Comment on Proposed Rule of Overdraft Lending by Very Large Financial Institutions

Docket No. CFPB-2024-0002

April 1, 2024

The Financial Health Network appreciates this opportunity to comment on the Consumer Financial Protection Bureau's Notice of Proposed Rulemaking (NPRM) on "Overdraft Lending by Very Large Financial Institutions." The Financial Health Network brings together financial institutions, employers, innovators, and nonprofits all working to achieve financial health for all. The Financial Health Network is a recognized expert on the state of financial health in the United States and on the ways in which various financial products and services affect consumers' financial health.

Of particular relevance to this rulemaking, for the past six years the Financial Health Network has conducted an annual Financial Health Pulse® survey, using a nationally representative, probability-based sample (the USC Understanding America panel), to explore the evolving financial health landscape using our FinHealth Score® as well as supplemental questions relevant to understanding consumers' financial lives. Additionally, for the past four years the Financial Health Network has conducted an annual FinHealth Spend survey, using the same probability-based panel, to explore in greater detail how households are using, and how much they are paying for, financial services. Using data from the Spend surveys we published research briefs on overdraft usage in 2022 and again in 2023.[1, 2] That research has been widely cited, including in the Bureau's NPRM and also by some who have come out in opposition to the proposed rule.[3]

As an organization that strives to produce empirically sound, objective research, we take pride in the fact that our research is seen as authoritative and insightful across the political and ideological spectrum. At the same time, we think it important to set forth our understanding of what the data – both our own research and other published research – say about overdraft users and usage. We do so in Part I of this comment. In Parts II and III, we then address some of the major questions raised by the NPRM, urging that the Bureau set the safe harbor level for non-covered overdraft at $14 or $15 (Part II), and proposing that the Bureau create a narrowly-tailored exception to some of the rules that would apply to covered overdraft with respect to small-dollar overdraft lines of credit meeting a set of consumer-protective requirements (Part III).

Before turning to that analysis, we pause to emphasize the magnitude of the issues implicated here. The Bureau has estimated that in 2022, consumers paid $6.16 billion in overdraft fees to the financial institutions covered by the proposed rule.[4] That is more than our estimate of the combined

[1] MK Falgout, Meghan Greene, & Necati Celik, "Overdraft Trends Amid Historic Policy Shifts," Financial Health Network, June 2023.

[2] Meghan Greene & Stephen Arves, "Amid Resurgence of Interest in Overdraft, New Data Reveal How Inequitable It Can Be," Financial Health Network, September 2021.

[3] "McHenry, Barr Bash Harmful CFPB Overdraft Proposal," Financial Services Committee, January 2024.

[4] 89 Fed. Reg. at 13888. We believe this is a conservative estimate since it assumes that overdraft revenue of credit unions declined at the same rate as at banks between 2019 and 2022 and thus that the share of such revenue attributable to banks held constant. Our analysis and information collected by the CFPB, Data Spotlight (Oct. 11, 2023), and also by the California Department of Financial Protection and Innovation, Annual Report of Income from Fees on Nonsufficient Funds and Overdraft Charges, suggest that credit unions, including the larger ones covered by the rule, have made fewer changes to their overdraft practices and thus may have experienced a lesser decline in revenue.

amount consumers spent for payday loans and vehicle title loans in 2022, and 40% above what we estimate consumers spent on pawn loans in 2022.[5] And, although Call Report data from 2023 indicates suggests that for banks with over $10 billion in assets, overdraft revenue declined by 30% compared to 2022, the total still would be substantially above what consumers pay for payday loans or vehicle title loans and comparable to what they pay for pawn loans.[6]

I. Overdraft Users and Usage

In order to assess how the Bureau's proposal would affect the welfare – which is to say the financial health – of consumers, it is important to understand overdraft users and their usage. The Financial Health Network's research, coupled with research by the CFPB, sheds considerable light on those questions.[7]

To begin with, we have consistently found that roughly 1 in 6 households with a checking account incur at least one overdraft or NSF fee over the course of a year. Based on a survey conducted in January 2023 we reported that 17% of households who had a checking account in 2022 incurred one or more overdraft fees during that year.[8] Importantly, our most recent survey, conducted in January 2024, found an identical percentage of overdrafting households in 2023.[9]

Our research sheds light on the financial situation of households that overdraft. Not surprisingly, we have found that the share of low- to moderate-income households who incurred overdraft fees was

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[5] Meghan Greene, Wanjira Chege, MK Falgout, & Necati Celik, "FinHealth Spend Report 2023: U.S. Household Spending on Financial Services Amid Historic Inflation and an Uncertain Economy," Financial Health Network, June 2023.

[6] In 2022, banks with over $10 billion in assets reported $6.42 billion in overdraft and NSF revenue of which the Bureau estimated that 91% ($5.81 billion) was attributable to overdraft. 89 Fed. Reg. at 13887. In 2023, these banks reported $4.5 billion in overdraft/NSF revenue. If the share of that revenue attributable to overdraft held constant, that would imply $4.1 billion in overdraft revenue for these banks. That is a conservative estimate given that many large banks stopped charge NSF fees some time in 2022 in which event 100% of their reported overdraft/NSF revenue would be attributable to overdraft fees.

[7] Our research, like most prior research, does not distinguish between those who pay overdraft fees and those who pay NSF fees. Thus, when we use the term "overdrafter" here we are referring to a household that incurred either an overdraft or an NSF fee and when we discuss "frequent overdrafters" below we are counting both overdraft and NSF fees. The Bureau's recent research finds that only 3.9% of consumers incur NSF fees but not overdraft fees and that the vast majority of those who incur overdraft fees also incur NSF fees in the same year. See "Overdraft and Nonsufficient Fund Fees: Insights from the Making Ends Meet Survey and Consumer Credit Panel," Consumer Financial Protection Bureau, December 2023.

[8] MK Falgout, Meghan Greene, & Necati Celik, "Overdraft Trends Amid Historic Policy Shifts," Financial Health Network, June 2023. We note that the CFPB's 2023 Making Ends Meet Survey, *supra* n.7, which was mailed in January 2023, found that 24% of consumers reside in a household that incurred at least one overdraft fee in 2022. On the other hand, in the Federal Reserve Board's 2023 Survey of Household Economics and Decisionmaking (SHED) which was conducted in October 2022, 11% of households reported incurring an overdraft fee in the prior year. See "Report on the Economic Well-Being of U.S Households in 2022 - May 2023. Differences in panel construction, question wording, and the ordering of questions along with margins of error may have contributed to this variation in findings.

[9] Results from this survey will be published in our forthcoming FinHealth Spend 2024 Report. If it would be helpful to the CFPB, we can submit for the record tables showing the relevant questions and responses.

almost twice the share of higher-income households;[10] the share of households with individuals with a (self-reported) nonprime credit score who incurred an overdraft fee was more than three times higher than for those with prime credit scores;[11] and the share of Financially Vulnerable households – that is, households whose FinHealth Score indicates that they are struggling with almost all aspects of their financial lives – who incurred at least one overdraft fee was more than 10 times higher than for the Financially Healthy.[12] Indeed, fully 46% of Financially Vulnerable households reported incurring at least one overdraft fee compared to just 4% of Financially Healthy households.[13] These same patterns hold in our most recent (not yet published) survey. We also found in that survey that the share of overdrafting households that also pay monthly maintenance fees on their checking accounts (44%) is more than three times higher than the share among non-overdrafting households (14%).

Also not surprisingly, given the vast disparities in income, wealth, and financial health across racial and ethnic groups in the United States, our research has found large disparities along these lines. For example, in our most recent survey, 31% of Black households and 24% of Latinx households reported incurring at least one overdraft fee compared to just 14% of White households.[14]

Of particular significance are frequent overdrafters, as the FDIC, drawing on administrative data collected from state-chartered banks in 2005-2008, and the CFPB, drawing on administrative data collected from large national banks from 2011-2012, each found in their discrete datasets that frequent overdrafters – defined by the FDIC as those with 10 or more overdrafts and by the CFPB as those with over 10 overdrafts – represented 9% of accounts but paid 74% of all overdraft fees.[15, 16, 17] The Bureau, of course, has done seminal research documenting the financial distress of these

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10 Meghan Greene & Stephen Arves, "Amid Resurgence of Interest in Overdraft, New Data Reveal How Inequitable It Can Be," Financial Health Network, September 2021.

11 This finding from the survey conducted in January 2023 for the FinHealth Spend Report 2023 was not included in that report.

12 Meghan Greene & Stephen Arves, "Amid Resurgence of Interest in Overdraft, New Data Reveal How Inequitable It Can Be," Financial Health Network, September 2021.

13 MK Falgout, Meghan Greene, & Necati Celik, "Overdraft Trends Amid Historic Policy Shifts," Financial Health Network, June 2023.

14 The SHED, *supra* n.9, has found similarly sized disparities, albeit at different levels.

15 "FDIC Study of Bank Overdraft Programs," Federal Deposit Insurance Corporation, November 2008.

16 "Data Point: Frequent Overdrafters," Consumer Financial Protection Bureau, August 2017.

17 Survey research – both our own and also the Bureau's Making Ends Meet research – has identified a far smaller population of frequent overdrafters. We have found that 9% of overdrafters – representing roughly 1.5% of all banked households – report having incurred more than 10 overdraft fees in a year, Overdraft Trends Among Historic Policy Shifts,. The Bureau found that 3.2% of households reported more than 10 overdraft fees and the Federal Reserve Bank of New York found that under 1% of individuals reported overdrafting more than 10 times. Learning by Bouncing: Overdraft Experience and Salience (Liberty Street Economics, April 1,2024). The differences between the survey findings and findings from the administrative data may reflect difficulties consumers have in recalling precisely how many fees their household incurred over a 12-month period as well as some reticence to acknowledge the frequency with which such fees are incurred but also may reflect changes in the intensity of overdraft usage since 2011-2012 .

frequent overdrafters using administrative data, including data from consumers' credit reports.[18] Our research confirms and adds further texture to the Bureau's findings. For example, we have found that of those who reported incurring more than 10 overdraft fees in the prior year, fully 82% were Financially Vulnerable.[19] To put that in context, the majority of the Financially Vulnerable have household incomes of $30,000 or less and only 9% report that they were able to pay all of their bills on time during the prior year.[20]

Although overdrafting is thus not an uncommon experience especially among those who are struggling financially, it often does not produce a large amount of liquidity. The CFPB found that in 2011-2012, the median overdraft transaction was for just $50[21] and although some recent industry-sponsored research has suggested that this has ticked up over the ensuing decade,[22] in the survey we conducted in January 2023 we found that 48% of respondents who recalled the size of their most recent overdraft transaction reported it was for $50 or less.[23] The same held true in our recent, not yet published survey and in a just-published survey conducted by the Federal Reserve Bank of New York.[24] And, the Bureau has recently reported that in data it has collected through supervisory examinations, the percentage of transactions for which the amount of overdraft coverage provided was less than the relevant per-item overdraft fee ranged from 32% to 74% across institutions.[25]

Furthermore, our research indicates that the liquidity that overdraft provides is often obtained inadvertently. In our 2023 survey, 50% of respondents said that, with respect to their last overdraft transaction, they did not realize that their account balance would be insufficient to cover the expense when they made the transaction and another 28% said they knew their balance was low but thought there was a chance it would cover the expense; only 16% said they knew that their account balance wouldn't cover the expense but chose to proceed anyway. (The remaining 6% did not know which of these was true.)[26] This varied substantially with the intensity of overdraft usage:

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18 "Data Point: Frequent Overdrafters," Consumer Financial Protection Bureau, August 2017.

19 MK Falgout, Meghan Greene, & Necati Celik, "Overdraft Trends Amid Historic Policy Shifts," Financial Health Network, June 2023.

20 *Id.*

21 "Data Point: Checking account overdraft," Consumer Financial Protection Bureau, July 2014.

22 Hank Israel & Don Kumka, "Competition Drives Overdraft Disruption," *available at https://curinos.com/our-insights/competition-drives-overdraft-disruption/*. This study, which was based on data collected from a convenience sample of 14 banks with assets between $10 billion and $100 billion, reported that the average overdraft transaction in 2019 was for $198.

23 MK Falgout, Meghan Greene, & Necati Celik, "Overdraft Trends Amid Historic Policy Shifts," Financial Health Network, June 2023. This calculation excludes the 3% of respondents who did not recall the size of their most recent overdraft.

24 Learning by Bouncing: Overdraft Experience and Salience (Liberty Street Economics, April 1,2024). In this survey 49% of overdrafters reported that their "typical" overdraft produced a negative balance of $50 or less.

25 "Supervisory Highlights Junk Fees Update Special Edition: Issue 31, Fall 2023," Consumer Financial Protection Bureau, October 2023.

26 MK Falgout, Meghan Greene, & Necati Celik, "Overdraft Trends Amid Historic Policy Shifts," Financial Health Network, June 2023.

for example, among those who incurred one overdraft fee, only 8% did so knowing that their account balance wouldn't cover the expense, whereas among those with more than 10 overdraft fees, 35% said that they knew their account balance was insufficient when they made the last transaction that incurred an overdraft fee.[27] Even among this latter group, however, fully 59% either were uncertain whether they would incur an overdraft fee or believed they had sufficient funds to cover the transaction.[28] (Another 6% reported that they did not know what they had thought at the time.) The results from our most recent survey, conducted in January 2024, confirm these findings.[29] And, the New York Federal Reserve Bank's just-published study, which asked overdrafters what percentage of their overdrafts were expected at the time the transaction was made, found that 2% of respondents anticipated all of their overdrafts while 58% anticipated none.[30]

At the same time, the data suggest that the liquidity that overdraft can provide is valued by, and important to, many consumers. We found in our 2023 survey that 60% of consumers preferred to incur the overdraft fee on their most recent overdraft transaction rather than having the transaction declined or returned.[31] Not surprisingly, this was especially true for those who knew that their balance was insufficient to cover the transaction that resulted in an overdraft – 92% of that group preferred incurring the fee – but even among those who had believed that their balance was sufficient, more than half (53%) preferred incurring the fee to having the transaction declined or returned.[32]

In our most recent (not yet published) survey, we asked the intentional overdrafts – those who said that they knew that their balance was insufficient to cover their last overdraft – what they would have done if overdraft had not been available to them. Just under half said that they would have covered the transaction in some other way, including by borrowing from friends and family (16%) or using a credit card (12%). (Only 3% said they would turn to a payday or pawn loan). However, 39% said they would not have made the purchase or payment without the availability of overdraft and another 15% said that they did not know what they would have done. It stands to reason that at least some of those who would not have made the purchase or payment would have suffered some degree of hardship as a result.

[27] *Id.*

[28] *Id.*

[29] The CFPB likewise found in its Making Ends Meet survey that 43% were surprised to incur an overdraft fee on their most recent transaction, 35% thought it was possible, and 22% expected to incur a fee; we view this finding as broadly consistent with our own research. The Bureau also found, consistent with our research, that the expectations varied based on the intensity of overdraft usage.

[30] Learning by Bouncing: Overdraft Experience and Salience (Liberty Street Economics, April 1,2024).Of the remainder, 28% said that their overdrafts were expected about ten percent of the time while between 3% and 5% expected their overdrafts between 25 percent and 75 percent of time.

[31] *Id.*

[32] *Id.*

Adding to the picture, the CFPB's recent analysis of credit availability for those incurring overdraft fees does indicate that, as could be expected, the availability of other forms of mainstream credit is correlated with the intensity of overdraft usage. Although over two-thirds of non-overdrafters had credit available on a credit card, among those incurring one to three overdraft fees, roughly one half (52%) had credit available and among those incurring more than 10 overdraft fees, only about a third (36%) had credit available on a credit card.[33]

We draw from these findings two main conclusions that are directly relevant to the policy and legal questions posed by the Bureau's NPRM.

First, given the financial fragility of those who incur overdraft fees – and especially the frequent overdrafters who bear the lion's share of overdraft costs – it is problematic, to say the least, if the fees they are paying are disproportionate to the costs of delivering the service. The CFPB's 2013 finding that net losses from overdraft represented only 14.4% of net overdraft fees from a group of large banks, the New York Department of Financial Services' recent finding that the cost of overdraft was 35% of overdraft revenue for New York banks and credit unions, and the CFPB's recent finding that across five large institutions net losses from overdraft represented 16.4% of overdraft fees all strongly indicate that, in fact, is the case. [34,35,36]

Second, unless and until our society is able to address the root causes of persistent cash shortfalls, there will be a sizable segment of families who periodically are challenged to make ends meet and for whom credit is essential. We believe that depository institutions can and should play an important role in meeting that need by providing both small dollar installment loans and also, as discussed in Part III, by offering a low-cost overdraft line of credit that enables consumers to amortize the amount they borrow over several months. But although there have been some promising developments along these lines, the reality is that in today's world a sizable segment of hard-pressed consumers do not have better alternatives available to them and prefer to pay an overdraft fee to obtain liquidity rather than to forgo the transaction. Consequently, any effort to rein in the level of overdraft fees to protect vulnerable consumers needs to be done cautiously so as to assure that the result is not to unduly restrict access to overdraft for those who find themselves needing this form of liquidity. As we discuss below, we believe this is an eminently achievable goal within the confines of this rulemaking.

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[33] Calculations from Table 13. See "Overdraft and Nonsufficient Fund Fees: Insights from the Making Ends Meet Survey and Consumer Credit Panel," Consumer Financial Protection Bureau, CFPB Office of Research Publication No. 2023-9, December 2023.

[34] "CFPB Study of Overdraft Programs," Consumer Financial Protection Bureau, June 2013, p.17.

[35] "Consumer Fee Practices in New York," New York State Department of Financial Services, July 14 2023.

[36] The CFPB found the average overdraft fee at these institutions to be $32.50 and the average amount attributable to losses to be $5.34 per fee assessed. See "Overdraft and NSF Practices at Very Large Financial Institutions," Consumer Financial Protection Bureau, January 2024.

II. Defining the Line of Demarcation for "Covered" and "Non-Covered" Overdraft

The heart of the NPRM is its proposal to draw a new line between overdraft programs that are covered by the Truth in Lending Act (TILA") and non-covered programs. The Bureau's rationale for drawing such a line appears to rest on three premises: first, that when a depository institution covers a transaction for which there is insufficient funds in the consumer's account, the institution creates a "debt" for which payment is deferred and thus extends "credit' as defined in TILA[37]; second, that the overdraft fees that depository institutions charge are "incident to the extension of credit" and thus fall within the literal terms of the Truth in Lending Act's definition of "finance charge"[38]; and third, that when, in 1969, the Federal Reserve Board excluded overdraft fees from the definition of "finance charge" in Regulation Z, it did so as an exercise of its discretionary authority to create "adjustments and exceptions for any class of transactions, as in the judgment of the Board are necessary or proper to effectuate the purposes" of the Act.[39]

We leave it to others to debate these premises. Suffice it to say that the premises seem to us entirely reasonable and, indeed, may be beyond dispute.[40]

Based on these premises, the NPRM indicates that the CFPB has preliminarily concluded that it has the authority to revisit the scope of the overdraft exclusion and can revise it based on its judgment, in light of developments in the market since 1969, as to what is currently "necessary or proper'' to effectuate TILA's purposes. On that theory, the NPRM proposes to narrow the exception as it pertains to what the Bureau terms "very large financial institutions" and to exempt only fees that are set at a breakeven level. The NPRM reasons that this narrowing "would return the exception to its original conception—excepting overdraft services from Regulation Z when offered as a courtesy or

[37] 15 U.S.C. § 1602(f).

[38] 15 U.S.C. § 1605(a).

[39] 15 U.S.C. § 1604(a). The language quoted in text is from the statute as it stood in 1969 when the Board excluded overdraft fees from the definition of finance charge. P.L. 90-321 § 105. In 1996, Congress granted the Board the further authority to "exempt, by regulation, from or all or part of [TILA] any class of transactions … for which, in the determination of the Board, coverage … does not provide a meaningful benefit to consumers in the form of useful information or protection." P.L. 104-208, § 2102(b), 15 U.S.C. § 1604(f).

[40] The Federal Reserve Board viewed overdraft as a form of credit at least since 1981 when it amended Reg. E to create an exception to the "compulsory use" prohibition so as to permit overdraft lines – which the Board referred to as "overdraft credit" – to be conditioned on repayment via a preauthorized electronic transfer. 46 Fed. Reg. 2972 (1981). (This exception was not thought to be necessary for "plans [that] have automatic debiting whenever funds are deposited into the consumer's account" as those payments were not considered "preauthorized transfers." 45 Fed. Reg. 66348 (Oct. 8, 1980)). As the NPRM notes, the OCC viewed overdraft as credit at least by 2001, 89 FR at 13858 n.64, and in 2005 the banking regulators issued joint guidance governing the offering of what the guidance termed this "credit service," 76 Fed. Reg. 9127, 9128 (Feb. 24, 2005).

accommodation to customers—while adapting it to fit within the modern payments system."[41] In this regard we would note that the individual who is generally credited to be the father of the automated overdraft programs that are prevalent today believed it was necessary to position these programs as a "courtesy" in order to avoid coverage under TILA.[42]

To this we would add that, in our view, at least for those consumers who are customers of the set of institutions to which the rule applies, the proposed approach to overdraft fees also would address what we have identified as one of the primary financial health concerns raised by overdraft as it exists today: namely, that the fees are "disproportionate to the cost of delivering the service" and thereby "exacerbate financial burdens for those already struggling households."[43]

The narrowing of the overdraft exception proposed in the NPRM, if finalized, inevitably would lead to a significant reduction in overdraft fee revenue. It could, as the NPRM acknowledges, affect the level of and/or frequency with which account maintenance fees are charged although the Bureau has found that revenue from accountant maintenance and ATM fees remained flat from 2019 to 2022 even as overdraft revenue declined by nearly 50%.[44] Be that as it may, we do not believe – as some have suggested – that the proposed narrowing of the overdraft fee exception necessarily will result in a reduction of access to the liquidity that overdraft provides for those who may need it.

In our view, it is unlikely that depository institutions – who, we believe, are genuinely interested in serving their customers and advancing customers' financial health – would elect to withdraw liquidity that as many as one-sixth of their customers are using today if the depository institutions were able to continue to offer that service and still cover their costs of doing so. But the "if" in the prior sentence is an important one: it seems to us entirely unrealistic to expect depository institutions to provide overdraft services to the same extent that they do today if the institutions cannot reasonably expect to recover their costs, including the credit losses associated with extending this form of credit as well as any variable operational costs.

[41] 89 Fed. Reg. at 13868. As the NPRM notes, this was the way Board staff conceptualized overdraft in offering an official interpretation in 1977. 42 Fed. Reg. 22360, 22362-63. The Board itself offered a similar perspective in 2004 when it proposed to require new disclosures of overdraft costs under the Truth in Savings Act. *See* 69 Fed. Reg. 31760, 31761 (June 7, 2004). ("The exemption was designed to facilitate depository institutions' ability to accommodate consumers on an ad hoc basis"), and the banking regulators adopted this perspective as well in their 2005 guidance cited in the NPRM.

[42] Public Broadcasting System, Frontline: Interview Bill Strunk (Nov. 24, 2009).

[43] MK Falgout, Meghan Greene, & Necati Celik, "Overdraft Trends Amid Historic Policy Shifts," Financial Health Network, June 2023.

[44] 89 Fed. Reg. at 13893, citing "Data Spotlight: Overdraft/NSF revenue in Q4 2022 down nearly 50% versus pre-pandemic levels," Consumer Financial Protection Bureau, May 2023. In a similar vein, Bankrate has reported that "Free checking accounts are still widely available, either on a standalone basis or when signing up for regular direct deposits" and that the "average minimum balance requirement to have the service fee waived is $469, which is the lowest since 2010." See Karen Bennett & Matthew Goldberg, "Survey: ATM fees hit record high while overdraft and NSF fees fell sharply," Bankrate, August 2023.

The Bureau's proposal would allow each covered institution either to calculate its own "direct costs and chargeoff losses" for providing overdraft coverage and charge a "pro rata share" of those costs to each overdraft transaction that incurs an overdraft fee or, alternatively, to charge what the NPRM refers to as a "benchmark" to be set by the Bureau and that effectively would function as a safe harbor.[45] As a practical matter, however, any institution that chose the first method would be taking on legal risk because, if the institution were found to have miscalculated the pro rata cost, the institution would be deemed to be providing TILA-covered "overdraft credit" without complying with the various provisions of Reg. Z that the proposed rule would make applicable to "covered overdraft." And it seems to us relatively unlikely that many depositories would choose to run that risk – and expose themselves to potentially large liability either in private litigation or public enforcement actions – to offer a program that, at best, would be provided at cost.

Accordingly, we believe that covered depository institutions are especially likely to hew to whatever safe harbor the Bureau establishes for defining non-covered overdraft. Thus, here, perhaps more than in other contexts, it is especially important to set the safe harbor at a level that realistically captures the cost it is designed to cover. Given that, we discuss below in some detail our recommendations for the safe harbor level.

Safe Harbor Calculation Methodology: The NPRM poses what can be viewed as a methodological question regarding setting the safe harbor that will define non-covered overdraft: should the Bureau factor in both "transactions that resulted in an overdraft fee and … overdraft transactions that did not result in an overdraft fee" or should it, instead, "count[] only … overdraft transactions that resulted in an overdraft fee."[46] The difference is quite material as the Bureau's data indicates that 50% of overdraft transactions do not result in a fee.

If the Bureau adopted the former method, it would necessarily follow that the safe harbor would not be sufficient to cover overdraft costs since, as a matter of law, depository institutions *cannot* charge overdraft fees on transactions that are authorized by an institution, i.e., authorized-positive, settle-negative transactions.[47] Moreover, many depository institutions, especially in the last several years, have adopted consumer-friendly policies pursuant to which they do not charge fees on certain classes of transactions for which they would be free, as a matter of law, to assess a fee. These include policies that provide consumers with a 24-hour grace period before an overdraft fee is assessed, policies that cap the number of fees that can be charged in a given day (including policies of at least one bank that limit the charges to one fee per day), and policies that exempt transactions or negative balances below a certain size from overdraft charges (including policies that provide a

[45] 89 Fed. Reg. at 13869.

[46] 89 Fed. Reg. at 13871.

[47] For consumers who have not opted in to debit card overdraft coverage, such fees are precluded by Reg. E. For consumers who have opted in, such "surprise" fees have been deemed to be unfair by the CFPB. See Circular 2022-06, 87 Fed. Reg. 66935 (Nov. 7, 2022), the FDIC, Supervisory Guidance on Charging Overdraft Fees for Authorized Positive, Settle Negative Transactions (April 26, 2023), the OCC, Overdraft Protection Programs--Risk Management Practices (April 26, 2023), and the Federal Reserve Board, Consumer Compliance Supervision Bulletin -- July 2018.

$50 or even $100 cushion before overdraft fees are assessed). These policies mitigate the risk that consumers will be hit with overdraft fees that they did not expect and reduce the overall cost to consumers of inadvertent (or even intentional) overdrafts. All of these policies would be at serious risk if the Bureau were to set the safe harbor by spreading overdraft costs over all overdraft transactions without regard to whether the transaction resulted in an overdraft fee.

The NPRM recognizes this risk in setting forth the methodology that banks would be permitted to use if they were to calculate their breakeven fee without regard to the safe harbor. For those banks, the NPRM would expressly allow overdraft costs to be spread over only those transactions that incur a fee, thereby "giv[ing] financial institutions flexibility to maintain or to implement fee waiver policies." We believe the Bureau should take the same approach in setting the safe harbor and thus should choose a benchmark that would allow depository institutions to cover their costs from the share of transactions that incur a fee. To do otherwise would lead to less forgiving waiver policies as well as an overall reduction in access to overdraft. Indeed, given that, as noted above, roughly 50% of overdraft transactions do not incur a fee, if the safe harbor were calculated based on all overdraft transactions it likely would have a substantial impact both in narrowing these accommodations and also in reducing access.

Safe Harbor Data Points: In proposing alternative numbers for the safe harbor, the Bureau not only offered alternative methodologies as just discussed but also looked to two alternative sets of data. One set of calculations is based on the average overdraft costs across the five institutions for which the Bureau has obtained data; using those data point yielded proposed safe harbors of $3 (if those costs were factored over the average number of all overdraft transactions) or $6 (if, as recommended above, the costs were factored over the average number of transactions incurring a fee). The alternative set of calculations used data from the institution with the highest costs, yielding proposed safe harbors of $7 and $14.

At first blush, it might seem that using average costs is a sounder approach than using the costs of the institution with the highest costs, as that institution potentially could be an outlier and basing a safe harbor on its data could produce an inflated number. However, because the Bureau was able to collect data from only five of the upward of 125 institutions that would be potentially subject to the rule, the average is necessarily unstable and could be artificially skewed down by an outlier at the low end of the spectrum.[48] Further, the five institutions from whom the Bureau collected data are not necessarily representative of the run of institutions covered by the proposed rule – to protect confidentiality, the Bureau has not provided any description of the size or nature of these institutions – making the average less probative of an appropriate safe harbor.

Given this uncertainty, we recommend that for this initial rulemaking the Bureau set the safe harbor level using the data from the institution in the Bureau's data with the highest average costs. In

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48 The Bureau identified 125 depository institutions with consumer overdraft programs and assets over $10 billion in a Data Spotlight regarding NSF fees issued in October 2023.

concrete terms, that would mean setting the safe harbor level at $14 (or, potentially, rounding up to $15). That would still represent a sizable reduction from the $34 being charged today on average, saving low-balance account holders, on average, just over $90 per year[49] and frequent overdrafters at least $220 per year. And, using this benchmark for the safe harbor would reduce the risk of restricting credit access as the Bureau's data indicates that the institutions covered by those data would be able to recover their costs for 96.3% of low balance accounts and 98.5% of all accounts without having to charge fees on a greater share of overdraft transactions. (In contrast, with the $7 benchmark, the institutions would not cover their overdraft costs for 40% of low balance accounts.)[50]

Additionally, setting the safe harbor level at $14 would give the Bureau the assurance that the safe harbor would accommodate the fee charged by Bank of America which has adopted an industry-leading fee level of $10 among large institutions, and would be at least within striking distance of three of the other top 20 banks as measured by overdraft revenue in 2021.[51]

At the same time, we urge the Bureau to commit to continue monitoring the market and to collecting a more robust dataset that would allow the Bureau, in a future rulemaking, to reassess the safe harbor level if the data so warranted. Such an ongoing data collection also will be important to determine whether the safe harbor needs to be adjusted periodically to account for inflation as would seem likely if the average size of overdraft transactions were to increase in nominal dollar terms. And, such an expanded data collection could be extended to depository institutions with less than $10 billion in assets so that the Bureau can develop the empirical basis for extending the rule to all depositories, potentially with differing safe harbors for different size institutions based upon their costs.

III. Regulating Covered Overdraft

Under the proposal, overdraft fees that are set above breakeven level would be deemed to be finance charges and thus the overdraft would be covered by TILA. Toward that end, the proposal would require that the overdraft be structured as a credit account separate from the asset (i.e., checking) account. Under this structure, if a consumer overdraws their checking account, money would be pulled from the credit account and added to the asset account to cover the overdraft. At periodic intervals, the consumer would receive a statement showing the amount due on the credit account and the due date of such payment, which payment the consumer could choose to make from money in the checking account. However, deposits that the consumer makes after accessing

49 The NPRM reports that in 2022 low balance accounts paid on average $220 in overdraft fees. 89 Fed. Reg. at 13889.

50 "Overdraft and NSF Practices at Very Large Financial Institutions," Consumer Financial Protection Bureau, January 2024.

51 The Bureau's matrix of Overdraft/NSF metrics for Top 20 banks based on overdraft/NSF revenue reported during 2021 indicates that as of December 6, 2022, Huntington National Bank, Manufacturers and Traders Trust Company, and Green Dot Bank were all charging $15.

the credit account would add to the checking account balance and would not automatically repay the credit account.

This is, of course, the way that overdraft lines of credit – which, since the promulgation of Reg. Z in 1969 have been understood to be covered by TILA[52]– have always worked and the way that they work today for the relatively small group of consumers who qualify under current underwriting standards deployed by most depositories offering the product. It is also the way that checking accounts that are linked to a credit card account work. And, we agree that these same basic requirements should govern all forms of covered overdraft as these are core elements of TILA.

The NPRM proposes two changes to the rules that have heretofore governed overdraft lines of credit. First, the Bureau proposes to repeal the exception to the EFTA's no compulsory-use rule that the Board added as part of Regulation E and that currently allows depositories to condition overdraft lines of credit on repayment via preauthorized electronic debits.[53] Second, the Bureau proposes to repeal an exception to the definition of "credit card" that the Board adopted as part of Reg. Z so that overdraft lines of credit that can be accessed by a debit card or through an account number that can be used to purchase goods or services would be deemed to be a credit card and subject to the provisions of TILA and Reg. Z that apply to credit cards, including the provisions of the Credit Card Accountability Responsibility and Disclosure Act (CARD Act).

As a general matter, we see merit in shoring up the regulations governing overdraft lines of credit as the Bureau expands the parameters of covered overdraft. We are concerned, however, that absent some regulatory flexibility the Bureau's proposal could have the unintended consequence of stifling and even shutting down potentially useful innovation in the small dollar credit arena.

In particular, we can envision a small dollar overdraft line of credit product that, by allowing consumers who go negative on their checking account to repay the debt in manageable installments, would better enable consumers to manage their financial lives – and thus advance their financial health – than traditional overdraft which is repaid out of the next deposit even if the overdraft fee were priced at a breakeven level. The product we envision would have a number of core elements including:

- A modest limit comparable to shadow overdraft lines (e.g., up to $250 or $500), which is automatically accessed to cover overdrafts up to the line limit.

[52] As originally promulgated, Reg. Z provided that overdraft charges are excluded from the definition of finance charges "unless the payment of such checks and the imposition of such finance charge were previously agreed upon in writing." 34 Fed. Reg. 2002, 2004 (Feb. 11, 1969). With minor revisions, that language continues to be part of Reg. Z. 12 C.F.R. § 1026.4(c)(3). And since overdraft lines of credit do operate under written agreements for paying overdrafts and imposing interest, they have always been understood to be covered by Reg. Z.

[53] Under EFTA, a lender cannot "condition the extension of credit to a consumer on such consumer's repayment by means of preauthorized electronic fund transfer." 15 U.S.C. § 1693(k)(1). Reg. E creates an exception for "for credit extended under an overdraft credit plan." 12 C.F.R. § 1005.10(e)(1).

- An amortization schedule that assures each draw is repaid in a relatively short period (e.g., no more than three or six months).
- Careful underwriting to assure that the consumer will have the ability to make the required payments.
- Free transfers to the checking account to cover overdrafts with interest on outstanding balances assessed at a fair, periodic rate.

We are aware of one large bank that has introduced a product with many of these features. Specifically, in September 2022 Regions Bank introduced what it terms its "Protection Line of Credit" with a limit that can range from $50 to $500 and an APR of 12%. The product is offered to consumers who have been Regions' customers for 12 months, thereby allowing Regions to underwrite the product based on cash flow data. If a consumer accepts the offer, the Protection Line of Credit is linked to the consumer's checking account and automatically covers overdrafts; the consumer cannot use the line for other purposes without obtaining express authorization from the bank, thereby reducing the risk that consumers will use the product on top of non-covered overdraft. Consumers with outstanding Protection Line of Credit balances receive monthly statements and have 10 days to make the minimum payment which is set at 10% of the outstanding balance with a minimum of $5. If a consumer fails to make the minimum payment by the due date a $5 late fee can be assessed.[54]

As suggested above, we see significant potential benefits for consumers in a product structured along these lines, although the fact that Regions' minimum payments are tied to the outstanding balance – and thus will decline as the balance is paid off, thereby extending the term – seems to us suboptimal. But to leave room for innovative and affordable small dollar overdraft line of credit products along these lines we urge the Bureau to clarify certain aspects of Reg. Z that would apply to such products and also to create an exception to certain of Reg. Z's requirements for affordable, small dollar overdraft line of credit products meeting specifications established by the Bureau along the lines set forth above. In particular, we suggest that the Bureau:

1. Clarify that cash flow underwriting suffices to satisfy the ability to pay requirement contained in Reg. Z, even if the creditor does not specifically identify "debt obligations" from the cash flow data;[55]

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[54] The terms of this product can be found in A Quick Guide to Your Regions Protection Line of Credit. See also How can I access my Regions Protection Line of credit?.

[55] Reg. Z, requires credit card issuers to "establish and maintain reasonable written policies and procedures to consider the consumer's ability to make the required minimum payments," and further provides that such policies and procedures must "include consideration of at least one of the following: The ratio of debt obligations to income; the ratio of debt obligations to assets; or the income the consumer will have after paying debt obligations." 12 C.F.R. § 1026.51(a)(ii). The Official Interpretation to this provision adds that "A card issuer may consider the consumer's current obligations based on information provided by the consumer or in a consumer report." Ibid. Comment 1026.51(a)(i)-7. Since cash flow underwriting does not involve the use of a "consumer report" or require the consumer to list "current obligations" – and since the underwriter may not necessarily seek to determine, through the consumer's transactional data, which transitions constitute repayment of "debt obligations" – there is some uncertainty as to whether such underwriting is consistent with Reg. Z.

2. Allow for payments on affordable, small dollar line of credit products to be scheduled bi-weekly or semi-monthly; and for repayment periods of less than 21 days after a statement is mailed or delivered[56],[57]; and
3. Relieve creditors of the special dispute resolution and chargeback rules applicable to credit cards[58].

The Bureau may also want to consider whether all of the credit card-specific disclosure requirements – both for account openings and for periodic statements – are well suited for an affordable, small dollar overdraft line of credit product and also whether including the account agreements for such products within the Bureau's credit card agreement database would create more confusion than value.

To be clear, we recognize that the path of least resistance, if the proposed rule were to be finalized, will be for depository institutions to reduce their overdraft fee to the safe harbor level and continue to offer non-covered overdraft. We expect most depositories would proceed down that path which, as previously discussed, we believe would lead to healthier outcomes for consumers – and especially for frequent overdrafters – than the status quo. But as also discussed above, because such products recoup the money that is advanced to cover an overdraft from the consumer's next deposit, these products can make it challenging for hard-pressed consumers to manage their financial lives and may be less desirable than a product that allows an advance to be repaid in manageable installments, at least so long as the product is structured to avoid creating persistent debt. Accordingly, we urge the Bureau to use its exception and adjustment authority under TILA to leave room for such affordable, small dollar line of credit products.

We again thank the Bureau for this opportunity to comment on the proposed rule. We stand ready to support the Bureau in any way that would be helpful, including sharing any further information the Bureau desires concerning our research findings, as the Bureau moves forward to issue a final rule.

56 Reg. Z requires that the payment due date "shall be the same day of the month for each billing cycle." 12 C.F.R. § 1026.7(b)(11)(i). It is unclear whether a card issuer can have multiple billing cycles in a month so long as each cycle has the same payment due date although the language of the CARD act implies a single payment cycle ("The payment due date … shall be the same day each month"). 15 U.S.C. § 1637(o)(1).

57 The CARD Act requires issuers to adopt "reasonable procedures designed to ensure that each periodic statement…is mailed or delivered …not later than 21 days before the payment due date." 15 U.S.C. § 1666b(a).

58 *See* 12 C.F.R. § 1026.12.