Overdrawn: Consumers Face Hidden Overdraft Charges From Nation’s Largest Banks

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Introduction

Consumers with depository accounts at financial institutions are at increasing risk of paying expensive penalty fees for overdrawn accounts due to a convergence of changes in law, electronic processing of transactions, and the decision by many banks to permit, and sometimes encourage, consumers to overdraw their accounts and incur penalty fees. Banks increasingly earn profits from penalty fees charged to consumers who run out of money in their checking accounts before payday. One analyst estimates that consumers paid $33 billion in insufficient funds and overdraft fees to all depository institutions in 2003.1 And the fees banks charge for bounced checks are on the rise. Bankrate.com reports a 5 percent jump in insufficient funds fees in just the last six months.2

Smaller institutions are more likely to market and promote their bounce protection as a “courtesy” service, using programs marketed by bank industry consultants, often in combination with “Free Checking.” In 2003, CFA and the National Consumer Law Center documented the fast-spreading adoption of “courtesy overdraft,” or “bounced check loan” programs, especially at smaller financial institutions.3 In January 2003, at least 1,000 banks had these bounce protection or courtesy overdraft programs or policies; sixteen months later, nearly 3,000 banks offered them.4

While the promotional vigor of smaller depository institutions has received the most regulatory, media and to a lesser extent consumer group attention, larger financial institutions include discretionary bounce protection in their checking account disclosures which are not promoted and not subject to new federal Truth in Savings regulation

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marketing rules. Larger financial institutions are more likely to quietly cover overdrafts with disclosures in the fine print of account agreements. Large institutions use internal systems that automate decisions on honoring overdrafts, expecting customers to learn through experience that overdrafts will be honored, rather than actively marketing “overdraft protection.”

**CFA Big Bank NSF and Overdraft Fee Survey**

Consumer Federation of America surveyed 33 of the nation’s largest financial institutions with checking accounts with 35,151 branches and $2.8 trillion in deposits (or 51.7% of U.S. deposits) and found that overdraft loan programs are common at the country’s largest financial institutions. At least 27 institutions have courtesy overdraft provisions written into the fine print of their account agreements that say that the bank may or may not, at its discretion, cover debits to checking accounts that would overdraw the account. The fees for these “courtesy” services are high, do not require the consent of depositors, and can be applied to many more transactions than to the paper checks that the traditional discretionary courtesy overdraft practice was meant to address. Moreover, fee revenue from overdraft services was significant even for the largest banks.

**Overdrafts Harder to Avoid Due to Electronic Processing of Transactions**

Both insufficient funds (NSF) and overdraft fees have become more common because of changes in the banking industry and the increased application of these fees to more transactions. The flow of funds out of bank accounts has accelerated due to electronic check conversion at the cash register or lockbox, and faster processing of withdrawals brought on by Check 21, the new federal law that removed the “float” that some cash-strapped consumers took for granted. Although Check 21 accelerated the processing of withdrawals, time delays in processing consumers’ deposits were left in place, making a cascade of penalty fees even more likely.

Now that electronic transactions exceed paper checks, banks have found a new way to maximize the revenue from bounced checks by permitting consumers to overdraw accounts electronically at the ATM, using a debit card at a retailer’s point of sale, and through preauthorized debits. An industry consultant points out that electronic transactions have contributed to the doubling of overdraft volume in the last ten years and

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6 CFA surveyed the fifty largest depository institutions as listed by the Federal Deposit Insurance Corporation (FDIC) Summary of Deposits database. The list of fifty individual depository institutions was reduced to 33 by consolidating affiliates, taking mergers and acquisitions into account, eliminating three institutions without checking accounts, and disregarding an institution in the midst of a merger for which CFA could obtain no fee information. See methodology on page 24.
7 Woodstock Institute surveyed seven large banks in Chicago in 2004 and found that all banks provide a bounced loan overdraft product permitting ATM, POS, and internet transactions to overdraw bank accounts for a per item fee ranging from $25 to $30 per incident. See Westrich, Tim and Malcolm Bush, Woodstock Institute, “Banking on Bounced Checks: Federal Proposal on Bounce Protection Still Exposes Consumers to Hidden Bank Fees,” Reinvestment Alert, No. 26, October 2004.
notes that consumers are unable to respond fast enough on the deposit side of bank account management to keep up with the faster velocity of transactions that withdraw funds from accounts.\(^9\)

**Bounced Check (NSF) vs. Overdraft Fees**

Consumers are familiar with bounced check fees. Banks charge penalty fees if a paper check presented for payment to a retailer exceeds the balance in the account and is returned to the retailer unpaid. This is called an insufficient check and the penalty fee is a non-sufficient funds (NSF) charge, which typically ranges from $17 to $35 per incident.\(^10\) Most consumers are less familiar with banks paying their checks (or other debits) even if the transaction exceeds their balance. If banks choose to cover a withdrawal (check, ATM, POS or electronic transfer) that would overdraw a bank account, a similar overdraft (OD) fee is charged. Some banks add a sustained overdraft fee if the overdraft is not repaid immediately. Banks claim their NSF fees are intended to discourage “misuse” of bank accounts by consumers who write checks without enough money on deposit to cover checks.\(^11\)

**Real Overdraft Protection**

In the past, consumers could avoid penalty fees from bouncing checks by affirmatively choosing an overdraft protection option for their checking accounts. Consumers who apply for bank lines of credit must be reasonably credit-worthy. Consumers ask for these services, the programs are governed by a contract between the depositor and the institution which guarantees that overdrafts will be paid, and consumers can repay extensions of bank credit with affordable installment payments.

The three most common forms of overdraft protection use a linked savings account, a credit card or a line of credit from the bank (often secured by a home equity line on the depositor’s mortgaged home) to cover any possible shortfalls in a depositor’s account. A bank will transfer money from another account for a small fee, apply the overdraft balance to a linked credit card, or advance the overdraft amount from a line of credit for either a small fee and/or a predetermined interest rate. Sometimes these programs require annual or monthly fees as well.

Banks have traditionally covered the occasional inadvertent overdraft for customers on an ad hoc basis for the bank’s best customers (those with long histories at the bank or those who routinely held high balances), imposing overdraft penalty fees but paying the check that would have otherwise bounced.\(^12\) While banks continue to offer real overdraft

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\(^9\) Stoneman, quoting Alex Shushenoff’s Giltner, at 4.
\(^10\) Stoneman at 2, quoting comments filed by John M. Floyd & Associates.
\(^11\) Feddis, Nessa, American Bankers Association, Letter to CFA and Consumers Union, September 10, 2004 on implementation of Check 21, included this statement: “An overdraft fee serves as a deterrent to keep customers from bouncing checks — much like a parking ticket.”
\(^12\) Bill Stoneman, “Sizing NSF-Related Fees,” BAI Banking Strategies, Jan/Feb. 2005, p. 1. “Banks traditionally levied a fee when customers overdrew their checking accounts. They honored checks on occasion, depending upon their comfort that the customer was good for the funds.”
protection, the quaint notion that a bank manager makes individual decisions to cover overdrafts as a discretionary service is no longer the way business is done.

“Courtey” Overdraft Services

Banks now provide a new method of handling overdrafts. Financial institutions, often using a third-party vendor, began promoting “courtesy overdraft” or “bounce protection,” which relies on the bank, credit union or savings and loan to pay overdrafts for depositors at the discretion of the depository institution. Depositors are required to pay a penalty overdraft fee but because the financial institution covers the check, depositors avoid paying a bounced check fee to the retailer. Instead of discouraging consumers from writing checks that overdrew accounts, banks and their consultants encourage overdrafts as a form of credit, offered as a “courtesy” without affirmative choice, credit underwriting, disclosure of comparable credit costs, or a contract committing the bank to cover overdrafts. Banks, using these non-contractual overdraft services, may cover any individual overdraft but reserve the right to refuse to cover any overdraft, maintaining that payment is discretionary on the part of the bank. Consumers who write checks that will overdraw their account do not know for a certainty that their bank will honor the overdraft.

Often consumers who overdraw at the ATM or point of sale get no warning that the transaction will overdraw the account and incur a penalty fee. Consumers who do not expect to be allowed to withdraw more funds than are on deposit believe bank policies that permit overdrafts with a debit card are unfair. A 2004 survey poll of a representative sample of 1,000 adult Americans conducted for CFA by Opinion Research Corporation International found that an overwhelming majority (82%) of consumers thought permitting overdrafts without any notice at the ATM was unfair, with 63% saying it was “very unfair.” Fewer than one in five (17%) people thought it was fair.

More than nine out of ten banks now have some form of non-contractual overdraft provisions – either marketed or hidden in the fine print of their account disclosures – and only eight percent of banks do not allow overdrafts.13

Bank Overdraft Loans Made Without Consumer Consent

Consumers think they should be provided the opportunity to affirmatively opt-in to overdraft provisions of their checking accounts. In CFA’s 2004 survey, more than twice as many consumers thought it would be unfair for banks to permit overdrafts without obtaining their customers’ consent (68%) rather than fair (29%). Banks do not seek affirmative consumer assent when permitting overdraft loans, and consumers are charged expensive overdraft fees without their consent or any prior warning except deep inside the fine print of account disclosure agreements. The shock is especially unpleasant when they unwittingly access overdraft bounce loans through ATM or debit cards, where traditionally it has not been possible or has been much harder to overdraft. Even JPMorganChase stated to the Federal Reserve that account disclosure agreements should

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13 Moebs Services, Presentation to Federal Financial Institution Examination Council, June 2004, at 32.
clearly “specify whether overdraft fees apply in connection with checks, automated teller machine withdrawals or other electronic fund transfers.”

Despite the broad public opinion supporting consumer opt-in provisions for overdraft services, the American Bankers Association is opposed to consumers affirmatively opting-in to these account provisions. The industry trade association contends that although consumers know about the courtesy overdraft provisions, they would fail to opt-in and instead would discard the opt-in notice. Apparently bankers were more persuasive than consumer advocates, since the Interagency Guidance issued in February 2005 by federal bank regulators advised banks to either provide an opportunity for consumers to opt-in or the ability to opt-out of bank overdraft programs.

**Overdraft Loans: Credit without Truth in Lending Protections**

Bank overdraft loans are very similar to payday loans. Consumers without enough money in the bank in the last until the next payday get a cash advance from the bank by overdrawing their account by check, at the ATM or by making a purchase that overdraws the account using a debit card. Some banks even market their overdraft loans as a way to make ends meet. The bank levies its overdraft fee and requires payment in full within days. Using its right of set-off, the bank pays itself back for the loan and its fees from the next deposit made to the consumer’s account. Like payday loans, the finance charge for the short-term cash advance translates to triple digit interest rates. A $100 overdraft repaid in two weeks for a $20 penalty fee amounts to an annual percentage rate (APR) of 520% APR.

Cash advances using a debit card to overdraw a bank account are also very similar to cash advances using a credit card. The law provides very different protections when a cash advance is made using a debit card to overdraw a bank account as compared to cash advances using a credit card. Banks are prohibited from taking funds directly from a bank account to repay a credit card debt. However, consumers who obtain cash advances made by overdrawing an account with a debit card lack this protection. A bank can use the right of setoff when a customer creates an overdraft with a debit card to repay itself immediately when the customer deposits funds into the account.

The Federal Reserve Board’s Regulation Z, adopted in 1969, exempts overdraft fees from Truth in Lending coverage when two conditions are met: First, the bank does not have a contract with the consumer to pay overdrafts, and second, the fee charged is equivalent to

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the fee for bouncing the check.\textsuperscript{18} That regulation was intended to apply to the bank practice of paying consumers’ occasional or inadvertent overdrafts, considered a long-established customer service.\textsuperscript{19}

Recent guidance to financial institutions on overdraft programs, issued by federal bank regulators except the Office of Thrift Supervision, clearly states that banks that cover overdrafts extend credit.\textsuperscript{20} The Joint Guidance warned that overdraft programs may expose institutions to more credit risk than traditional overdraft options or lines of credit. In May 2005, the Federal Reserve Board adopted regulations under the Truth in Savings Act that treat overdraft loan fees as checking account service fees rather than as extensions of credit subject to the Truth in Lending Act.\textsuperscript{21} CFA and other consumer organizations had filed comments in August 2004 urging the Federal Reserve to require banks to treat overdraft loans as open-end credit and to provide comparable cost disclosures to benefit consumer choice and competition.\textsuperscript{22} In adopting its Final Rule under Truth in Savings, the Fed suggested that overdraft loans may need to be covered by the Truth in Lending Act in the future:

\begin{quote}
The Board’s adoption of final rules under Regulation DD does not preclude a future determination that TILA disclosures would also benefit consumers. The Board expressly stated in its proposal that further consideration of the need for coverage under Reg Z may be appropriate in the future.\textsuperscript{23} (Emphasis added.)
\end{quote}

CFA and other consumer organizations criticized the Fed’s TISA rule decision as ineffectual and a failure to protect consumers.\textsuperscript{24}

**Big Bank Overdraft Loans**

While the largest banks do not use third-party vendor software and marketing programs to provide fee-based overdraft coverage for their accountholders, they are providing this form of credit to consumers. Banks use internal data to make automated decisions to permit customers who meet predetermined conditions to overdraw their accounts. Advocates anticipate that large banks will step up their overdraft services following the permissive signals from bank regulators. The largest banks are beginning to more openly

\textsuperscript{18} 12 CFR 226.4(c)(3). However, the consumer is obligated to pay overdrafts and fees under terms of bank account agreements.
\textsuperscript{20} Joint Guidance on Overdraft Protection Programs, OCC, Federal Reserve System, FDIC, NCUA, Feb. 17, 2005, p. 7. “When overdrafts are paid, credit is extended.”
\textsuperscript{23} Federal Reserve Board, Final Rule, Regulation DD, p. 8.
market their fee-based overdrafts. Bank of America is now informing its customers that they can overdraw at the ATM for the bank’s $25 per incident fee.\(^{25}\)

Banks are making overdraft loans when they routinely pay checks that overdraw an account, when they knowingly permit consumers to electronically withdraw funds at the ATM or to make purchases at point of sale, or when banks pay pre-authorized debits despite the lack of funds in the consumer’s account. Other indicators of overdraft loan programs are that banks advertise the existence of its program or communicate to the consumer a monetary limit for overdraft coverage.\(^{26}\)

Is It Contractual Overdraft Protection or “Courtesy” Overdraft Loans?

The layering on of contractual overdraft protection, “courtesy” overdraft loans, and ad hoc payment of the occasional check that overdraws an account can be confusing for consumers. The distinction between the contractual overdraft protection like linked savings accounts, transfers to credit cards or lines of credit and “courtesy” overdraft loans can be lost on consumers. Although federal regulators have been particularly concerned with the aggressive promotion and marketing of overdraft loan programs more prevalent at smaller financial institutions, the “courtesy overdraft” practices common at the nation’s largest banks also have the capacity to encourage consumers to overuse or rely on courtesy overdrafts to their detriment.\(^{27}\) First, there could be confusion between the contractual overdraft protection services that banks offer and courtesy bounce protection, which is commonly described in the fine print of account disclosure agreements. The distinction between the more traditional, contractual overdraft protection and “courtesy” overdraft services can be difficult to discern, but the cost differences for consumers are significant.

Some of the big banks in CFA’s survey promote their contractual overdraft protection, while the “courtesy” overdraft loan policies are hidden deep within the banks’ deposit account agreements. For example, Citizens Bank’s overdraft protection language on its website sells its line of credit or savings account transfer overdraft protection product as offering “convenience and peace of mind.” On the other hand, Citizens Bank sent an addendum to its deposit disclosure in late 2004 describing the account’s “courtesy” overdraft provisions and informing consumers that overdrawing a check, ATM or debit card transaction would incur a fee of between $25 and $33 each, depending on the number of days the account remains overdrawn.\(^{28}\) This disclosure did not inform

\(^{27}\) See: “Consumer Federation of America Review of Bounced Loan Advertisements and Disclosures,” filed with the Federal Reserve, Comments of the National Consumer Law Center, Consumer Federation of America, Consumers Union, National Association of Consumer Advocates and Woodstock Institute to the Federal Reserve on 12CFR230 Docket No. R-1197, Proposed Amendments to Regulation DD, August 6, 2004. The review of 50 financial institution websites found 34% of advertisements encouraged customers to overdraft accounts; most sites had contradictory language on whether overdrafts would be honored; and many institutions gave incomplete or confusing information on how bounced check loans worked.
consumers that they could purchase optional savings account overdraft transfer coverage for $3 per month or apply for an overdraft protection line of credit which costs $20 annually, both of which could be more affordable for consumers. Marshall & Ilsley (M&I) bank offers its contractual overdraft protection program under the “Worry Free” program name, which the bank promotes to “avoid accidental overdrafts, cover unexpected expenses and relax knowing we’ve got you covered.” At the same time, M&I’s deposit agreement allows for the discretionary payment of debits (paper checks, ATM withdrawals, telephone transfers, on-line transactions or preauthorized debits) that would incur a $29 NSF fee.

### Big Banks’ Traditional Overdraft Protection Cheaper than “Courtesy” Overdraft Loans

The confusion between “courtesy” overdraft loans and contractual overdraft protection can cost consumers more money in fees. On average, fees for contractual overdraft protection transfers are lower than fees for “courtesy” overdraft loans. The comforting language used to promote the contractual overdraft protection opt-in policies is of especial concern because the distinction between the contractual programs and the courtesy overdraft account provisions is not described by any of the banks CFA surveyed.

Contractual programs are prevalent at large depository institutions. CFA found that 84.8% (28 of 33 institutions) offered programs to transfer deposit money from savings to checking accounts to cover checking account overdrafts, 42.4% (14 of 33 institutions) offered overdraft protection through a linked credit card, and 81.8% (27 of 33) offered programs to cover overdrafts through lines of credit.

Moreover, these programs are much more affordable than the “courtesy” overdraft loan provisions which all impose an overdraft penalty fee. CFA found that:

- Fees for overdraft transfers from savings accounts averaged $7.38 per transfer, about one-fourth the average overdraft loan fee of $28.57, although four of the

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banks with this service (14.1%) have an average annual fee for this service of $23.75.

- The average credit card overdraft transfer fee of $10.00 is less than half (35.0%) the average “courtesy” overdraft fee.31 The credit card’s interest is additional.
- Fees for transfers from lines of credit were cheaper – although some banks also require an annual fee. Lines of credit transfers averaged $5.20 per transfer and/or an average annual fee of $29.00, which would be cheaper by the second overdraft even for the average banks with annual fees.

Despite the significant price disparity and the relative affordability of the contractual overdraft protection programs versus bank “courtesy” overdraft loans, none of the banks CFA examined compared the overdraft coverage options on their websites, in their account disclosures or in their fee schedules.

**Big Banks Permit Overdrafts at the ATM and Point of Sale**

Bank overdraft loan programs go beyond covering paper checks, also permitting consumers to overdraw accounts at the ATM, at point of sale (POS), and through preauthorized debits. As the volume of paper transactions has been surpassed by electronic transactions, bank can no longer rely for revenue on NSF fees for bounced paper checks. One industry expert warned in 2003 that: “The head of retail banking must commit to designing tactics to make the organization less dependent on punitive NSF fees and more dependent, for instance, on overdraft lending.”33

ATM transactions and many debit card transactions are on-line and real time. The availability of funds is confirmed,34 and traditionally transactions are declined with no fee when consumers have insufficient funds in their account. Thus, the decision of a bank to permit overdrafts where none would have occurred previously permits banks to collect additional fees.35 Finance industry consultants Bernstein Research Call estimate that one in three NSF fees are for ATM withdrawals.36

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31 Consumers must also pay their credit card interest in addition to the fee levied by banks to transfer an overdraft to the accountholder’s credit card.
33 Stoneman quoting Gwenn Bezard, Celent Communications.
34 See In re Visa Check/Mastermoney Antitrust Litigation, 192 F.R.D. 68 (E.D.N.Y. 2000).
35 Some banks include the overdraft protection limits when displaying available balances at the ATM. This encourages consumers to overdraw their accounts by artificially inflating their account balances and is likely to increase the number of overdrafts and overdraft fees. Although none of the surveyed banks have
Financial institutions defend “courtesy” overdraft programs by claiming they save consumers from merchant penalties, late charges, and embarrassment. These defenses are completely inapplicable to ATM and many debit transactions. With ATM cards, the transaction is to provide cash directly to the consumer – there is no merchant or other third party involved. Since POS transactions for insufficient funds would be denied, absent bank overdraft loans, the consumer is not saved from paying the merchant’s NSF fees. Industry consultant Profit Technologies noted in a white paper that bounce protection can “increase fee income through the collection of overdraft fees for items that would have been denied at ATM or POS terminal[s].”

CFA found that 27 of the surveyed banks allow depositors to overdraw their accounts at the ATM, 26 allow overdrafts at point-of-sale debit transactions at merchants, and 17 allow overdrafts from automated or scheduled electronic payments. For example, Bank of America introduced its bounce protection service in the Boston area early in 2005, charging $25 per overdraft when consumers overdraw at the ATM or when using debit cards at retailers. The bank’s account statements stated “our goal is to authorize more transactions made using your ATM or check card even if it creates an overdraft on your account.”

Debit card Point-of-Sale (POS) transactions present similar concerns. Like ATM withdrawals, PIN-based debit card transactions are also on-line and real-time. With debit card transactions through the MasterCard or VISA networks, most merchants will check funds availability from the bank, which has the ability to inform the merchant that a transaction will overdraw the account. Because debit card transactions are at the point-of-sale, if the transaction is declined or at least the consumer warned that she is about to overdraw the account, the consumer often has the ability to undo the transaction (i.e. put the merchandise back on the shelf) or use an alternative form of payment without incurring a hefty penalty. While there is a third party involved and perhaps a chance of slight embarrassment if a transaction is declined, that risk is preferable to a hefty $20 to $35 fee.

bounce protection programs with defined credit lines and thus do not display them at the ATM. Citizens Bank includes any linked savings account overdraft protection on checking account available balances which encourages overdrafts, albeit for cheaper fees. See Citizens Bank Customer Service Quick Tips webpage available at www.citizensbank.com/customerservice/howdoi/cust_quick_tips.asp accessed March 7, 2005.


37 Foust, Dean, “‘Protection’ Racket?,” Business Week, May 2, 2005 at 68. “The bank insists its doing a service by covering checks and purchases that would otherwise bounce.”


40 See In re Visa Check/Mastermoney Antitrust Litigation, 192 F.R.D. 68 (E.D.N.Y. 2000).
Big Banks Charge High and Rising Overdraft Fees to Consumers

Consumers are paying exorbitant fees to borrow from their bank when they overdraw their accounts. Consumer Federation of America findings on “courtesy overdraft” fees charged by the largest banks include:

- **Fees for Overdrafts that Banks Honor Are Higher than for Bounced Checks:** Banks charged an average of $28.57 to pay a debit (either check, ATM or POS) that over drew a checking account. The bounced check fees for submitting a check that the bank does not honor averaged $28.09 at the 29 banks that disclosed these fees to CFA.

- **Six Banks Charge More for Paid Overdrafts than Returned Bounced Checks:** BankNorth, Bank of the West, Comerica, US Bank, Union Bank of California and Wells Fargo charge between $2 and $3 more for paying a check or debit which overdrafts a checking account than they do for refusing to pay the overdraft. Banks that charge more for “courtesy” overdraft loans than for returned bounced check fees may not be meeting one of two terms of the Fed’s Truth in Lending rules that exempt overdraft fees from credit cost disclosures if payment is discretionary and fees are the same for paying or returning the check.  

- **Fees for Overdrafts and Bounced Checks Rising:** Current fees for overdrafts and bounced checks at the surveyed banks are higher than the fees charged for these services at larger banks in 2002. Current average overdraft fees of $28.57 are $1.73 (6.4%) higher than the Federal Reserve reported larger banks were charging in 2002. Current bounced check fees of $28.09 are $1.90 (7.3%) higher than the Federal Reserve reported large banks were charging in 2002. In 2003, the Federal Reserve Board’s study on retail banking fees found that large banks charged $26.19 for bounced checks and $26.84 for honoring overdrafts in 2002 (the most recent Federal Reserve data available).

- **Fees at Big Banks Higher than Average Fees:** NSF fees at the largest banks are 5.3% higher than they are at average banks. The average NSF fee at the banks CFA surveyed was $28.57 compared to the NSF fee of $27.13 that bankrate.com found in a May 2005 study.

- **More than One Quarter of Banks Have Tiered Bounce/Overdraft Fees Based on Overdraft History:** Eight banks have surcharges or higher fees for depositors who have accrued overdrafts over the previous year. Bank of America, Bank of the West, Charter One (which has been acquired by Citizens Bank), Citizens Bank, KeyBank, National City, US Bank and Union Bank of California charge either a surcharge or a higher schedule of fees as the number of overdrafts increases within twelve months.

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41 12 CFR 226.4(c)(3).
Nearly Half of Banks Charge Sustained Overdraft Charges: Twelve of the banks charge additional fees for not repaying the overdraft within a certain period. These sustained overdraft charges begin on average after the fifth day the account is deficient. Seven banks charge a per-day sustained overdraft charge which averages $5.57 per day; and five banks charge a single sustained overdraft fee which averages $27.50.

High Overdraft Fees Benefit Big Banks’ Bottom Lines

The increasing prevalence of “courtesy” overdraft account provisions has helped to increase revenues at many banks large and small. Service fees on deposit accounts have been a growing component of non-interest income in the banking sector for the past five years.44 The single largest portion of non-interest income for banks was their service charges on deposit accounts, with $32.8 billion in bank and thrift deposit service fees amounting to 16.1% of non-interest income in 2004.45 Business Week stated that bank account fee profits exceed earnings from all other forms of bank lending, including mortgages and credit cards.46 A bank consulting firm estimated that financial institutions collected $22 billion in overdraft fees in 2003; and industry-wide, NSF related fees are estimated to account for up to 50% of total consumer checking account revenue.47

Banks contend that overdraft and bounced check fees are in place to deter depositors from mismanaging their checking accounts. Certainly the nearly $30 fees exceed the cost of processing bounced and overdraft transactions since the cost of processing checks is very low per check, including the costs of returned checks.48 The reality is that these low processing costs coupled with the high incidences of NSF and overdraft fees generate income for banks and other depository institutions.

Estimating revenue from bank NSF and overdraft fees is inexact because bank regulators do not require financial institutions to separately report these penalty fees. In the late

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46 Foust at 68.
47 Stoneman at 1.
48 In 1996, an article in the Federal Reserve Bank of Minneapolis Quarterly Review estimated that the unit check processing costs were between $0.15 and $0.43 including the per unit cost of $0.03 for returned items (Wells, Kristen E., “Are Checks Overused?,” Federal Reserve Bank of Minneapolis Quarterly Review, Vol. 20, No. 4, Fall 1996). In 2003, a banking industry consultant estimated the total unit cost of processing checks averaged between 6¢ and 10¢ and declining check volumes would drive up the unit processing costs to 20¢ if no improvements were made to processing efficiency (Mulhern, Michael, Partner, First Annapolis Consulting, presentation to “After the Hype: e-Commerce Payments Grow Up,” Payment Cards Center of the Federal Reserve Bank of Philadelphia and Electronic Commerce Payments Council of the Electronic Funds Transfer Association, Jun. 18, 2003). In 2005, the Federal Reserve Financial Services system charged between 13¢ in New York and 25¢ in San Francisco to process a basic returned check (Federal Reserve Financial Services, Check Service 2005 Schedules from Federal Reserve Bank of New York (effective January 3, 2005) and San Francisco (revised December 28, 2004)).
1990’s, CFA published a series of reports on the high cost of bounced checks to consumers. “Bounced Checks: Billion Dollar Profits II,” issued in June 1998 estimated that banks generated more than $5.6 billion in annual revenue and $5.2 billion in annual profits from bounced checks. An earlier report from 1993 calculated profits from bounced checks of $3.67 billion. Both reports examined bank fees and returned check volume for checks drawn on insufficient funds. These reports did not calculate the volume or profits for paid or “courtesy” overdrafts. Overdrafts were viewed as occasional and discretionary incidents, with the focus on the high volume and expense to consumers of checks that bankers returned unpaid to the check’s recipient.

Bank fee revenue from overdrafts is increasing because more types of transactions trigger overdraft fees, the dollar amount of fees is growing, and more bank customers overdraw more often as a result of bank marketing or learned behavior. Fee revenue estimates vary by expert and access to information. In a 2003 paper, Fusaro found that when banks implement bounce protection policies, they experience a 50% increase in overdraft checks. Overdraft loan fees are a significant and growing driver of overall fee income for depository institutions. In 2003, some analysts had estimated that fees from bounced checks accounted for between one quarter and half of all deposit fees earned by banks. By 2005, industry analysts estimate that bounce protection programs and policies account for two thirds of the total $12 to $14 billion in NSF fees, which are themselves more than one third of total deposit service charges of $32 billion. Industry consultant Moebis Services documented that fees from all financial institutions’ overdrafts created $33 billion in revenue for financial institutions representing nearly one-fifth (19.1%) of these institutions’ net income.

The Center for Responsible Lending (CRL) recently estimated that borrowers are paying more than $10 billion per year for fee-based overdraft loans. CRL considered bank, thrift and credit union fee income and conservatively applied analysts’ estimates of the share attributable just to fees charged for non-contractual overdraft loans. The range of total overdraft fees in CRL’s study could be as large as $22.7 billion per year. The CRL estimate exceeds the projection that consumers annually pay $11.7 billion for both bank NSF and overdraft fees included in 2004 CFA testimony to the House Financial Services Committee.

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54 Moebis Services, Presentation to Federal Financial Institution Examination Council, June 2004, at 1.
Revenue from bank overdraft fees is also growing because electronic transactions are increasingly covered by bank overdraft services. Some promotional material from industry consultants suggests fee income can increase as debits are honored that once would have been rejected without bounce protection. An industry-consultant authored article in *Connecticut Banker* noted that implementing overdraft protection services could double fee income from bounced checks or overdrawn accounts at the ATM.\(^5\)

Although there has been attention to the increase in fee revenue from overdraft loan programs at smaller banks, even larger depository institutions have highlighted their increased income from overdraft policies. CFA found that more than one fourth of big banks (27.3%) single out overdraft fees as a source of important revenue. Although some of the largest surveyed banks have business lines which are too extensive to include every revenue stream even in their Securities and Exchange Commission filings, nine of the top 33 depository institutions report that overdraft fees in particular are important contributors to the institution’s revenue either in their Securities and Exchange Commission (SEC) filings or in their annual reports to shareholders.\(^58\)

- **AmSouth**’s 2004 service charges increased by $40.0 million (or 12.0%) to $378.7 million as “primarily the result of increases in overdraft fees on consumer and small business accounts, driven by increases in the volume of overdrafts.”\(^59\) AmSouth Bank’s fees on deposit accounts grew by $48.7 million (or 16.8%) between 2002 and 2003, which AmSouth attributes to “primarily the result of increase in overdraft fees.”\(^60\) AmSouth was able to increase this revenue by increasing the fee per insufficient fund transaction and by the addition of ATM debit transactions to overdraft eligibility.
- **Banknorth**’s deposit services income increased 12% in 2004 as a result of “volume and fee increases in deposit accounts and an increase in the volume of overdraft fees.”\(^61\)
- **Bank of the West**’s deposit fee income increased by $8.4 million in 2004, a 5.4% increase over 2003, and Bank of the West noted that “a significant portion of the increase in service charges on deposit accounts was due to higher fee income from overdraft and nonsufficient funds transactions” as the primary driver of this income growth.\(^62\) Bank of the West attributed some of its $16.2 million increase

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\(^58\) Only one bank that referenced its overdraft fee income had that income decline. Keycorp Bank’s non-interest income declined by $2 million between 2002 and 2003 because of lowered service charges resulting from “lower overdraft and maintenance fees” according to its 2003 SEC10K filing.

\(^59\) AmSouth, Annual Report 2004, at 51.

\(^60\) AmSouth 2003 Annual Report at 50.


in service charge revenue to “higher fee income from overdraft and nonsufficient fund transactions.”

- **Huntington Bank** earned $3.3 million more in deposit account service charges in 2004 than 2003 as a result of higher overdraft charges and NSF fees.\(^{64}\)
- **National City Bank’s** deposit fees increased by $88 million between 2003 and 2004, a 15.5% increase and the institution attributed these increases in part to “Growth in overdraft and insufficient funds fees result[ing] from increases in the number of transaction accounts and increased transaction activity.”\(^{65}\)
- **SouthTrust**, now a subsidiary of Wachovia, reported that increased fees charged for overdrafts were a key factor in increasing the bank’s deposit account revenues by 6% in 2003.\(^{66}\)
- **SunTrust** Bank’s service charges on deposit accounts increased by $30.2 million between 2002 and 2003, and SunTrust lists increased insufficient funds volumes and “increased pricing and revenue enhancement initiatives.”\(^{67}\)
- **Union Bank** of California service charges on deposit accounts grew by $30.8 million (9.9%) between 2003 and 2004 primarily because deposits increased but also because of higher overdraft fees.\(^{68}\) Total service charges on deposit accounts increased by $35.6 million between 2002 and 2003. Increased fees from a new overdraft program introduced in the second quarter of 2003 contributed $10.7 million to these deposit account service charges, or 30.0% of the increase.\(^{69}\)
- **Union Planters** (now a subsidiary of Regions Financial) reported that its 2003 fourth financial quarter deposit fee income rose by $1.0 million (or 1.7% over the previous quarter) “primarily on the strength of overdraft charges.”\(^{70}\)

**Bank Debit Processing Order Maximizes Overdrafts**

Banks decide the order in which withdrawals will be processed from accounts, including electronic transactions, preauthorized debits and paper checks. The order of processing withdrawals has a large impact on the frequency of overdrafts and the cost to consumers with low balances. A bank that pays the largest check first can cause more checks to bounce for low-balance customers and can charge a penalty fee for each one. Consumers do not know the order in which items drawn on their account will be presented to their bank and are not likely to know the order in which their bank pays items. As a result, the Federal Reserve noted in adopting Truth in Savings regulations that consumers who are aware that their account may be overdrawn are not likely to know the number of items that will bounce or the total fees they will be charged.\(^{71}\)

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\(^{63}\) BancWest Corporation, 2003 SEC10K filing, at 23.
\(^{64}\) Huntington Bancshares Incorporated, 2004 Annual Report, at 46.
\(^{65}\) National City Bank, 2004 SEC10K.
\(^{69}\) Union Bank of California, 2003 SEC10K filing, at 22.
The Uniform Commercial Code (UCC) authorizes banks to clear withdrawals in any order they select.\textsuperscript{72} A few states include comments to the UCC that specifically prohibit a bank from adopting a procedure designed to maximize the number of dishonored checks in order to increase fee income.\textsuperscript{73} The Comptroller of the Currency issued Interpretive Letters approving high to low check clearing (i.e. largest to smallest sized check) when banks have followed the OCC regulation considerations in adopting this policy.\textsuperscript{74} The considerations include: the cost incurred by the bank in providing the service; the deterrence of misuse by customers of banking services; the enhancement of the competitive position of the bank in accordance with the bank’s business plan and marketing strategy; and the maintenance of the safety and soundness of the institution.\textsuperscript{75}

A rash of lawsuits were filed in the 1990’s against banks that changed check clearing processes, alleging abuse of discretion, bad faith and breach of contracts with consumers. Courts have ruled that the bank practice of honoring the largest check first is not bad faith.\textsuperscript{76} The Comptroller of the Currency noted that, “a relevant factor in evaluating good faith may be whether a bank’s actions were consistent with the practices it had represented to its customers that it would follow.”\textsuperscript{77} In other words, according to the OCC, if the fine print of the bank account agreement discloses that the bank uses high to low check clearing, even if it increases the number and cost of bounced check fees, the bank has not engaged in bad faith.

\begin{figure}[h]
\centering
\includegraphics[width=\textwidth]{large_bank_debit_processing_order.png}
\caption{Large Bank Debit Processing Order}
\end{figure}

\textsuperscript{72} Uniform Commercial Code 4-303(b) “Subject to subsection (a), items may be accepted, paid, certified, or charged to the indicated account of its customer in any order.”
\textsuperscript{73} NCLC “Consumer Banking and Payments Law,” page 16. Footnote 180 refers to Official Comment to the state version of UCC 4-303, as enacted in Texas and California with similar comments in Massachusetts and New Jersey.
\textsuperscript{74} OCC Interpretive Letter #916, May 22, 2001 and Interpretive Letter #997 August 2004. The OCC issued revised regulations in 2001 to state “fees resulting from the method the bank employs to post checks presented for payment are included within the authorization provided by section 7.4002.” Another federal regulator has stated disapproval of high to low check clearing if used to maximize bounced items. See Office of Thrift Supervision Guidance on Overdraft Protection Programs, February 14, 2005.
\textsuperscript{75} 12 C.F.R. 7.4002(b).
\textsuperscript{77} OCC Interpretative Letter #997, August 2004, at 3.
Bankers claim that consumers want their largest checks paid first because those may be for important payments such as mortgage or insurance. However, a 1998 CFA public opinion poll found that only 13% of respondents wanted banks to “Pay the largest checks first, since those may be the most important.” Almost two-thirds of consumers thought banks should pay checks in the order the bank receives them while 16% wanted banks to pay the smallest checks first to minimize the number of checks that bounce.\footnote{CFA, “Bounced Checks: Billion Dollar Profits II,” Appendix reporting results of an Opinion Research Corporation International poll of 1005 consumers, June 1998.}

The CFA survey of big bank account disclosures indicates that depository institutions do not generally disclose the order they process debits (paper checks, ATM withdrawals, POS purchases or electronic transfers) and many state they could change their processing order without notice to depositors. CFA found that nearly one fourth (24.2%) of banks refuse to disclose any debit processing order beyond “any order;” one seventh (15.2%) of banks reserve the right to process debits in any order but disclose they generally process debits from largest to smallest; and one third (33.3%) disclose they process debits largest to smallest.

Wachovia discloses that it will process debit items (checks or ATM withdrawals) in “any order determined by [Wachovia]” and reserves the right to “without prior notice to [depositors], change the order in which we generally pay items.”\footnote{Wachovia “Deposit Agreement and Disclosures for Personal Accounts,” Effective February 1, 2005, at 12.} Although Bank One discloses that it processes checks from highest denomination to lowest, it discloses that it may change its processing order without notice to depositors.\footnote{Bank One, “Deposit Agreement and Disclosures,” effective January 28, 2005 at 15.} KeyBank also processes debit items “in any order that we choose” and reserves the right to “change the processing order at any time without notice to you [the depositor].”\footnote{KeyBank, “Deposit Account Agreement and Funds Availability Policy,” Effective December 10, 2004, Part I, 6.} The banking lobby wants to keep debit processing order from being disclosed to consumers. The ABA contends that order in which debits are processed is so complex that it is “virtually impossible to explain in a manner understandable to most consumers” and would require several pages to disclose to consumers.\footnote{Feddis, Nessa, Senior Federal Counsel ABA, Letter to Jennifer J. Johnson, Secretary Board of Governors of the Federal Reserve System, Re: Proposed Interagency Guidance on Overdraft Protection Programs, August 6, 2004, at 6.}

Although banks generally do not disclose the debit processing order, some banks have acknowledged different processing orders can result in higher total fees for consumers in the fine print of their account agreement disclosures. For example, Bank of America will clear debits “in any order” and change that order “at any time without notice to [consumers] even though some processing orders may result in more insufficient funds fees.”\footnote{Bank of America Deposit Agreement & Disclosures, October 1, 2004, at 26.} Wachovia’s Deposit Agreement and Disclosure acknowledges that the bank’s selection of check and debit processing order could “result in the payment of fewer
checks or other items or the imposition of additional fees.” 84 Citizens Bank warns that depositors “should be aware that the order in which we pay checks drawn on your account may increase the insufficient available/overdraft funds fees you have to pay.” 85

The justification banks give for clearing checks high to low is to make sure important big ticket items are paid, but that rationale can not justify this practice for banks that routinely cover overdrafts because all debits will get covered. If banks choose to pay transactions that overdraw accounts for the vast majority of customers, the only purpose for clearing the largest transactions first is to maximize the imposition of multiple overdraft fees for low balance customers. Banks that give their customers “permission” to overdraw bank accounts also cannot justify high fees to deter “misuse” by customers of banking services.

The Office of Thrift Supervision (OTS) addressed manipulation of transaction-clearing rules in the Final Guidance on Thrift Overdraft Protection Programs issued February 14, 2005. The OTS advised thrifts that transaction-clearing rules (including check-clearing and batch debit processing) should not be administered unfairly or manipulated to inflate fees. 86 The Guidelines issued by the other federal regulatory agencies merely urged banks and credit unions to explain the impact of their transaction clearing policies. The OCC, FRB, FDIC, and NCUA “Best Practices” states: “Clearly explain to consumers that transactions may not be processed in the order in which they occurred, and that the order in which transactions are received by the institution and processed can affect the total amount of overdraft fees incurred by the consumer.” 87 None of the agencies addressed the combination of debit clearing order and overdraft loan practices.

**Bank Overdraft Loans Disproportionately Impact Some Bank Customers**

Overdraft fees do not fall uniformly on bank customers. Some depositors pay more overdraft fees than others. The depositors who most frequently face these fees are the lowest income and youngest consumers. 88 High overdraft fees can also have a much higher impact on moderate-income consumers and African American consumers. CFA’s 2004 national opinion poll found that the consumers who state they overdraw their accounts and are most likely to pay overdraft and bounced check fees were moderate-income consumers with household incomes of $25,000 to $50,000 (37%). Those 25 to 44 years of age (36%), and African Americans (45%) were most likely to have bounced checks. Twenty two percent of the lowest income group surveyed, making less than $25,000 a year, and less educated consumers (33%) reported that they do not have a bank account to overdraw.

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84 Wachovia “Deposit Agreement and Disclosures for Personal Accounts,” Effective February 1, 2005, at 12.
86 Office of Thrift Supervision, Guidance on Overdraft Protection Programs, February 14, 2005, p. 15.
The USA Federal Credit Union in San Diego studied the usage of its experimental overdraft privilege program and reported that nearly 33% of users were overdrawing their accounts more than five times a month. One fourth of the overdraft users were under the age of 25 and were likely sailors and soldiers in their military field of membership. The credit union also found that the average amount triggering an overdraft was less than $100.89

In one of the few empirical studies of consumer behavior with “courtesy bounce protection,” East Carolina University economist Marc Fusaro examined the transaction records of a Chicago-based bank and found that nearly a quarter of depositors (24.2%) had overdrawn their checking accounts in a four month period and nearly three-fifths of depositors (59.1%) had ever overdrawn their checking accounts.90 Of the depositors that had overdrawn their account in the previous four months, one in five had overdrawn their account more than 30 times. More than half (53.6%) had overdrawn their accounts between 1 and 10 times within four months.91

Professor Fusaro’s study confirmed that younger and lower-income depositors overdrafted their accounts the most frequently.92 Fusaro found that more than one third (34%) of depositors’ aged 18 to 35 had bounced more than 16 checks, compared to one fourth (24%) of all depositors. One fourth (25%) of depositors making less than $18,000 bounced nearly one out of every twenty checks (4.5%) compared to 14% of all depositors. Industry analysts estimate that the poorest 20% of the country’s 135 million checking account customers generate 80% of the $12 billion in annual overdraft fees.93 A study conducted by the Washington Department of Financial Institutions revealed that fifteen percent of bank customers use overdraft loan programs. Of the people who overdraw their accounts, 12% overdraw once or twice a month, 1% overdraw two to five times per month; and 2% overdraw over five times per month.94

CFA’s 2004 public opinion survey found that 28% of consumers say they overdraw their bank accounts. One third of consumers who overdrew their accounts (9.3% of all consumers) had bounced at least three checks in the previous year. Other sources report similar data. A third party vendor who promotes bounce loans has said that about 15% of customers incur overdraft loans.95 A study by the Washington State Department of Financial Institutions revealed that over 20% of borrowers who incur overdraft loan fees

89 Cunningham, Mary, “Why Our Credit Union Has Wrestled With Realities of ‘Courtesy Pay,,’” Credit Union Journal, January 17, 2005.
90 Fusaro 2005 at 20.
92 Fusaro 2005 at 21.
93 Foust, Dean “‘Protection’ Racket?,” Business Week, May 2, 2005, at 69, citing Bernstein Research Call.
are charged such fees two or more times per month. According to another overdraft loan vendor, 4% of these loan customers are responsible for 50% of loan fees.

In an earlier study, Fusaro estimated that consumers who utilize overdraft loans fewer than 10 times a year will pay $99 in fees annually, but consumers who use overdraft loans between 10 and 30 times a year will pay more than $1 a day ($366 annually) for the service. The nearly 5% of consumers that use overdraft loans more than 30 times a year will pay at least $1,229 in fees and the 1% that use it more than 100 times annually will pay $3,254 for the service. The overdraft fees consumers face at the nation’s largest depository institution could be even higher. Paying overdraft fees ten times a year would cost on average $286 annually at the large banks CFA surveyed. The one in twenty customers that overdraw more than 90 times a year would pay $2,571 in fees even if their bank did not use tiered overdraft fee structures, which could significantly increase total overdraft fees.

Thus, bounced check and overdraft loan fees are mostly generated from a small minority of customers, who are probably the most vulnerable of consumers. These consumers are more likely to use overdraft loans repeatedly and rack up cumulative fees to their bank, potentially trapping them in a cycle of debt. By permitting overdrafts, not just through checks but ATMs and debit cards, these banks are creating new ways to impose exorbitant fees and create financial hardship.

**Overdraft Loan Provisions Inadequately Disclosed to Depositors**

Banks do not generally inform consumers of the terms under which they will or will not pay debits (check or electronic) in their depository disclosure agreements. Instead, banks employ general and vague language that suggests that banks will honor debits which overdraw depositors’ accounts at the banks’ own discretion. The Conference of State Bank Supervisors has suggested that banks utilize such vague and unclear language precisely to avoid being subject to the Truth in Lending Act (TILA), which requires that banks fully disclose the terms of a loan to consumers including the finance charge and its annual percentage rate of interest before extending credit. The Conference stated that banks are concerned that “providing customers with clear written agreements that describe the terms governing overdraft protection programs would trigger Regulation Z [TILA] disclosures, many financial institutions did not provide clear written agreements” but that “this non-contractual courtesy concept can be misleading to consumers and, therefore, is inappropriate.”

The State of Wyoming Division of Banking has repeatedly informed banks it regulates that merely going “to great lengths to state that [automatic overdraft protection programs]

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98 Fusaro 2003 at 17.
is a ‘non-contractual courtesy’ and that the Bank is ‘not obligated to pay any item presented for payment’” does not obviate the practical applications of these programs which are in effect “regular criteria for determining if an account qualifies for protection” which is essentially not discretionary.  

Under bank “courtesy” overdraft loan services, consumers cannot rely on their banks to routinely cover overdrafts. Maine-based Banknorth’s deposit account agreement states that “An overdraft is an advance of funds made by us to you, at our sole discretion, to cover a check or other withdrawal.” Bank One’s customer disclosure states that “under no circumstances shall you have the right to rely upon the Bank crediting your account for payment [...] notwithstanding the bank having done so on one or more prior occasions.” Citibank describes “the most common” circumstances where it will not cover overdrafts which include unavailable funds, insufficient funds, a dispute related to the account or a suspicion of fraud or irregularity. Although Citibank is the only institution that lists any conditions for refusing to pay overdrafts, the list is not especially helpful to consumers since paying overdrafts is unnecessary with accounts that do not have insufficient or unavailable funds.

The American Bankers Association (ABA) has stated that “whether or not specifically informed,” consumers know about courtesy overdrafts and many “want and expect the bank to pay an accidental overdraft.” The 2003 ABA brochure Overdraft Protection: A Guide for Bankers recommended that banks clear up the confusion customers face, noting “Customers are often confused by the NSF decision-making process in those banks that do not have a formalized program, since there is often inconsistency in payment of NSF items.” Despite the confusion discretionary courtesy overdraft presents to depositors, a year later the ABA opposed requiring banks to disclose the conditions when they will not pay overdrafts.

**Banks Make It Hard to Find Out NSF and Overdraft Fees and Practices**

In collecting information for this report, CFA surveyed banks’ web sites for account and fee information. Where that information was not available, CFA sent individuals into bank lobbies in search of checking account fee information.

Few large depository institutions make fee or account disclosures available on the Internet. Only 12 of the 33 (36.5%) banking companies examined made either a fee

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100 Letter from L. Bruce Hendrickson, Administrator of Uniform Consumer Credit Code, State of Wyoming, Department of Audit, Division of Banking, to redacted Bank, Feb. 2, 2001.
schedule and/or account agreement available on their websites. Many banks do not disclose their fee schedule or account agreements online unless a full account application is first made, including providing social security numbers, addresses, employment history and other private information.

CFA found that many banks were reluctant to provide account disclosures and fee schedules when individuals went to the bank branches. The purpose of the Truth In Savings Act (TISA) is to enable consumers “to make meaningful comparisons among depository institutions” to find the best bank accounts for their particular needs. Moreover, the regulation requires that banks provide account disclosures upon request. Some surveyed banks contended that they would only provide disclosures to customers who were actually going to open an account, but not to prospective customers shopping for an account, which is contrary to the purpose of TISA. If consumer advocates have difficulty getting banks to provide required account disclosures, average consumers are likely to have similar problems, making competition based on full information less likely. The inability of consumers to comparison shop online or in brick and mortar banks makes it even harder for them to avoid unnecessary fees and charges to their accounts.

Policy Recommendations

Congress should clarify that overdrafts are covered by the Truth in Lending Act, limit penalty fees charged for overdrafts and returned checks to an amount based on the bank’s actual cost plus a reasonable return, require federally insured depository institutions to provide affordable repayment terms when making overdraft loans, and warn consumers when ATM and debit card transactions will overdraw an account and trigger a fee.

The Federal Reserve Board should close the Truth in Lending Regulation Z loophole used by banks to make cash advances to consumers without providing TILA protections and comparable cost disclosures to accountholders. Besides requiring that overdraft loan costs be disclosed under open-end credit rules, this action would require banks to get consumers’ affirmative consent to extend credit and result in more affordable repayment terms.

The Federal Reserve should direct banks to examine their check hold policies to ensure that the full check hold time period is not used except in instances where it is in fact required to avoid significant risk of an insufficient funds check. The Fed should examine check hold periods and reduce them by regulation at the earliest possible time.

The Fed should find it an unfair practice for financial institutions to charge overdraft fees on any check which would not have bounced if a hold period had been completed on a timely deposit or to bounce a check when a deposit has been made that would cover the withdrawal but for the hold period.

106 Truth In Savings Act, Regulation DD, 12CFR11§230.1(b).
The Federal Deposit Insurance Corporation should require financial institutions to separately report checking account fee revenue for insufficient funds and for overdrafts to provide policymakers with an accurate measure of the cost to consumers.

Bank regulators should bring Federal Trade Commission Act cases against banks that order debit processing to maximize fee revenue while routinely covering overdrafts for their account holders. Regulators should also bring deceptive practices cases against banks that claim their “courtesy bounce protection” is discretionary while also advertising, representing or implying that consumers can expect the bank to cover overdrafts or while permitting consumers to overdraw at the ATM, POS or through preauthorized debits.

Banks should not permit their account holders to overdraw at ATM and POS terminals unless the bank clearly discloses that the transaction will overdraw the account, provides TILA disclosures including an effective APR in the consumer’s periodic statement, and provides the opportunity for the consumer to affirmatively consent to the cash advance.

Banks should redesign contractual overdraft protection products to serve the needs of most bank customers. Real contractual overdraft protection at a fair price and with affordable repayment terms should meet customers’ needs for small cash advances instead of burdening cash-strapped bank customers with either payday loans or overdraft bounced check loans at triple digit interest rates which must be repaid on the consumer’s next payday.

Advice to Consumers

The prevalence of overdraft loans and the high cost of bounced checks at the nation’s largest financial institutions mean that consumers need to take action to protect themselves from hidden overdraft provisions and NSF fees which can be expensive for consumers. Consumers can take these steps to avoid paying penalty fees:

- Select a financial institution that offers real overdraft protection and apply for it. Also compare account fees and ask about bank practices in processing check and debit card withdrawals and deposits.

- Avoid paying penalty fees for NSF checks or overdrafts. If your bank provides “courtesy” overdraft services, ask to opt out of the program if you do not want to pay penalty fees to be able to overdraw at the ATM, point of sale, or by check.

- Establish a savings account as a first bank account and build up a large enough balance for it to provide linked-account overdraft protection before opening a checking account. Keep at least $500 in emergency savings to cover inadvertent overdrafts. Note that there is a fee to make transfers from savings to checking.
• Keep careful track of the balance in the checking account, including how long it takes for deposits to become available to cover withdrawals. Write down every ATM withdrawal, point of sale transaction, foreign ATM fee, as well as all checks written on the account.

• Do not assume that “float” will permit you to write checks a few days before deposits will be available. When you pay by check, you have no control over the way the retailer or its bank will process the check. Just assume that any checks written will clear the bank on the same day.

**Methodology:** Consumer Federation of America analyzed the cost structure of depository accounts of the fifty largest depository institutions insured by the Federal Deposit Insurance Corporation (FDIC) and listed on the FDIC’s Summary of Deposits (SOD) database. CFA used the June 2004 SOD summary of deposits, the most recent available. The list of fifty depository institutions was reduced to 33 by eliminating institutions without checking accounts, consolidating affiliates, taking mergers and acquisitions into account and eliminating one institution for which CFA could obtain no cost structure information, perhaps because it is undergoing a merger (Hibernia).

Three of the institutions on the list only had savings or money market depository accounts which could not be debited with paper checks and primarily are affiliated with other financial services companies were excluded from this survey (they include ING which has only one branch, and MBNA and Merrill Lynch Bank which each have three branches). CFA consolidated institutional affiliates (for example Citibank NA, Citibank FSB, Citibank West FSB share a fee structure and were recorded as Citibank) as well as merged institutions where the institutions shared institutional websites (for example, Bank One is a subsidiary of JPMorganChase but continues to operate under the Bank One brand, but Union Planters depositors are forwarded to the Regions Bank website).

CFA looked for deposit agreements on the corporate websites, information on the accounts available on the corporate websites and in some cases sought depository account disclosure information from the banks themselves. In cases where accounts varied by location, CFA attempted to use fee schedules from the state where the financial institution is headquartered.

Average calculations were based on the number of institutions that provided definitive information for the costs of services. In some cases, surveyed banks indicate that they provide a service but not what it costs, in those cases the number of banks with the service is counted separately from the average cost of that service. For example, more banks may indicate they have balance transfer services than reveal what those services cost, so the percentage that offer the service is reported and an average of those that disclose the cost is reported.
<table>
<thead>
<tr>
<th>Institution</th>
<th>Fee Schedule on Web</th>
<th>Traditional Overdraft Protection</th>
<th>&quot;Courtesy&quot; Overdraft Loans</th>
<th>Notes</th>
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<td>Line of Credit</td>
<td>Annual Savings Transfer Fee</td>
<td>Savings Transfer Fee</td>
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<td></td>
<td>Credit Card</td>
<td>Home Equity</td>
<td>Opt-In Contract</td>
<td></td>
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<td></td>
<td>Clearane Policy</td>
<td>Automatic</td>
<td>ATM Odraft</td>
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<td>AutoPayment Odraft</td>
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<tr>
<td></td>
<td></td>
<td>Paid NSF/OD Fee</td>
<td>Sustained OD Fee</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>Average/Count of Banks</td>
<td>After Days</td>
<td></td>
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<td>BankNorth, National Association</td>
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<td>$ 5</td>
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<tr>
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<td>Y</td>
<td>$ 10</td>
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<td>$20</td>
<td>High-low</td>
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<td>$5 fee/y + 1.75% APR R*</td>
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<td>$60/y*</td>
<td>Y</td>
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**Notes**: Italics throughout chart indicates website material, non-italics indicates information from deposit account disclosures and fee schedules.
<table>
<thead>
<tr>
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<th>Paid Overdraft Fee</th>
<th>Sustained OD Fee</th>
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<tr>
<td>LaSalle Bank (ABN AMRO subsidiary, includes Standard Federal)</td>
<td>Y</td>
<td>$220 + $250/y</td>
<td>$3</td>
<td>Y</td>
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<td>Y Y Y</td>
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<tr>
<td>M&amp;I Marshall and Ilsley Bank</td>
<td>Y</td>
<td>$220 + $250/y</td>
<td>$3</td>
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<td>Y Y Y</td>
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<tr>
<td>Manufacturers and Traders Trust Company</td>
<td>N</td>
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<td>$3</td>
<td>Y</td>
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<td>Y Y Y</td>
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<td>$30</td>
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<td>National City Bank (includes National City Bank of the Midwest)</td>
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<td>$220 + $250/y</td>
<td>$3</td>
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<td>Y</td>
<td>Y Y Y</td>
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<td>Northern Bank</td>
<td>Y</td>
<td>$220 + $250/y</td>
<td>$3</td>
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<td>$30</td>
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<tr>
<td>PNC Bank, National Association</td>
<td>Y</td>
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<td>$3</td>
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<td>Regions Bank (includes Union Planters subsidiary)</td>
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<td>$3</td>
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<td>SunTrust Bank (includes National Bank of Commerce)</td>
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<td>$3</td>
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<td>Union Bank of California, National Association</td>
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<td>Y</td>
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<td>Y Y Y</td>
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<tr>
<td>Washington Mutual Bank (including WA &amp; CA affiliates)</td>
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<td>Y</td>
<td>Y Y Y</td>
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<td>World Savings Bank, FSB</td>
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Notes: Italics throughout chart indicates website material, non-italics indicates information from deposit account disclosures and fee schedules.