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March 27, 2009

VIA ELECTRONIC MAIL
Ms. Jennifer J. Johnson
Secretary
Board of Governors of the
Federal Reserve System
20th Street and Constitution Avenue, NW
Washington, DC 20551

Re: Regulation E; Docket No. R-1343

Dear Ms. Johnson:

NACHA – The Electronic Payments Association[1] appreciates this opportunity to respond to the Request for Comment issued by the Federal Reserve Board ("Board") regarding proposed amendments to Regulation E and its Official Staff Commentary addressing overdraft services provided by financial institutions ("Proposal"). Our response is confined to matters in the Proposal and specific questions of the Board that directly or indirectly involve ACH transactions or the ACH Network, including the role of financial institutions, businesses, consumers, processors and solution providers as Network stakeholders.

NACHA strongly supports the Board's well-defined rationale for excluding from coverage ACH transactions (as well as check and recurring debit card transactions) that give rise to an overdraft for the following reasons: (1) consumers have a strong interest in ensuring their bills (including mortgage, utility, or insurance payments) and other transactions are paid, and (2) when these bills are not paid, consumers could incur NSF fees from both the biller and the financial institution, and possibly negative credit reporting and loss of services for non-payment. For these reasons, this exclusion is a significant improvement over the scope of overdraft service amendments to Regulation DD[2] proposed in May 2008 (and superseded by this Proposal) that would have covered all transactions debiting a consumer account, including ACH transactions and checks. In addition, because checks are specifically excluded from coverage by Regulation E,[3] excluding ACH transactions from coverage in the final rule will prevent consumer confusion and disparate

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[1] NACHA is a not-for-profit association representing more than 15,000 financial institutions and a network of regional payments associations through direct membership, and 650 organizations through its industry councils. NACHA develops operating rules and business practices for the Automated Clearing House (ACH) Network and for electronic payments in the areas of Internet commerce, electronic bill and invoice presentment and payment (EBPP, EIPP), e-checks, financial electronic data interchange (EDI), international payments, and electronic benefits services (EBS).
[2] 73 FR 28904, May 19, 2008.
[3] Unlike ACH transactions, checks are specifically excluded from coverage by Regulation E and the *Electronic Fund Transfer Act*. The Board's rationale for excluding both check and ACH transactions cites the same fundamental consumer interests and practical implications as justification. NACHA concurs that the underlying features of both forms of payment in the context of this Proposal are comparable.

protection when a check is used to initiate an ACH payment, as is the case with check conversion applications. Finally, as discussed below, we believe the Board's proposed "opt-out" approach is substantially preferable to the "opt-in" approach for practical reasons.

Proposal summary: The Board proposes to define "overdraft service" to mean a service (subject to certain exceptions, e.g., overdrafts pursuant to a line of credit) under which a financial institution assesses a fee or charge to a consumer's account for paying a transaction, including a check or other item, when the consumer has insufficient or unavailable funds in the account.[4]

> Opt-Out vs. Opt-In Approach: The Board proposes two distinct alternatives to meet its policy objectives of assisting consumers in understanding how overdraft services operate and ensuring consumers have the opportunity to limit overdraft costs associated with ATM withdrawals and one-time debit card transactions. The first alternative would prohibit a financial institution from assessing an overdraft fee on such transactions (subject to certain exceptions) unless the consumer has been given the opportunity to opt out of the service ("opt-out alternative"). The second alternative would generally prohibit a financial institution from assessing an overdraft fee, subject to certain exceptions, for such transactions unless the consumer has specifically opted into the service ("opt-in alternative").
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> Covered Transactions: The Board specifically proposes to limit the types of transactions for both alternatives to ATM withdrawals and one-time debit card transactions that result in an overdraft ("covered transactions"), and specifically excludes ACH transactions, recurring debit card transactions/pre-authorized EFTs, and checks. As proposed, a consumer that has ACH debit transactions could benefit from overdraft services if provided by the financial institution, regardless of whether the accountholder had opted-out of such services (or, depending on the approach adopted by the Board, not opted in). However, the Board explicitly seeks public comment as to whether this proposed scope of covered transactions should be expanded to include ACH and/or recurring debit card transactions.
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> Implementation Timeframe: Finally, the Board seeks public comment on the implementation timeframe for the proposed rule.

NACHA's Response: The rationale for excluding ACH transactions from either alternative is sound. ACH transactions include recurring payments associated with an existing relationship and a standing payment authorization (e.g., monthly bill payments), and non-recurring payments in which each ACH transaction is tied to a specific authorization (e.g., some Internet-initiated transactions and check conversion transactions). Regulation E and the *NACHA Operating Rules* impose specific consumer protections, disclosure, and authorization requirements for ACH transactions that apply to financial institutions and merchants/billers.

The ACH Network is not a real-time network, but instead is a batch processing network. Once a payment has been initiated, the consumer has no way of canceling the transaction if there are insufficient funds in their account in order to avoid an overdraft fee. The payment would post and, even if the ACH transaction were returned unpaid, the consumer would likely be assessed a fee. Consequently, as the Board rightly notes in the Proposal, there are benefits to overdraft services when an ACH transaction to a consumer's account would result in an overdraft or return. This is

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[4] Proposed Section 205.17(a).

especially true in the case of recurring debits where consumers and billers have an ongoing relationship, such as mortgage, utility, or insurance payments. Consumers have a strong interest in ensuring that these types of payments are not returned unpaid. For both recurring and single-entry ACH debit transactions, when overdraft services are in place, the transaction is paid, the consumer's obligation to the merchant or biller is fulfilled, and NSF fees from the merchant or biller are avoided. Alternatively, if no overdraft services are in place, the transaction is returned unpaid, typically subjecting the consumer to NSF fees from both the financial institution and the merchant or biller without fulfilling the payment obligation. Weighing these alternatives, both the consumer and the biller are typically in a better position when the transaction is paid. Based on this rationale, the disadvantages to consumers of including ACH debit entries as covered transactions in any final rule exceed any benefits to consumers.

A. Discussion of Proposed Changes

As stated previously, we do not believe that it serves consumers well to extend the scope of the rule to include ACH debit entries as covered transactions. Whether the Board ultimately chooses to pursue an opt-out or opt-in approach, the practical implications to the ACH Network are effectively the same, as long as ACH transactions are excluded. Regardless, NACHA believes the opt-out approach is a substantially better and more practical approach since it allows consumers the best opportunity to ensure their mortgage and other bills are paid.

> 1A. Impact of the Opt-Out or Opt-In Approach on Overdraft Services Generally: Both alternatives would require a financial institution to apply the same criteria for deciding whether to pay checks, ACH and other types of transactions regardless of the consumer's opt-out (or opt-in) choice with respect to ATM and one-time debit card transactions. For example, if the institution's criteria would lead the institution to pay a check or ACH debit overdraft (and assess a fee) if the consumer had *not* opted out of the institution's overdraft service, it would *also* have to apply the same criteria in determining whether to pay the overdraft if the consumer *had* opted out for ATM and one-time debit card transactions. In this scenario, the status of an opt-out on a particular consumer account for such transactions would have no material impact on an institution's decision to pay, or not pay, overdrafts to that account from non-covered transactions and a common, consistent policy could be applied to all consumer accounts for non-covered transactions.
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> 1B. Conditioning the Opt-Out or Opt-In Approach: The Board specifically seeks comment as to whether institutions should be expressly permitted to condition the consumer's ability to opt out of overdraft services for ATM and one-time debit card transactions on the consumer also opting out of the institution's overdraft services for non-covered transactions. In this alternative scenario, an institution could make opting out of overdraft services a blanket policy across all transaction types – i.e., a consumer that opts out of overdraft services for ATM and one-time debit card transactions would also be opting out of overdraft services for checks, ACH transactions and other non-covered transactions.[5]

NACHA's Response: NACHA supports financial institutions having flexibility under the rule to structure their overdraft services in a way that is best suited to their operational and customers' needs. Allowing institutions to condition the consumer's ability to opt out of the institution's

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[5] Proposed Section 205.17(b)(2).

overdraft services could benefit those institutions that do not (or are unable to) distinguish between payment types in their posting and overdraft payment operations. This reflects the difficulties financial institutions may face in daily operations of distinguishing between transaction types in the process of posting to consumer accounts, and further determining the opt-out or opt-in status of a particular account when there are insufficient funds to pay the transaction.

In the event institutions are permitted to condition the consumer's ability to opt out (again, the preferred approach) of overdraft services for ATM and one-time debit card transactions on the consumer also opting out of the institution's overdraft services for non-covered transactions, NACHA believes that consumers opting out (or failing to opt in to) are best served if they are educated as to the implications for their recurring bill payments. For example, a consumer opting out (or not opting in) may later inadvertently make an error and, without the benefit of overdraft services, have a recurring transaction (such as their mortgage payment) returned unpaid and incur NSF fees from both the financial institution and the biller.

> 2. Implementation Timeframe: The Board recognizes the likelihood that implementing the provisions contemplated by the Proposal will require a long implementation period and specifically seeks comment as to what period would be sufficient.

NACHA Response: Provided ACH transactions remain outside the scope of covered transactions in any final rule, NACHA is not in a position to comment on what would constitute an appropriate lead time for implementation. If, however, either approach is adopted that includes ACH transactions as covered transactions, NACHA believes the resulting impact on financial institutions across a broader operational base would compound implementation complexities, possibly necessitating a longer implementation period. If sufficient implementation time is not allowed, financial institutions' ability to effectively comply by the deadline could be compromised, and implementation costs associated with systems implementation and integration, testing, employee training and ensuring operational integrity will be increased. For these reasons, a minimum implementation period of eighteen months would seem necessary.

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If NACHA can be of further assistance to the Board as it evaluates this Proposal, please do not hesitate to contact me at (703) 561-3929, or by e-mail at: **NACHA-government-rel@NACHA.org**.

Sincerely,

Ian W. Macoy, AAP
Managing Director, Network Strategy and Outreach