

NEIGHBORHOOD ECONOMIC DEVELOPMENT ADVOCACY PROJECT (NEDAP)
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March 30, 2009

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

Re: Federal Reserve Board: Docket No. R-1343

Dear Ms. Johnson:

Thank you for the opportunity to comment on the proposed regulatory changes to protect consumers from unfair and deceptive practices with respect to overdraft protection. We applaud the Federal Reserve Board's efforts to curb these abusive practices and to provide transparency and choice to consumers.

We strongly urge the Board to establish an opt-in rule for overdraft services, requiring affirmative consent from consumers before a financial institution may assess fees for paying overdrafts. The Board's proposal to apply this rule to overdrafts incurred through ATM and debit card transactions would address the most egregious overdraft abuses by financial institutions. We strongly urge that the opt-in rule be applied to existing, as well as new, accounts, as provided under proposed § 205.17(g), to ensure equity for all consumers.

The Neighborhood Economic Development Advocacy Project (NEDAP) is a resource and advocacy organization, based in New York City. NEDAP's mission is to promote community economic justice, and to eliminate discriminatory economic practices that harm communities and perpetuate inequality and poverty. Founded in 1995, NEDAP employs multiple strategies – including community outreach and education, advocacy, policy research and analysis, and direct legal services – to ensure that communities have access to fair and affordable credit and financial services, and to address inequities in the financial services system. NEDAP's founder and co-director, Sarah Ludwig, recently completed a three-year term on the Federal Reserve Board's Consumer Advisory Council.

NEDAP has been dismayed by the proliferation in recent years of "courtesy" overdraft services, which cause immense confusion and financial hardship for low and moderate income people, in particular. Unlike traditional forms of overdraft protection – such as lines of credit or transfers from linked savings accounts – automated overdraft services are distinguished by several predatory features: they are provided without customers' consent or even awareness; they are applied unevenly, on a transaction-by-transaction basis; they are exorbitantly priced; and they actively encourage people to overdraw their accounts, as overdraft coverage amounts are typically included as part of customers' account balances.

Automated overdraft services are a financial landmine for people new to the banking system or living on limited means. It is not uncommon for someone to pay hundreds of dollars in fees for overdrafts as small as \$5 or \$10. The Center for Responsible Lending has estimated that financial institutions reap \$17.5 billion in abusive overdraft fees each year, for \$15.8 billion extended in overdraft coverage. In cases where people are unable to repay automated overdraft fees, financial institutions typically close their accounts and report them to ChexSystems or TeleCheck – effectively barring these consumers from opening new accounts and relegating them to check cashers and other fringe services. In light of the pervasiveness of these overdraft services, and the hardship they have caused so many people, groups like ours are increasingly hard-pressed to recommend categorically that people open bank accounts.

Through its Consumer Law Project, NEDAP provides legal representation, advice and referrals to thousands of lower income NYC residents each year. We include here just one client's story, which illustrates the abusive nature of automated overdraft services.

Mr. A. is deaf and functionally illiterate. His only income is \$666 he receives in monthly Supplemental Security Income (SSI). Before his troubles with overdraft protection began, he followed a regular pattern of withdrawing his money from his account. On the first day of the month, when his SSI benefits were directly deposited, Mr. A. would typically withdraw several hundred dollars to pay his rent and bills. Over the next week he would make additional ATM withdrawals and pay a monthly bill for Internet service.

Mr. A. opened his account with a federal savings bank in the early 1990s and had no problems until around May 2005, when he unknowingly overdrew his account by \$3.44 and triggered bounce protection fees that led him into a spiral of continued overdrafts. Mr. A. did not understand what was going on. Following his regular pattern of withdrawing cash and paying bills, he unknowingly continued to overdraw on the account as mounting overdraft protection fees dug him deeper into debt. The bank paid each overdraft, charging \$30 for each one, including several electronic debits that amounted to less than \$8 each.

At the beginning of each month, Mr. A. continued to think he had \$666 to pay his rent and cover his basic expenses. In fact, he had far less in his account, because the bank repeatedly set off the previous month's overdrafts and fees. Six months after his first overdraft, the bank closed Mr. A's account for failure to maintain a positive balance. Mr. A.'s account contained only his SSI benefits, which are statutorily protected and should not have been debited from his account to set off the overdraft loan charges.

The country is in the midst of rising unemployment and foreclosures, mega-bank mergers and taxpayer-funded bank bailouts. More than ever, strong regulation is needed to ensure that predatory financial products and exploitative "gotcha" fees do not siphon people's vital income, and that financial institutions are held to high standards of transparency and accountability.

NEDAP urges the Board to adopt the following recommendations in its final rule:

- ***Establish an opt-in rule for all accounts. The Board should not adopt a hybrid rule that requires new customers to opt-in, but existing customers to opt-out, of overdraft services.*** Existing customers subject to automated overdraft fees should not be penalized for having opened their accounts prior to the issuance of the final rule. By applying the opt-in rule to all accounts, the Board will ensure equal opportunity for all bank customers and credit union members to affirmatively select, or reject, this controversial service.
- ***Prohibit banks from conditioning payment of ACH and check overdrafts on the consumer also opting-in to overdraft services for debit and ATM transactions.*** Unlike overdraft services for debit and ATM transactions, people generally derive benefit from a bank's coverage of ACH and check overdrafts. Allowing banks to adopt an "all-or-nothing" policy on overdraft coverage would undermine the Board's goal to provide consumers with meaningful choice. Banks would undoubtedly adopt such a policy to compel customers to opting-in to full automated overdraft services.
- ***Require banks to provide someone who does not opt-in to overdraft services an account with equal terms, conditions and features as it provides to someone who does opt-in.*** Banks should not be allowed to provide inferior or costlier accounts to customers who have declined to opt-in to overdraft services. Allowing banks to do so would, again, provide them with a tool to effectively compel customers to opt-in to overdraft services.
- ***Regulate overdraft services as extensions of credit.*** Like other commentators, NEDAP argues that automated overdraft services are, in fact, extensions of credit and should be subject to disclosure requirements of the Truth in Lending Act. It is imperative that if people are given the choice to opt-in to overdraft services, they also be provided a way to meaningfully measure and compare the costs – for example, through the Annual Percentage Rate (APR).
- ***Require financial institutions to notify customers, in opt-in notices and otherwise, about the full range of overdraft protection services offered.*** Alternatives to automated overdraft services include overdraft lines of credit (regulated under the Truth in Lending Act) and transfers between linked accounts. These alternatives cost significantly less than automated overdraft services and provide more reliable and consistent protection.
- ***Prohibit overdraft fees incurred as a result of debit holds.*** Most people who make purchases with their debit cards are unaware that some merchants place large holds on their accounts, lasting hours or even several days. Financial institutions should be prohibited from charging fees on overdrafts incurred as a result of debit holds – regardless of whether someone has opted in to overdraft services – as these are beyond the control of the account holder.

Abusive overdraft services have taken a huge toll on citizens of New York City and State, and throughout the country. The Federal Reserve Board has an important opportunity to issue strong and effective rules that will curb these abuses, and protect American consumers. We commend the Board for examining the issues addressed in its proposed rule, and we thank you for your consideration of our comments.

Sincerely,

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