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New CFPB Overdraft Study Confirms that Much-Needed Reforms are Overdue

Study Shows that Big Bank Profits Depend on Excessive Fees
Charged to the Most Vulnerable Consumers

(BOSTON) A study on bank overdraft fees released today by the Consumer Financial Protection Bureau (CFPB) confirmed what advocates have long argued: the bulk of bank profits on checking accounts come from costly overdraft fees, much of which are paid by a small percentage of consumers who are frequently walloped by these fees. The study also found that banks differ widely in what practices they use regarding overdrafts, and these practices can greatly increase the number of overdrafts and the fees charged to consumers.

The CFPB study found that 61% of bank profits from consumer checking accounts come from overdraft and non-sufficient funds (NSF) fees. A substantial portion of these fees are paid by consumers who are charged 10 or more overdraft or NSF fees per year – less than 8% of consumers. Earlier studies by the FDIC and the Center for Responsible Lending indicate frequent overdrafters were more likely to be lower-income and minority consumers. "The consumers who pay the most overdraft fees are also the most economically vulnerable," said National Consumer Law Center staff attorney Chi Chi Wu, "So the fattest profits of some of the biggest banks are being made off the backs of those least able to afford it."

The CFPB study indicates that overdraft fees are enormously profitable for banks. Currently, the median overdraft fee is about $35. The CFPB study indicated that only 14.4% of net overdraft revenue goes toward the cost of covering unpaid overdrafts. While the CFPB report does not include information about processing and administrative costs, NCLC recently issued a report "Common Sense from the Common Law" estimating that such costs range from 54 cents to $3.50. "Fourteen percent of $35 is only about $5," calculated report author Wu, "Even assuming the higher estimate for processing, it means the average big bank makes over $25 in pure profit from each overdraft fee."

Indeed, the NCLC report argued that these outsized profits are the driving force behind other abusive overdraft practices that maximize overdrafts, such as:

- re-ordering checks and other debits from high-to-low amount in order to maximize the number of overdraft fees that are charged;
- extending overdrafts to debit and ATM card transactions, where previously transactions had been declined without a fee;
- pressuring, badgering, and using deceptive statements to persuade consumers to opt in to debit and ATM card overdrafts;
- charging "sustained" overdraft fees in addition to the initial overdraft fee if an account remains overdrawn for a certain number of days; and
- promoting overdrafts to consumers, and encouraging them to use overdrafts as a source of credit.

The CFPB study noted that banks differ widely in their use of some of these and other practices, and that these differences had dramatic financial consequences for their customers, with average fees paid by consumers ranging from $147 at some banks to more than twice as much ($298) at other banks. One notable variation was the percentage of consumers who opted in to debit and ATM card overdrafts, ranging from the single digits at some banks to more than 40% at others. These differences could result from whether the bank used pressuring tactics to persuade consumers to opt-in. (Some banks, such as Bank of America, do not permit overdrafts by debit card.)

The CFPB also found that rules issued in 2009 by the Federal Reserve Board requiring consumer opt-in for debit and ATM card transactions did help reduce the amount of overdraft fees paid by consumers. National Consumer Law Center Deputy Director Carolyn Carter noted, “It appears that a modest amount of regulation has resulted in a modest improvement but more needs to be done. We hope that more robust regulation will be adopted and will result in the end of overdraft abuses.”

Some of the reforms urged by NCLC advocates include:

- Limiting the number of times consumers can overdraw their accounts and be charged an overdraft fee to six times per year.
- Prohibiting point-of-sale debit and ATM card overdrafts, given that these transactions can be declined in real time without a fee.
- Requiring that overdraft fees be “reasonable and proportional” to the cost incurred by the banks for overdrawn or not sufficient funds transactions.
- Prohibiting banks from posting transactions from highest to lowest in amount, or in any manner that increases the number of overdrafts, and instead requiring that banks post transactions to minimize fees, or at least in a chronological or other neutral order
- Requiring banks to provide Truth in Lending disclosures, given that overdrafts actually represent a form of very high cost credit.

Related Materials

Common Sense from the Common Law: Why a Longstanding Legal Doctrine Supports Limiting Bank Overdraft Fees to a “Reasonable and Proportional Standard, April 2013

– Issue Brief: http://www.nclc.org/images/pdf/high_cost_small_loans/ib-common-sense-common-law.pdf

– Full Report: http://www.nclc.org/images/pdf/banking_and_payment_systems/common-law-overdraft-fees.pdf

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