



ProBank
Austin



2019 Fall Compliance Superhero Conference

Let's Talk Overdrafts

Speaker: Leah M. Hamilton, JD | VP and Sr. Consultant | ProBank Austin | ProBank Advisor

© 2019. Professional Bank Services, LLC

What You Will Learn

- Overdrafts
 - The Rules
 - Guidance
 - Safe and soundness
 - Fair Lending
 - Regulation O (insider lending)
- Are you covered?

- 2 -



Overdraft

- Overdraft program compliance is not merely satisfaction with a single, clear-cut rule
 - Riddled with multiple laws
 - Regulations E, DD and O
 - Doctrines of fairness
 - Supervisory guidance
 - UDAP/UDAAP
 - Safety and soundness implications
 - What's in a name ...
 - "Overdraft Protection"



- 3 -



Overdraft Rules

- Foundation
 - Regulation E (12 CFR 1005.17) where "overdraft service" is defined as:
 - "a service under which a financial institution assesses a fee or charge on a consumer's account held by the institution for paying a transaction (including a check or other item) when the consumer has insufficient or unavailable funds in the account."
- Does not include
 - any payment of overdrafts pursuant to:
 - a line of credit subject to Regulation Z (12 CFR part 1026), including transfers from a credit card account, home equity line of credit, or overdraft line of credit;
 - a service that transfers funds from another account held individually or jointly by a consumer, such as a savings account;
 - a line of credit or other transaction exempt from Regulation Z (12 CFR part 1026) pursuant to 12 CFR 1026.3(d)"; or
 - Effective April 1, 2019, a covered separate credit feature accessible by a hybrid prepaid-credit card as defined in Regulation Z, 12 CFR 1026.61; or credit extended through a negative balance on the asset feature of the prepaid account that meets the conditions of 12 CFR 1026.61(a)(4)

- 4 -



Regulation E Opt-in

- Opt-in (Model A-9 form)
 - Consumer must be provided a written notice (or one electronically subject to E-SIGN) that:
 - Describes the overdraft service;
 - Provides the consumer a reasonable opportunity to opt-in to the service for ATM and POS transactions;
 - Obtains the consumer's affirmative consent or opt-in to the institution's payment of ATM or POS transactions; and
 - The institution must provide the consumer a confirmation in writing (electronically if consumer agrees) that includes a statement that the consumer may opt out or revoke consent at any time

- 5 -

What You Need to Know about Overdrafts and Overdraft Fees

An **overdraft** occurs when you do not have enough money in your account to cover a transaction, but we pay it anyway. We can cover your overdrafts in two different ways:

1. We have **standard overdraft practices** that come with your account.
2. We also offer **overdraft protection plans**, such as a link to a savings account, which may be less expensive than our standard overdraft practices. To learn more, ask us about these plans.

This notice explains our **standard overdraft practices**.

What are the **standard overdraft practices** that come with my account?

We do authorize and pay overdrafts for the following types of transactions:

- Checks and other transactions made using your checking account number
- Automatic bill payments

We **do not** authorize and pay overdrafts for the following types of transactions unless you ask us to (see below):

- ATM Transactions
 - Everyday debit card transactions
- We pay overdrafts at our discretion, which means we **do not guarantee** that we will always authorize and pay any type of transaction.

If we do not authorize and pay an overdraft, your transaction will be declined.

What fees will I be charged if [institution name] pays my overdraft?

Under our standard overdraft practices:

- We will charge you a fee of up to \$30 each time we pay an overdraft.
- Also, if your account is overdrawn for 5 or more consecutive business days, we will charge an additional \$5 per day.
- There is **no limit** on the total fees we can charge you for overdrawing your account.

What if I want [institution name] to authorize and pay overdrafts on my ATM and everyday debit card transactions?

If you also want us to authorize and pay overdrafts on ATM and everyday debit card transactions, call [telephone number], visit [website], or complete the form below and present it at a branch/mail it to:

_____ I do not want [institution name] to authorize and pay overdrafts on my ATM and everyday debit card transactions.

_____ I want [institution name] to authorize and pay overdrafts on my ATM and everyday debit card transactions.

Printed Name: _____

Date: _____

[Account Number]: _____



Paying Overdrafts is Discretionary

- Because overdraft services are generally discretionary, institution may terminate service at any time
 - Reserve discretionary right to mitigate UDAP/UDAAP
- For example
 - May suspend the discretionary overdraft service due to abuse of the service or lack of sufficient funds for an extended period
 - However, terminating or limiting the program would require re-notification, consent and confirmation

- 6 -



Marketing Tactics

- *“Would you like to add any overdraft service to your account?”*
 - Be sure to explain the program
- Aggressive tactics raise UDAP/UDAAP concerns
 - Sales pitch - *“The service is free”*
 - Could be viewed as deceptive if in fact there is a fee if the service is used
 - Marketing copy that incites action based on fear - *“You don’t want to be stuck with a broken down car with your kids in the backseat”*
 - Could be viewed as unfair
 - Email blasts after consumer has declined or revoked consent



- 7 -



Truth-in-Savings (Regulation DD/Part 707)

- Advertising or promoting overdraft programs
 - Any advertisement promoting the payment of overdrafts shall disclose in a clear and conspicuous manner:
 - The fee or fees for the payment of each overdraft;
 - The categories of transactions for which a fee for paying an overdraft may be imposed;
 - The time period by which the consumer must repay or cover any overdraft; and
 - The circumstances under which the institution will not pay an overdraft
- A simple compliant disclosure

“You may be charged our standard overdraft fee of \$30 for each item created by check, in-person withdrawals, ATM withdrawals or other electronic means paid under the limit. All negative balances must be brought positive within 30 days. Whether your overdrafts will be paid is discretionary, and we reserve the right not to pay. For example, we typically do not pay overdrafts if your account is not in good standing, or you are not making regular deposits, or you have too many overdrafts. Please contact a customer service representative for more details.”

- 8 -



Add UDAP / UDAAP Analysis

- Today, expectation for more robust disclosures
 - Provide alternatives to OD
 - Detail inner-workings of how OD program / alternatives work
- Offer OD management tools:
 - Alerts via mobile or online banking;
 - Convenient funds transfer tools;
 - Account sweeps or overdraft lines of credit;
 - Caps on the number or amount of overdraft fees; and most importantly,
 - Explaining the options in plain-English, detailed clearly and conspicuously

- 9 -



The Guidance

- *2005 Joint Guidance on Overdraft Protection Programs* is the cornerstone for OD programs and services
 - Addresses wide-range of impact areas, including safety and soundness, legal risks, best practices
 - Parts have been codified in Regulations E and DD
- Several recommendations remain best practices and/or have become regulator expectations
 - Avoid promoting poor account management;
 - Train staff to explain program features and other choices;
 - Clearly explain the discretionary nature of program;
 - Distinguish overdraft services from “free” account features free of charges,
 - Clarify that fees count against the disclosed overdraft dollar limit;
 - Demonstrate when multiple fees will be charged;
 - Explain the impact of transaction clearing policies;
 - Illustrate the type of transactions covered;
 - Provide election or opt-out of service—not just ATM/POS transactions;
 - Alert consumers before a transaction triggers any fees;
 - Promptly notify consumers of overdraft program usage each time used;
 - Monitor overdraft program usage; and
 - Fairly report program usage

- 10 -



Safety and Soundness

- Overdraft services are subject to examiner review
 - Compliance exams
 - Safety and soundness exams
- Every institution should be prepared to have its overdraft services, formal or ad hoc, reviewed during both compliance and safety and soundness examinations
- 2005 Overdraft Guidance also sets forth certain safety and soundness considerations institutions should consider when establishing overdraft programs and services

- 11 -



Safety and Soundness

- From the 2005 Overdraft Guidance
 - Written policies and procedures **adequate to address the credit, operational, and other risks** associated with overdraft programs;
 - Prudent risk management practices including the establishment of **express account eligibility standards** and well-defined and properly documented dollar limit decision criteria;
 - **Account monitoring on an ongoing basis** with the ability to identify consumers who may represent **an undue credit risk** to the institution;
 - Programs should be administered and adjusted, as needed, to **ensure that credit risk remains in line** with expectations;
 - *Reports on a regular basis that are sufficient to enable management to identify, measure, and manage overdraft volume, profitability, and credit performance;*
 - **Prudent risk management** practices related to account repayment and suspension of overdraft services, including specific timeframes for when consumers must pay off their overdraft balances;
 - For **reporting of income and loss recognition** on overdraft programs, institutions should follow generally accepted accounting principles (GAAP) and the instructions for the Reports of Condition and Income (Call Report), and NCUA 5300 Call Report;
 - **Overdraft balances should be reported on regulatory reports as loans and should be charged off against the allowance for loan and lease losses; agencies expect all institutions to adopt rigorous loss estimation processes to ensure that overdraft fee income is accurately measured;**
 - **Proper risk-based capital treatment** of outstanding overdrawn balances and unused commitments; risk-weighted according to the obligor;
 - Contracts with third-party vendors **must conduct thorough due diligence reviews** prior to signing a contract

- 12 -



Fair Lending

- Fair lending laws apply to all forms of credit, including overdrafts
- Whether program is ad hoc, formal, a line of credit or an account sweep, fair lending considerations come into play
 - For example, age limits on overdraft programs and fees can pose a discrimination issue under ECOA
 - If an institution offers a checking product with overdraft services for 55+ and the overdraft fee is \$25 versus \$35 for all other checking products, this would be age discrimination under Regulation B
 - The product and service could be offered to age 62+ without violating ECOA

- 13 -



Fair Lending

- Overdraft fee waivers
 - Track overdraft fee waivers, whether discretion to pay is automated or by human-decisioning
 - Patterns and trends should be carefully scrutinized to ensure no fair lending concerns can be perceived, actual or potential
 - Policies and procedures should clearly indicate who has authority to waive an overdraft fee or to pay/not pay an item into overdraft as well as parameters of when an overdraft fee should be waived
- Fair lending training
 - Include the potential of discrimination of waiving fees and discretion to pay/not pay
 - Particularly true when it comes to waiving fees for high net worth customers and executive officers and directors
 - Fair lending concerns could arise if your high net worth customers tend to be of a particular race, ethnicity, age, or gender, for example
 - Executive officers and directors are subject to restraints under Regulation O

- 14 -



Regulation O (Insider Lending)

- No bank may pay an overdraft of an executive officer or director of the bank or executive officer or director of its affiliates on an account at the bank, unless the payment of funds is made in accordance with:
 - (i) a written, preauthorized, interest-bearing extension of credit plan that specifies a method of repayment; or
 - (ii) a written, preauthorized transfer of funds from another account of the account holder at the bank
- One exception
 - A bank may honor an “inadvertent overdraft”
 - Such overdrafts, in the aggregate, may not exceed \$1,000;
 - Account cannot be overdrawn for more than five business days; and
 - The executive officer or director is charged the same fee as any other customer of the bank in similar circumstances
 - Notes:
 - This prohibition does not apply to the payment by a member bank of an overdraft of a principal shareholder of the member bank, unless the principal shareholder is also an executive officer or director
 - This prohibition also does not apply to the payment by a member bank of an overdraft of a related interest of an executive officer, director, or principal shareholder of the member bank or executive officer, director, or principal shareholder of its affiliates

- 15 -



Are you covered?



What can you do? What should you do?

- Not an impossible feat
 - Ensure compliance with the regulations
 - Monitor consent orders and the guidance issued by all of the agencies as regulators may adopt similar findings or practices
- To get your overdraft programs or services on a compliance-track, consider the following best practices in addition to regulatory requirements

- 17 -



Best Practices

- Memo post holds
 - Ensure systems do not charge overdraft fees when a preauthorized hold for a lower amount comes back higher and now there are insufficient funds (e.g., gas stations and restaurants may have a lower amount initially and settle at a higher amount)
- Collecting opt-ins with no intent to pay
 - Do not collect opt-ins for ATM/POS transactions if the policy is not to pay such overdrafts as force-pays may trigger a charge
- Linked accounts
 - Offer services with details of how transfers work (in part or whole only transfers) and fees; charge appropriate fees for sweep vs. overdraft
- Limiting fees
 - Consider limits on maximum amount of fees charged in a day; consider fees proportional to the amount overdrawn; ensure system parameters are functioning accordingly; ensure fees are comparable to peers and competitors

- 18 -



Best Practices

- Transaction clearing
 - Ensure system parameters and manual processes have a neutral process for clearing transactions (high to low is strongly discouraged)
- Notifications
 - Notify customers electronically, at teller window and/or ATMs if transaction will cause overdraft, in order to allow the customer to cancel the transaction without a fee
- Disclosures
 - Ensure consistent terminology is used across advertisements, disclosures and account agreements (e.g., overdraft fee across all three vs. NSF); use model language provided in regulations
- Advertising overdraft options
 - Ensure compliance with advertising overdraft rules if you promote programs or services, including all required disclosures and recommended disclosures as applicable; do not reference “free” if in fact there are fees associated; include alternative options; do not use pressure tactics to obtain opt-ins

- 19 -



Best Practices

- Naming overdraft services
 - Do not call overdraft services “overdraft protection” which implies that it is on all the time (you wouldn’t want your home security system to work some of the time); title the service what it is: Overdraft Courtesy, Overdraft Coverage, or Overdraft Management, for example
- Training
 - Ensure staff are trained on the impact of fair lending and UDAAP concepts on overdraft programs as well as the product/service offered to ensure sales pitches are accurate and without undue pressure; provide customer education information and materials (e.g., brochures, financial workshops, detailed disclosures)
- Monitoring
 - Do regularly monitor service usage to ensure the same customers are not incurring overdraft fees on a recurring basis (if they are, the bank should have a process in place to address such excessive overdraft usage); front line ongoing monitoring of systems and manual processes (including that automated fees are charged accurately); and re-validate systems after updates and patches
- Reporting
 - Provide usage, cost, loss reports to senior management and the Board of Directors on a regular basis

- 20 -



- **Complaint Management**
 - Monitor complaints about the services; adjust programs and services to avoid unfair, deceptive or abusive acts or practices; monitor complaints of third party overdraft products/services institution utilizes
- **Third-party risk management**
 - Ensure third parties have strong compliant overdraft programs, policies, procedures and practices in place; request regular reports as applicable; ensure oversight in place and performed
- **Corrective Action**
 - Take identified issues seriously and address promptly; provide refunds or restitution promptly

Questions?



Overdraft: Are you covered?

By Leah M. Hamilton, J.D.

March 2019

Financial institutions have struggled with overdraft compliance for more than a decade. What was once a revenue stream, has become a compliance challenge and expense. Nevertheless, institutions continue to offer overdraft services and customers welcome the option.

Overdraft program compliance is not merely satisfaction with a single, clear-cut rule. Rather, compliance is riddled with multiple laws (e.g., Regulations E, DD and O), doctrines of fairness, supervisory guidance, UDAAP, and safety and soundness implications.

The Rules

The primary foundation of a compliant consumer overdraft program, particularly as applied to ATM and one-time point-of-sale debit card transactions (POS), is unearthed in Regulation E (12 CFR 1005.17) where “overdraft service” is defined as:

“a service under which a financial institution assesses a fee or charge on a consumer's account held by the institution for paying a transaction (including a check or other item) when the consumer has insufficient or unavailable funds in the account.”

Regulation E further defines that overdraft service does not include: “any payment of overdrafts pursuant to:

1. a line of credit subject to Regulation Z (12 CFR part 1026), including transfers from a credit card account, home equity line of credit, or overdraft line of credit;
2. a service that transfers funds from another account held individually or jointly by a consumer, such as a savings account; or
3. a line of credit or other transaction exempt from Regulation Z (12 CFR part 1026) pursuant to 12 CFR 1026.3(d).”

Effective April 1, 2019, what overdraft service is *not*, also includes “a covered separate credit feature accessible by a hybrid prepaid-credit card as defined in Regulation Z, 12 CFR 1026.61; or credit extended through a negative balance on the asset feature of the prepaid account that meets the conditions of 12 CFR 1026.61(a)(4).”¹

Regulation E generally provides that a consumer must be provided a written notice (or one electronically subject to E-SIGN) that:

- Describes the overdraft service;
- Provides the consumer a reasonable opportunity to opt-in to the service for ATM and POS transactions;
- Obtains the consumer’s affirmative consent or opt-in to the institution's payment of ATM or POS transactions; and

¹ At the time of printing, the CFPB had not issued any extension of the effective date of April 1, 2019.



- The institution must provide the consumer a confirmation in writing (electronically if consumer agrees) that includes a statement that the consumer may opt out or revoke consent at any time.

Because overdraft services are generally discretionary, an institution may terminate the service at any time. For example, a bank could suspend the discretionary overdraft service due to abuse of the service or lack of sufficient funds for an extended period. However, terminating or limiting the program would require re-notification, consent and confirmation.

The opt-in requirement has been a source of contention among regulators, media and consumer groups over the years. Straightforward opt-in marketing communications might ask: “Would you like to add any overdraft service to your account?” Other banks have taken a more aggressive stance which has raised UDAAP questions. For example, a sales pitch that states, “The service is free,” could be viewed as deceptive, when in fact there is a fee if the service is used. Alternatively, marketing copy that incites action based on fear could be viewed as unfair, such as: “You don’t want to be stuck with a broken down car with your kids in the backseat”. In other cases, banks have continued to send emails marketing overdraft services after the consumer has already declined the overdraft service or revoked consent. Such tactics do not follow the spirit of Regulation E, nor do they align with the advertisement of overdraft service requirements of Regulation DD.

Regulation DD, the implementing regulation for the Truth-in-Savings Act, provides regulatory requirements for advertising overdraft services as well as certain periodic statement disclosures. To comply with Regulation DD, the advertisement requirements appear to be straightforward:

“any advertisement promoting the payment of overdrafts shall disclose in a clear and conspicuous manner:

- (i) The fee or fees for the payment of each overdraft;
- (ii) The categories of transactions for which a fee for paying an overdraft may be imposed;
- (iii) The time period by which the consumer must repay or cover any overdraft; and
- (iv) The circumstances under which the institution will not pay an overdraft.”

However, when you overlay unfair, deceptive or abusive acts or practices (UDAP/UDAAP), the requirements become basic elements to a more robust advertisement to ensure customers, not just consumers, are provided full disclosures of the inner-workings of the overdraft service, available coverage options and customer responsibilities.²

A decade ago, a simple compliant disclosure may have read, *“You may be charged our standard overdraft fee of \$30 for each item created by check, in-person withdrawals, ATM withdrawals or other electronic means paid under the limit. All negative balances must be brought positive within 30 days. Whether your overdrafts will be paid is discretionary, and we reserve the right not to pay. For example,*

² UDAP – Section 5 of the Federal Trade Commission (FTC) Act applies to both consumer and commercial customers; UDAAP – Section 1036(a) of Dodd-Frank statute applies only to consumers and only to a consumer financial product or service (which includes overdraft services).



we typically do not pay overdrafts if your account is not in good standing, or you are not making regular deposits, or you have too many overdrafts. Please contact a customer service representative for more details.”

However, today’s supervisory expectations have broadened to include more robust disclosures to incorporate overdraft management tools also, such as:

- Alerts via mobile or online banking;
- Convenient funds transfer tools;
- Account sweeps or overdraft lines of credit;
- Caps on the number or amount of overdraft fees; and most importantly,
- Explaining the options in plain-English, detailed clearly and conspicuously.

Moreover, more consent orders are issued for non-compliant overdraft programs that arise from unfair, deceptive and abusive acts and practices than Regulation E or DD.

The Guidance

The 2005 “*Joint Guidance on Overdraft Protection Programs*” (2005 Overdraft Guidance) issued by Office of the Comptroller of the Currency (OCC); Board of Governors of the Federal Reserve System (FRB); Federal Deposit Insurance Corporation (FDIC); and National Credit Union Administration (NCUA) is the cornerstone for overdraft programs and services. The 2005 Overdraft Guidance was issued to assist banks in the disclosures and administration of overdraft programs. Issued in February 2005, the Guidance addresses safety and soundness considerations, legal risks and best practices, which still hold true today. Although some of the recommendations in the 2005 Overdraft Guidance have since been incorporated into Regulations E (e.g., opt-in) and DD (e.g., periodic statement disclosures), several recommendations remain that are considered best practices and/or have become regulator expectations, such as to:

- Avoid promoting poor account management;
- Train staff to explain program features and other choices;
- Clearly explain the discretionary nature of program;
- Distinguish overdraft services from “free” account features free of charges,
- Clarify that fees count against the disclosed overdraft dollar limit;
- Demonstrate when multiple fees will be charged;
- Explain the impact of transaction clearing policies;
- Illustrate the type of transactions covered;
- Provide election or opt-out of service—not just ATM/POS transactions;
- Alert consumers before a transaction triggers any fees;
- Promptly notify consumers of overdraft program usage each time used;
- Monitor overdraft program usage; and
- Fairly report program usage.

The agencies have issued additional guidance through FILs, bulletins and letters.³ Recently, the agencies issued the Interagency Statement Clarifying the Role of Supervisory Guidance. Although this guidance

³ For example, FDIC’s 2010 *FDIC Overdraft Payment Program Supervisory Guidance Frequently Asked Questions* and FDIC’s regional offices 2014 *Fees Associated with Extended Overdrafts*; OCC’s 2015 *Deposit Related Credit* handbook for examiners, section *Overdraft Protection Services*; CFPB’s *Understanding the “Opt-in” Choice* for consumers.



covers all supervisory guidance, institutions should consider its application to overdraft products and services, particularly the impact to safety and soundness.

Safety and Soundness

Overdraft services are subject to examiner review for compliance and safety and soundness examinations. Every institution should be prepared to have its overdraft services, formal or ad hoc, reviewed during both compliance and safety and soundness examinations. The 2005 Overdraft Guidance also set forth certain safety and soundness considerations institutions should consider when establishing overdraft programs and services:

- ✓ Written policies and procedures adequate to address the credit, operational, and other risks associated with overdraft programs;
- ✓ Prudent risk management practices including the establishment of express account eligibility standards and well-defined and properly documented dollar limit decision criteria;
- ✓ Account monitoring on an ongoing basis with the ability to identify consumers who may represent an undue credit risk to the institution;
- ✓ Programs should be administered and adjusted, as needed, to ensure that credit risk remains in line with expectations;
- ✓ Reports on a regular basis that are sufficient to enable management to identify, measure, and manage overdraft volume, profitability, and credit performance;
- ✓ Prudent risk management practices related to account repayment and suspension of overdraft services, including specific timeframes for when consumers must pay off their overdraft balances;
- ✓ For reporting of income and loss recognition on overdraft programs, institutions should follow generally accepted accounting principles (GAAP) and the instructions for the Reports of Condition and Income (Call Report), and NCUA 5300 Call Report;
- ✓ Overdraft balances should be reported on regulatory reports as loans and should be charged off against the allowance for loan and lease losses; agencies expect all institutions to adopt rigorous loss estimation processes to ensure that overdraft fee income is accurately measured;
- ✓ Proper risk-based capital treatment of outstanding overdrawn balances and unused commitments; risk-weighted according to the obligor;
- ✓ Contracts with third-party vendors must conduct thorough due diligence reviews prior to signing a contract;

To be sure, safety and soundness is a vital component of any overdraft program or service. After all, paying items into overdraft is credit. And because it is credit, financial institutions must manage its risk accordingly, including its safety and soundness risk and fair lending risk.

Fair Lending

Fair lending laws apply to all forms of credit, including overdrafts. Whether the bank's overdraft product or service is ad hoc, formal, a line of credit or an account sweep, fair lending considerations come into play. For example, age limits on overdraft programs and fees can pose a discrimination issue under ECOA. For example, if an institution offers a checking product with overdraft services for 55+ and the overdraft fee is \$25 versus \$35 for all other checking products, this would be age discrimination under Regulation B. The product and service could be offered to age 62+ without violating ECOA.

Institutions would be wise to track overdraft fee waivers, whether discretion to pay is automated or by human-decisioning. Patterns and trends should be carefully scrutinized to ensure no fair lending concerns can be perceived, actual or potential. Policies and procedures should clearly indicate who has authority to waive an overdraft fee or to pay/not pay an item into overdraft as well as parameters of when



an overdraft fee should be waived. Fair lending training should include the potential of discrimination of waiving fees and discretion to pay/not pay. This is particularly true when it comes to waiving fees for high net worth customers and executive officers and directors. Fair lending concerns could arise if your high net worth customers tend to be of a particular race, ethnicity, age, or gender, for example. Executive officers and directors are subject to restraints under Regulation O.

Regulation O

Under Regulation O (12 CFR 215.4), no bank may pay an overdraft of an executive officer or director of the bank or executive officer or director of its affiliates⁴ on an account at the bank, unless the payment of funds is made in accordance with: (i) a written, preauthorized, interest-bearing extension of credit plan that specifies a method of repayment; or (ii) a written, preauthorized transfer of funds from another account of the account holder at the bank. The one exception to the rule is that an institution may honor an “inadvertent overdraft”, which such overdrafts, in the aggregate, may not exceed \$1,000, the account is not overdrawn for more than five business days, and the executive officer or director is charged the same fee as any other customer of the bank in similar circumstances.

Are You Covered?

Offering overdraft programs and services can be a compliance challenge, but it is not an impossible feat. In addition to complying with the regulations, financial institutions should monitor consent orders and the guidance issued by all the agencies as regulators may adopt similar findings or practices. To get your overdraft programs or services on a compliance-track, consider the following best practices in addition to regulatory requirements:

- Memo post holds—Ensure systems do not charge overdraft fees when a preauthorized hold for a lower amount comes back higher and now there are insufficient funds (e.g., gas stations and restaurants may have a lower amount initially and settle at a higher amount).
- Collecting opt-ins with no intent to pay—Do not collect opt-ins for ATM/POS transactions if the policy is not to pay such overdrafts as force-pays may trigger a charge.
- Linked accounts—Offer services with details of how transfers work (in part or whole only transfers) and fees; charge appropriate fees for sweep vs. overdraft.
- Limiting fees—Consider limits on maximum amount of fees charged in a day; consider fees proportional to the amount overdrawn; ensure system parameters are functioning accordingly; ensure fees are comparable to peers and competitors.
- Transaction clearing—Ensure system parameters and manual processes have a neutral process for clearing transactions (high to low is strongly discouraged).
- Notifications—Notify customers electronically, at teller window and/or ATMs if transaction will cause overdraft, in order to allow the customer to cancel the transaction without a fee.
- Disclosures—Ensure consistent terminology is used across advertisements, disclosures and account agreements (e.g., overdraft fee across all three vs. NSF); use model language provided in regulations.
- Advertising overdraft options—Ensure compliance with advertising overdraft rules if you promote programs or services, including all required disclosures and recommended disclosures as

⁴ Under 12 CFR 215.4, this prohibition does not apply to the payment by a member bank of an overdraft of a principal shareholder of the member bank, unless the principal shareholder is also an executive officer or director. This prohibition also does not apply to the payment by a member bank of an overdraft of a related interest of an executive officer, director, or principal shareholder of the member bank or executive officer, director, or principal shareholder of its affiliates.



applicable; do not reference “free” if in fact there are fees associated; include alternative options; do not use pressure tactics to obtain opt-ins.

- Naming overdraft services—Do not call overdraft services “overdraft protection” which implies that it is on all the time (you wouldn’t want your home security system to work some of the time); title the service what it is: Overdraft Courtesy, Overdraft Coverage, or Overdraft Management, for example.
- Training—Ensure staff are trained on the impact of fair lending and UDAAP concepts on overdraft programs as well as the product/service offered to ensure sales pitches are accurate and without undue pressure; provide customer education information and materials (e.g., brochures, financial workshops, detailed disclosures).
- Monitoring—Do regularly monitor service usage to ensure the same customers are not incurring overdraft fees on a recurring basis (if they are, the bank should have a process in place to address such excessive overdraft usage); front line ongoing monitoring of systems and manual processes (including that automated fees are charged accurately); and re-validate systems after updates and patches.
- Reporting—Provide usage, cost, loss reports to senior management and the Board of Directors on a regular basis.
- Complaint Management—Monitor complaints about the services; adjust programs and services to avoid unfair, deceptive or abusive acts or practices; monitor complaints of third party overdraft products/services institution utilizes.
- Third-party risk management—Ensure third parties have strong compliant overdraft programs, policies, procedures and practices in place; request regular reports as applicable; ensure oversight in place and performed.
- Corrective Action—Take identified issues seriously and address promptly; provide refunds or restitution promptly.

While overdrafts programs continue to be a source of regulatory scrutiny, by studying the regulations and regulatory guidance institutions can design and manage successful overdraft programs that provide a benefit to customers while managing regulator expectations.