

## How to ace new Fed overdraft compliance rules

July 1 marks mandatory compliance date. 21 key questions answered

By  
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Special Notice: You can sign up to attend/or purchase CDs after the fact of ABA's two-hour telephone briefing of March 10, "New Overdraft Rules: Steps Communications and Operations Staff Need To Take To Ensure Success on July 1, " here. Among the speakers are the authors of the following article, Nessa Feddis and Virginia O'Neill.

Additional Preparation: You can purchase CDs of ABA's earlier two-hour telephone briefing of Jan. 21, "The New Overdraft Rules: Will Your Bank Be Compliant," here. The presentation features ABA's Nessa Feddis and speakers from the Federal Reserve and Morrison and Foerster LLP.

On Nov. 12, 2009, the Federal Reserve Board released final amendments to Regulation E (Electronic Fund Transfer Act) related to overdraft policies and disclosures.

The final rule, available here, reflects input that the Board evaluated from consumer testing and public comments on its two proposed regulations to address overdraft fees.

In brief, the new rule provides that banks may not charge overdraft fees on certain debit card overdrafts—specifically ATM and one-time debit card overdrafts—unless the customer has expressly consented or "opted in" to pay such fees. The mandatory compliance date is July 1, 2010.

Many bankers have had questions about the new rules. Here are answers to the most frequent:

Q1. We don't offer an automated service for paying overdrafts. Instead, daily, we review the non-sufficient funds reports and decide to pay or return, for each transaction. So, does the rule apply?

A. Yes. The rule applies even if a bank does not have an automated program for paying overdrafts and makes decisions to pay ATM and one-time debit overdrafts on an ad hoc basis. In addition, there are no exceptions to the prohibition against charging an overdraft fee to a customer who has not opted in.

Section 205.17(b) (4) appears to provide an exception for inadvertent overdrafts paid by institutions with a policy and practice of not paying ATM or one-time debit overdrafts. However, Federal Reserve staff has made it clear that this exception was not intended. Instead, the staff has stated that the intent was only to create an exception to the notice and opt-in requirement. The agency is expected to clarify this in later amendments to the regulation.

Q2. Does this rule impact non-sufficient fund (NSF) fees, that is, the fees imposed when an item that would overdraw the account is returned?

A. No, the rule does not cover fees imposed when an item is returned. However, Congress is currently scrutinizing the amount and frequency of overdraft fees and may well turn to NSF fees if it perceives those fees are too high or frequent.

Q3. What about a bank that has a "courtesy" overdraft program that applies to all items (checks, all debit card transactions, and ACH transactions), but whose core processor cannot allow some customers to have debit card overdrafts paid and others not? In other words, the core processor only permits the bank to provide debit card overdraft protection for all customers or for no customers. Must the bank discontinue its program?

A. If the bank's core processor does not permit it to make a debit card opt-in available on a per customer basis, the bank will probably have to discontinue the overdraft service for debit card transactions. In effect, this is what banks previously did--denied authorizations if the account had insufficient funds at the time authorization was requested. However, the bank may continue to offer overdraft protection for non-debit card transactions such as ACH and check transactions.

Q4. Does the rule apply to fees for overdrafts paid from an overdraft line of credit, or paid by a transfer from another account, such as a savings account?

A. No. The rule does not apply to fees related to overdraft lines of credit or services which transfer funds from another account to pay overdrafts.

Q5. Does the opt-in requirement apply to all customers, including existing customers, or only to new customers?

A. The opt-in provision applies to both new customers and existing customers.

- New customers may receive the notice at account opening or some other time.

- Existing customers must receive the written notice, and, unless they have opted in by Aug. 15, 2010, the bank may not impose a fee for covered overdraft transactions after that date.

Q6. What about daily overdraft fees and negative balance fees? Must customers opt-in to this fee before the bank may charge it for covered debit card transactions?

A. The Commentary makes it clear that any fee charged for an ATM or one-time debit card overdraft is subject to the opt-in requirement, including but not limited to a per item, per occurrence, daily, sustained overdraft, or negative balance fee.

Q7. May the bank condition the payment of overdrafts for checks, ACH transactions, or recurring debit card transactions on the customer opting-in to the payment of overdrafts for ATM and one-time debit card transactions?

A. No, the rule prohibits such an "all or nothing" choice. The rule requires banks to use the

same criteria for declining or paying non-covered overdrafts, such as check and ACH transactions, whether or not the customer has opted in.

The rule also prohibits banks from conditioning the payment of recurring debit card transactions on a customer opting-in to the bank's ATM and one-time debit card overdraft program.

This means that the recurring debit card transactions of those who do not opt in must be treated in the same way with regard to overdraft payment decisions as those of customers who do opt in. This may present operational challenges.

Q8. What is the difference between a one-time debit card transaction and a recurring one?

A. Recurring debit card transactions would include, for example, debit card transactions used for payment of monthly or other recurring bills. One-time debit card transactions include point-of-sale (POS) transactions, as well as the periodic payment of a bill via on-line bill pay. The rule requires that banks provide opt-in prior to imposing fees for paying ATM and one-time debit card overdrafts.

Q9. How will the bank know that a debit card transaction is recurring or not?

A. Good question. Merchants are supposed to code debit card transactions to indicate whether or not the transactions are recurring-but many do not.

Accordingly, the Commentary to the regulation provides a safe harbor: Banks may rely on the code supplied by merchants.

Thus, if the transaction is coded as a recurring debit card transaction-even though it is a one-time debit-the bank may treat the transaction as recurring and is free to charge an overdraft fee.

However,

to take advantage of this safe harbor, bank processing systems must be able to recognize this code at the point where it makes the decision to pay or reject the transaction.

Q 10. Let's

say the ATM/debit card network is temporarily off-line, goes into stand-in mode, and authorizes transactions without checking the account balance. Is the bank only allowed to charge the overdraft fees on overdrafts for customers who have opted-in?

A. Yes, there are no exceptions to the rule that banks may not charge overdraft fees on covered transactions unless the customer has opted-in. This includes overdrafts paid when using a stand-in processor to authorize the transaction, because the card network was temporarily off-line.

Q 11. What if there were sufficient funds when the bank authorized a debit card transaction, but there are insufficient funds when the actual transaction is presented? May the bank charge a fee?

A. If the customer has not opted-in, the bank may not charge a fee, even if the bank is not in a position to avoid the overdraft. The Federal Reserve understood that there would be instances when this would happen.

For example, it may happen if a merchant fails to obtain approval for a small-dollar transaction. Or it may happen if a deposit is returned after the debit card transaction has been approved or paid.

However, because such instances would be rare and pose limited risk, and because it would be confusing to customers to be told they would not be charged debit card overdraft fees and then have one imposed, the final rule prohibits charging a fee in these instances unless the customer has opted in.

Q12. Some banks allow customers to overdraw at the ATM. Customers may receive a warning on the ATM screen that proceeding with the transaction will cause an overdraft and an overdraft fee. If the customer has opted-in, must the bank disclose the amount of the fee on the ATM?

A. Federal regulations, including recently amended Regulation E, do not require such a notice on ATMs. However, in the 2005 "Interagency Guidance on Overdraft Protection Programs," the federal banking agencies suggested that providing such a notice would be a best practice.

The Guidance provides:

"When consumers attempt to withdraw or transfer funds made available through an overdraft protection program, [banks should] provide a specific consumer notice, where feasible, that completing the withdrawal may trigger the overdraft fees (for example, it presently may be feasible at a branch teller window). This notice should be presented in a manner that permits consumers to cancel the attempted withdrawal or transfer after receiving the notice. If this is not feasible, then [banks should] post notices (e.g., on proprietary ATMs) explaining that transactions may be approved that overdraw the account and fees may be incurred."

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Q13. May the bank pay a covered debit card overdraft if the customer has not opted-in?

A. Yes. The bank may pay the covered overdraft. It simply cannot charge the fee if the customer has not opted-in.

Q14. What if a combination of transactions (e.g., ACH transaction, check, or recurring debit card transaction) causes the overdraft and the customer has not opted in. May the bank charge a fee?

A. The bank may impose fees for check, ACH, and recurring debit card overdrafts. The bank may also want to review its payment order policies. If it is obligated to pay certain transactions, such as debit card transactions, it might consider paying them first so that it is not the debit card transaction that overdraws the account. However, even if the bank does not knowingly pay debit card overdrafts, they may still occur, and the bank may not charge an overdraft fee unless the customer has opted in.

Q15. May banks charge a "denial fee" for denied ATM withdrawals and denied POS transactions?

A. Although the rule does not address such fees, the Supplementary Information to the final rule discusses "declined transaction fees," warning banks that the imposition of "such fees could raise significant fairness issues under the Federal Trade Commission Act, because the institution bears little, if any, risk or cost to decline authorization of an ATM or one-time debit card transaction."

That being said, banks may incur network costs associated with a request and denial. In addition, legislation has been introduced in Congress that would prohibit such fees.

Q16. Are there requirements about the form and content of the opt-in notice?

A. Yes. The notice must be in writing and may be given electronically, if the customer agrees. The notice must be segregated from all other information and may not contain any information not specified or permitted by the rule. The notice may describe alternative ways to cover overdrafts. The final rule includes a model opt-in notice.

Q17. Must the customer's consent to opt in be in writing?

A. No. While the regulation specifically requires the bank to provide written notice of customers' right to opt-in and written confirmation if they do, it does not require that the consent be in writing, although it may be.

The Commentary specifically provides that reasonable methods of consent include those made by telephone. For example, if the bank has provided written notice of the opt-in and a customer calls in wanting the bank to pay the dinner bill at the restaurant, the customer may opt-in over the phone. The bank must then, however, provide written confirmation of the customer's consent.

Q18. For joint accounts, is it necessary to obtain affirmative consent from all of the account holders?

A. No. If one

account holder opts-in, the bank may honor the request and pay all covered debit card overdrafts for the account and impose a fee.

Q19. Under the rule, customers must be allowed to revoke their consent at any time in the manner made available to the same consumer for providing consent. Does that mean if a customer opens an account online the bank must have a method immediately available to allow the customer to revoke it electronically?

A. The regulation

provides that a bank must provide a means for a consumer "to revoke consent at any time in the manner made available to the consumer for providing consent."

However, the words

"at any time" should not be read too literally. It seems unlikely that the Federal Reserve intended to require banks that permit accounts to be opened online to provide the opportunity to opt-in and then immediately follow that with an on-line opportunity to opt-out. In fact, that would unnecessarily confuse consumers—a result that the Fed was working hard to avoid. The intent of the language quoted was to ensure that banks make it just as convenient for a customer to revoke consent as they make it for a customer to opt-in.

Q20. May customers opt-in and out at their convenience and discretion?

A. Yes, the rule requires banks to provide a continuing right to opt-in or out at any time in the manner described in the opt-in notice. The rule also states that a bank must implement the consumer's revocation "as soon as reasonably practicable" after receiving the request. However, revocation does not require the bank to waive or reverse fees assessed prior to receipt of the revocation request.

Q21.

Do banks have to disclose the "privilege" amount?

A. The rule does not address disclosure of "privilege" amounts. However, when disclosing ATM balances, including the "privilege" amount as part of an undifferentiated available balance has been considered as unfair or deceptive by the banking agencies.

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