LAW OFFICES OF MICHAEL A. BRODSKY
115 FAIR AVENUE
SANTA CRUZ, CA 95060
VOICE 415-861-2779
FACSIMILE 831-471-9705

August 6, 2004

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

Re: Docket R-1197
Proposed Revisions Rule DD
12 CFR Part 230
Bounce Protection
Docket OP-1198
Proposed Interagency Guidance
Bounce Protection

Dear Ms. Johnson:

These comments are submitted on behalf of the Greenling Institute ("Greenlining"). Greenlining has long worked with the Federal Reserve Board of Governors ("Board") in carrying out our mission: to empower communities of color and other disadvantaged groups through multi-ethnic economic and leadership development, civil rights, and anti-redlining activities. Because bounce loans (sometimes referred to as "bounce protection" or "overdraft protection") often constitute an illegal overcharge for financial services and are marketed to and disproportionately impact low-income and minority communities, we include bounce loans among the redlining practices that we oppose. See N.Y. Times, June 8, 2004 at C3 (reporting that bounce loan fees are "paid disproportionately by low and moderate income people," and that banks maximize income by targeting "downmarket" consumers with bounce loans); see also N.Y. Times, June 12, 2003 at A12 (reporting that through bounce loans "some 1500 financial institutions prey on mostly low-income customers"); Newsweek, July 12, 2004 at 68 (reporting on "expensive bounce protection plans for low-income customers").

Greenlining presents below a number of legal arguments that of necessity canvas a complicated and interwoven scheme of federal statutes, regulations, staff interpretations, and proposed regulations and guidance documents. Because the Board is engaged in an informal rulemaking process governed by the Administrative Procedure Act, 5 U.S.C. § 553, our analysis also incorporates principles of administrative law antecedent to all federal rulemaking authority.

We wish to stress however, that our fundamental point is a simple one: bounce loans are high-cost extensions of credit and should be regulated as such. We urge the Board not to adopt the proposed revisions to Regulation DD and accompanying Staff

Interpretations and Interagency Guidance, which would allow Banks to continue high-cost bounce loans, albeit with modest additional requirements for advertising. Instead, the Board should take the necessary steps to fully regulate bounce loans under Regulation Z, which would entitle low-income households to the same basic protections afforded affluent customers with traditional lines of credit attached to checking accounts.

We appreciate the opportunity to provide these comments and thank you in advance for considering our views in reaching your ultimate decision.

THE ADMINISTRATIVE RECORD ESTABLISHES THAT BOUNCE LOANS ARE EXTENSIONS OF CREDIT AND SHOULD BE REGULATED UNDER THE TRUTH IN LENDING ACT.

The Board has taken an important step in recognizing that financial institutions ("Banks") market, and consumers use, bounce loans "as an alternative to a traditional line of credit." Proposed Rule, Truth In Savings, Federal Reserve System, 12 CFR Part 230, 69 Fed. Reg. 31,760 (June 7, 2004), and that Banks encourage "consumers to overdraw their accounts and use the [bounce] service as a line of credit." Id. Not only has the Board concluded that bounce loans are a credit product, but a host of other federal agencies have reached the same conclusion. The Office of the Comptroller of the Currency, the Federal Deposit Insurance Corporation, the Office of Thrift Supervision, and the National Credit Union Administration have all unequivocally concluded that bounce loans are a "credit service," that is "offered to transaction account customers." Notice of Proposed Interagency Guidance on Overdraft Protection Programs, 69 Fed. Reg. 31,858, 31,859 (June 7, 2004). The Board has found that these bounce loans are often no different in actual practice than so-called "payday loans," an infamous form of exorbitantly priced short-term credit that the Board has recently clamped down on: "Some institutions have encouraged consumers specifically to use an overdraft as an advance on their next paycheck." Proposed Rule, Truth In Savings, 69 Fed. Reg. at 31,761.

Another particularly disturbing aspect of bounce loans is the deceptive practice used by some institutions when consumers make cash withdrawals from ATM machines. Upon accessing their accounts, consumers are informed via the ATM display that they have a certain amount of cash available. However, they are *not* informed that some or all of the cash available exceeds the balance in their account and in fact represents available credit (in the form of a bounce loan). When consumers request a withdrawal of "available cash" the ATM display does not inform them that they are overdrawing their account and incurring a bounce loan. The Board has found this lending practice to be used by some institutions under the guise of "bounce protection": "some institutions do not clearly inform consumers that ATM withdrawals, debit card transactions, or other electronic transfers may routinely be authorized under these overdraft services and that fees will be imposed in such cases." Id.

Greenlining applauds the Board's candid finding of facts: that banks market and consumers use bounce loans "as a line of credit." Id. at 31,760. We suggest that the Board now take the next logical step and make a "connection between the facts found and the choice made," Motor Vehicle Mfrs. Ass'n v. State Farm Mut. Auto Ins. Co., 463 U.S. 29, 43 (1983), by regulating bounce loans under the Truth In Lending Act

("TILA"), 15 U.S.C. § 1601–1667f . It is the purpose of TILA "to assure a meaningful disclosure of credit terms so that the consumer will be able to compare more readily the various credit terms available to him and avoid the uniformed use of credit." 15 U.S.C. § 1601(a). The administrative record before the Board (comments submitted in response to docket R-1136 and comments submitted in response to docket R-1197)[1] is devoid of *any* evidence refuting the Board's own conclusion that banks market and consumers use bounce loans as an extension of credit. In order to effectuate TILA's purpose of allowing consumers to compare various credit terms available, bounce loans should be disclosed and regulated just as other extensions of credit are. So too, with effectuating TILA's purpose of avoiding uniformed use of credit. It would be hard to imagine a better example of "uninformed use of credit" than the bounce loans foisted on unsuspecting consumers who unwittingly overdraw their accounts at ATM machines, or through other electronic means, because of inadequate or non-existent disclosure. Because bounce loan programs are in fact high-cost credit programs that are at best strongly predisposed to uninformed use, and at worst marketed and operated in a predatory manor, they should be regulated under TILA without delay.

The Truth In Savings Act ("TISA"), 12 U.S.C. § 4301–4313, on the other hand, does not cover extensions of credit and does not provide for regulation and disclosure that would allow consumers to make informed comparisons between bounce loans and other available short-term credit products. The Board has recognized that it may regulate bounce loans under TILA. See Proposed Rule, Truth In Savings, 69 Fed. Reg. at 31, 761 (noting that "coverage [under TILA] may be appropriate," but declining to provide coverage "at this time"). We hope that upon careful consideration the Board will conclude that regulation of bounce loans under TISA, as is currently proposed, "runs counter to the evidence before the agency," State Farm, 463 U.S. at 43, and will opt for regulation under TILA instead.

BOUNCE LOANS UNAMBIGUOUSLY FALL WITHIN TILA'S STATUTORY DEFINITION OF FINANCE CHARGE AND SHOULD BE REGULATED UNDER TILA.

Whenever "credit" is extended by a "creditor" within the meaning of those terms as established by TILA, full disclosure and regulation pursuant to the terms of TILA is required. 15 U.S.C. §1601–1667f. TILA defines credit as the right "to defer payment of debt or to incur debt and defer its payment." 15 U.S.C. § 1602(e). Bounce loans clearly fall within this definition and all relevant federal agencies have so concluded. See supra at 2. A "creditor" includes any person (including natural persons and other business

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[1] The Board's proposed action announced at 69 FR 31760 is based on "[t]he Board's study of bounced-check protection services." 69 FR 31761. The undersigned was informed by Jane Arons, Staff Attorney, Division of Consumer and Community Affairs, that the "study" consists of the Fed's review of comments received in response to Docket R-1136. If the Board receives any new technical studies or data in comments responding to Docket R-1197, or from its own research, and intends to rely on that information in formulating its final decision, Greenling requests that the Fed identify that information and where appropriate allow responses thereto. See generally Solite Corp. v. United States Envtl. Prot. Agency, 952 F.2d 473, 484 (D.C. Cir. 1991); Air Transport Ass'n v. FAA, 169 F.3d 1 (D.C. Cir. 1999).

entities) who regularly extends credit "for which the payment of a finance charge is or may be required." 15 U.S.C. § 1602(f). A "finance charge," in turn, is any charge "imposed directly or indirectly by the creditor as an incident to the extension of credit." 15 U.S.C, § 1605(a). Because bounce loan fees are finance charges within the definition of TILA, Banks regularly imposing those charges are "creditors" within the meaning of TILA and are extending "credit" that is subject to TILA regulation.

It is true that not all charges related to the extension of credit are "incident to" the extension of credit. Household Credit Services v. Pfennig, 124 S. Ct. 1741, 1748 (April 21, 2004). However, where a charge is imposed as a "direct result of an extension of credit" and cannot reasonably be characterized as anything other than "imposed for obtaining an extension of credit," it must be considered as incident to the extension of credit and is therefore a finance charge within the purview of TILA. See id at 1747 (reasoning that where charges are levied "in connection with" an extension of credit but are not a "direct result" of an extension of credit and are not "imposed for" an extension of credit, they may be classified as other than finance charges).

The Banks of course argue that bounce loan charges are imposed equally whether the check is paid or not and are thus not imposed for the extension of credit but rather for handling the check. In light of the way the Board has found that Banks and consumers function it is simply not reasonable to characterize the charges in this way. The Banks own characterization of bounce loans in their promotional literature shows that this argument is a fiction and does not reflect the true nature of the transaction:

First Federal Bank:

> Have you ever been shopping on the weekend and find a must-have item, but don't have the money in your checking account to cover your check? Have you ever had unplanned expenses between paydays? There is no need to worry! With First Federal's Powerdraft Plan, you will be covered without the embarrassment of a returned check.

First National Bank & Trust Company, Oklahoma:

> Access your Paycheck Before you have it! Sound too good to be true? Well it isn't, you can now start writing checks before you get paid without the worry of returned checks.

See Comments Docket R-1136-216, Appendix at 3. Although the Banks are careful to state in the fine print that they are not obligated to pay overdrawn checks, it is clear that Banks intend consumers to use the plans as lines of credit and to profit from consumers' repeated use of that credit. The Board solicited comments on bounce loans to determine "how 'bounce protection' service are designed and operated" in order to determine "potential coverage under regulation Z." Proposed Rule, Truth in Lending, Official Staff Commentary, 12 C.F.R. Part 226, 67 Fed. Reg. 72618, 72620 (Dec. 6, 2002). As the Board has recognized in its solicitation for comments, it is the true nature of the transaction that is determinative, not a convenient and very profitable fiction advanced by the banks in defense of their product.[2]

Based on the information submitted in response to the solicitation for comments, the Board subsequently found that despite many Banks' statements that payment of overdrafts is discretionary and disclaimer of any "legal obligation of the institution to pay any overdraft," Proposed Rule, Truth In Savings, 69 Fed. Reg. at 31,761, in actual practice Banks "promote the use of the service," id. at 31,760, and "[c]overage is automatic for consumers who meet the institution's criteria." Id. at 31,761. The administrative record establishes that bounce loan fees are not check handling charges or anything else other than fees imposed for obtaining an extension of credit.

With respect to ATM and other electronic debit transactions, there isn't even the theoretical possibility that the charge is a handling charge, rather than charge for obtaining credit. See, e.g, Indiana Dept. of Financial Institutions, Newsletter--Winter 2002 ed. (November 2002) at 3 (explaining that if the ATM bounce loan transaction is completed, the consumer is charged a fee for the service, but if the transaction is refused, the consumer "is charged nothing for making the attempt").

Because bounce loan fees are precisely charges "imposed for obtaining an extension of credit" they fall unambiguously within TILA's definition of finance charge as interpreted by the Supreme Court.

Congress unambiguously intended finance charges to be covered by TILA. 15 U.S.C. 15 U.S.C. § 1605. We hope that upon consideration the Board will agree with us and conclude that regulation of bounce loans under TISA would not "give effect to the unambiguously expressed intent of Congress," Chevron U.S.A. v Natural Resources Defense Council, 467 U.S. 837, 843 (1984), and will ultimately decide to regulate bounce loans under TILA instead. See also Comments of Hon. Paul S. Sarbanes, Ranking Member, Senate Committee on Banking, R-1197-14 (noting that Congress intended bounce loans to be regulated under TILA).

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[2] The doctrine of substance over form applies with particular force here, where the banks are obviously attempting to hide behind the fine print in the form of their agreements in order to escape regulation that applies to the actual substance of the transaction. In applying the "doctrine of substance over form, the Court has looked to the objective economic realities of a transaction rather than to the particular form the parties employed." Frank Lyon Co. v. United States, 435 U.S. 561, 573 (1978). Courts have applied the doctrine of substance over form in interpreting TILA in order to "look to the substance of the transaction and the borrower's purpose in obtaining the loan, rather than the form alone." Riviere v. Banner Chevrolet, 184 F.3d 457, 462 (5th Cir. 1999) (applying doctrine of substance over form to definition of "consumer" under TILA).

BOUNCE LOAN FEES SHOULD BE DISCLOSED AS FINANCE CHARGES UNDER REGULATION Z.

The Board was Correct in its Initial Inclination to Regulate Bounce Loans Under Regulation Z.

In considering bounce loans, the Board initially requested comment as to "whether and how to provide guidance on potential coverage under Regulation Z." Proposed Rule, Truth in Lending, 67 Fed. Reg at 72,620.[3] We suggest that the Board's initial inclination, looking to Regulation Z, was correct. Regulation Z does indeed encompass bounce loans.

Bounce loan fees meet Regulation Z's general definition of finance charge, which is essentially the same as that of TILA. 12 C.F.R. § 226.4(a). However, the Banks argue that bounce loan fees are not finance charges because 12 C.F.R. §226.4(c)(3) specifically excludes from the definition of finance charges those charges that "are imposed by a financial institution for paying items that overdraw an account, unless the payment of such items and the imposition of the charge were previously agreed upon in writing." The Banks argue that because their bounce loan agreements reserve the right to decline to pay overdrafts they have not "agreed" to pay overdrafts, and hence bounce loans fall within the exception. We disagree with the Banks' interpretation of the exception and suggest that the exception is not applicable to bounce loan fees for two alternative and independently sufficient reasons: 1) bounce loans do not "overdraw" an account but rather draw on a credit feature attached to the account; and 2) the payment of bounce loans exceeding the funds on deposit is in fact "previously agreed upon in writing" within the meaning of TILA.

Bounce Loans Do Not "Overdraw" An Account.

To "overdraw" may be defined as to draw "in excess of the deposit balance." Webster's Third New International Dictionary Unabridged 1607 (1993). However, overdraw is also defined as "make a draft upon beyond the proper or authorized amount." Id. Bounce loans are not overdrafts because they do not draw against a deposit balance, but rather draw upon a credit feature within an authorized amount, such as Cecilian Banks' Hometown Coverage that provides for "up to a maximum of $500" for customers who "run short of cash between paydays." R-1136-216 Appendix at 3. Even the names of some bounce loan products differentiate them from the traditional notion of overdraft: "Powerdraft" in particular implies that drawing up to the authorized amount is *not* an overdraft, and "Hometown Coverage," implies coverage *against* overdrafts.

The Board's understanding of how bounce loans will be operate *after* implementation of Revised Regulation DD confirms that bounce loans do not overdraw a customer's deposit balance in an account but rather relate to the provision of credit: "fees for bounced-check protection services would not be considered maintenance or activity fees, because the fees relate to the institution's provision of credit as opposed to fees

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[3] In December 2002, while considering unrelated amendments to the Staff Commentary for Regulation Z, the board used the occasion to solicit public input on bounce loans. The board never considered or rejected any specific approach or language regulating bounce loans under Regulation Z.

related to the use of the consumer's own funds in the account." Proposed Rule, Truth in Savings, 69 Fed. Reg. at 31,764.

Bounce loans are therefore not excluded from coverage under 12 C.F.R. § 226.4(c)(3), which excludes from finance charges only charges for paying certain items that "overdraw an account." Only drafts in excess of the stated bounce loan limit, typically $500, could be considered to "overdraw" the authorized amount.

Because bounce loans do not fall within the exception, and meet the general definition of finance charge, they are subject to Regulation Z.

Payment of Bounce Loans and Bounce Loan Fees are "Previously Agreed Upon In Writing."

The Board has recognized that despite many Banks' statements that payment of overdrafts is discretionary and disclaimer of any "legal obligation of the institution to pay any overdraft," Proposed Rule, Truth in Savings, 69 Fed. Reg. at 31761, in actual practice Banks "promote the use of the service," and "[c]overage is automatic for consumers who meet the institution's criteria." Id at 31,760–761.

Regulation Z does not define the phrase "previously agreed upon in writing." However, it does provide that "[u]nless defined in this regulation, the words used have the meanings given to them by state law or contract." 12 C.F.R. § 226.2(b)(3). See also Proposed Interagency Guidance, 69 Fed. Reg. at 31,862 n.15 (confirming that "whether a written agreement exists is a matter of State law").

In the interpretation of agreements state courts applying the law of contract disregard provisions in written agreements that through their form camouflage the actual substance of the transaction. This is particularly true when interpreting an agreement to determine if charges purported to be something else are actually interest on a loan:

> Where, as here, the issue is whether the transaction was [something else] or a camouflaged loan, courts will look beyond the form to find the essential substance of the agreement made by the parties.

Atlas Credit of California v. Hill, 547 P.2d 894, 897 (Wash. App. 1976). The Banks do not want bounce loans recognized for what they are because if the high fees are translated into annual percentage rates bounce loans will run afoul of many state usury laws. State law is very clear on this point:

> We are mindful that in cases involving alleged usury the law has regard only for the actual facts, and searches for the real transaction between the parties, disregarding evasions, subterfuges, and all kinds and varieties of camouflage.

Id. (citing Home Savings & Loan Ass'n v. Sanitary Fish Co., 156 Wash. 80 (1930)). See also First Nat. Bank in Albuquerque v. Danek, 556 P.2d 31, 34 (N.M. 1976) (following other state courts that have traditionally "disregarded the form and looked to the substance of the transaction" to determine if a charge is interest) (collecting cases from California and Arizona and citing Rest. Contracts § 529 (1932)).

More recently, the Indiana Department of Financial Institutions has interpreted Indiana law with respect to the very issue now before the Board:

> Even though the documents to be provided to customers [the bounce loan agreement] regarding the Program repeatedly point out that this service is a non-contractual courtesy" and the bank is "not obligated to pay any item presented for payment," the Department would look beyond these statements to the actual operation of the plan, a matter of examining the substance of the agreement rather than the form.

Indiana Department of Financial Institutions Opinion Letter Regarding Automatic Overdraft Protection, February 21, 2002, available at http://www.in.gov/dfi/whatsnew/overdraft/MorrisseyNSFPhil_Goddard.htm, visited August 6, 2004.

Our research thus far indicates that bounce loans and bounce loan fees are "previously agreed upon in writing" as defined by state law and the law of contract. As of this writing, we have not found any contractual or state law authority to suggest otherwise.

Because bounce loans are previously agreed upon in writing, they do not fall within the exception contained in 12 C.F.R. §226.4(c)(3) and are subject to the requirements of Regulation Z.[4]

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[4] We acknowledge that the Staff Commentary to § 226.4(b)(2) does exempt the actual "service charge," that is imposed on a "checking or transaction account" in "connection with a credit feature" from inclusion in the finance charge. 12 C.F.R. § 226, Supplement I, Official Staff Interpretations. We agree that Banks need not include in the finance charge the actual portion of the bounce loan fee that is a bona fide handling charge made in connection with a credit feature as opposed to that part of the bounce loan fee that is integral to the cost of, and imposed for, obtaining the extension of credit. Accord Household Credit, 124 S.Ct. at 1748 (reasoning that where charges are levied "in connection with" an extension of credit but are not "imposed for" the extension of credit they may be classified as other than finance charges); see also Brief of the United States, Household Credit, 2003 WL 21999055 at *10 (distinguishing "other charges" from finance charges because they are not "integral to the cost of credit under the agreement" but rather "serve functions apart from" compensation for the risk of extending credit).

We believe the Staff Commentary is liberal in estimating such charges at $3 to $5 for illustrative purposes and in this age of automated processing, the actual handling charge exempt from finance charge treatment would likely be less than $1. The service charge, however, is still subject to disclosure under TILA and Regulation Z as an "other charge." See 12 C.F.R. § 226.6(b).

THE PROPOSED REVISIONS TO REGULATION DD AND ACCOMPANYING INTERAGENCY GUIDANCE DO NOT PROHIBIT THE EXTENSION OF BOUNCE LOANS AS CREDIT BUT RATHER ENCOURAGE BANKS TO EVADE COVERAGE UNDER TILA WHILE EXTENDING CREDIT.

Bounce Loans Will Continue as Extensions of Credit

Like the Notice of Proposed Rulemaking, the Notice of Proposed Interagency Guidance, 69 Fed. Reg. At 31,860, recognizes that bounce loans are "intended essentially as short-term credit facilities." However, rather than prohibit all those practices that make bounce loans extensions of credit the proposed revisions to Regulation DD and the Proposed Guidance allow continued extension of credit without regulation under TILA. After implementation of the Revised Regulation DD and accompanying Guidance the responsible agencies still classify bounce loans as loans: " Overdraft balances should be reported as loans," and overdraft losses "should be charged off against the allowance for loan and lease losses." Id. at 31,861. If it is the intent of revised Regulation DD to take overdraft protection services out of the credit arena, in other words to eliminate bounce loan practices and return overdraft services to the traditional ad hoc courtesy coverage of inadvertent overdrafts, the regulation must go much further than it does. Continued treatment of "overdraft balances" as loans reflects the accurate understanding that under revised Regulation DD bounce loans will continue as extensions of credit.

Proposed Revisions to Regulation DD and Staff Commentary

Regulations, including Proposed Regulation DD, adopted through notice and comment procedures have the force of law. See United States v. Mead Corp., 553 U.S. 218 (2001). The proposed Staff Commentary may provide a safe harbor for Banks from certain forms of civil liability. The "teeth" of the proposed actions are in the Regulation and Staff Commentary. We therefore discuss the Regulation and Commentary first.

Revised Regulation DD itself contains very few substantive restrictions on bounce loan practices. The section-by-section analysis of the Proposed Regulation notes that "A principal concern about institutions' promotion of overdraft protection services is that consumers may be led to believe that the service represents a traditional line of credit." Proposed Rule, Truth in Savings, 69 Fed. Reg. at 31, 764. The analysis then goes on to list problems with promotions that create this misleading impression, including creating "the impression that the service can be relied upon to obtain short term extensions of credit from time to time (up to a given amount) at minimal cost" and focusing on "the dollar amount of the overdraft limit, which may lead consumers to believe that a line of credit is being provided." Id. The proposed remedy is to "require certain disclosures in advertisements for automated overdraft payment services," because these additional disclosures "could reduce the potential that some consumers would be misled." Id. Unfortunately, the regulation exempts from these additional disclosures "advertisements using broadcast media, outdoor billboards, and telephone response machines." Id. If advertisements without the disclosures are misleading, we can see no reason to exempt what probably amounts to the majority of advertisements from the requirement.

The additional disclosures, in any event, read more like a firm offer of a line of credit than a warning that the service is not to be used as a line of credit. The proposed additional disclosures are as follows:

1) The fee for the payment of each overdraft item
2) They types of transactions covered
3) The amount of time the consumer has to repay or cover any overdraft
4) The circumstances under which the institution would not pay an overdraft

Id. Under this regulation a bank could pay overdrawn checks, up to for example ten checks a month (how many is too many?) and not exceeding a total of $500, for a fee of $35 per check, so long as the consumer maintains the account in good standing and repays all overdrafts within 30 days. Although the Proposed Staff Commentary states that an advertisement would be misleading by "[r]epresenting an overdraft protection service as a 'line of credit,'" Proposed Rule, Truth in Savings, 69 Fed. Reg. at 31,767, it is likely that consumers will take the required "disclosures" as an offer of a line of credit, albeit at usurious rates.

The Proposed Staff Commentary also lists as misleading advertisements "[r]epresenting that the institution will honor all checks or authorize all transactions that overdraw an account, when the institution retains discretion at any time not to honor checks or authorized transactions." Id. However, the Proposed Regulation requires that advertisements disclose the circumstances under which Banks will not pay an overdraft. Id. at § 230.8(f)(4), 69 Fed. Reg. at 31,766. The Proposed Staff Commentary clarifies that in "describing the circumstances under which an institution will not pay an overdraft. . . statements such as 'overdrafts will not be paid if your account is not in good standing, or you are not making regular deposits, or you have too many overdrafts,'" will satisfy the requirement. Id. at 31,767. The net effect of these proposed revisions is that Banks will be allowed, and in fact encouraged to make advertising statements such as the following:

> **With overdraft protection we may pay your overdrafts so long as your account is in good standing, you are making regular deposits, and you do not have too many overdrafts.**

Banks will continue to market, and consumers will continue to understand and use, "overdraft protection" as the high cost line of credit that it is.

Proposed Interagency Guidance Document.

The Guidance Document's "self-regulation" approach is inadequate.

Guidance documents do not have the force of law. See Skidmore v. Swift & Co., 323 U.S. 134, 140 (1944); Christensen v. Harris County, 529 U.S. 576, 587 (2000). Often guidance documents announce an enforcement agency's "trigger points" for enforcement action, and while not legally binding, have a significant deterrent effect because of regulated entities desire to avoid the stigma and risk of litigation. Here, however, the Guidance Document is essentially an invitation to industry self-regulation:

> Finally, the proposed Guidance sets forth best practices that serve as positive examples of practices that are currently observed in, or recommended by, the industry.

Proposed Interagency Guidance, 69 Fed. Reg. at 31,859–31,860. A section entitled "Best Practices" then sets out "best practices currently observed in or recommended by the industry." Id. at 31,863. There is no mention of enforcement thresholds. Although the guidance mentions that these "best practices currently observed in or recommended by the industry," also "may otherwise be required by applicable law," the guidance only suggests that "institutions should take into consideration" the suggestions that follow and indication is generally not given on what practices are actually firmly expected or required.

Bounce loan programs were developed and marketed to Banks by bank consulting firms that promise Banks the programs will be effective in "dramatically increasing your fee income." See comment R-1136-216, Appendix at 9. These consultants continue to advertise software and management services to Banks for overdraft programs designed for "improving your bottom line." http://www.overdrafthonor.com, visited August 4, 2004. At least eight consulting firms specialize in marketing and managing overdraft programs designed for "NSF Fee Income Enhancement." See comment R-1136-216, Appendix at 11. Some of these firms have no business other than figuring out ways for Banks to entice customers to bounce more checks, while staying technically within the law. Id. In short, an entire industry is devoted to enticing consumers to use bounce loans early and often. Washington Mutual alone earns more than $1 billion dollars a year on bounce loans. N.Y. Times at C3, June 8, 2004. With at least 1500 Banks offering bounce loans the total loss to low-income households (and commensurate profit to Banks) reaches into untold billions of dollars.

Upon further consideration, we hope the Board will agree that the time has long passed for invitations to self-regulation with a "wait and see" posture.

<u>The Guidance Document encourages banks to continue extending credit at usurious rates without regulation under TILA.</u>

Although the Guidance suggests that one of the most pernicious bounce loan practices should be discontinued and Banks should clearly inform consumers in real time at ATM displays before they incur an overdraft fee,[5] the Guidance still encourages banks to present ATM bounce loans as an available source of credit. The Guidance encourages banks to "[p]rominently distinguish actual balances from overdraft protection funds availability" at ATM displays and to "separately" and "prominently" display actual cash balance and available "overdraft protection." Proposed Guidance, 69 Fed. Reg. at 31,863.

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[5] Even this modest disclosure is only a suggestion, and the Guidance contemplates that ATM customers may not receive even this disclosure: "If this is not possible, then post notices on proprietary ATMs explaining that withdrawals" may trigger bounce loan fees. Proposed Guidance, 69 Fed. Reg. at 31,863. A worn out sticker on the side of an ATM machine may fail utterly to provide actual disclosure to customers.

This would allow banks to provide an ATM display as follows:

> **You have available cash funds: $42.00**
>
> **You have available overdraft funds: $475.00**
>
> **To access your overdraft funds press the Agree button and enter the amount you wish to draw. A Fee of $35 will be assessed for each overdraft withdrawal.**
>
> **You must repay all overdraft withdrawals within 30 days.**
>
> **To Cancel the transaction press Cancel.**

A consumer needing $65, would then withdraw the $42 account balance and an additional bounce loan of $23. This transaction represents an offer by the Bank to extend short term credit and an acceptance by the consumer by pressing "Agree." It is a binding contract by any definition. It is also a commitment "agreed upon in writing" by the bank to pay an "item" and agreement of the consumer to pay a charge in exchange that brings the transaction squarely within coverage of Regulation Z. 12 C.F.R. § 226.4(c)(3) (requiring that where charges are imposed by a Bank for paying an item that overdraws an account and payment of the item and imposition of the charge are agreed upon in writing, the charge is a "finance charge" subject to Regulation Z). However, the Guidance suggests that this transaction is *not* covered by Regulation Z and is therefore not subject to all of the consumer protections intended by Congress in TILA, including disclosure of the APR. The actual APR of this loan, if repaid in 30 days as required, would be over 1000%. Recognition of this transaction for what it is—a usurious loan—would confirm its illegality in many instances.

Unfortunately, the Proposed Guidance in its suggested best practices (which we feel are inadequate even in so far as they go) focuses on notification, advertising, representation, and accounting aspects of the bounce loan service. Nowhere is there even a serious suggestion that Banks should discontinue the *use* of usurious bounce loans as an ongoing short-term credit facility for low-income households. In fact the Guidance clearly contemplates frequent continued use, up to the point of suggesting that Banks "consider" a daily limit, similar to daily limits found in other routinely used services, such as ATM withdrawals:

> 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.

Proposed Guidance, 69 Fed. Reg. at 31,864 (emphasis added). The Banks, of course, argue that bounce loans are a convenience to customers. This argument has long ago been laid to rest by Congress and the fifty state legislatures alike. As one court aptly observed, in enacting its usury law, the Washington Legislature "confirmed a frequently reiterated judicial observation that usury has long been recognized as a social and economic evil affecting not only the parties to the transaction but society in general." Atlas Credit, 547 P.2d at 897.

Rather than promote exorbitantly priced credit, we hope the Board will upon consideration take steps to promote the availability of more reasonably priced short-term credit for low-income households, such as credit card links to checking accounts, or traditional small lines of credit with interest rates not exceeding low double digits. This approach would allow banks to earn a reasonable return while making credit available to low-income households.

The Guidance Document does not adequately address non-check bounce loans.

The Guidance fails to adequately address other non-check transactions that trigger bounce loan fees. For example, many point of sale terminals, such as gasoline stations, supermarkets, and department stores accept debit cards. Many vendors also accept debit cards for purchases of goods and services through the internet. The Guidance suggests that "[w]hen 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." Proposed Guidance, 69 Fed. Reg. at 31,863 (emphasis added). Merchants are interested in verifying that funds are available not in carrying out Banks' compliance duties. It is far from clear that it would be feasible for merchants to modify their hardware and software to transmit bounce loan notices to consumers at the point of sale, resulting in continued non-disclosure of bounce loan fees.

CONCLUSION

Bounce loans are high-cost credit devices that disproportionately impact low-income and minority communities. Bounce loans should be fully regulated under TILA and Regulation Z. The Proposed Revisions to Regulation DD, Proposed Staff Commentary, and Proposed Interagency Guidance, that place bounce loans under TISA, do not adequately address the bounce loan problem.

We urge the Board not to adopt the proposed regulations and urge the Board to instead take the necessary steps to fully regulate bounce loans under Regulation Z.

Thank you again for the opportunity to submit these comments and for considering our views in reaching your ultimate decision

S/Michael A. Brodsky
On behalf of the Greenlining Institute