



Capital One Financial Corporation  
1680 Capital One Drive  
McLean, VA 22102

July 18, 2008

Ms. Jennifer J. Johnson  
Secretary  
Board of Governors  
Federal Reserve System  
20<sup>th</sup> Street and Constitution Avenue, NW  
Washington, DC 20551  
[regs.comments@federalreserve.gov](mailto:regs.comments@federalreserve.gov)

Regulation Comments  
Chief Counsel's Office  
Office of Thrift Supervision  
1700 G Street, NW  
Washington, DC 20552  
Attn: OTS-2008-0004  
[www.regulations.gov](http://www.regulations.gov)

Ms. Mary Rupp,  
Secretary of the Board  
National Credit Union Administration  
1775 Duke Street  
Alexandria, VA 22314-3428  
[regcomments@ncua.gov](mailto:regcomments@ncua.gov)

**Re: Proposed Regulation DD Overdraft Rules (Docket No. R-1315)**

**Proposed Regulation AA Unfair or Deceptive Acts or Practices (UDAP) In  
Connection With Overdraft Services for Deposit Accounts  
Board (Docket No. R-1314)  
OTS (OTS-2008-0004)  
NCUA (RIN 3133-AD47)**

Ladies and Gentlemen:

Capital One Financial Corporation ("Capital One") is pleased to submit comments on amendments to Regulation DD proposed by the Federal Reserve Board ("Board"), and related amendments to Regulation AA proposed by the Board, Office of Thrift Supervision, and the National Credit Union Administration (collectively, "Agencies").<sup>1</sup>

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<sup>1</sup> Proposed Regulation DD, 73 Fed. Reg. 28739 (May 19, 2008). Proposed Regulation AA, 73 Fed. Reg. 28904 (May 19, 2008). The OTS and NCUA issued proposed rules similar to Regulation AA to be

Capital One Financial Corporation ([www.capitalone.com](http://www.capitalone.com)) is a financial holding company whose subsidiaries collectively had \$92.4 billion in deposits and \$147.2 billion in managed loans outstanding as of June 30, 2008. Headquartered in McLean, VA, Capital One has 740 locations in New York, New Jersey, Connecticut, Texas and Louisiana. It is a diversified financial services company whose principal subsidiaries, Capital One, N.A., Capital One Bank (USA), N. A., and Capital One Auto Finance, Inc., offer a broad spectrum of financial products and services to consumers, small businesses and commercial clients. A Fortune 500 company, Capital One trades on the New York Stock Exchange under the symbol "COF" and is included in the S&P 100 index.

Capital One believes in empowering its customers with notice and choice. We have advanced this position in our public statements as well as in our business practices. For example, when the Board proposed requiring creditors to provide a 45 day advance notice before changing customers' credit card terms,<sup>2</sup> Capital One advised the Board to require creditors to give customers the opportunity to opt out of changes to their accounts, in addition to giving advance notice.<sup>3</sup> Capital One currently provides opt-outs to our customers when their credit card terms change. We also currently provide opt-outs to our customers if they do not want us to cover overdrafts on their deposit accounts.

In 2005, the Board issued a Regulation DD amendment and the Agencies issued the OTS' and Interagency Guidance on Overdraft Protection Programs ("Overdraft Guidance").<sup>4</sup> Concerned about programs that were marketed and promoted in order to encourage consumers to use the programs,<sup>5</sup> the Regulation DD amendment and the

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contained in 12 CFR Part 535 and 12 CFR Part 706, respectively. References in this comment letter to Regulation AA also apply to the OTS and NCUA's proposed rules.

<sup>2</sup> 2007 Proposed Regulation Z, 73 Fed. Reg. 32948 (June 14, 2007).

<sup>3</sup> Capital One Letter of October 11, 2007.

<sup>4</sup> Regulation DD, 70 Fed. Reg. 29582 (May 24, 2005). NCUA issued a similar rule for credit unions. 71 Fed. Reg. 24568 (Apr. 26, 2006). Interagency Guidance on Overdraft Protection Programs, 70 Fed. Reg. 9127 (Feb. 24, 2005), and OTS Guidance on Overdraft Protection Programs, 70 Fed. Reg. 8428 (Feb. 18, 2005).

<sup>5</sup> The Overdraft Guidance states:

Aspects of the marketing, disclosure, and implementation of some overdraft protection programs, intended essentially as short-term credit facilities, are of concern to the Agencies. For example, some institutions have promoted this credit service in a manner that leads consumers to believe that it is a line of credit by informing consumers that their account includes an overdraft protection limit of a specified dollar amount without clearly disclosing the terms and conditions of the service, including how fees reduce overdraft protection dollar limits, and how the service differs from a line of credit.

In addition, some institutions have adopted marketing practices that appear to encourage consumers to overdraw their accounts, such as by informing consumers that the service may be used to take an advance on their next paycheck, thereby potentially increasing the institutions'

Overdraft Guidance imposed additional disclosure requirements and best practices on banks that marketed and promoted overdraft programs.<sup>6</sup> The Agencies were not concerned with, and thus the Overdraft Guidance and Regulation DD amendment did not apply to, courtesy overdraft coverage not marketed or promoted to consumers.<sup>7</sup> Capital One does not promote or advertise its courtesy coverage. In adopting this policy, Capital One seeks to avoid encouraging customers to rely excessively on such coverage, as well as to avoid other concerns articulated in the Overdraft Guidance and Regulation DD amendment.<sup>8</sup>

In contrast, the recent Regulation DD and related Regulation AA proposals would apply to banks even if they do not market or promote their overdraft programs. As further articulated below, we believe that the Board should continue to recognize this distinction in its revision and implementation of the proposed rules.

The proposals would require banks to give deposit account customers disclosure of their right to opt out of having overdrafts covered. Banks would have to provide the disclosure initially, such as at account opening, and following any overdraft that is covered. The right to opt out may cover any type of transaction that may overdraw the deposit account or may be limited to debit card transactions at the automated teller machine (ATM) and point of sale terminal (POS).<sup>9</sup>

We believe that the Agencies' proposals are an advance in empowering consumers with notice and choice. While we support the principles articulated in the Regulation AA and Regulation DD proposals, we believe that certain modifications are necessary to avoid unintended consequences and enhance the objectives of the rules.

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credit exposure with little or no analysis of the consumer's creditworthiness. These overdraft protection programs may be promoted in a manner that leads consumers to believe that overdrafts will always be paid when, in reality, the institution reserves the right not to pay some overdrafts.

Overdraft Guidance, 70 Fed. Reg. at 9129.

<sup>6</sup> Regulation DD §230.11. Overdraft Guidance, 70 Fed. Reg. at 9131-32.

<sup>7</sup> The Overdraft Guidance states:

[T]he institution may accommodate the consumer and pay overdrafts on a discretionary, ad-hoc basis. Regardless of whether the overdraft is paid, institutions typically have imposed a fee when an overdraft occurs, often referred to as a nonsufficient funds or "NSF" fee. Over the years, this accommodation has become automated by many institutions. Historically, institutions have not promoted this accommodation. This approach has not raised significant concerns.

Overdraft Guidance, 70 Fed. Reg. at 9128.

<sup>8</sup> For example, the Overdraft Guidance cautions against "encourag[ing] irresponsible consumer financial behavior that potentially may increase risk to the institution." Overdraft Guidance, 70 Fed. Reg. at 9129.

<sup>9</sup> Proposed Regulation AA §227.32.

**The opt-out notice should be modified to make it simpler, more accurate and less confusing for consumers**

The Agencies propose that an opt-out notice be provided to consumers on multiple occasions, including at some initial point such as account opening, and again during any periodic statement cycle where an overdraft fee is assessed. The opt-out notice would contain substantial information, including: (1) any fee for paying overdrawn items; (2) the lowest dollar amount on a transaction for which the overdraft fee may be assessed; (3) the maximum amount of overdraft fees that may be assessed in one day and one statement period; (4) an explanation of the customer's general and partial opt-out rights; (5) information on how to opt out; and (6) a statement about other ways to cover overdrafts, such as by a line of credit.

While Capital One supports the broader purpose of providing customers with sufficient information to make appropriate choices for their circumstances, our experience and consumer research show that notices must be both brief and timely to be effective. In this regard, while the more detailed information in the proposed notices might be relevant to some consumers when they first open an account, or might be appropriate in circumstances where a bank actively markets its overdraft services to consumers, it does not appear to be appropriate where a bank simply chooses to honor an overdraft as a courtesy.

In the context of courtesy overdrafts, Capital One is concerned that the length, complexity and timing of the notices serve to confuse rather than enlighten consumers regarding the nature of overdraft protection. In such cases, where there is no expectation of a continuing service, Capital One is concerned that the content of the proposed notice may have the unintended effect of promoting the use of courtesy overdraft coverage by leading consumers to believe that all overdrafts will be covered. The wording of the notice, which refers to courtesy coverage as a "service" and later refers to a line of credit as a comparable type of "service," elevates the concept of discretionary courtesy coverage to a product that consumers may rely on as they would a line of credit. Similarly, statements such as "we provide overdraft services for your account," "these are fees associated with our service," and "we will charge you a fee of \$\_\_ for each overdraft item that we pay," further leads consumers to believe that overdraft draft coverage is a feature or benefit of their account rather than a discretionary accommodation by their bank.<sup>10</sup> Use of such language results not only in creating a misleading consumer impression in the case of courtesy coverage, but also undermines the Agencies' stated goal in the current and proposed Regulation DD, Regulation AA, and the Overdraft Guidance to minimize consumers' use of overdraft coverage.

The proposed rule would compound the potential misimpression created by the initial notice by requiring a subsequent opt-out notice to consumers during the same

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<sup>10</sup> Proposed Regulation DD Model Opt-Out Form B-10.

periodic statement cycle that an overdraft is covered. This notice would further reinforce the perception that courtesy overdrafts are a “service” and will be covered as a routine matter.

The proposed opt-out notice may also be misleading because it does not explain that despite an opt-out, there are situations where the bank may cover an overdraft and assess an overdraft fee. Under proposed Regulation AA, these exceptions are when (1) the actual purchase amount exceeds the amount that had been authorized; and (2) the transaction is presented for payment by paper-based means and was not previously authorized.<sup>11</sup> These exceptions, however, are not explained in the opt-out notice. Consumers who have opted out but then are charged an overdraft fee for a transaction that falls within one of the two exceptions may be confused and upset by the overdraft fee.

As a result, Capital One believes that the proposed overdraft notice should be significantly shortened and simplified, particularly in cases where overdraft protection is offered solely as a periodic courtesy. In such cases, we recommend an abbreviated notice that articulates a consumers’ right to opt-out and provides the means to do so. At a minimum, we believe that including a similar, additional, lengthy explanation regarding the overdraft “service” is redundant since the notice would be sent with or before the periodic statement that lists and aggregates the overdraft fees that were assessed.<sup>12</sup>

Capital One agrees with the Board that the opt-out notice should be consumer tested. Consumer testing and modification of the opt-out notice may resolve the above issues and result in a more relevant, accurate and informative disclosure for consumers.

### **The rule should include the flexibility to provide a general opt-out**

As discussed above, Capital One generally supports providing customers with the right to opt out of overdraft protection. The Agencies also propose requiring banks to provide consumers a partial opt-out right. This partial opt-out right would permit customers to direct a bank to reject overdrafts occurring by debit card at ATMs and POS terminals, but to cover overdrafts occurring by other means, such as by check. Given that banks are not required to cover any overdraft, we question the rationale and basis for this right to a partial opt-out.<sup>13</sup>

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<sup>11</sup> Proposed Regulation AA §227.32(a)(3).

<sup>12</sup> Proposed Regulation DD §230.11.

<sup>13</sup> This faulty assumption appears in the proposed opt-out notice which tells consumers:

You also have the right to tell us not to pay overdrafts for ATM withdrawals and debit card purchases, but to continue to pay overdrafts for other types of transactions.

The Board and Agencies have recognized in Regulation Z, Regulation DD, the Overdraft Guidance and elsewhere in the proposed rules, that banks cover overdrafts as a courtesy to consumers and not as a consumer right.<sup>14</sup> Banks have a legal right, as well as a safety and soundness obligation to reject transactions, when there are insufficient funds in customers' accounts.<sup>15</sup> The partial opt-out right has the effect of overriding these legal and safety and soundness concerns and presenting customers with a misleading impression of their right to direct banks to pay certain overdrafts.

As noted above, Capital One supports the proposed requirement that banks provide consumers a general opt-out right. If consumers opt out, banks will know that courtesy coverage is not desired and honor that wish. That said, we strongly believe that the Agencies should permit, but not require, banks to also offer partial opt-outs. In addition to the concerns highlighted above, the cost and operational complexity of offering partial opt-outs should not be borne as an obligation if the bank chooses instead simply to opt customers out of all overdraft protection if they so choose (subject to the exceptions articulated in the proposed rules).

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The faulty assumption also appears in the Agencies' explanation of the proposed partial opt-out. For example, the Agencies states:

Some consumers may want their institution to pay overdrafts by check and ACH, but do not want overdrafts paid in other circumstances....

Accordingly, the partial opt-out requirement...is intended to allow consumers the ability to determine for themselves whether they prefer...to have overdrafts paid for check and ACH transactions....

[P]roviding consumers a choice regarding the transaction types for which they want to have overdrafts paid outweighs the potential programming costs associated with this requirement.

73 Fed. Reg. at 28930.

<sup>14</sup> Examples include Regulation Z §226.4(c)(3); Regulation DD §230.8(a) comment 10.ii.; Overdraft Guidance, 70 Fed. Reg. at 9128; Discussion of Proposed Regulation DD, 73 Fed. Reg. at 28739; and Discussion of Proposed Regulation AA, 73 Fed. Reg. at 28927.

<sup>15</sup> Uniform Commercial Code 4-402(a) makes clear that a bank has no duty to pay an overdraft. Payment of the overdraft is left to the bank's discretion and agreement with their depositor.

In discussing overdraft programs, the Overdraft Guidance warns that “[i]nstitutions should weigh carefully the risks presented by the programs including the credit, legal, reputation, safety and soundness, and other risks.” 70 Fed. Reg. at 9129. One of the three sections of the Overdraft Guidance discusses safety and soundness concerns in detail. 70 Fed. Reg. at 9129-30.

## Other issues

We have other suggestions about the proposed amendments:

- As mentioned above, proposed Regulation AA provides two exceptions when an overdraft fee may be assessed despite an opt-out. We believe that a third exception is necessary where insufficient funds may result when another withdrawal is processed after a debit card transaction is authorized but before it is presented for settlement. For signature debit transactions, settlement is typically two days after authorization, but can be weeks or even months. Though pin debit transactions typically settle the same day they are authorized, they can also be delayed significantly because a merchant may batch and submit the debit card transactions to the bank later. This lag between authorization and settlement exposes the bank to the risk of insufficient funds in the consumer's account. Even in cases of same-day settlement of debit transactions, there can be intervening transactions posted that day and processed in batch that evening. Although there are insufficient funds, the bank must cover the debit card transaction since it was authorized. Since the consumer has knowledge and control of the transactions and balance, it would be appropriate for the consumer to bear the consequences of overdrawing the account. A third exception to the opt-out would allow a bank to assess an overdraft fee in such a situation.
- Proposed Regulation DD requires that the periodic statement provide a monthly and year-to-date aggregate of the overdraft and non-sufficient funds (NSF) fees assessed. We seek clarification regarding how to reflect an overdraft or NSF fee credited in a month following the month it was assessed.<sup>16</sup> For example, assume the December statement reflects one overdraft fee. In January, the bank credits back the overdraft fee. We seek clarification on how the January statement would reflect the monthly and year-to-date aggregate of the overdraft fee in such a situation, assuming no other overdraft fee is assessed during the year.
- As discussed earlier, the Overdraft Guidance applies to overdraft protection programs that are marketed to consumers. We request confirmation that, if adopted, the proposed opt-out notices and responses to questions about the notices would not be deemed "marketing" that would trigger application of the Overdraft Guidance to courtesy coverage of overdrafts.<sup>17</sup>
- To implement the Regulation DD and Regulation AA overdraft rules as proposed, significant changes must occur, including system changes to aggregate fees,

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<sup>16</sup> Regulation DD §230.11(a)(1) comment 6.

<sup>17</sup> Proposed Regulation DD §230.11 would delete the listing of circumstances when communicating with the consumer would not be considered advertising payment of overdrafts. Similar standards may be useful in determining whether the Overdraft Guidance applies to a bank's coverage of overdrafts if opt-out notices are required.

handle opt-outs, and provide the opt-out disclosures and the periodic statement fee disclosures. As such, we request at least a 12 month implementation period.

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As a final matter, we believe that the Board possesses the legal authority under the Truth in Savings Act to implement each of the regulatory requirements articulated in both the Regulation DD and Regulation AA proposals. As such, we would urge the Board to consider utilizing this authority instead of relying on the Federal Trade Commission Act and Regulation AA. Doing so would further simplify and streamline the industry's efforts to comply with these new legal requirements.

Capital One appreciates the opportunity to comment on the Agencies' proposed Regulation DD and related Regulation AA overdraft rules. If you have any questions about this matter or our comments, please call me, Ducie Le, at 703-720-2260.

Sincerely,



Minh-Duc T. Le  
Assistant General Counsel, Policy Analysis