

Consumer Action

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Jennifer J. Johnson, Secretary
Board of Governors of the Federal Reserve System
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July 15, 2008

RE: Regulation DD; Docket No. R-1315 - Truth in Savings [12 CFR Part 230]

Dear Governors of the Federal Reserve System:

Consumer Action¹ is pleased to comment on your proposed rules to address overdraft loans. We appreciate that the Board, in issuing these proposed regulations, recognizes that the service referred to as “courtesy overdraft protection” is unfair to consumers and that marketing of the service to consumers has been deceptive.

Consumer Action has studied overdraft protection services offered by banks via an extension of credit (overdraft line of credit) and transfers from a linked savings account to a checking account when funds are needed to protect the account holder from bouncing a check.

The consumer actually chooses these services, and they provide real protection because they spare the account holder any bounced check fees (non-sufficient funds, or NSF, fees) at a minimal cost. The overdraft line of credit and savings-linked overdraft generally invoke small one-time transaction fees. Overdraft lines of credit additionally charge an interest rate comparable to credit cards for any period where an outstanding credit balance exists. Generally, consumers can use these services for short-term loans for just a small interest charge.

In our comments, we are going to refer to the subject of this rulemaking as “courtesy bounce protection” or “automatic bounce protection” to differentiate it from the truly helpful services mentioned in the previous paragraph.

¹ Consumer Action (www.consumer-action.org) is a non-profit organization founded in San Francisco in 1971. During its more than three decades, Consumer Action has continued to serve consumers nationwide by advancing consumer rights, referring consumers to complaint-handling agencies through our free hotline, publishing educational materials in Chinese, English, Korean, Spanish, Vietnamese and other languages, advocating for consumers in the media and before lawmakers, and comparing prices on credit cards, bank accounts, telephone plans and other consumer goods and services.

Automatic bounce protection often comes with checking accounts—especially “free checking”—but a lot of consumers don't even know they have it. The problem is, it allows them to spend more than they have in their accounts, triggering bounced check fees and opening them to a spiral of overdrafts when the funds are removed from their accounts when they next deposit funds.

Automatic bounce protection is added to consumer checking accounts by default. It does not protect the account holder from bounced check-type fees. Many account holders are unaware that they have it. Automatic bounce protection provides a small cushion in the account that becomes a short-term, high-cost loan if the account holder overdraws the account. Some banks actually include this cushion in the “available balance” provided to the account holder.

Banks should be prohibited from advertising or promoting automatic bounce protection without clearly disclosing all fees and conditions.

Consumer Action supports your proposal to require banks to disclose the actual account balance at the ATM, online or by phone. We suggest that POS be added to the requirement. We also support your intention to require a total of all overdraft and returned item fees assessed be listed on periodic statements.

Your proposal prohibits banks from charging an overdraft fee if the account holder has not received notice of the right to opt out—or if they have received the notice but failed to opt out. This notice and opt out notice needs only to be provided when new accounts are opened. For existing account holders, such notice would be given only after funds are extended, with high fees, to pay for a check with insufficient funds.

Consumers must be given the opportunity to sign up for courtesy bounce protection—it must never be automatic. This must be a proactive choice on the part of the consumer, with no default application of the service. We wonder why, if it is such a great service as many bankers have said, it must be deceptively applied to consumer accounts. If it were such a good deal, consumers would ask for it.

The Board must write this rule in such a way that allows the consumer to “opt in” to courtesy bounce protection. We believe account holders must initiate the request, not end up with it by default because they failed to read some fine print, contact the bank and say, “Take this off my account.”

Consumers especially should never have to “unsubscribe” from these loan programs after they already are obligated to pay high fees for these unauthorized small loans.

You propose to prohibit overdrafts caused by a merchant hold (such as a gas station or hotel) on a debit card. Your rules also should include holds placed on deposits. Many banks delay the availability of deposited funds. We strongly suggest that you require banks to make deposits available as soon as they clear. Today, checks clear in a matter of

days, if not hours, but some banks continue to stick with outdated guidelines on funds availability. Certainly, under no circumstances should adequate deposited funds on hold be allowed to trigger an expensive overdraft loan.

You should not permit automatic overdraft loans or fees for any overdraft triggered by a debit card ATM or POS transaction. The financial institution can avoid the overdraft easily by denying that transaction. The available balance at the ATM should never include any cushion made available via automatic bounce protection.

We urge you to close the loophole that lets banks make these cash advances to consumers without providing Truth in Lending protections and cost disclosures. We urge you to write strong rules that require the costs of automatic overdraft protection to be disclosed under open-end credit rules. Overdraft loans should be regulated under the Truth in Lending Act with sample APR disclosures. This would give account holders access to information on the comparable cost of credit so that they can make good choices in which financial products to use.

When a consumer has outstanding bounce protection loans, banks can reach in to their accounts and take the money to repay overdraft loans and fees before honoring other scheduled payments and checks. Truth in Lending coverage would prevent this from happening.

Banks are now free to process the largest daily transactions first, depleting the account and causing a “cascade” of bounced checks. For low-balance account holders, this practice depletes available funds and triggers multiple, costly overdraft fees in a single day.

We suggest you come down hard on the games banks play in processing daily transactions in order to maximize fee income—they are unfair to consumers. We have heard banks say that they are just protecting consumers by processing the largest payment first, which might be the consumer’s mortgage, car loan or credit card bill. We don’t buy this argument when it subjects consumers to multiple daily overdraft fees. Deposits should be credited to an account before checks are charged to it.

We are sure that you realize that low- to moderate-income consumers end up paying the bulk of these fees because they often live paycheck-to-paycheck. According to Center for Responsible Lending, 71% of overdraft fees were paid by “lower income, single, non-white, renters.” Please protect bank consumers from these patently profit making short-term loans. We urge you instead to guide the banks in creating useful products that help consumers manage their money—not flush it down the drain.

Truly yours,



Linda Sherry
Director of National Priorities