BROADWAY BANK

July 30, 2008

(VIA Electronic Submission)

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

RE: FRB Docket No. R-1314; Unfair or Deceptive Acts or Practices;
73 *Federal Register* 28904; May 19, 2008
(addressing Overdraft Services)

Dear Ms. Johnson:

I appreciate this opportunity to comment, on behalf of Broadway Bank, on the proposed changes to Regulation AA, Unfair or Deceptive Acts or Practices, dealing with overdraft protection programs and services.

Broadway National Bank is a $1.8 billion independent bank owned by Broadway Bancshares Inc., a one-bank holding company. The bank is headquartered in San Antonio, Texas, and serves several counties in south-central Texas; its Eisenhower Bank division serves military and related personnel throughout the world. Customer transactions and information are processed through one of the largest providers of financial information technology services.

Though we understand the consumer protection objectives of the Reg AA proposals, we also have serious concerns about portions of the proposed rules and the unintended consequences that could result.

I. Overdraft Services Opt-Out

We have an informal procedure in place today to disallow most overdrafts on a customer account when requested by the customer. We have no objection to a more formal program to provide consumers the right to opt-out of this program. However, we have concerns with several aspects of the proposal.

a. In today's environment, it is **impossible to completely avoid overdrafts**. When a customer overdraws his account at an ATM, usually when it is off-line, the cash is gone and his bank cannot return the transaction. When the bank has authorized a debit transaction based on the account balance, but is required to return a deposited item the next day, reducing the balance, the bank must still honor the debit transaction. If that bank could not overdraw the customer accounts in these and various other situations, it would take the loss, and would likely need to curtail issuance of ATM and debit cards, resulting in a reduction in service and convenience for the customer. Banks must be able to overdraw customer accounts in such situations, and should be allowed to charge overdraft fees when an overdraft cannot be prevented.

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b. The proposal to allow a **partial opt-out**, for ATM and point-of-sale (POS) debit card transactions, cannot be accommodated today through most, if not all, bank and third-party provider transaction processing systems, including our processor. Necessary changes may be extensive, and the costs of such system renovations are significant even for large banks and processors.

Also, it has become impossible for the consumer to know with certainty which of his transactions will be received by his bank as POS transactions. Debit card transactions may be authorized by signature or PIN (in some instances neither is required), however transactions are not necessarily processed through the PIN or signature network one might expect. The customer opting out of ATM and POS overdrafts will have no way of knowing which of his card-based transactions may actually be paid into overdraft.

It is interesting to note that, in an effort to separate transactions into two groups so that the consumer's checks to merchants may be paid into overdraft and avoid the merchant's returned check fee, the partial opt-out proposal actually penalizes banks; the ATM and POS transactions that could not be paid into overdraft are the two types of transactions that generally cannot be returned by the bank.

c. Initial opt-out **notices** should be simple, straightforward, and be designed to help the customer make the best personal decision. The customer should be informed that:

- Opting out does not guarantee you will prevent overdrafts or overdraft fees.
- Not opting out does not guarantee your items will be paid into overdraft.
- NSF items returned unpaid may (or will) incur a bank NSF fee.
- NSF items returned to merchants usually incur the merchant's returned check fee.
- Some businesses report repeated NSF activity as criminal behavior.

Subsequent notices required should be reasonably concise, so that the notice may be printed on the statement or on a NSF or Overdraft Notice as currently available through most vendors.
When a customer does opt-out, the bank must be allowed a reasonable time period to properly code his account to effect the opt-out.

II. Debit Holds

This paragraph proposes that banks would not be allowed to charge a fee for an overdraft caused solely by a hold on funds that exceeds the actual transaction amount. This proposal is complicated, difficult to explain to customers, and very difficult to implement.

a. Banks have little control over these holds generated by merchants, and cannot know whether the hold amount is correct, understated or overstated until the transaction is presented for final settlement.
b. Current debit hold practices are an important risk management tool, based on merchant practices and card network rules, as an authorized network transaction cannot be returned unpaid. They are a safeguard set to ensure that funds will actually be available when the authorized item is accepted for payment.
c. It would be very costly for banks to determine whether an overdraft was caused by a hold amount greater than the transaction amount. For the foreseeable future, this would of necessity require a manual procedure for nearly all affected institutions; for our bank we estimate two additional full time-equivalent employees would be required.

We believe that issues involving debit holds would be better addressed through the card networks such as MasterCard and Visa, which have their own sets of rules governing the procedures and processes used by merchants.

III. Comments

Posting Order – The order of payment of items received in a single day has many variations among banks. Most banks that pay high-to-low or low-to-high do so within categories of items; for example one bank may pay ATM withdrawals first, another may pay Cashed Checks first. Decisions on payment order are based on many variables, including customer base, general customer preference, historical transaction data, and overdraft income.

We have found, as have many other banks, that most customers want their largest items paid first. The largest items may include a mortgage or rent payment, a car payment, a credit card payment, a loan payment, etc. Even though this order may result in greater fees, when it becomes necessary to return items, those returned are likely to be small items and will have a much smaller impact on the customer in the long run. However, other banks have had other experience, and no single rule can reasonably be applied to all.

Today, it would be impossible for our bank and most others to make more than one posting order available in order to give the customer a choice. It would also be impossible to clear items using one method and determine the number of overdraft fees to charge using another method. And it would be costly to all banks and processors to implement such systems.

Final Comment – Broadway Bank is all about customer service; that is true for many community banks and others who have survived and even thrived despite the ups and downs of the economy, societal and political changes, the technological revolution, and regulatory change. We believe in giving our customers the best value we can offer at a fair price, and keeping them well informed regarding our products and policies.

Our customers can, and many do, avoid overdraft fees by properly managing their accounts. We also offer an overdraft transfer option to any customer, and an overdraft line of credit for any who qualify. We are not averse to offering a fair and reasonable opt-out, but we believe the partial opt-out and the debit hold proposals are simply unworkable as currently outlined.

Thank you for the opportunity to comment on these Regulation AA proposals. Should you have any questions regarding our comments, please feel free to contact me.

Sincerely,

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CC: Office of the Comptroller of the Currency