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Prepared remarks by Richard Cordray at the CFPB Roundtable on Overdraft Practices

By Richard Cordray

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Thank you to Hunter College for hosting this event. We are excited to be in this city, which plays such a central role in our nation's consumer financial system, as well as the broader global financial market. At the Consumer Bureau, our mission is to ensure that the consumer financial marketplace actually works for consumers. We also want to help educate consumers so they are able to make responsible, informed decisions.

Today, we are here to have a candid discussion on bank overdrafts. An overdraft occurs when a consumer spends or withdraws more money from their checking account than is available. Often this proves costly. The financial institution can choose to cover the overdraft by advancing funds on the consumer's behalf, and typically charges a large fee for doing so.

With the fast-moving pace of our modern economy, consumers may engage in numerous transactions and pile up multiple overdraft charges before realizing what has happened and how much damage has been done. They may do so by writing a check, paying a bill online, or using their debit card to make a purchase or withdraw funds from an ATM. Every penny counts, and consumers need to be able to understand how overdraft works and avoid costly penalty fees.

Overdrafts can provide consumers with needed access to funds, but the growing costs of overdraft practices have the capacity to inflict serious economic harm. We want to learn how consumers are affected and how well they are able to learn about the costs and risks of overdrafts. So today, we are announcing that the Consumer Bureau is launching an inquiry into overdraft practices and their impact on consumers.

There are similarities between overdrafts and payday loans, which we discussed at the Bureau's first field hearing last month in Alabama. Both products serve consumers who are strapped for cash and who feel they need short-term help. Both disproportionately affect a vulnerable demographic of consumers.

Evidence indicates that a small number of checking account customers – just under 10 percent – bear a whopping 84 percent of all overdraft fees. We know that these consumers are largely drawn from the ranks of the low-income. We also know that these charges greatly impact young consumers who are often inexperienced in the banking system. In fact, almost half of account holders who are young adults incur overdraft fees, according to an FDIC study published in 2008. And of those younger customers, 15 percent recorded more than ten overdrafts apiece in a single year.

We are concerned that overdraft practices employed by some banks unnecessarily increase consumer costs by making it difficult to anticipate and avoid fees. One of the practices that may contribute to consumer costs is transaction ordering. Some banks do not process transactions in chronological order. Instead, they collect the transactions from a specified period, such as a calendar day, and then process that set of transactions from the highest amount to the lowest amount. This approach can conceivably benefit consumers if it results in making certain that more significant payments – such as mortgage payments or student loan installments – get made. The down side is that this approach also tends to maximize the number of transactions that trigger overdraft fees.

Because of transaction ordering, along with the vagaries of funds availability and the settlement of various types of debits, consumers may not know when they have reached the limit of their available funds. Therefore, it is easy for them to overdraw their accounts inadvertently. We have heard many stories about the $40 cup of coffee: a man swipes a debit card at his local coffee shop, and unbeknownst to him, his balance is too low to cover the cost. Rather than the card being declined (with the result that he either pays in cash or goes uncaffeinated), the small transaction is processed – along with a $35 overdraft fee.

Many of the consumers we heard from did not realize this could happen – despite the opt-in requirement that is supposed to provide them with the means of protecting their own interests. Maybe they did not understand the potential consequences of this term in their checking account agreement. They may have been misled by marketing materials that suggested opting in to overdraft protection was necessary if they wanted to continue to use their debit card. Or maybe they saw one-sided advertising that emphasized the benefits of overdraft while burying information about the costs.

Overdraft provisions are often masked by the fine print of complex checking account agreements. The Bureau recently surveyed the websites of several larger banks to examine whether the information was presented in a manner that would be intuitively informative for their customers. While some banks did provide user-friendly information, many did not. One website required consumers to visit three separate pages and then scroll through fifty pages of dense text – just to obtain all of the pertinent information about account fees. This so-called “disclosure” is virtually the opposite of transparency.

We want to fix these problems, but first we need to learn more about how the overdraft product is working today. To begin, we are publishing a Request for Information (RFI) to seek broad public input on questions about actual consumer experiences and the consequences of different overdraft practices. The information we gather will shape our policy decisions and help us evaluate the impact on consumers and the financial industry.

We are also launching a study using data that a number of the largest banks will be providing to us. We want to understand the effects of prior federal regulations and guidance. We are committed to being a data-driven agency. We want to know the facts and figures about all of this, and more, in order to carry out our role of protecting consumers.

I would note that we have already seen some changes in overdraft policies by the banking industry. Some of these changes resulted from new regulatory requirements. Most significantly, the Federal Reserve adopted a rule two years ago, which prohibits overdraft charges on transactions with debit and ATM cards unless the consumer has affirmatively opted in by signing up for overdraft. Other changes came in response to litigation and still other changes were made voluntarily. Let me say a special thanks to the various consumer groups who have consistently advocated for these changes.

These voluntary changes include extending a cushion of $5 to $15 before a consumer is charged an overdraft fee or imposing a limit on the number of overdraft charges that a consumer can accrue in a single day. Some banks allow consumers to decide at an ATM whether to proceed with a transaction that overdraws their account. Other banks now allow a 24-hour grace period for the consumer to repay the overdraft without cost, or send account holders a text message alerting them when their balances have fallen below a certain level.

We applaud and encourage these innovative approaches to improving customer service. But we still have concerns about the risks posed to consumers from overdraft fees and that is why we are launching an inquiry.

This is not a brand-new subject in the consumer financial marketplace. Our inquiry will build on actions taken by other federal banking regulators, including the FDIC, OCC, OTS, and the Federal Reserve, and we will consult and collaborate with them as we undertake to address these issues.

As part of our mission to educate consumers, we are also seeking public feedback on a sample "penalty fee box" that could appear prominently on the checking account statements of consumers who overdraw their accounts. The penalty fee box is an example of a prominent disclosure that highlights how much the consumer overdrew and the amounts of any ensuing fees. And we are launching a "What's your overdraft status?" campaign to let consumers know what steps they can take to avoid overdraft penalty fees in the future.

While we study this market and seek to foster innovative overdraft disclosures, we will also use our supervisory and enforcement authorities to protect consumers. The Bureau plans to take action against financial institutions that exploit consumers with deceptive marketing about opting in to overdraft or other unlawful overdraft practices. It is wrong to confuse consumers deliberately for financial gain. We want to work with the industry to make it easier for consumers to understand the choices they are making, including the costs and risks of overdraft programs.

In order to accomplish these goals and better serve consumers, we need your input. We look forward to a frank and productive discussion, both today and in the future.

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