August 5, 2004

Office of the Comptroller of the Currency
250 E Street, SW
Washington, DC 20219
Docket No. 04-14

Jennifer J. Johnson, Secretary
Board of Governors of the Federal Reserve System
20th St. & Constitution Ave., N.W.
Washington, D.C. 20551
Docket No. OP-1198

Robert E. Feldman
Executive Secretary
Federal Deposit Insurance Corporation
550 17th Street, NW
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Regulation Comments
Chief Counsel's Office
Office of Thrift Supervision
1700 G Street, NW
Washington, DC 20552
No. 2004-30

Becky Baker
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National Credit Union Administration
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Re: Interagency Guidance on Overdraft Protection Programs

Dear Ms. Johnson:

The Consumer Bankers Association (CBA)[1] appreciates the opportunity to submit the comments below on

[1] The Consumer Bankers Association is the recognized voice on retail banking issues in the nation's capital. Member institutions are the leaders in consumer financial services, including auto finance, home equity lending, card products, education loans, small business services, community development, investments, deposits and delivery. CBA was founded in 1919 and provides leadership, education, research and federal representation on retail banking issues such as privacy, fair lending, and consumer protection legislation/regulation. CBA members include most of the nation's largest bank holding companies as well as regional and super community banks that collectively hold two-thirds of the industry's total assets.

the proposed issuance of this Interagency Guidance. We are separately submitting comments to the Federal Reserve Board on the parallel proposal, Docket No. OP-1198, for amendments to Regulation DD.

1. **General:**

There is a sense in the Board's proposal that it views the use and marketing of "automated" overdraft systems as intrinsically suspect and undesirable. We disagree with that intimation. As discussed below, automation of overdraft programs is as healthy and as inevitable as the introduction of credit scoring on the underwriting side. There is much less risk of unsafe, inconsistent or discriminatory practices where the payment vs.dishonor decision rests on an empirical basis which automation provides. As for marketing, of course *false and deceptive* claims or practices should be unlawful – and have been under the FTC Act and other federal and state law for decades. We do not believe that providing overt and accurate information about overdraft systems is undesirable, where that information has traditionally been known only to the institutions themselves. The focus of regulatory and enforcement agencies should be on the accuracy of the information.

2. **Scope of coverage:**

CBA's major concern with the proposed Guidance is the same as we have with respect to the Regulation DD amendments,[2] and that is uncertainty about its scope of coverage. These two proposals together would add significant new compliance responsibilities, and before CBA members can interpret and adjust to the Guidance, they need to know what kinds of "programs" or activities are affected.

Fairly read, the Supplementary Materials for both the Guidance and the Regulation DD amendments express concern about some combination of three characteristics of overdraft programs. One is that they are "automated" programs. Two is that they are provided by third-party vendors. Three is that the programs are advertised and marketed to customers, sometimes with overtones of guaranteed overdraft protection. But neither the Guidance nor the Regulation as proposed actually provide a definition of what specific subset of institutional practices is intended to be covered by them.

These three characteristics are by no means adequate, or even accurate, descriptions of the type of service that we assume the regulation and Guidance are intended to cover. First, overdraft handling is "automated" whether or not the institution uses a third-party vendor or markets the program to its customers. The days of an employee in green eyeshade poring over individual overdraft items are long gone. Overdraft payment decisions are commonly made based on reports generated from institutional databases that are more empirically reliable in predicting risk patterns than subjective individualized assessments. Second, it is rare in our experience for third party vendors to provide overdraft services. Third-party vendors, rather than selling overdraft programs, typically act as consultants, assisting institutions in the use of existing, internal reporting systems. The resulting decisions are more sound and consistent than traditional *ad hoc* systems. Singling them out from those institutions which do not rely on vendors does not provide a rational basis for coverage. Lastly, the concept of marketing, alone, does not create the need for special handling, unless it is more clearly linked to the promotion of misleading information (such as a guarantee of repayment). It merely creates the impression that any information that may be provided about the program may be a form of marketing that would trigger the coverage of the Guidance and revised Regulation. At face value, therefore, every one of the approximately 20,000 institutions subject to Regulation DD will have to comply with the new requirements on periodic statements and advertising and to the broad prescription of the Guidance.

Although definitional clarification is more appropriately done in the Regulation and Commentary than in the separate Guidance, the Guidance is less than helpful when the scope and thrust of the Regulation itself is unclear. We recommend that the other agencies work with the Board to define more clearly the scope of both the Regulation and the Guidance.

3. **Safety & Soundness Considerations**

[2] The proposed amendments to Regulation DD would add new disclosures for periodic statements under § 230.6, and would impose new restrictions on advertising concerning certain kinds of overdraft services under § 230.8. There would also be new explanatory Commentary related to the revisions.

The proposed Guidance begins by setting what we believe is a false or at least questionable premise, and that is that overdraft protection programs "expose an institution to more credit risk . . . than . . . traditional overdraft programs because of a lack of individual account underwriting." While there may be more extensive underwriting for a formal line of credit, "traditional," seat-of-the-pants overdraft systems often lacked any semblance of true "underwriting" or credit assessment. Bank officials would make ad hoc judgments on which overdrafts to pay and which to return, often with no more underwriting than the official's intuition. The new, often automated systems draw on a range of institutional and customer information to set benchmarks for when overdrafts should be paid, and up to what dollar limit. We submit that while obviously banks need to be careful of risk exposure, there is no more risk, and perhaps less, in the statistically based – "automated" – overdraft programs than in their predecessors.

Several of our member banks have reviewed their overdraft experience and concluded that charging off uncovered overdrafts in 30 days is premature, and that, in their experience, the percentage of customers who cover the overdraft rises dramatically out to 45 or 60 days. It should be noted that some customers pay overdrafts through monthly automatic deposits, which may not occur within 30 days of the overdraft. If balances must be charged off within 30 days, the consumers will be the worse for it. Requiring formal charge-offs on overdrafts that are likely to be paid creates unnecessary disruption of the account relationship if the account must be closed and a new one established and results in negative information being reported to credit bureaus unnecessarily. We therefore urge that the normal charge-off period be extended to 60 days. Or at least the Guidance should acknowledge that longer than 30 days may be reasonable for banks that can document experience such as the CBA members mentioned above have done.

CBA strongly disagrees with that paragraph of the proposed guidance that begins:

> When an institution routinely communicates the available amount of overdraft protection to depositors, these available amounts should be reported as *"unused commitments"* in regulatory reports. The Agencies also expect proper risk-based capital treatment of outstanding overdrawn balances and *unused commitments*. (Emphasis added.)

The essence of all the overdraft systems of which we are aware is that they remain discretionary with the institution. They are – or should be – marketed with that discretionary character clearly revealed. Non-deceptive disclosure of a cap on overdraft amounts is potentially very useful information to the customer – certainly more useful than the total lack of such disclosure from institutions which maintain internal, but unpublicized, caps. In fact some customers are surprised that the permissible overdraft amount is so modest. If these plans are in fact discretionary, they should not be treated as "commitments," subject to reporting and reserve requirements. The Agencies can't have it both ways. These programs are being addressed under Regulation DD and the Guidance rather than Regulation Z for the correct reason, i.e., that they are not in fact credit commitments. To the extent they are aspects of a deposit account relationship, there is no credit extended until an overdraft is paid.

4. **Legal Risks:**

We do not really quarrel with the proposed guidance concerning legal risks. Institutions that violate the FTC Act standards, or that are not in compliance with other federal laws, ought to be subject to sanctions. We note, however, that the Guidance refers to possibly applicable state laws as well, including usury, criminal laws, and unfair or deceptive practices acts. For national banks and federal thrifts, however, some otherwise applicable state laws may be preempted by virtue of the federal charter. The Guidance may not be the place to address those issues expansively, but it may be useful to acknowledge that state laws affecting overdraft programs may be displaced by federal preemption. This could be particularly relevant where state banking departments issue guidelines or best practices that are different from or more restrictive than this federal Guidance.

5. **Best Practices**:

With respect to the Best Practices segment on "Marketing and Communications With Consumers," we have no quarrel with any of the individual items listed, and we certainly agree that full and honest disclosure and explanation is appropriate. But to do full justice to all the suggested items, in a form the consumer would likely read and understand, could require a substantial brochure or similar publication. That raises the question of costs (which

the customers ultimately pay). It also raises some concern that enhanced disclosure for the overdraft aspect of the account may diminish the effectiveness or impact of other required disclosures – under Regulation Z if there is a credit line, under Regulation E if there are electronic transfer capabilities, and under Regulation CC with respect to funds availability.

In the segment on "Program Features and Operations," we question whether some of the suggested practices are realistic or feasible.

• For example, what would consumers opt into, or out of, under the first bulleted item ("*Provide election or opt-out of service"*)? Should customers be encouraged to demand that the bank *never* pay an overdraft, even for a dollar? What is the customer benefit in that?

• As to bullet 2 ("*Alert consumers before a non-check transaction triggers any fees"*), we expect it would involve a monumental reprogramming chore, and is perhaps impossible, to provide on ATM screens or on merchant authorization terminals an alert that a transaction in process will trigger the overdraft program. The same applies to bullet 3 (*"Prominently distinguish actual balances from overdraft protection funds availability"*), and is complicated further if the customer has an overdraft credit line in place: how many balances should be disclosed?

• We believe many banks already follow the practice described in bullet 4 (*"Promptly notify consumers of overdraft protection program usage each time used"*), but some may notify customers only when a check is returned dishonored – usually a circumstance of more urgency for the customer. We should also note that the requirement to notify the consumer on the same day could be, in many cases, logistically unfeasible. In any case, if the overdraft feature and its cost have been fully disclosed as part of the account documentation, it would seem that consumers ought to have some responsibility to monitor their use of the account within the limits of available funds.

Thank you for considering these comments.

Sincerely,

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Senior Counsel

Ralph J. Rohner
Special Counsel