

**DEPARTMENT OF THE TREASURY**

**Office of Thrift Supervision**

**[Docket ID OTS-2010-0008]**

**Supplemental Guidance on Overdraft Protection Programs**

**AGENCY:** Office of Thrift Supervision, Treasury (OTS).

**ACTION:** Proposed Guidance with request for comment.

**SUMMARY:** OTS is proposing to issue this Supplemental Guidance on Overdraft Protection Programs (Supplemental Guidance) to update the Guidance on Overdraft Protection Programs OTS previously issued on February 18, 2005.

**DATE:** Comments must be submitted on or before **[INSERT DATE 60 DAYS AFTER PUBLICATION IN THE FEDERAL REGISTER]**.

**ADDRESSES:** You may submit comments, identified by OTS-2010-0008, by any of the following methods:

- **E-mail:** [regs.comments@ots.treas.gov](mailto:regs.comments@ots.treas.gov). Please include ID OTS-2010-0008 in the subject line of the message and include your name and telephone number in the message.
- **Fax:** (202) 906-6518.
- **Mail:** Regulation Comments, Chief Counsel's Office, Office of Thrift Supervision, 1700 G Street, NW., Washington, DC 20552, Attention: OTS-2010-0008.
- **Hand Delivery/Courier:** Guard's Desk, East Lobby Entrance, 1700 G Street, NW., from 9 a.m. to 4 p.m. on business days, Attention: Regulation Comments, Chief Counsel's Office, Attention: OTS-2010-0008.

Instructions: All submissions received must include the agency name and docket number for this rulemaking. All comments received will be entered into the docket and posted on Regulations.gov without change, including any personal information provided. Comments, including attachments and other supporting materials received are part of the public record and subject to public disclosure. Do not enclose any information in your comment or supporting materials that you consider confidential or inappropriate for public disclosure.

Viewing Comments Electronically: OTS will post comments on the OTS Internet Site at <http://www.ots.treas.gov/?p=LawsRegulations>.

Viewing Comments On-Site: You may inspect comments at the Public Reading Room, 1700 G Street, NW., by appointment. To make an appointment for access, call (202) 906-5922, send an e-mail to [public.info@ots.treas.gov](mailto:public.info@ots.treas.gov), or send a facsimile transmission to (202) 906-6518. (Prior notice identifying the materials you will be requesting will assist us in serving you.) We schedule appointments on business days between 10:00 a.m. and 4:00 p.m. In most cases, appointments will be available the next business day following the date we receive a request.

**FOR FURTHER INFORMATION CONTACT:** April Breslaw, Director, Consumer Regulations, Compliance and Consumer Protection, (202) 906-6989; or Richard Bennett, Senior Compliance Counsel, Regulations and Legislation Division, (202) 906-7409, Office of Thrift Supervision, 1700 G Street, NW., Washington, DC 20552.

## **SUPPLEMENTARY INFORMATION:**

### **Background**

OTS is proposing to issue this Supplemental Guidance on Overdraft Protection Programs (Supplemental Guidance) to update the Guidance on Overdraft Protection Programs (Overdraft

Guidance) OTS issued February 18, 2005 (70 FR 8428). OTS issued the Overdraft Guidance after notice and comment. See 69 FR 31858 (June 7, 2004).

Through its Overdraft Guidance, OTS explained concerns about how overdraft protection programs had been implemented and suggested Best Practices intended to improve these programs. The Office of the Comptroller of the Currency (OCC), the Board of Governors of the Federal Reserve (Board), the Federal Deposit Insurance Corporation (FDIC), and the National Credit Union Administration (NCUA) issued guidance shortly thereafter containing many of the same Best Practices. See Joint Guidance on Overdraft Protection Programs, 70 FR 9127 (Feb. 24, 2005). Although OTS believes many institutions provide overdraft protection in a responsible manner, those that do not may be violating federal law.

As stated in the preamble to the Overdraft Guidance (74 FR at 8429):

OTS reminds savings associations ... that overdraft protection programs must comply with all applicable Federal laws and regulations. It is important that savings associations have their overdraft protection programs reviewed by counsel for compliance with all applicable laws prior to implementation. As these laws and regulations are subject to amendment, savings associations are reminded to monitor applicable laws and regulations for revisions and to ensure that their overdraft protection programs are fully compliant with them.

Since 2005, the legal landscape has changed considerably. As discussed in detail in the proposed Supplemental Guidance, these changes are particularly evident with respect to Regulation DD (12 CFR pt. 230), which implements the Truth in Savings Act (12 U.S.C. 4301 et seq.), and Regulation E (12 CFR pt. 205), which implements the Electronic Fund Transfer Act (15 U.S.C. 1693 et seq.). The Board has significantly amended Regulation DD twice since 2005

and Regulation E once since 2005 to address overdraft services. See Truth in Savings; Final rule, 70 FR 29582 (May 24, 2005); Truth in Savings; Final rule, official staff commentary, 74 FR 5584 (Jan. 29, 2009); and Electronic Fund Transfers; Final rule, official staff commentary, 74 FR 59033 (Nov. 17, 2009). Most recently, the Board proposed further amendments to Regulations E and DD to clarify certain overdraft issues. See Electronic Fund Transfers; Proposed rule, 75 FR 9120 (March 1, 2010) and Truth in Savings; Proposed rule, 75 FR 9126 (March 1, 2010). As a result, many of the Best Practices addressed in the Overdraft Guidance are now required by law.

Further, since 2005 OTS has articulated the standards that it applies to determine whether an act or practice is unfair or deceptive under section 5 of the Federal Trade Commission Act (FTC Act) (15 U.S.C. 45). See Unfair or Deceptive Acts or Practices; Final rule, 74 FR 5498, 5502-5504 (Jan. 29, 2009) (UDAP final rule). OTS's proposed guidance, if adopted, would conclude that certain overdraft practices violate the FTC Act prohibition against unfair or deceptive acts or practices. The proposed Supplemental Guidance explains these situations in more detail.

### **Discussion of the Supplemental Guidance**

This proposed Supplemental Guidance is designed to complement, rather than replace, the Overdraft Guidance. Accordingly, it does not revisit the safety and soundness concerns addressed in the Overdraft Guidance. Savings associations should continue to provide overdraft protection in conformity with the risk management advice contained in the Overdraft Guidance. In addition, OTS continues to encourage institutions to adhere to the following Best Practices, although the proposed Supplemental Guidance does not restate them:

- Avoid promoting poor account management. The Overdraft Guidance recommended as a Best Practice that a savings association should not market an overdraft program in a

manner that encourages routine or intentional overdrafts. Rather, it indicated that a savings association should present the program as a customer service that may cover inadvertent consumer overdrafts. 70 FR at 8430.

- Train staff to explain program features and other choices. The Overdraft Guidance recommended as a Best Practice that a savings association train customer service or consumer complaint processing staff to explain their overdraft protection program's features, costs, and terms including how to opt out of the service. 70 FR at 8431. It also recommended that staff be able to explain other available overdraft products offered by the savings association and how consumers may qualify for them. Id.
- Alert consumers before a transaction triggers any fees. The Overdraft Guidance recommended as a Best Practice that when consumers attempt to withdraw, transfer, or otherwise access funds made available through an overdraft protection program (other than by check), a savings association should alert consumers that completing the transaction will trigger an overdraft protection fee. Id. It also indicated that a savings association should give consumers an opportunity to cancel the attempted transaction. Id.

The remainder of the Best Practices contained in the Overdraft Guidance would be updated by the proposed Supplemental Guidance. Aside from minor changes in the order in which they have been presented, the proposed Supplemental Guidance is organized into the same broad categories as the Overdraft Guidance: "Marketing and Consumer Communications" and "Program Features and Operation." However, for ease of reference, the following table shows where the Overdraft Guidance Best Practices are addressed in the proposed Supplemental Guidance.

## Organization of Overdraft Guidance vs. Supplemental Guidance

Overdraft Guidance Title	Supplemental Guidance Title and Location
<b><u>Marketing and Consumer Communications</u></b>	
Avoid promoting poor account management.	No change – Best Practice remains in effect.
Fairly represent overdraft protection programs and alternatives.	Fairly represent overdraft protection programs – Part III.A.1.  Provide information about alternatives when they are offered – Part III.A.2.
Train staff to explain program features and other choices.	No change – Best Practice remains in effect.
Clearly explain the discretionary nature of the program.	Same title, updated discussion – Part III.A.3.
Distinguish overdraft protection services from “free” account features.	Same title, updated discussion – Part III.A.4.
Clearly disclose program fees.	Same title, updated discussion – Part III.A.5.
Clarify that fees count against the disclosed overdraft protection dollar limit.	Clarify that fees will reduce the amount of overdraft protection provided – Part III.A.6.
Demonstrate when multiple fees will be charged.	Same title, updated discussion – Part III.A.7.
Do not manipulate transaction-clearing rules.	Same title, updated discussion – Part III.B.3.
Explain the impact of transaction-clearing policies.	Same title, updated discussion – Part III.A.8.
Illustrate the type of transactions covered.	Same title, updated discussion – Part III.A.9.
<b><u>Program Features and Operation</u></b>	
Provide election or opt-out of service.	Provide consumer choice – Part III.B.1.
Alert consumers before a transaction triggers any fees.	No change – Best Practice remains in effect.
Prominently distinguish balances from overdraft protection funds availability.	Disclose account balances in a manner that distinguishes consumer funds from funds made available through overdraft protection – Part III.A.10.
Promptly notify consumers of overdraft protection program usage each time used.	Same title, updated discussion – Part II.A.11.
Consider daily limits on fees imposed.	Reasonably limit aggregate overdraft fees – Part III.B.2.
Monitor overdraft protection program usage.	Same title, updated discussion – Part III.B.4.
Fairly report program usage.	Same title, updated discussion – Part III.B.5.

In addition, the Supplemental Guidance addresses one practice that was not addressed in the Overdraft Guidance. The practice concerns informing consumers when access to overdraft services will be or has been reinstated after suspension. See Part III.A.12 of the proposed Supplemental Guidance.

### **Request for Comment**

OTS requests comment on all aspects of the proposed Supplemental Guidance. OTS specifically requests comment on the following issues:

- Part III.B.2 of the proposed Supplemental Guidance discusses reasonably limiting aggregate overdraft fees but does not provide guidance on reasonable per transaction overdraft fees. We note that section 102 of the Credit Card Accountability Responsibility and Disclosure Act of 2009 (Credit CARD Act), Pub. L. 111-24, 123 Stat. 1734 (2009), provides in the context of credit cards, “The amount of any penalty fee or charge that a card issuer may impose with respect to a credit card account under an open end consumer credit plan in connection with any omission with respect to, or violation of, the cardholder agreement, including any late payment fee, over-the-limit fee, or any other penalty fee or charge, shall be reasonable and proportional to such omission or violation.” Section 102 of Pub. L. 111-24, 123 Stat. 1734 (2009). The Board has issued a proposal to implement that requirement. See Truth in Lending; Proposed rule, 75 FR 12334 (March 15, 2010). Although section 102 and the Board’s proposed rule apply only to penalty fees or charges on certain credit card accounts under open-end consumer credit plans, should OTS’s final guidance include similar standards for overdraft fees on overdraft protection plans?

- Is the relationship between the Overdraft Guidance and the proposed Supplemental Guidance clear?

### **Paperwork Reduction Act**

In accordance with section 3512 of the Paperwork Reduction Act of 1995, 44 U.S.C. 3501-3521 (PRA), OTS may not conduct or sponsor an information collection, and respondents are not required to respond to an information collection, unless it displays a currently valid Office of Management and Budget (OMB) control number.

Comments are invited on:

(a) Whether the collection of information is necessary for the proper performance of OTS's, including whether the information has practical utility;

(b) The accuracy of the estimates of the burden of the information collection, including the validity of the methodology and assumptions used;

(c) Ways to enhance the quality, utility, and clarity of the information to be collected;

(d) Ways to minimize the burden of the information collection on respondents, including through the use of automated collection techniques or other forms of information technology; and

(e) Estimates of capital or start up costs and costs of operation, maintenance, and purchase of services to provide information.

All comments will become a matter of public record. Please follow the instructions found in the **ADDRESSES** caption above for submitting comments.

A copy of the comments may also be submitted to the OMB desk officer for the Agencies: Office of Information and Regulatory Affairs, Office of Management and Budget, New Executive Office Building, Washington, DC 20503.

Title of Information Collection: Supplemental Guidance on Overdraft Protection Programs

OMB Control Numbers: 1550-0NEW

Regulation Requirement: 12 CFR 563.27

Description: Through previous Overdraft Guidance, OTS explained concerns about how overdraft protection programs had been implemented and suggested “Best Practices” intended to improve these programs. Both failure to adhere to certain Best Practices and the emergence of controversial implementation strategies raise the risk that overdraft protection programs have been operated in an unfair or deceptive manner that violates section 5 of the FTC Act and the OTS Advertising Rule. Consequently, OTS is providing this Supplemental Guidance to clarify its supervisory expectations and the application of relevant laws and regulations. The burden associated with this collection of information may be summarized as follows:

Type of Review: New collection

Affected Public: Savings associations

Estimated Number of Respondents: 759

Estimated Time for Developing Disclaimers: 4 hours

Estimated Time for Training: 4 hours

Total Estimated Time Per Respondent: 8 hours

Total estimated annual burden: 6,072 hours

The text of the proposed OTS Supplemental Guidance on Overdraft Protection Programs follows:

## OTS Supplemental Guidance on Overdraft Protection Programs

### I. Background

Most institutions offer consumers a variety of options to avoid overdrawing their deposit accounts. These include providing consumers with lines of credit and permitting consumers to link one account to another. Fee based overdraft programs, in which a flat fee is charged each time that an overdraft is paid, have become common. Overdraft protection has typically been extended for checking, debit card, automated teller machine (ATM), and other deposit account transactions.

Through previous Guidance on Overdraft Protection Programs<sup>1</sup> (Overdraft Guidance), the Office of Thrift Supervision (OTS) explained concerns about how overdraft protection programs had been implemented and suggested “Best Practices” intended to improve these programs. While overdraft protection programs continue to be widely used,<sup>2</sup> new concerns about their implementation have emerged. In addition, both new rules and well-established laws have been applied to these programs. OTS is, therefore, providing this Supplemental Guidance to clarify its supervisory expectations and the application of relevant laws and regulations, although the Overdraft Guidance remains in effect with respect to matters not addressed here.

As discussed in Part III, many of the “Best Practices” covered in the Overdraft Guidance are now mandated. However, even where these practices are not legally required, OTS strongly

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<sup>1</sup> Guidance on Overdraft Protection Programs, 70 FR 8428 (Feb. 18, 2005), issued as CEO Memorandum #211, available at <http://files.ots.treas.gov/25211.pdf>. The other federal banking agencies and the National Credit Union Administration (NCUA) issued guidance shortly thereafter containing many of the same Best Practices. See Joint Guidance on Overdraft Protection Programs, 70 FR 9127 (Feb. 24, 2005).

<sup>2</sup> For example, close to 90% of the institutions recently studied by the Federal Deposit Insurance Corporation (FDIC) had some form of overdraft protection program. See FDIC Study of Bank Overdraft Programs at page 5 (Nov. 2008) (FDIC Overdraft Study), available at [http://www.fdic.gov/bank/analytical/overdraft/FDIC138\\_Report\\_FinalTOC.pdf](http://www.fdic.gov/bank/analytical/overdraft/FDIC138_Report_FinalTOC.pdf).

encourages institutions to implement them as a means of addressing reputation risk.<sup>3</sup> Such risk has intensified due to public concern about the lack of choice, cost, and ways in which some overdraft protection programs have been provided.

Savings associations should review their overdraft programs to confirm that they are being operated in a manner that is effective, compliant with the law, and fair to consumers. To inform the examination process, OTS has added several questions to the Preliminary Examination Response Kit (PERK) that gather information about the way associations manage their overdraft programs. OTS will use this information to determine whether such programs warrant heightened review.

## **II. Legal Developments**

Changes in the legal landscape mean that many of the Best Practices covered in the Overdraft Guidance are now required by law. These changes are particularly evident with respect to Regulation DD,<sup>4</sup> which implements the Truth in Savings Act,<sup>5</sup> and Regulation E,<sup>6</sup> which implements the Electronic Fund Transfer Act.<sup>7</sup>

Although OTS believes that many institutions provide overdraft protection in a responsible manner, the proposed guidance, if adopted, would conclude that institutions that engage in certain overdraft practices violate the prohibition on unfair or deceptive acts or practices in section 5 of the Federal Trade Commission Act (FTC Act).<sup>8</sup> OTS has recently

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<sup>3</sup> Consistent with the “Best Practices” recommended in the Overdraft Guidance, OTS continues to encourage institutions to avoid promoting poor account management, train staff to explain program features and other choices, and alert consumers before a transaction triggers any fees. See 70 FR at 8430-31.

<sup>4</sup> 12 CFR pt. 230.

<sup>5</sup> 12 U.S.C. 4301 et seq.

<sup>6</sup> 12 CFR pt. 205.

<sup>7</sup> 15 U.S.C. 1693 et seq.

<sup>8</sup> 15 U.S.C. 45.

articulated the standards that it applies to determine whether an act or practice is unfair or deceptive under the FTC Act.<sup>9</sup>

Essentially, an act or practice is unfair if: (1) it causes or is likely to cause substantial injury to consumers; (2) the injury is not reasonably avoidable by consumers themselves; and (3) the injury is not outweighed by countervailing benefits to consumers or to competition. While established public policy may be considered, public policy may not serve as the primary basis for a determination that an act or practice is unfair. An act or practice is deceptive if: (1) there is a representation or omission of information that is likely to mislead consumers acting reasonably under the circumstances; and (2) that information is material to consumers. The adoption of these standards provides OTS with a useful method of analyzing whether practices are unfair or deceptive. The other federal financial institution regulatory agencies and FTC take the same approach.<sup>10</sup>

### **III. Specific Overdraft Practices**

#### **A. Marketing and Consumer Communications**

The Overdraft Guidance recommended a number of Best Practices for communicating with consumers. It explained that following such practices can minimize consumer confusion and complaints, foster good customer relations, and reduce legal and compliance risks to the savings association. The following updates that discussion.

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<sup>9</sup> See Unfair or Deceptive Acts or Practices; Final rule, 74 FR 5498, 5502-5504 (Jan. 29, 2009) (UDAP final rule).

<sup>10</sup> Id. (Board of Governors of the Federal Reserve (Board) and NCUA); Board and FDIC, Unfair or Deceptive Acts or Practices by State-Chartered Banks (Mar. 11, 2004), available at <http://www.federalreserve.gov/boarddocs/press/bcreg/2004/20040311/attachment.pdf>; Office of the Comptroller of the Currency (OCC) Advisory Letter 2002-3, Guidance on Unfair or Deceptive Acts or Practices (Mar. 22, 2002), available at <http://www.occ.treas.gov/ftp/advisory/2002-3.doc>; FTC Policy Statement on Unfairness, Letter from the FTC to the Hon. Wendell H. Ford and the Hon. John C. Danforth, S. Comm. on Commerce, Science & Transp. (Dec. 17, 1980), available at <http://www.ftc.gov/bcp/policystmt/ad-unfair.htm>; and FTC Policy Statement on Deception, Letter from the FTC to the Hon. John H. Dingell, H. Comm. on Energy & Commerce (Oct. 14, 1983), available at <http://www.ftc.gov/bcp/policystmt/ad-decept.htm>.

1. Fairly represent overdraft protection programs.

The Overdraft Guidance encouraged savings associations to identify the consequences of extensively using overdraft protection for consumers.<sup>11</sup> The need to do so is heightened where associations target consumers who have experienced financial difficulties. For these consumers, associations should avoid marketing accounts covered by overdraft protection in a manner that leaves the impression that the accounts are designed to help avoid future financial challenges, especially when contrary information is omitted. For example, it would be a material misrepresentation to market an account as particularly suitable for those with prior credit or bank account problems without informing consumers of significant overdraft fees associated with an account. As consumers who have had problems with their bank account in the past may be particularly likely to overdraw their accounts in the future, such fees may be likely to lead to significant expenses for them. Failing to provide such consumers with fee information appears to significantly impair their ability to determine whether an account meets their needs. Consequently, these circumstances violate the FTC Act prohibition against deceptive practices. For similar reasons, they also violate OTS's Advertising Rule.

2. Provide information about alternatives when they are offered.

The Overdraft Guidance recommended that, when informing consumers about an overdraft protection program, associations should also provide general information about other overdraft services or credit products, if any, that the associations offers.<sup>12</sup> Such information should address how the terms, including fees, for these services or products differ. For example, research indicates that most institutions offer overdraft protection through linked accounts or

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<sup>11</sup> 70 FR at 8431.

<sup>12</sup> 70 FR at 8430-31.

lines of credit,<sup>13</sup> and fees for such arrangements are typically lower than for automated overdraft programs.<sup>14</sup> OTS continues to recommend providing information about these services as a Best Practice.

An affordable small dollar term loan might also serve as an alternative to fee based overdraft protection. If an institution chooses to provide such credit, it may consider guidelines on affordable small dollar loans that the FDIC has developed.<sup>15</sup> Research indicates that institutions that employ these guidelines have been able to offer affordable small dollar loans that meet multiple business goals, including building long term customer relationships, cross selling additional products, and creating goodwill in the community.<sup>16</sup>

### 3. Clearly explain the discretionary nature of the program.

The Overdraft Guidance encouraged savings associations to make clear, where applicable, that the payment of an overdraft is discretionary.<sup>17</sup> Consistent with this advice, Regulation DD has since been interpreted to prohibit a financial institution from representing that it will honor all checks or authorize the payment of all transactions that overdraw an account, when the institution retains discretion at any time not to honor checks or authorize transactions.<sup>18</sup> Pursuant to Regulation DD, any advertisement promoting the payment of

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<sup>13</sup> See FDIC Overdraft Study at page 5 (finding that 62.1% of studied banks offered linked accounts and 50.1% of studied banks offer lines of credit).

<sup>14</sup> For example, according to the FDIC Overdraft Study, almost half of the banks studied with linked-account programs (48.9%) reported charging no explicit fees for the service. The most common fee associated with linked-account programs was a transfer fee; where charged, the median transfer fee was \$5. The primary cost associated with overdraft line of credit programs was the interest charged on funds advanced, usually accruing at an annual percentage rate (APR) of around 18 percent. FDIC Overdraft Study at page iii.

<sup>15</sup> FDIC Affordable Small-Dollar Loan Guidelines, FIL-50-2007 (June 19, 2007), available at <http://www.fdic.gov/news/news/financial/2007/fil07050.pdf>.

<sup>16</sup> See “The FDIC’s Small-Dollar Loan Pilot Program: A Case Study after One Year,” FDIC Quarterly 2009, Vol. 3, No. 2, available at [http://www.fdic.gov/bank/analytical/quarterly/2009\\_vol3\\_2/smalldollar.html](http://www.fdic.gov/bank/analytical/quarterly/2009_vol3_2/smalldollar.html).

<sup>17</sup> 70 FR at 8431.

<sup>18</sup> 12 CFR pt. 230, Supp. I, Comment 230.8(a) -10(ii) (interpreting § 230.8(a)).

overdrafts must also now clearly disclose the circumstances under which the institution will not pay an overdraft.<sup>19</sup>

#### 4. Distinguish overdraft protection programs from “free” account features.

The Overdraft Guidance discouraged savings associations from promoting free accounts and overdraft protection programs in the same advertisement in a way that suggests that overdraft protection is provided free of cost.<sup>20</sup> Regulation DD’s prohibition against misleading or inaccurate advertising has since been interpreted in a manner that essentially bans this practice. Specifically, Regulation DD has been interpreted to ban marketing an account-related service for which the institution charges a fee – such as overdraft protection – in an advertisement that also describes the account as “free” or “no cost” (or a similar term), unless the advertisement clearly and conspicuously indicates that there is a cost associated with the service.<sup>21</sup> In addition, Regulation DD now prohibits institutions from advertising an account as “free” where any maintenance or activity fee may be imposed on it.<sup>22</sup>

Moreover, it would be a material misrepresentation to use marketing that focuses on account features that are “free” or inexpensive, but omits information about the cost of each overdraft transaction. This is particularly true when consumers have been automatically enrolled in programs that charge a significant fee for each overdrawn transaction. The net impression of such marketing may be to mislead consumers acting reasonably under the circumstances to believe that the total cost of the account (including overdraft protection) is free or inexpensive and to be unaware that engaging in overdraft transactions will result in the assessment of

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<sup>19</sup> 12 CFR 230.11(b)(1)(iv).

<sup>20</sup> 70 FR at 8431.

<sup>21</sup> 12 CFR pt. 230, Supp. I, Comment 230.8(a)-10(v) (interpreting § 230.8(a)).

<sup>22</sup> 12 CFR 230.8(a)(2) and 12 CFR pt. 230, Supp. I, Comment 230.8(a)-10(v).

significant overdraft fees. Consequently, these circumstances violate the FTC Act prohibition against deceptive practices. For similar reasons, they also violate OTS's Advertising Rule.

Although not discussed in the Overdraft Guidance, associations should also be cautious about representing overdraft protection as "free" when it is only provided for accounts with higher costs for other services or less favorable terms. Such a situation might occur when "free" overdraft protection is provided only for accounts with increased maintenance fees or for accounts that pay lower deposit interest rates. Although a reasonable consumer may be misled into believing that the "free" overdraft protection was being provided at no cost, the consumer would essentially pay for the program through increased fees or a lower return, compared to other accounts offered by that association.<sup>23</sup> This kind of misrepresentation is material because it may affect the consumer's decision to select the account with "free overdraft protection" over another type of account. Consequently, these circumstances violate the FTC Act prohibition against deceptive practices. For similar reasons, they also violate OTS's Advertising Rule.

#### 5. Clearly disclose program fees.

The Overdraft Guidance encouraged savings associations to disclose the dollar amount of the fee for each overdraft and any interest rate or other fee that may apply.<sup>24</sup> After the Overdraft Guidance was issued, Regulation DD was amended to require that institutions that promote overdraft protection provide periodic deposit account statements that include a total dollar amount for all fees or charges imposed on the account for paying overdrafts.<sup>25</sup> These disclosures

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<sup>23</sup> Cf. Federal Trade Commission's Guide Concerning Use of the Word "Free" and Similar Representations, 16 CFR 251.1 ("[W]hen the purchaser is told that an article is 'Free' to him if another article is purchased, the word 'Free' indicates that he is paying nothing for that article and no more than the regular price for the other. Thus, a purchaser has a right to believe that the merchant will not directly and immediately recover, in whole or in part, the cost of the free merchandise or service by marking up the price of the article which must be purchased, by the substitution of inferior merchandise or service, or otherwise.")

<sup>24</sup> 70 FR at 8431.

<sup>25</sup> Truth in Savings: Final rule, 70 FR 29582, 29593 (May 24, 2005) (promulgating § 230.11(a)).

were required for both the statement period and the calendar year-to-date.<sup>26</sup> Recently, Regulation DD was further revised to require these disclosures by all institutions, not just those that promote overdraft protection.<sup>27</sup>

6. Clarify that fees will reduce the amount of overdraft protection provided.

The Overdraft Guidance recommended that savings associations alert consumers that the fees charged for covering overdrafts, as well as the overdraft items themselves, will be subtracted from the overdraft protection limit disclosed.<sup>28</sup> Failing to explain the treatment of such fees is deceptive. Such an omission may mislead a reasonable consumer into believing that a more substantial amount of overdraft protection is available for use than is actually available. Such an omission is material because it may affect the consumer's decision about whether to engage in a transaction that would overdraft the account. For example, the consumer might believe that a transaction may be covered by overdraft protection when it would not because fees had eroded the limit available. Consequently, these circumstances violate the FTC Act prohibition against deceptive practices. For similar reasons, the omission of information on how fees affect overdraft limits also violates OTS's Advertising Rule.

7. Demonstrate when multiple fees will be charged.

The Overdraft Guidance recommended that savings associations promoting overdraft protection programs clearly disclose that more than one overdraft fee may be charged against the account each day, depending on the number of items presented for withdrawal from the consumer's account.<sup>29</sup> Omitting such information is deceptive, whether a savings association

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<sup>26</sup> Id. Further, as previously discussed in Part III.A.3, after the Overdraft Guidance was issued, Regulation DD was revised to provide that any advertisement promoting the payment of overdrafts must clearly disclose the circumstances under which the institution will not pay an overdraft. 12 CFR 230.11(b)(1)(iv).

<sup>27</sup> Truth in Savings: Final rule, official staff commentary, 74 FR 5584, 5593 (Jan. 29, 2009) (amending § 230.11(a)). This provision took effect on January 1, 2010.

<sup>28</sup> 70 FR at 8431.

<sup>29</sup> Id.

promotes overdraft protection, or not. Such an omission may mislead a reasonable consumer into believing that only one overdraft fee will be charged against an account each day. Such an omission is material because it may affect a number of consumer decisions, including whether to open an account in the first place, or whether to later engage in more than one transaction that overdraws an account on a specific day. Consequently, such an omission violates the FTC Act prohibition against deceptive practices. For similar reasons, such an omission also violates OTS's Advertising Rule.

8. Explain the impact of transaction-clearing policies.

The Overdraft Guidance encouraged savings associations to clearly explain to consumers that transactions may not be processed in the order in which they occur and that the order in which transactions are processed and cleared can affect the total amount of overdraft fees incurred by a consumer.<sup>30</sup> The Overdraft Guidance also recommended that associations clearly disclose their processing and clearing policies.<sup>31</sup>

Omitting such information is deceptive. Such an omission may mislead reasonable consumers to believe that transactions will be processed in the order in which they have occurred. The omission is material because it may affect a consumer's decision about when to engage in transactions to minimize or avoid overdrafts. Consequently, the omission violates the FTC Act prohibition against deceptive practices. For similar reasons, such an omission also violates OTS's Advertising Rule.

9. Illustrate the type of transactions covered.

The Overdraft Guidance recommended that savings associations clearly explain to consumers that overdraft protection fees may be imposed on transactions such as ATM

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<sup>30</sup> Id.

<sup>31</sup> Id.

withdrawals, debit card transactions, preauthorized automatic debits, telephone-initiated transfers, or other electronic transfers, if applicable, to avoid implying that check transactions are the only transactions covered.<sup>32</sup>

Since the Overdraft Guidance was issued, Regulation DD has been interpreted to expressly address this practice. This rule is now interpreted to prohibit advertisements that describe an institution's overdraft service solely as protection for overdrawn checks, when the institution also provides overdraft protection when an account is overdrawn by other means, such as ATM withdrawals, debit card transactions, or other electronic fund transfers.<sup>33</sup>

10. Disclose account balances in a manner that distinguishes consumer funds from funds made available through overdraft protection.

The Overdraft Guidance discouraged savings associations that provide consumers with a single deposit account balance from including overdraft protection funds in the balance.<sup>34</sup> Instead, the Overdraft Guidance advised associations to disclose only a consumer's own funds available for withdrawal. The Overdraft Guidance encouraged associations to separately and prominently identify the balance that does not include overdraft protection, if more than one balance is provided.<sup>35</sup>

Regulation DD has recently been amended to require that where an institution discloses balance information through an automated system, it must disclose a balance that excludes funds that the institution provides to cover overdrafts through a discretionary overdraft protection service, line of credit, or linked account.<sup>36</sup> Institutions are permitted to provide another balance that includes these funds, so long as they prominently disclose the types of funds that have been

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<sup>32</sup> Id.

<sup>33</sup> 12 CFR pt. 230, Supp. I, Comment 230.8(a)-10(iv) (interpreting § 230.8(a)).

<sup>34</sup> 70 FR at 8431.

<sup>35</sup> Id.

<sup>36</sup> 74 FR at 5593 (promulgating § 230.11(c)). This provision took effect on January 1, 2010.

included.<sup>37</sup> Consistent with the Overdraft Guidance, OTS continues to encourage associations to make use of this approach whenever account balances are disclosed, not just when automated systems are employed.

11. Promptly notify consumers of overdraft protection program usage each time used.

The Overdraft Guidance advised savings associations to “promptly notify consumers of overdraft protection program usage each time used.”<sup>38</sup> Failing to do so – including failing to provide a consumer with the information necessary to return the account to a positive balance – is deceptive. Such omissions may mislead a reasonable consumer into assuming that an account is in balance, when it is not. The omissions are material because this type of information would likely influence decisions about whether to proceed with additional transactions or replenish a deposit account first. Prompt notification is important because the shorter the time that elapses between the occurrence of an overdraft and consumer notification that overdraft protection has been accessed, the more benefit a consumer derives from the information. This is because the notification may prevent a consumer from incurring further overdrafts, as well as alert a consumer of the need to replenish funds in the underlying deposit account.<sup>39</sup> Consequently, such omissions violate the FTC Act prohibition against deceptive practices. For similar reasons, they also violate OTS’s Advertising Rule. Where technologically feasible to do so, real time notification should be provided.

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<sup>37</sup> Id.

<sup>38</sup> 70 FR at 8431.

<sup>39</sup> According to the FDIC Overdraft Study, about one-fourth of the banks it surveyed (24.6%) assessed fees on accounts that remained in negative balance status in the form of flat fees or interest charged on a percentage basis. FDIC Overdraft Study at page iii.

12. Inform consumers when access to overdraft services will be or has been reinstated after suspension.

Although not discussed in the Overdraft Guidance, it is deceptive to fail to notify consumers about the circumstances in which overdraft protection may be reinstated after suspension, e.g., when a deposit clears the outstanding overdraft and fee balance. Failure to provide this information, particularly when a consumer has been previously notified that overdraft protection has been suspended, may lead a reasonable consumer to believe that overdraft protection will definitely not be available, when in fact, it is or may be available. As a result, a consumer may overdraw an account without appreciating that significant overdraft fees may result. For example, a consumer may attempt a point of sale transaction believing that it will be denied without charge if sufficient funds are not available. However, if overdraft protection has been reinstated and the transaction is paid despite insufficient funds, the consumer would be charged potentially significant overdraft fees. Consequently, failure to clearly and conspicuously notify a consumer about the circumstances in which overdraft protection may be reinstated after suspension violates the FTC Act prohibition against deceptive practices. For similar reasons, the failure also violates OTS's Advertising Rule.

B. Program Features and Operation

The Overdraft Guidance also recommended a number of Best Practices on the manner of providing overdraft protection. As the Overdraft Guidance noted, "appropriate management oversight of the program [is] fundamental to enabling responsible use of overdraft protection."<sup>40</sup> The following updates that discussion.

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<sup>40</sup> 70 FR at 8430.

## 1. Provide consumer choice.

A longstanding concern about overdraft protection is the lack of consumer choice. In response to this concern, the Overdraft Guidance encouraged institutions to “obtain affirmative consent of consumers to receive overdraft protection.”<sup>41</sup> Since then, the Board has revised Regulation E to partially address this practice.<sup>42</sup> When compliance is required on July 1, 2010, institutions will not be permitted to assess an overdraft fee for paying automated teller machine (ATM) withdrawals and one-time debit card transactions that overdraw a consumer’s account, unless the consumer affirmatively “opts in” to the institution’s payment of overdrafts for these transactions.

The revision to Regulation E will address opt-in for certain electronic transactions, which account for the largest share of overdraft transactions.<sup>43</sup> OTS recommends as a Best Practice, however, that associations also provide their customers with the opportunity to affirmatively choose or “opt in” to overdraft protection for transactions outside the scope of Regulation E’s opt-in requirement.<sup>44</sup> Checking and ACH transactions fall into this category. Using an “opt in”

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<sup>41</sup> Id. at 8431.

<sup>42</sup> Electronic Fund Transfers; Final rule, official staff commentary, 74 FR 59033, 59052 (Nov. 17, 2009) (promulgating § 205.17).

<sup>43</sup> According to the FDIC Overdraft Study, point of sale and debit transactions account for 41% of overdraft transactions at banks studied with automated programs. FDIC Overdraft Study at page 78. Further, debit transactions at banks studied with automated programs are generally small – around \$20 – while the typical \$27 overdraft fee often exceeds the value of the transaction. FDIC Overdraft Study at page 79 and n.51. According to a Center for Responsible Lending report, debit card transactions (either at the point of sale or ATM) cause 46% of total overdrafts, while checks trigger just 27%, while the average overdraft fee for a point of sale or ATM transaction is \$34. See Eric Halperin, Lisa James & Peter Smith, Debit Card Danger: Banks offer little warning and few choices as customers pay a high price for debit card overdrafts (CRL Debit Card Danger Report), Center for Responsible Lending (January 25, 2007) at 7-8, available at <http://www.responsiblelending.org/overdraft-loans/research-analysis/Debit-Card-Danger-report.pdf>.

<sup>44</sup> In some circumstances, the Overdraft Guidance also endorsed a different approach – automatically providing overdraft protection, but offering consumers the opportunity to “opt out” of it. However, such an approach will soon be impermissible for ATM and one-time debit card transactions under Regulation E. Further, since the Overdraft Guidance was issued, questions have been raised about the value of an “opt out” strategy for consumers. See, e.g., 74 FR at 59038 (“Due to various factors such as consumer inertia and the difficulty in anticipating future costs, consumers may end up with suboptimal outcomes even when given a choice.”); U.S. Gov’t Accountability Office, Credit Cards: Increased Complexity in Rates and Fees Heightens Need for More Effective Disclosures to Consumers (Sept. 2006) at 26-27, available at <http://www.gao.gov/new.items/d06929.pdf> (indicating that although state laws

approach to such transactions means that consumers who decline to consent to the payment of overdraft items will occasionally incur both a merchant fee and an insufficient funds fee for a returned item. However, as explained in Part III.B.2, research indicates that the large majority of overdraft fees are paid by a small portion of consumers who frequently overdraw their accounts. These consumers may have difficulty both repaying overdraft fees and bringing their accounts current, which may in turn cause them to incur additional overdraft fees. An opt-in approach could therefore ensure that these consumers make an informed, affirmative choice about whether to enroll in an overdraft protection program that could result in material overdraft fees unless sound account management is exercised.

## 2. Reasonably limit aggregate overdraft fees.

Research suggests that a relatively small number of consumers pay most of the overdraft fees incurred. For example, the FDIC Overdraft Study found that while 87% of consumers have less than five overdrafts per year, consumers that have more than five overdrafts annually pay over 90% of the total overdraft fees reported.<sup>45</sup> The Overdraft Guidance helped address this problem by advising institutions to consider providing a daily cap on the overdraft fees charged against any one account.<sup>46</sup>

Historically, OTS and its predecessor agency, the Federal Home Loan Bank Board (FHLBB), have indicated in rules<sup>47</sup> and legal opinions<sup>48</sup> that fees charged by savings associations are to be “reasonable.” Indeed, going back at least 30 years the position of the

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applying to four of the six largest credit card issuers require them to provide consumers with the opportunity to “opt-out” of retroactive rate increases, few consumers exercise that right).

<sup>45</sup> FDIC Overdraft Study at page iv.

<sup>46</sup> 70 FR at 8431.

<sup>47</sup> See, e.g., 12 CFR 550.380 (“If the amount of your compensation for acting in a fiduciary capacity is not set or governed by applicable law, you may charge a reasonable fee for your services.”) and 12 CFR 533.6, 563e.27, 563e.43 (savings associations may charge reasonable copying and mailing fees).

<sup>48</sup> See, e.g., FHLBB Op. Deputy Gen. Counsel (Oct. 22, 1986), available at 1986 FHLBB LEXIS 98 (“It is also our view that acceptance of reasonable fees for permissible activities is authorized for Federal associations.”).

agency has been that “a practice of charging grossly unreasonable fees might be objectionable as unsafe or unsound.”<sup>49</sup>

In some circumstances, failure to impose a reasonable limit on aggregate overdraft fees is an unfair practice under the FTC Act. The risk of engaging in an unfair practice is heightened when an association fails to limit fees for consumers who frequently overdraw their accounts and, as a result, such consumers incur substantial injury in the form of unreasonable and excessive overdraft fees. Depending on the circumstances, these consumers may not be able to avoid the harm caused by high overdraft fees. For example, where overdraft protection is marketed deceptively, consumers may lack the information needed to make a reasonable choice among programs. Regardless of how overdraft protection is promoted, those who frequently overdraw accounts may simply not have other options in the market, as they may have credit histories and other characteristics that prevent them from obtaining less expensive services. Notably, younger consumers and those with lower incomes tend to exhibit a pattern of recurring overdrafts and a high volume of fees.<sup>50</sup> While some consumers may benefit from the occasional use of overdraft protection, the harm caused by high fees outweighs this benefit for consumers who frequently overdraw their accounts. Two of the circumstances in which the harm may particularly outweigh the benefit are where consumers' aggregate overdraft fees exceed the average daily balance of their accounts or the overdraft limit on their accounts. Based on OTS supervisory experience, most institutions do not provide overdraft protection in a manner that permits overdraft fees to reach such levels. However, when fees become excessive, consumers may have difficulty both repaying overdrafts and bringing accounts current, which may cause them to incur additional fees.

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<sup>49</sup> FHLBB Op. Acting Gen. Counsel (1980), [available at](#) 1980 FHLBB LEXIS 274.

<sup>50</sup> FDIC Overdraft Study at pages 77-79.

Aside from imposing a reasonable limit on overdraft fees, associations should also monitor customer usage of overdraft protection. This strategy is discussed below. Where use becomes excessive, associations should either limit it or offer consumers any lower cost services that may be available, as previously discussed in Parts III.A.1 and III.A.2.

### 3. Do not manipulate transaction-clearing rules.

The Overdraft Guidance warns savings associations, “Transaction-clearing rules (including check-clearing and batch debit processing) should not be administered unfairly or manipulated to inflate fees.”<sup>51</sup> Such a situation would occur if, for example, a savings association varied its transaction-clearing rules on a daily, customer-by-customer basis in order to maximize each customer’s fees. Where consumer accounts lack a sufficient balance, such a practice could cause consumers substantial injury in the form of unnecessary fees. Because consumers have no control over the order in which an institutions clears transactions and would not know which transaction clearing rule would be applied to any given transaction, this is a harm that consumers cannot avoid. While manipulating transaction-clearing order to inflate fees could increase an institution’s fee income, it would not benefit consumers. Moreover, such fee generation not only fails to benefit the market, it suggests a lack of transparency: economically rational consumers would likely move their accounts to other institutions if they understood that their transactions were being posted in an unfair manner. Consequently, manipulating transaction clearing in this way violates the FTC Act prohibition against unfair practices. Instead of operating an overdraft protection program in this manner, a savings association should establish consistent transaction clearing rules for similar accounts.

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<sup>51</sup> 70 FR at 8431.

#### 4. Monitor overdraft protection program usage.

The Overdraft Guidance notes the importance of monitoring overdraft protection usage as both a safety and soundness consideration and a Best Practice.<sup>52</sup> Where an association informs consumers that their usage will be held to specific limits, it is critical that the association monitor how the program is implemented as consumers are likely to rely on such representations. Such monitoring may identify excessive consumer usage of overdraft protection, which may indicate a need for alternative arrangements or other services.<sup>53</sup>

#### 5. Fairly report program usage.

The Overdraft Guidance advises savings associations against furnishing negative information to credit reporting agencies (CRAs) when overdrafts have been paid under the terms of an overdraft protection program.<sup>54</sup> This advice was provided pursuant to the Fair Credit Reporting Act, which has long prohibited furnishing consumer information to a CRA that is known or reasonably believed to be inaccurate.<sup>55</sup> Savings associations should also be cognizant of new rules issued by OTS and other agencies effective July 1, 2010. These rules will require, among other things, that each furnisher establish and implement written policies and procedures regarding the accuracy and integrity of the information that it furnishes to a CRA.<sup>56</sup> Each furnisher must consider agency guidelines, which include, as an objective, furnishing consumer account information that is accurate.<sup>57</sup> In this context, “accuracy” means that the furnished information reflects the terms of the account and the consumer’s performance and other conduct

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<sup>52</sup> 70 FR at 8430-31.

<sup>53</sup> See Part III.A.2.

<sup>54</sup> 70 FR at 8431.

<sup>55</sup> See 15 U.S.C. 1681s-2(a)(1)(A).

<sup>56</sup> Procedures to Enhance the Accuracy and Integrity of Information Furnished to Consumer Reporting Agencies under Section 312 of the Fair and Accurate Credit Transactions Act, 74 FR 31484, 31520 (July 1, 2009) (promulgating § 571.42(a)).

<sup>57</sup> See 74 FR at 31520 (promulgating § 571.42(b)) and 74 FR at 31521 (promulgating paragraph I.(b)(1) of Appendix E to pt. 571).

with respect to the account.<sup>58</sup> Furnishing negative information to CRAs when overdrafts are paid under the terms of an overdraft protection program may not be accurate because such information may not reflect the terms of the account or the consumer's performance and other conduct with respect to the account.

#### **IV. Conclusion**

Overdraft protection programs can provide a service that consumers value. However, these programs pose a number of operational risks. OTS expects institutions under its jurisdiction to manage these risks in a responsible manner and comply with applicable laws and regulations.

This concludes the text of the proposed OTS Supplemental Guidance on Overdraft Protection Programs.

Dated:

By the Office of Thrift Supervision

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**John E. Bowman,**  
*Acting Director.*

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<sup>58</sup> See 74 FR at 31520 (promulgating § 571.41(a)) and 74 FR at 31521 (promulgating paragraph I.(b)(1) of Appendix E to pt. 571).