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NBA Nebraska Bankers Association

July 26, 2004

Jennifer J. Johnson, Secretary
Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue, NW
Washington, DC 20551

RE: Overdraft Protection Guidance
Docket No. OP-1198

Dear Ms. Johnson:

We appreciate the opportunity to comment on the proposed Interagency Guidance on Overdraft Protection Programs issued by the member agencies of the Federal Depository Institutions Examination Council ("Agencies"). The Nebraska Bankers Association (NBA) is a trade association representing 262 of the 264 commercial banks and 9 of the 16 savings and loans in the state of Nebraska. Many of our financial institution members which utilize discretionary overdraft services, including so-called "bounce protection" type services, will be impacted by the Agencies' Proposal. Our comments on the Proposal are set forth below and are identified by the title of the section of the Proposal to which they relate.

Concerns

The proposal characterizes overdraft protection services as "intended essentially as short-term credit facilities." We would submit that the Agencies need not mischaracterize discretionary overdraft services as short-term credit facilities to address the concerns outlined in the Proposal. If indeed institutions do not clearly disclose the nature of the overdraft protection services they offer, the Agencies *and* consumers have adequate remedies under existing law to address any misleading or deceptive practices. We share the commitment of the Agencies to the promotion of accurate disclosure and feel that transparency is integral to public confidence in the overdraft protection services provided by all depository institutions; however, we see no point, other than attempting to establish a basis for imposing capital requirements, for the characterization of these services as "short-term credit facilities" if there is no contractual obligation on the part of the depository institution to pay the overdraft.

Safety & Soundness Considerations

We believe that the 30-day time frame for charge off of an overdraft is too short. It has been the experience of our financial institution members that 90% of consumers will, within a 45- to 60-day time period, deposit sufficient funds in their transaction account to clear any overdraft created.

We believe that charge off of an overdraft balance within 30 days from the date first overdrawn is too inflexible. In many cases, if not most, such an approach is premature and results in unnecessary expense to both the depository institution and the consumer. Once a transaction account is charged off, the account number is often removed from the system of the depository institution. If the customer pays the overdraft amount and wishes to reactive the transaction account, new account documentation usually must be executed, a new account number must be assigned and new checks must be printed for the new account.

In addition to the added costs associated with opening a new account, many institutions report the charge off of a transaction account to credit bureaus. In light of the fact that a large percentage of overdrafts will be paid in full by consumers within the 45- to 60-day period, the premature charge off of an overdraft would be detrimental to the credit history of many consumers. The "Best Practices" suggested by the Agencies urge that depository institutions not report negative information to consumer reporting agencies when overdrafts are paid under the terms of the transaction account agreement. Premature charge off of an overdraft results in many cases in the truthful, but largely unnecessary, reporting of negative information to consumer reporting agencies.

It has also been the experience of many of our Financial Institution members that charging off an overdraft reduces the chances of collection of the overdraft dramatically. One of the overdraft protection program vendors utilized by a number of our Financial Institution members has indicated that their customers report that their success rate in the collection of overdrafts has gone from 20%, where the overdraft is charged off within 30 days, to over 80%, where the account is not charged off for an additional 15 to 30 days. That recovery rate also applies where the overdraft is converted to a closed-end, interest-free, loan in which the consumer is given an opportunity to pay the overdraft in installments. By the addition of a very small increment of time, consumers are provided a greater opportunity to avoid additional costs and negative impact on their credit rating, and depository institutions dramatically increase the likelihood that they will recover on the overdrafts.

We also strongly disagree with reporting the available amount of overdraft protection as an "unused commitment." "Commitment" is defined as "an agreement or pledge to do something in %hefuture; an engagement to assume a financial obligation at a future date." Discretionary overdraft protection services do not involve agreements or engagements to pay overdrafts at a future date. They are *discretionary* services, accommodations to consumers, that are exercised at the sole option of the depository institution. While some institutions may "routinely communicate the available amount of overdraft protection to depositors," the promotional materials that communicate that information generally make clear that payment of any overdraft is purely discretionary, that the depository institution will consider payment of reasonable overdrafts only as long as the account is in good standing, but that the depository institution has no obligation to pay any item, even if the account is in good standing and even if overdrafts have been paid in the past. It could not be more clear that there is no obligation on the depository institution's part to pay items that create an overdraft on the customer's account.

Thus, while the promotional materials provide more detailed information relating to the criteria considered by a depository institution before paying an overdraft, and may even include the available amount of overdraft protection, the disclosure of that information does not constitute a written agreement to pay overdraft items in the future. It is, rather, merely a restatement of the provisions of the agreement governing the maintenance of the transaction account and the disclosure of the depository institution's policies with respect to the discretionary payment of overdraft items. We submit that the establishment of a limit on the amount of an overdraft a depository institution is willing to permit on a transaction account and the communication of that limit to a consumer is totally irrelevant to the question of whether the limit constitutes an unused commitment that should be reported and subjected to capital standards.

If the Agencies assume that the automation of part or all of the discretionary overdraft payment process divests the depository institution of its discretion to pay or return the item and, therefore, results in a commitment to pay the overdraft items, we respectfully disagree. Even though part or all of the overdraft payment process may be automated, the depository institution always retains discretion to change any of the criteria it uses to make the determination of whether to pay or reject an item or to raise or lower its risk tolerance level in connection with the payment of overdraft items. Moreover, factors unrelated to the criteria used to generate reports, recommendations for payment or ultimate decisions may be relied upon by a depository institution to refuse to pay an item. Depository institutions may receive information relating to the financial condition of a customer from any number of sources, direct or anecdotal and, based on that information, decline to pay overdrafts on that customer's account. Moreover, all depository institutions retain the capability to override the decision or recommendation resulting from an overdraft payment system's analysis and to return, rather than pay, items. In addition, all depository institutions have processes for manual review of items that exceed a certain threshold amount and have the discretion to either pay or return those items. Thus, all depository institutions retain the discretion to alter the system criteria as a whole or alter the outcome of the application of those criteria to a single item. The decision to pay or return an item is, therefore, always at the sole option and discretion of the depository institution, in accordance with the terms of the transaction account agreement.

We believe that the Agencies can address the concerns regarding misleading promotion of the overdraft protection services without mischaracterizing the contractual obligations of depository institutions in the discretionary payment of overdrafts. As the Agencies point out under the "Legal Risks" section of the Proposal, the Agencies have the authority to enforce Section 5 of the Federal Trade Commission Act pursuant to their authority in section 8 of the Federal Deposit Insurance Act. We suggest that the Agencies rely on that authority to address perceived problems of unfair or deceptive practices, rather than forcing depository institutions to comply with reporting provisions that are clearly inapplicable as a means to discourage disclosure of overdraft limits.

BEST PRACTICES

Marketing and Communications with Customers

Fairly represent overdraft programs and alternatives. The Proposal suggests that, when informing consumers about an overdraft protection services, depository institutions should also inform consumers generally of other available overdraft services or credit products and explain to the consumers the costs and advantages of various alternatives to the overdraft protection service. The Proposal could be read to assume that discretionary overdraft services are automatically disadvantageous for all consumers. This approach ignores the fact that the costs and advantages of various alternatives will depend upon patterns of use and the habits of consumers, which are as varied as the consumers themselves. For example, a depository institution may impose an annual or other periodic fees to participate in the service and transfer or transaction fees in connection with individual advances. If the consumer never utilized their overdraft line of credit that imposes such fees, or used the credit line only once in any given year, a discretionary overdraft service would be more advantageous because the customer is charged a fee only if and when an overdraft is paid. The point is that an advantage of one service versus another is relative and completely dependent upon the consumer's own particular pattern of use and habit. If other information should be delivered with the information on the overdraft protection service, we believe that it should be factual information and not conjecture. Thus, if comparisons are suggested, a comparison of annual fees, per transaction fees, periodic fees or periodic rates, payment amounts and due dates, *etc.*, would be much more useful to the consumer. Consumers could determine, based on their own anticipated usage or experience, which of the alternatives is most advantageous in their particular circumstance. We do not believe that the Agencies should adopt the Proposal as drafted based on the Agencies' assumptions regarding the relative merits, or demerits, of discretionary overdraft services.

Clearly explain discretionary nature of program. We agree that if a depository institution promotes a discretionary overdraft protection service, it should not imply that the payment of items under the service is automatic. We believe that many of the abuses that were identified when attention was first focused on overdraft protection services have been "self-corrected" by the industry. Nonetheless, depository institutions should be encouraged to ensure that their advertising or other materials do not overstate the obligation of the depository institution to pay overdrafts.

Most account agreements provide that the depository institution may, in its discretion and at its sole option, pay or return a check or other item presented for payment against insufficient funds. We believe that the final Interagency Guidance ("Guidance") should stress that, if the depository institution retains the discretion to pay or not to pay overdrafts, consumers should be advised that they may not rely on the fact that the depository institution will pay any item, even if it has done so in the past. The Proposal suggests, however, that a depository institution "describe the circumstances in which the depository institution would refuse to pay an overdraft or otherwise suspend the overdraft protection program." This implies that all of the circumstances in which the depository institution would take those actions should be described with particularity. If depository institutions are required to be unnecessarily specific, the delineation gives rise to the implication that items will be paid if all of the criteria set forth are met.

Because depository institutions retain the discretion to pay or not pay the items, that is simply not the case. If the Agencies are concerned about consumers being misled about overdraft protection services, the Agencies should not require disclosures that may lead to such confusion. Rather, the Agencies should require that depository institutions, make clear that, *even if* certain qualifications are met, *e.g.*, an account meets the depository institution's definition of "good standing," items may still be returned unpaid because the depository institution retains the discretion to do so. The emphasis should be on the discretionary nature of the service, not on disclosing the circumstances in which the discretion will be exercised.

Clearly disclose program fee amounts. Many depository institutions provide customers with transaction account agreements that contain terms and conditions for the use of multiple types of accounts and services associated with those accounts. The agreements also provide the disclosures required under the various regulations that may apply to the accounts such as Regulation E, Regulation CC and Regulation DD. Because the terms and conditions and the applicable disclosures are not likely to be amended very often, depository institutions provide cost disclosures on separate inserts that may be reprinted to reflect changes in fees or charges assessed. The foregoing practice does not appear to comport with the Proposal as written. The Guidance should clarify that the practice of delivering a fee schedule that clearly sets forth applicable fees together with account agreements that cross-reference the fee schedule is acceptable practice under the Guidance.

Program Features and Operation

Provide election or opt-out of service. As indicated above, we believe that all depository institutions have provisions in their transaction account agreements that provide that the depository institution may, in its sole discretion, pay or return a check or other item that is presented against insufficient funds. Thus, we believe that in all cases, overdraft protection is automatically provided in transaction account agreements. The Proposal suggests that each depository institution now disclose that overdrafts may be paid and invite each and every account holder to opt out of the service. Although we clearly recognize the right of consumers to decline overdraft protection, we do not see the value in requiring a burdensome opt-out process that does not also clearly explain the potential negative ramifications of declining the service.

If the Guidance does suggest that consumers be given the right to opt out of the service, best practices should likewise acknowledge that depository institutions should obtain a signed written disclosure from the consumer that, by opting out, the consumer understands that (a) no overdrafts will be paid at any time, under any circumstances, no matter what the size of the overdraft that would be created; (b) that there will be a fee assessed for each returned item; (c) that the depository institution is not liable for any fees and charges that are imposed by merchants or other payees to whom items are returned; and (d) that the depository institution is not liable for any consequential damages (*e.g.*, late fees, default charges, increases in applicable interest rates) as a result of the return of any item. It seems clear that, if for no other reason than reputational risk, a depository institution would be ill-advised not to obtain something in writing from the consumer indicating that they understand the consequences of an opt-out.

Alert customer before a non-check transaction triggers any fees. The Proposal acknowledges that giving prior notice that a given transaction will trigger an overdraft fee is not always feasible and suggests that notices be posted instead. We believe that the Guidance should clarify that there are situations, other than access by an ATM, in which it is not possible to post notices. Even with advances in technology, there may be situations in which it will not be possible to give prior notice, such as with preauthorized automatic debits. We would suggest that the Guidance clearly state that, even though such prior notice is not feasible in those instances, the benefit to consumers in having those items paid rather than returned far outweighs the negative effects of eliminating such transactions from the coverage of an overdraft service simply because no prior notice can be provided.

Prominently distinguish actual balances from overdraft protection funds availability. In interchange transactions, the standards have never mandated the display of more than one balance. than one balance. According to shared network standards, the balance that must be displayed is the "available balance" on which the depository institution will base its decision to pay or not pay an item. An expectation that more than one balance would be displayed in an interchange transaction is unrealistic in light of existing interchange rules. If an inquiry is being made at a proprietary machine, it is most common to disclose a "ledger balance" and an "available balance." We believe that use of the terminology "actual balance" is very misleading to consumers since it implies that it is the exact amount that is in an account at a particular point in time. Since transactions may be posting at any point in time and the account balance is always subject to items outstanding, we believe that use of the term "actual balance" should be avoided, and, to our knowledge, no depository institution currently uses the term "actual balance." We suggest that the Agencies make clear that disclosing that something is an "actual" balance may, in and of itself, prove to be confusing or misleading to consumers.

Promptly notify consumer of overdraft program usage each time used. We question the necessity, utility and feasibility of providing a restatement of overdraft protection policies the first time an overdraft is created. Tracking whether a customer has accessed the overdraft service for the first time seems unnecessarily cumbersome and may not be possible under some systems. Most, if not all, overdraft notices contain all of the information that the Proposal suggests be included in the notice. Restating the terms of the overdraft protection service when the service is accessed for the first time is excessive. We believe that a clear reference to information previously provided and an offer to provide a copy on request should suffice.

The Proposal suggests that, where feasible, the institution should notify consumers in advance if the institution plans to terminate or suspend the consumer's access to the service. Although we are strongly committed to full transparency to the consumer, we urge the Agencies to be more specific with respect to when notification of suspension is suggested. If the Agencies are suggesting that depository institutions notify consumers each and every time the service is unavailable for an account, we are of the view that depository institutions are faced with an impossible compliance task. An account may not qualify under a system's parameters for a short period of time and may "requalify" a short time later. If no items were presented during that time that would trigger the service, there is no issue of suspension of the service. Thus, the issue of qualification arises only at the time an item is presented for payment against insufficient funds. There is no way to forecast when that may arise. In addition, because "qualification" is fluid, depository institutions could be continually notifying consumers of the suspension and reinstatement of the service. Moreover, by the lime notification of suspension or reinstatement is received by the consumer, reinstatement or suspension may have occurred again.

We would also suggest that such notification gives the impression that the service is more like a credit line that the depository institution is obligated to fund rather than a discretionary service. The Agencies have expressed concerns that depository institutions not mislead consumers into thinking that there is a guarantee that items will be paid. It seems that notification that the service is or will be suspended and subsequent notice that it is again available may lead consumers to expect that their items will be honored when in fact they may not be.

Consider daily limits. We disagree that there should be a cap on overdraft fees. Each item that is paid avoids the possible imposition of retailer- or payee- assessed fees, late charges and derogatory credit implications. There are no limits placed on the number of items on which a retailer or payee may assess a returned item fee. Moreover, such fees are generally imposed pursuant to statutory provisions that permit collection of return item fees, plus fees imposed by the payee's depository institution.

Thank you for the opportunity to submit our comments on the Proposal to the Agencies. We would be happy to answer any questions the Agencies might have regarding our comments.

Sincerely,

George Beattie

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President
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