From: "Ken Golliher" <Pegasus@aye.net> on 06/24/2004 10:32:10 AM

Subject: Overdraft Protection Programs

Re: Overdraft Protection Guidance
Date: June 24, 2004

This information is offered in response to a request for comments on Interagency Guidance on Overdraft Protection Programs (ODPs). I am employed as an independent trainer within the banking industry. During the last 20 years, I have worked for the FDIC, the OTS, and more than 25 state banking associations in that capacity. The opinions expressed are entirely my own and I not compensated for offering them; they differ in some material respects from those held by some of my clients.

My primary criticism of the proposal is that it reflects a regulatory reaction to the paradigm established by ODP vendors. Instead, it should reflect a fresh look at how consumers should be discouraged from authorizing payments against insufficient funds and informed of the effects of such actions if they do.

Debits presented against checking accounts are generally either electronic funds transfers or checks. The essence of an ODP is that a bank is predisposed to pay, rather than return, a debit presented against insufficient funds. However, there are substantial opportunities for abuse in the way ODPs are marketed to consumers. Those abuses should be prohibited.

Although the proposed guidance conclusively refers to ODPs as "a credit service," the lack of a definition as to what constitutes an ODP makes it difficult to trace any philosophical consistency through the proposed guidelines. To reach consistent and logical results in this area, all "guidance" and relevant regulations will need to rest on a practical and legal fiction: Any item presented against insufficient funds is the result of an error by the consumer who authorized the charge. That fiction will best protect the consumer and reflect a regulatory philosophy rather than a regulatory reaction.

Clearly, consumers like ODPs. The alteration of Regulation DD and these guidelines will put banks who do not offer a formal program at a disadvantage. The net effect of these initiatives will be that all banks will offer and promote formal ODPs.

The Legal Foundation for Overdrafts on Checking Accounts

The law governing the deposit and payment of checks is articles 3 and 4 of the Uniform Commercial Code (UCC). The UCC is a model law promulgated as a state statute. Some state legislatures modify its terms before enactment, but its provisions relating to overdrafts are largely uniform among the states. The model version of the UCC is accompanied by an Official Commentary which some, but not all, states reference as a source of interpretation in their statutory framework. The UCC is a commercial law which attempts to treat all parties fairly; the model version of the UCC contains very few, if any, provisions aimed at consumer protection.

First, the UCC does not require a bank to pay a check presented against insufficient funds (NSF). Any commitment on the bank's part to pay NSF items must come from some other specific agreement with the customer. Second, if several items are presented for payment on the same day and there are funds to pay some, but not all, the UCC allows the bank to pay the items in any order; the bank may pay some and return others randomly. Alternatively, it may follow a predetermined, but undisclosed pattern in deciding what items to pay or return. Third, any payment of a check against insufficient funds overdraws the account and creates an implied promise to repay by the drawer of the item. Usually, contractual terms make all account signatories liable for the overdraft, regardless of who authorized the offending debit(s).

Electronic funds transfers (EFTs) are generally governed by consumer protection provisions in Regulation E and, in many operational contexts, the National Automated Clearing House Association (NACHA) rules. In combination, those rules and regulations do not address:

- the concept of overdrafts or
- the idea that one electronic debit should be paid in preference over another, or
- the idea that an electronic debit should be paid in preference to a paper item or
- any personal liability the person who authorized an electronic debit might have if the item is presented against insufficient funds.

It is worth noting that many EFTs are individual transactions such as those initiated at ATMs or through the use of a debit card. However, many more are preauthorized transfers occurring at somewhat regular intervals without specific prompting by the consumer. There are many aspects of checking account administration that are routinely resolved by references to the UCC due to lack of a parallel structure for EFTs.

Banks customarily disclose "NSF fees" rather describing one fee for debit returned and different fee for debits paid; i.e. the fee imposed for an NSF check paid is the same as that imposed for an NSF check returned. Banks generally do not distinguish between checks and electronic debits in the imposition of NSF fees. Generally, they purposefully avoid varying fees between items paid and items returned in order to avoid any suggestion that the fee is for the extension of credit rather than the handling of an aberrant item.

When a bank decides to pay an NSF debit, the consequences for the consumer are nominal:

If a drawee bank or receiving depository financial institution…	**and…**
pays a debit issued against insufficient funds the drawer is generally assessed an NSF fee	no third party is aware that the check was written against insufficient funds; there are no secondary expenses or consequences.

When a bank decides to return an NSF check unpaid, the consequences to the drawer are significant:

If a drawee bank…	**and the drawer may also be…**
returns a check drawn against insufficient funds the drawer is generally assessed an NSF fee	assessed a returned check charge by a merchant payee <u>and</u>
	reported to a negative data base (other merchants may refuse to accept the drawer's checks) <u>and</u>
	subject to civil suit in small claims or some other state court for breach of the drawer's promise <u>and</u>
	subject to criminal prosecution under state law on the assumption that the drawer knew there were not adequate funds to pay the item.

If the receiving depositary financial institution (RDFI) returns an EFT debit, oftentimes a preauthorized transfer, the consequences to the consumer are less subject to generalization. However, the RDFI will surely impose an NSF fee. If the preauthorized transfer that is returned unpaid is payment for an ongoing contractual obligation, the originator may impose a fee on the consumer or may terminate the service; e.g. gym membership, life insurance, health insurance, utilities, etc.

The NSF fee is the common element regardless of whether an NSF debit is paid or returned.

Again, as illustrated, negative consequences increase exponentially when a debit is returned unpaid. <u>Clearly, anyone knowingly or mistakenly issuing a debit against insufficient funds would prefer that the drawee bank pay the item.</u> That simple fact is not acknowledged in the proposed guidance. Any regulatory action that discourages banks from paying overdrafts will be the antithesis of consumer protection.

Banks pay NSF debits for a variety of reasons:

If …	then it may be because it has…	and the bank imposes…
a drawee bank pays a check or an EFT presented against insufficient funds	made an informal, individual, decision based on factors unknown to the drawer which are intended to be objective, but may not be applied consistently in identical situations	an NSF fee regardless of whether the item is paid. (The bank has no financial incentive to pay the item versus returning it – payment is a courtesy extended to the customer.)
	fulfilled a contractual commitment pursuant to a separate agreement in transferring funds from an open – end line of credit established by the consumer to the transaction account	a fee for the transfer plus interest charges on the line of credit. The bank has a financial incentive to pay the item rather than return it, but the fee and interest income may be substantially less than an NSF fee.
	fulfilled a contractual commitment pursuant to a separate agreement in transferring funds from another asset account owned by the consumer to the transaction account.	a fee for the transfer. The bank has a financial incentive to pay the item, but the amount of the fee is substantially less than an NSF fee.

Generally, overdrafts are reflected on the bank's official reports as loans. Federal functional regulatory agencies analyze them accordingly. Banks are encouraged to address overdrafts in their written lending policies. They are expected to evaluate them as conservatively and consistently as they would any other type of unsecured credit. They cannot discriminate on legally prohibited bases under Regulation B in making decisions regarding the payment or return of NSF debits.

What is an ODP program?
At no point does the guidance define what an ODP program is. The process of naming and defining the service is best addressed in Regulation DD. However, under proposed amendments announced on May 28, 2004, Regulation DD uses, but also does not define "overdraft protection program." That proposal also coins, without defining, an additional term "automated overdraft services."

Obviously, the terminology needs to be homogenized and a definition provided. In effect, it needs to be made clear whether the guidance is relevant to any financial institution that pays overdrafts <u>or</u> only those financial institutions that actively promote their ODP/AOS programs. The best place for establishing the appropriate moniker is in Regulation DD. In my comments on that proposal, I will suggest that it be called an "Inadvertent Overdraft Policy" or any other label reflecting the concept that any overdraft is unintentional.

As for the coverage issue, for example, Bank A has an established practice, addressed in its loan policy, but not communicated to customers in any fashion, of paying NSF items based on the amount of the proposed overdraft and the bank's prior experience with the customer. Dollar limits are judgmental and not recorded, but they are based on the customer's average balance and the length of the customer relationship. The bank's practices are not communicated to customers in any formal way. Alternatively, Bank B purchased an ODP program from a vendor and actively markets its existence to customers including a "maximum" amount for a potential overdraft and customer opt-out provisions. Clearly, bank B has an ODP. Does Bank A?

Will promulgation of the guidelines encourage/force Bank A develop printed materials, train contact employees to discuss the program with customers, set and disclose limits, etc. even though Bank A considers its techniques to be more of a procedure rather than a product? In candor, are Bank A's customers better off if the federal government forces it to tell them the program exists?

Practical Meaning of "Best Practices"

Guidance from the federal functional regulatory agencies on the details of ODP programs is highly desirable. However, I do not find any precedent to indicate how a mechanism described as "Best Practices" and adopted on an interagency basis will be handled in on-site examinations. Obviously there is no statutory or regulatory mandate for interagency guidance on this topic; the foundation seems rather thin. The worst case scenario is that some examiners will treat it like a regulation and expect lock-step adherence. It would be helpful if any final guidance on this issue reflects the philosophy with which it is to be enforced or clearly indicates that it is provided only as a suggestion for supervised institutions and cannot be cited as the basis for formal criticism.

Emphasis on Safety and Soundness

The original request for information made no mention of any concerns that ODP's represented a safety and soundness issue. The extent to which it is emphasized here reflects conclusions regarding risks not supported with even anecdotal evidence; I have not heard of any bank that has suffered significant losses from its operation of an ODP designed for consumers with limits of \$100 - \$500, the scenario noted as common in the request for comments. If the agencies have examples of such circumstances, it would be helpful to the industry if they were publicized.

The proposal's suggested level of credit administration for ODPs poses a greater threat to their existence than the consumer protection provisions; they should be in some way justified by the proponents.

In any case, it is not accurate to state that no individual account underwriting is performed on these accounts. A great many banks pull consumer reports from negative data bases prior to account opening. Others obtain complete reports from other consumer reporting agencies prior to account opening. (One of the circumstances that often trigger the ordering of a detailed consumer report is a customer's request for a debit card at account inception. Based on their experience, banks clearly consider giving a consumer a debit card a far greater risk than enrolling him in an ODP.)

While a consumer may prevail on a loan application even though a consumer report contains negative information, a report from a negative data base is generally the death knell for a checking account application. If one bank learns that another bank has been left with a loss in connection with the applicant's previous account or that the applicant has written bad checks to merchants, the application is normally denied. (If evidence is needed that many people are denied checking accounts under these circumstances, please visit: Chex Systems Bites, http://chexsys.tripod.com/) A very significant amount of culling is done at the new accounts desk, regardless of whether it is recognized as conventional underwriting.

In addition, as noted in the information accompanying the request, most banks do not offer the service at account inception. Qualifying accounts have an age requirement so, in addition to the initial review, the bank has some experiential information on the customer. When a bank applies this program to an existing group of customers it oftentimes has years of experience to rely on in evaluating whether a consumer will take responsibility for an overdrawn account. Those excluded are account holders whose accounts:

- have sustained prolonged, unsatisfied overdrafts,
- are new,
- do not reflect routine deposits,
- do not reflect recent activity, or
- maintain a very low average balance, etc.

Obviously, people who write occasional NSF checks are included in the program.

Finally, many banks with ad hoc programs use more than deposit account information when deciding to pay or return a particular check. As one loan officer put it in a recent seminar, "If the bank has enough financial information to comfortably loan John Doe $300,000 and he is paying as agreed, I'm going to look profoundly stupid if I return an NSF check that would have overdrawn him by $1,300." Banks simply do not enter into these relationships blindly and they deserve substantially more credit for their risk analysis than the supplementary information accompanying the proposal implies.

While indicating that banks should establish "properly documented dollar limit decision criteria" seems like a consensus statement, no cost – benefit analysis would support it. The enhanced income substantially outweighs any conjectural risk. It may also be too restrictive and serve to limit overdrafts which the bank would otherwise pay for well established individual customers.

In practice, a bank should be able to assign a $300 - 500 limit to all customers who have survived an adverse selection process. A formal requirement for documentation of acceptable amounts implies that some sort of individual underwriting can be cost justified. It cannot.

Moreover, the suggestion that acceptable amounts should be established in advance suggests there should be no individual discretion in allowing overdrafts in greater amounts on a case by case basis. That is, if a customer's has been "approved for a $500 overdraft and a $1300 overdraft is eminent, the bank could not make decisions based on factors apparent at the moment; e.g. the presence of additional funds in other accounts owned by the same customer, knowledge of a pending loan, etc.

The suggested guidelines indicate "when an institution routinely communicates the available amount of overdraft protection to depositors…" those amounts should be reported as "unused commitments" in regulatory reports. This appears to be based on a theoretical assumption that all the bank's customers could overdraw their accounts at once. That seems disingenuous. In the alternative, if the agencies will adopt the philosophy that their guidance should restrict any such programs to "inadvertent overdrafts" and indicate that the service is not to be promoted using any other philosophy, it will be easier to allocate "commitments" of this type to some percentage of the entire portfolio of checking accounts, providing external analysts with much more accurate information.

Some banks acknowledge that their uncollectible overdrafts increased when they began using a formal ODP, but indicate those losses were dramatically offset by the increased fee income. Others are adamant that the ODP did not increase their losses at all. Nevertheless, it is important that income not be overstated and that losses are recognized in a timely fashion. It may be necessary to offer a broader explanation than to just say that uncollected overdraft fees are reversed against overdraft fee income. For example if the customer is overdrawn , but made a subsequent deposit which was not sufficient to satisfy the overdraft, is that deposit first credited against the "uncollected fees" or the "loan" portion of the overdraft amount?

Finally, the suggestion that overdrafts more than 30 days in duration should be automatically charged off assumes many facts not in evidence. My recollection is that when a "real" loan is more than 90 days past due and not in the process of collection, no one presupposes that it should be charged off, only that it be put on nonaccrual. The OCC standards for check credit (including a line tied to a checking account) would only consider the credit subject to charge off if it were 180 days past due. The implication of the 30 day period is an assumption that such a debt is simply not collectible. That assumption is baseless.

When a checking account is "charged off" the standard practice is that the account is credited for the amount of the overdraft and that the appropriate general ledger accounts; e.g. fee income and allowance for loan and lease losses, are debited with offsetting entries. Effectively, that closes the account. However, the standard industry practice is to give the consumer 7 - 14 days advance notice of account closure in order to give time for outstanding checks to clear. If consumers are to continue to receive that courtesy, then that letter would have to be sent 7 - 14 days prior to the end of that 30 day period. Effectively, the decision to charge off the loan would be in 2 – 3 weeks after the overdraft took place.

Obviously, losses should be recognized in a timely fashion, but 60 days is a far more realistic suggestion. At a minimum, as noted in the proposal, one of the regulatory agencies currently suggests a 45 day period. Unless it can be established that that time period was ill conceived and unworkable, the other agencies should give it some deference.

Finally, the charge off will begin the initiation of formal collection activity and the signal to turn the consumer's information in to a negative data base. Because the charge off triggers wholly negative consequences for the consumer, the guidelines do not do consumers any favors by setting a very brief time frame in which the bank must recognize a loss.

Best Practice Suggestions
Following are comments based on the individual bullets included in the request for comment:

• Avoid promoting poor account management. Do not market the program in a manner that encourages routine or intentional overdrafts; rather present the program as a customer service that may cover inadvertent consumer overdrafts.

This is a key concept and I have nothing to add, except to reiterate the suggestion that the this service be named consistently with this bullet; e.g. "Inadvertent Overdraft Policy" or any other label that conveys the same thought. An "overdraft protection program" does not protect the consumer from overdrafts.

• Fairly represent overdraft protection programs and alternatives. When informing consumers about an overdraft protection program, inform consumers generally of other available overdraft services or credit products, explain to consumers the costs and advantages of various alternatives to the overdraft protection program, and identify for consumers the risks and problems in relying on the program and the consequences of abuse.

Not all banks have alternative offerings and not all consumers would qualify for them at those banks that do. For example, a bank may have the ability to tie a credit card or a home equity line of credit to a consumer's checking account to cover inadvertent overdrafts. However, it may not offer an unsecured line of credit to consumers for the same purpose. Banks should be encouraged to discuss only those alternatives that they offer, not those that are available on a theoretical basis. In this context, it should be made clear that "available" means available at this institution.

For lack of a better place to mention it, it is highly likely that consumers who have a small line of credit as protection against NSF check would borrow up the amount of the line, but not pay it off. It would become an "evergreen" loan. Whatever the drawbacks of the ODP, it clearly communicates the concept that it is short term borrowing. (I only have one credit card, an American Express. It must be paid in full at the end of every month. Therefore, I have enforced discipline that does not allow me to accumulate credit card debt.) We do not do people any favors by granting open end credit which becomes part of their long term financial picture.

• Train staff to explain program features and other choices. Train customer service or consumer complaint processing staff to explain their overdraft protection program's features, costs, and terms, including how to opt out of the service. Staff also should be able to explain other available overdraft products offered by the institution and how consumers may qualify for them.

This bullet largely reiterates the preceding bullet, but does a better job of focusing on available products offered by the institution. The emphasis on the consumer's ability to "opt-out" of the program is senseless, but is better addressed in a later comment.

• Clearly explain discretionary nature of program. If the overdraft payment is discretionary, describe the circumstances in which the institution would refuse to pay an overdraft or otherwise suspend the overdraft protection program. Furthermore, if payment of overdrafts is discretionary, information provided to consumers should not contain any representations that would lead a consumer to expect that the payment of overdrafts is guaranteed or assured.

In the event of a dispute in connection with a returned check, a bank's description of the circumstances in which it would refuse to pay an overdraft or otherwise suspend the overdraft protection program will be argued to create a contractual commitment to pay an NSF debit in all other circumstances. If the assumption that the any NSF debit is the result of inadvertence is maintained, there is no reason to discuss why the item might not be paid. <u>No matter what else happens, the primary reason it will not be paid is because there was not enough money in the bank to pay it.</u> The portion of the bullet suggesting banks should describe the circumstances under which a check will not be paid should be deleted.

Clearly, inclusion of representations that would lead a consumer to expect that payment of NSF items is guaranteed or assured would be misleading advertising and violate Regulation DD. Perhaps, worse yet, it would reflect a commitment to loan money and trigger the application of Regulation Z. If the revision of Regulation DD would render this inaccurate advertising and a violation of that regulation, there is no point in mentioning it as an undesirable practice.

• Distinguish overdraft protection services from "free" account features. Avoid promoting "free" accounts and overdraft protection services in the same advertisement in a manner that suggests the overdraft protection service is free of charges.

Accounts which can legally be described as "free" under Regulation DD can still have any number of fees in connection with specific services. Regulation DD also has restrictions which prohibit misleading advertising. Avoiding advertisements that suggest the ODP is "free" is already required by law and is appropriate here. However, a suggestion that "free" accounts and ODPs should not be mentioned in the same advertisement is baseless. That statement should be deleted.

• Clearly disclose program fee amounts. Marketing materials and information provided to consumers that mention overdraft protection programs should clearly disclose the dollar amount of the overdraft protection fees for each overdraft and any interest rate or other fees that may apply. For example, rather than merely stating that the institution's standard NSF fee will apply, institutions should restate the dollar amount of any applicable fees in the overdraft protection program literature or other communication that discloses the program's availability.

Since it was created by the same design firm, it should be presumed that Regulation DD currently provides consumers with adequate information. Consumers are told the specific amount of the NSF fee in writing, in a form they can keep, at account inception. If it is subsequently changed, consumers are told of the change 30 days in advance, in writing, in a form they can keep. Any NSF fee that was actually imposed appeared on the consumer's periodic statement. Any interest rate that might apply would presumably be subject to advance disclosure under Regulation Z. While there is every reason to make certain that consumers understand that fees will apply and the circumstances under which they are imposed, an ODP disclosure that reflects current fees will cause banks to replicate needless printing expenses when fees change.

• Clarify that fees count against overdraft protection program limit. Consumers should be alerted that the fees charged for covering overdrafts, as well as the amount of the overdraft item, will be subtracted from any overdraft protection limit disclosed, if applicable.

No comment.

• Demonstrate when multiple fees will be charged. Clearly disclose, where applicable, that more than one overdraft protection program fee may be charged against the account per day, depending on the number of checks presented on and other withdrawals made from the consumer's account.

No comment.

• Explain check clearing policies. Clearly disclose to consumers the order in which the institution pays checks or processes other transactions (e.g., transactions at the ATM or point-of-sale terminal).

The phrase "check clearing policies" does not indicate that an ODP can incorporate EFTs as these guidelines elsewhere indicate is advisable. More importantly, it is not the correct term for describing the sequence in which competing items are paid. The circumstance addressed here is generally referred to as "order of payment." I suggest that the latter phrase be used in any future discussions in order to better facilitate industry understanding based on terms currently in use. Following is a sample of such a disclosure:

"We process checks and other debit items to your account in the following order: Web Banking transfers, Web banking bill payments and wire transfers, service charges, ATM withdrawals, ACH withdrawals and Empower PC Banking bill payments, scheduled loan payments and transfers, point of sale (POS) transactions, Visa Checkcard purchases, checks drawn on your account used at our bank (in serial number order), and checks drawn on your account processed by another financial institution (in serial number order). We reserve the right to change this order of processing at any time without prior notice to you."

The above sample was posted on a commercial web site, Bankersonline.com during a discussion of the pros and cons of voluntarily disclosing payment order. It is believed to be from an actual bank. It is among the most well written and all encompassing I have seen. Yet, if it were provided to a consumer at account inception, it would, far more likely than not, be incomprehensible.

Assuming any debit against funds not on deposit is accidental, this disclosure has no meaning at account inception; i.e. it will not help the consumer make a choice between financial institutions. On the other hand, if a consumer later knowingly authorizes debits for which there are insufficient funds to pay, the disclosure will still be of little value – the consumer would have to know the date the NSF item would be presented and what other items will be presented on that day in order to predict which of the NSF debits he is issuing will be paid.

The disclosure's only true value is to provide the consumer with an "after-the-fact" road map to follow to see if the bank has failed to adhere to the disclosure. If it paid an item instead of the one the disclosure indicated would be paid, the consumer will argue that the disclosure reflected a contractual commitment and the bank has "wrongfully dishonored" the returned item. The disclosure is both the bullet and the gun; if it does not provide the disclosure, the bank does not have a problem.

Also, please note the pattern the sample disclosure reflects; it will be adopted by all banks. Any bank will pay the items on which it is already liable first and it will pay items processed through another financial institution (checks) last. EFT items are routinely paid before checks arriving via cash letters are paid. As the number of checks processed in the United States is declining each year, a disclosure focusing on the order in which the items with the lowest possible payment priority are paid seems to be out of step.

Finally, the law governing payment of checks is the Uniform Commercial Code (UCC). Overdrafts are specifically addressed at 4-303(b) in the model version of the UCC. The Official Commentary to this portion of the UCC is brutally objective:

7. As between one item and another no priority rule is stated. This is justified because of ***the impossibility of stating a rule that would be fair in all cases****, having in mind the almost infinite number of combinations of large and small checks in relation to the available balance on hand in the drawer's account; the possible methods of receipt; and other variables.* ***Further, the drawer has drawn all the checks. The drawer should have funds available to meet all of them and has no basis for urging that one should be paid before another…*** *(emphasis supplied)*

The Official Commentary, authored by scholars and legal practitioners who have worked with the UCC for decades, notes the impossibility of establishing any payment order that would be fair in all cases. A long line of court cases supports the concept that the bank should be able to pay items presented in any order. (Those seeking verification need spend only 10 minutes reviewing the relevant section of "Brady on Bank Checks.") Those who would stipulate a disclosure regarding the order of payment expect banks to draw on a source of wisdom untapped by the authors of the UCC and state court judges.

This is an absolutely worthless disclosure that creates several issues and resolves none. It should only be expected that they do it in New York and California.

• Illustrate the type of transactions covered. Clearly disclose that overdraft protection fees may be imposed in connection with transactions such as ATM withdrawals, debit card

transactions, preauthorized automatic debits, telephone initiated transfers or other electronic transfers, if applicable. If institutions' overdraft protection programs cover transactions other than check transactions, institutions should avoid language in marketing and other materials provided to consumers implying that check transactions are the only transactions covered.

There is no evidence of a general assumption by consumers that ODP provisions only apply to check payments. Electronic payments make up an increasingly large portion of the retail payment system and it is reasonable to assume that consumers know a $254 EFT will overdraw their account by exactly the same amount as a $254 check and that, if the money is not there to pay it the bank may return either item. This bullet is apparently spawned by the ODP promotional materials provided by a single vendor. Vendors should not drive this initiative in either the practical or the legal sense. This bullet should be deleted.

• **Provide election or opt-out of service. Obtain affirmative consent of consumers to receive overdraft protection. Alternatively, where overdraft protection is automatically provided, permit consumers to "opt out" of the overdraft program and provide a clear consumer disclosure of this option.**

If the consumer does <u>not</u> opt-out, an NSF debit will be paid if it is within the program's boundaries. However, if the consumer does opt-out, that same debit will be returned unpaid. In both circumstances, the bank will impose an NSF fee.

Return of the item will undoubtedly cause collateral financial and reputational harm to the consumer. That same item may be sent through the clearing system a second time and even a third time if it has been converted to an RCK entry under the ACH rules. Thus, it may generate two more NSF fees with no hope of payment if the funds are not there.

Whenever a consumer opts-out, the inescapable conclusion has to be that the consumer does not understand the service. Opting out is simply a ridiculous choice – one the consumer will say was not adequately explained when the results finally become clear. I suggest that this bullet be deleted and that all emphasis on opt outs be removed from any guidance offered.

If this provision is to be retained, I suggest that it be expanded to indicate that the practical effect of an opt out is that all debits presented against insufficient funds will be returned unpaid and the consumer may incur merchant charges, interruption of services and damages to his reputation in addition to other consequential damages. Hopefully, this disclosure will protect the consumer from making a decidedly foolish decision.

• **Alert consumers before a non-check transaction triggers any fees. When consumers attempt to use means other than checks to withdraw or transfer funds made available through an overdraft protection program, provide a specific consumer notice, where feasible, that completing the withdrawal will trigger the overdraft protection fees. This notice should be presented in a manner that permits consumers to cancel the attempted withdrawal or transfer after receiving the notice. If this is not possible, then post notices on proprietary ATMs explaining that withdrawals in excess of the actual balance will access**

the overdraft protection program and trigger fees for consumers who have overdraft protection services. Institutions may make access to the overdraft protection program unavailable through means other than check transactions.

Again, following the concept that any ODP should address only inadvertent withdrawals, I do not believe that it should be accessible by an ATM or an equivalent method. Accordingly, I do not think the notices are necessary.

If a decision is made not to criticize overdrafts via ATM, then I think the notice should be explicit and appear on the screen, something to the effect: "The proposed transaction will overdraw your account. If your institution has approved such activity, it may impose its fee for "insufficient funds" which was disclosed to you earlier. Do you wish to continue?" If the consumer is entitled to actual notice of a $2.00 charge for using a foreign ATM, he should be entitled to notice that a $28 NSF fee is going to be imposed for this $50 withdrawal.

• Prominently distinguish actual balances from overdraft protection funds availability. When disclosing an account balance by any means, the disclosure should represent the consumer's own funds available without the overdraft protection funds included. If more than one balance is provided, separately (and prominently) identify the balance without the inclusion of overdraft protection.

I absolutely agree; the undifferentiated inclusion of the overdraft protection funds in the balance is blatantly misleading. However, the agencies need to be more specific in indicating whether those funds should be included in response to callers if a bank offers check verification services. For example, in a manual environment, if Wal-Mart calls and wants to know if Ms. Jones check for $437 is good, what should the bank say if there is $114 in the account, but the bank's ODP indicates Ms. Jones is eligible for a $500 overdraft?

• Promptly notify consumers of overdraft protection program usage each time used. Promptly notify consumers when overdraft protection has been accessed, for example, by sending a notice to consumers the day the overdraft protection program has been accessed. The notification should identify the transaction, and disclose the overdraft amount, any fees associated with the overdraft, the amount of time consumers have to return their accounts to a positive balance, and the consequences of not returning the account to a positive balance within the given timeframe. Institutions should also consider reiterating the terms of the overdraft protection service when the consumer accesses the service for the first time. Where feasible, notify consumers in advance if the institution plans to terminate or suspend the consumer's access to the service.

Aside from the suggestion to re-disclose the terms of the ODP on its first use, I agree and note that most banks still send NSF notices. All this requires is additional verbiage which could be pre-printed on the notice.

I suggest that the content of the notice should be expanded to reflect the fact that payment of a series of overdrafts does not constitute a course of dealing; i.e. that the bank is not obligated to pay future NSF items just because it paid this one. There is ample judicial precedent to indicate that consumers have filed many suits using such an argument. The court's decision would be rendered based on state law, not federal law; federal "Best Practices" would be meaningless. Such a disclosure would help protect the consumer from over reliance and the bank from frivolous law suits.

Triggering a first use notification with expanded terms would be difficult and serve no real purpose. The standard notice suggested above certainly contains more than enough information and I suggest reference to the first use notification be deleted.

Providing consumers with advance notice of termination or suspension is theoretically desirable, but is a practical impossibility. The bank cannot know when the consumer plans to write his next NSF check and be expected to act prior to then. Moreover, a decision to terminate or suspend ODP will probably be made based on the presentment of a specific NSF item, not a decision to pay the current NSF item, but to refuse to pay the next one. The notice that the item is being returned constitutes constructive notice of termination. Providing advance notice of termination would be consistent with a line of credit and be the equivalent of adverse action in connection with a loan; it is inconsistent with this product or service. A suggestion that notice should be provided to the customer within a reasonable time after suspension or termination would be workable.

• **Consider daily limits. Consider limiting the number of overdrafts or the dollar amount of fees that will be charged against any one account each day while continuing to provide coverage for all overdrafts up to the overdraft limit.**

With the operative word being "consider," I agree. However, it should be noted that returning checks unpaid involves more time and handling than paying checks. Banks would be more inclined to agree to a daily cap under circumstances where the items are not being re-handled. There is no reason why banks should cap daily NSF fees when a number of items are being returned.

• **Monitor overdraft protection program usage. Monitor excessive consumer usage, which may indicate a need for alternative credit arrangements or other services, and should inform consumers of these available options.**

The lack of a parallel requirement to monitor consumer borrowings with any other type of credit makes this illogical and more than a little paternalistic. Writing NSF checks at $28 or more a pop is a ridiculous way to borrow money. However, so is buying a new car every two years if you are paying off a four year installment loan that was based on precomputed interest. Yet, there is no "best practice" that indicates banks should enter into financial counseling sessions when consumers are making decisions that waste their own money. This bullet should be deleted. Some consumers might actually suggest that, as long as the fees are paid, it's really none of the bank's business. I would tend to agree.

• **Fairly report program usage. Institutions should not report negative information to consumer reporting agencies when the overdrafts are paid under the terms of overdraft**

protections programs that have been promoted by the institutions.

This bullet can be read two different ways and needs to be clarified. One is fair. The other is nonsensical.

If the suggestion is that consumers who have adhered to the terms of the ODP and repaid amounts due according to its terms, then it is obvious that it would be inappropriate to attach any negative connotation to those overdrafts by reporting them to a negative data base.

However, if the meaning is that, because the bank offered an ODP, negative consumer information should not be reported, that makes no sense. The popular phrase from a 1970's television show, "Laugh-In," was "The Devil made me do it!" not "The bank made me do it!"

Daily Fees on Overdrawn Accounts

The omission of any comment on the practice of imposing periodic fees on overdrawn accounts is a surprise. While such an observation might not be expected from someone in my business, this omission is also a personal disappointment to me. If the underlying concept is that debits issued against unavailable funds are due to an oversight on the part of the consumer, payment of those debits is clearly a service. However, once the account is overdrawn, a fee imposed for each day the account remains overdrawn does not relate to the provision of additional services.

Daily fees are only justified by the time value of money; i.e. they are the equivalent of interest; they should be subject to state usury laws and disclosure under the Truth-in-Lending Act.

The most logical response would be for the Federal Trade Commission to make the periodic fee an unfair and deceptive practice analogous to pyramiding late charges.

Pay Off Agreements

I do not understand why these guidelines do not address the issue of pay off arrangements even though they are raised in the supplementary information which accompanies them. It would seem more empathetic with the concept of consumer protection to make suggestions about what actions banks could comfortably implement in this area rather than to wait and attempt to afford protections after the fact. In any case, it is critical to note that an overdraft is already an enforceable legal obligation. (The supplementary information clearly notes the overdraft is shown as a loan on the bank's official reports.) Replacing the overdraft with a note is the simple creation of the memorial of a debt rather than the creation of a debt or an extension of credit.

ATM and Over the Counter Withdrawals Against ODPs

The omission of any comment on the practice of allowing what are clearly intentional draws against a line of credit is a surprise to me. As noted previously, I do not think this should be allowed unless the supporting extension of credit is governed by Regulation Z. At a minimum, the consumer should be entitled to actual notice that the fee will be imposed prior to consummating the transaction.

In candor, I think this and the two preceding elements are the most systematically egregious features of some ODP's. They were the three most persuasive points in the argument that ODPs should be regulated under the Truth-in-Lending Act. Yet, the regulatory initiatives do not mention any of them. Many banks and even some ODP vendors have exercised self restraint and avoided these tactics. <u>You have to know that if any "Best Practices" guidance fails to criticize these practices, it will be read as condoning them; i.e. more banks will adopt them.</u>

Is the Fed saving ammunition for a second assault which will use Regulation Z as the weapon of choice? The preface to the Regulation DD proposal promises reconsideration "… if concerns about these overdraft programs persist in the future." As noted, failing to address these issues assures these problems will not only persist, they will grow with the agencies' imprimatur of disinterest.

ODP Programs for Businesses

Any guidance offered for ODPs should make it plain that banks cannot offer such programs to business customers without additional analysis and adaptation. For example, corporations, partnerships, and LLCs borrow money by resolutions that empower specific individuals to commit the entity to specific borrowings. It is not "automatic" that the person who signs on an entity's checking account has the power to borrow money on the entity's behalf. No amount of language in a signature card is going to change that. Banks that just transfer this activity to commercial accounts will find larger issues to deal with.

Effect of Proposed Changes to Regulation DD

I do not understand why some elements of the proposed guidelines clearly overlap the proposed changes to Regulation DD unless it is to establish a "fall back" position in case those changes are not made to the regulation, but are still thought to be important by the agencies. In order to be able to comment on the guidelines effectively, I have avoided any attempt to reconcile the two initiatives. However, when both documents are issued in final form I hope any overlap will be eliminated from the guidelines; i.e. nothing good can come from an attempt to reiterate a requirement clearly spelled out in a regulation.

Conclusion

I understand full well the implications of the fact that several agencies are involved in this initiative and those agencies do not always agree within, let alone with one another. The difficulty is compounded by the fact that there is no statutory guidance to follow. Nevertheless, consumers and the banking industry will both be better served if the proponents can agree that protecting the consumer, not countering the vendors is the