensure that they have a checking account plus associated ATM card or debit card. Those who failed to satisfy these requirements were not qualified to participate.

- Overall, nearly 7 in 10 consumers (69%) contacted by telephone said they have both a checking account and ATM or debit card. These individuals (679 total) proceeded with the survey.

- Qualified consumers disproportionately were:
  - ✓ High-income (90% of those reporting household earnings of $75,000 or more satisfied the screeners)
  - ✓ Middle-aged (75% of those 35-54 years old qualified)
  - ✓ Residents of the West (74%) or South (70%)

QD1A-C - Please tell me which of the following you have.

		Gender		Age			Household Income			Region			
	TOTAL	Men	Women	18-34	35-54	55+	<$40K	$40-74K	$75K+	NE	NCntrl	South	West
	%	%	%	%	%	%	%	%	%	%	%	%	%
Checking account	84	83	85	73	87	92	70	91	98	84	83	85	85
Checking account with ATM or debit card (Net)	*69*	*69*	*68*	*68*	*75*	*62*	*52*	*76*	*90*	*66*	*63*	*70*	*74*
ATM card with checking account	65	66	64	62	72	58	50	72	84	65	57	65	71
Debit card with checking account	62	62	61	64	68	50	48	68	81	61	57	60	68
Don't know/Refused	2	1	3	2	1	3	1	1		1	3	3	1
NO ANSWER	14	16	13	25	13	6	29	8	2	15	14	13	15

Overdraft via Debit Card
Base: Checking With Debit Card

- Only half (52%) of respondents with a debit card correctly described banks' typical policy regarding debit card overdrafts—the bank permits the transaction, docks your next deposit and charges you for the loan. Young (68%) and low-income (57%) consumers were most likely to understand debit card policy.

- Nearly half of consumers are misinformed. Almost 3 in 10 (28%) of respondents said the bank would block the transaction, and an additional 1 in 9 (11%) expected the bank to allow the purchase and deduct the shortage later without imposing a fee.

- Overall, older consumers (aged 55+ years) were the least informed. At least 30% of respondents aged 35 years or more thought that the bank would deny a debit purchase if it would overdraw the account.

QD2 - If you had $25 in your checking account and you tried to make a $40 purchase with your debit card, what do you think would happen?

Base: Checking Account With Debit Card

		Gender		Age			Household Income			Region			
	TOTAL	Men	Women	18-34	35-54	55+	<$40K	$40-74K	$75K+	NE	NCntrl	South	West
	%	%	%	%	%	%	%	%	%	%	%	%	%
Your bank would allow the purchase and then deduct the shortage from your next deposit, and also charge you a fee	52	53	50	68	47	39	57	44	53	52	52	49	54
Your bank wouldn't allow you to make the purchase	28	28	29	22	32	30	29	30	30	31	36	25	25
Your bank would allow the purchase and then deduct the shortage from your next deposit	11	10	12	6	12	15	8	15	10	9	8	13	11
Don't know/Refused	9	9	9	4	8	17	7	10	6	8	4	12	10

Overdraft via ATM Card

Base: Checking With ATM or Debit Card

- Consumers evaluated a companion scenario about overdrafts at an ATM machine. Only 31% knew what the most-likely result would be—the bank permits the overdraft, docks the account later on and tacks on a fee. Young (42%) and low-income (39%) respondents revealed the highest awareness of actual bank policy.

- In contrast, nearly half (48%) of consumers incorrectly said the ATM card would not work if they attempted to overdraw. Another 10% said the bank would permit the withdrawal and cover the shortage with their next deposit.

QD3 - If you had $25 in your checking account and you tried to take $40 out of the ATM machine, what do you think would happen?

Base: Checking Account With ATM or Debit Card

		Gender		Age			Household Income			Region			
	TOTAL	Men	Women	18-34	35-54	55+	<$40K	$40-74K	$75K+	NE	NCntrl	South	West
	%	%	%	%	%	%	%	%	%	%	%	%	%
Your ATM card wouldn't work	48	50	47	44	56	43	43	49	49	47	47	52	45
Your bank would allow the withdrawal and then deduct the shortage from your next deposit and also charge you a fee	31	30	33	42	27	27	39	27	34	34	36	25	36
Your bank would allow the withdrawal and then deduct the shortage from your next deposit	10	11	10	7	10	15	8	11	10	11	15	9	8
Don't know/Refused	10	9	10	7	8	15	9	13	7	7	2	14	12

Overdraft Fee Policy Preference

Base: Checking With ATM or Debit Card

- After the two questions about beliefs regarding bank overdraft policy, the telephone interviewer explained to respondents how banks usually treat debit and ATM overdrafts, and then asked them to indicate a preference for opt-in vs. opt-out.

- Two-thirds of consumers said they prefer to expressly authorize overdraft coverage, so that there would be no overdraft loan—or fee—until they opted into the service. More high-income and middle-aged consumers chose opt-in than others, along with Northeasterners.

- Only 27% of respondents preferred an opt-out policy, where the bank provides overdraft coverage and charges a fee until the customer requests otherwise.

QD4 - When you use your debit or ATM card and make a purchase or a withdrawal for more than you have in your account, your bank may charge you a fee to cover the overdraft. This is a fee-based overdraft loan service, which your bank may call overdraft protection. If your bank provides this service, which policy do you prefer?

Base: Checking Account With ATM or Debit Card

		Gender		Age			Household Income			Region			
	TOTAL	Men	Women	18-34	35-54	55+	<$40K	$40-74K	$75K+	NE	NCntrl	South	West
	%	%	%	%	%	%	%	%	%	%	%	%	%
Your bank should be required to have you sign up before covering your overdrafts, if it wants to charge you for them. This means that you wouldn't pay the fee, and wouldn't get the overdraft loan, unless you asked for it	66	66	66	64	70	63	63	63	72	71	67	63	67
Your bank should be able to provide the overdraft loan for a fee until ask the bank to stop providing this service	27	26	27	30	26	24	31	30	22	23	29	27	26
Don't know/Refused	7	7	7	5	4	14	6	7	6	6	4	10	7

Deny vs. Cover Overdraft

Base: Checking With ATM or Debit Card

- This question focused on whether consumers want an overdraft transaction to proceed. Two-thirds (65%) said that banks should deny a debit card or ATM transaction if the checking account balance is too low. Young and low-income consumers, and women, were mostly likely to express this preference.

- One-third of respondents—disproportionately middle-aged and male—want the bank to cover the transaction, even if a fee is involved.

QD5 - If you don't have enough money in your account to cover a debit card or ATM transaction, what do you want your bank to do?

Base: Checking Account With ATM or Debit Card

		Gender		Age			Household Income			Region			
	TOTAL	Men	Women	18-34	35-54	55+	<$40K	$40-74K	$75K+	NE	NCntrl	South	West
	%	%	%	%	%	%	%	%	%	%	%	%	%
Your bank should deny the transaction	65	63	68	73	63	62	70	66	63	67	64	65	66
Your bank should cover transaction, even if it costs you a fee	33	36	29	25	37	34	29	32	34	31	35	32	32
Don't know/Refused	2	2	2	2	1	4	1	2	2	2	1	2	2

Opt-in/Opt-out Notification Preference

Base: Checking With ATM or Debit Card

- A strong majority of respondents (74%) said they want to be notified about signing up for or canceling a fee-based overdraft loan service in a separate letter.
- In contrast, only 23% would like notification via the bank statement.

QD6 - How do you want your bank to notify you about signing up for or canceling a fee-based overdraft loan service?

Base: Checking Account With ATM or Debit Card

		Gender		Age			Household Income			Region			
	TOTAL	Men	Women	18-34	35-54	55+	<$40K	$40-74K	$75K+	NE	NCntrl	South	West
	%	%	%	%	%	%	%	%	%	%	%	%	%
In a separate letter from the bank	74	74	75	72	76	76	69	74	76	68	75	76	76
On your bank statement	23	23	22	26	23	18	27	25	22	29	23	21	20
Don't know/Refused	3	3	3	2	1	6	3	1	2	4	2	3	4

Punitive Pricing

Base: Checking With ATM or Debit Card

- Nearly three-quarters (73%) said that a checking account should cost the same regardless of whether the customer declines the bank's overdraft service. Segments that were most adamant: age 18-34 years, women, low-income.

- One-quarter (24%) of respondents said the bank should be able to set its product offering and pricing.

QD7 - Should your bank be permitted to charge you more for basic banking if you decline the overdraft service?

Base: Checking Account With ATM or Debit Card

		Gender		Age			Household Income			Region			
	TOTAL	Men	Women	18-34	35-54	55+	<$40K	$40-74K	$75K+	NE	NCntrl	South	West
	%	%	%	%	%	%	%	%	%	%	%	%	%
No, you should receive the same type of bank account whether or not you agree to pay for an overdraft service	73	68	77	79	71	68	76	71	74	72	76	71	73
Yes, the bank should be able to decide what products to offer and at what price	24	29	19	18	27	26	20	26	24	23	20	27	24
Don't know/Refused	3	2	4	3	2	5	5	3	2	4	4	2	3

Notification After Regulatory Change

Base: Checking With ATM or Debit Card

- Overwhelmingly, respondents said that if an opt-in law is passed, banks should have to notify existing customers about their rights before they incur additional fees.
- Only 1 in 11 respondents felt that the bank should be able to charge an initial fee before notifying existing customers of their new rights.

QD8 - Suppose that a new law requires that the bank get your permission before assessing an overdraft fee. When would you want to be notified of your new rights?

Base: Checking Account With ATM or Debit Card

		Gender		Age			Household Income			Region			
	TOTAL	Men	Women	18-34	35-54	55+	<$40K	$40-74K	$75K+	NE	NCntrl	South	West
	%	%	%	%	%	%	%	%	%	%	%	%	%
Before being charged any additional fees	90	87	92	90	91	88	91	93	88	90	92	91	87
After being charged the first fee in order to avoid future fees	9	11	7	9	9	8	8	7	10	8	7	9	12
Don't know/Refused	1	1	1	1		3	1		1	2	1	1	1

ATM-Debit Card Fees

Base: Checking With ATM or Debit Card

- Overall, 14% of consumers recalled being assessed a fee for an ATM or debit card overdraft during the past half-year. Respondents aged 18-34 years (26%) were most likely to be aware of a fee.

QD9 - In the PAST 6 MONTHS, have you been charged a fee by your bank for using your debit card to make a purchase or your ATM card for an ATM withdrawal that exceeded the balance in your account?

Base: Checking Account With ATM or Debit Card

		Gender		Age			Household Income			Region			
	TOTAL	Men	Women	18-34	35-54	55+	<$40K	$40-74K	$75K+	NE	NCntrl	South	West
	%	%	%	%	%	%	%	%	%	%	%	%	%
Yes	14	15	14	26	10	7	18	16	11	11	8	16	19
No	85	85	85	72	90	92	80	84	89	87	91	83	81
Don't know/Refused	1	0	1	2		1	2			1	1	0	0

Profile

- Women and men were equally represented in the poll, and the median age of respondents was 44 years.
- Overall, 43% of participants reported having at least a four-year college degree, but 30% had no education beyond high school.
- Median household income of interviewed consumers was about $66,000, and 46% said they are employed full time.
- Most respondents (59%) said they are married, and around 8 in 10 identified themselves as Caucasian.

Profile

Base: Checking Account With ATM or Debit Card

		Gender		Age			Household Income		
	TOTAL	Men	Women	18-34	35-54	55+	<$40K	$40-74K	$75K+
	%	%	%	%	%	%	%	%	%
UNWEIGHTED BASE	679	346	333	104	256	318	155	183	245
GENDER									
Male	49	100		45	52	49	44	42	58
Female	51		100	55	48	51	56	58	42
AGE									
18-34	30	28	33	100			44	35	15
35-44	20	23	17		48		7	20	32
45-54	22	21	22		52		16	19	31
55-64	15	16	15			55	13	15	16
65+	13	12	14			45	20	11	6
Refused/Nr	0		0						
MEDIAN (Years)	43.9	43.8	45.0	26.0	45.3	63.2	43.4	41.6	45.9
EDUCATION									
Some HS or less	7	8	5	12	4	5	12	5	3
HS graduate	23	22	24	29	19	23	37	27	12
Some college	26	24	29	25	27	26	28	29	23
College grad+ [Net]	*43*	*45*	*41*	*33*	*51*	*43*	*22*	*39*	*62*
College grad	27	29	26	24	33	23	14	29	37
Postgrad degree	15	16	15	9	17	20	8	10	25
Refused/Nr	1	1	2	1	1	3		0	
HOUSEHOLD INCOME									
Under $25,000	12	10	14	24	5	11	48		
$25,000 but less than $50,000	20	17	23	21	16	28	52	24	
$50,000 but less than $75,000	24	22	25	29	21	22		76	
$75,000 but less than $100,000	14	17	12	6	22	11			37
$100,000 or more	25	29	20	14	34	21			63
Refused	5	5	5	6	2	8			
MEDIAN (000s)	$65.8	$73.2	$59.6	$52.0	$83.5	$58.2	$26.0	$58.6	$121.0

Profile (cont.)

Base: Checking Account With ATM or Debit Card

		Gender		Age			Household Income		
	TOTAL	Men	Women	18-34	35-54	55+	<$40K	$40-74K	$75K+
	%	%	%	%	%	%	%	%	%
UNWEIGHTED BASE	679	346	333	104	256	318	155	183	245
EMPLOYMENT									
Employed full time	46	54	38	38	65	26	27	48	62
Retired	17	16	18		4	54	23	15	11
Not currently employed	14	8	21	27	10	7	18	19	7
Self-employed	12	15	10	12	15	8	11	12	13
Employed part time	10	7	14	22	5	5	20	6	7
Refused/Nr	0		0		0		1		
MARITAL STATUS									
Married	59	62	56	44	70	58	30	67	77
Single and never been married	21	23	19	50	10	5	35	15	13
Divorced	9	7	10	1	10	14	18	9	3
Widowed	5	3	7		1	17	10	4	2
Living as married	3	3	3	3	3	2	4	2	3
Separated	2	2	3	1	4	0	3	3	2
Refused/Nr	1	1	2	1	1	3	0		0
RACE*									
White/Caucasian	79	79	80	68	81	89	74	75	86
Black/African-American	10	8	12	15	9	5	12	16	3
Asian/Asian-American	1	1	1	2	0	1	1	1	1
Some other race	11	13	9	15	10	7	15	9	10
Refused/Nr	1	1	1	1	2	0	1	0	0
REGION									
Northeast	18	16	20	19	20	15	18	16	20
North Central	20	21	20	21	24	15	26	19	21
South	37	39	36	41	34	38	31	40	34
West	24	24	24	19	23	32	25	25	25

*Multiple responses allowed

Appendix B

Stories about Overdraft Loans

Rachel of Raleigh, NC

"[The banks] clear the largest amounts first because they want to charge the [$35] fee on the $1 purchase." —Rachel

Rachel is a married mother of three, who finds it difficult to manage her household when overdraft fees pile up. Throughout 2008, she paid $1000 in overdraft fees – and in October alone she paid almost $500. By the end of the first week in October, when she realized she had overdrawn her account, Rachel found 7 overdraft charges for debit card transactions. Through the following week, Rachel also had overdrawn on five more debit card transactions because she needed to use her card and simply could not catch up on the overdraft fees.

All of the purchases which caused Rachel's account to overdraft were for less than $20 each, and at least half of these were under $10. The smallest of these charges was for a $1 beverage purchased at a gas station; however, all of these transactions were penalized for a $35 fee. In describing her bank's overdraft policy, Rachel explained, "They clear the largest amounts first because they want to charge the [$35] fee on the $1 purchase." After working with the Better Business Bureau, Rachel was able to get a few of her overdraft charges reversed but the bank refused to refund any more.

The overdraft fees deducted from her account took away from the grocery money Rachel uses to feed her children – she describes: "When you're taking $300 from us in two weeks, we get behind on other expenses. It literally took us two months to catch up." Although she would rather be declined on small purchases, Rachel would like recurring payments, such as her car payments, to be processed even in the event of an overdraft – she explained, "They should give us an option – if it was something like a car payment I would probably want [the bank] to put the payment through, but not the little debit card purchases."

Vanessa of Columbus, OH

"I got into this huge overdraft whirlpool that just pulled me under" —Vanessa

Vanessa is a small business owner in commercial interior design who has recently been struggling with unfair banking practices. In May 2008, the bank which she had done business with for ten years suddenly disabled her pre-existing overdraft program. Prior to this, Vanessa had a line of credit with a very reasonable interest rate connected to her account to be drawn upon in the event of an overdraft. Starting February 2008 this option was no longer offered but she was never notified of this change and incurred a number of overdrafts unknowingly. The bank eventually reversed these charges and linked a new credit card to her account; however, the account failed to draw upon the new credit card and again she was being charged overdraft fees.

After many frustrating encounters with her bank, Vanessa changed banks and was enrolled in another overdraft program. Because she has a business account, Vanessa is required to call or e-mail the bank to initiate money transfers. On two occasions, her bank has erred in processing these transactions, and she was charged overdraft fees. The fees are currently being disputed with the bank as Vanessa has documentation of completing the transfers. Vanessa is mostly distressed about the way banks charge overdrafts – she describes: "By the time I am notified about the overdraft, several checks have already processed, and the overdraft of under $25 can become as much as $200 or more. The total sum is mostly bank charges."

In her frustration, she notes: "Sometimes overdraft charges aren't posted until 3 days after the day of the overdraft, and then it takes at least 2 days to get to me. This allows a lot of time to pile up charges of $37.50 per check, and $7.00 a day for each overdraft." When Vanessa contacted the new bank in August and asked for an alternative overdraft solution, she was told that it would involve a line of credit for which she did not qualify. Almost five months later, Vanessa contacted the bank again and was now offered the option of opening a savings account which could be drawn upon in the event of an overdraft. Vanessa is fed up with the errors, overdraft fees, and misinformation from her bank. She plans to close her account as soon as the outstanding disputes are settled.

Richard of Elk Grove, CA

"What actually happened was, my bank had not reversed any of the holds – even the original hold of $100, and had subsequently placed $762.00 in holds on funds in my account." —Richard

Richard and his wife were in the final stages of buying a home, and rented a U-Haul truck for the day that they were expecting to move. Unfortunately, they closed escrow five days later than originally planned, and ended up keeping the U-Haul truck during that time. The U-Haul rental center initially charged a $100 hold to cover the cost of the rental agreement.

On the fourth day, U-Haul placed another $400 hold on Richard's account, for which he began incurring $30 overdraft fees as the money the bank was holding for U-Haul was no longer part of his available balance.

When Richard contacted his bank, he was told that the two holds would be reversed on the 30th of the month. However, when Richard returned the truck to U-Haul on the 26th, the agent told him that the two previous holds had been reversed, and he was only being charged the cost of the actual rental - $262.00. Richard explains, "What actually happened was, my bank had not reversed any of the holds – even the original hold of $100, and had subsequently placed $762.00 ($100.00+$400.00+$262.00) in holds on funds in my account." In total, Richard was assessed 8 overdraft fees ($240) that his bank was not willing to reverse. If the bank had not processed the holds and the actual amount due at the same time, Richard would not have incurred any overdraft fees.

Joyce of Greensboro, NC

Joyce runs a small business out of North Carolina, and has very recently run into trouble with overdraft fees. In January 2009, Joyce overdrew her business checking account and Bank of America transferred $155 from her personal account without notifying her, to cover the deficit. A week later, Joyce had also overdrawn her personal business account 7 times for $35 each, because her bank's unauthorized money transfer left her personal checking account in the negative. One of the charges which caused an overdraft fee was for as little as $5, while most of the others were for less than $35.

With the current state of the economy, Joyce's business has not been doing very well. The money that she uses from her Social Security checks to support the minimal expenses of maintaining her business was being confiscated for the overdraft fees she owed Bank of America. Joyce contacted the bank and was given the run-around. When she finally spoke with the appropriate representative, she was offered a reverse on the overdraft fees if she could pay the amount she actually owed – but Joyce simply did not have the money at the moment. Because she could not pay immediately, the bank representative told her, "if you're not going to pay us right away we're not going to remove your overdrafts – we'll be turning your account over to collections."

Joyce was never given the option to opt-out of her overdraft protection, nor could she recall when her bank had adopted this policy. She couldn't believe how quickly and unexpectedly everything happened as she explained: "Thursday my money was there, and Friday it was gone. All of a sudden they take the money out and everything is overdrawn." Joyce chose to take her business elsewhere and no longer does business with Bank of America – she describes "I would not wish Bank of America on anybody."

Linda of Valley Village, CA

Linda is an independent contractor from California who does not usually have problems with overdrafts. However, in February 2005, Linda incurred over $500 in overdraft fees because Wells Fargo had not notified her of the negative balance in her account, and continued to allow charges on her debit card. One week from the initial overdraft, Linda had unknowingly overdrawn her account 15 times – half of these transactions were debit charges under $20, and only three of these purchases were for more than $33.

Upon discovering that her account was charged $33 for each of these overdrafts, Linda contacted the bank and asked for the fees to be reversed. Strangely enough, Linda describes: "I was told that a bank manager had been aware of the overages from the very first [overdraft], but because I was a longtime customer he let them go through." Linda objected to this explanation. She would have preferred that her purchases be denied so that she would become immediately aware that her account was in a negative balance. Eventually, the bank agreed to reduce the fees by $166 and Linda still ended up paying $331 for overdrafts that wouldn't have occurred had the initial overdraft purchase been declined. On her next statement, Linda was surprised to also find a $2 fee for speaking to a bank representative over the telephone.

Linda was not given the option to opt-out of overdraft protection, nor was she aware that this was possible. After this incident, Linda has been careful not to overdraft but still remains wary of her bank's policies – she explains "If that was their way of rewarding a longtime, good customer, something is definitely wrong."

Justin of Clifton Park, NY

"To tack on fees and change policies to increase fee income is completely intolerable." —Justin

Since the beginning of 2008, Justin has incurred excessive overdrafts because of an arbitrary change in his bank's policy. Justin keeps two accounts separately – one for general spending, and the other for bills. He explains, "Previously, the bank would process credits prior to debits so if I went over in my spending account I could transfer money from my bills account and be covered with no overdraft charges. This has changed; now if I go over in my spending account, which I have, even if I transfer money the same day (which is immediately available), I receive an overdraft fee." Now, in addition to not being able to replenish his account immediately in order to avoid overdrafts, he is also being charged additional overdrafts as his bank chooses to debit the larger overdrafts before the smaller ones.

At one point, Justin was charged $385 for 11 overdrafts over a ten day period. Some of these transactions were for less than $10 – all but two were worth less than $50. Eventually, after multiple telephone calls to the bank, Justin was refunded $100 of his $385 total overdraft fees. Justin would rather have his debit card denied on transactions that would cause overdrafts. He wishes that he could choose whether the bank should cover transactions which overdraw his accounts, and he feels that "to tack on fees and change policies to increase fee income is completely intolerable."

Catherine of Mentor, OH

"Some of the overdrafts were directly caused by the fees themselves." —Catherine

Catherine is a disabled single mother raising two disabled children, who has recently gone back to school for a nursing degree. She struggles to cover her family's expenses with the Social Security Disability checks that she receives, and sometimes there just isn't enough.

In August 2008, Catherine received about $1200 in overdraft fees for overdrafts totaling less than $300 without even realizing it. At least half of these $39 overdraft fees were for $1.75 coffees which she purchases between classes when she doesn't have time to eat. Catherine explains, "Some of the overdrafts were directly caused by the fees themselves." Prior to this, her bank had also held her deposits for a nine day processing period, leading to overdrafts when she paid bills before her money was available.

After two weeks and $1200 in overdraft fees, Catherine contacted her bank and asked about opening a line of credit through the bank to be drawn upon in the event of an overdraft. She was told by the bank representative that this option was not available, but that she could opt-out of the overdraft program. Catherine had never been informed that this was possible and enthusiastically chose to opt-out. She has had no overdraft problems since.

Vickie of West Virginia

"Banks are making a killing with overdraft fees – they rob people without a gun and get away with it." —Vickie

Vickie relies on Social Security checks as her only source of income and is having trouble with her bank's overdraft policy. Over the past eight years, Vickie has paid her bank over $1,000 in overdraft fees alone. On one of these occasions, her account was overdrafted by only 2 pennies, and for this she incurred an overdraft fee of $34. When she first opened her account in 2001, the fee for overdrafts was $30 – and over the years it has increased to $32 and now is $34.

Vickie has also experienced overdrafts fees triggering other overdrafts because her bank does not notify her when she has a negative balance. Often times, these overdraft fees are deducted from her social security check deposits which she finds particularly upsetting. She describes, "If you miss one little thing in [your account], it can set you way back."

In her frustration Vickie explains, "If [the overdraft] was just two dollars, they didn't care – if two dollars knocked you out of balance then [the effect] is like dominos, they just don't care." For now, Vickie nervously watches her account balances in fear of overdrafting again.

Mary of Tolland, CT

Mary has suffered greatly from excessive overdraft fees. As a freelance administrative assistant, she has many responsibilities that don't leave her much time to watch her bank account. On countless occasions, Mary has deposited checks thinking that the amounts would be available immediately – as the bank tellers assured the deposits would "go in right away". Unfortunately, Mary has overdrafted her account on numerous occasions because her bank sometimes put a hold on her deposits, triggering a $25 fee each time.

In one instance, Mary was charged $400 in overdraft fees resulting from a delayed deposit. These fees were later reversed after her bank acknowledged that she had not been at fault. Mary has also had trouble with restaurants and gas stations putting holds for "double or triple" the amounts of her purchases, leading to more overdrafts even though she had enough in her account to cover the actual transaction amount.

Mary estimates that she has incurred overdraft fees at least 50 times in situations over the past year where unfair banking policies have led her to overdraft – 80% of these overdrafts were for purchase amounts much less than $25. If she could, Mary would prefer to be declined by retailers in the event that her debit transactions would cause an overdraft. After more than $1250 in overdraft fees, Mary is tired of haggling with her bank.

Clifford of Spokane, WA

Clifford has been stung by high overdraft loan fees, like many Americans. After he lost his job in 2007, he got hit with multiple overdraft fees, even though he has tried to keep a close eye on his finances.

Over the past two years he estimates that he has overdrafted 70-80 times, and 80% of these transactions were for amounts much less than the $35 fees which were debited from his checking account each time. He offered this example: "If I overdraft my account for a $5.50 transaction and my bank charged me $34, the interest rate for that mini-loan is quite large – 618.18%". Some of these fees were caused by holds on his deposits, as well as overdrafts induced by other overdrafts. He also points to the problem of having two debit cards connected to a joint account, and the inevitable difficulty that he and his wife experience in constantly tracking their balance. From his experiences, Clifford admits that he would rather be declined at a retailer and suffer the embarrassment than put himself another $35 in the negative.

Not being allowed to opt-out of his bank's "overdraft protection" policy has hindered his financial situation significantly. On multiple occasions, he contacted his bank and was denied the ability to opt-out of the program. As an alternative, his bank suggested that he link his checking account to a second account. Clifford now pays a $15 transfer fee every time he overdrafts his checking account, and the amount is borrowed from the secondary account. He admits that this is still less than the previous $35 fee, but objects to the idea of paying the bank to borrow his own money.

Nancy of Tampa, FL

"I cannot accept as fair and reasonable, a $35 fee for a $2.79 cup of coffee!" **—Nancy**

Nancy is a divorced mother, raising two children without child-support – and with such a tight budget she sometimes overdrafts her checking account because the bank will allow an ATM purchase to go through, even though the funds are not available. She overdraws her account about 3 – 4 times per year at $35 per item each time. Sometimes there are as many as six $35 overdraft fees assessed to her account at one time. Approximately 90% of the overdrafts are caused by transactions worth less than $5. Most of these overdrafts occur during fast food or coffee purchases for $2 - $3, or charges at the gas station when she uses her debit card.

In February 2009, Nancy noticed that she had incurred multiple overdraft charges even though her online statement did not show any negative balances. After contacting her bank, Nancy explained: "The bank claims they are looking at a 'different screen' than the screen they provide me of my account online. They claim their screen is in 'real time' and the online screen provided for clients to view is not." Through providing documentation and by making numerous complaints, Nancy was eventually refunded $87 out of the $175 she was charged for the 5 overdrafts. An issue which she wasn't able to fix, however, was the fact that her bank pays larger debits before smaller debits causing her to incur more overdrafts than necessary. Her bank's policies affect Nancy greatly: "If you live week to week like most of us, you can't afford to be out $175 in overdraft fees; particularly when your balance can cover most of the items, but the bank is choosing to pay the larger item – thus assessing numerous overdraft fees on the smaller items." Nancy feels that the bank should be required to "pay as many items as they can with the amount of money we have in our checking account, and only assess a fair and reasonable fee for the items the account does not have funds to cover." Nancy went on to state that "a $35 overdraft fee is abusive on a $3 fast food purchase – the bank should be required to charge a fair percentage of the actual charge as their fee." Nancy explains, "A smaller item would incur a smaller fee, while a larger item, such as a car payment or mortgage payment, would incur a larger fee. This would be a fair and reasonable practice by the very banks as a taxpayer I am bailing out!"

In her banking experience, Nancy has also had problems with restaurants placing holds on her debit card. She explains, "I had a $20 meal - [the restaurant] swiped my card and I received a $20 hold. After I added $5 for the tip, they swiped another $25. [The bank] was now applying two holds for a total of $45 against my account. It took 3 days for the first hold of $20 to drop off." These holds cause overdraft fees that cause even more overdraft fees because her account remains in the negative – even though she actually did have enough money in the account to pay for the meal initially.

Nancy wants to be able to choose the types of transactions to apply her overdraft protection to, but realizes this option is not realistic. She says, "if the bank requires all or nothing – I would choose nothing," and continues to explain, "if you don't have the money in your account, your ATM card should not let you make the purchase– but more often than not the banks let it go through because they know they can hit us with that $35 fee per transaction." When she attempted to opt-out of overdraft protection with a bank representative, she was told that if a transaction came through and there wasn't enough money in her account to cover it, they would deny it but would still charge her $35 for an "insufficient funds" fee. The bank representative further explained that "if we pay the item as a courtesy to you, you will be charged an overdraft protection fee of $35, if you opt out of overdraft protection, we will still charge you a $35 fee, which we call an insufficient funds fee for returning that item. Our bank has every right to charge the fees we assess." In closing, Nancy really feels that the dollar amount of the fee they charge is "abusive." Nancy reiterates that "the overdraft protection fee and insufficient funds fee need to be based on a percentage of the actual charge. It is absurd to charge a customer $35 for a $2 transaction! If the bank wanted to charge me a $35 fee for paying my $1,200 rent check, I could accept that as fair and reasonable. However, I cannot accept as fair and reasonable, a $35 fee for a $2.79 cup of coffee!"

Justin of Crestone, CO

***" [the representative] said his hands were tied because the bank rules were the bank rules..."* —Justin**

Because Justin's business accepts credit cards, he is required to keep a merchant account connected to his Chase business account. This merchant feature accepts the full amount of a customer's payment and deposits the credit into the business account, and then automatically deducts a fee for the use of the merchant account.

In October 2008 Justin's credit card deducted $250 from his checking account as part of his monthly auto-pay – he was unaware that he had less than $250 in his account at the time. Justin was charged a $35 fee for being overdrawn. Justin then used his business debit card to make a $400 purchase causing another unintentional overdraft – he assumed that if there was not enough money in the account to cover the transaction it would be denied. Within three days, Justin had also accepted a credit card payment from a customer for $150, and when the merchant account deducted its $4.48 usage fee, Justin incurred another $35 overdraft fee. Because Justin did not realize that his account was overdrawn, he was charged an extra $27.50 fee for each of the two overdrafts that were left unresolved.

With $160 total overdraft fees in just three days, Justin contacted his bank representative. Justin recalls, "[the representative] said his hands were tied because the bank rules were the bank rules – when I told him that I don't want overdrafts, and that if I have insufficient funds my charges should be denied, he told me that he could not turn off my overdraft service." Eventually, half of Justin's overdraft fees were reversed – but he explains, "With my business, it takes at least $150 to make a $70 profit." Although he was able to reduce his overdraft charges, Justin attributes his experience to Chase's "bad policy."

Don of Ohio

***"It was a snowball effect, I couldn't get away from it –the more you put in the more they take out."* —Don**

Don and his wife rely on a limited income – the paycheck from his part time job, and the social security payment she receives for disability. Don checks his account balances regularly, but has recently been hit with a flurry of overdraft fees because of his bank's overdraft policy.

In October 2008, Don used his debit card and overdrafted his checking account by 85 cents. Before the bank opened the next day, Don deposited $30 at the ATM thinking that this would cover the 85 cent overdraft – only to discover a day later that he had incurred two overdraft fees, one for the 85 cents and the other because the $30 he had deposited did not cover the deficit caused by the first fee. The second overdraft triggered another overdraft fee and a $5 per day fee for each was also added. Altogether Don got hit with $120 in overdraft fees for an 85 cent overdraft. After haggling with this bank, Don reached a compromise where he only had to pay one of the $35 overdraft fees.

A few months later, in February 2009, Don decided to make a car payment through his bank's online services, for the first time. When he placed this payment for $399, the website stated that it would take 5 business days for the transfer to process. To his surprise, in a few days, Don checked his account and found $468 in overdraft fees. Over two days, Don had used his debit card to make a number of small purchases, mostly under $10, with the understanding that his car payment would be pending for 5 days. To the contrary – the bank had deducted the $399 immediately even though the transaction was still processing, and left his account $64 overdrawn. Each of the small purchases incurred the $35 overdraft fee and he was also paying a $5 per day fee for each overdraft. Luckily, Don was able to negotiate his $468 overdraft fee down to $66, which he thought was unfair. In retrospect, Don explains: "[sixty six dollars] was a hell of a lot more than a 42 cent stamp," which is what it would have cost him to make his car payment by mailing a paper check.

He would have preferred that the bank decline all of the transactions which caused overdrafts. . Don has resolved never to make an online payment through his bank again and is exasperated with all of the trouble he has gone through because of the bank's overdraft policy.

NAFCU

Testimony of

Mark Colley
President and CEO
Tulsa Postal & Community Federal Credit Union

The National Association of Federal Credit Unions

"H.R. 3904, the Overdraft Protection Act of 2009"

Before the

House Financial Services Committee
United States House of Representatives

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Good Morning Chairman Frank, Ranking Member Bachus, and Members of the Committee. My name is Mark Colley and I am here today to testify on behalf of the National Association of Federal Credit Unions (NAFCU). I serve as the President and Chief Executive Officer of Tulsa Postal & Community Federal Credit Union, headquartered in Tulsa, Oklahoma.

Tulsa Postal & Community FCU was chartered in 1923, making us the oldest credit union in the state of Oklahoma. We are a small credit union, with only 11 full-time employees and approximately $23.6 million in assets. U.S. Postal Service employees and retirees, as well as their family members, make up most of our membership base. The rest of our members are people who live, work, or worship in Tulsa County and are classified as "underserved." These are low-income, hard-working people, the vast majority of which are on some form of public assistance.

NAFCU is the only national organization exclusively representing the interests of our nation's federally chartered credit unions. NAFCU is comprised of nearly 800 federal credit unions—member-owned financial institutions across the nation—representing more than 28 million individual credit union members. NAFCU-member credit unions collectively account for 79 percent of the assets of all federal credit unions. NAFCU and the entire credit union community appreciate the opportunity to participate in this hearing regarding H.R. 3904, the *Overdraft Protection Act of 2009.*

Historically, credit unions have served a unique function in the delivery of financial services to Americans. Established by an act of Congress in 1934, the federal credit union system was created, and has been recognized, as a way to promote thrift and make financial services available to all Americans, many of whom would otherwise have no access to financial services. Congress established credit unions as an alternative to banks and to meet a precise public need—a niche that credit unions continue to fill today for approximately 92 million Americans. Every credit union is a cooperative institution organized "for the purpose of promoting thrift among its members and creating a source of credit for provident or productive purposes" (12 U.S.C. 1752(1)). While 75 years have passed since the *Federal Credit Union Act* (FCUA) was signed into law, two fundamental principles regarding the operation of credit unions remain every bit as important today as in 1934:

- Credit unions remain committed to providing their members with efficient, low-cost personal service; and
- Credit unions continue to emphasize traditional cooperative values, such as democracy and volunteerism.

Credit unions are not banks. The nation's 7,691 federally insured credit unions serve a different purpose and have a fundamentally different structure, existing solely for the purpose of providing financial services to their members. As owners of cooperative financial institutions united by a common bond, all credit union members have an equal say in the operation of their credit union—"one member, one vote"—regardless of the dollar amount they have on account. Unlike their counterparts at banks and thrifts, federal credit union directors generally serve without pay—a fact epitomizing the true "volunteer spirit" permeating the credit union community.

Credit Union Overdraft Services

Most credit union members welcome and appreciate the opportunity to benefit from a courtesy pay or overdraft protection program, and consider it a useful and convenient service. Overdraft programs can prevent high fees and penalties that result from bounced checks, and provide important financial coverage in unexpected circumstances when members may need it most. For instance, the nation's largest retailer, Wal-Mart, charges a $35.00 fee for a returned check. Many credit union members have thanked their credit unions after using these services and have added that, as with insurance, they did not realize the true benefit until they actually needed it.

At Tulsa Postal & Community FCU, we currently provide courtesy pay programs for 936 of our 1,440 share draft (or checking) accounts. Only two of those 936 members have chosen to opt out of the courtesy pay program. In order to be enrolled in the program, a member must select a transfer from another deposit account as the first overdraft coverage option; courtesy pay is not triggered unless coverage is still needed after transfer options have been exhausted. Members must also qualify for courtesy pay protection. We check each applicant's credit history, eFunds, and past performance on checking accounts; in short, we do essentially the same kind of underwriting as we would for a car loan. Furthermore, we have several casinos in the vicinity, and if we notice frequent casino activity, we shut off debit cards and courtesy pay to prevent our members from running up high debts.

We also do not report any overdraft protection balances to ATM or debit networks. Only funds that actually exist and are available in a member's account are displayed. In addition, if a member comes to us concerned that they have overdrafted their account because of an error, we refund 100% of the courtesy pay fee they were charged. If this happens multiple times, we ask them to come in so that we can educate them about proper use of the service. I have read the stories about individuals who are charged a $35 fee for spending just a few dollars more than what they have in their accounts. At my credit union, we refund these fees without a problem, provided the member does not abuse the privilege. Many credit unions do the same, as they have a finite field of membership and cannot afford to lose members. This program prevents our members from seeking to obtain funds they need from the pawn shop across the street from our credit union, or from local payday lenders who charge high interest rates and can institute legal action in Oklahoma if these rates are not repaid within 14 days. We have never had a single member complain about our courtesy pay program.

While overdraft and courtesy pay programs vary from credit union to credit union, data from the Government Accountability Office (GAO) has demonstrated that credit union overdraft protection programs are generally more favorable to consumers than are those at banks and thrifts. According to the findings contained in a January 2008 GAO Report on Bank Fees, commissioned by Congresswoman Carolyn Maloney, banks and thrifts charge higher fees on almost all checking and savings account services. The GAO report specifically stated that "on average, large banks and thrifts consistently charged the highest insufficient funds and overdraft fees, while small credit unions consistently charged the lowest." Furthermore, NAFCU data shows that approximately 83% of our members who offer overdraft protection programs have waived overdraft or NSF fees for their members, whether the member requested that the fee be waived or not. In addition, 98% of NAFCU credit unions offer their members the choice to opt-out of overdraft protection programs, if they choose to do so.

Finally, although the report notes that the percentage of income institutions are deriving from non-interest sources has somewhat risen since the year 2000, this increase is not solely the result of a rise in fees. According to the GAO, the growth in non-interest income over the last few years may be due in significant part to consumer behavior. The report found that more and more consumers are using electronic forms of payment, which result in instant debits to their account. Since electronic payments can be made in large numbers very quickly, overdraft charges can likewise be incurred at an increased rate.

H.R. 3904, the *Overdraft Protection Act of 2009*

I would now like to turn to H.R. 3904, the *Overdraft Protection Act* introduced by Congresswoman Maloney last week. This well-intentioned legislation would make considerable changes to overdraft protection programs at all financial institutions, including federal credit unions.

NAFCU appreciates the bill's effort to address credit union concerns with the inclusion of overdraft protection programs under the *Truth in Lending Act* (TILA). Under TILA, any fee associated with an overdraft protection program would be counted as a finance charge. This would pose a particular problem for federal credit unions, as they are the only federal financial institutions subject to a statutory usury ceiling of 18%. Since it is impossible for a credit union to determine when a member will pay back an overdraft credit line, it cannot calculate the APR when an account is overdrawn, meaning every transaction could potentially violate the usury ceiling. Under H.R. 3904, credit union overdraft fees would be exempt from the usury ceiling, addressing a significant credit union concern. We thank Congresswoman Maloney for taking this critical issue into account when drafting this legislation.

The *Overdraft Protection Act* continues to be problematic from a credit union perspective, however, and NAFCU maintains several significant concerns with the legislation and opposes it in its current form.

First, the current "opt-in" provision contained in the bill would impose a considerable regulatory burden on credit unions and create consumer confusion among those who believe that they already have this protection. This requirement would cause significant operational difficulties, particularly for smaller institutions. Credit unions would be forced to contact their members, who currently enjoy these programs, to obtain an affirmative response stating they would like to continue to receive a service from which they already benefit and which many believe is already in place. NAFCU would support language establishing an "opt-out" requirement instead, allowing existing members who are currently covered by overdraft protection programs to deny the coverage if they wish. This would reduce the burden on credit unions while still providing consumers with the option of avoiding any charges associated with overdraft protection programs. We would support a provision stating that all providers of such programs are required to contact their members after enactment of the legislation to notify them of their ability to opt out. We could also support a condition that new member or customer accounts include an opt-in requirement, as those that are signing up do not already have a presumption that they are being provided with these services.

Second, NAFCU is concerned about provisions in the bill limiting NSF fees for debit card and ATM transactions. These types of transactions are covered by financial institutions when the transaction is made, even if there are insufficient funds in the consumer's account at the time the transaction actually clears. Since the transaction is authorized by the merchant at the time it takes place, the credit union is contractually obligated to post the payment, even though the funds are not available in the consumer's account to cover it. Many credit unions complain that merchants are not checking accounts in "real time" to ensure a transaction has cleared the account and does not create an overdraft. Merchants instead often process all transactions at the end of the day, when a consumer's multiple transactions may cause him or her to overdraft several times. As it stands, this provision appears impractical and impossible to comply with unless all merchants were required to process in real time. The limitation to one overdraft fee per month is therefore highly problematic for the vast majority of credit unions that receive transactions not cleared by the merchant at the exact point in time that they are made.

Further, providing same-day notification to members who have overdrawn their accounts would constitute another considerable burden for credit unions. Credit unions that batch their transactions may not learn that an overdraft has taken place until all transactions clear at the end of the day, including checks. It would also be impossible for a credit union to provide notification to a consumer the same day an account has been overdrawn, if merchants process all transactions at the end of the day. NAFCU could support a more reasonable and realistic notification timeframe, however.

I would also like to add that many of the policy concerns that have been expressed in relation to overdraft protection programs and disclosures at financial institutions will be addressed when the Federal Reserve makes changes to Regulation E next year. The Federal Reserve has already issued a proposed rule prohibiting the assessment of overdraft fees for the payment of ATM withdrawals and one-time debit card transactions, unless the consumer is given notice of the right to opt out of overdraft protection and chooses not to, or if the consumer specifically opts in to overdraft protection. The changes may also speak to some of the concerns that form the basis for this legislation.

NAFCU is also concerned about the bill's limitation on the number of overdraft coverage fees charged by a depository institution. We believe that the restriction to no more than one overdraft fee per month and six overdraft fees per year would significantly limit consumer choice. To limit a consumer who is fully informed of his or her choices and decides on this product, smacks of a big-brother approach. In order to continue to provide consumers with the choice of benefiting from overdraft protection, NAFCU instead proposes that the bill require financial institutions to send a notification to consumers who have overdrafted several times during the course of a month delineating other options available to them. Consumers would then have the choice of opting out of the overdraft protection program, continuing to receive overdraft coverage, or obtaining some form of credit from the institution, such as a short-term loan.

NAFCU does support efforts to prevent overdraft fee maximization. We are opposed to attempts by some financial institutions to take advantage of consumers by manipulating the order in which transactions are posted, as a way to increase their overdraft fee revenue. In fact, many credit unions, particularly those with university and college student fields of membership, seek to post the smallest transactions first to prevent their members from being charged avoidable overdraft fees.

NAFCU also supports efforts to increase disclosure. At Tulsa Postal & Community FCU, we provide our members notification on their monthly statement of the amount of overdraft fees paid in the previous month and their year-to-date total. We believe such a disclosure requirement is reasonable.

We would also support Congress making changes to increase the outdated limitation on the six Regulation D transfers the Federal Reserve allows each month. This arbitrary limitation is actually harming consumers and restricting many overdraft programs. Many credit unions, like mine, use their members' savings accounts as a first line of defense when an overdraft takes place, by making automatic transfers from savings accounts to cover overdrafts, often at no charge. However, this outdated limitation only permits such transfers six times a month, meaning members would then have to resort to courtesy pay programs for protection and face additional fees. We would encourage this change to be included as part of any overdraft reform legislation.

Enactment of the *Overdraft Protection Act* in its current form will likely cause many federal credit unions to end overdraft protection programs for their members, drying up an important customer service. The many members who currently benefit from these programs would lose this option; what is worse, if they are unaware of this change in the law and do not read the disclosures they are sent from their financial institutions, consumers may continue to assume that they have overdraft coverage and potentially incur even higher fees for their bounced checks, or have important transactions declined.

Many credit unions are no longer primarily interest income-only institutions, and rely on fee income to continue to operate. The exponential growth in the number and complexity of regulatory requirements on financial institutions is staggering, and the constant change in these requirements necessitates the hiring of additional legal and compliance staff. Moreover, credit unions are limited in the amount of non-fee income they can raise. Credit union options for balance sheet management are limited in that they may only raise capital through retained earnings. While there is industry support for other sources of capital being raised from the membership, at present, Congress has not changed the capital regime for credit unions. In addition, as I mentioned earlier, credit unions are subject to an 18% usury ceiling. While a good thing, this cap significantly limits the amount of income credit unions can derive from interest, as compared to other financial institutions.

Furthermore, such limitations on credit union income as those contained in H.R. 3904 could severely impact the ability of many credit unions to continue to operate, and potentially force some of our smaller members to close their doors forever. Credit union members in some regions, particularly rural and low-income areas, may have few other banking options and may be forced to look to payday lenders, check cashiers, and pawn shops to obtain the financial services they need. NAFCU does not believe that this is the result the *Overdraft Protection Act* is seeking to achieve.

NAFCU welcomes the opportunity to work with members of the Committee to address credit union concerns with this legislation and improve it for both consumers and financial institutions. While we support the Committee's mission to increase protections for consumers, we believe that this legislation is deeply flawed and could severely hurt both credit unions and their members if enacted in its current form.

Conclusion

In conclusion, I would like to note that when I joined Tulsa Postal & Community Federal Credit Union in 2002, our net worth was less than 4% and we had a CAMEL rating of 4.5. Previous management's poor performance in following loan and accounting policies nearly resulted in a forced merger. My staff and I have worked very hard to rescue this credit union, and our net worth is now up to 7.8%. This year, for the second year in a row, our credit union has earned a CAMEL 1 rating after its NCUA examination. We are dismayed to learn that all of our hard work may be for nothing should the *Overdraft Protection Act* become law. Although our credit union only earned $150,000 from overdraft fees in 2008, these fees made the difference between being open to serve our members this year, or possibly closing our doors after 86 years of service and forcing our members to find other options, such as the pawn shop across the street or the payday lenders around town.

Credit union fees for overdraft protection and courtesy pay programs continue to be lower on average than they are at banks and thrifts, but are an important source of income for these not-for-profit institutions. The limitations that would be imposed by this legislation would cause considerable drops in income for most credit unions, forcing many of them to either make up their losses by charging for other services, or face the possibility of going out of business. Finally, I would urge the Committee to keep in mind that consumers can avoid overdraft fees no matter what the law is, in one simple way – by managing the funds in their accounts. Increased focus on financial education and literacy to teach consumers this personal responsibility would make the need for overdraft protection moot. We urge the Committee to take these concerns into account and make some significant changes to the legislation before it moves forward.

I thank you for the opportunity to testify before you today, and I welcome any questions that you may have.

STATEMENT OF

DENNIS DOLLAR

FORMER CEO
GULFPORT VA FEDERAL CREDIT UNION
GULFPORT, MISSISSIPPI
AND
FORMER CHAIRMAN
NATIONAL CREDIT UNION ADMINISTRATION
ALEXANDRIA, VIRGINIA
AND
CURRENTLY,
PRINCIPAL PARTNER
DOLLAR ASSOCIATES, LLC
BIRMINGHAM, ALABAMA

BEFORE THE

HOUSE COMMITTEE ON FINANCIAL SERVICES

HEARING ON
HR 3904
"THE OVERDRAFT PROTECTION ACT OF 2009"

FRIDAY, OCTOBER 30, 2009

Good morning. My name is Dennis Dollar. I served as a member of the National Credit Union Administration Board from 1997 to 2004 and as the NCUA Chairman from 2001-2004. Prior to that appointment I was President and CEO of the Gulfport VA Federal Credit Union, a relatively small $32 million credit union with approximately 12,000 members in Gulfport, Mississippi. Since leaving NCUA, I have formed a consultancy that works with credit unions and other financial service entities in their strategic initiatives.

I guess you could say that, from my experience, I have had the opportunity to view the overdraft protection issue, as Judy Collins famously sang in the 1960s, from "both sides now." Today, I have been asked by Ranking Member Bachus to come before you representing no particular group or organization, only as a former credit union CEO and a former credit union regulator who now sees overdraft protection programs in action on a daily basis and whose experience indicates that, while there are always ways in which such programs can be structured better for both the consumers and the financial institutions they do business with, it would not be good public policy to effectively eliminate them from the marketplace as HR 3904 would effectively do.

During my years in credit union management there was no overdraft protection program offering. If a member wrote a bad check, we charged a NSF fee and returned the item. For concern about being discriminatory about which ones we honored and the ones we didn't, we seldom honored the item. Our hope was that the NSF fee would have a deterrent effect on the member writing bad checks and, if abuse continued that caused significant loss to the credit union, we often referred the matter to local prosecutors to initiate criminal proceedings.

Needless to say, the members, who like all consumers are always opposed to any user fee imposed upon them, did not like this fee assessment process at all. They not only faced our NSF fee, but they were often charged an additional returned check fee by the merchant to whom they wrote the item. Often they also faced late charges if the returned item was for their rent or insurance. I even dealt with some irate members who said we cost them their insurance renewal or their apartment lease because we wouldn't honor a check on Friday when they had a payroll ready to post to their account at our credit union on Tuesday.

In most instances, those members were rightfully upset. NSF fees can be very punitive and, frankly, ours did very little to deter the need some members felt to write a check for rent, groceries or insurance when the payment was due – even when they knew a deposit to cover the check was still a few days away. They hoped that either we would waive the NSF fee for them or that they would be able to cover it from their next deposit, but their situation in life left them few options but to use the NSF process to help them try to manage their cash flow. These folks were not slugs or deadbeats. They were good, hard working members who on occasion simply ran out of money before they ran out of month.

It was for these members that the overdraft protection programs we are here today to discuss were developed to assist. Rather than being charged a NSF fee, the member would be charged an identical fee (it is important to recognize that, if structured properly, an overdraft fee is not an additional fee above and beyond the NSF fee) to honor the overdrawn item up to a specific fully disclosed limit and that the item must be settled within 45 days or it would be written off and formal collection efforts begun.

Credit union members, as did bank customers, saw value in these programs because they were able to realize the additional cost savings associated with avoiding merchant fees, late charges and cancellations of service. In addition, these programs (for the same amount of fee they were otherwise being charged when their financial institution bounced their check and assessed a NSF fee) prevented the embarrassment and potential legal liability of writing a check that was returned for insufficient funds. A well structured overdraft protection program could also enable them to maintain their relationship with a traditional financial institution and not be forced to go outside of the financial mainstream for their short term cash flow needs.

As consumers began to utilize these programs, financial institutions began to find themselves with considerable earnings from these programs. These earnings, at least in the overwhelming majority of credit union cases of which I am familiar, did not come from manipulation of the programs to maximize earnings or failure to disclose the terms of the programs so that consumers did not know what they were doing. The earnings came because the consumer recognized a benefit, or a value, from the program and used it when needed.

When some of the critics claim that consumers do not see any value in these programs and feel ripped off by them, but yet the financial institutions are making a significant amount of fee income each year from the programs – something just does not compute. It is important to note that overdrafting an account is a controllable action. Consumers can always choose to write the check later, make the debit purchase at another time or withdraw from the ATM after their next payroll posts. The fact that financial institutions have increased earnings from these programs should not automatically be viewed as suspect, but rather should be seen as evidence that the consumer sees some value in overdraft programs and is comfortable utilizing them when needed.

Does that mean there is not some abuse? Certainly there is abuse. We've all seen documented examples where there was manipulating of item clearance order solely to maximize profits or assessing $35 in overdraft fees on a $5 debit purchase of a venti cup of latte at Starbucks. Those exceptions should be corrected and appropriately regulated.

But overdraft programs can be done right and should be done right. When that happens, consumers and financial institutions benefit.

Overdraft program disclosures must be accurate and in plain English. The right to "opt out" upon request by the consumer should be honored at any time. A written notice of right to "opt out" should be clearly provided to all participants on at least an annual basis. Ongoing cumulative totals of overdraft fees should be clearly disclosed on monthly statements. Smaller overdrafts could be exempted or perhaps a smaller fee assessed on smaller transactions. Daily limits on the number of overdraft fees could be imposed. Check processing order should be disclosed and perhaps options for the processing order given to the consumer. When technology allows it, even an "opt out" at a point of sale would be a best practice worth implementing.

Most of the above listed standards are the way most responsible financial institutions handle their overdraft programs today. Because some institutions do not follow these best practices does not, in my view, make a case to over-regulate those who do with punitive or burdensome legislation that will result in many consumers losing their checking accounts and many financial institutions being forced to transfer the costs of overdrafts from the consumers who use these programs to the vast majority who do not.

Fewer loans. Shorter hours at the branch. Less interest on a CD. A reduction in new branches. All of these could be among the consumer costs and service casualties of financial institutions losing access to this user based fee program.

But, although my regulatory experience gives me great pause about the potential impact on the long term safety and soundness of some institutions that could come from effectively eliminating this source of earnings, my primary reason for supporting these types of programs is the benefit to the consumer of getting his check or debit honored (up to clearly defined and disclosed limits) for the same fee that would otherwise be imposed upon him as an NSF fee. In my view, the additional merchant fees and late charges that a consumer will face if items that were previously honored are now bounced could conceivably bring a backlash against any legislation or regulation that makes these programs too costly to offer.

If there is no deterrent in the system, bad check writing will grow. A half century of NSF fees, often increasing in amount, proved that the number of overdrafts would not be lowered simply by charging fees. Overdraft programs, with the proper disclosures and a financial education commitment on the part of those offering them, can provide greater consumer value and improve the likelihood of someone getting out of their cycle than would doubling their costs with merchant fees and late charges from NSF check returns.

To limit the number of overdrafts that a financial institution can charge to one monthly or a maximum of six per year as this legislation proposes would be a moral hazard equivalent of someone being only subject to one parking ticket per month. What would then be in place to prevent an individual from parking by the fire hydrant each of the other 30 out of 31 days each month since he has already received his one citation for the month. Property could be in considerable danger if a deterrent is not in place. Others should not have to pay for an individual's irresponsibility.

The same concept applies in the case of overdraft programs.

Credit unions, which are the primary group of financial institutions that I work with, have not been among the abusers of overdraft programs. I strongly urge the focus of any statutory or regulatory action to be on abuse of these programs, not in effectively dismantling them from those who do the right thing in administering their overdraft programs.

My background as a federal regulator who sat on the Federal Financial Institutions Examination Council for four years from 2001 to 2004 leads me to believe that the regulatory agencies are best positioned to police this arena and to eliminate abuse of overdraft programs.

Solid regulatory scrutiny and enforcement action can protect these valuable programs for both consumers and financial institutions. Abuse can be ferreted out and best practices put in place.

The result can be a balanced approach to overdraft protection that does not return us to dark ages of costly NSF fees, merchant fees and late charges but yet does not create a cycle of dependency on such programs. A regulatory balance can keep consumers within the traditional financial institutions but yet ensure that these programs are fully and understandably transparent with reasonable limits in place for both the consumer and the financial institution. Legislation that would largely dismantle these programs through untenable restrictions that would force financial institutions to eliminate their overdraft protection programs is not good public policy.

October 30, 2009

Testimony of

Nessa Feddis

On Behalf of the

AMERICAN **BANKERS** ASSOCIATION

Before the

Committee on Financial Services

United States House of Representatives

AMERICAN BANKERS ASSOCIATION

Testimony of Nessa Feddis
Before the
Committee on Financial Services
United States House of Representatives
October 30, 2009

Chairman Frank, Ranking Member Bachus, and members of the Committee, my name is Nessa Feddis, vice president and senior counsel of the American Bankers Association (ABA). The American Bankers Association brings together banks of all sizes and charters into one association. ABA works to enhance the competitiveness of the nation's banking industry and strengthen America's economy and communities. Its members – the majority of which are banks with less than $125 million in assets – represent over 95 percent of the industry's $13.3 trillion in assets and employ over 2 million men and women.

I appreciate the opportunity to testify today on overdraft protection and H.R. 3904 which was recently introduced by Representative Maloney (D-NY) and Chairman Frank (D-MA). The bill will regulate and limit overdraft services, services which government consumer testing has found bank customers value and expect. In addition, the bill would have significant business and technological challenges that will mean a complete retooling and redesign of checking account features and particularly its pricing. The result will be more hassle and costs for consumers who find their payments returned or rejected, and the bill will likely have significant unintended consequences on the availability of services and cost to all checking account customers.

In my testimony today, I would like to make several points:

- Consumers value depository institutions paying their overdrafts – and have come to expect it – as it helps to avoid the embarrassment, inconvenience, fees imposed by merchants and others, and other adverse consequences of having a check bounce or a transaction denied.

- Overdrafts fees are very easy to avoid and most consumers avoid them. The banking industry has been responsive to consumer concerns and will continue to work to improve overdraft protection practices. Even prior to some recent announcements by some banks about limiting and reducing overdraft fees, many institutions had already adjusted policies so that fees are not imposed for small overdrafts and the number of overdrafts is limited.

- H.R. 3904 would require significant changes in the business model for transaction accounts and a retooling of technology necessary to support them, all of which will have significant unintended consequences.

I would like to discuss each of these in turn.

I. Consumers Value Depository Institutions Paying Their Overdrafts

American consumers enjoy the most affordable, efficient, and accessible banking system of any country in the world. Today, consumers can open a checking account with a minimal deposit and have access to the entire menu of payment services -- ***at little or no cost.*** They can write checks, use debit cards to withdraw cash or make purchases, pay bills, and make fund transfers online 24/7 from virtually anywhere in the world – all for free. Indeed, a 2008 Government Accountability Office report found that most banks offer free checking accounts. For consumers, such an easy and convenient service, however, comes with important responsibilities.

Bank response to consumer demand drove this expansion of payment services, access, capabilities, and pricing (including free checking). In the memories of many of us, bank accounts typically had minimum balance requirements and maintenance fees. Today, those minimum balance requirements and maintenance fees are not the common experience. With the elimination of the minimum balance requirement, there is no longer the incentive to keep a cushion which helps customers to avoid inadvertent overdrafts. This means customers must manage their accounts more carefully and keep them from going below zero.

In the best of all worlds, people would only write a check or make an electronic payment when there are sufficient funds in their bank accounts to cover the transaction. Of course, this is not a perfect world. There are also many different ways for consumers to make payments today, which, while convenient for consumers, increases the challenge for them to know what payments they have made and what resources are available to them in their bank accounts to cover them.

Today's modernized version of bank's traditional practice of paying overdrafts helps customers manage these challenges. Bank overdraft accommodations are successful because they provide desirable back-up for customer payment decisions. People want the bank to recognize that when they inadvertently overdraw their account they can be trusted to make it right and understand what they will pay for the bank's accommodation.

Most consumers generally want banks to pay their overdrafts even if it means paying a fee so they can avoid the inconvenience, embarrassment and potential cost of having a payment or transaction rejected. In fact, 96 percent of customers who had the overdraft covered by their bank were glad the payment was covered. Similar studies by the Federal Reserve also documented that most participants expect and want coverage to ensure their transactions went through and felt it was a positive feature.[1] This is because consumers understand there are costs and consequences of having a payment rejected or returned. Return or rejection of a check or electronic payment, for example, means not only paying an additional fee to the person who received the check or electronic payment, such as the mortgage lender, landlord, or merchant, but not having checks or automated payments accepted in the future and instead being required to purchase a money order or pay by cash. It may also mean an important bill is not paid on time which causes negative information to be put into a credit report. Customers also often want their debit card transactions to go through, whether it is for groceries already selected and bagged or for a meal that has already been eaten – or a bill they want paid though their debit card.

Consumers have also shown a keen understanding of the timing of transactions and how to manage within the overdraft accommodations provided by the bank. For example, some customers are aware of and avail themselves of the fact that even with debit card transactions, there is some window of opportunity to deposit funds ***after*** a transaction is made. For example, someone can make a purchase in the morning with their debit card – uncertain about their available funds at that time – and transfer or deposit money into their account before the books are closed for that day to cover the shortfall. Indeed, banks have reported that over half of debit card transactions for which there were insufficient funds at the time the transaction was made settle into good funds. This means that even though there was not enough money in the account at the time of the transactions, there is money in the account when it settles later that night. Some customers have obviously figured out that they can use their card during the day even though there are insufficient funds so long as they make a deposit before the end of the day -- and avoid an overdraft fee.

Today's "bounce protection" or overdraft accommodation programs are basically the latest, customer-driven innovation of this traditional practice. The primary difference is that many of the more recent overdraft protection practices rely on automated systems. The advantage of the automation of the historical practice of paying overdrafts on a discretionary basis is that it reduces costs associated with case-by-case assessment and manual intervention and promotes consistent treatment of customers.

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[1] "Review and Testing of Overdraft Notices," Federal Reserve, December, 2008

II. Overdraft Fees are Easy to Avoid and Most Consumers Avoid Them

Keeping track of transactions and the balance is critical to avoiding overdrawing an account. This is, of course, never a pleasant task and most of us would like to avoid it altogether. But doing so is part of good financial management and an important responsibility of using any transaction account. Writing transactions in the checkbook or ledger is, of course, the best way to track transactions. This is even more important today with the variety of ways that customers have available to make transactions.

Another reason for customers to keep track of their transactions is that there are occasions when the bank's record of the balance will not reflect transactions the customer has authorized, but which have not yet reached the bank. This includes not only checks written and scheduled automatic payments, but also some debit card transactions. For example, some merchants will forego transaction processing, especially for small dollar transactions which tend to draw the most attention. To save time or money the merchants verify that the card is valid, but choose not to get authorization. Thus, while the customer knows about the transaction, the bank has no knowledge of the transaction until it arrives at the bank that night or even later. The bottom line is that customers are in the best position to know what their actual balance is – only they know what checks they have written, automatic payments they have authorized, and debit card transactions they have approved.

Customers can – and should – check their balances and transactions often by phone, at the ATM, online, or using the Internet browser on their phone or other handheld devises. Knowing the balance – but also what transactions have been authorized by the customer but have yet to be processed and are not reflected in that balance – are very important to avoid overdrafts. Simply put, consumers are in control of their finances and can avoid overdraft fees.

Even with careful tracking, however, inadvertent overdrafts can occur. This is why banks have traditionally paid overdrafts on a discretionary basis, based on the historical activity of the account and the likelihood that the accountholder will cover the overdraft. However, customers who find it challenging to manage their accounts and avoid overdrafts have other options available to them. Many consumers avoid overdrafts by maintaining a cushion in the account to cover transactions they may have forgotten about or not written down in the checkbook. Others, for example, link their account to a savings account, credit card, or line of credit to cover overdrafts. In contrast to simple overdraft accommodation provided as a courtesy by banks, overdraft lines of credit are legal agreements where the bank is obligated to pay overdrafts and customers must complete applications and be subject to the bank's underwriting standards to qualify. What works best for one customer may not work as well for another.

Depository institutions will also often waive the fee for an initial or occasional overdraft. After the first incident, the consumer is then aware that debit card transactions may cause an overdraft and can take appropriate steps to avoid them. Of course, customers dissatisfied with their bank's services have many other banks to choose from in our very competitive industry.

In addition, most depository institutions permit customers to opt out of having overdrafts authorized or paid. The FDIC found the fast majority (86 percent) gave customers a choice: 75.1 percent allowed opt out and 11 percent provided opt in.

While anyone's bank account can fall short from time to time, overdraft fees are 100 percent avoidable. Just like a parking ticket or speeding ticket, they are meant to be a deterrent. Like any penalty, they are designed to get the person's attention in a way that nominal fees simply do not. In fact, most consumers manage their accounts and avoid any overdraft fees. In an annual survey of 1,000 consumers conducted by Ipsos-Reid for the ABA in 2009, 82 percent of bank customers said they did not pay an overdraft fee in the previous 12 months (up by two percent from the year before). Clearly, consumers who pay overdraft fees are the minority, and that number is shrinking.

Simply put, overdraft protection is an important service for our customers. We believe customers should understand the process, the responsibilities to track deposits and withdrawals, and any fees associated with overdrafts and options to avoid them. Banks can and do provide convenient access to account information today to help customers manage their financial flows, but ultimately it is consumers who are in the best position to track and manage their accounts.

III. H.R. 3904 Would Require Significant Changes Which Will Have Many Unintended Consequences

The ABA is very concerned about the potential unintended consequences that would result from H.R. 3904. Below we highlight some, but not all, of the specific concerns that we have:

Limits on overdraft fee amounts: Overdraft fees are set to create incentives for good management of accounts and discourage overdrawing of the account. This is very similar to the incentives provided for parking illegally or speeding tickets. These fees are designed to get people's attention in a way that nominal fees simply do not. If parking fees or speeding tickets were set according to the cost of enforcement, there clearly would be many more cars parked illegally and many drivers would ignore speed limits altogether.

The bill limits the amount of overdraft fees to those that are "reasonable and proportional to the cost of processing the transaction." First, the cost of "processing" ignores the deterrent value of overdrafts. Second, the cost of "processing" the overdraft does not possibly reflect the risk of loss that the bank assumes in providing the overdraft coverage. This risk varies by the type of account and how well the customer has managed the account and how often the account is overdrawn.[2] Third, the cost of processing does not reflect the consequences of a negative balance on the account. Because the bank has to cover this deficit, it is not able to use those funds for other interest earning purposes, such as loans. This lost income makes it more difficult to provide checking account services for all depositors and means that those who manage their accounts well must absorb those costs in the form of higher or additional fees and/or fewer services.

Such artificial limitations – which do not reflect either the value of the product to consumers, the incentives it creates, the risks involved, or the opportunity cost that ultimately impacts the cost of transaction accounts for depositors – will lead to significant unintended consequences. As history has shown time and time again, government price fixing does not work and ends up hurting the very people it is intended to help.

Limitations requiring not more than one overdraft charge per month and six per year: In effect, this provision limits consumer choice by prohibiting overdrafts they want paid from being paid. Under the bill, banks would return or reject overdraft transactions once the maximum fee limits have been met. Some banks might simply not offer overdraft protection at all, given the limits on the amount of fees as they will not cover the actual costs and risks associated with paying an overdraft. This means consumers will suffer the consequences as discussed earlier: the hassle, inconvenience, costs, and embarrassment of rejected or returned items – the very reasons that consumer testing has found people value and want the service.

There are also negative consequences for those accepting the payments. For example, a landlord might not have the funds to meet her or his own obligations or the merchant might end up providing merchandise for free. A restaurant might not get paid for a meal or a grocer might have to spend resources to re-stock the shelves for items left un-bought or discard them. To protect against the risk, banks may re-institute minimum balance requirements to encourage customers to have a cushion

[2] Some overdrafts cannot be avoided. For example, as discussed, some merchants do not obtain authorization and as a practical matter, the bank cannot return the item when the actual transaction is presented to the bank. In addition, there are numerous other circumstances when transactions cannot be returned or rejected, e.g., when transactions go to a back-up system.

or re-institute monthly fees for checking accounts. Thus, such a provision ends up hurting customers that have managed their accounts well and rarely if ever overdraw their account.

Effective APR Calculation. H.R. 3904 classifies overdraft coverage fees as "finance charges" – and hence include them in disclosed calculations of interest rates. This means that banks would have to calculate an effective annual APR for those fees. Given that the number, amount, and duration of overdrafts are unknowable in advance (and are entirely within the control of the customer), it is obviously not possible to incorporate them into a nominal or forward-looking APR calculation.

The alternative is to use a historical or effective APR. However, consumers do not understand effective APRs, raising questions over whether this cumbersome process for calculating interest rates in the bill makes any sense. Given the nature of overdraft fees, the APR will be greatly inflated to the point of distortion. Any time an ***annual*** percentage rate is calculated for a term ***less than a year***, the inclusion of a fixed fee, even a modest one, will distort and overstate the APR. In the instance of overdrafts, the fee is fixed, the overdraft often small, and the term of repayment short (as the banking agencies encourage banks to request prompt repayment). It is easy to see how triple digit APRs would result. However, it is not at all clear how this would be meaningful to or assist consumers.

First, the shorter the repayment period, the greater the APR will appear in instances where there is a fixed fee. **This means that the *sooner* the consumer repays, the *greater* the calculated APR – a difficult concept to explain to consumers, as it appears that paying *earlier* actually *increases* the cost of credit and that it is better to delay repaying the overdraft.**

Second, the larger the amount overdrawn, the lower the APR will appear in instances where there is a fixed fee. This means that the more customers exceed their available funds, the lower the APR, implying it is better to overdraw one's account by more rather than less. Such a lesson is contrary to sound personal account management.

Third, the inflated and distorted APR will confuse consumers as they attempt to reconcile this APR with other APRs with which they are familiar, such as the nominal APRs for credit card, home, auto, and personal loans. The result will be to dilute the effectiveness of the APR generally, rather than enlighten them with regard to overdrafts. In the overdraft fee context, consumers understand a dollar amount far better than an inflated and meaningless APR.

Indeed, in a recent study, the Federal Reserve noted, "The quantitative consumer research conducted by the Board validated the results of the qualitative testing conducted both before and after the June 2007 proposal; it indicates that most consumers do not understand the effective APR, [as applied to open-end credit such as credit cards] and that for some consumers, the effective APR is confusing and detracts from the effectiveness of other disclosures." For this reason, the Federal Reserve has rejected the effective APR for open-end credit and in its stead will soon require disclosure of total interest and fees (by period and year to date) to be disclosed on periodic statements – because this is what customers understand.

Technological and other issues: There are also a number of other issues the legislation poses for which we are happy to provide additional information. They include technical operating issues as well as inconsistency in the legislative language that creates ambiguity and uncertainty, and thus potential liability for inadvertent violations. Other issues involve serious technological difficulties related to ATMs not owned by the bank and debit card holds that will impact all institutions, but particularly small and medium size banks.

Conclusion

Mr. Chairman and members of the committee, ABA believes that overdraft protection services provide a valuable service to bank customers and small businesses. Taken together, the provisions of H.R. 3904 will mean a complete retooling and redesign of checking account features. The result will be more hassle and costs for customers who find their payment returned or rejected; less access to checking account services for some people; and higher prices due to the higher cost of providing bank accounts. It will also mean that those who manage their accounts well will pay for those who do not. Because of these and other significant unintended consequences, ABA has to oppose H.R. 3904 in its current form. We are ready to work with this committee to address ways to improve how overdraft accommodation programs serve bank customers.

Consumer Federation of America
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Testimony of

Jean Ann Fox
Director of Financial Services
Consumer Federation of America

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 House Financial Services Committee

Regarding
H.R. 3904, the Overdraft Protection Act of 2009

October 30, 2009

Chairman Frank, Ranking Member Bachus, and members of the Committee, I appreciate the opportunity to testify in support of the **Overdraft Protection Act of 2009, H.R. 3904**, 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 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.

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

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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 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 H.R. 3904 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.

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 H.R. 3904, a solution that will put real protection back into overdraft policy.

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, 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.

<u>Overdraft Loans Give Banks First Claim on Consumers' Pay or Benefits</u>

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

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[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"].

[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').

account fees under the Truth in Savings Act. As a result, banks can and do use their 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 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

[9] FDIC Study. *Id.*
[10] ORCI Poll for CFA, July 2009.
[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.

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]

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

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[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 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

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.

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.

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).

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

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.[26] 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.[27]

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.[28] The survey further found, not surprisingly, that

[26] *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."

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

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

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.[29]

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.[30] 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.

Consumers Want Choice and Warning on Overdrafts

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

29 FDIC Study at 62.
30 CFA ORCI Poll, July 24-27, 2009.

the default arrangement for most institutions continues to be coverage—whether or not the account holder asked for it.

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.[31]

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.[32] 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.

[31] *Consumer Reports* National Research Center, Financial Regulation Poll, as filed with the Federal Reserve Board in Reg E Docket R-1343, March 12, 2009.
[32] CUNA News: "Consumers ignore ATM fees, get irked at overdraft fees," January 17, 2006

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.[33] As a result of the outcry over this practice, Congress stepped in, amending TILA in 1970 to ban unsolicited credit cards.[34] 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.[35] 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. H.R. 3904 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.

<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. As a result, H.R. 3904 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.

<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

[33] 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 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).
[34] Pub. L. No. 91-508, 84 Stat. 1126-27 (Oct. 26, 1970).
[35] S. Rep. No. 91-739, at 2-44 (1970).

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 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."[36] 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%[37] 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.

A proposed rule currently being considered by the Federal Reserve amends Reg E and is substantially weaker than the provisions of H.R. 3904, even if the Board selects the policy of having consumers opt-in for some types of overdraft. Not only does the Board's proposal address only debit card purchases and ATM transactions instead of all transactions, but it also does not recognize that overdrafts are extensions of credit that should require Truth in Lending disclosures, nor does it prohibit manipulating the clearing of transactions to maximize overdraft fees. The Federal Reserve's Reg E proposal also does nothing to curb excessive fees. Industry calls for Congress to defer to a weak Federal Reserve rule-making should be ignored.

Overdraft Lending Costs 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.[38] High fees,

[36] 15 U.S.C. § 1601(a)
[37] Keith Ernst, et al., *Quantifying the Economic Cost of Predatory Payday Lending*, Center for Responsible Lending (December 18, 2003), at 3.
[38] 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*

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.[39] 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.[40] 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

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Balance]. CRL analyzed 18 months of bank account transactions from participants in Lightspeed Research's Ultimate Consumer Panel, from January 2005 to June 2006. For further discussion of CRL's database and methodology, *see Out of Balance* at 13-14.

[39] *Out of Balance* at 10.

[40] FDIC Study at v.

$72, and at U.S. Bank $69.50. In recently announced changes to overdraft programs, six of the 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. 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.)

H.R. 3904 Protects Bank Account Customers

H.R. 3904, the Overdraft Protection Act of 2009, 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.

H.R. 3904 requires financial institutions to obtain account holders' specific written consent in order for financial institutions to enroll them in fee-based overdraft programs. This control over bank account credit features is what consumers expect and want to have.

H. R. 3904 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.

H.R. 3904 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.

H.R. 3904 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.

H.R. 3904 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 H. R. 3904 is comparable to the Credit CARD Act's requirement that the Board set the over-the-limit fee.

H.R. 3904 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[41] as well as the over-the-limit policy in the Credit 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. The 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.

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. H.R. 3904 would benefit consumers by requiring financial institutions to get consumers' affirmative and informed consent to select fee-based overdraft programs; 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

[41] 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/fil1405a.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.

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 H.R. 3904.

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.[42] 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.[43]

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."[44]

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.

[42] 12 C.F.R. 7.4002(b).

[43] Office of Thrift Supervision, Guidance on Overdraft Protection Programs, February 14, 2005, p. 15.

[44] 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%

Testimony of Eric Halperin, Center for Responsible Lending
U.S. House of Representatives Committee on Financial Services
"The Overdraft Protection Act of 2009"

October 30, 2009

Good morning Chairman Frank, Ranking Member Bachus, Congresswoman Maloney, and other members of the Committee. Thank you for inviting me to testify on H.R. 3904, the Overdraft Protection Act of 2009. The Center for Responsible Lending enthusiastically supports this bill as a crucial measure for protecting consumers from abusive bank overdraft fees.

I am the director of the DC office of the Center for Responsible Lending (CRL), a not-for-profit, non-partisan research and policy organization dedicated to protecting homeownership and family wealth by working to eliminate abusive financial practices. CRL is an affiliate of Self-Help, which consists of a credit union and a non-profit loan fund. For the past 28 years, Self-Help has focused on creating ownership opportunities for low-wealth families, primarily through financing home loans to low-income and minority families who otherwise might not have been able to purchase homes. Self-Help has provided over $5.6 billion in financing to more than 62,000 low-wealth families, small businesses and nonprofit organizations in North Carolina and across the United States.

Self-Help has operated a North Carolina-chartered credit union since the early 1980s. In 2004, Self-Help Credit Union (SHCU) merged with three community credit unions offering a full range of retail products,[1] and it now services over 3,500 checking accounts and approximately 20,000 other deposit accounts.[2] In 2008, Self-Help founded Self-Help Federal Credit Union (SHCU) to expand Self-Help's scope of work. SHCU does not offer a fee-based overdraft program, and it routinely denies debit and ATM transactions when the customer does not have sufficient funds. If a debit card overdraft is inadvertently paid, SHCU does not charge the customer a fee for covering the payment. SHCU customers can apply for an overdraft line of credit of up to $500, carrying an interest rate of 16 percent, with no transfer fees.

In my testimony, I will describe the explosion of overdraft fees in recent years and the lack of meaningful action by bank regulators to curb these abuses. I will also summarize the reforms needed to stop unfair overdraft practices and explain how H.R. 3904 would implement these reforms.

I. Overdraft Fees Have Exploded in Recent Years

Overdraft fees are the fees charged when an institution chooses to pay a customer's debit card, check, ATM or other electronic transaction, even though the customer's account lacks sufficient funds to cover the charges. In 2008, overdraft fees cost consumers $23.7 billion and we project that in 2009, fees will reach $26.6 billion.[3] In 2004, these fees cost $10.3 billion – which means these fees are now a whopping two-and-a-half times the size they were just half a decade ago.[4] Overdraft fees paid now exceed the amount of credit extended in overdraft loans themselves.[5]

By far, the most common triggers of overdraft fees are small debit card transactions, transactions that could easily be denied at the point of sale at no cost to the consumer.

Total overdraft fees have increased due to both an increase in cost and an increase in frequency:

- ***Cost.*** From 1997 to 2007, the average overdraft fee charged by financial institutions increased from $16.50 to $29.[6] CRL estimates that the average fee *paid* by consumers is $34,[7] which is unsurprising since the sixteen largest banks charge an average fee of $35.[8] The FDIC's 2008 survey, which included many smaller financial institutions, found an average among its institutions of $27 per overdraft.[9]

- ***Frequency.*** As recently as 2004, 80 percent of institutions denied debit card transactions that would have overdrawn the account.[10] Today, approximately 80 percent of institutions routinely approve these transactions and charge a fee for each overdraft.[11] This shift has increased the frequency of overdrafts significantly, particularly given the overall increase in debit card use.[12]

Overdraft fees affect a very large number of consumers each year. CRL recently estimated that over 50 million Americans overdraw their accounts annually, with 27 million paying five or more overdraft or NSF fees.[13] Most of these fees are paid by a relatively small number of consumers – the FDIC found that 93 percent of all overdraft fees are paid by only 14 percent of account holders. These consumers are more likely to be lower-income, non-white or young account holders least able to afford such fees.[14] In the midst of a recession, abusive overdraft practices are making the dire financial situations faced by many families even worse.

II. Regulators Have Failed to Stop the Abuses

In January 2009, the Federal Reserve Board (FRB) promulgated a set of proposed rules related to debit card and ATM overdraft fees. However, the FRB proposal does not adequately address the fundamental problems with today's fee-based overdraft programs. The strongest possible version of the FRB's proposal would establish an opt-in requirement for fee-based overdraft on debit card and ATM transactions applicable to both new and existing accounts.

While we have strongly encouraged the FRB to choose this outcome because express consent is an essential baseline protection for any credit product, this measure alone is inadequate. The FRB's proposal does not address checks and electronic payments at all; it condones the approval of debit card overdrafts that could easily be denied for no fee; it does nothing to address the dramatic disparity between the amount of the overdraft and the amount of the fee institutions charge for covering it; and it does nothing to address the excessive number of overdraft fees borne by a relatively small portion of consumers.

In short, neither the FRB nor any other banking regulator has meaningfully addressed the harm to consumers caused by abusive overdraft programs. Since regulators first recognized high-cost overdraft programs as a problem in the early 2000s, practices have only grown worse, and consumers have paid more than $100 billion in overdraft fees. *See* Appendix A for further discussion of how the regulatory agencies have failed to stem these abusive practices.

III. H.R. 3906 Will Provide Much-Needed Reform of Overdraft Practices

Given the federal regulators' lack of significant action to address abusive overdraft practices, we are very encouraged to see the House of Representatives considering the meaningful protections proposed by H.R. 3904. The bill contains the following provisions that we consider essential to addressing the fundamental problems with today's overdraft programs:

- A requirement that overdraft fees be reasonable and proportional to the actual cost to the institution of covering the overdraft.
- A limit of six overdraft fees per year. Once a customer has incurred six fees in a 12-month period, the institution would be required to provide a longer-term, lower cost alternative, such as a line of credit, in order to continue covering the customer's overdrafts for a charge.
- A prohibition on overdraft fees unless institutions have obtained the customer's affirmative consent, or "opt-in."

These provisions correspond well with the best practices provided in the 2005 Joint Guidance addressing overdraft programs. The Guidance suggested that institutions consider making overdraft coverage unavailable for transactions other than checks; monitor excessive overdraft program usage, which may indicate a need for an alternative credit arrangement or other services; and obtain customers' affirmative consent to receiving overdraft coverage.[15]

IV. The Problems with Today's Fee-Based Overdraft Programs

Today's fee-based overdraft programs cause substantial injury to account holders. The cost of overdraft fees far exceeds any benefit they may provide. Moreover, the large majority of fees are paid by a relatively small number of account holders who incur numerous fees and are least able to quickly recover from them. For these account holders, one overdraft fee causes even more overdraft fees, driving them further into debt and ultimately making them less likely to be able to meet essential expenses. As our real-life case study detailed below demonstrates, fee-based overdraft leaves these account holders worse off than cheaper overdraft alternatives or even than no overdraft coverage at all.

A. The cost of overdraft fees far exceeds any benefit provided.

In the aggregate, fee-based overdraft programs cost consumers nearly $24 billion each year, which is even more than the $21.3 billion in loans extended in exchange for those fees.[16] The most common triggers of overdraft fees, debit card transactions, cause an average overdraft of under $17 yet trigger an average fee of $34.[17] This fee—twice the size of the loan itself—does not even provide the account holder the benefit of avoiding a denied transaction fee because the cost of a denied debit card transaction is zero.[18]

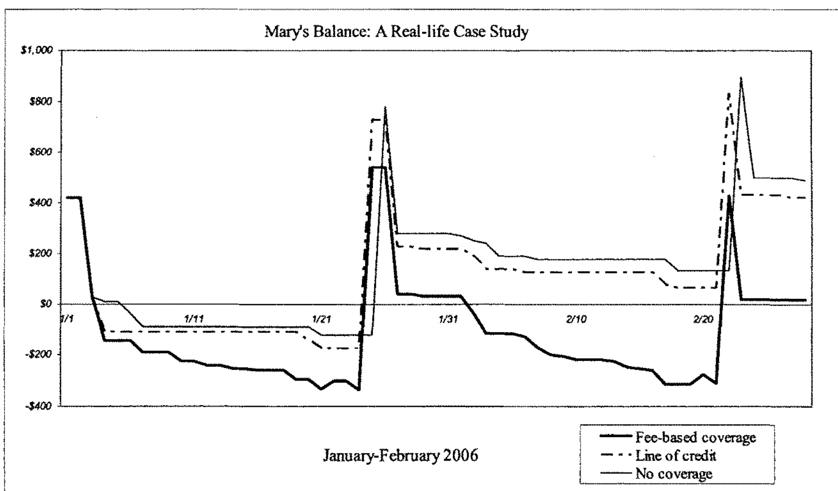
In other contexts, federal regulators have taken steps to address high fees imposed for low levels of credit. In the credit card context, for example, the FRB determined that the excessive fees associated with "fee harvester" credit cards "diminish the value of the account"; as a result, the FRB limited upfront fees on these cards to 50% of the total credit provided and required any fees exceeding 25% of the credit line to be charged over a six-month period.[19]

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

The large majority of fees are paid by overdrafters who pay large numbers of fees and are least able to recover from them. The FDIC's recent study of overdraft programs, consistent with CRL's previous research, found that account holders who overdrew their accounts five or more times per year paid 93 percent of all overdraft fees.[20] It also found that consumers living in lower-income areas bear the brunt of these fees.[21] Seniors, young adults, military families, and the unemployed are also hit hard.[22] Americans aged 55 and over pay $6.2 billion in total overdraft fees annually—$2.5 billion for debit card/ATM transactions alone[23]—and those heavily dependent on Social Security pay $1.4 billion annually.[24]

C. Overdraft fees leave account holders worse off than lower cost coverage or even no coverage at all.

Not only do fee-based overdraft leaves account holders worse off than cheaper overdraft alternatives, but they even leave account holders worse than *no overdraft coverage at all.* In a recent report on the impact of overdraft fees on older Americans, we followed two months of actual checking account activity of one panelist, whom we call Mary, from our database.[25] Mary is entirely dependent on Social Security for her income. We compared the actual activity with what her account activity would have been with an overdraft line of credit. We then added a third scenario: no fee-based coverage at all. The results are graphically demonstrated below.



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

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

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

Mary's situation illustrates a problem common among the chronic overdrafters who pay the vast majority of the fees: Overdraft fees simply beget more overdraft fees. *Ultimately, fee-based overdraft coverage prevents account holders from being able to meet obligations they otherwise would have been able to meet.*

D. Overdraft fees are not reasonably avoidable by many consumers.

1. Account holders often lack sufficient information about their accounts.

The FRB has acknowledged the difficulty of knowing one's own checking account balance, noting that "consumers often lack information about key aspects of their account" and "cannot know with any degree of certainty when funds from a deposit or a credit from a returned purchase will be made available."[26] Debit holds (occurring when institutions make a portion of a customer's account balance unavailable pending settlement of the final amount of a purchase) and deposit holds (occurring when institutions delay a customer's access to deposited funds) and the lack of transparency about the order in which transactions are cleared contribute to account holders' confusion about their balances. Making matters worse, account balance disclosures sometimes include funds available for overdraft, without including warning that accessing those funds could trigger fees, potentially leading customers to unwittingly spend more money than they have.[27]

2. Economic hardship prevents those who pay the large majority of fees from reasonably avoiding them.

The FRB has acknowledged in multiple contexts that broader economic hardship could prevent consumers from reasonably avoiding injury. In the context of raising interest rates on existing credit card balances, for example, the FRB cited several sources indicating that loss of income, illness, or other factors outside the consumer's control lead to delinquency.[28]

Likewise, in its discussion of ability to repay in the final HOEPA rule, the FRB identified several reasons why borrowers, especially in the subprime market, cannot necessarily avoid unsustainable loans, including that "they may . . . urgently need the cash that the loan will provide for a household emergency."

In the overdraft context, there is no question that economic hardship contributes to many account holders' inability to avoid fees.[29]

3. Widespread practices are aimed at maximizing overdraft revenue.

The increase in overdraft fees—both the cost and the frequency—over the past several years is the result of a concerted effort on the part of many financial institutions to maximize overdraft revenue. These institutions:

- have purchased specialized software that helps them maximize fee revenue and paid consultants to help them do so;
- have expanded their overdraft programs to debit card purchases and ATM transactions;
- often post debits as quickly as possible, while delaying for as long as possible making those deposits available for use;[30] and
- manipulate the order in which they clear transactions.[31] (Institutions often clear purchases in order from highest to lowest, rather than the order in which they occurred, in order to deplete the account to below zero more quickly. Once the account balance is negative, the institution is able to charge an overdraft fee on each subsequently posted transaction, often resulting in significantly more overdraft fees.)

V. H.R. 3904 Addresses the Fundamental Problems with Today's Overdraft Programs

H.R. 3904 addresses three key unfair features of fee-based overdraft programs: (1) charging fees that are not reasonable or proportional to the cost to the institution of covering the overdraft; (2) charging excessive numbers of fees that create a debt trap for those paying the majority of overdraft fees; and (3) charging overdraft fees without obtaining a customer's affirmative consent to having overdrafts covered.

A. Addressing High Cost: Reasonable and Proportional Requirement.

H.R. 3904 would require that overdraft fees be reasonable and proportional to the actual cost to the institution of covering the overdraft, with the FRB providing additional guidelines for what constitutes "reasonable and proportional," potentially including a safe harbor.

As noted earlier, the average overdraft fee exceeds the amount of the overdraft covered. This disparity is particularly outrageous given the short period of time for which the typical overdraft is outstanding—three to five days[32]—and the low default risk overdrafts carry. Indeed, the only circumstances under which an overdraft loan is not repaid is when another deposit is never made into the account or when the customer walks away from the account. Operational cost is also low because most programs are highly automated.

The recently passed CARD Act requires the FRB to promulgate standards for reasonable penalty fees and specifies that penalty fees be proportional not only to cost but also to the violation or omission. We support H.R. 3904's slightly different approach, which does not authorize consideration of the "violation or omission" because it is overwhelmingly clear that overdraft fees as currently administered do not deter overdrafting.[33] In fact, institutions' overdraft practices have evolved from approving the occasional overdraft as a customer courtesy to routinely approving transactions, even those they could easily deny at the point of sale for no fee. These practices encourage rather than discourage overdrafts.

In addition, the primary effect of the increase in the average overdraft fee charged over the last decade has not been deterrence; rather, it has been to increase the number of overdraft occurrences by chronic overdrafters, due in large part to the debt trap created by high fees.

The obvious way to deter overdrafts is to deny transactions that would overdraw the account— not to approve them for an exorbitant fee that only drives consumers deeper into debt and makes them more likely to overdraw their account again.

We note that while H.R. 3904 would exclude overdraft fees from the interest rate cap applicable to federal credit unions, we do not support such exclusion and believe all credit extended by federal credit unions should be subject to the interest rate cap.

B. Addressing Frequency: Annual Limit on the Number of Fees.

H.R. 3904 would limit the number of overdraft fees an institution may charge a customer to six per year. After six fees have been incurred, the institution may continue covering overdrafts for a charge only if it offers the customer a lower-cost alternative. The banking agencies have long advised institutions to discourage excessive use of overdraft programs, but this guidance has not, by and large, been followed.[34]

Banking regulators have also long discouraged practices analogous to excessive overdraft loans.[35] The repeat borrowing illustrated in our case study above is analogous both to loan flipping of other high-cost short-term loans, such as payday loans, loan flipping in the mortgage context, and pyramiding late fees:

- ***Other high-cost, short-term loan flipping.*** Excessive overdraft loans create a debt trap similar to that caused by other high-cost, short-term lending. CRL's recent research finds that over three-fourths of payday loan volume is generated within two weeks of a customer's previous payday loan.[36] While technically a borrower typically closes an old payday loan and opens a new one, effectively the borrower is being flipped from one loan into another—unable to repay one loan and meet essential expenses without taking out another loan.[37] Payday loans beget payday loans, much like overdraft loans beget overdraft loans.

- ***Mortgage loan flipping, which has already been identified as abusive.*** The repeated extension of overdraft loans is also analogous to flipping borrowers from one mortgage loan to the next. In the mortgage context, an originator sells the borrower an unaffordable loan only to later refinance the borrower into another unsustainable loan, extracting fees and stripping home equity from the borrower in the process. Earlier this session, the House of Representatives passed H.R. 1728, which would ban this practice for mortgage loans. In the overdraft context, cash is similarly stripped from customers who are flipped.

- ***Pyramiding late fees, which the FRB has prohibited as an unfair practice.*** Pyramiding late fees occur when lenders apply future payments to the late fee first, making it appear future payments are delinquent even though they are, in fact, paid in full within the required time period. As a result, lenders charge additional late fees.[38] These fees provide no benefit to the consumer while driving them further into debt.[39] For customers who incur the majority of overdraft fees, they often would have had sufficient funds in their account to meet future expenses *but for* the excessive overdraft fees they have incurred in previous periods.

How regulators have addressed these analogous abuses informs what is appropriate in the overdraft context. In 2005, the FDIC limited excessive refinancings of payday loans by prohibiting the entities it regulates from making payday loans to anyone who has had payday loans outstanding for three months in any 12-month period.[40] The FDIC guidance encourages lenders to offer borrowers an alternative longer term product at that point but notes that even if such alternative is not available, "an extension of a payday loan is not appropriate under such circumstances."[41] Assuming a 14-day pay period, this standard limits the number of loans any borrower can have to six per year, alleviating the debt trap while continuing to allow loans to the occasional users. The FDIC further urges institutions to require "cooling off" or waiting periods between payday loans.[42] The limit on fees in H.R. 3904 is closely analogous to the FDIC's approach to limiting payday loans. It would address the debt trap caused by overdraft loans in much the same way.

Similarly, the FRB has long prohibited pyramiding late fees as an unfair practice through its Credit Practices Rule,[43] and it recently reinforced its stance by prohibiting the same under TILA through its recent HOEPA final rule.[44]

C. Permitting Customers to Opt In is Crucial.

Consumers should be provided a meaningful choice about whether to participate in fee-based overdraft programs. Automatically enrolling a customer in the program, even if an institution allows the customer to opt out later (often after the damage has been done), does not provide a meaningful choice.

An opt-in arrangement provides the customer a moment during which he or she may evaluate the options available and affirmatively choose the one most suitable. In its proposed rulemaking, the FRB recognized the productive incentives an opt-in arrangement would offer: "[Opt-in would] provide an incentive for institutions to persuade consumers of the benefits of the overdraft service and enable the consumer to make an informed choice about the merits of the service before he or she incurs any overdraft fees."[45]

While an opt-in requirement must be coupled with other substantive protections, greater transparency will foster competition in the marketplace, resulting in better choices for consumers. Allowing no choice at all, or allowing automatic enrollment with only an opportunity to opt out, are anti-consumer, non-transparent practices that have facilitated the race to the bottom in this area over the past several years. For a complete discussion of this issue, see our 2008 and 2009 regulatory comment letters.[46]

VI. Conclusion

We support H.R. 3904 for comprehensively addressing the most abusive features of today's overdraft programs. The bill would limit the high costs of these fees, would cut down on the frequency which fees are charged to those least able to shoulder them, and would require the customer's express consent.

Thank you again for the opportunity to testify today. I look forward to your questions.

APPENDIX A: Regulators Fail to Curb Abuses

Regulators first identified overdraft practices as a problem as early as 2001, when the OCC noted the "complete lack of consumer protections" associated with these programs. Since then, overdraft practices have grown exponentially worse. While regulators have taken no meaningful steps to rein in abuses, *Americans have paid well over $100 billion in overdraft fees.*[47]

2001—OCC Interpretive Letter discusses numerous concerns about automated overdraft programs, noting "the complete lack of consumer safeguards built into the program," including a lack of limits on the number of fees charged per month; similarities between overdraft fees and other "high interest rate credit;" and the failure of banks to meet the needs of repeat overdrafters in a more economical way.[48]

2002—The FRB issues a preliminary request for comment on overdraft programs.[49]

2005—Three years later, the FRB affirmatively exempts overdraft loans from the protections of the Truth in Lending Act when it chooses to address overdraft programs under the Truth in Savings Act instead.[50] Overdrafts continue to be made without consumers' explicit consent and with no cost-of-credit disclosures to allow comparisons of overdraft fees to less costly options.

2005—Regulators issue joint guidance, which reflects several of the OCC's 2001 concerns. But rather than explicitly prohibiting any of these practices as unfair and deceptive, the guidance only provides "Best Practices." When asked whether this guidance would be treated as law, regulators responded: "The best practices, or principles within them, are enforceable to the extent they are required by law."[51] But the regulators required none of them by law, and the guidance has largely been ignored in the years since.

2007—Despite its joint guidance acknowledging that overdrafts are an extension of credit, the OCC asserts in *Miller v. Bank of America* that its regulations allow banks to seize exempt benefits such as Social Security to pay overdraft loans and fees, claiming that they are not "collect[ing] a debt."

2008—Regulators issue a proposal under their authority to address unfair and deceptive practices (UDAP). The proposal covers all transaction types (checks, electronic payments, debit card and ATM) but proposes only that consumers have the right to "opt out" of high-cost overdraft programs—not that institutions must obtain consumers' explicit consent before enrolling them. Regulators later withdraw the proposal.

2009—The FRB issues a new proposal addressing only debit card and ATM transactions. It considers two alternative approaches—opt-out and opt-in. It considers no additional substantive protections, such as a limit on excessive fees or a requirement that fees be reasonable and proportional to the cost to the institution of covering the overdraft.

Ongoing—Best Practices Guidance continue to be largely ignored by institutions and the regulators alike. The OCC's Compliance Handbooks make no reference to overdraft programs at all,[52] much less to Best Practices.

[1] SHCU merged with Wilson Community Credit Union and Scotland Community Credit Union in 2004 and with Cape Fear Community Credit Union in 2006.

[2] These include traditional savings accounts, money market accounts, certificates of deposits, and individual retirement accounts.

[3] Leslie Parrish, *Overdraft Explosion: Bank fees for overdrafts increase 35% in two years,* Center for Responsible Lending (Oct. 6, 2009), *available at* http://www.responsiblelending.org/overdraft-loans/research-analysis/crl-overdraft-explosion.pdf [hereinafter *Overdraft Explosion*].

[4] In 2004, CRL first estimated the annual cost consumers paid in overdraft fees at $10.3 billion. Jacqueline Duby, Eric Halperin, Lisa James, *High Cost and Hidden from View: The $10 Billion Overdraft Loan Market*, Center for Responsible Lending (May 26, 2005).

[5] *Overdraft Explosion* at 7 (estimating $23.7 billion in fees charged in exchange for $21.3 billion in credit extended).

[6] Comments of the Center for Responsible Lending to the Board of Governors of the Federal Reserve System, Office of Thrift Supervision, and National Credit Union Administration on Proposed Rule Regarding Unfair and Deceptive Practices—Overdraft Practices (Aug. 4, 2008), notes 62-63, and accompanying text, *available at* http://www.responsiblelending.org/overdraft-loans/policy-legislation/regulators/overdraft-comments-udap-final-as-submitted-w-appendices-080408-2-1.pdf [hereinafter CRL 2008 UDAP Comments].

[7] 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 25 (Jan. 25, 2007), *available at* http://www.responsiblelending.org/overdraft-loans/research-analysis/Debit-Card-Danger-report.pdf [hereinafter *Debit Card Danger*].

[8] Consumer Federation of America, *CFA Survey: Sixteen Largest Banks Overdraft Fees and Terms* (updated July 31, 2009), *available at* http://www.consumerfed.org/pdfs/overdraft_fee_report_09.pdf [hereinafter 2009 CFA Survey].

[9] FDIC Study of Bank Overdraft Programs, p. iii of the Executive Summary, *available at* http://www.fdic.gov/bank/analytical/overdraft/FDIC138_ExecutiveSummary_v508.pdf (2008) [hereinafter FDIC 2008 Overdraft Study].

[10] Mark Fusaro, *Are "Bounced Check Loans" Really Loans?*, note 4, at 6 (noting 20% of institutions in June 2004 were applying "bounce protection" to debit cards or ATM) (Feb. 2007), *available at* http://personal.ecu.edu/fusarom/fusarobpintentional.pdf.

[11] FDIC 2008 Overdraft Study at iv (Nov. 2008). Moreover, while as recently as 2004, overdraft loans accounted for 60 percent of institutions' total overdraft/insufficient funds revenue, today they account for approximately 70% percent of that revenue—indicating covering overdrafts, rather than denying them, is increasingly the norm. 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 (June 2007), *available at* http://www.responsiblelending.org/overdraft-loans/research-analysis/out-of-balance-report-7-10-final.pdf [hereinafter *Out of Balance*].

[12] In 2007, the Federal Reserve reported that debit card transactions were increasing at a rate of 17.5 percent per year. 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.

[13] *Overdraft Explosion* at 3.

[14] FDIC 2008 Overdraft Study, Executive Summary at IV.

[15] Department of the Treasury-Office of the Comptroller of the Currency, Federal Reserve System, Federal Deposit Insurance Corporation, National Credit Union Administration, Joint Guidance on Overdraft Protection Programs, 70 Fed. Reg. 9127 (Feb. 24, 2005) [hereinafter 2005 Joint Guidance].

[16] *Overdraft Explosion* at 7.

[17] The average overdraft amount for debit card transactions is $16.46. *Debit Card Danger* at 25.

[18] In its Regulation E Proposal, the FRB states: "the consequence of not having overdraft services for ATM and one-time debit card transactions is to have a transaction denied with no fees assessed." 74 Fed. Reg. 5218. Currently, charging NSF fees for denied debit or ATM transactions is not a common practice. *See* Center for Responsible Lending's CRL 2008 UDAP Comments at 18-19 for discussion of why this practice should be prohibited by the FRB.

[19] 74 Fed. Reg. 5542.

[20] FDIC 2008 Overdraft Study at iv.

[21] *Id.* at v. Two CRL surveys, conducted in 2006 and 2008, found that 71 percent of overdraft fees were shouldered by only 16 percent of respondents who overdrafted, and those account holders were more likely than the general population to be lower income, non-white, single, and renters. Respondents reporting the most overdraft incidents were those earning below $50,000/year. Leslie Parrish, *Consumers Want Informed Choice on Overdraft Fees and Banking Options*, CRL Research Brief (Apr. 16, 2008) (http://www.responsiblelending.org/overdraft-loans/research-analysis/consumers-want-informed-choice-on-overdraft-fees-and-banking-options.html. *See* CRL 2008 UDAP Comments at 19-21 for further discussion.

[22] For further discussion, *see* Comments of the Center for Responsible Lending to Board of Governors of the Federal Reserve System on Proposed Rule to Amend Regulation E—Overdraft Practices (Mar. 30, 2009), Part II.B.1(b), pp.10-12, *available at* http://www.responsiblelending.org/overdraft-loans/policy-legislation/regulators/comments-on-regulation-e-overdraft-practices.html [hereinafter CRL 2009 Regulation E Comments].

[23] Leslie Parrish and Peter Smith, *Shredded Security: Overdraft practices drain fees from older Americans*, Center for Responsible Lending (June 18, 2008), *available at* http://www.responsiblelending.org/overdraft-loans/research-analysis/shredded-security.html. The report found that debit card POS and ATM transactions account for 37.4 percent and 2.5 percent, respectively (p.7), which, when calculated, together equal $2.5 billion.

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

[25] CRL analyzed 18 months of bank account transactions, from January 2005 to June 2006, from participants in Lightspeed Research's Ultimate Consumer Panel. For further discussion of our database and methodology, *see Out of Balance* at 13-14.

[26] 73 Fed. Reg. 28929.

[27] *See* 2008 Proposed Rule to amend Regulation DD, 73 Fed. Reg. 28743-44. While the FRB's final Regulation DD rule will require that the first balance displayed exclude overdraft funds available, it will allow a second balance to be displayed that includes overdraft funds available, even with no disclosure that accessing such funds will or may incur a fee. 74 Fed. Reg. 5593.

[28] 74 Fed. Reg. 5523. The FRB cites the FTC Credit Practices Rule, which found "the majority [of defaults] are not reasonably avoidable by consumers" because of factors such as loss of income or illness; Bank of America testimony noting that falling behind on an account is likely due to circumstances outside the customer's control; and an economic journal finding conclusive evidence that unemployment is critical in determining delinquency.

[29] Some may posit that the injury caused by overdraft fees must be avoidable because only a relatively small portion of consumers frequently overdraw their accounts. But the FRB has already concluded that, although injury may be avoidable by some consumers under some circumstances, it may not be reasonably avoidable as a general matter. In its analysis of payment allocation methods in the credit card context, the FRB noted that "[a]lthough a consumer could avoid the injury by paying the balance in full every month, this may not be a reasonable expectation as many consumers are unable to do so." It applied a similar analysis to increasing interest rates on existing balances. The FRB acknowledged that the injury resulting from increases in the annual percentage rate "may be avoidable by some consumers under certain circumstances," but it nonetheless concluded that, "as a general matter," consumers cannot reasonably avoid interest rate increases on existing balances." 74 Fed. Reg. 5522. In both circumstances, the FRB concluded that the injury caused by these practices was not reasonably avoidable.

[30] *See* CRL 2008 UDAP Comments at 37, Part III.B.

[31] *See* CRL 2008 UDAP Comments at 38, Part IV. Recently, an advisor on overdraft and card strategies at Profit Technologies acknowledged that fees are a key driver of institutions' transaction clearing practices: "'Banks will say (high-to-low clearing) is for the consumer,' he says. 'Bottom line is, when it was pitched, we'd say ... a side effect is that it results in more fee income to you because it bounces more checks.' [The advisor] says that after leaving Profit Technologies, he joined a credit-counseling firm and saw the damage fees did to consumers." Kathy Chu, *Banks' 'courtesy' loans at soaring rates irk consumers*, USA Today, July 13, 2009.

[32] *Debit Card Danger* at 25.

[33] There are two primary penalty fees charged in the credit card context today—late fees and over-the-limit fees. A reasonable late fee is not as likely as an overdraft fee to simply perpetuate the scenario it purports to deter. In the credit card context, avoiding an additional late fee requires that the customer pay only a minimum payment on time—not the entire outstanding balance, including fees. In the overdraft context, the entire loan, plus all fees, are repaid upon the customer's next deposit, typically three to five days later. Therefore, customers have more time to recover from a late fee than they do from an overdraft fee, and late fees are not as likely to beget late fees as overdraft fees are to beget overdraft fees.

Overdraft fees in the debit card context are very similar to over-the-limit fees in the credit card context in that they result from transactions the institution approves that it could easily deny for no fee. The clear way to deter the behavior in both contexts is to deny the transaction.

[34] 2005 Joint Guidance; OTS Guidance, 70 Fed. Reg. 8428 (2005).

[35] *See, e.g.*, OCC Advisory Letter on Abusive Lending Practices, AL 2000-7, July 25, 2000; FDIC Financial Institution Letters, Guidelines for Payday Lending, FIL 14-2005, February 2005; FDIC Financial Institution Letters, Affordable Small-Dollar Loan Products, Final Guidelines, FIL-50-2007, June 19, 2007.

[36] Leslie Parrish and Uriah King, *Phantom Demand: Short-term due date generates need for repeat payday loans, accounting for 76% of total volume*, Center for Responsible Lending (July 9, 2009), *available at* http://www.responsiblelending.org/payday-lending/research-analysis/phantom-demand-final.pdf.

[37] The typical payday borrower pays an additional $45 in interest every two weeks, with effectively no reduction in principal—i.e., no benefit—and ultimately pays $450 in interest on a $300 loan.

[38] 12 CFR 227.15 (Regulation AA).

[39] 16 CFR 444.

[40] FDIC Financial Institution Letters, Guidelines for Payday Lending, FIL 14-2005, February 2005.

[41] *Id.*

[42] *Id.* The OCC, in its payday guidance, has noted that its guidance addressing abusive lending practices more generally should also be applied in the context of payday lending. That guidance identifies the following indicators of abusive lending: pricing and terms that far exceed the cost of making the loan; loan terms designed to make it difficult for borrowers to reduce indebtedness; and frequent and multiple refinancings. OCC Advisory Letter on Abusive Lending Practices, AL 2000-7, July 25, 2000.

[43] 12 CFR 227.15(a).

[44] The FRB noted that pyramiding late fees "give rise to charging excessive or unwarranted fees to consumers, who may not even be aware of the default or fees . . . . Once consumers are in default, these practices can make it difficult for consumers to catch up." 73 Fed. Reg. 44569.

[45] 74 Fed. Reg. 5225.

[46] CRL 2008 UDAP Comments at 25-27; CRL 2009 Regulation E Comments at 8-18.

[47] Determined as follows:

2009	$20.0B	(per CRL's projection for 2009, *Overdraft Explosion*, through September)
2008	$23.7	(per CRL 2009 report, *Overdraft Explosion*)
2007	$20.6	(assumes midpoint between 2006 and 2008 figure)
2006	$17.5	(per CRL 2007 report, *Out of Balance*)
2005	$14.0	(assumes midpoint between 2004 and 2006 figure)
2004	$10.3	(per CRL 2005 report, *High Cost and Hidden From View*)
Total	**$106.3 B**	(Conservative estimate as it does not include any fees paid in 2001, 2002, or 2003.)

[48] OCC Interpretive Letter # 914 (August 3, 2001), *available at* http://www.occ.treas.gov/interp/sep01/int914.pdf. The OCC raised compliance issues with respect to TILA, TISA, EFTA, ECOA, and Regulation O (extensions of credit to bank insiders).

[49] 67 Fed. Reg. 72620 (2002).

[50] 70 Fed. Reg. 29582 (May 2005).

[51] *Id.*

[52] There is little evidence to suggest that the OCC has instructed its examiners to even evaluate overdraft practices—much less attempted to encourage best practices. A search of the OCC's Compliance Handbook for depository services finds no reference to the guidance and a search of the OCC's "Other Consumer Protections" Compliance Handbook finds no reference to overdraft protection, or, indeed, to the FTC Act's UDAP provisions at all. Moreover, the OCC's message to its banks' customers has essentially been that the banks can do as they please. For example, the OCC's online consumer reference "HelpWithMyBank" has a FAQ on its overdraft section concerning transaction posting order (generally manipulated by banks to maximize overdraft fees) that validates the banks' own claim that they can post transactions in whatever order they please. http://www.helpwithmybank.gov/faqs/banking_overdraft.html#drop08. Additionally, Consumer Federation of America's 2009 survey of overdraft fees at the 16 largest banks finds that their average fee is $35, compared to $27 at FDIC-regulated institutions. 2009 CFA Survey. Eleven of the 16 largest banks are OCC-supervised.

CBA | CONSUMER BANKERS ASSOCIATION

Testimony of

Richard Hunt

On Behalf of the

Consumer Bankers Association

Before the

Committee on Financial Services

United States House of Representatives

October 30, 2009

Testimony of

Richard Hunt

President, Consumer Bankers Association

On H.R. 3904, the Overdraft Protection Act of 2009

Before the Committee on Financial Services
U.S. House of Representatives

October 30, 2009

Good morning Mr. Chairman and Members of the Committee, my name is Richard Hunt and I am the President of the Consumer Bankers Association ("CBA"). For 90 years, CBA has been the recognized voice on retail banking issues in the nation's capital. Member institutions are the leaders in consumer financial services, including auto finance, home equity lending, card products, education loans, small business services, community development, investments, deposits and delivery. CBA provides leadership, education, research and federal representation on retail banking issues such as privacy, fair lending, and consumer protection legislation/regulation. CBA members include most of the nation's regional and super community banks as well as the largest bank holding companies that collectively hold two-thirds of the industry's total assets. I appreciate the opportunity to appear before you this morning to discuss H.R. 3904, the Overdraft Protection Act of 2009.

CBA supports the efforts of the Board of Governors of the Federal Reserve to provide appropriate consumer protections pertaining to bank overdraft practices. Although we do not necessarily agree with several of the items proposed in the Federal Reserve's overdraft regulation, we believe the Federal Reserve's efforts will likely strike the appropriate balance regarding the regulation of overdraft services without unnecessarily limiting consumers' access to these services. It is our understanding the Federal Reserve will issue its overdraft regulation in the near future, and certainly within the next two months.

It is important to note the Federal Reserve's efforts are the culmination of consumer testing, a review industry and consumer feedback, consideration of unintended consequences, and an evaluation of appropriate consumer protections. CBA has no expectation the banking industry will necessarily be pleased with the requirements in the Federal Reserve's regulation, but we do expect it will address many of the concerns addressed in H.R. 3904. It is obviously the job of Congress to make public policy, but we urge Congress, at this point in the rulemaking, to wait only a short period of time to review the fruit of the Federal Reserve's efforts before considering whether further legislation is necessary.

Before providing our thoughts on the legislation, I believe it is important to give some context for CBA's testimony. I want to provide you with insight about overdraft services that Americans are not getting from the media or from industry critics. Courtesy overdraft services are just that—a courtesy that the banks have traditionally offered as a service to their customers. Our members report and the statistics show that the vast majority of consumers manage their checking accounts in a responsible manner. But even the most conscientious consumer can overdraw an account once in a while. When this happens, the bank has one of two choices: it can bounce the check, or it can honor the check. If the bank bounces the check, the consumer will pay a fee to the bank; the consumer will likely pay a fee to the person to whom the check was written; the consumer may also face late payment fees and delinquencies if the check was written to pay a bill; and the consumer may also be at risk of violating state laws pertaining to bad checks. If the bank denies a debit card transaction, the consumer may be faced with a plate full of food or a cart full of groceries and no way to pay for them. With this in mind, it is not hard to understand why consumers generally prefer that their overdraft transactions be honored, even if they result in overdraft fees. Because this is a service, and not a loan product, the customer has no guarantee the item will be paid and cannot rely upon it for short-term credit. Rather, it is a courtesy for the benefit of the consumer. It is an important courtesy that is provided by thousands of banks to millions of customers. So, despite the frequent criticism of overdraft services, there can be no question that consumers and retail merchants would suffer unnecessary and unwanted harms if banks did not provide these courtesy services.

It is also important to note that, despite the claims of some, only a small percentage of consumers benefit from overdraft services more than just once in a while. Furthermore, at least one study indicates that, of those consumers who do benefit from overdraft services more than once in a while, only about 15% are low to moderate income. In other words, overdraft services are generally not repeatedly used by low or moderate income consumers as a short-term loan, or a "payday" loan. Rather, of the small percentage of consumers who receive overdraft coverage more than occasionally, the majority appear to be consumers of some means who simply are not managing their accounts.

Honoring an overdraft has costs for a bank, however. The cost of processing the overdraft is only one of several costs that a bank must recover when it pays an overdraft for a consumer. There are risks associated with extending the overdraft to the consumer, such as whether the overdraft will ultimately be repaid. It is the bank—not the merchant or even the customer—that bears this risk. It is not only reasonable, but *it is expected* that a bank is compensated for taking such risks. It is also important to note that overdraft fees are an important deterrent to future overdrafts on the account.

With respect to H.R. 3904, CBA is still gathering feedback from its members to develop a position on the overall bill. CBA generally supports several of the concepts addressed in H.R. 3904. For example, we believe consumers should receive information describing overdraft services at account opening, and information about overdraft fees incurred in monthly statements. CBA also believes consumers may find information about alternative products, such as overdraft lines of credit, beneficial. CBA understands why some consumers may want the option of opting out of all overdraft services, and we would support legislation ensuring that such choice is provided. We also support the provision in H.R. 3904 that prohibits banks from engaging in unfair or deceptive acts or practices pertaining to overdraft services. In effect, we support giving consumers the necessary information to understand overdraft services, understand possible alternatives, and to ensure that banks treat their customers fairly.

We are concerned, however, this legislation would significantly increase bounced checks, debit transaction denials, and the number of dissatisfied bank customers. One of our biggest concerns is with the prohibition on the number of overdrafts permitted each month and year. H.R. 3904 would limit a bank to charging only one overdraft fee a month and six overdraft fees a year. Although it may seem reasonable to expect that a consumer would not overdraft an account more than once a month, or six times a year, I can tell you that this is not always the case, even for the most responsible customers. For example, a consumer could write several checks not realizing that his or her spouse recently made an ATM withdrawal, or wrote other checks. This could result in several checks bouncing. If a bank is permitted to charge only one overdraft fee when those checks bounce, the bank simply may not honor all of those checks. Indeed, it may not even be a safe or sound banking practice to honor the checks without charging a fee. We believe the consumer would rather have those checks paid, even if it results in multiple overdraft fees, than have to clean up the aftermath of several bounced checks.

CBA is also concerned that H.R. 3904 would cause banks to limit overdraft coverage even for those consumers who want it. For example, the legislation would limit the cost of an overdraft fee to an amount that is reasonable and proportional to the cost of processing the transaction. As I describe above, there are other costs that are very real to the bank other than simply "processing" the transaction. If a bank cannot recover these costs, it may not be in a position to offer the services. It may also be an unsafe or unsound banking practice to charge only a minimal "processing" fee for allowing a consumer to overdraft an account. Furthermore, a combination of consumer inertia and the opt-in requirement will undoubtedly result in consumers not realizing the consequences of foregoing overdraft services until it is too late and transactions are denied.

We ask the Committee to consider not only the impact on consumers if their transactions are not honored as a result of H.R. 3904, but also the impact on all checking account customers. If Congress restricts the ability of banks to charge overdraft fees, not only will those services be less available to consumers who want them, but it will also force banks to recover revenue in other ways. For example, bank revenues have increasingly depended on behavior-based fee income as a result of the shift away from account maintenance fees. We believe consumers benefit greatly from the variety of free checking account options that banks offer. These options are especially beneficial to those of low or moderate incomes who may not choose to use a bank if there are additional fees. But checking accounts are not free to offer, and banks must recover some costs, including through overdraft fees. Some of that fee income includes fees from overdrafts. If H.R. 3904 is enacted, it is possible (perhaps even likely) that many banks may need to reevaluate their ability to offer free checking accounts to those consumers who manage their accounts well. We are certain the majority of consumers would prefer to keep their free checking accounts instead of returning to the days of account maintenance fees or transaction fees, even if it means that banks charge overdraft fees.

There are also broader implications beyond just banks and their customers. The legislation will have a significant impact on retailers and the marketplace. Merchants will likely see a significant increase in bounced checks (or an increase in the price they pay for services to protect themselves from bounced checks). With respect to debit card transactions, merchants will see an increase in denied transactions after the groceries have been bagged, or food has been plated or eaten. When this happens, it is not simply a question of asking the consumer to pay with something other than a debit card. Approximately 25% of households do not have a credit card, and this number may be increasing. Asking the consumer to have sufficient cash on hand, or to write a bad check at the point of sale, when a debit card is denied also do not seem like appropriate alternatives. Yes, there are anecdotes of the $39 cup of coffee resulting from an overdraft debit card transaction ($4 coffee and $35 overdraft fee). But Congress should not legislate based on anecdotes of consumers who did not keep track of their account balance, especially when the legislation will harm a far greater number of consumers than it helps.

Mr. Chairman, CBA is pleased to have the opportunity to share some of our thoughts with the Committee about H.R. 3904. We look forward to working with you and the other Members of the Committee to refine and improve this legislation to provide consumers with appropriate protections without creating significant unintended consequences. I would be happy to answer any questions you may have.

WRITTEN STATEMENT

OF

OLIVER I. IRELAND

ON H.R. 3904

THE OVERDRAFT PROTECTION ACT OF 2009

BEFORE THE

COMMITTEE ON FINANCIAL SERVICES

U.S. HOUSE OF REPRESENTATIVES

October 30, 2009

Good morning Chairman Frank and Ranking Member Bachus. My name is Oliver Ireland. I am a partner in the financial services practice in the Washington, D.C. office of Morrison & Foerster LLP. I have over 30 years of experience in financial services issues. I also worked for the Federal Reserve System for 26 years and spent 15 years as an Associate General Counsel of the Board of Governors of the Federal Reserve System ("Board") in Washington, D.C. In my capacity at the Board, I was responsible for drafting Regulation CC, which implemented the Expedited Funds Availability Act ("EFAA") and, in doing so, substantially revamped the check return system. I was also responsible for drafting and interpreting certain Board regulations affecting deposit accounts, including the regulation governing reserve requirements, which distinguishes between savings deposits and transaction accounts based on the level of transactions, the regulation implementing the prohibition against the payment of interest on demand deposits, and was responsible for legal support of the Board's own overdraft policy, which governs overdrafts by depository institutions in their accounts at Federal Reserve Banks. I have also litigated and served as an expert witness in cases involving dishonored checks and have advised private clients in connection with the treatment of deposit account overdrafts. In addition, I was an advisor to the National Conference of Commissioners on Uniform State Laws Drafting Committee for the 1990 revisions to Articles 3 and 4 of the Uniform Commercial Code.

I am pleased to be here today to discuss H.R. 3904, the "Overdraft Protection Act of 2009." H.R. 3904 would address the practice of many depository institutions, both large and small, of charging fees for paying overdrafts due to check, automated clearinghouse and debit card transactions. While these practices have enabled consumers to meet unexpected expenses and to avoid additional costs and other consequences of failing to make timely payments when the consumers did not keep adequate track of their account balances, these practices have also been criticized as costly and unfair, particularly when imposed on small debit card transactions that consumers understood to be authorized by their depository institutions.

H.R. 3904 would amend the Truth in Lending Act to:

- require that consumers must opt in in writing before they are enrolled in overdraft coverage programs on every type of transaction;
- prohibit depository institutions from charging more than one overdraft per month and more than six overdraft fees in a single year;
- require that overdraft fees relate to the "actual cost" of processing the overdraft, as defined by bank regulators;
- prohibit charges for ATM and debit card transactions that are declined;
- regulate the order in which transactions are paid;
- require notification if a transaction at an ATM would trigger an overdraft fee and offer the consumer the chance to cancel the transaction before a fee is incurred; and
- require the GAO to study the feasibility of providing an overdraft warning notice and the opportunity to cancel the transaction for point-of-sale transactions.

In addition, as you are no doubt aware, the Board has issued a series of regulatory proposals in this area over the last few years and is currently considering a proposal to address overdrafts at ATMs and in debit card point-of-sale transactions. H.R. 3904 would go well beyond the Board's proposals by addressing overdrafts due to all types of payment transactions and by limiting fees even when a consumer chooses to receive overdraft services.

Recognizing that this Committee is likely to pass some form of H.R. 3904, and that even if the Congress does not adopt this, or similar legislation, the Board will adopt significant new requirements for overdraft programs, I will not debate the merits of these programs but rather focus on some technical aspects of H.R. 3904 and the likely effect that the adoption of the H.R. 3904, or similar requirements, would be likely to have on the pricing of transaction account services to consumers.

As an initial matter, it is not clear why the Truth in Lending Act has been chosen as the vehicle for these requirements. Applying the Truth in Lending Act to overdrafts is likely to be confusing to consumers both with respect to their rights regarding the transaction and the costs of the transaction. Under H.R. 3904, the Truth in Lending Act's billing error provisions would appear to apply whenever an overdraft coverage fee is imposed on a consumer and presumably to the transaction that resulted in the overdraft. This would mean that for checks that result in an overdraft, the consumer would have Truth in Lending billing error rights and rights under the Uniform Commercial Code, but for checks that do not result in an overdraft, only the Uniform Commercial Code would apply. Similarly, for debit card transactions, the consumer would have billing error rights under the Electronic Fund Transfer Act for transactions that do not result in an overdraft, but would have Electronic Fund Transfer and Truth in Lending billing error rights as well for transactions that result in an overdraft.

In addition, it is not clear how the Truth in Lending Act disclosure requirements would treat overdrafts. The Truth in Lending Act could be interpreted to require depository institutions to calculate an effective or historical annual percentage rate on periodic statements for overdrafts. The effective annual percentage rate has been eliminated for open-end credit because extensive consumer testing by the Board has shown that it was not an effective disclosure.

Second, H.R. 3904 applies both the choice, or opt-in, provision and the limitation on the number of overdraft fees that can be assessed to check and ACH transactions, as well as ATM and debit card transactions. At a minimum, the limitations on the number of fees that may be imposed should not apply to check and ACH debit transactions. As a practical matter, there are significant differences between these types of transactions, both in the manner in which the transactions are authorized or processed and the consequences of refusing to pay those transactions. ATM and debit card transactions are often authorized by the card issuer against a current balance in a consumer's account. Although this balance may be withdrawn before the authorized transaction settles, leading to an overdraft, a merchant accepting a debit card typically is assured of payment, and does not have to attempt to collect funds from the cardholder. In contrast, check and ACH transactions generally proceed without confirmation that good funds are on deposit to cover the transaction, leading to transactions that are disrupted after the fact by a return of the check or ACH entry.

These returns, coupled with the fact that check and ACH payments are often used for transactions that are not conducted face to face, place the payees on these transactions in the position of having to both process an often manual exception transaction, and to attempt to obtain payment for goods or services already provided from the consumer. Accordingly, merchants, utilities and other providers of goods and services that accept payment by check or ACH debit transaction typically charge significant fees to their customers for returned checks and ACH transactions. These fees, when coupled with the returned transaction fees charged by the paying institutions to cover their costs and risks from returning check and ACH transactions, lead to costs to consumers for returned transactions that significantly exceed the costs of having these transactions paid under most, if not all, overdraft payment programs. Accordingly, consumers generally benefit by paying less in fees when check and ACH transactions are paid under an overdraft program rather than returned unpaid. In addition, consumers may avoid other more costly consequences from failing to make payments on time. For example, failure to make mortgage, insurance or other bill payments on time due to a returned transaction may lead to higher costs or the inability to obtain some services. Although subject to the debit card authorization process, these additional consequences also result from the denial of preauthorized debit card transactions. Debit card use for bill payment is growing rapidly and, therefore, there is a good case for treating these transactions like check and ACH transactions and excluding them from limitations on the number of fees.

Third, H.R. 3904 would prohibit overdraft fees due to "debit holds" where a hold is placed on an account at the time that an ATM or debit card transaction is authorized and that hold exceeds the amount of the transaction that actually settles. This practice has been a particular issue with respect to pay-at-the-pump gas station transactions where the amount of the transaction can exceed the amount authorized—often only \$1—by a material amount. As a practical matter, the card-issuing depository institution cannot know for sure that the amount authorized for any debit card transaction will match the amount settled until the transaction settles. Further, under the regime contemplated by H.R. 3904, in order to avoid overdrafts on ATM and debit card transactions, card issuers will have an increased incentive to place holds on ATM and debit card transactions that they have authorized in order to prevent these transactions from causing an overdraft due to intervening withdrawals or transactions.

Although there has been progress in addressing the discrepancies between amounts authorized in pay-at-the-pump transactions, most notably Visa's real-time clearing program, if card issuers are to be prohibited from charging fees for overdrafts for transactions that exceed the authorized amount, merchants accepting debit cards should have a duty to submit the actual amount of the transaction promptly to minimize these occurrences.

Fourth, H.R. 3904 would require consumers to affirmatively choose to incur overdraft fees, limit the number of overdraft fees that can be charged per month and per year, and require that overdraft fees be reasonable and proportional to the amount of the transaction. There is substantial overlap between these provisions. For example, individual overdraft fees should be viewed as reasonable if the consumer has been notified of the amount of the fee and chosen to incur the fee. In addition, the limitation on the number of overdraft fees that may be imposed may effectively prevent the payment of overdrafts that the consumer wants to have paid because an arbitrary threshold has been reached. At a minimum, the limits on the number of fees that may be imposed should not apply to ATM transactions where the consumer elects to proceed with the transaction after being informed that the transaction will, or is likely to, result in an overdraft. Further, the requirement that fees relate to the cost of processing the transaction ignores the credit risks associated with overdraft transactions.

Fifth, H.R. 3904 would require depository institutions to post transactions in a manner that the consumer does not incur avoidable overdrafts. Under current posting procedures where some transactions are batch posted and others may be "flow" posted more or less as they occur, it is not at all clear what this standard requires. In addition, although posting contemporaneous batch processed transactions in specified order, such as high to low, may result in higher overdraft fees in some cases, it may also result in paying the larger, more important transactions first. To the extent that overall overdraft fees are limited, that limit should address the concerns that gave rise to the order of pay provision. To the extent that check and ACH overdraft fees are not limited, as I have suggested, the order of pay issue remains, but there may be no universal solution to this concern. As a practical matter, consumers' preferences for order of payment are likely to depend on the actual transactions involved and it is simply not practical to consult with consumers every time that these decisions are made.

Finally, various sources have estimated the amount of revenue that depository institutions receive from overdraft services. These numbers are high, often tens of billions of dollars per year. To the extent that H.R. 3904, or similar requirements, reduce overdraft fees and overdraft revenues to depository institutions significantly, amounts of this magnitude cannot simply be absorbed by depository institutions as an additional cost of doing business, particularly in today's troubled economy. Further, reliance on overdraft fees for revenue is not limited to large depository institutions. Overdrafts are an important source of revenue to community banks and credit unions that played no part in creating the current economic difficulties.

In order to compensate for the loss of overdraft revenue, depository institutions will be forced to reprice checking account services to consumers. Lower interest rates, more and higher account maintenance fees and per transaction fees are all likely to result from any significant limitation on overdraft fees. With interest rates at historically low levels, it is likely that checking account pricing will focus on fees that may correlate more highly with account costs rather than further reductions in interest rates paid on accounts. In addition, interest rate reductions would penalize high balance accounts that may be more profitable. On the other hand, more or higher account maintenance fees would tend to discourage consumers from maintaining small, relatively low activity accounts, possibly leading to an increase in the number of unbanked consumers. Further, per transaction fees may penalize more active accounts, thereby encouraging consumers to rely more heavily on the use of cash, which is more susceptible to loss and theft and less traceable for law enforcement purposes.

Regardless of the pricing structure that ultimately evolves, consumers will need to manage their account balances more carefully, such as by recording individual payment transactions in a register and continually updating the register to reflect not only deposits and payments, but also, potentially, the time of posting and availability of these transactions. In addition, consumers likely will need to maintain higher balances in their accounts to avoid timing errors that may result in the denial or return of a critical transaction. The need to take these steps will apply not only in the case of consumers who have not opted in, but to all consumers who may have transactions denied or returned because transactions have reached the allowable limit for overdraft fees in that month or for the year.

Thank you for the opportunity to be here today and to address this important issue. I would be happy to address any questions.

INDEPENDENT COMMUNITY
BANKERS *of* AMERICA

Testimony of

R. Michael S. Menzies, Sr.
President and CEO, Easton Bank and Trust Company
Easton, Maryland

On behalf of the
Independent Community Bankers of America

Before the

Congress of the United States
House of Representatives
Committee on Financial Services

Hearing on

"The Overdraft Protection Act of 2009"

October 30, 2009
Washington, D.C.

Chairman Frank, Ranking Member Bachus, Members of the Committee, my name is Michael Menzies. I am the President and CEO of Easton Bank and Trust Company in Easton, Maryland, and the Chairman of the Independent Community Bankers of America[1]. ICBA appreciates the opportunity to express our views on the regulation of overdraft programs through the Overdraft Protection Act of 2009, H.R. 3904, introduced by Representative Carolyn Maloney.

Approximately 76% of community banks provide some form of overdraft coverage, and all of those do so fairly and in a way that best meets the needs of their customers. However, community bank customers understand that when they spend money that does not belong to them, there are consequences and costs. It is this understanding that encourages community bank customers to avoid spending money they do not have, and creates the perception of overdraft services as a valued benefit of doing business with a community banker, not a predatory means of ripping someone off.

While community banks always seek to treat customers honestly, the same expectations must hold true in reverse: customers should not – and generally do not – expect a free pass when a bank covers their overdrafts. The alternatives for a consumer – merchant returned check fees, possible credit report and check verification system blemishes, collections hassle, embarrassment, and the potential reliance on payday lenders – are far worse than incurring an overdraft fee.

[1] The Independent Community Bankers of America, the nation's voice for community banks, represents 5,000 community banks of all sizes and charter types throughout the United States and is dedicated exclusively to representing the interests of the community banking industry and the communities and customers we serve.
With nearly 5,000 members, representing more than 20,000 locations nationwide and employing nearly 300,000 Americans, ICBA members hold $1 trillion in assets, $800 billion in deposits, and $700 billion in loans to consumers, small businesses and the agricultural community.

The issue of returned checks, and the process that occurs when a consumer writes a bad check, must be emphasized. First of all, I must note that banks are not required to honor checks drawn on insufficient funds. When a check is returned unpaid to a merchant, the customer often must pick the check up and pay a fee to the store. By that point, the bad check has likely been scanned into a nationwide check verification database such as TeleCheck. When a consumer has a bad check recorded in a system like this, retailers that use check verification systems at the point-of-sale will likely not accept a check from that consumer for future purchases. Thus, any legislation that is likely to increase the amount of returned checks will unquestionably harm consumers.

ICBA strongly supports ensuring consumers are fully informed about the terms and conditions of overdraft protection programs and are made fully aware of other services for covering overdrafts that are available to them. It is also reasonable to prohibit reporting overdraft protection program usage to consumer reporting agencies when overdrafts and fees are paid according to program terms. Additionally, community bankers support the provisions in H.R. 3904 that restrict the advertising and marketing of overdraft products in ways that are deceptive to consumers. Overdraft protection programs are a last resort, and should not be portrayed as an extra line of credit or in any way that encourages consumers to overdraw their accounts.

Beyond those provisions, however, the Overdraft Protection Act fails to protect community bank customers who appreciate the overdraft services their banker provides. While a one-size-fits-all legislative band-aid such as H.R. 3904 will have the desired effect of curbing abusive overdraft practices, it will also drastically limit the ability of fairly run overdraft programs to meet customer needs.

Legislation must exempt discretionary overdraft services

It is critical to draw a distinction among the types of overdraft services a community banker can provide. The most commonly known programs include automated programs which are usually run by a third-party vendor that provide consumers with pre-established overdraft limits, lines of credit which require credit approval to qualify, and sweep accounts which draw overdraft coverage from a consumer's linked savings account or another checking account. Automated programs have become more common as a means of meeting consumers' evolving needs; yet these are the same programs that have understandably drawn the ire of many members of this Committee for scenarios in which a consumer overdraft results in a $35 cup of coffee. Many community bankers tailor their automated programs so that this situation, involving a low-dollar transaction or overdraft, would never occur. Moreover, if it did occur, most community bankers would gladly refund the fees associated with such a nominal overdraft.

A final method of overdraft coverage is the discretionary coverage that a community banker provides on an individualized basis. These services are not provided through a third party, but instead involve a banker actively evaluating, on a case-by-case basis, a customer's overdraft and financial circumstances. Most often these situations arise with important, high-dollar items like a mortgage, car, or utility bill payment by check or ACH debit. As such, they are the most important expenditures faced by consumers, which would have the most harm if rejected for insufficient funds by the bank[2]. Processing these

[2] The Federal Reserve, in its January 29, 2009 Final Rule on amendments to Regulation DD (the Truth in Savings Act), addressed discretionary overdraft coverage: "The Board recognized this longstanding practice when it initially adopted Regulation Z in 1969 to implement the Truth in Lending Act (TILA). The regulation provided that these transactions are generally not covered under Regulation Z where there is no written agreement between the consumer and institution to pay an overdraft and impose a fee…The treatment of overdrafts in Regulation Z was designed to facilitate depository institutions' ability to accommodate consumer's transactions on any ad hoc basis."

transactions is a burdensome task for small banks, which among other things must notify the customer and make the decision on whether to pay or return the transaction. In some of these instances, overdraft situations occur just because the consumer made an error in computing their account balance. These situations are generally corrected quickly. But, if the balance is negative for a prolonged period of time, the bank must attempt to recover the funds or suffer a loss.

Our members' practices demonstrate the strength of the relationship-driven model of community banking and how overdraft coverage can be the most personal service a banker can provide. Unfortunately, H.R. 3904 would jeopardize a community banker's ability to fulfill this role, leaving consumers in the lurch. ICBA urges this committee to exempt discretionary overdraft coverage from any legislation moving forward.

H.R. 3904 would have unintended consequences for community bank customers

ICBA strongly opposes the Overdraft Protection Act. A fundamental flaw of this legislation is that it attempts to restrict the supply of overdraft coverage while discounting the fact that community bankers offer these programs to meet customer demand. Our future depends on maintaining good customer relationships by meeting their legitimate demands. It is unfortunate that H.R. 3904 does not focus on encouraging personal financial responsibility, and instead would dramatically burden small financial institutions who cannot afford to harm their customers with unfair or deceptive overdraft coverage.

Providing overdraft coverage is not without risk to the bank. Overdraft fees are meant to cover the real loss exposure for overdrafts a bank faces by carrying an unsecured, unpaid loan on its books. Since nothing in H.R. 3904 mandates that the federal government will guarantee payment to banks of any overdraft on which no fee was charged, this legislation is likely to have serious consequences for a community bank's ability to control its risk exposure. In fact, community banks have informally reported that between 15-30% of overdraft fees must be charged off as uncollectible, and any unpaid overdraft balance must be reclassified into a loan and eventually charged off against the loan loss reserve of the bank.

Beyond this, there are numerous issues with H.R. 3904 that I would like to address:

- Mandatory opt-in for all consumers is anti-consumer: Generations of community bank customers have come to expect that their banker will ensure they have access to their accounts, even if granting that access means overextending themselves temporarily. Community bank customers understand and appreciate that it is in their best interest to accept a reasonable overdraft fee in exchange for their banker clearing a check or allowing a debit card point-of-sale transaction to be completed, rather than paying a non-sufficient fund fee, a bounced check fee, and facing the possibility of being late on a mortgage or other critical payment. If they do not, then they already have the means to opt-out. Additionally, requiring opt-in for existing accounts with overdraft protection would cause significant disruption of service and inconvenience to those who have and value the service.
- Price controls and quantity limits on overdrafts will reduce the availability of overdraft coverage and, potentially, other deposit services: If arbitrary caps are imposed on overdraft fees, community bankers – who are proven risk managers – must find other ways to manage the risk. These ways could include eliminating free checking for all customers, eliminating the convenience of debit cards for

overdraft-prone customer, and closing overdraft-prone accounts. A likely unintended consequence of this bill would be to increase the ranks of the unbanked.

- Prohibiting banks from issuing NSF fees will not eliminate debit card overdrafts, and will result in greater losses for community banks: Debit cards pose unique risk management challenges for community banks. When a merchant obtains an authorization code from the bank, the risk does not disappear. Instead, it is transferred from the merchant to the bank, which guarantees the merchant that it will pay the transaction. While the authorization happens using the most recent balance (frequently the ledger balance from the previous night's processing) the transaction does not settle until the next day, and sometimes longer, depending on how long the merchant takes to settle their transaction. If the consumer has checks and other transactions clear in the meantime, the transaction may result in an overdraft.

  One tool that community banks use to manage the risk of the point-of-sale debit guarantee is by placing a hold on the authorized amount. These holds protect the bank against funds that it has pledged to pay to the merchant, on a customer's behalf. These holds remain on the account until the transaction clears, and the bank will remove the hold if the authorization has not cleared after several days. *If an overdraft occurs while that hold is in place, the bank should not be faulted because the merchant has not settled funds and fulfilled its end of the payments process.*

- Real-time account balance information at an ATM or branch teller is not feasible. Not all banks process debits and ATM transactions in the same manner or at the same time. As a consequence, even at a bank's proprietary ATM or branch teller, the means do not exist to verify with 100% certainty that a transaction at a given moment in time will not lead to an overdraft situation should, for example, another bank process its transactions at a later time. Additionally, banks that use a daily ledger balance rather than a real-time balance will be unable to comply with this requirement without significant financial burden.

However, ICBA appreciates the inclusion of a study to be conducted by the Government Accountability Office on the feasibility of providing an accurate means for a consumer to be informed of an overdraft situation at a point-of-sale. The system is not intended to carry this sort of information, and implementing these changes will not only carry significant cost, but will also disrupt the customer experience going forward by adding to the length of time required to complete a transaction, and also placing the customer at risk of embarrassment in the event a charge is declined. This sort of change will also require significant and costly upgrades to merchants' point-of-sale terminal equipment, another cost that likely will be passed on to merchants and ultimately to consumers.

Conclusion

In a perfect world, consumers would never find themselves in a situation where they may overdraw their account. But as this Committee is well aware, consumers do encounter situations in which overdrafts happen, be it a result of economic hardship or something as simple as a math error in computing their balance. But whatever the reason, community banks should be able to provide overdraft protection and receive a market-based, competitive fee for the cost and risk of paying transactions for a consumer with the bank's own funds.

For community banks, the consequences of this legislation are clear: if enacted, a significant portion of community banks would stop offering discretionary and automated overdraft programs. Consumers will not appreciate the consequences of this legislation either when they face a significant increase in the amount of returned checks and rejected debit card transactions. These will not only cause embarrassment, but could affect their credit rating and cost them more money than an overdraft due to returned check charges from the merchant.

Overdraft programs are not all created equal, a fact which gives community banks the ability to leverage the unique and close relationship they have with their customers to offer them competitively priced programs to best meet their needs. This competitive advantage is an important part of what allows community banks to serve their customers, especially those who are already at the margin.

Thank you, and I look forward to your questions.

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TESTIMONY
OF
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PRESIDENT AND CEO
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ON BEHALF OF
THE CREDIT UNION NATIONAL ASSOCIATION
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OCTOBER 30, 2009

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COMMITTEE ON FINANCIAL SERVICES
UNITED STATES HOUSE OF REPRESENTATIVES

OCTOBER 30, 2009

"THE OVERDRAFT PROTECTION ACT OF 2009"

Mr. Chairman, Ranking Member Bachus, Members of the Committee, thank you very much for the invitation to testify before the Committee today to express the views of the Credit Union National Association (CUNA)[1] on the Overdraft Protection Act of 2009. My name is Rod Staatz and I am President and Chief Executive Officer of State Employees Credit Union of Maryland (SECU).[2] I am also a member of CUNA's Board of Directors.

The Impact of Proposed Overdraft Legislation

CUNA strongly supports the ability of credit unions to offer overdraft protection plans as a means to help their members resolve short-term financial problems. While the terms of credit union overdraft protection programs may vary, they are structured to help to pay, rather than return, non-sufficient funds transactions in exchange for fees that are similar to those charged for returned items. This spares members the embarrassment of returned checks, as well as additional fees charged by merchants and other payees. Such programs, when used appropriately by consumers, serve as a valuable back-up to overdrawing checking accounts or relying on payday lenders or check-cashing businesses, and are fully consistent with the philosophy and principles of the credit union system.

However, CUNA recognizes concerns exist about how some overdraft protection programs operate and is sympathetic to Congressional interest in enacting a law to address abusive

[1] CUNA is the nation's largest credit union advocacy organization representing nearly 90% of America's 8,000 state and federally chartered credit unions and their 90 million members.
[2] Founded in Baltimore in 1951, SECU is the largest credit union in Maryland and serves 248,000 members. SECU's total assets were $2.06 billion as of June 2009.

practices. CUNA is convinced that the provisions in H.R. 3904, particularly the provisions that would limit the number of overdraft fees that could be charged per month and per year, would simply end overdraft programs -- to the detriment of many consumers who truly value these programs. Consumers will incur more non-sufficient fund (NSF) fees with none of the benefits of having many transactions honored. They will pay more merchant return check fees and have more bad checks reported to consumer reporting agencies. Merchants will deal with more bounced checks and have more bills that are currently paid under automated bill-paying services rejected. Inevitably, other adjustments will be made in checking account services and maintenance fees that will impact a wide range of accountholders. All consumers lose under this scenario.

Credit Unions' Best Practices

While there is certainly an exception to every rule, we believe most credit unions approach overdraft protection in a manner that is in the best interest both of the individual member using the service as well as the overall membership of the credit unions, who put their own money behind the program.

Several years ago, CUNA's Board of Directors adopted policy calling on every credit union that is a member of CUNA and offering overdraft protection services to adopt overdraft protection standards and ethical guidelines to emphasize credit unions' consumer-orientation. Our policy states:

> *Credit unions recognize that the following practices are not consistent with the credit union philosophy and principles and publicly affirm that they will not engage in any of these practices:*
>
> - ***Deceptive Advertisement***
> *Advertising, representing, or implying that the member should expect that all overdrafts will be paid but then stating in other documents that the paying of overdrafts is discretionary, which is a standard feature of overdraft protection plans. Such advertising may lead members to rely on the service in expectation that all overdrafts will be paid, which would be detrimental if any overdrafts are not ultimately paid by the financial institution.*

- ***Enticing Members to Overdraw Accounts Repeatedly***
  Advertising or promoting the overdraft protection plan in a manner that encourages the member to overdraw repeatedly his or her share draft account, ***as opposed to*** *such a plan being used as an occasional convenience for the member. The frequent overdraw of accounts is a practice that financial education programs, such as those offered by credit unions, generally discourage.*
- ***Structuring Programs that Mislead Members***
  Including a feature that records the amount of coverage being offered to cover overdrawn share drafts as part of the "available funds," such as on ATM receipts, online statements and telephone balance statements.
- ***Failure to Inform Heavy Users of Overdraft Protection Programs of Alternatives***
  Overdraft protection programs may not be appropriate for members who heavily use and rely on overdraft protection programs as a means to pay a significant proportion of every day living expenses. For these members, credit unions may offer a number of other products and services that would be more appropriate. These may include transfers from a savings account to the share draft account, as well as other types of less expensive secured and unsecured loans that the credit union offers to all its members.
- ***Failure to Provide Financial Counseling Information***
  Credit unions recognize that they have a role in helping their members use overdraft protection services in a responsible manner. In addition to providing adequate disclosures regarding the features and fees associated with the programs, credit unions should also provide information regarding counseling services provided by the credit union or other reputable counseling services.

SECU's Overdraft Program

Mr. Chairman, please allow me to describe how SECU's overdraft protection program, "Courtesy Pay," works. The objective of Courtesy Pay is to permit members to have many transactions completed even when they lack sufficient funds in their checking accounts and to spare them from merchant and collection agency fees incurred for returned checks. Courtesy Pay is <u>not</u> factored into available balances for approval of debit card, ATM or teller transactions. I am sure that many elements of my program are similar to overdraft programs used by credit unions throughout the United States.

Here is how our program works. A member can pre-arrange to have funds drawn from a selected savings account or establish a line of credit, and if he or she writes a check without enough funds in his checking account, the necessary funds are automatically drawn from the other account or line of credit. There is no fee for this overdraft service. Courtesy Pay for qualified members allows SECU to pay an item after all other funds from a member's accounts have been exhausted or a pre-arrangement transfer plan has not been established.

SECU covers the necessary amount up to the member's Courtesy Pay limit established by SECU ($500, $750, $1,000 depending on the member's standing.) The member's checking account is debited that amount plus a $27 fee. The member is sent a non-sufficient funds notice explaining that the account is negative and a deposit is required to bring the account to a positive status. If the account is not positive within 30 days, all future items will be returned "NSF" with a $27 NSF fee assessed.

SECU does not allow members to draw their balance into the negative at the teller line, ATM, or through their debit card. Courtesy Pay only pertains to written checks and approved ACH debits.

SECU does not market Courtesy Pay because we do not want to encourage members to live beyond their means -- knowing Courtesy Pay is an option to cover overdrafts may lead them to view it as available funds. Approximately 90% of our members qualify for Courtesy Pay. To be eligible, the account must be open for at least 30 days, and the member must be in good standing with no current delinquencies and no previous charge-offs.

Guidelines for Refunds

If a member contacts SECU for a fee refund, we review the account and consider the specific circumstances. SECU makes full fee refunds without question if the fee was assessed through a SECU error or if the member is in good standing and has had no non-sufficient funds/overdraft refunds in the past.

If the member is in good standing with unusual circumstances that warrant a refund of some kind, we consider a full or partial refund based on the member's situation. Examples include a job loss, merchant holds, deposit holds, a single mathematical error that triggers a series of incoming items to create overdrafts, and payday lending where lenders repeatedly withdraw from the account. Additionally, we refer them to free financial counseling.

Program Abuse

SECU monitors overdraft protection abuse. Even those members who honor the terms of our agreement to restore their balance to a positive balance within 30 days but demonstrate repeated overdraft behavior will have progressive notification from warnings to account closure for overuse of Courtesy Pay. In 2008, SECU closed 486 checking accounts for abuse.

Why Overdraft Programs Assist Working America

While we have several concerns with H.R. 3904, our primary concern is the provision that limits the number of overdrafts that can be provided by a credit union to a member. H.R. 3904 prohibits a credit union from charging more than one overdraft fee per month and no more than six in a calendar year per transaction account.

Any arbitrary limit would basically end credit unions' overdraft programs and cause member dissatisfaction and even potential hardships. Overdraft fees are obviously assessed both because covering an overdraft is a service and because the fee is there to control overuse of the service. Members cannot necessarily predict when they will need the help – what if they already incurred an overdraft fee early in the month and then needed our Courtesy Pay to help cover the car payment due later in the month?

I can give you many examples of how the SECU Courtesy Pay program is of value to our membership everyday. But when a smaller credit union yesterday heard I was testifying, it sent me an email, imploring that I make a strong case to Congress about how important overdraft programs are to credit union members. So while I can give you similar examples from SECU's file, let me share some real world examples that credit union sent to me, a credit union with 18,000 members who are mostly blue- collar workers and their families:

1. A scenario that arises time and again is the member using the overdraft program so the rent check doesn't bounce, which avoids late payment fees and possible problems with the landlord.
2. An elderly member who received her Social Security check early in the month used the overdraft program to pay her electric bill.
3. A few days before payday, a member's child got sick and funds were low in her account, but she could cover the cost of the doctor's visit by relying on the overdraft program.
4. A similar example was provided about the member who needed to rely upon the overdraft program to buy groceries for the family before payday.
5. A member used the overdraft program to make his car payment when his checking account was a little short of what was owed, which prevented a late payment fee and a report to the credit bureau for being 30 days late.
6. And a member who had opted out of the overdraft protection service -- certainly something allowed by credit unions – called back a few weeks later and wanted to resume the overdraft protection service, deciding that it wasn't worth paying NSF fees to the credit union plus the returned check charge to merchants.

As these examples show, overdraft programs at credit unions are there primarily to serve working America, the people who basically live paycheck to paycheck. To put arbitrary limits on overdraft programs offered by depository institutions will only undermine these programs and drive people to alternative money providers who will undoubtedly charge more.

Merits of a Regulatory Approach

Instead of the legislation before the Committee, CUNA strongly believes that concerns should be addressed through the federal regulatory system, which allows for a notice-and-comment process to evaluate what regulations may be appropriate and to hopefully protect from unintended consequences of federal restrictions on overdraft programs. We note that just over a week ago, the Committee approved legislation to create a robust federal consumer protection regulator, which would have the authority to promulgate rules governing overdraft protection programs. Moreover, the Federal Reserve and other banking regulators, which currently have the authority to issue these rules, have rulemaking processes underway which address key concerns with overdraft programs.

The periodic statement disclosure requirement proposed in Section 4 of H.R. 3904 is already scheduled to go into effect on January 1, 2010. The Federal Reserve Board (Regulation DD) and the National Credit Union Administration (NCUA) (Section 707) earlier this year amended their implementing regulations to the Truth in Savings Act to require the dollar amounts charged for overdraft fees and returned item fees, both for the month and year-to-date, to be disclosed on the periodic statements of transaction accounts, starting nine weeks from now. Currently, only financial institutions that advertise or otherwise promote their payment of overdrafts are required to provide these disclosures. I should add that SECU does not market our overdraft Courtesy Pay program because we do not want to encourage members to live beyond their means – knowing that there is an option to cover overdrafts may lead them to view it as available funds. We think disclosure of dollars spent, rather than the proposed disclosure of the fee as a "finance charge" under the Truth in Lending Act (TILA) is of more practical meaning to the consumer.

Another Truth in Savings amendment effective January 1, 2010 mandates that financial institutions providing account balance information through an automated system only disclose the amount of funds available for withdrawal *without* including the additional funds that would be available under an overdraft program. We believe this new regulatory requirement is what will be expected under Section 4 of the bill on "Exclusion from Account Balance Information." Even without this regulatory mandate, available checking balances at SECU do not reflect availability of courtesy pay amounts.

A third possible change to overdraft programs is under active consideration by the Federal Reserve using its Regulation E implementing authority of the Electronic Funds Transfer Act. In its January 2009 proposal, the Federal Reserve outlined two approaches for providing consumers a choice regarding the payment of ATM and one-time debit card overdrafts by their financial institutions, asking for comments on which approach should be adopted by regulation. Under an "opt out" approach, an institution would be prohibited from imposing an overdraft fee unless the accountholder is given an initial notice and a reasonable opportunity to opt-out of the overdraft service, and the consumer does not opt out. Under the "opt in" approach, the institution would be prohibited from imposing an overdraft fee if it chooses to pay an overdraft unless the accountholder affirmatively consents to the overdraft service.

In CUNA's comment to the Federal Reserve last spring, we generally supported action in this area if limited to ATM and one-time debit services. If an opt-in approach were to be adopted, CUNA strongly urged the Fed to permit financial institutions to continue to use an opt-out system for existing accounts. CUNA raised many other operational concerns and considerations in our comment letter on implementing possible new Regulation E requirements on overdraft programs. This proposal provides a good example of why the regulatory process, not the legislative process, should be used to address consumer disclosures and protections.

In 2005, NCUA and the other federal financial institution regulators issued guidelines on overdraft protection plans that addressed safety and soundness considerations, legal risks and best practices. These guidelines are still in effect, and attached to this testimony is a two-page chart that summarizes the agencies' best practices and SECU's Courtesy Pay program. I feel our program measures very favorably to what the regulators have laid out in their guidelines and provides a valuable service to our membership.

CUNA is uncertain about what other TILA requirements may be triggered if overdrafts are brought under TILA and Regulation Z, something that needs further analysis. While we are certainly pleased that the bill's sponsors acknowledge the problem that would be created for federal credit unions without an exception to the federal usury ceiling (Section 3 in the bill), we strongly believe that overdraft protection programs are not lending programs but rather are accommodation services provided at the discretion of the credit union, not based on any loan underwriting standards CUNA continues to believe that overdraft programs are appropriately regulated by Truth in Savings rules.

Additional Credit Union Concerns Regarding H.R. 3904

Prompt Notification

H.R. 3904 would require prompt notification of the consumer when an overdraft occurs including the date of the transaction, the type of transaction, the overdraft amount, the overdraft coverage fee, the amount necessary to return the account to a positive balance, and whether the participation of the consumer in the program will be terminated if the balance is not returned to positive within a given period of time. The bill requires the credit union to use a notification method requested by the consumer.

Credit unions would have significant concern with any requirement for same-day or "real time" notification of an overdraft occurrence given the fact that many of them do not have the technological capacity to provide such a notification to their members in a short period of time.

Additionally, while larger financial institutions may have a greater capacity to provide this type of notification via email or text messaging, we are concerned that credit unions would not be able to provide this type of notification. Moreover, there would increased burden associated with keeping track of which members want which types of notification.

ATM Notification

H.R. 3904 would require credit unions to warn consumers at ATM machines if the transaction would trigger overdraft coverage fees and provide the consumer the opportunity to cancel the transaction. While this provision would appear to be well-intentioned, we do believe that this requirement would represent a compliance burden that we do not believe can be met given current technology and the structure of the payment system.

There are other ways to notify consumers that the transaction that they are about to complete may cause an overdraft event. A "sticker" on the side of any ATM – which has been used in the past for other warnings – or a first screen general notice alerting the consumer that a withdrawal from the ATM may trigger an overdraft fee by his own institution, may be appropriate notice for consumers. At some point, however, we do think the consumer has the responsibility to know how much money he has in his checking account. We are also mindful of the fact that there is no warning given when a consumer writes that check which puts him in an overdraft position.

Treatment of Debit Holds

H.R. 3904 would prohibit charging an overdraft fee on any transaction if the overdraft results solely from a debit hold that exceeds the actual dollar amount of the transaction. The significant problem with debit holds is that financial institutions have little control over the holds placed by merchants and are unable to determine the exact amount of the transaction or control how long the hold is in place. We believe merchants should be subject to additional rules that require them to submit debit card transactions promptly for settlement as this will significantly reduce the overall amount of overdraft fees that are assessed as a result of debit holds.

Government Accountability Office Study

The Committee will undoubtedly hear conflicting information with respect to consumer opinion of overdraft protection programs. We encourage Congress to ask the Government Accountability Office to study consumer opinion with respect to these programs, specifically if consumers prefer overdraft protection services to having their checks bounce and other debits denied.

Conclusion
Mr. Chairman, credit unions generally agree that consumers of financial products—especially those consumers of financial products provided by for-profit and unregulated entities—need greater protections. That is why we have said for the last several months that a consumer financial protection agency *could* be a good way of providing those protections; however, in order for such an agency to work, consumer protection regulation must be consolidated and streamlined. For the better part of the last two decades, many of the consumer protection statutes that Congress has enacted actually resembled regulations, in terms of level of specificity. While we do not believe that H.R. 3904 should become law under any circumstances, the bill is another example of Congress attempting to legislate a question that may be better answered by a regulator responsible for consumer protection working in conjunction with a safety and soundness regulator.

Mr. Chairman, thank you very much for the opportunity to testify at today's hearing. I look forward to answering questions from the Members of the Committee.

Comparison of SECU to Federal Financial Institution Regulators' Guidance on Best Practices for Courtesy Pay

Best Practice	SECU Practice
Avoid promoting poor account management.	Discussion of no-fee options (savings overdraft, LOC) occurs at account opening and is repeated in every paid item notice. Three step NSF abuse program applied to members who carry YTD NSF counts of 20 or more for periods of 6, 9 and 12 months.
Fairly represent overdraft protection programs and alternatives.	Every paid item notice includes the message "Avoid NSF fees – apply for a line of credit or use savings for overdraft protection on your account" with the corresponding phone number and web address for application.
Train staff to explain program features and other choices.	No-fee options are explained consistently at account opening. SECU does not promote Courtesy Pay; however staff are trained to explain the program features in response to member inquires.
Clearly explain discretionary nature of program.	SECU does not represent that the payment of items is guaranteed. Courtesy Pay is a privilege.
Distinguish overdraft protection services from "free" account features.	SECU does not market Courtesy Pay as part of free services.
Clearly disclose program fees.	Overdraft/Non-Sufficient Funds/Uncollected Funds (whether paid or not paid) = $27. Disclosed on fee schedule provided to all members at account opening.
Clarify that fees count against the disclosed overdraft protection dollar limit.	SECU has standard limits ranging between $500 and $1,000 based upon account type. SECU does not disclose the limits as to not promote the program and the ability to utilize the limits. Therefore we do not clarify that the fees count against the disclosed overdraft protection limit. Yes, both the dollar amount of the item and the associated fee are combined to count towards the dollar limit.
Demonstrate when multiple fees will be charged.	Each overdraft occurrence incurs one fee. There are no multiple fees.
Explain impact of transaction clearing policies.	SECU does not currently disclose the process or the impact of transaction clearing policies.
Illustrate the type of transactions covered.	Yes, we disclose that Courtesy Pay covers in-clearing checks and previously approved ACH debits only.
Provide election or opt-out of service.	Opt out service is offered.
Alert consumers before a transaction triggers any fees.	Courtesy Pay is NOT considered for approval of electronic transactions (card purchases and ATM withdrawals) or for cashing over the counter checks in branches. It is therefore impossible for the member to accidentally trigger fees in situations where advance notification could be provided.
Prominently distinguish balances from overdraft	The amount of overdraft protection is not included in checking available balance. Available checking balances do not reflect

Best Practice	SECU Practice
protection funds availability.	savings balances, available Line of Credit or available courtesy pay amounts. Knowing Courtesy Pay is an option to cover overdrafts may lead members to view it as available funds.
Promptly notify consumers of overdraft protection program usage each time used.	Daily notices are sent by mail and populated in online banking whenever a check and/or ACH debit triggers either a paid or returned NSF fee.
Consider daily limits on the consumer's costs.	We do not have a daily cap.
Monitor overdraft protection program usage.	SECU monitors overdraft protection abuse. For those who honor the terms of our agreement but demonstrate repeated overdraft behavior, we have three levels of progressive notification from warnings to account closure. Level 1: First letter is triggered when the member has carried 20 or more NSF's for six consecutive months. Member is warned that courtesy pay may be revoked with continued abuse. Level 2: Second letter is triggered when the member has carried 20 or more NSF's for nine consecutive months. The member's courtesy pay is revoked and the member is warned that their checking account will be closed with continued abuse. Level 3: Final letter is triggered when the member has carried 20 or more NSF's for twelve consecutive months. Account is reviewed and may be closed unless the member has had extenuating circumstances. In 2008, SECU closed 486 checking accounts for abuse.
Fairly report program usage.	SECU does not report negative information to consumer reporting agencies when the overdrafts are paid under the terms of the overdraft protection programs.

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