June 28, 2019

Comment Intake
Consumer Financial Protection Bureau
1700 G St. NW
Washington, DC 20552
Via Electronic Submission

**RE: Overdraft Rule Review Pursuant to the Regulatory Flexibility Act;
Docket No. CFPB-2019-0023**

Director Kraninger:

Attached to this letter are comments from The Pew Charitable Trusts regarding the Consumer Financial Protection Bureau's (CFPB, or Bureau) request for information noted above. The Pew Charitable Trusts is a global, non-governmental research and public policy organization dedicated to serving the public. We strive to improve public policy by conducting rigorous analysis, linking diverse interests to pursue common cause, and focusing on tangible results. Consumer finance is an area to which Pew has dedicated significant resources in recent years.

Pew's consumer finance team began its work on overdraft in December of 2010, five months after Congress created the CFPB through the Dodd-Frank Act. We did this because there were significant gaps in available research about consumer checking accounts, financial institution disclosures, overdraft programs, and small-dollar credit products at small and large institutions.

Pew's research, as well as that from the CFPB and numerous other sources, makes clear that consumers want to avoid debit point-of-sale and ATM overdraft penalty fees. As noted below, the overdraft rule remains a unique and necessary part of federal law that is strongly supported by public sentiment generally and bank customers specifically. Because of this, and because there is no evidence that the rule has imposed disproportionate burdens on small entities, we believe that there is no basis for amending the rule under a Section 610 analysis. As the Bureau considers the impacts of the overdraft rule, we remain available to provide assistance based on our extensive research and publications on overdraft programs, checking accounts, bank disclosures, and small-dollar credit.

Sincerely,

Nick Bourke
Director, Consumer Finance
The Pew Charitable Trusts
www.pewtrusts.org/small-loans

Attachments: Comment letter; Appendix A

Contents

Overview: There is no basis for the CFPB to adjust the overdraft rule under its Section 610 analysis

Effective January 19, 2010, the Board of Governors of the Federal Reserve System (Board) issued a final rule (overdraft rule) amending Regulation E, which implements the Electronic Fund Transfer Act (EFTA). EFTA was enacted by Congress to expand consumers' rights in the financial system, granting the Board broad authority to carry out the provisions of the law. The overdraft rule limits the ability of a financial institution to assess an overdraft fee for paying ATM and one-time debit card transactions that result in a negative account balance unless the consumer affirmatively consents to such an overdraft program. Today, the CFPB promulgates the overdraft rule. The overdraft rule remains necessary to carry out the provisions of EFTA, specifically to provide consumers with the right to choose their financial products.

The Regulatory Flexibility Act (RFA) requires an agency either to certify that a final rule will not have a significant economic impact on a substantial number of small entities or provide a final regulatory flexibility analysis of those impacts. Additionally, within 10 years of a rulemaking, the promulgating agency is obligated to review the impacts of the rule on these small entities, pursuant to Section 610 of the RFA. As the Bureau conducts its Section 610 review of the overdraft rule to understand its impact and effects, it is required by the Act to consider the following questions:

1) Is there a continuing need for the overdraft rule?
2) Has the public provided comments or complaints about the rule?
3) How complex is the rule?
4) Do other federal or state requirements accomplish the same objectives?
5) Have circumstances changed in a way that may affect regulated entities?

Pew's research shows that there is a continuing need for the overdraft rule and that both checking account customers and the public strongly support policies such as those reflected in the rule. The overdraft rule is a unique legal provision that is serving an important role in protecting consumers and promoting a healthy banking system, with little burden on the system generally or on small providers specifically—though regulators could be doing much more to encourage a safe, transparent, and competitive market for consumers.

- **Section 1** of this letter focuses on the need for the overdraft rule. It shows that the public views overdraft penalty fees negatively, and that most consumers prefer to have ATM and debit overdrafts declined as opposed to having them approved and paying overdraft penalty fees. The cost of overdraft penalty programs falls primarily on low- and moderate-income consumers and is a major cause of customers exiting the banking system. The overdraft rule addresses only some of these problems, but it remains necessary because there are no other federal or state requirements that address the unique challenges of ensuring informed consent for charging overdraft penalty fees on electronic transactions associated with checking accounts.

- **Section 2** discusses how the Bureau can further assist consumers by promoting clearer and more comprehensive disclosures, create a level playing field for providers, and stimulate a competitive market for services.

- **Section 3** shows the evolution of checking account usage, noting the shift away from checks and toward debit cards and demonstrating that a large majority of overdraft activity and revenue is attributable to a small minority of checking account holders who overdraft repeatedly. One-third of all overdrafters primarily view it as a way to borrow money. This section also discusses initial attempts to modernize overdraft regulations to reflect this shift toward credit usage.

- **Appendix A** includes an analysis of the scope of the Section 610 review, noting that this review is limited to small entities, defined by the Small Business Act as having less than $550 million in assets. In this light, any actions the Bureau takes resulting from this review should pertain only to these institutions.

1. The overdraft rule is necessary to protect consumers and has benefitted the banking system

When it promulgated the original rule, the Federal Reserve Board of Governors (Board) believed its adoption could impact a substantial number of small entities. In finalizing the rule, the Board underscored the importance of protecting consumers from automatic enrollment in a penalty fee program for electronic transactions. Results from the Board's consumer testing provide a strong basis for the rule, and the findings shed light on consumers' disposition toward overdraft:[1]

1) While consumers largely prefer to have checks paid through overdraft, many prefer to have ATM withdrawals and debit cards declined if they have insufficient funds.
2) Consumers are generally charged the same fee whether an overdraft on a check is paid (overdraft) or not (nonsufficient funds)—however, having an ATM or debit transaction declined does not trigger any fees.
3) Many consumers are unaware that they could incur overdraft fees at the ATM or point of sale, and erroneously believed that a transaction would only be paid if the consumer had sufficient funds to cover the charge.
4) ATM and one-time point-of-sale debit transactions are the key driver behind the growth in volume and therefore total cost of overdraft fees.

Pew's research on consumer use of overdraft penalty programs shows the continued need for the overdraft rule. Consumers continue to want protection from overdraft penalty fees, and overdrafters tend to feel that the programs hurt them more than help them. Despite these strong concerns, banks rarely discuss these programs or the alternative options available with their customers, even the ones who overdraw often. Consumers remain confused about the programs. These findings emphasize the

[1] 74 FR 59034-59035.

importance of the overdraft rule in requiring a minimum set of disclosures and rights when consumers open accounts, and strongly suggest that the Bureau should do more—not less—to help consumers protect themselves from overdraft penalty charges.

While lucrative overdraft penalty programs may appeal to banks in the short term, federal regulators have prioritized increased participation in the financial system in order to foster public confidence[2] and to provide consumers with financial services.[3] Overdraft penalty programs are detrimental to meeting that longer-term goal.

As discussed in this section, FDIC data show that 30 percent of previously banked customers have left the banking system because the "fees are too high,"[4] and Pew research confirms this. Thus, it is clear that banks and credit unions have lost substantial numbers of customers who have closed their accounts (or had their accounts closed involuntarily) because of overdraft fees. As consumers are pushed out, their confidence in the financial system is eroded, their options for financial services are limited, and the aggregate banking system's pool of customers is smaller.

But the overdraft rule may help regulators meet their long-term goals of financial inclusion and specifically, maximizing the share of banked Americans: Since 2011, the number of unbanked households has fallen by one-fifth, from 8.2 percent to 6.5 percent.[5] It is not clear what role, if any, Regulation E had in contributing to that drop, but it would be important to explore that relationship before considering weakening the protections in Regulation E in general or the overdraft rule specifically.

Consumers want protection from overdraft penalty programs

The Board received over 20,000 comment letters as it promulgated the overdraft rule, the majority of which were submitted by individual consumers. Overwhelmingly, these consumers urged the Board to adopt the proposed opt-in approach, arguing that "the harm to consumers from overdraft fees outweigh any benefits."[6] Further, consumers made these views clear in the Board's consumer testing, and these views are echoed in Pew's surveys of overdrafters and the public. [7]

Research from Pew in 2014 found that a majority of consumers—including 80 percent of overdrafters—support closer regulation of overdraft programs, and over half say overdraft mostly hurts them.[8] Further, more than three-quarters of those who paid an overdraft fee voiced concern about specific overdraft policies—including the cost (at big banks, typically $35 to $38 per transaction), the imposition

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[2] Martin J. Gruenberg, "Remarks -- FDIC Economic Inclusion Summit: Strategies to Bring Consumers into the Financial Mainstream," Apr. 26, 2017, https://www.fdic.gov/news/news/speeches/spapr2617.pdf.

[3] Brian Johnson, "Consumer Protection and Financial Inclusion: Remarks to the Cato Institute's Summit on Financial Inclusion (as prepared for delivery)," Jun. 12, 2019, https://www.consumerfinance.gov/about-us/newsroom/consumer-protection-and-financial-inclusion/.

[4] Federal Deposit Insurance Corporation, "2017 FDIC National Survey of Unbanked and Underbanked Households," (Oct. 2018), 23, https://www.fdic.gov/householdsurvey/2017/2017report.pdf.

[5] Federal Deposit Insurance Corporation, "Unbanked and Underbanked Findings: Banking Status of U.S. Households," accessed Jun. 2019, https://economicinclusion.gov/surveys/2017household/banking-status-findings.

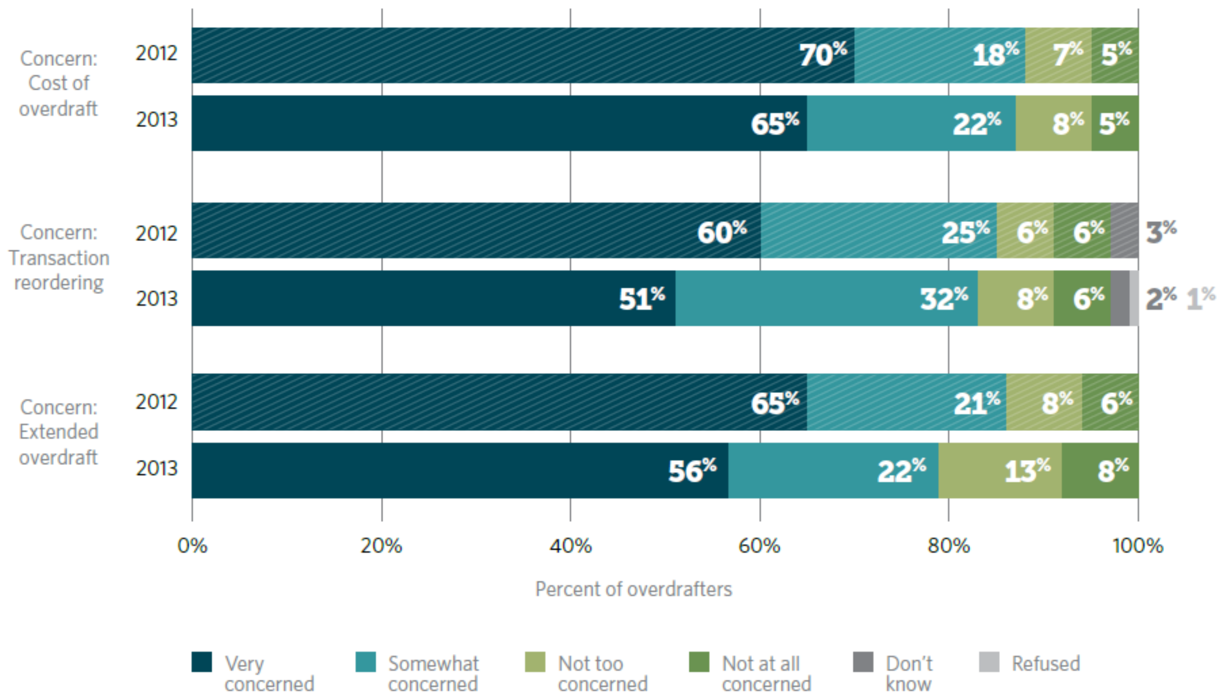
[6] 74 FR 59034-59035.

[7] Pew's overdraft and checking account research is collected at www.pewtrusts.org/banking.

[8] The Pew Charitable Trusts, "Overdrawn: Persistent Confusion and Concern About Bank Overdraft Practices" (2014), 13-14, http://www.pewtrusts.org/~/media/assets/2014/06/26/ safe_checking_overdraft_survey_report.pdf.

of “extended” fees, and the practice at some banks of reordering transaction amounts from largest to smallest to maximize fee revenue.[9] (See Figure 1.)

Figure 1: Overdrafters Continue to Have Strong Concerns About Bank Overdraft Practices



Notes: The 2013 figures for “Extended overdraft” do not total to 100% due to rounding.

Respondents were asked, “Does that make you very concerned, somewhat concerned, not too concerned, or not at all concerned?” for each of these three bank overdraft practices:

a. “Reordering your withdrawals in a way that makes you more likely to overdraft your account.”

b. “Charging a fee of around $35 for each overdraft.”

c. “Charging an extended overdraft fee of around $12.00 for not paying off the overdraft penalty on time, usually within 7 days.”

Source: The Pew Charitable Trusts, “Overdrawn,” (2014)

Pew’s research suggests that tens of millions of customers are unknowingly enrolled in overdraft programs that they do not understand or want. There are around 39 million overdrafters[10] in the U.S., and 68 percent of them would prefer that a transaction be declined as opposed to paying a fee.[11] (See also Figure 2.) However, seven in ten overdrafters (more than 27 million) do not understand that they

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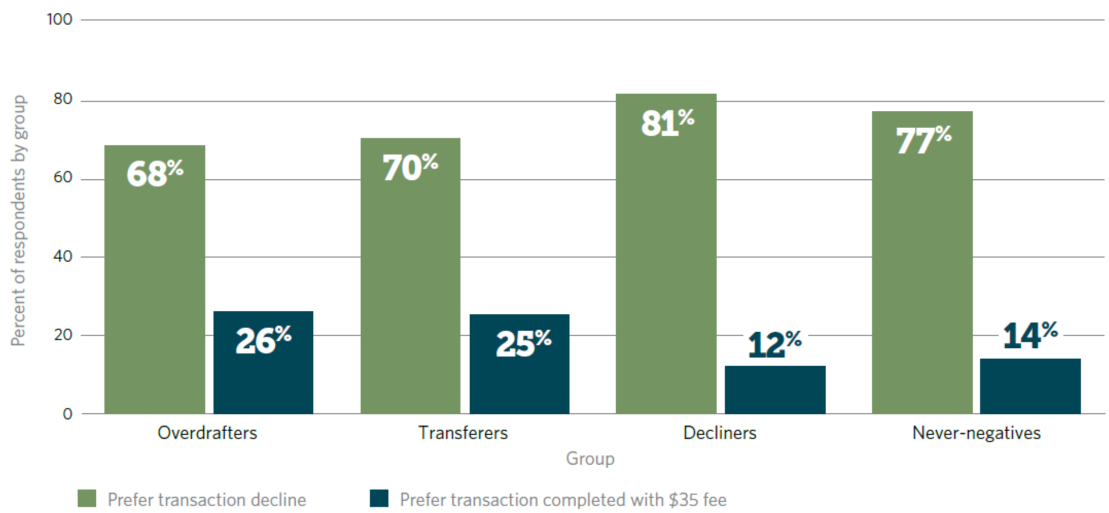
[9] Ibid., 11

[10] The Pew Charitable Trusts, “Consumer Overdraft Survey: Methodology and Topline Result,” updated Mar. 6, 2018, 1, https://www.pewtrusts.org/-/media/assets/2018/03/methodology_od-survey_update_030218.pdf

[11] The Pew Charitable Trusts, “Overdrawn: Persistent Confusion and Concern About Bank Overdraft Practices” (2014), 10, http://www.pewtrusts.org/~/media/assets/2014/06/26/ safe_checking_overdraft_survey_report.pdf

can avoid these fees by simply choosing not to opt in to bank overdraft programs.[12]

Figure 2: More Than Two-thirds of Overdrafters Prefer a Declined Transaction Over the $35 Fee



Note: Respondents were asked, "Pretend for a moment that you are at a store about to use your debit card to make a purchase and that you are unaware there is not enough money in your checking account to cover that purchase, would you rather..."

Source: The Pew Charitable Trusts, "Overdrawn," (2014)

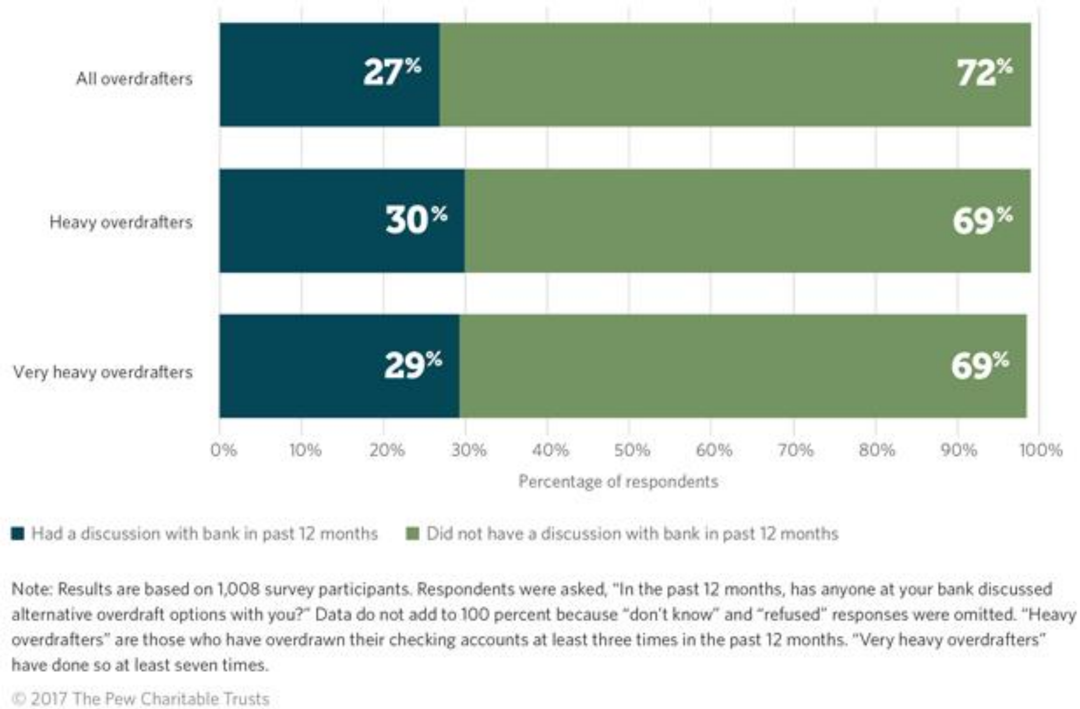
Many banks fail to communicate with consumers about these programs. (See Figure 3.) Pew's 2017 survey of consumers who overdrafted their account in the previous 12 months found that only 27 percent have had a conversation with their bank about their options. This rate is not significantly different among the most frequent overdrafters – or even among those who have done so at least seven times. This research suggests that out of the 39 million Americans who overdrafted in the past year, only 10 million discussed overdraft with someone at their bank.[13] Among these consumers, only 35 percent (roughly 3.5 million) understand they have a right to have their bank decline charges without a fee.[14] This leaves bank customers—including the most frequent overdrafters—with little or no communication about their rights or options outside the initial disclosures required by the overdraft rule, and it helps explain the ongoing frustration and dissatisfaction that bank customers feel about overdraft fees.

[12] The Pew Charitable Trusts, "Overdraft Does Not Meet the Needs of Most Consumers: Bank programs often function as costly, inefficient credit," (Dec. 2017), 2, https://www.pewtrusts.org/-/media/assets/2017/12/cb_overdraft_does_not_meet_the_needs_of_most_consumers.pdf#page=2.

[13] Ibid., 4.

[14] Ibid., 5. This number is derived from taking 35 percent of 27 percent of 39 million.

Figure 3: Banks Rarely Discuss Options, Including with Customers Who Overdraw Often



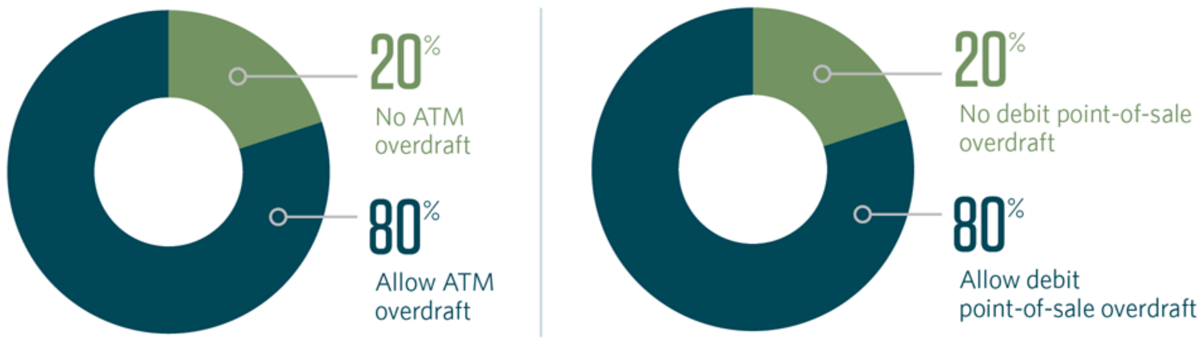
Source: The Pew Charitable Trusts, "Overdraft Does Not Meet the Needs of Most Consumers," (2017)

Despite public preferences, most banks continue to charge overdraft penalty fees rather than decline debit card transactions

The Board responded to negative consumer sentiment and experiences by codifying the overdraft rule, which gave bank customers a right to have information and a choice to enter overdraft programs that is unique in federal or state law. Yet neither the rule nor negative public sentiment discouraged banks from continuing to charge penalty overdraft fees. Pew found that 80 percent of the largest 50 banks continue to have ATM and debit point-of-sale overdraft.[15] (See Figure 4.) Similarly, in Pew's study of 45 smaller banks ($360 million to $1 billion in assets), more than 90 percent allowed customers to incur overdraft penalty fees on ATM and debit point-of-sale transactions.[16]

[15] The Pew Charitable Trusts, "Consumers Need Protection From Excessive Overdraft Costs," Dec. 20, 2016, 8, https://www.pewtrusts.org/en/research-and-analysis/issue-briefs/2016/12/consumers-need-protection-from-excessive-overdraft-costs
[16] The Pew Charitable Trusts, "How a Set of Small Banks Compares on Overdraft," Dec. 20, 2016, 1, https://www.pewtrusts.org/en/research-and-analysis/reports/2016/12/how-a-set-of-small-banks-compares-on-overdraft.

Figure 4: 20% of Large Banks Prohibit ATM and Debit Point-of-Sale Overdrafts



Note: Banks that do not charge a fee for an overdraft, significantly lessening the harm to consumers of overdrawing at an ATM or point of sale, automatically get credit for these best practices.

Source: The Pew Charitable Trusts, "Consumers Need Protection from Excessive Overdraft Costs," (2016)

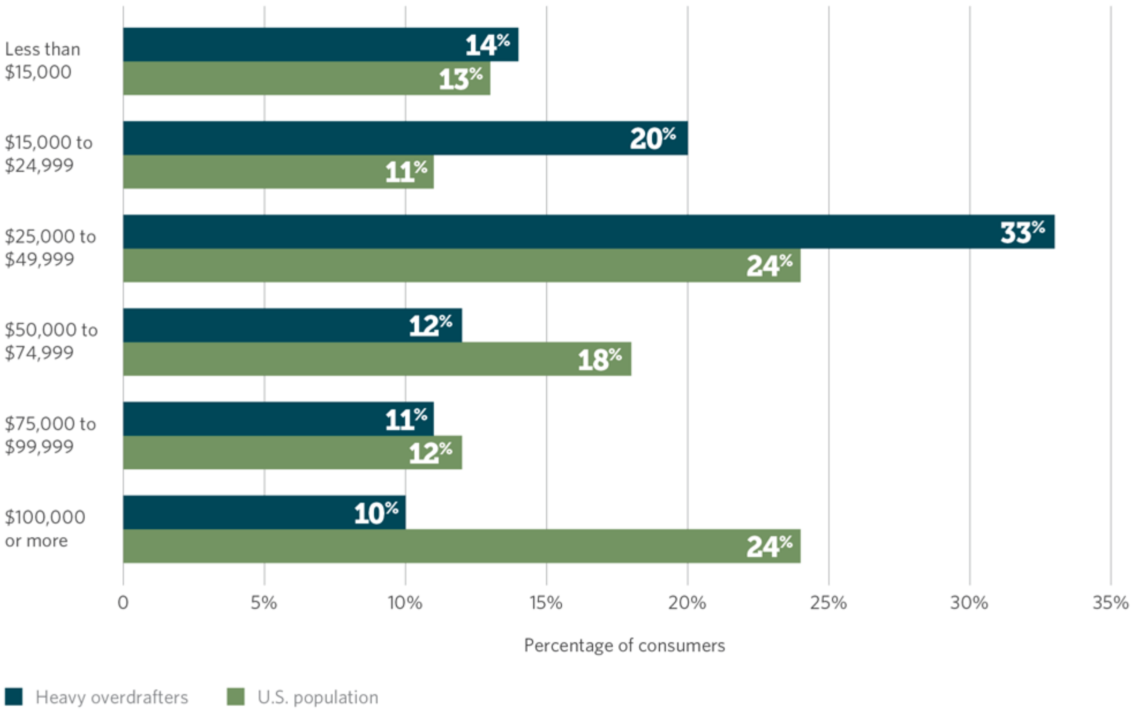
Overdraft causes financially vulnerable consumers to leave the banking system

Pew's research shows that consumers who overdraft frequently tend to be financially vulnerable, low and moderate income, and struggle to cover expenses. Pew studied consumers who overdrafted their accounts at least three times a year and found these consumers typically make less than $50,000 annually and 1 in 4 pays at least a week of wages in overdraft fees in a year.[17] (See Figure 5 and Figure 6.) Eighty-two percent of all overdrafters struggle to meet their financial obligations.[18]

[17] The Pew Charitable Trusts, "Heavy Overdrafters," Apr. 20, 2016, https://www.pewtrusts.org/en/research-and-analysis/fact-sheets/2016/04/heavy-overdrafters.

[18] The Pew Charitable Trusts, "Overdraft Does Not Meet the Needs of Most Consumers," Dec. 20, 2017, https://www.pewtrusts.org/-/media/assets/2017/12/cb_overdraft_does_not_meet_the_needs_of_most_consumers.pdf

Figure 5: 2 in 3 Heavy Overdrafters Make Less Than $50,000 a Year

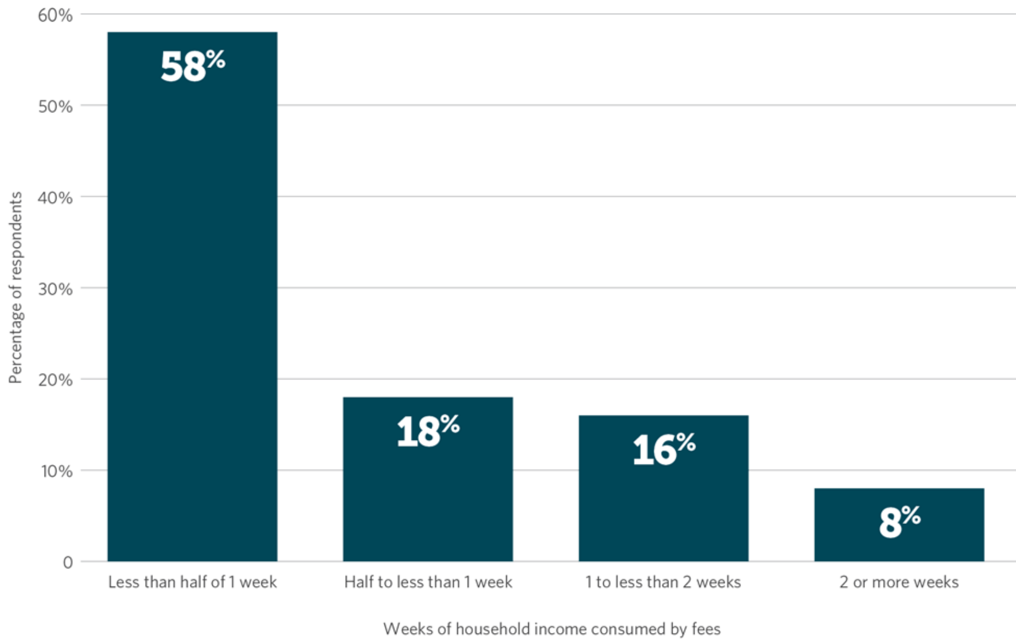


Note: Results are based on 304 survey participants who reported paying more than $100 in overdraft fees in the past year. Respondents were asked, "Is your total annual household income from all sources, and before taxes …?" Differences between heavy overdrafters and the U.S. population were significant at the 99 percent confidence level.

Source: U.S. population data from 2014 American Community Survey one-year estimates

Source: The Pew Charitable Trusts, "Heavy Overdrafters," (2016)

Figure 6: 1 in 4 Heavy Overdrafters Pay the Equivalent of 1 or More Weeks of Wages in Overdraft Fees



Note: Results are based on 304 survey participants who reported paying more than $100 in overdraft fees in the past year. Respondents were asked, "Is your total household income from all sources, and before taxes ...?" and "Taking your best guess, how much have you paid in these types of [overdraft] fees during the past year, in total?" Weekly income is calculated by dividing yearly income by 52 workweeks a year. Weeks of work to pay overdrafts are calculated by dividing the amount of overdraft fees paid during the past year by weekly income.

Source: The Pew Charitable Trusts, "Heavy Overdrafters," (2016)

A small number of consumers pay the majority of overdraft fees, suggesting that bank overdraft revenue comes primarily at the expense of financially vulnerable consumers. The CFPB found in 2014 that 8.3 percent of account holders were responsible for 73.7 percent of overdraft fees.[19] Overdraft penalty fees have pushed many consumers out of the regulated banking system. The Federal Deposit Insurance Corporation's National Survey of Unbanked and Underbanked Households shows that 30 percent of households that previously had a bank account no longer do because of high fees, though fees other than overdraft could be part of this issue.[20] Similarly, Pew research reveals that 28 percent of overdrafters have closed their checking account in the past because of overdraft.[21] The growth of the prepaid card market also highlights the negative impact of penalty overdraft on the banking system: Nearly three-quarters of unbanked prepaid card customers report that a reason for using the cards is to avoid overdraft fees.[22]

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[19] Consumer Financial Protection Bureau, "Data Point: Checking Account Overdraft," (July 2014), 11, http://files.consumerfinance.gov/f/201407_cfpb_report_data-point_overdrafts.pdf.

[20] Federal Deposit Insurance Corp., "FDIC National Survey of Unbanked and Underbanked Households," (October 2018), 4, https://www.fdic.gov/householdsurvey/2017/2017report.pdf.

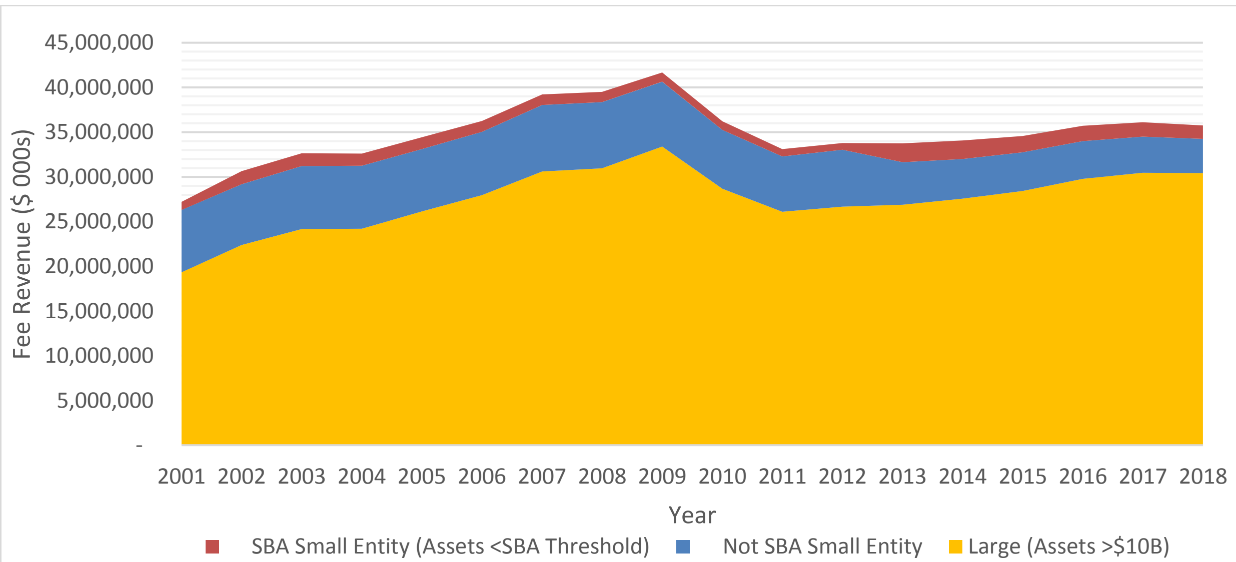
[21] The Pew Charitable Trusts, "Overdrawn: Consumer Experiences with Overdraft," Jun. 26, 2014, 1, https://www.pewtrusts.org/-/media/assets/2014/06/26/safe_checking_overdraft_survey_report.pdf.

[22] The Pew Charitable Trusts, "Banking on Prepaid: Survey of motivations and views of prepaid card users," Jun. 30, 2015, 6, https://www.pewtrusts.org/-/media/assets/2015/06/bankingonprepaidreport.pdf.

Bank revenue from fees and overdraft programs is stable, and the overdraft rule has not led to an increase in prices

When it issued the overdraft rule, the Board provided mechanisms to help financial institutions comply with it, including a standardized form and a safe harbor for institutions that rely on merchant coding for different transaction types. These measures helped minimize the impact of the rule on banks, including small entities. Available evidence suggests that small entities have recovered from any short-term impact the rule may have had on them. The implementation of the overdraft rule coincides with the peak in bank service fee revenue. (See Figure 7.) In the years after the rule was implemented, fee revenue fell initially,[23] and stabilized quickly around $34 billion. While consumers certainly benefited by paying fewer fees in the aftermath of the crisis, banks' revenue from overdraft fees remains stable today.

Figure 7: Fee revenue peaked in 2009 and stabilized shortly after the Great Recession



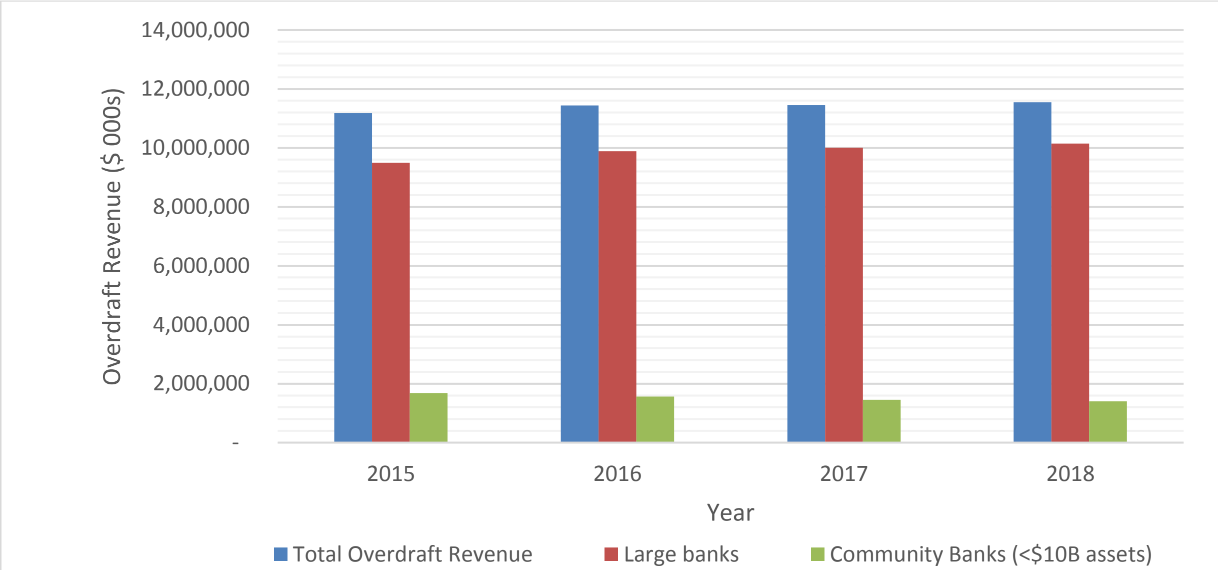
Source: Pew calculations from Call Report Bulk Data

In 2015, when banks started reporting a breakout of their fees, overdraft revenue totaled roughly $11.2 billion, comprising about a third of fee revenue. Today, that number is largely the same, with banks bringing in $11.5 billion of overdraft revenue in 2018, or 32 percent of all fee revenue.[24] (See Figure 8.)

[23] Call Report data show that the banking system consolidated significantly after the Great Recession; From 2009 to 2018, the number of financial institutions fell from more than 7,300 to fewer than 5,500.

[24] It is noteworthy that many smaller banks were not obligated to report these data, and so this value underestimates the total overdraft market. For information on the reporting standards, see: Consumer Financial Protection Bureau, "Variation in Bank Overdraft Revenues and Contribution," Feb. 22, 2016, https://files.consumerfinance.gov/f/201602_cfpb_variation-in-bank-overdraft-revenues-and-contribution.pdf.

Figure 8: Overdraft Revenue is Stable



Source: Pew calculations from Call Report Bulk Data

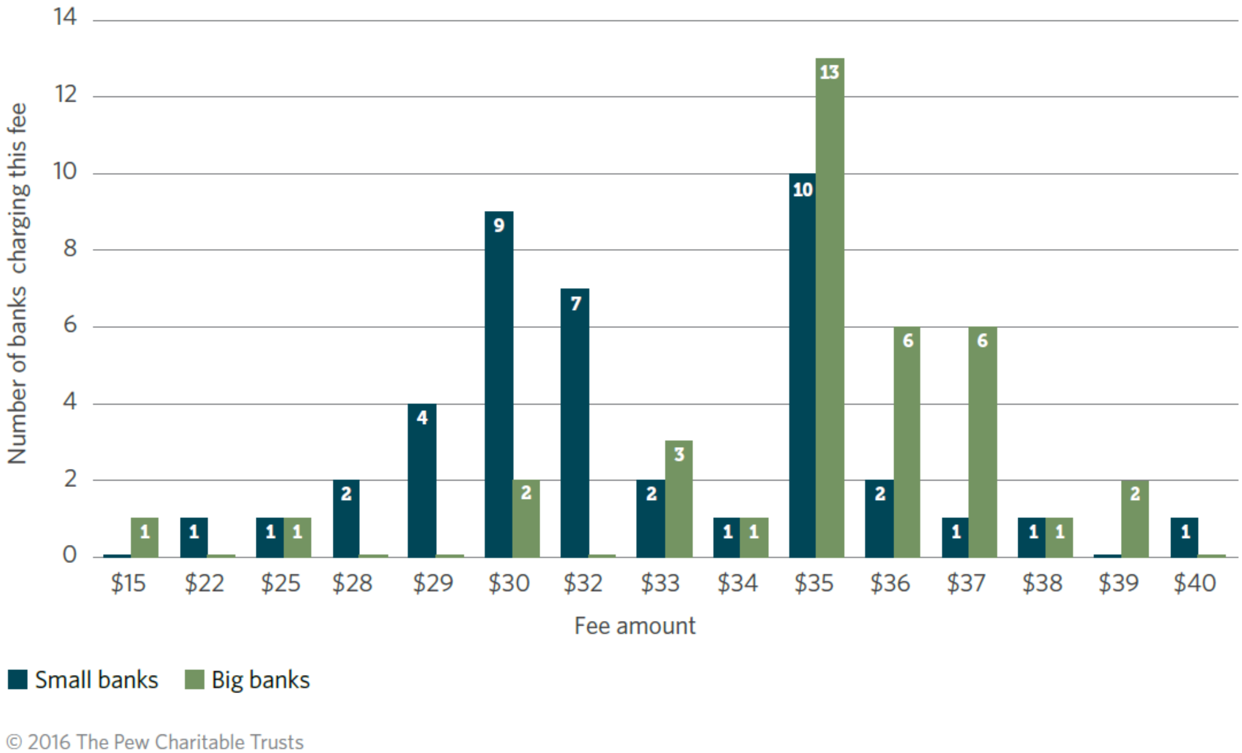
One concern posited by financial institutions was that the Board's original overdraft rule would lead to increased prices, but this did not occur. A report in 2008 by the FDIC showed the median overdraft fee at smaller institutions (assets between $250 million and $1 billion) was $28 and that 89 percent of these institutions charged fees from $25-$35.[25] Similarly, Pew released research in 2016 on 45 small institutions with deposits between $360 million and $1 billion and found that the median overdraft fee at these institutions was $32, with 88 percent of those banks charging fees between $28-$36.[26] These studies were conducted nearly 10 years apart, and the differences in pricing are in line with inflation. ($28 at the end of 2008 is worth $32 at the end of 2016.[27]) This lack of real price change suggests that concerns that the overdraft rule would cause price changes did not materialize. Figure 9 shows the distribution of overdraft fees among the small and large banks that Pew studied in 2016.

[25] Federal Deposit Insurance Corp., "Overdraft Survey—Complete Aggregated Results," (Nov. 2008), 16-17, https://www.fdic.gov/bank/analytical/overdraft/FDIC138_OverdraftSurvey_v508.pdf;

[26] The Pew Charitable Trusts, "How a Set of Small Banks Compares on Overdraft," Dec. 20, 2016, 4, https://www.pewtrusts.org/-/media/assets/2016/12/sm_overdraft_report_f.pdf.

[27] Using the Bureau of Labor Statistics' inflation calculator, the inflation-adjusted value of $28 in December 2008 is equal to $32.16 in December 2016. The calculator can be found at: http://data.bls.gov/cgi-bin/cpicalc.pl

Figure 9: Most Small Banks Studied Charge $28-36 per Overdraft



Source: The Pew Charitable Trusts, "How a Set of Small Banks Compares on Overdraft," (2016)

2. The Bureau should improve the overdraft rule by promoting clearer and more comprehensive disclosures to consumers

If the Bureau makes any changes to the overdraft rule, it should be to strengthen its consumer protections, both to help consumers compare and understand the terms and price differences among financial services providers, and to make overdraft programs safer.

Better communication from banks and credit unions would help customers understand their options, especially the right to have debit and ATM transactions declined without a fee. In transparent and competitive markets, customers who shop around can benefit from well-structured standardized disclosures. In its opt-in rule, The Board notes that, "adopting a model form that can be used to ease compliance with the final rule" can "minimize the significant economic impact on small entities while still meeting the stated objectives of Regulation E."[28] But as Pew has noted previously, the current model form is confusing, makes comparing options difficult, and does not note that customers can avoid a fee by choosing to opt out (or not opt in)—which most consumers do not know.[29] Indeed, in 2017, the

[28] 74 FR 59051.

[29] The Pew Charitable Trusts, "Customers Can Avoid Overdraft Fees, but Most Don't Know How," Mar. 21, 2018, https://www.pewtrusts.org/en/research-and-analysis/articles/2018/03/21/customers-can-avoid-overdraft-fees-but-most-dont-know-how

Bureau identified areas to improve[30] the effectiveness of the Board's model form and proposed updates to the standard disclosure forms which would have laid out information in a side-by-side format allowing for easy comparison of options.[31] But the Bureau has not yet adopted these proposed updates.

Pew designed a model disclosure box for checking accounts that more than 30 banks adopted, including 12 of the largest. This form emphasizes the most important checking account fees and makes clear that the default overdraft option is to have debit card transactions declined at no cost. (See excerpt, Figure 10.) A spokesperson from BB&T praised the form as a "clear, concise resource designed to help consumers thoroughly understand and compare the deposit products we offer, avoid fees and compare BB&T's products to others in the market."[32]

Figure 10: Disclosures Should Clearly and Completely Describe Overdraft Programs, Policies, Fees

Overdraft Options for Consumers with Debit Cards				
	Option A: (Default)	No Overdraft Service		If you choose not to opt in to any kind of overdraft service, transactions that would cause an overdraft will be declined at no cost to you.
	Option B: Overdraft Transfer Plan	Overdraft Transfer Fee	$	per overdraft covered by a transfer from a linked savings account, line of credit, or credit card
	Option C: Overdraft Penalty Plan	Overdraft Penalty Fee	$	per overdraft covered by an advance from your financial institution
		Maximum Number of Overdraft Penalty Fees per Day		You will only be charged this number of overdraft penalty fees per day, even if we elect to cover additional overdrafts.
		Minimum Amount Required to Trigger an Overdraft Penalty Fee	$	If you are overdrawn by this amount or less, you will not incur an overdraft penalty fee.
		Extended Overdraft Penalty Fee	$	charged every X day the account is overdrawn, starting Y days after the account is first overdrawn

Source: The Pew Charitable Trusts, "How a Set of Small Banks Compares on Overdraft," (2016)

Though many consumers have not understood they have the right to avoid overdraft penalty fees, it is extremely important that they retain the ability to do so. Avoiding these fees can help keep consumers in the mainstream banking system, reducing the incentive for customers to give up their checking accounts and switch to prepaid cards. Among the unbanked, the Federal Deposit Insurance Corporation found 27 percent are using a prepaid account or an expensive non-bank option like check cashing.[33] Pew's research revealed that nearly three-quarters of unbanked prepaid customers are doing so to

[30] Consumer Financial Protection Bureau, "Know Before You Owe: We are designing new overdraft disclosure forms," Aug. 04, 2017, https://www.consumerfinance.gov/about-us/blog/know-you-owe-we-are-designing-new-overdraft-disclosure-forms.

[31] Consumer Financial Protection Bureau, "What You Need to Know about Overdrafts and Overdraft Fees," (Aug. 2017), https://files.consumerfinance.gov/f/documents/201708_cfpb_A-9-form-ficus_overdraft-model-forms-prototypes.pdf

[32] The Pew Charitable Trusts, "Eight of Top 12 U.S. Banks Adopt Pew's Model Checking Account Disclosure Box" Jun. 6, 2013, https://www.pewtrusts.org/en/about/news-room/press-releases-and-statements/2013/06/06/eight-of-top-12-us-banks-adopt-pews-model-checking-account-disclosure-box

[33] Federal Deposit Insurance Corp., "2017 FDIC National Survey of Unbanked and Underbanked Households," (Oct. 2018), 7, https://www.fdic.gov/householdsurvey/2017/2017report.pdf

avoid overdraft fees.[34] But avoiding overdraft fees should be as easy as telling a bank to rescind opt-in on an account, or not opting in to paying penalty fees initially. Retaining the current opt-in requirements and improving the standard opt-in form would be a step in the right direction. Any of the three options for altering the standard opt-in form already proposed by the CFPB in 2017 would increase transparency over the current form about overdraft options and would provide customers with much-needed information.[35] Bankers can use these forms to explain programs to their clients easily and avoid back-end regulatory penalties for misleading consumers.[36] The forms would also allow customers to compare programs and adjust their choices as their borrowing needs change.

Research indicates that when consumers become more aware of overdraft costs, a small reduction in usage follows.[37] This suggests that improved disclosures are a small piece of helping consumers better protect themselves from unwanted overdraft charges. But disclosures alone are not nearly sufficient to resolve the problems associated with overdraft penalty fees. Research strongly suggests that overdraft costs are not salient to consumers.[38] Economic research has documented that consumers react when costs are salient, for example, buying less of a good when sales tax is included in its purchase price than when sales tax is applied at the cash register.[39] But clear information is imperative. Evidence from the mortgage market indicates consumers struggle to comparison shop when prices are not displayed in a uniform manner.[40] The combination of shrouded costs, low salience, and lack of uniform disclosures explains why the overdraft market is not price competitive and why consumers have struggled to navigate it and experienced harm as a result.

As we have noted in the market for small-dollar loans, price sensitivity is a prerequisite for price competition. If consumers are not price sensitive, either because they are in financial distress (payday loans), or if they do not expect to pay penalty fees, do not know what those fees are, or do not know how to avoid them (overdraft), firms do not have a motivation to compete on price.

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[34] The Pew Charitable Trusts, "Banking on Prepaid: Survey of motivations and views of prepaid card users," Jun. 30, 2015, 6, https://www.pewtrusts.org/-/media/assets/2015/06/bankingonprepaidreport.pdf.

[35] Consumer Financial Protection Bureau, "CFPB Unveils Prototypes of 'Know Before You Owe' Overdraft Disclosure Designed to Make Costs and Risks Easier to Understand: New CFPB Study Shows Opted-In Frequent Overdrafters Typically Pay Almost $450 More in Fees, (Aug. 2017), https://www.consumerfinance.gov/about-us/newsroom/cfpb-unveils-prototypes-know-you-owe-overdraft-disclosure-designed-make-costs-and-risks-easier-understand/.

[36] Bureau of Consumer Financial Protection Settles with TCF National Bank, July 20, 2018, https://www.consumerfinance.gov/about-us/newsroom/bureau-consumer-financial-protection-settles-tcf-national-bank/.

[37] Sule Alan, Mehmet Cemalcilar, Dean Karlan, and Jonathan Zinman, "Unshrouding: Evidence from Bank Overdrafts in Turkey," 2017, https://onlinelibrary.wiley.com/doi/abs/10.1111/jofi.12593. This study found that when a bank advertised a 50 percent discount on overdrafts to consumers, usage dropped. The most likely explanation for the decrease in usage is that the advertising reminded consumers of the high cost of overdraft, leading them to reduce their overdraft activity. The authors also noted that "banks lack incentives to unshroud or compete on overdraft prices because doing so backfires." The authors discussed their findings, explaining: "Altogether our results are consistent with models where consumers have limited and reactive attention to add-ons like overdrafts, and suppliers respond by shrouding add-on costs. Specifically, it seems that overdraft costs and availability are not at the top of mind for consumers, and even when brought closer to top of mind they do not stay there for long. As such recent behavioral models of add-on pricing, marketing, and usage do capture key aspects of reality with consumers that tend to underestimate add-on costs and react strongly but temporarily when their attention is drawn to add-on, and with firms that lack incentives to unshroud or compete on add-on costs." Therefore, the authors believe, "competing on overdraft prices will *not* capture market share or increase usage, and thus will lower revenue."

[38] See, e.g., Victor Stango and Jonathan Zinman, "Limited and Varying Consumer Attention: Evidence from Shocks to the Salience of Bank Overdraft Fees," 2014, https://academic.oup.com/rfs/article-abstract/27/4/990/1603971. See also footnote 37, above.

[39] Raj Chetty, Adam Looney, and Kory Kroft, "Salience and Taxation: Theory and Evidence," 2009, https://www.aeaweb.org/articles?id=10.1257/aer.99.4.1145.

[40] Susan E. Woodward, "Consumer Confusion in the Mortgage Market," 2003, https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2049629.

3. Overdraft programs have changed, and regulators should do more to help consumers meet their financial needs

Policymakers can and should do more to help consumers manage their finances successfully. In addition to maintaining the overdraft rule and improving overdraft disclosures, this should include modernizing regulations to treat frequent overdraft as credit and establishing guidelines for offering safe small installment loan alternatives.

The overdraft rule appropriately addressed payments innovation by establishing clear opt-in rules for debit card transactions

Overdrafts were originally applied to checks. The practice was occasional, and it was often considered a courtesy service. The innovation of the debit card created a very different landscape in payments. Today, the majority of payments from a checking account are completed using a debit card (See Figure 11), but these tend to be relatively small and numerous compared with the way checks were used in the past. The CFPB found that debit card overdrafts occurred on a median transaction value of just $24 compared with $100 for checks.[41] The typical fee was $34, larger than the debit transaction value.[42]

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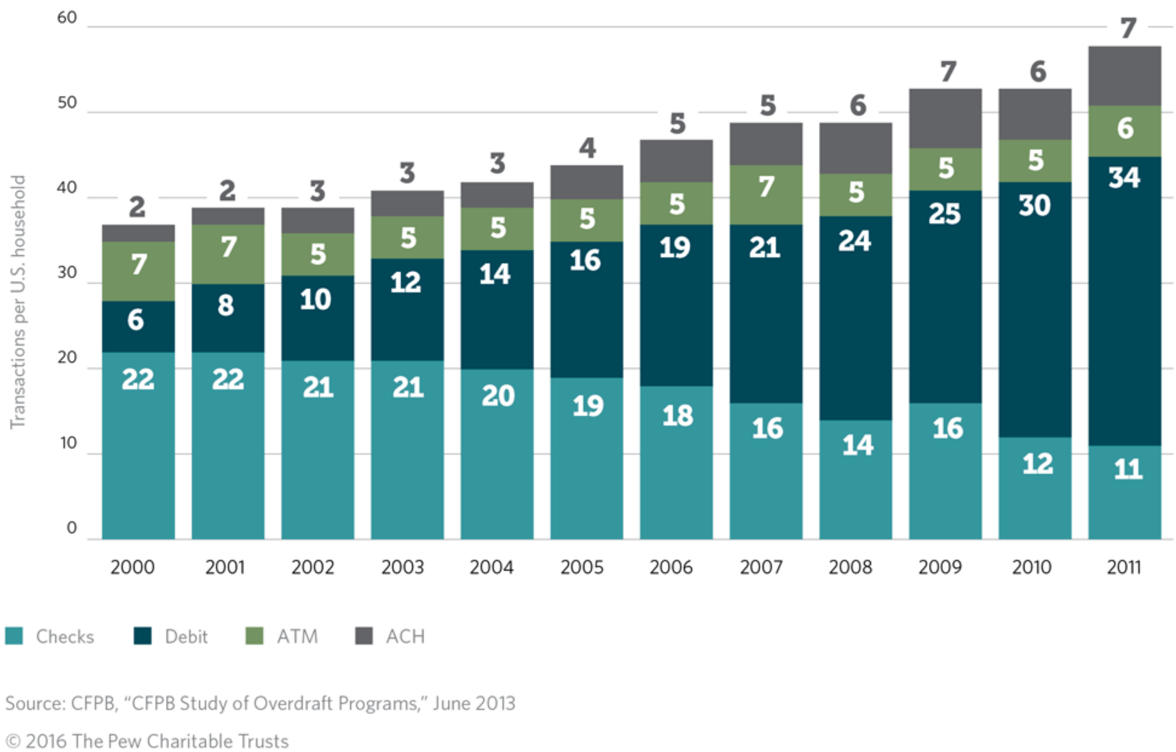
[41] Consumer Financial Protection Bureau., "Data Point: Checking account overdraft," (Jul. 2014), 18, https://files.consumerfinance.gov/f/201407_cfpb_report_data-point_overdrafts.pdf;

[42] Consumer Financial Protection Bureau., "CFPB Unveils Prototypes of "Know Before You Owe" Overdraft Disclosure Designed to Make Costs and Risks Easier to Understand: New CFPB Study Shows Opted-In Frequent Overdrafters Typically Pay Almost $450 More in Fees," (Aug. 4, 2017), https://www.consumerfinance.gov/about-us/newsroom/cfpb-unveils-prototypes-know-you-owe-overdraft-disclosure-designed-make-costs-and-risks-easier-understand/

Figure 11: Debit Cards are the Most Commonly Used Method of Checking Account Payments



Source: The Pew Charitable Trusts, "Consumers Need Protection from Excessive Overdraft Costs," (2016)

The overdraft rule provided a much-needed, if modest, update to regulation—establishing that bank customers should not be auto-enrolled in costly penalty fee programs with respect to electronic transactions. This was an important step toward helping customers translate their preferences into outcomes.

Regulations have not kept pace as "courtesy" overdraft has largely become high-cost, short-term credit for constrained low and moderate-income borrowers

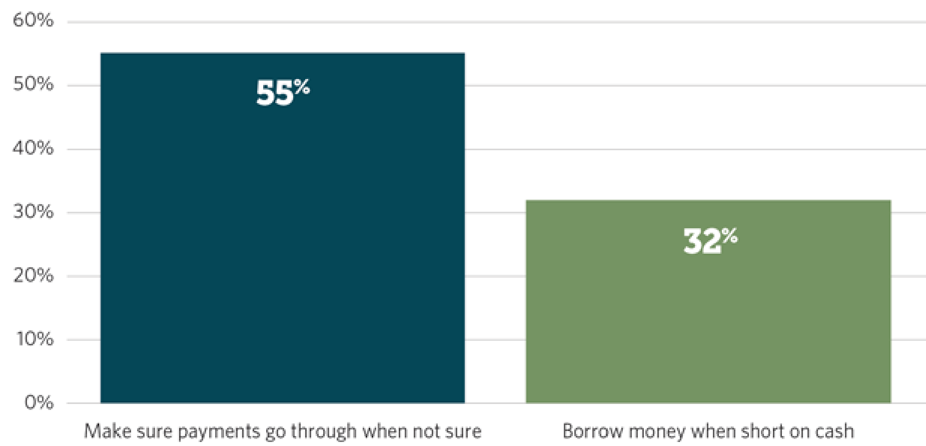
Many experts now talk about overdraft as a credit device. For example, the American Bankers Association recently wrote a comment letter in response to the FDIC's request for information on small-dollar lending, stating that, "[b]ecause borrowers' needs are diverse, there should be a vibrant credit market with many small dollar credit options, including credit cards, installment loans, single payment loans, and overdraft protection services, among others."[43]

More than 39 million American adults incurred at least one fee for overdrawing their bank account or having insufficient funds in the past 12 months. Most view overdraft as a way to ensure that payments

[43] American Bankers Association, "Request for Information on Small-Dollar Lending, 83 Fed. Reg. 58,566 (Nov. 20, 2018) [RIN 3064-ZA04]," Jan. 22, 2019, https://www.aba.com/Advocacy/commentletters/Documents/fdic-small-dollar-lending-012219.pdf.

will go through if checking account balances are low; but a large portion view it as credit: one third said they view overdraft as a way to borrow when short on cash.[44] (See Figure 12.) Given that a small number of high-frequency overdrafters accounts for the vast majority of overdraft revenue, it is likely that those seeking credit account for a disproportionate share of overdraft revenue at banks.[45]

Figure 12: 1 in 3 Overdrafters View Overdraft as a Way to Borrow



Note: Results are based on 1,008 survey participants. Respondents were asked, "In general, do you see overdraft as more of a way to make sure payments go through when you're not sure how much money is in your account or more of a way to borrow when you're short on cash?" Data do not add to 100 percent because "don't know" and "refused" responses were omitted.

Source: The Pew Charitable Trusts, "Overdraft Does Not Meet the Needs of Most Consumers," (2017)

Overdraft is expensive, and when used as credit, is often poorly suited to consumers' needs. Many overdraw using debit cards for small purchases[46] and then face flat fees of around $35 for each transaction,[47] an extremely high cost to borrow a very small amount for a very short period of time. Though regulators may never have intended for overdrafts to become a form of credit, survey data[48] and comments from bank representatives indicate that millions of adults use it for just that purpose. Repeated overdrafts can lead to punitive fees, customer dissatisfaction, and account closures.[49] Research by Pew in 2014, for example, found that more than a quarter of overdrafters had closed a bank account because of these fees. Further, the desire to avoid overdraft fees also can push some banked

[44] The Pew Charitable Trusts, "Overdraft Does Not Meet the Needs of Most Consumers: Bank programs often function as costly, inefficient credit," (Dec. 2017), 8, https://www.pewtrusts.org/-/media/assets/2017/12/cb_overdraft_does_not_meet_the_needs_of_most_consumers.pdf

[45] The Bureau found in 2014 that 8.3 percent of account holders were responsible for 73.7 percent of overdraft fees. Consumer Financial Protection Bureau, "Data Point: Checking Account Overdraft" (July 2014), 11, http://files.consumerfinance.gov/f/201407_cfpb_report_data-point_overdrafts.pdf.

[46] Consumer Financial Protection Bureau, "Data Point: Checking Account Overdraft," (Jul. 2014), 18, https://files.consumerfinance.gov/f/201407_cfpb_report_data-point_overdrafts.pdf.

[47] The Pew Charitable Trusts, "Consumers Need Protection from Excessive Overdraft Costs," Dec. 20, 2016, 6, https://www.pewtrusts.org/-/media/assets/2016/12/consumers_need_protection_from_excessive_overdraft_costs.pdf.

[48] The Pew Charitable Trusts, "Overdraft Does Not Meet the Needs of Most Consumers," Dec. 20, 2017, 8, https://www.pewtrusts.org/-/media/assets/2017/12/cb_overdraft_does_not_meet_the_needs_of_most_consumers.pdf.

[49] The Pew Charitable Trusts, "Overdrawn," Jun. 26, 2014, 10, https://www.pewtrusts.org/~/media/assets/2014/06/26/safe_checking_overdraft_survey_report.pdf.

customers to borrow using costly nonbank services, such as payday loans. A Pew study has found that most payday loan borrowers also overdraw.[50]

Major regulators are starting to modernize policies to treat overdraft as credit

Regulations in the United States have not kept up with overdraft's evolution to a form of credit. The Bureau has tended to continue policies set in place many years ago by other agencies, which exempted fee-based overdraft from compliance with the laws of credit (the Truth in Lending Act and Regulation Z) based on theories formed at a time when paper checks were a dominant means of conducting transactions with a checking account.[51] Under these theories, overdraft is generally assumed to be an occasional courtesy and its associated fees are presumed to be reasonable alternatives to non-sufficient funds fees of the sort commonly charged on bounced checks. With the minor exceptions of the disclosure and opt-in provisions of the overdraft rule (the subject of this RFI) and the Bureau's prepaid card rule, regulators in the United States have not modernized these theories to account for a market that is now dominated by electronic debit card transactions (to which nonsufficient funds fees do not apply) and in which one-third of overdrafters mostly use it intentionally as a form of credit.[52]

But other major financial regulators have begun to modernize their approach to checking account overdraft. For example, the U.K.'s Financial Conduct Authority (FCA) introduced a new set of policies that will regulate overdraft programs as credit.[53] The FCA is requiring financial institutions to price overdraft using a simple annual interest rate and to advertise prices with an annual percentage rate to help customers compare them with other products. The FCA expects the cost of borrowing £100 through an overdraft to drop by more than 90 percent, from £5 a day to less than 20 pence a day. The new rules will be in force by April 6, 2020.

Small installment loans can better meet consumers' credit needs

Treating overdraft as credit does not mean that consumers will be unable to access it when they need it, but some reforms would have to be made to ensure both safe lending and regulatory acceptance of efficient lending practices that make it economically viable for banks to make small-dollar installment loans and lines of credit available.

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[50] The Pew Charitable Trusts, "Overdraft Frequency and Payday Borrowing," (Feb. 2015), https://www.pewtrusts.org/-/media/assets/2015/02/consumerbanking_overdraftsupplementbrief_v9.pdf.

[51] See, e.g., Department of the Treasury, Federal Reserve System, Federal Deposit Insurance Corp., National Credit Union Administration, "Joint Guidance on Overdraft Protection Programs" (2005), 5–6, 10, https://www.federalreserve.gov/boarddocs/press/bcreg/2005/20050218/attachment.pdf.

[52] The Bureau's final prepaid rule codified consumer protections for prepaid accounts that are similar to those for checking accounts, except that the rule requires any overdraft program offered via a prepaid account to comply with regulations governing credit. This means, for example, that payments would be made over time and not in one lump sum, and lenders would be required to set underwriting standards and disclose the annual percentage rate. The prepaid card rule could serve as a template for modernizing overdraft regulations more generally. See: Consumer Financial Protection Bureau, "CFPB Finalizes Strong Federal Protections for Prepaid Account Consumers: New Rule Includes 'Know Before You Owe' Prepaid Disclosures", (Oct. 2016), https://www.consumerfinance.gov/about-us/newsroom/cfpb-finalizes-strong-federal-protections-prepaid-account-consumers/

[53] Financial Conduct Authority, "FCA confirms biggest shake-up to the overdraft market for a generation," Jun. 7, 2019, https://www.fca.org.uk/news/press-releases/fca-confirms-biggest-shake-up-overdraft-market.

Today, those who overdraw and want credit are often unable to access it through more conventional loans. For example, more than half said they do not have enough available on a credit card to cover a $400 emergency expense.[54] Four in 10 said they had applied for credit in the past year; of those, 30 percent were declined for the entire amount, and 10 percent were approved for only a fraction of the amount requested.[55] These numbers do not include those who did not apply for credit because they believed they would not have been approved, an indication that the gap between demand and access may be even higher. The CFPB's findings that among customers who overdraw 20 or more times a year, the average credit score is a deep subprime 563 and the average amount of credit card liquidity is $225 are strong corroborating evidence that very heavy overdrafters are credit constrained.[56]

Policies that give financial institutions simple guidelines to offer affordable small installment loans represent a sensible approach to meeting consumer needs. In 2017, the Consumer Financial Protection Bureau finalized a rule to limit the harms caused by short-term payday and auto title loans. By leaving the market for small installment loans lasting longer than 45 days essentially unregulated, the rule opens the door to banks and credit unions providing lower-cost small installment loans; but federal and state bank regulators will need to concur with the CFPB that this type of lending is acceptable, and provide guidelines establishing acceptable safe lending practices in order for it to become widespread.[57]

If regulators allowed banks to offer new small installment loans under strong but reasonable consumer protection guidelines, consumers would have access to safe and affordable credit (Pew has published standards and recommendations for this purpose).[58] This would help checking account holders obtain affordable installment loans rather than payday loans or overdraft products—two very expensive forms of credit that have very short terms and tend to lead to repeat usage. Safer, affordable small installment loans would also help keep more consumers in the banking system.

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[54] The Pew Charitable Trusts, "Overdraft Does Not Meet the Needs of Most Consumers: Bank programs often function as costly, inefficient credit," (Dec. 2017), 9, https://www.pewtrusts.org/-/media/assets/2017/12/cb_overdraft_does_not_meet_the_needs_of_most_consumers.pdf.

[55] Ibid., 10

[56] Consumer Financial Protection Bureau, "Data Point: Frequent Overdrafters," Aug. 4, 2017, 16, http://files.consumerfinance.gov/f/documents/201708_cfpb_data-point_frequent-overdrafters.pdf.

[57] Pew discussed this topic extensively in prior comments to the Bureau. See: Comment letter from The Pew Charitable Trusts re: payday, vehicle title, and certain high-cost installment loans; docket no. CFPB-2019-0006 (RIN 3170-AA80; May 15, 2019), 28 et. seq., https://www.regulations.gov/document?D=CFPB-2019-0006-27848.

[58] Pew has laid out detailed evidence in other publications, and provided research-based standards for safe small installment loans from banks and credit unions. See: The Pew Charitable Trusts, "Standards Needed for Safe Small Installment Loans From Banks, Credit Unions," Feb. 15, 2018, https://www.pewtrusts.org/-/media/assets/2018/02/standards_needed_final.pdf.

Appendix A: Scope of Section 610 review

Section 610 of the Regulatory Flexibility Act (RFA) requires agencies to review rules that have had or will have a significant economic impact on a substantial number of small entities within ten years of publication of the final rule. The Bureau states in its 2019 *Notice of section 610 review and request for comments* that it wishes to conduct an RFA Section 610 review of the overdraft rule, implemented in November 2009 by the Federal Reserve Board of Governors.

This review is limited in scope to "small entities." Three types of small entities are defined in the RFA: small business, small organization, and small government jurisdiction.[59] Among these, the Bureau's review of small depository financial institutions pertains to "small business," defined in Section 601(3) of the RFA as "having the same meaning as 'small business concern' under section 3 of the Small Business Act."[60] Section 3 of the Small Business Act gives the Small Business Administration (SBA) the power to define "small business," and it does so by establishing size standards that vary by industry. The SBA decides how a small business in each industry is identified (e.g., by assets, workforce, or income) and occasionally updates these standards for inflation or other reasons.[61] These standards are published on the Administration's website.

The threshold for a small business in the commercial banking and credit union industry is limited to financial institutions with assets less than $550,000,000. As of May 23, 2019, just over 4,000 banking institutions met this threshold, comprising roughly 5 percent of domestic deposits in the U.S. banking system.[62] Accordingly, any actions the Bureau takes resulting from this review would presumably pertain only to these institutions. Pew's research identifying harmful overdraft practices at banks of all sizes, including very small banks, demonstrates the likely harm of modifying the overdraft rule to weaken its protections for consumers who bank at small institutions.

[59] In the second footnote of its notice, the Bureau refers to a small entity as "defined in the RFA. *See* 5 U.S.C.(6)."

[60] 5 U.S.C.(6). See also: U.S. Small Business Administration, "How to Comply with the Regulatory Flexibility Act," Aug. 2017, 14. https://www.sba.gov/sites/default/files/advocacy/How-to-Comply-with-the-RFA-WEB.pdf.

[61] The SBA has updated the threshold for commercial banks and credit unions several times in the past 20 years: A final rule in 1994 established the standard at $100 million (59 FR Doc No: 94-8274). In 2002 an interim final rule revised the level to $150 million (67 FR 3050). In 2005, an interim final rule brought the level to $165 million (70 FR 72588), and a final rule in 2008 raised it again to $175 million (73 FR 41247). In 2013, a final rule raised the level to $500 million (78 FR 37411), and the most recent standard was established with an interim final rule in 2014 (FR 79 33661).

[62] Call Report data from year-end 2018 suggest that 4,143 banking institutions met the threshold. These institutions held $657 billion in domestic deposits, or 5.21 percent of the total domestic deposit base. By May 23, 2019, consolidations through mergers and other means resulted in 4,043 institutions classified as "small businesses." Pew's analysis of the most current available credit union data from year-end 2018 Call Reports shows 4,861 credit unions meet the small business threshold; these institutions totaled $299 billion in shares and deposits, or 24.52 percent of the credit union total.