Myths vs. Facts – CFPB's Overdraft Final Rule

Myth: If the CFPB's overdraft rule is invalidated, it would leave overdraft unregulated.

Fact: Overdraft services offered by banks are already highly regulated and closely supervised by the banking agencies and CFPB—and they would continue to be so if the CFPB's final rule is invalidated. In 2009, the Federal Reserve issued a strong, pro-consumer rule governing overdraft services resulting from point-of-sale debit card or ATM transactions. That rule, which is now administered by the CFPB, ensures that a customer receive a consumer-tested disclosure about its bank's overdraft service (and related fees) as well as alternative options for covering transactions that overdraw an account. The 2009 rule requires consumers to affirmatively consent—or "opt in"—to overdraft services before the bank can charge an overdraft fee. Importantly, the rule gives consumers an unfettered right to opt in and out of overdraft at any time without question or cost.

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Myth: Overdraft services are an extension of credit, which the CFPB is authorized to regulate under the Truth in Lending Act (TILA).

Fact: Congress passed TILA to ensure consumers receive "meaningful disclosure of credit terms," and expressly defined "credit" as "the right granted by a creditor to a debtor to defer payment of debt or to incur debt and defer its payment." Overdraft is not "credit" because bank deposit agreements do not give consumers the *right* to have an overdraft transaction paid or to defer payment—the bank retains discretion to pay (or not pay) the overdraft transaction. If the bank pays the transaction into overdraft, the overdrawn amount is due immediately to the bank. The Federal Reserve, which until 2010 had authority to issue regulations under TILA, has consistently concluded that discretionary overdraft services are not extensions of "credit" under TILA.

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Myth: The CFPB has authority under the Truth in Lending Act to impose substantive restrictions on overdraft services.

Fact: The CFPB does <u>not</u> have authority under the Truth in Lending Act to impose substantive restrictions on overdraft. TILA is a disclosure statute; Congress established a consumer protection regime grounded on clear disclosure and consumer choice—not regulation of the terms of consumer credit products. Yet Director Chopra's final rule goes far beyond mandating disclosure and would impose substantive restrictions on bank overdraft services, including fee caps and creation of separate "credit" accounts.

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Myth: The CFPB's overdraft rule does not impose a fee cap.

Fact: The entire regulatory proposal is designed to force banks to cap overdraft fees or offer a different form of credit. The rule unlawfully creates a new type of "credit" called "overdraft credit" that is subject to TILA/Reg. Z unless the bank charges a "true courtesy" overdraft fee that either (1) reflects the institution's "breakeven" costs to operate its overdraft program; or (2) conforms to a "benchmark" fee of $5 set by the CFPB. Thus, the CFPB has effectively imposed a price cap if a bank seeks to sustainably offer discretionary overdraft services.

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Myth: The CFPB's overdraft rule is necessary because the market for deposit account services is not competitive.

Fact: The consumer deposit account market is highly competitive. Responding to that competition, many banks have introduced changes to their overdraft programs to attract and retain customers. These innovations include sending low-balance alerts, imposing *de minimis* threshold triggering an overdraft fee, capping total fees that the bank may charge per day, and providing overdraft "grace periods" during which a customer can make a deposit and avoid a fee. Additionally, some banks no longer charge overdraft or NSF fees, and many banks offer overdraft-free accounts that meet the Bank On initiative's National Account Standards. The CFPB's own research confirms that, as a result of banks' innovations, consumers are paying less in overdraft and NSF fees now than they did six years ago.

***Myth*:** The CFPB's overdraft rule is necessary because overdraft fees are "junk fees."

***Fact*:** Studies have found that the average transaction that overdraws the customer's account is in the hundreds of dollars. One analysis of transaction data from 11 banks found that the median size of items paid into overdraft is $370 (see p. 18 of the analysis). Another analysis of data from 14 financial institutions found that the average size of items paid into overdraft was $198. One midsize ABA member bank reported that the average dollar amount of an item paid into overdraft where a fee was charged was $312 in 2023. These studies demonstrate that many consumers use overdraft strategically to ensure that important expenses – such as rent, utilities, and medical bills – are paid when the consumer experiences a shortfall in funds.

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***Myth*:** The CFPB's overdraft rule is necessary because overdraft services do not benefit consumers.

***Fact*:** Surveys consistently show that consumers appreciate and value their bank's overdraft program and are glad that their bank covered their overdraft payment, rather than returned or declined the payment. A survey conducted in October 2024 by Morning Consult found that 69% of consumers find their bank's overdraft protection valuable – as compared with only 13% who do not find it valuable. Eight in 10 consumers (80%) who have paid an overdraft fee in the past year were glad their bank covered their overdraft payment, rather than returning or declining payment, and 65% of consumers think it's reasonable for banks to charge a fee for an overdraft, as opposed to only 23% who think it's unreasonable. Seven in 10 consumers view overdraft fees as reasonable when considering that large payments like mortgages or rent payments are covered and paid on time (71%) or when considering that customers are protected from late or other penalty fees if payments overdraw a customer's account (69%).

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***Myth*:** The CFPB's overdraft rule will not limit consumer options for covering liquidity shortfalls.

***Fact*:** Available evidence indicates banks will reduce, if not eliminate, access to overdraft for the vast majority of their customers in response to the final rule. For example, a November 2024 survey of 21 banks found that a $3 or $7 price cap on overdraft fees would lead the surveyed banks to reduce overdraft liquidity by 76 to 100%. A March 2024 survey found that 67% of frequent users of overdraft report they had been denied a credit card in the past, indicating that overdraft users have few other options to cover emergency or unexpected expenses. Customers who lose access to overdraft because of the rule will be driven to payday and other nonbank lenders to meet their liquidity needs.

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***Myth*:** By capping overdraft fees at $5, the overdraft rule promotes financial inclusion.

***Fact*:** "[O]verdraft fee caps hinder financial inclusion," according to a 2021 Federal Reserve Bank of New York staff report. "When constrained by fee caps, banks reduce overdraft coverage and deposit supply, causing more returned checks and a decline in account ownership among low-income households." In addition, the rule – when coupled with other regulatory changes that may reduce fee income – will put pressure on banks to impose higher minimum balance requirements and to limit the availability of low-cost, full-service deposit accounts. Customers who lose access to their deposit account will be forced to turn to check cashers.

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***Myth*:** The rule applies only to large banks and will not affect community banks.

***Fact*:** The rule purports to apply only to banks and credit unions with more than $10 billion in assets, but if the rule takes effect, all depository institutions – and their customers – will be impacted. Large banks will be forced to lower their overdraft fee to the benchmark fee of $5 or to discontinue or restrict access to overdraft services. If a large bank reduces its overdraft fee to the $5 benchmark fee, the neighboring community bank will feel compelled to do the same or risk losing its customers to the large bank. Community banks have limited product lines and fewer sources of revenue to offset reduced overdraft fee income; therefore, the overdraft rule may lead to greater consolidation in the banking industry.