CONSUMER FINANCIAL PROTECTION BUREAU

12 CFR Parts 1005 and 1026

[Docket No. CFPB–2024–0002]

RIN 3170–AA42

Overdraft Lending: Very Large Financial Institutions

AGENCY: Consumer Financial Protection Bureau.

ACTION: Proposed rule; request for public comment.

SUMMARY: The Consumer Financial Protection Bureau (CFPB) proposes to amend Regulations E and Z to update regulatory exceptions for overdraft credit provided by very large financial institutions, thereby ensuring that extensions of overdraft credit adhere to consumer protections required of similarly situated products, unless the overdraft fee is a small amount that only recovers applicable costs and losses. The proposal would allow consumers to better comparison shop across credit products and provide substantive protections that apply to other consumer credit.

DATES: Comments must be received on or before April 1, 2024.

ADDRESSES: You may submit comments, identified by Docket No. CFPB–2024–0002 or RIN 3170–AA42, by any of the following methods:

- *Federal eRulemaking Portal: https://www.regulations.gov.* Follow the instructions for submitting comments. A brief summary of this document will be available at *https://www.regulations.gov/docket/CFPB-2024-0002.*
- *Email: 2024-NPRM-OVERDRAFT@cfpb.gov.* Include Docket No. CFPB–2024–0002 or RIN 3170–AA42 in the subject line of the message.
- *Mail/Hand Delivery/Courier:* Comment Intake—2024 NPRM Overdraft, c/o Legal Division Docket Manager, Consumer Financial Protection Bureau, 1700 G Street NW, Washington, DC 20552.

Instructions: The CFPB encourages the early submission of comments. All submissions should include the agency name and docket number or Regulatory Information Number (RIN) for this rulemaking. Commenters are encouraged to submit comments electronically. In general, all comments received will be posted without change to *https://www.regulations.gov.*

All submissions, including attachments and other supporting materials, will become part of the public record and subject to public disclosure. Proprietary information or sensitive personal information, such as account numbers or Social Security numbers, or names of other individuals, should not be included. Submissions will not be edited to remove any identifying or contact information.

FOR FURTHER INFORMATION CONTACT: Anna Boadwee, Attorney-Advisor; Joseph Baressi, Pedro De Oliveira, Thomas Dowell, Brandy Hood, Kristin McPartland, or Mark Morelli, Senior Counsels, Office of Regulations, at 202–435–7700 or *https://reginquiries.consumerfinance.gov/.* If you require this document in an alternative electronic format, please contact *CFPB_Accessibility@cfpb.gov.*

SUPPLEMENTARY INFORMATION:

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I. Summary of Proposed Rule

Overview

This proposed rule would update non-statutory exceptions in Regulations Z and E that have allowed very large financial institutions to avoid statutory requirements when extending certain overdraft credit.[1]

Consumer credit is subject to Regulation Z if the creditor imposes a finance charge, which generally includes any charge payable directly or indirectly by the consumer and imposed directly or indirectly by the creditor as an incident to or a condition of the extension of credit.[2] However, when the Board of Governors of the Federal Reserve System (Board) first adopted Regulation Z in 1969,[3] it excepted from Regulation Z's definition of finance charge any charges for honoring checks that overdraw a checking account unless the payment of the check and imposition of the fee were previously agreed upon in writing. The Board subsequently made ''minor editorial changes'' to this exception, *e.g.,* to reflect ''items that are similar to checks, such as negotiable orders of withdrawal.'' [4] This exception is unique to credit extended to pay account overdrafts. In adopting this exception, the Board did not rely on an interpretation of the statute; rather, the Board used its authority to create regulatory exceptions. Similar consumer credit products are subject to Regulation Z.

This exception was evidently intended to allow banks to continue providing limited overdraft services, as a courtesy to consumers who inadvertently overdrew their account, without the banks complying with Regulation Z. In the early years of the regulation, decisions to pay an item that

[1] When amending commentary, the Office of the Federal Register (OFR) requires reprinting of certain subsections being amended in their entirety rather than providing more targeted amendatory instructions. The sections of regulatory text and commentary included in this document show the language of those sections if the Bureau adopts its changes as proposed. In addition, the Bureau is releasing an unofficial, informal redline to assist industry and other stakeholders in reviewing the changes that it proposes to make to the regulatory text and commentary of Regulation E and Regulation Z. This redline may be found on the Bureau's website, *https://files.consumerfinance.gov/f/documents/cfpb_unofficial-redline_overdraft-credit-very-large-financial-institutions-proposed-rule_2024-01.pdf.* If any conflicts exist between the redline and the text of Regulation E or Regulation Z, its commentary, or this proposed rule, the documents published in the **Federal Register** are the controlling documents.

[2] Consumer credit is also subject to Regulation Z in other circumstances. *See, e.g.,* 12 CFR 1026.1(c).

[3] 34 FR 2002 (Feb. 11, 1969).

[4] 46 FR 20848, 20855 (Apr. 7, 1981).

overdraws an account instead of returning it unpaid were made as a relatively infrequent part of administering asset accounts. At the time, consumers typically withdrew funds from their bank accounts through in-person withdrawals or by writing checks. If a consumer mistimed when funds from a check deposit would be available for withdrawal [5] and inadvertently overdrew their account and the overdrawing check were returned unpaid, the bank would typically charge the consumer a nonsufficient funds (NSF) fee and the consumer could be subject to additional fees imposed by the payee and other negative consequences from bounced checks. If, instead of returning the check, the financial institution paid it notwithstanding the unavailable or insufficient funds in the account, such courtesy payment could provide a benefit to the consumer, who would avoid all of the negative consequences of a bounced check without being charged any additional fees beyond the amount charged for nonsufficient funds.

Over the last 30 years, in conjunction with widespread financial institution adoption of information technology systems as well as the expansion of debit card transactions that can overdraw an account, overdraft credit products provided under the exception have morphed from an occasional courtesy provided to consumers into frequently used and promoted products that increase costs to consumers (in certain instances) and generate a substantial portion of the direct fee revenue that financial institutions make from checking accounts (and much of the total revenue that financial institutions make from low-balance accounts). The volume of overdrawing transactions rose drastically over the years, including on transactions where the consumer may have suffered no negative consequences if the transaction were declined. Since the CFPB focused substantial enforcement and supervision attention on overdraft fees in 2021, overdraft fee revenue has contracted somewhat. However, it is still a source of billions of dollars in profits every year, and most very large financial institutions continue to charge $35 today. Financial institutions today generally make pay/no-pay decisions in advance—for example, by setting overdraft limits that the consumer may not be aware of and using information technology systems to make automated pay/no-pay decisions. They sometimes calibrate these systems with the goal of generating fee revenue. Because of these market changes, which increase the risk that a consumer will unwittingly incur high overdraft fees, helping consumers make informed decisions about overdraft credit has become a much more serious concern.

Key Changes

Given these changes over the past 30 years and consistent with TILA's purpose of promoting the informed use of credit, the CFPB is proposing to update several non-statutory exceptions in Regulation Z to extend consumer credit protections that generally apply to other forms of consumer credit to certain overdraft credit provided by very large financial institutions. These changes would allow consumers to better compare certain overdraft credit to other types of credit and would provide consumers with several substantive protections that already apply to other consumer credit.

These amendments would apply only to very large financial institutions—*i.e.,* insured depository institutions and credit unions with more than $10 billion in assets. The proposal would not change the regulatory framework for overdraft services offered by financial institutions with assets of $10 billion or less. The CFPB plans to monitor the market's response to this rule before determining whether to alter the regulatory framework for financial institutions with assets less than or equal to $10 billion.

Under this proposal, Regulation Z would generally apply to overdraft credit provided by very large institutions unless it is provided at or below costs and losses as a true courtesy to consumers. The proposed rule would accomplish this result by updating two regulatory exceptions from the statutory definition of finance charge. First, the proposal would update an exception that currently provides that a charge for overdraft is not a finance charge if the financial institution has not previously agreed in writing to pay items that overdraw an account [6] so that the exception would not apply to "above breakeven overdraft credit" offered by a very large financial institution. The proposal would give financial institutions the ability to determine whether an overdraft charge is considered above breakeven overdraft credit by either: (1) calculating its own costs and losses using standards set forth in the proposal; or (2) relying on a benchmark fee set by the CFPB in the proposal. The CFPB is considering setting the benchmark fee at $3, $6, $7, or $14. Second, the proposal would update a related exception that provides that a charge imposed in connection with an overdraft credit feature (*e.g.,* a charge for each item that results in an overdraft) is not a finance charge if the charge does not exceed the charge for a similar transaction account without a credit feature (*e.g.,* the charge for returning each item).[7] As a result of the proposed change, all transfer charges that very large financial institutions impose on asset accounts with linked overdraft lines of credit (*i.e.,* fees imposed for transferring funds to an asset account from an overdraft line of credit to cover an item that would otherwise take the asset account's balance negative) would be finance charges.

If the proposal is finalized, above breakeven overdraft credit that is not currently subject to Regulation Z would become subject to Regulation Z, including provisions in subpart B that govern open-end credit (*e.g.,* the account opening disclosures, periodic statements, and advertising rules). For ease of reference, this proposal generally refers to overdraft credit that is not subject to Regulation Z as non-covered overdraft credit and overdraft credit that is subject to Regulation Z as covered overdraft credit. Above breakeven overdraft credit is currently a type of non-covered overdraft credit, but it would become covered overdraft credit if this proposal is finalized.

The proposal would also require covered overdraft credit offered by very large financial institutions to be put in a credit account separate from the asset account, and it would update exceptions relating to credit cards. Among other changes, it would apply the portions of Regulation Z that implement the Credit Card Accountability Responsibility and Disclosure Act of 2009 (CARD Act) to covered overdraft credit that can be accessed by a hybrid debit-credit card, such as a debit card or other single credit device (including certain account numbers) that a consumer may use from time to time to obtain covered overdraft credit from a very large financial institution. Provisions of the CARD Act that would apply to such overdraft credit include, but are not limited to, ability-to-pay underwriting requirements, limitations on penalty fees including certain fees on

[5] In 1987, Congress enacted the Expedited Funds Availability Act (12 U.S.C. 4001 *et seq.*) to provide depositors of checks with prompt funds availability and to foster improvements in the check collection and return processes. *See* 82 FR 27552, 27552 (June 15, 2017). Section 229.2(d) of Regulation CC (12 CFR 229), which implements that act, defines "available for withdrawal."

[6] 12 CFR 1026.4(c)(3).

[7] 12 CFR 1026.4(b)(2).

transactions that are declined due to nonsufficient funds, and various requirements related to rate changes.

The proposal would also prohibit compulsory use of preauthorized electronic fund transfers (EFTs) for repayment of covered overdraft credit provided by very large financial institutions, which would ensure that consumers using those products have a choice of at least one alternative method of repayment. As a result of this change, covered overdraft credit offered by very large financial institutions could not be conditioned on consumers agreeing to automatic debits from their checking account. Consumers could still opt into automatic payments on a periodic basis if offered by their financial institution, but they would have the right to repay this overdraft credit manually if they prefer.

The CFPB proposes that the final rule, if adopted, would take effect on the October 1 which follows by at least six months the date it is published in the **Federal Register**, consistent with 15 U.S.C. 1604(d). The CFPB expects that would likely fall on October 1, 2025.

The CFPB invites comment on all aspects of this notice of proposed rulemaking and on the specific issues on which it solicits comment elsewhere herein, including on any appropriate modifications or exceptions to the Proposed Rule.

II. Background

A. Overview of Overdraft Credit

An overdraft occurs when consumers do not have a sufficient balance in their asset account to pay a transaction, but the financial institution pays the transaction anyway. Typically, the financial institution pays an overdraft transaction by either transferring the consumer's own funds from another asset account held by the financial institution, such as a savings account, or by extending overdraft credit (*i.e.,* using the financial institution's own funds and requiring the consumer to repay).

Currently, not all overdraft credit is subject to Regulation Z. For example, when the Board first adopted Regulation Z in 1969,[8] it excepted from Regulation Z's coverage charges for honoring checks that overdraw a checking account unless the payment of the check and imposition of the fee were previously agreed upon in writing. A Board official interpretation stated that this exception for ad hoc credit decisions applies only to ''regular demand deposit accounts which carry no credit features and in which a bank may occasionally, as an accommodation to its customer, honor a check which inadvertently overdraws that account.'' [9] The Board subsequently adopted commentary excluding debit cards with no credit agreement from Regulation Z's definition of ''credit card.'' [10] While the Board did not explain this exception, it appears it was intended to exclude discretionary overdraft services from being subject to Regulation Z when they are accessed by a debit card, consistent with the exclusion for overdraft charges from the definition of finance charge.[11]

Some overdraft credit is previously agreed upon in writing and is currently covered by Regulation Z. Such covered overdraft credit enables consumers to link a checking account to a credit account, like an overdraft line of credit or a credit card, from which funds are transferred automatically to pay transactions when the checking account balance is insufficient to pay them. Some financial institutions charge a fee, often referred to as an overdraft protection transfer fee, for these transfers.[12] Financial institutions may assess such a fee once per day that a transfer is made, once to transfer a round dollar value increment (*e.g.,* a fee for $100 transferred to cover any overdraft(s) less than $100), or, less commonly, once per overdraft transaction; [13] however, since late 2021, a number of financial institutions have voluntarily eliminated such fees.[14] Credit accounts used to cover overdrafts also carry an interest rate applied to the outstanding balance. Repayment of the overdrawn amount and interest is typically made periodically according to a payment schedule. The ability to obtain and use covered overdraft credit is typically limited to consumers whose credit history allows them to qualify for an overdraft line of credit or who have available credit on a credit card.

Financial institutions may also pay overdrafts through currently non-covered overdraft credit, where the financial institution typically pays overdrafts up to certain limits but does not agree in advance to pay the overdrawn transactions, reserving discretion to decline any given overdraft transaction. This type of overdraft credit is currently non-covered overdraft credit because it is currently not subject to Regulation Z. This proposal may also refer to currently non-covered overdraft credit as an overdraft service, overdraft services, or an overdraft program. With certain exceptions provided for by internal policies, the financial institution typically assesses a flat fee for each overdraft transaction the financial institution pays. In addition, some financial institutions charge an additional fee or fees, known as extended or sustained overdraft fees, if the consumer does not bring the account back to a positive balance within a specified period. To collect repayment of the funds advanced to cover overdraft transactions as well as payment of the fees assessed, the financial institution typically deducts those amounts as a lump sum from the consumer's next incoming deposit(s), usually within three days after the account became overdrawn.[15]

Financial institutions typically provide non-covered overdraft credit for certain transaction types—primarily checks, automated clearinghouse (ACH) transactions, and recurring debit card transactions—as a default, up to certain coverage limits. For one-time (non-recurring) debit card and ATM transactions, financial institutions may not assess overdraft fees for paying such transactions without first obtaining the consumer's opt-in following the process required by Regulation E 12 CFR 1005.17(b).

Financial institutions employ a number of different practices and policies when making pay/return decisions in connection with non-covered overdraft.[16] While, as noted above, overdraft credit must technically be discretionary to be excepted from Regulation Z, in practice, financial

[8] 34 FR 2002 (Feb. 11, 1969).

[9] 42 FR 22360, 22362 (May 3, 1977).

[10] 46 FR 50288, 50293 (Oct. 9, 1981) (providing that a ''credit card'' does not include ''[a] check-guarantee or debit card with no credit feature or agreement, even if the creditor occasionally honors an inadvertent overdraft''); *see also* Regulation Z comment 2(a)(15)–2.ii.A.

[11] Under Regulation Z, an issuer of a credit card can be a creditor regardless of whether the credit is subject to a finance charge. 12 CFR 1026.2(a)(17)(iii); *see also* 12 CFR 1026.2(a)(7) (defining ''card issuer''). Thus, without the 1981 exception, a financial institution that extends overdrafts could be a ''creditor'' for purposes of subpart B of TILA even with an exemption of overdraft fees from the finance charge.

[12] Consumer Fin. Prot. Bureau (CFPB), *CFPB Study of Overdraft Programs: A white paper of initial data findings,* at 55 (June 2013), *https://files.consumerfinance.gov/f/201306_cfpb_whitepaper_overdraft-practices.pdf* (CFPB 2013 White Paper) (noting 28 of a sample of 33 large institutions charged a transfer fee in 2012, ranging from $3 to $20 per transfer, with a median of $10, while smaller institutions charged a median of $5).

[13] *Id.*

[14] Between December 2022 and July 2023, CFPB reviewed publicly available information describing the overdraft-related practices of very large financial institutions (CFPB Market Monitoring of Publicly Available Overdraft Practices, Dec. 2022–July 2023).

[15] Trevor Bakker et al., CFPB, *Data Point: Checking account overdraft,* at 5, 22 (July 2014), *https://files.consumerfinance.gov/f/201407_cfpb_report_data-point_overdrafts.pdf* (CFPB 2014 Data Point).

[16] CFPB 2013 White Paper at 48–52.

institutions typically assign each account an overdraft coverage limit representing the maximum amount of overdraft coverage the financial institution will extend on the account. Once an account reaches its overdraft coverage limit, the financial institution will no longer pay transactions into overdraft and will return those transactions unpaid. Overdraft coverage limits may be static (*i.e.,* the financial institution assigns an unchanging limit to each customer) or dynamic (*i.e.,* the financial institution changes the limit for each account periodically based on account usage patterns, market conditions, or account and accountholder characteristics in an attempt to manage more precisely credit risk, overdraft program revenues, and customer retention).[17] Financial institutions that use static limits may communicate those limits to account holders, while financial institutions that use dynamic limits generally do not communicate those limits to account holders.

Historically, financial institutions have charged an NSF fee when they reject, rather than pay, transactions initiated by check or ACH or other electronic payments; in contrast, financial institutions have rarely if ever charged an NSF fee when declining a one-time debit card purchase or an ATM withdrawal. Financial institutions typically have charged the same amount for an NSF fee as for a non-covered overdraft fee.[18] As noted in part II.C, many financial institutions have eliminated NSF fees over the past two years.

B. Evolution and Growth of Non-Covered Overdraft

Non-covered overdraft credit started as a courtesy that financial institutions provided when they would decide on a manual, ad hoc basis to pay particular check transactions into overdraft rather than returning those checks unpaid.[19] This courtesy would help consumers avoid NSF fees, merchant fees, and other negative consequences from bounced checks. Over time, non-covered overdraft credit began to move away from that historical model, as financial institutions shifted to a system involving heavy reliance on automated programs to process transactions and to make overdraft decisions.[20] Financial institutions also began to extend overdraft credit to debit card transactions, even though a declined debit card transaction did not pose the same risk to consumers of an NSF fee, a merchant fee, or certain other consequences associated with a bounced check.[21] Over time, debit card transactions became more numerous than checks, increasing the number of transactions that could generate overdrafts, with typical debit card transactions involving smaller amounts than typical check transactions.[22] Even as transaction processing and overdraft decisioning became more automated and overdraft transactions increased in frequency and decreased in size, financial institutions increased the size of overdraft fees. In 1976, when the process was typically manual and included only checks, one survey of banks in Washington, DC, and New York found that the median fee was $5, while some banks charged zero.[23] By 1994, concern had risen about the increase in the average fee to over $15 ($5.77 in 1976 dollars);[24] by 2000, the average had surpassed $20 ($6.61 in 1976 dollars) and continued to increase thereafter.[25]

As a result of these market shifts and operational changes, fee revenue from non-covered overdraft credit began to significantly influence the overall business model for many asset accounts. Financial institutions became less likely to charge consumers upfront monthly checking account fees, which consumers could more easily compare across the market, and instead began to rely heavily overdraft fees.[26] In essence, the provision of non-covered overdraft credit moved away from its original purpose—paying occasional or inadvertent overdrafts as a courtesy—and became the dominant component of

[17] Common account and account holder characteristics include account tenure, average balance, overdraft history, and deposit patterns, as well as other relationships the accountholder may have with the institution.

[18] *See Consumers Guide to Banking: Staff Report on Commercial Bank Charges in the New York and Washington, DC Metropolitan Area,* S. Comm. on Banking, Hous. and Urban Affairs, 94th Cong. 10–11 tbl.3 (1976) (Senate Staff Report); *see also* 70 FR 8428, 8429 (Feb. 18, 2005) (''Regardless of whether the overdraft is paid, institutions typically charge the NSF fee when an overdraft occurs.''); 74 FR 59033, 59035 (Nov. 17, 2009) (''Second, a consumer will generally be charged the same fee by the financial institution whether or not a check is paid; yet if the institution covers an overdrawn check, the consumer may avoid other adverse consequences, such as the imposition of additional merchant fees); Fed. Deposit Ins. Corp. (FDIC), *2008 FDIC Study of Bank Overdraft Programs,* at 16 n.18 (Nov. 2008), *https://www.fdic.gov/bank/analytical/overdraft/FDIC138_Report_Final_v508.pdf* (FDIC 2008 Study) (''For most of the survey population operating automated programs, the per-item fee charged when items were paid under automated overdraft programs was the same as the fee charged by the bank on NSF items that it did not pay. These two fees were equal to each other for 98.1 percent of 451 institutions reporting the two fee items.'').

[19] *See* 42 FR 22360, 22362 (May 3, 1977) (describing the exception from Regulation Z as applying when overdraft is provided ''as an accommodation . . . honoring a check which inadvertently overdraws that account.''); *see also Federal Reserve Board Staff Opinion Letter No. 948* (Nov. 17, 1975) (explaining that the exception ''relates only to regular demand deposit accounts which carry no credit feature and in which a bank may occasionally, as an accommodation to its customer, honor a check which inadvertently overdraws that account'').

[20] *See* 74 FR 59033, 59033 n.1 (Nov. 17, 2009) (citing *FDIC's Study of Bank Overdraft Programs* (Nov. 2008), which found that nearly 70 percent of banks surveyed implemented their automated overdraft program after 2001).

[21] *See id.* at 59035; *see also id.* at 59034 n.6 (citing *Overdraft Protection: Fair Practices for Consumers: Hearing before the House Subcomm. On Financial Institutions and Consumer Credit, House Comm. On Financial Services,* 110th Cong., at 72 (2007)) (''noting that as recently as 2004, 80 percent of banks still declined ATM and debit card transactions without charging a fee when account holders did not have sufficient funds in their account.'').

[22] Federal Reserve Payments Studies from 2004 to 2013 (exhibit 1 in each study) show that from 2000 to 2012, annual debit card transactions increased from 8.3 billion to 47 billion, while annual check transactions decreased from 41.9 billion to billion to 18.3 billion. By 2008, debit card transactions exceeded the number of checks. *See* Bd. of Governors of the Fed. Rsrv. Sys. (FRS), *Federal Reserve Payments Study (FRPS)—Previous Studies, https://www.federalreserve.gov/paymentsystems/frps_previous.htm* (last updated Apr. 21, 2023); *see also* FRS, *The 2013 Federal Reserve Payments Study,* at 9 ex.2 (Dec. 2013), *https://www.frbservices.org/binaries/content/assets/crsocms/news/research/2013-fed-res-paymt-study-summary-rpt.pdf* (showing the average debit card transaction ranged from $37 to $40 from 2003–2012, while the average check transaction ranged from $1,103 to $1,410). The CFPB has found that the median transaction amount that leads to an overdraft fee in the case of debit card transactions is $24, while the median check and ACH transactions that lead to overdraft fees are $100 and $90, respectively. *See* CFPB 2014 Data Point at 5; *see also* Fin. Health Network (FHN), *Overdraft Trends Amid Historic Policy Shifts* (June 1, 2023), *https://finhealthnetwork.org/research/overdraft-trends-amid-historic-policy-shifts/* (FHN Brief 2023) (finding almost half (45 percent) of overdrafters reported that their most recent overdraft occurred on a transaction of $50 or less).

[23] Senate Staff Report at 10–11.

[24] *See Bank Fees Associated with Maintaining Depository, Checking, and Credit Card Accounts,* Hearing Before the Subcomm. on Consumer Credit and Ins., Comm. on Banking, Finance and Urban Affairs, 103rd Cong. 73 tbl.3 (1993) (Testimony by Susan M. Phillips, Member, Bd. of Governors of the Fed. Rsrv. Sys.) (showing average overdraft fee of over $15 in 1993); *see also id.* at 95–96, 101–02 (Statement of Chris Lewis, Dir. of Banking and Hous. Pol'y, Consumer Fed'n of Am.) (noting concerns about the rise in the size of ''bounced check fees'', a term the organization used to describe the fee assessed when funds were insufficient, whether the transaction was returned unpaid or paid into overdraft).

[25] Gov't Accountability Off., *Bank Fees: Federal Banking Regulators Could Better Ensure That Consumers Have Required Disclosure Documents Prior to Opening Checking or Savings Accounts,* at 14 (Jan. 2008), *https://www.gao.gov/assets/gao-08-281.pdf; see also* FDIC 2008 Study (by 2007, among primarily financial institutions with less than $5 billion in assets, the average fee was $27); CFPB 2013 White Paper at 52 (by 2012, among the nation's largest financial institutions, the average fee was $34).

[26] CFPB 2013 White Paper at 16–17.

a back-end pricing business model. By 2004, marketwide overdraft revenue was estimated at approximately $10 billion and, by 2009, had increased to an estimated $25 billion.[27]

C. Non-Covered Overdraft Credit Today

Marketwide overdraft revenue declined following the 2010 implementation of the Board's ''opt-in'' rule under Regulation E to an estimated $12 billion in 2011 before beginning to increase again.[28] In the several years preceding the COVID–19 pandemic, marketwide overdraft revenue was persistent, climbing from an estimated $11.8 billion in 2015 to $12.6 billion in 2019.[29] With the onset of the pandemic in March 2020, overdraft revenue dropped significantly. The drop was likely primarily due to pandemic-related stimulus payments pushing up average checking account balances, as well as temporarily decreased use of debit cards.[30] In addition, Federal regulators encouraged, and some State regulators encouraged or mandated, financial institutions to offer leniency around imposition of overdraft fees in light of the pandemic.[31] Notwithstanding the trend downward during the pandemic, estimated marketwide overdraft revenue exceeded $9 billion in 2020 and 2021.[32]

Beginning in late 2021, a number of large banks began announcing and implementing changes to their overdraft policies.[33] Some banks eliminated overdraft fees altogether or reduced them to $10 or $15 per transaction.[34] Some banks made changes to their policies by expanding their fee waiver policies, including establishing a daily limit of one fee per day; [35] establishing de minimis negative balance thresholds, within which overdrafts do not result in a fee of $50 or more; and implementing grace periods giving consumers time through the next business day to bring their accounts positive before a fee is assessed.[36] Collectively these changes resulted in a sustained reduction in overdraft revenues as compared to pre-pandemic levels.[37] Marketwide overdraft revenue in 2022 was an estimated $9.1 billion ($7.9 billion in 2019 dollars, a 37 percent drop in real terms).[38] Of that, an estimated $6.16 billion, or 68 percent, was earned by financial institutions with above $10 billion in assets.[39] At the same time, most very large financial institutions eliminated NSF fees.[40]

Despite these changes, the vast majority of banks and credit unions with over $10 billion in assets continue to charge between $30 and $37 per overdraft fee, and more than half charge $35.[41] Most financial institutions' policies allow consumers to incur multiple overdraft fees per day. Financial institutions continue charging these high fees even though the fees far exceed institutions' costs and losses associated with providing non-covered overdraft credit. CFPB data collections and outreach have found that the single largest cost or loss to financial institutions associated with overdraft programs is charged-off account balances, which most frequently occur when a consumer's subsequent deposits do not cover the negative balance created by the overdraft(s) and associated fee(s).[42] The CFPB's study of 2011 bank data found that charge-offs were small relative to the fee revenue banks earned through their overdraft programs.[43] Among those banks, charged-off principal account balances due to overdraft programs represented 14.4 percent of the net overdraft fees (not including NSF fees) at those banks.[44] During the first half of 2023, the CFPB collected additional data from several banks, which again showed that charge-offs associated with negative account balances were the largest cost or loss associated with providing overdraft. As discussed further in part V.C.2, charge-offs amounted to an average of $2 per overdraft transaction whether or not such transaction incurred an overdraft fee, and an average of $5 per overdraft transaction that incurred an overdraft fee—representing 6 percent and 15 percent, respectively, of the average fee of $32.50 charged by the banks during the period studied.

[27] CFPB's estimates of marketwide overdraft revenue, before banks with over $1 billion in assets began reporting overdraft/NSF revenue on call reports in 2015, are based on the esitmated share of aggregated fee revenue that banks and credit unions reported on call reports that was attributable to overdraft fees. For more details on methodology, *see* Jacqueline Duby et al., Ctr. for Responsible Lending (CRL), *High Cost & Hidden From View: The $10 Billion Overdraft Loan Market* (May 26, 2005), *https://www.responsiblelending.org/sites/default/files/nodes/files/research-publication/ip009-High_Cost_Overdraft-0505.pdf; see also* Leslie Parrish, CRL, *Overdraft Explosion: Bank fees for overdrafts increase 35% in two years,* at 4 (Oct. 6, 2009), *https://www.responsiblelending.org/research-publication/overdraft-explosion-bank-fees-overdrafts-increase-35-two-years.*

[28] *Id.*

[29] CFPB's estimates of marketwide overdraft revenue for 2015 to 2022 extrapolate total overdraft/NSF revenue reported on call reports by banks with over $1 billion in assets to banks with less than $1 billion in assets and to credit unions in order to reach a total marketwide estimate of overdraft/NSF revenue, and then estimate the portion of that combined overdraft/NSF revenue that is attributable to overdraft revenue alone. To extrapolate reported overdraft/NSF revenue to banks with less than $1 billion in assets and to credit unions, the CFPB uses data collected from core processors for the number of accounts by asset size and the overdraft/NSF revenue per account, and from 2014 call report data for distribution of institutions by asset size, and then assumes that overdraft/NSF revenue at small institutions saw the same growth from 2014 to 2019 as at large banks to arrive at the 2019 estimate. These extrapolations result in estimates where banks with over $1 billion in assets comprise 77.4 percent of marketwide overdraft/NSF revenue, banks with less than $1 billion in assets comprise 7.3 percent of such revenue, and credit unions comprise 15.3 percent of such revenue. *See* Éva Nagypál, Ph.D., CFPB, *Data Point: Overdraft/NSF Fee Reliance Since 2015—Evidence from Bank Call Reports,* at 7 (Dec. 2021), *https://files.consumerfinance.gov/f/documents/cfpb_overdraft-call_report_2021-12.pdf* (CFPB 2021 Data Point). For the 2022 estimate, the CFPB assumes that banks with assets over $1 billion, banks with assets below $1 billion, and all credit unions represent the same relative portions of total marketwide overdraft/NSF revenue in 2022 as they did in 2019.

[30] CFPB 2021 Data Point at 22–24.

[31] *See* Press Release, FRS, FDIC & Off. of the Comptroller of the Currency (OCC), *Joint Statement on CRA Consideration for Activities in Response to COVID–19* (Mar. 19, 2020), *https://www.occ.gov/news-issuances/bulletins/2020/bulletin-2020-19a.pdf;* Press Release, CFPB, *Consumer Financial Protection Bureau Encourages Financial Institutions and Debt Collectors to Allow Stimulus Payments to Reach Consumers* (Mar. 17, 2021), *https://www.consumerfinance.gov/about-us/newsroom/consumer-financial-protection-bureau-encourages-financial-institutions-and-debt-collectors-to-allow-stimulus-payments-to-reach-consumers/; see also, e.g.,* State of Cal. Bus., Consumer Servs. & Hous. Agency, *Guidance to Financial Institutions During the COVID–19 Pandemic* (Mar. 22, 2020), *https://www.bcsh.ca.gov/coronavirus19/dbo_banks.pdf;* Press Release, N.Y. State Dep't of Fin. Servs., *DFS Issues New Emergency Regulation Requiring New York Regulated Financial Institutions To Provide Financial Relief To New Yorkers Demonstrating Financial Hardship From COVID–19 Pandemic* (Mar. 24, 2020), *https://www.dfs.ny.gov/reports_and_publications/press_releases/pr202003241.*

[32] *See* discussion of methodology at FN 29.

[33] Rebecca Borné & Amy Zirkle, *Comparing overdraft fees and policies across banks,* CFPB (Feb. 10, 2022), *https://www.consumerfinance.gov/about-us/blog/comparing-overdraft-fees-and-policies-across-banks/.*

[34] *Id.*

[35] *Id.*

[36] *Id.*

[37] CFPB, *Data Spotlight: Overdraft/NSF revenue down nearly 50% versus pre-pandemic levels* (May 24, 2023), *https://www.consumerfinance.gov/data-research/research-reports/data-spotlight-overdraft-nsf-revenue-in-q4-2022-down-nearly-50-versus-pre-pandemic-levels/full-report/* (CFPB May 2023 Data Spotlight).

[38] *See* discussion of methodology at FN 29.

[39] Estimated using data from 2022 Federal Financial Institutions Examination Council (FFIEC) Call Reports and methodology discussed at FN 29.

[40] CFPB, *Data spotlight: Vast majority of NSF fees have been eliminated, saving consumers nearly $2 billion annually* (Oct. 11, 2023), *https://www.consumerfinance.gov/data-research/research-reports/vast-majority-of-nsf-fees-have-been-eliminated-saving-consumers-nearly-2-billion-annually/* (CFPB October 2023 Data Spotlight) (finding that nearly two-thirds of banks with over $10 billion in assets have eliminated NSF fees).

[41] CFPB Market Monitoring of Publicly Available Overdraft Practices, Dec. 2022–July 2023.

[42] CFPB 2013 White Paper at 17.

[43] *Id.*

[44] *Id.*

D. Consumer Impact of Overdraft Fees

As cumulative overdraft fee revenue for financial institutions increased, so did the cumulative burden of overdraft fees on consumers. CFPB research found that 79 percent of combined overdraft and NSF fees were paid by 9 percent of consumers who paid more than 10 such fees per year, incurring a median of $380 in these fees in a year.[45] Consumers paying more than 20 such fees in a year accounted for about 5 percent of accounts, while paying over 63 percent of the fees.[46]

High overdraft fees can make it more difficult for consumers to return their account to a positive balance, contributing to account charge-offs, involuntary account closures, and consumers blocked out of the banking system. The CFPB found that the banks with the highest share of accounts with frequent overdrafts tended to have the highest rates of involuntary account closure; conversely, those with the lowest share of accounts with frequent overdrafts tended to have the lowest rates of involuntary closure.[47] Account closures, in turn, are often reported to account screening consumer reporting agencies, and a negative report from an account screening company may limit a consumer's ability to open an account at a bank or credit union in the future. Negative experiences with overdraft fees likely also discourage many consumers from wanting a bank account at all. The FDIC estimates that there were nearly 6 million unbanked households in the U.S. in 2021,[48] nearly half of which had a bank account in the past.[49] Of those previously banked households, more than two-thirds have little or no interest in having a bank account again,[50] with high fees, unpredictable fees, and not enough funds to meet minimum balance requirements among the most cited reasons.[51]

Consumers can face significant uncertainty about whether they will incur overdraft fees. Though financial institutions may provide disclosures related to their transaction processing, deposit availability, and overdraft assessment policies, these policies can be extraordinarily complex.[52] Even consumers who closely monitor their account balances may not know with certainty when transactions will post to their accounts, whether a particular transaction will be paid or returned unpaid, and whether a particular paid transaction will be deemed an overdraft and assessed an overdraft fee.[53]

In response to the CFPB's 2022 request for information regarding fees that are not subject to competitive processes that ensure fair pricing, which received over 80,000 responses,[54] overdraft-related fees were by far the most common issue raised. Common concerns included that the fees were unclear or confusing, disproportionate compared to the incidents resulting in the fees, and difficult or impossible to avoid. These concerns were generally consistent with those reflected in complaints about overdraft fees consumers have submitted to the CFPB's Consumer Complaints Database since its inception in 2011.

The CFPB has also studied how consumers who are opted-in to overdraft services on one-time debit card and ATM transactions—and thus subject to overdraft fees on those transactions—fare compared to those who are not opted-in. In total, opted-in accounts incurred more than seven times as many overdraft fees as accounts that were not opted-in.[55] At the account level, opted-in accounts were three times as likely to have more than 10 overdrafts per year as accounts that were not opted-in.[56] And among frequent overdrafters, those who were opted-in appeared similar across a number of dimensions to frequent overdrafters who were not opted-in, but incurred significantly more—at the median, 13 more—overdraft/NSF fees per year.[57] In addition, involuntary account closure was about 2.5 times as likely for consumers who had opted-in than for consumers who had not.[58]

Consumers whose accounts are frequently overdrawn are typically more financially insecure than those who do not overdraw or who do so infrequently.[59] Compared to non- or infrequent overdrafters, frequent overdrafters tend to have lower incomes and lower end-of-day balances.[60] They are also less likely to have access to alternative credit options: they have lower credit scores, are less likely to have a general purpose credit card, and, if they do have such a card, they have less credit available on it.[61] Black households and Latino households are more likely to incur overdraft fees than white households.[62]

E. Growing Regulatory Concerns About Non-Covered Overdraft Credit

As financial institutions began to evolve provision of non-covered overdraft away from the historical

[45] David Low et al., CFPB, *Data Point: Frequent Overdrafters,* at 5 (Aug. 2017), *https://files.consumerfinance.gov/f/documents/201708_cfpb_data-point_frequent-overdrafters.pdf* (CFPB 2017 Data Point); CFPB 2014 Data Point at 12 (both analyzing 2011–2012 data).

[46] CFPB 2017 Data Point at 5.

[47] CFPB 2013 White Paper at 25.

[48] FDIC, *2021 FDIC National Survey of Unbanked and Underbanked Households,* at 1, *https://www.fdic.gov/analysis/household-survey/2021report.pdf* (last updated July 24, 2023).

[49] *Id.* at 17 tbl.3.3 (48.8 percent of unbanked households previously had a bank account).

[50] *Id.* at 18 fig.3.4 (49.4 percent of previously banked households are not at all interested in having a bank account, and 18.3 percent are not very interested).

[51] FDIC, *2021 FDIC National Survey of Unbanked and Underbanked Households—Appendix Tables,* at 11 tbl.A.6, *https://www.fdic.gov/analysis/household-survey/2021appendix.pdf* (last updated July 24, 2023) (FDIC Tables) (among previously banked households, 30.5 percent cited bank account fees are too high, 28.8 percent cited bank account fees are too unpredictable, and 43 percent cited that they do not have enough money to meet minimum balance requirements).

[52] *See* Press Release, CFPB, *CFPB Orders Regions Bank to Pay $191 Million for Illegal Surprise Overdraft Fees* (Sept. 28, 2022), *https://www.consumerfinance.gov/about-us/newsroom/cfpb-orders-regions-bank-pay-191-million-for-illegal-surprise-overdraft-fees/.*

[53] *Id.; see also* 87 FR 66935, 66935–40 (Nov. 7, 2022).

[54] 87 FR 5801 (Feb. 2, 2022).

[55] CFPB 2014 Data Point at 21.

[56] *Id.* at 13.

[57] CFPB 2017 Data Point at 6, 32–33. This dynamic was likely driven primarily by the scenario where a debit card or ATM transaction is authorized against a sufficient balance but then settles against an insufficient balance. A consumer who was not opted-in would have had this transaction approved and assessed no fee. A consumer who was opted-in may have been charged a fee. For discussion of regulatory guidance and CFPB enforcement actions addressing overdraft fees assessed on these ''authorize positive, settle negative'' transactions, *see* part II.E.

[58] CFPB, *A Closer Look: Overdraft and the Impact of Opting-In* (Jan. 19, 2017), *https://files.consumerfinance.gov/f/documents/201701_cfpb_Overdraft-and-Impact-of-Opting-In.pdf* (citing a rate of 6.2 percent in a given year for non-opted-in consumers and 2.5 percent for opted-in consumers, based on calculations using the same large bank data used in CFPB 2014 Data Point).

[59] CFPB has previously used ''frequent overdrafters'' to describe those who incur more than 10 overdraft/NSF fees in one year and ''very frequent overdrafters'' to describe those who incur more than 20 overdraft/NSF fees in one year. *See* CFPB 2017 Data Point at 4–5.

[60] CFPB 2017 Data Point at 15–16 (finding that as neighborhood income decreases, overdraft frequency increases); *id.* at 6 (finding that nearly 70 percent of frequent overdrafters had end-of-day balances with medians between $237 and $439, while another 20 percent had median end-of-day balances of $140). *See also* FHN Brief 2023 (finding that households with incomes under $30,000 were twice as likely to report at least one overdraft than those with incomes of $100,000 or more).

[61] CFPB 2017 Data Point at 15–16.

[62] FHN Brief 2023 (finding that 26 percent of Black, 23 percent of Latinx, and 14 percent of White households reported having overdrafted, making Black and Latinx households 1.9 and 1.6 times as likely as White households, respectively, to have overdrafted); *see also* Meghan Greene et al., FHN, *FinHealth Spend Report 2022: What U.S. Households Spent on Financial Services During COVID–19,* at 14 (Apr. 2022), *https://finhealthnetwork.org/wp-content/uploads/2022/05/FinHealth_Spend_Report_2022_Final.pdf* (finding in a 2021 survey that Black and Latinx households with a savings or checking account were 1.8 and 1.4 times as likely as White households to report having overdrafted).

model and toward increased automation, greater frequency, and higher revenues, Federal regulators expressed increasing consumer protection concerns. In 2001, in declining to issue a requested ''comfort letter'' for a financial institution's overdraft program, the OCC stated that overdraft services are extensions of credit and that the associated charges may be ''just as burdensome as those imposed on borrowers utilizing other types of high interest rate credit.'' [63] In 2002, the Board noted that some non-covered overdraft credit may not be all that different from overdraft lines of credit,[64] and in 2004 the Board stated that further consideration of the need for Regulation Z coverage of overdraft services would be appropriate if consumer protection concerns were to persist.[65] In 2005, the Federal banking agencies issued joint guidance on non-covered overdraft credit noting that ''the existing regulatory exceptions [*i.e.,* exceptions in Regulation Z such that it does not apply] were created for the occasional payment of overdrafts, and as such could be reevaluated by the Board in the future, if necessary. Were the Board to address these issues more specifically, it would do so separately under its clear [TILA] authority.'' [66] In 2009, the Board adopted a rule under Regulation E prohibiting institutions from assessing overdraft fees on one-time debit card and ATM transactions unless the institution obtained the consumer's affirmative consent to such fees (''opt-in rule'').[67] Following the adoption of the Board's rule, the FDIC issued additional supervisory guidance,[68] which advises, among other things, that where transactions overdraw an account by a de minimis amount, the overdraft fee should be eliminated or be reasonable and proportional to the amount of the transaction.[69]

More recently, in October 2022, the CFPB issued a policy statement stating that the assessment of overdraft fees that consumers would not reasonably anticipate, including overdraft fees on debit card or ATM transactions that are authorized when the consumer's available balance is sufficient to cover the transaction but that later settle against a negative balance due to intervening transactions or complex processes (''authorize positive, settle negative'' or ''APSN'' transactions), likely violates the Consumer Financial Protection Act of 2010 (CFPA)'s statutory prohibition against unfair practices.[70] In April 2023, the OCC and FDIC issued guidance advising that overdraft fees charged on such transactions raise heightened risk of unfair, deceptive, or abusive acts or practices.[71] The OCC's guidance also describes certain practices that it notes may help to manage risks associated with overdraft programs, including assisting consumers in avoiding ''unduly high costs'' in relation to the face value of the item being presented, the amount of their regular deposits, and their average account balances, and implementing fees and practices that bear a reasonable relationship to the risks and costs of providing overdraft programs.[72]

The CFPB has previously established rules governing overdraft credit on prepaid accounts. In 2016, the CFPB amended Regulation Z to provide that prepaid accounts that offer credit features are generally covered under Regulation Z's credit card rules.[73] The CFPB also amended the compulsory-use provision under Regulation E to prohibit prepaid card issuers from requiring consumers to set up preauthorized EFTs to repay credit extended through an overdraft credit feature accessible by a hybrid prepaid-credit card.[74]

In applying Regulation Z to overdraft credit features on prepaid accounts, the CFPB noted that the term ''credit'' in TILA includes ''the right to . . . incur debt and defer its payment'' [75] and explained that that definition ''covers the situation when a consumer makes a transaction that exceeds the funds in the consumer's account and a person elects to cover the transaction by advancing funds to the consumer.'' [76] The CFPB further stated that overdraft fees on prepaid accounts ''generally constitute finance charges, because they are directly payable by the consumer and imposed directly by the creditor as a condition of the extension of credit.'' [77] The CFPB also stated that overdraft services offered in connection with prepaid accounts ''can be regulated by Regulation Z as a 'plan' when the consumer is contractually obligated to repay the debt, even if the creditor retains, by contract, the discretion not to extend credit.'' [78] At that time, the CFPB stated that it was continuing to study overdraft services on checking accounts and would propose any further regulatory consumer protections in that space through a separate rulemaking.[79]

F. Need for CFPB Action

As a result of the evolution of the overdraft market over the last few decades, the overdraft-related exception to the definition of finance charge in Regulation Z no longer serves its original purpose. The CFPB is proposing to update the exception, and several others that allow financial institutions to follow different rules for overdraft credit than for other forms of consumer credit, to ensure that overdraft credit offered by very large financial institutions is generally treated no differently than any other form of consumer credit, except in the narrow cases where it is provided as a courtesy to consumers. Preserving a limited exception from Regulation Z may encourage the availability of overdraft coverage, which can benefit consumers, especially given that much overdraft

[63] OCC, Interpretive Letter No. 914, at 6 (Sept. 2001), *https://www.occ.gov/topics/charters-and-licensing/interpretations-and-actions/2001/int914.pdf.*

[64] 67 FR 72618, 72620 (Dec. 6, 2002). In 2003, the Board noted that ''[t]he Board's staff is continuing to gather information on these services, which are not addressed in the final rule.'' (68 FR 16185 (Apr. 3, 2003)).

[65] 69 FR 31760, 31761 (June 7, 2004).

[66] *See* 70 FR 9127, 9128–29 (Feb. 24, 2005).

[67] 74 FR 5212 (Jan. 28, 2009).

[68] FDIC, *Final Overdraft Payment Supervisory Guidance,* FIL–81–2010 (Nov. 24, 2010), *https://www.fdic.gov/news/news/financial/2010/fil10081.html.*

[69] *Id.*

[70] *CFPB Circular 2022–06: Unanticipated Overdraft Fee Assessment Practices,* 87 FR 66935 (Nov. 7, 2022). The CFPB, the Board, and the FDIC also highlighted risks related to the imposition of overdraft fees from 2015 to 2018. *See* CFPB, *Supervisory Highlights,* at 8–9 (Winter 2015), *https://files.consumerfinance.gov/f/201503_cfpb_supervisory-highlights-winter-2015.pdf* (last visited Jan. 4, 2024) (CFPB Winter 2015 Highlight); FRS, *Interagency Overdraft Services Consumer Compliance Discussion,* Outlook Live presentation slides, at 20–21 (Nov. 9, 2016), *https://www.consumercomplianceoutlook.org/-/media/cco/Outlook-Live/2016/110916.pdf;* FRS, *Consumer Compliance Supervision Bulletin,* at 12 (July 2018), *https://www.federalreserve.gov/publications/files/201807-consumer-compliance-supervision-bulletin.pdf* (FDIC 2018 Highlight); FDIC, *Consumer Compliance Supervisory Highlights,* at 2–3 (June 2019), *https://www.fdic.gov/regulations/examinations/consumercomplsupervisory highlights.pdf?source=govdelivery&utm_medium=email&utm_source=govdelivery* (FDIC 2019 Highlight).

[71] OCC, *OCC Bulletin 2023–12, Overdraft Protection Programs: Risk Management Practices* (Apr. 26, 2023), *https://www.occ.treas.gov/news-issuances/bulletins/2023/bulletin-2023-12.html* (OCC Bulletin 2023–12); FDIC, *Supervisory Guidance on Charging Overdraft Fees for Authorize Positive, Settle Negative Transactions,* FIL–19–2023 (Apr. 26, 2023), *https://www.fdic.gov/news/financial-institution-letters/2023/fil23019a.pdf.*

[72] OCC Bulletin 2023–12.

[73] 81 FR 83934, 83934–35 (Nov. 22, 2016). The CFPB amended the 2016 Prepaid Final Rule in 2017 and 2018. *See* 82 FR 18975 (Apr. 25, 2017); 83 FR 6364 (Feb. 13, 2018). The 2016 Prepaid Final Rule and subsequent amendments to that rule are referred to collectively herein as the Prepaid Accounts Rule.

[74] 81 FR 83934, 83935–36 (Nov. 22, 2016).

[75] 15 U.S.C. 1602(f).

[76] 81 FR 83934, 84168 (Nov. 22, 2016).

[77] *Id.* at 84160.

[78] *Id.*

[79] *Id.* at 84162.

credit is incidental in nature, as consumers often do not know with certainty whether or not a transaction will be presented against sufficient funds. But a blanket exception for all of today's non-covered overdraft credit—which poses serious risks to consumers as reflected in the discussion of consumer impacts noted above, and resembles other mass-marketed high-cost consumer credit products—cannot be justified as an exception for a courtesy, nor as consistent with TILA's purposes of promoting the informed use of credit and comparison shopping across credit products. Therefore, the CFPB proposes to limit the exception from TILA, for very large financial institutions, to overdraft credit that is offered at a cost to the consumer that does not exceed the financial institution's costs and losses associated with providing such coverage.

III. Outreach and Related Research

The CFPB has engaged in outreach and research related to overdraft fees since soon after the CFPB's inception. In 2012, the CFPB initiated a broad inquiry into overdraft programs for consumer checking accounts.[80] This inquiry included a request for information on the impacts of overdraft fees on consumers,[81] and collection and analysis of overdraft-related data from several large banks with over $10 billion in assets that provided a significant portion of all U.S. consumer checking accounts.[82] The CFPB published analyses of these data in a series of reports from 2013–2017, which examined institution-level policies and data, as well as account- and transaction-level data.[83] These studies assessed, among other things, overdraft fee size, prevalence, and related account closure; overdraft policies and practices across institutions; the distribution of overdraft fee incurrence across accounts; how overdraft transactions and fees vary across opt-in status; the size of transactions that lead to overdrafts; how long account balances stay negative after overdrafts; and the characteristics of account holders (including end-of-day balance, deposits, credit score, and available credit on a credit card) across distributions of overdraft frequency. The CFPB also collected anonymized institution-level information from several core processors, which provide operations and accounting systems to financial institutions. This data collection informed the CFPB's 2021 report assessing policies and practices among a large sample of financial institutions using core processors.[84]

In 2021, the CFPB examined financial institutions' reliance on overdraft/NSF fees from 2015 to 2019, finding that it was persistent.[85] Since then, the CFPB has continued tracking trends in the marketplace[86] and evaluating some banks' key overdraft-related metrics through the CFPB's supervision work.[87] From December 2022 to June 2023, the CFPB reviewed the publicly available overdraft practices of financial institutions with assets over $10 billion.[88] In addition, the CFPB has recently collected information from several financial institutions under the CFPB's supervision, including data regarding financial institutions' costs associated with offering overdraft credit, which is discussed further in part V.C.2 as well as in a separate report titled Overdraft and NSF Practices at Very Large Financial Institutions.

Consistent with the CARD Act, the CFPB consulted with the following agencies regarding rules that implement TILA section 149: (1) the Office of the Comptroller of the Currency; (2) the Board of Directors of the Federal Deposit Insurance Corporation; and (3) the National Credit Union Administration Board. The CFPB also consulted with the Board and several other Federal agencies, as discussed in [part VIII].

IV. Legal Authority

The CFPB is issuing this proposal pursuant to its authority under TILA, EFTA, and the CFPA. This part includes a general discussion of the provisions on which the CFPB relies in this rulemaking.

A. Truth in Lending Act

TILA section 105(a). TILA section 105(a) directs the CFPB to prescribe regulations to carry out the purposes of TILA and provides that such regulations may contain additional requirements, classifications, differentiations, or other provisions, and may provide for such adjustments and exceptions for all or any class of transactions, that the CFPB judges are necessary or proper to effectuate the purposes of TILA, to prevent circumvention or evasion thereof, or to facilitate compliance therewith.[89] A purpose of TILA is to assure a meaningful disclosure of credit terms so that the consumer will be able to compare more readily the various available credit terms and avoid the uninformed use of credit.[90] This stated purpose is tied to Congress's finding that economic stabilization would be enhanced and competition among the various financial institutions and other firms engaged in the extension of consumer credit would be strengthened by the informed use of credit.[91] Thus, strengthened competition among financial institutions is a goal of TILA, achieved through the effectuation of TILA's purposes. A purpose of TILA is also to protect the consumer against inaccurate and unfair credit billing and credit card practices.[92]

CARD Act Section 2. Section 2 of the CARD Act, which amended TILA to establish fair and transparent practices relating to the extension of credit under an open-end consumer plan, and for other purposes, also specifically grants the CFPB authority to issue rules and model forms it considers necessary to carry out the CARD Act and amendments made by the CARD Act.[93]

For the reasons discussed in this notice, the CFPB is proposing amendments to Regulation Z with respect to overdraft credit to carry out TILA's purposes. The CFPB at this time is proposing to retain additional requirements, adjustments, and exceptions as, in the CFPB's judgment, are necessary and proper to carry out the purposes of TILA, prevent

[80] Press Release, CFPB, *CFPB Launches Inquiry into Overdraft Practices* (Feb. 22, 2012), *https://www.consumerfinance.gov/about-us/newsroom/consumer-financial-protection-bureau-launches-inquiry-into-overdraft-practices/.*

[81] 77 FR 12031 (Feb. 28, 2012).

[82] *See* CFPB 2013 White Paper at 8; *see also* CFPB 2014 Data Point at 6–7.

[83] *See* CFPB 2013 White Paper; CFPB 2014 Data Point; CFPB 2017 Data Point.

[84] Nicole Kelly & Éva Nagypál, Ph.D., CFPB, *Data Point: Checking Account Overdraft at Financial Institutions Served by Core Processors* (Dec. 2021), *https://files.consumerfinance.gov/f/documents/cfpb_overdraft-core-processors_report_2021-12.pdf.*

[85] CFPB 2021 Data Point.

[86] CFPB, *Trends in overdraft/non-sufficient fund (NSF) fee revenue and practices, https://content.consumerfinance.gov/data-research/research-reports/trends-in-overdraftnon-sufficient-fund-nsf-fee-revenue-and-practices/* (last updated Oct. 11, 2023) (reflecting data and analysis published periodically from Dec. 1, 2021 to present).

[87] *See* Patrick Gibson & Lisa Rosenthal, *Measuring the impact of financial institution overdraft programs on consumers,* CFPB (June 16, 2022), *https://www.consumerfinance.gov/about-us/blog/measuring-the-impact-of-financial-institution-overdraft-programs-on-consumers/;* CFPB, *Fall 2023 Supervisory Highlights Junk Fees Update Special Edition,* at 7–9 (Oct. 2023), *https://files.consumerfinance.gov/f/documents/cfpb_supervisory_highlights_junk_fees-update-special-ed_2023-09.pdf* (CFPB Fall 2023 Highlight).

[88] CFPB Market Monitoring of Publicly Available Overdraft Practices, Dec. 2022–July 2023.

[89] 15 U.S.C. 1604(a).

[90] 15 U.S.C. 1601(a).

[91] *Id.*

[92] *Id.*

[93] Public Law 111–24; § 2, 123 Stat. 1734, 1735 (2009).

circumvention or evasion thereof, or to facilitate compliance. In developing these aspects of the proposal pursuant to its authority under TILA section 105(a), the CFPB has considered the purposes of TILA, including ensuring meaningful disclosures, facilitating consumers' ability to compare credit terms, helping consumers avoid the uninformed use of credit, and protecting consumers against inaccurate and unfair credit billing and credit card practices, and the findings of TILA, including strengthening competition among financial institutions and promoting economic stabilization.

B. Electronic Fund Transfer Act

EFTA section 902 establishes that the purpose of the statute is to provide a basic framework establishing the rights, liabilities, and responsibilities of participants in EFT and remittance transfer systems but that its primary objective is the provision of individual consumer rights.[94] Among other things, EFTA contains provisions regarding compulsory use of EFTs.[95]

EFTA section 904(a) authorizes the CFPB to prescribe regulations to carry out the purposes of EFTA.[96] EFTA section 904(c) provides that regulations prescribed by the CFPB may contain such classifications, differentiations, or other provisions, and may provide for such adjustments or exceptions for any class of EFTs or remittance transfers, that the CFPB deems necessary or proper to effectuate the purposes of EFTA, to prevent circumvention or evasion, or to facilitate compliance.[97] The Senate Report accompanying EFTA noted that regulations are ''essential to the act's effectiveness'' and ''will add flexibility to the act by permitting the [CFPB] to modify the act's requirements to suit the characteristics of individual EFT services. Moreover, since no one can foresee EFT developments in the future, regulations would keep pace with new services and assure that the act's basic protections continue to apply.'' [98]

EFTA section 904(c) also provides that the ''CFPB shall by regulation modify the requirements imposed by this subchapter on small financial institutions if the CFPB determines that such modifications are necessary to alleviate any undue compliance burden on small financial institutions and such modifications are consistent with the purpose and objective of this subchapter.''

As discussed in part V below, the CFPB is adopting amendments to Regulation E, including with respect to compulsory use of preauthorized repayment and the definition of overdraft services, pursuant to the CFPB's authority under, as applicable, EFTA section 904(a) and (c). The CFPB is proposing to retain existing rules for financial institutions with less than $10 billion in assets because the CFPB has determined that such exceptions will alleviate undue compliance burdens as the CFPB continues to examine the market for smaller financial institutions.

C. Consumer Financial Protection Act

CFPA section 1022(b)(1). Section 1022(b)(1) of the CFPA authorizes the CFPB to prescribe rules ''as may be necessary or appropriate to enable the [CFPB] to administer and carry out the purposes and objectives of the Federal consumer financial laws, and to prevent evasions thereof.'' [99]

Among other statutes, TILA, EFTA, and the CFPA are Federal consumer financial laws.[100] Accordingly, in setting forth this proposal, the CFPB is exercising its authority under CFPA section 1022(b) to prescribe rules that carry out the purposes and objectives of TILA, EFTA, and the CFPA and prevent evasion of those laws.

V. Discussion of the Proposed Rule

A. Who is covered? (§ 1026.62(b)(8))

This proposed rule would expand protections to consumers of overdraft credit at financial institutions with more than $10 billion in assets. This proposal would not change the regulatory framework for overdraft credit offered by financial institutions with $10 billion or less in assets.

To limit the proposed rule to overdraft credit offered by financial institutions with assets of more than $10 billion, the proposed rule would define in proposed § 1026.62(b)(8) the term ''very large financial institution'' as an insured depository institution or an insured credit union with total assets of more than $10 billion and any affiliate thereof. A financial institution may determine whether it has total assets of more than $10 billion using the same determination that is used to determine whether such institutions are subject to the CFPB's supervisory authority under 12 U.S.C. 5515(a). The CFPB currently publishes a list of such institutions at *https://www.consumerfinance.gov/compliance/supervision-examinations/institutions/*. As discussed below, the proposed rule then uses the term ''very large financial institution'' to limit the scope of overdraft credit that would be subject to the proposed rule.

The CFPB has preliminarily determined that overdraft services offered by financial institutions with more than $10 billion in assets should be subject to this rule. As noted above, in the supervisory context, Congress adopted in 12 U.S.C. 5515(a) a $10 billion threshold to define the ''very large banks, savings associations, and credit unions'' that would be subject to the CFPB's primary supervision authority. The CFPB has preliminarily determined that a $10 billion threshold similarly should be used to define ''very large financial institution'' for limiting the scope of overdraft credit that would be covered by the proposed rule.

The CFPB has preliminarily determined that consumers would benefit from the CFPB's proceeding with a rule that would apply to very large financial institutions—*i.e.,* those with assets of $10 billion or more. Such a rule would increase protections for the overwhelming majority of consumers of overdraft credit. This proposal would cover financial institutions holding approximately 80 percent of consumer deposits as of December 2022 [101] and responsible for approximately 68 percent of overdraft charges as of December 2022.[102] The CFPB believes that consumers at very large financial institutions would benefit from the expanded protections that would be provided by the proposed rule.

In light of the different circumstances smaller financial institutions may face in adapting to the proposed regulatory framework, the CFPB is proposing not to extend the new rule to those institutions with $10 billion or less in assets. While the CFPB is not proposing any changes to the regulatory requirements for smaller financial institutions, the CFPB will continue to monitor the market in coordination with State and Federal supervisors.

The CFPB seeks comment on its preliminary determination to apply the proposed rule only to very large financial institutions and on whether $10 billion is an appropriate threshold for defining very large financial institutions.

[94] 15 U.S.C. 1693.

[95] 15 U.S.C. 1693k.

[96] 15 U.S.C. 1693b(a).

[97] 15 U.S.C. 1693b(c).

[98] *See* S. Rept. No. 95–1273, at 26 (1978).

[99] 12 U.S.C. 5512(b)(1).

[100] CFPA section 1002(14), 12 U.S.C. 5481(14) (defining ''Federal consumer financial law'' to include the provisions of the CFPA and enumerated consumer laws; ''enumerated consumer laws'' is defined in CFPA section 1002(12), 12 U.S.C. 5481(12)).

[101] Computed from 2022 FFIEC and National Credit Union Administration call report data.

[102] Estimated using data from 2022 FFIEC Call Reports and methodology discussed at FN 29.

B. What transactions and accounts are covered?

The CFPB proposes to add § 1026.62(a) and (b) to define the scope of transactions and accounts that would be covered under the proposed rule. The proposed rule would introduce new terms and amend several existing Regulation Z definitions and their commentary to state that overdraft credit is credit and assist with ease of reference to various types of overdraft credit. First, the proposal would define overdraft credit in proposed § 1026.62(a)(2), and proposed comment 2(a)(14)–4 would provide a brief example to illustrate that overdraft credit is credit under TILA and Regulation Z.

The CFPB's proposed rule would add commentary to the definition of open-end credit in § 1026.2(a)(20) to confirm that overdraft credit that is subject to a finance charge is generally open-end credit and is therefore subject to the Regulation Z provisions that apply to open-end credit. The proposed definitions of covered overdraft credit and non-covered overdraft credit in new § 1026.62(b) would assist with referencing overdraft credit that would be or not be credit subject to Regulation Z under this proposal. Covered overdraft credit under this proposal would be overdraft credit that is subject to a finance charge or is payable by written agreement in more than four installments, and would be subject to Regulation Z. Non-covered overdraft credit under this proposal would be overdraft credit that is neither subject to a finance charge nor payable by written agreement in more than four installments, and would not be subject to Regulation Z. Additionally, the CFPB proposes to add a new definition of covered overdraft credit account to facilitate ease of reference to credit accounts through which the financial institutions extend or can extend covered overdraft credit.

1. Overdraft Credit (§§ 1026.2(a)(14) and 1026.62(a))

TILA defines ''credit'' to mean the right granted by a creditor to a debtor to defer payment of debt or to incur debt and defer its payment.[103] Regulation Z similarly defines ''credit'' in existing § 1026.2(a)(14) to mean the right to defer payment of debt or to incur debt and defer its payment. To facilitate compliance with the proposed rule, proposed comment 2(a)(14)–4 would provide a brief, illustrative example of overdraft credit. The 2016 Prepaid Final Rule similarly notes that a ''person, in extending overdraft funds, has provided the consumer with 'the right . . . to incur debt and defer its payment.' ''[104]

The CFPB is proposing to update several exceptions in Regulation Z, increasing consumer protections that apply to overdraft credit offered by very large financial institutions. To that end, the CFPB would add a definition of ''overdraft credit'' in proposed § 1026.62(a) to help clarify the scope of transactions covered by the proposed rule. Proposed § 1026.62(a) would define ''overdraft credit'' as any consumer credit extended by a financial institution to pay a transaction from a checking or other transaction account (other than a prepaid account as defined in § 1026.61) held at the financial institution when the consumer has insufficient or unavailable funds in that account. Proposed § 1026.62(a) would provide non-exhaustive examples, such as consumer credit extended through a transfer from a credit card account or overdraft line of credit.

The proposed definition of ''overdraft credit'' would not cover credit features with respect to a prepaid account as defined in § 1026.61. The CFPB has preliminarily determined that it would be unnecessary and unduly burdensome to include prepaid accounts within the scope of this proposed rule. The CFPB's Prepaid Accounts Rule already provides comprehensive consumer protections tailored to prepaid accounts.[105]

Proposed § 1026.62(a) would also clarify that the term ''overdraft credit'' does not include credit exempt from Regulation Z pursuant to existing § 1026.3. For example, consistent with TILA section 104(2),[106] transactions in securities or commodities accounts in which credit is extended by a broker-dealer registered with the Securities and Exchange Commission or the Commodity Futures Trading Commission are not subject to Regulation Z pursuant to existing § 1026.3(d).

2. Open-End Credit (§ 1026.2(a)(20))

The term ''open-end credit'' is defined in § 1026.2(a)(20) as (1) consumer ''credit,'' (2) that is extended under a ''plan,'' (3) where the person extending the credit may impose a ''finance charge'' from time to time on an outstanding unpaid balance, (4) the person extending the credit is a ''creditor,'' (5) the person extending the credit reasonably contemplates repeated transactions, and (6) the amount of credit that may be extended to the consumer during the term of the plan (up to any limit set by the creditor) is generally made available to the extent that any outstanding balance is repaid.

For the reasons discussed below, the CFPB has preliminarily determined that virtually all overdraft credit that financial institutions provide today, such as through negative balances on checking accounts, would meet the Regulation Z definition of open-end credit, but for Regulation Z excepting overdraft fees from the definition of finance charge. Specifically, but for those exceptions, the typical $35 overdraft fee plainly constitutes a finance charge and a financial institution that regularly assesses such a finance charge is a creditor.[107]

The CFPB has preliminarily determined that overdraft credit that is typical in the market today would become covered overdraft credit under the proposed rule and would meet the six elements of open-end credit under Regulation Z. For clarity and to facilitate compliance, the CFPB is proposing additional commentary regarding two terms used in the definition of open-end credit: ''plan'' and ''finance charge.'' The following discusses each of the six elements in turn.

(1) Credit. As discussed above, a person extending overdraft funds has provided credit under TILA and Regulation Z.[108] Because the consumer is obligated to repay the funds, the financial institution is allowing the consumer to incur debt and defer its payment consistent with the TILA and Regulation Z definitions of ''credit.''

(2) Plan. The CFPB has preliminarily determined that a checking account agreement offered in connection with overdraft credit would—but for the Regulation Z exceptions of overdraft fees from the definition of finance charge—constitute a ''plan'' consistent with the definition of ''open-end credit plan'' in TILA.[109] Specifically, but for the Regulation Z exceptions, the checking account agreement—consistent with the language of comment 2(a)(20)–2.i—would be ''a contractual arrangement between the creditor [the institution offering checking account overdraft credit] and the consumer.'' As noted, the CFPB's proposed rule would modify those exceptions. The CFPB has preliminarily determined that an

[103] 15 U.S.C. 1602(f).

[104] 81 FR 83934, 84168 (Nov. 22, 2016).

[105] The 2016 Prepaid Final Rule and subsequent amendments to that rule are referred to collectively herein as the Prepaid Accounts Rule.

[106] 15 U.S.C. 1603(2).

[107] *See* § 1026.2(a)(17)(i) (defining ''creditor'' as ''[a] person who regularly extends consumer credit that is subject to a finance charge. . . .'').

[108] 15 U.S.C. 1602(f); 12 CFR 1026.2(a)(14).

[109] 15 U.S.C. 1602(j).

institution offering checking account overdraft credit would be a creditor (discussed under *(4) Person extending credit is a creditor,* below) and the account agreement would be ''a contractual arrangement between the creditor and the consumer.'' The CFPB proposes to add comment 2(a)(20)–2.iv to clarify that with respect to covered overdraft credit, a plan means a program where the consumer is obligated contractually to repay any credit extended by the creditor, even if the creditor retains discretion not to extend credit in individual transactions.

The CFPB has preliminarily determined that the reservation of such discretion in connection with covered overdraft credit does not connote the absence of an open-end credit plan. The CFPB understands that financial institutions offering automated overdraft services include in their agreements provisions about how the overdraft service will operate and information about overdraft fees. These terms-and-conditions documents typically stipulate that consumers using overdraft programs must and do agree to repay the debt created by an overdraft and the related fee, indicating that a contractual arrangement between the creditor and the consumer exists. Although these agreements typically state that the financial institution retains discretion to authorize or decline any particular overdraft, as a practical matter, financial institutions operating automated overdraft programs exercise limited if any discretion in authorizing particular transactions so long as the overdraft transaction is within the overdraft coverage limit that the institution internally established. The CFPB notes that credit card issuers similarly reserve the right to reject individual transactions in their contractual agreements, yet credit card programs are treated as open-end credit plans under TILA and Regulation Z. Treating the provision of automated overdraft credit in a comparable way would promote consistency. Therefore, the CFPB has preliminarily determined that a checking account agreement offered in connection with overdraft credit is a plan notwithstanding that the person offering the agreement reserves the right to not extend credit on individual transactions.

(3) Imposing a ''finance charge'' from time to time. The CFPB has preliminarily determined that overdraft credit is generally subject to fees that would be finance charges but for Regulation Z's exceptions to the statutory finance charge definition. As noted, the CFPB's proposed rule would modify those exceptions such that checking account overdraft fees would generally be finance charges. In the absence of the exceptions, the CFPB has preliminarily determined that an institution offering checking account overdraft credit would be imposing a finance charge from time to time.

While the proposed definition of covered overdraft credit includes overdraft credit that is subject to a finance charge as well as overdraft credit payable by a written agreement in more than four installments, the CFPB anticipates that most overdraft credit would meet the definition of covered overdraft credit because it is subject to a finance charge rather than because it is payable in more than four installments.[110] The CFPB proposes comment 2(a)(20)–4.iii to explain that charges for paying a transaction that overdraws a consumer's account generally would be finance charges unless they are expressly excluded from the definition of finance charge by the proposed rule.

Proposed comment 2(a)(20)–4.iii would clarify that these are charges ''imposed from time to time on an outstanding unpaid balance'' as long as there is no specific amount financed for the plan for which the finance charge, total of payments, and payment schedule can be calculated. The CFPB does not anticipate that there will be a specific amount financed for overdraft credit at the time the credit plan is established because the CFPB anticipates that the credit lines on these credit plans generally will be replenishing (discussed under *(6) Amount of credit replenishes when outstanding balance is repaid,* below). In such cases, an amount financed for the plan could not be calculated because the creditor will not know at the time the plan is established the amount of credit that will be extended under the plan. Thus, to the extent that any finance charge may be imposed in connection with such a credit plan, the credit plan will meet this criterion.

(4) Person extending credit is a creditor. Assuming overdraft fees are finance charges, the CFPB has preliminarily determined that an institution providing covered overdraft credit is a ''creditor'' for purposes of the definition of ''open-end credit.'' A ''creditor'' is generally defined under Regulation Z to mean a person who regularly extends consumer credit that is subject to a finance charge or is payable by written agreement in more than four installments (not including a down payment), and to whom the obligation is initially payable, either on the face of the note or contract, or by agreement when there is no contract.[111] Therefore, to the extent that overdraft credit is subject to a finance charge and is accordingly covered overdraft credit, it is also extended by a creditor if the creditor ''regularly extends'' overdraft credit. The CFPB anticipates that most persons offering covered overdraft credit regularly extend overdraft credit and therefore would meet the definition of ''creditor.'' If an institution providing open-end covered overdraft credit is considered a ''card issuer,'' then it would also be considered a creditor under current § 1026.2(a)(17)(iii) for purposes of Regulation Z, subpart B.

(5) Reasonably contemplates repeated transactions. The CFPB has preliminarily determined that institutions providing checking account overdraft credit typically contemplate repeated overdraft transactions as the CFPB found that 93.2 percent of overdraft and NSF fees were assessed on consumers with four or more overdraft and NSF transactions per year.[112] The CFPB has therefore preliminarily determined that this fifth element of the open-end credit definition is satisfied.

(6) Amount of credit replenishes when outstanding balance is repaid. The CFPB has preliminarily determined that institutions providing checking account overdraft credit generally replenish the amount of overdraft credit available to consumers up to any overdraft coverage limit (*i.e.,* consumers' ''shadow lines'') to the extent that any outstanding overdraft balance is repaid. This replenishable credit distinguishes open-end credit from a series of advances made pursuant to a closed-end credit loan commitment, but it does not mean that the credit plan must always be replenished to the original amount. The creditor may refuse to extend new credit in a particular case due to changes in the creditor's financial condition or the consumer's creditworthiness, if permitted by Regulation Z. While consumers should have a reasonable expectation of obtaining credit as long as they remain current, further extensions of credit need not be an

[110] A card issuer that extends covered overdraft credit that takes the form of closed-end credit and is subject to a finance charge or payable by a written agreement in more than four installments (including closed-end credit accessed by a hybrid debit-credit card) would be a creditor under § 1026.2(a)(17)(iv) and subject to the special rules in that paragraph. A person who is not a card issuer and regularly extends covered overdraft credit that takes the form of closed-end credit and is subject to a finance charge or is payable by written agreement in more installments would be a creditor under § 1026.2(a)(17)(i) and subject to the closed-end credit rules in Regulation Z, subpart C.

[111] *See* § 1026.2(a)(17)(i).

[112] CFPB 2017 Data Point at 13.

absolute right in order for the plan to meet the self-replenishing criterion. Because the CFPB anticipates that financial institutions will generally replenish overdraft credit to the extent that any outstanding overdraft balance is repaid, the CFPB has preliminarily determined that covered overdraft credit plans are generally replenishing.

3. Covered Overdraft Credit (§ 1026.62(b)(3)), Non-Covered Overdraft Credit (§ 1026.62(b)(6)), and Card Issuer (§ 1026.2(a)(7))

The CFPB proposes to define ''covered overdraft credit'' as overdraft credit that is subject to a finance charge or is payable by written agreement in more than four installments and ''non-covered overdraft credit'' as overdraft credit that is not subject to a finance charge and is not payable by written agreement in more than four installments. The purpose of the proposed definitions is to assist with ease of reference to overdraft credit that is subject to, or covered by, Regulation Z. As discussed in more detail in part V.C, some charges imposed in connection with overdraft credit are not considered finance charges. Thus, use of the proposed definitions will also help a person extending overdraft credit to readily ascertain whether they are subject to the requirements of the regulation.

The proposed definition of ''overdraft credit'' is limited to consumer credit, but, even with that qualification, not all overdraft credit would be subject to Regulation Z if the definition is finalized as proposed. Many provisions of Regulation Z apply to a ''creditor,'' which generally is defined at § 1026.2(a)(17)(i) as ''[a] person who regularly extends consumer credit that is subject to a finance charge or is payable by written agreement in more than four installments.'' Thus, a financial institution must offer overdraft credit that is subject to a finance charge or is payable by written agreement in more than four installments (*i.e.,* covered overdraft credit) to be considered a creditor under Regulation Z. (Any financial institution offering overdraft credit will generally satisfy the definition of ''regularly'' under § 1026.2(a)(17)(v).) Because some charges imposed in connection with overdraft credit are not considered finance charges, a financial institution may charge for overdraft credit without being considered a creditor under Regulation Z if certain requirements are met.

Section 1026.2(a)(7) defines ''card issuer'' as a person that issues a credit card or that person's agent with respect to the card. Unlike other creditors, card issuers are subject to Regulation Z even if they extend credit that is not subject to a finance charge and is not payable by written agreement in more than four installments.[113] However, this does not apply to overdraft credit that is not subject to a finance charge or repayable by written agreement in more than four installments, even if the financial institution extending such credit would otherwise be considered a card issuer.[114] Under the proposal, extensions of overdraft credit that are not subject to a finance charge and are not payable by written agreement in more than four-installments (non-covered overdraft credit) would continue to not be covered by Regulation Z. Further, under the proposal, institutions providing debit cards that access only non-covered overdraft credit would continue to not be card issuers, and would therefore not be creditors under § 1026.2(a)(17)(iii), because the CFPB has preliminarily determined that allowing financial institutions to offer debit cards that access only below breakeven overdraft credit without being subject to Regulation Z would further the purposes of this proposal as discussed in part V.C.

For these reasons, the CFPB has preliminarily determined that a new definition of ''covered overdraft credit'' that parallels the general definition of creditor will assist with ease of reference to overdraft credit that is subject to Regulation Z. Additionally, the CFPB has preliminarily determined that a new definition of ''non-covered overdraft credit'' will assist with ease of reference to overdraft credit that is not subject to, or covered by, Regulation Z, particularly in the proposed rule's costs and losses calculation in § 1026.62(d).

4. Covered Overdraft Credit Account (§ 1026.62(b)(4))

The CFPB proposes to define ''covered overdraft credit account'' as a credit account through which a financial institution extends or can extend covered overdraft credit. The term includes any line of credit, credit card account, credit feature, credit line, credit plan, or credit subaccount through which the financial institution extends or can extend covered overdraft credit. Proposed § 1026.62(c) would require very large financial institutions to structure covered overdraft credit as a separate credit account. Therefore, the term ''covered overdraft credit account'' would assist in ease of reference to these separate credit accounts and in distinguishing them from tied checking or other transaction accounts.

C. Changes to the Definition of ''finance charge'' (§ 1026.4(b)(2), (b)(12), and (c)(3); § 1026.62(d))

Under Regulation Z, the term ''finance charge'' generally is defined in § 1026.4(a) to mean ''the cost of consumer credit as a dollar amount.'' It includes any charge payable directly or indirectly by the consumer and imposed directly or indirectly by the creditor as an incident to or a condition of the extension of credit. It does not include any charge of a type payable in a comparable cash transaction.

Regulation Z currently excludes certain fees or charges imposed by a financial institution for paying items that overdraw an account from the definition of ''finance charge'' unless ''the payment of such items and the imposition of the charge were previously agreed upon in writing.''[115] Additionally, where the payment of such items and imposition of the charge were previously agreed upon in writing, when a creditor imposes a service, transaction, activity, or carrying charge for each item that results in an overdraft on an account, such fees are excluded from the definition of finance charge if they do not exceed the charges imposed for paying or returning overdrafts on a similar transaction account that does not have such a written agreement.[116] Neither of these exclusions appear within the statutory text of TILA.

The proposal would amend the definition of ''finance charge'' in § 1026.4 in three ways. First, it would modify the partial exception provided in § 1026.4(b)(2) for certain charges imposed on checking and other transaction accounts so that the partial exception would no longer apply to ''covered asset accounts'' as defined in proposed § 1026.62. Second, it would add proposed § 1026.4(b)(12) that would provide examples of charges imposed in connection with covered overdraft credit that are finance charges. Third, it would amend the exception provided in § 1026.4(c)(3) so that the exception would no longer apply to ''above breakeven overdraft credit'' as defined

[113] *See* 12 CFR 1026.1(c), and 1026.2(a)(17)(iii). Card issuers are also covered by the general rule that subjects them to Regulation Z if they extend open-end credit.

[114] Comment 2(a)(15)–2.ii.A. This comment provides that a debit card is not a credit card if there is no credit agreement, even if the creditor occasionally honors an inadvertent overdraft. Because the debit card is not considered a ''credit card'' under Regulation Z, a financial institution offering a debit card that can access non-covered overdraft credit is not considered a card issuer.

[115] 12 CFR 1026.4(c)(3).

[116] 12 CFR 1026.4(b)(2).

in proposed § 1026.62. These proposed amendments are intended to specify which overdraft transactions include a finance charge and, therefore, may be subject to the requirements of TILA and Regulation Z.

1. Comparable Cash Transactions (§ 1026.4(b)(2))

Under TILA section 106(a) (15 U.S.C. 1605(a)), the term ''finance charge'' generally provides that ''the amount of the finance charge in connection with any consumer credit transaction shall be determined as the sum of all charges, payable directly or indirectly by the person to whom the credit is extended, and imposed directly or indirectly by the creditor as an incident to the extension of credit.'' [117] The finance charge does not include any charge of a type payable in a comparable cash transaction.[118]

The current official interpretations address comparable cash transactions by stating that charges imposed uniformly in cash and credit transactions are not finance charges and by instructing that, to determine whether a transaction is a finance charge, the creditor should compare the credit transaction to a similar cash transaction.[119] The Board updated the commentary addressing finance charges numerous times.[120]

Section 1026.4(b) lists examples of the types of charges that generally are finance charges. In particular, § 1026.4(b)(2) provides that the finance charge includes ''[s]ervice, transaction, activity, and carrying charges, including any charge imposed on a checking or other transaction account (except a prepaid account as defined in § 1026.61) to the extent that the charge exceeds the charge for a similar account without a credit feature.''

The historical roots of § 1026.4(b)(2) trace back to the first version of Regulation Z, published by the Board in 1969. In that version, § 226.4(a)(2) indicated that the finance charge included service, transaction, activity, or carrying charges. The 1969 version of § 226.4(a)(2) also included a footnote stating that the charges listed in § 226.4(a)(2) included ''any charges imposed by the creditor in connection with a checking account to the extent that such charges exceed any charges the customer is required to pay in connection with such account when it is not being used to extend credit.'' [121]

As part of its 1981 amendments to Regulation Z, the Board moved the text of § 226.4(a)(2) to its current location in § 1026.4(b)(2) and incorporated the language from the accompanying footnote into the main regulation text.[122] Later that year, the Board also published comment 4(b)(2)–1, which provided two examples of service charges assessed on asset accounts with tied overdraft lines of credit that are not finance charges.[123] In 1998, the Board revised comment 4(b)(2)–1 to clarify that a service charge on a checking or other transaction account with a credit feature is a finance charge only if the charge exceeds the charge for a similar account without a credit feature.[124]

The CFPA generally granted rulemaking authority under the TILA and transferred primary oversight of Regulation Z to the CFPB. Subsequently, the CFPB renumbered § 226.4 to § 1026.4.[125] In 2016, the CFPB amended both § 1026.4(b)(2) and comment 4(b)(2)–1 to exclude prepaid accounts as defined in § 1026.61.[126] As part of that rulemaking, the CFPB provided detailed guidance in comment 4(b)(11)(ii) regarding how fees on prepaid accounts with a covered separate credit feature accessible by a hybrid prepaid-credit card should be compared to fees imposed on prepaid accounts without a covered separate credit feature. This guidance was more detailed and more restrictive than the guidance provided under § 1026.4(b)(2) with regard to checking and transaction accounts other than prepaid accounts.[127] As part of this guidance, the CFPB noted that the per transaction fee for a credit extension in the course of a transaction from a covered separate credit feature cannot be compared to a fee for declining to pay a transaction that is imposed on a prepaid account without such a credit feature in the same prepaid account program.[128] The CFPB was concerned about possible evasion of the rule, noting that many prepaid cardholders who wish to use covered separate credit features may not have other asset accounts or savings accounts from which they can transfer funds to prevent an overdraft on the prepaid account in the course of authorizing, settling, or otherwise completing a transaction to obtain goods or services, obtain cash, or conduct person-to-person (P2P) transfers.[129] As a result, if such a comparison were permitted, card issuers could charge a substantial fee to transfer funds from the checking account or savings account during the course of a transaction using the prepaid account (which many prepaid cardholders who wish to use covered separate credit features may not be able to use as a practical matter) and then charge that same substantial per transactions fee for credit drawn or transferred from the covered separate credit feature during the course of a transaction without such fee being considered a finance charge.[130] The CFPB thus concluded that it was appropriate to limit the comparable fee in this case to per transaction fees imposed on prepaid accounts for transactions that access funds in the prepaid account in the same prepaid account program that does not have a covered separate credit feature because all prepaid accountholders can use prepaid accounts to make transactions that access available funds in the prepaid account and thus these types of transactions are available to all prepaid accountholders.[131]

i. What is changing?

The proposal would revise § 1026.4(b)(2) and comment 4(b)(2)–1 to provide that § 1026.4(b)(2) does not apply to ''covered asset accounts'' as defined in § 1026.62. This proposed exception would mirror the exception created by the CFPB's Prepaid Rule.

The proposal also would add a paragraph at § 1026.4(b)(12). Proposed § 1026.4(b)(12) would add examples of finance charges with regard to covered asset accounts, as defined in proposed § 1026.62(b)(2). These proposed changes would broaden the definition of

[117] 12 CFR 1026.4(a). Current § 1026.4 implements TILA section 106 by largely mirroring the statutory definition of finance charge and the specific exclusions from that definition. In addition, § 1026.4 specifies certain inclusions and exclusions from the finance charge that are not specifically listed in the statute. For example, § 1026.4(c) specifically excludes application fees and forfeited interest from the definition of finance charge, whereas TILA does not.

[118] *See* 15 U.S.C. 1605(a).

[119] Regulation Z comment 4(a)–1.

[120] For example, the Board initially adopted comment 226.4(a)–4 to indicate that a fee charged by a card issuer when a consumer takes a cash advance on a credit card account using an ATM was not a finance charge to the extent that it did not exceed the charge imposed by the card issuer on its cardholders for using an ATM to withdraw cash from a consumer asset account, such as a checking or savings account. 48 FR 54642 (Dec. 6, 1983) and 49 FR 40560 (Oct. 17, 1984). After subsequent rulemaking activity, current comment 4(a)–4.1 provides that, for example, any charge imposed on a credit cardholder by a card issuer for the use of an ATM to obtain a cash advance is a finance charge regardless of whether the card issuer imposes a charge on its debit cardholders for using the ATM to withdraw cash from a consumer asset account, such as a checking or savings account. 74 FR 5263 (Jan. 29, 2009).

[121] 34 FR 2002, 2004 n.2 (Feb. 11, 1969).

[122] 46 FR 20848, 20894 (Apr. 7, 1981).

[123] 46 FR 50288, 50299 (Oct. 9, 1981).

[124] 63 FR 16669, 16675 (Apr. 6, 1998).

[125] 76 FR 79767 (Dec. 22, 2011).

[126] 81 FR 83934, 84369, 84374 (Nov. 22, 2016).

[127] *Id.* at 84185.

[128] *Id.* at 84186.

[129] *Id.*

[130] *Id.* at 84186–87.

[131] *Id.* at 84187.

''finance charge'' for covered asset accounts to apply the applicable rules to such accounts so that the full cost of credit is more accurately disclosed. The effect of the proposed changes would be to limit the existing exclusion in § 1026.4(b)(2) such that nearly all service, transaction, activity, and carrying charges imposed on covered asset accounts, including, in particular, fees commonly known as ''transfer fees'' for moving funds from overdraft lines of credit to covered asset accounts, would be ''finance charges'' under Regulation Z unless subject to another exclusion or limitation.[132]

ii. Charges Imposed on Credit Accounts Required by § 1026.62(c) (§ 1026.4(b)(12)(i))

Proposed § 1026.4(b)(12)(i) would specify that any service, transaction, activity, or carrying charge imposed on the separate credit account required by § 1026.62(c) is a finance charge. That is, the fees described in proposed § 1026.4(b)(12)(i) would be finance charges without regard to a comparison to fees for a comparable cash transaction.

Under § 1026.62(c), the required credit account exists for the purpose of providing credit. Therefore, service, transaction, activity, or carrying charges on this separate credit account are, per the finance charge definition in § 1026.4(a), generally imposed as an incident to or a condition of the extension of credit, separate and distinct from any such fees applied to a separate checking or other transaction account. Because of the nature of the credit account, it would be difficult or impossible to determine which, if any, charge applied to a checking or other asset account is a charge for a similar or comparable cash transaction for the purpose of § 1026.4(a). As with the Board's analysis in the 2009 amendment regarding credit card fee transactions, there is not necessarily a single or standard checking account to use for fee comparison. For example, there may be different fees applied to a checking account with a low balance minimum versus another type of checking account. Thus, it would be difficult in many cases to say which checking account provides the appropriate fee for comparison. Even assuming a comparable transaction could be identified, the disclosure a consumer might receive would depend on whether the creditor provides other asset accounts and imposes service, transaction, activity, or carrying charges on those accounts and whether the fees applied to those accounts exceed the fees for those on the separate credit account. As with the distinctions analyzed by the Board in the 2009 amendment, it is not clear that these distinctions are meaningful to consumers.[133] The CFPB has thus preliminarily determined that any service, transaction, activity, or carrying charge imposed on the separate credit account required by § 1026.62(c) would be a finance charge, except for charges specifically excluded by paragraphs (c) through (e) of section 1026.4.

iii. Charges Imposed on Covered Asset Accounts (§ 1026.4(b)(12)(ii))

Proposed § 1026.4(b)(12)(ii) would specify that any service, transaction, activity, or carrying charge imposed on the covered asset account is a finance charge to the extent that the charge exceeds a comparable charge imposed on a checking or other transaction account that does not have covered overdraft credit tied to it. That is, any such charge is a finance charge to the extent that it exceeds a comparable charge imposed on a checking or other transaction account that is not a covered asset account. This provision would largely mirror existing § 1026.4(b)(2) but with adjustments for covered asset accounts.

iv. Examples of Charges Imposed on Covered Asset Accounts (§ 1026.4(b)(12)(iii)(A) Through (C))

Proposed § 1026.4(b)(12)(iii) would describe certain charges on a checking or other transaction account that does not have covered overdraft credit tied to it that are not comparable to charges imposed on a covered asset account, which, by definition, does have covered overdraft credit tied to it. These charges would therefore not be permitted to be subtracted from charges applied to the covered asset account for the purpose of determining whether or not a charge on the covered asset account is a finance charge.

Proposed § 1026.4(b)(12)(iii)(A) would exclude from the determination of a finance charge comparison of a charge for authorizing or paying a transaction that overdraws the checking or other transaction account that does not have covered overdraft credit. Proposed § 1026.4(b)(12)(iii)(B) would exclude from the determination of a finance charge comparison of a charge for declining to authorize or pay a transaction, and proposed § 1026.4(b)(12)(iii)(C) would exclude from the determination of a finance charge comparison of a charge for returning a transaction unpaid.[134] Thus, under proposed § 1026.4(b)(12)(iii)(A) through (C), a very large financial institution may impose a service fee on a covered asset account when the institution transfers funds into the account from a covered overdraft credit account to cover a transaction that would otherwise overdraw the covered asset account. The institution may also impose a fee on a checking or other transaction account that does not have covered overdraft credit (*i.e.,* is not a covered asset account) when the institution authorizes or pays a transaction that would otherwise overdraw the checking or other transaction account, declines to authorize or pay a transaction that would otherwise overdraw the checking or other transaction account, or returns unpaid a transaction that would otherwise overdraw the checking or other transaction account. However, the fee applied to a checking or other transaction account that does not have covered overdraft credit may not be compared to the fee on a covered asset account for the transfer of funds to cover a transaction. Accordingly, under proposed § 1026.4(b)(12)(iii)(A) through (C), the full amount of the service fee on a covered asset account when a very large financial institution transfers funds into the account from a covered overdraft credit account to cover a transaction that would otherwise overdraw the covered asset account would be a finance charge. Taken together, these three provisions would clarify that the service, transaction, activity, or carrying charges imposed on covered asset accounts may not, for the purposes of determining whether such fees are ''finance charges,'' be reduced by fees that relate to granting or denying a transaction that would overdraw an account without covered overdraft credit.

The CFPB has made the preliminary determination to exclude from the determination of a finance charge these categories of charges for two reasons.

[132] Under the proposal, fees would continue to be excluded from the definition of finance charge if they are described in existing § 1026.4(c) through (e).

[133] 74 FR 5263 (Jan. 29, 2009). As discussed above, the purposes of TILA are to provide a meaningful disclosure of credit terms to enable consumers to compare credit terms available in the marketplace more readily and avoid the uninformed use of credit and to protect consumers against inaccurate and unfair credit billing and credit card practices. 15 U.S.C. 1601(a).

[134] Some or all of the fees described in proposed § 1026.4(b)(12)(iii)(A) through (C) are sometimes referred to as ''overdraft fees,'' ''declination fees,'' or ''NSF fees.'' Proposed § 1026.4(b)(12)(iii)(A) through (C) are broadly inclusive of the types of fees described therein, regardless of how such fees are labeled.

First, these types of charges are charges associated with decisions regarding whether or not to extend credit. The charges described in proposed § 1026.4(b)(12)(iii)(A) are applied if credit is extended; the charges described in proposed § 1026.4(b)(12)(iii)(B) and (C) are applied if credit is denied. As such, they are not charges associated with cash transactions, comparable or otherwise, and should not be compared to or subtracted from fees associated with covered overdraft credit. Additionally, the charges described in proposed § 1026.4(b)(12)(iii)(B) may be described as a penalty, while the charges described in proposed § 1026.4(b)(12)(iii)(C) may be described as a service charge. In neither case are the charges of a type payable in comparable cash transactions.

v. Additional Examples of Charges Imposed on Covered Asset Accounts (§ 1026.4(b)(12)(iii)(D) and (E))

Proposed § 1026.4(b)(12)(iii)(D) would exclude, for purposes of determining whether the fee is a finance charge, comparison of a charge for transferring funds from any credit account into a checking or other transaction account that does not have covered overdraft credit. Proposed § 1026.4(b)(12)(iii)(E) would exclude, for purposes of determining whether the fee is a finance charge, comparison of a charge for transferring funds from any other asset account, such as a savings account, into a checking or other transaction account that does not have covered overdraft credit. Thus, under proposed § 1026.4(b)(12)(iii)(D) and (E), a very large financial institution may impose a service fee on a covered asset account when the institution transfers funds into the account from a covered overdraft credit account to cover a transaction that would otherwise overdraw the covered asset account. The institution may also impose a fee to transfer funds into the checking or other transaction account (*i.e.,* an account that is not a covered asset account) from any credit account or from any other asset account, such as a savings account, to cover a transaction that would otherwise overdraw the checking or other transaction account. But the fee applied to a checking or other transaction account that does not have covered overdraft credit may not be compared to the fee on a covered asset account for the transfer of funds to cover a transaction. Accordingly, under proposed § 1026.4(b)(12)(iii)(D) and (E), the full amount of the service fee on a covered asset account when a very large financial institution transfers funds into the account from a covered overdraft credit account to cover a transaction that would otherwise overdraw the covered asset account would be a finance charge.

The exclusion in proposed § 1026.4(b)(12)(iii)(D) addresses charges in connection with an extension of credit that is regulated as credit, albeit not overdraft credit. Because these are charges payable in a credit transaction, the CFPB has preliminarily determined that these are not charges payable in a comparable cash transaction and should not be used for comparison in the determination of a finance charge.

The exclusion in proposed § 1026.4(b)(12)(iii)(E) addresses charges to transfer funds into a checking or other transaction account that is not a covered asset account from any other asset account to cover a transaction that would otherwise overdraw the checking or other transaction account. This is because the CFPB is concerned about the possibility for evasion from the requirements of Regulation Z if comparison of the charges described in § 1026.4(b)(12)(iii)(E) were to be permitted.

The majority of combined overdraft and NSF fees are paid by a small subset of consumers. CFPB research found that 79 percent of combined overdraft and NSF fees were paid by 9 percent of consumers who paid more than 10 such fees per year, incurring a median of $380 in these fees in a year.[135] Consumers paying more than 20 such fees in a year accounted for about 5 percent of accounts, while paying over 63 percent of the fees.[136]

Consumers whose accounts are frequently overdrawn are typically more financially insecure than those who do not overdraw or who do so infrequently.[137] Accordingly, many consumers who overdraft may not have other asset accounts or may not have sufficient funds in those accounts from which they can transfer funds to prevent such overdraft.

If such a comparison were permitted, a bank could potentially avoid the definition of ''finance charge'' by charging a substantial fee for transferring funds into a checking or other transaction account that is not a covered asset account from any other asset account and then charge that same substantial amount for any service, transaction, activity, or carrying charge imposed on the covered asset account. By comparing the two substantial fees to each other, the amount of the charge on the covered asset account would not be considered a finance charge. For the subset of consumers who pay the majority of overdraft and NSF fees, however, this comparison of fees would be a comparison between a product that such consumers can readily access (*i.e.,* covered asset accounts) to a product that a majority of such consumers may not be able to access (*i.e.,* other asset accounts) because they do not have such accounts or do not have sufficient funds in those accounts to easily execute transfers. As a result, the CFPB preliminarily concludes that a per transaction fee for transferring asset funds from other asset accounts such as a savings account should not be compared with (should not be allowed to be subtracted from) a service, transaction, activity, or carrying charge assessed on a covered asset account. The CFPB seeks comment on the proposed revisions to § 1026.4(b)(2), the proposal to add § 1026.4(b)(12), and the CFPB's preliminary conclusions regarding comparable cash transactions.

2. History of the Current § 1026.4(c)(3) Exception

Historically, whenever a consumer bounced a check written against a deposit account that lacked a credit feature, the consumer's financial institution typically returned the check unpaid and assessed the consumer an NSF fee. In addition, the payee on the check might have taken various actions against the consumer, such as assessing the consumer a late fee or returned item fee, reporting the consumer's payment as late to a credit bureau, or bringing legal action against the consumer for writing a bad check.[138] However, instead of returning the check unpaid, a financial institution, in its discretion, might have paid the check into overdraft as a courtesy.[139]

Although Congress did not exempt any category of overdraft credit from TILA,[140] the Board used its exception (not its interpretive) authority to create a limited exception for this longstanding practice when it issued Regulation Z in

[135] CFPB 2017 Data Point at 5; CFPB 2014 Data Point at 12.

[136] CFPB 2017 Data Point at 5.

[137] *See id.* at 5–6.

[138] 74 FR 5212, 5214 (Jan. 29, 2009); 74 FR 59033, 59035 (Nov. 17, 2009); Steve Cocheo, *Follow the Bouncing Check,* 95 ABA Banking J. 32, at 34 (Apr. 2003) (Cocheo 2003).

[139] *See* Peter G. Weinstock & Stephanie E. Dreyer, *Overdraft Protection Programs: The Emerging Battleground for Bankers and Consumer Advocates,* 121 Banking L. J. 791, at 795 (2004) (''Banks have been paying NSF items as a service to customers on a case-by-case basis for decades.''); *see also* Cocheo 2003 at 34 (''Our overdraft program formalizes the traditional courtesy of paying insufficient checks. . . .'') (quoting Gaynell Lawson, Executive Vice-President and Chief Financial Officer of Citizens Bank of Blount County).

[140] *See* Public Law 90–321, 82 Stat. 146 (May 29, 1968), codified as amended at 15 U.S.C. 1601 *et seq.*

1969.[141] Specifically, the Board added § 226.4(d), which provided that ''[a] charge imposed by a bank for paying checks which overdraw or increase an overdraft in a checking account is not a finance charge unless the payment of such checks and the imposition of such finance charge were previously agreed upon in writing.'' [142] A bank providing discretionary, check-centric overdraft (*a.k.a.* ''bounce-check protection'' or ''courtesy overdraft protection'' services, as noted in later **Federal Register** publications [143]) was not a creditor subject to Regulation Z because, pursuant to this exception, it did not impose a finance charge (and otherwise did not structure the repayment of credit by written agreement in more than four installments).[144] As Board commentary on Regulation Z noted, this exception enabled a bank to ''occasionally, as an accommodation to its customer, honor a check which inadvertently overdraws that account'' without having to comply with the requirements of Regulation Z.[145]

In 1981, the Board amended Regulation Z to, among other things, make ''a few minor editorial changes'' to the § 226.4(d) exception.[146] Specifically, the Board changed the term ''bank'' to ''financial institution'' and the term ''checks'' to ''items.'' [147] The Board made these changes ''to reflect the ability of financial institutions other than banks, such as savings and loan associations, to pay items that are similar to checks, such as negotiable orders of withdrawal, into overdraft.'' [148] Additionally, the Board renumbered § 226.4(d) to § 226.4(c)(3).[149] By making these ''minor editorial changes,'' the Board stated that ''[n]o substantive change is intended . . . .'' [150] In other words, the Board did not change the purpose of the § 226.4(d) exception, which was to allow financial institutions to provide consumers with courtesy check-centric overdraft services without having to comply with the requirements of TILA and Regulation Z.

The language from the Board's 1981 version of § 226.4(c)(3) remains in effect unchanged at § 1026.4(c)(3) in the CFPB's current version of Regulation Z.[151]

3. Proposed Changes to the § 1026.4(c)(3) Exception

It is the CFPB's preliminary view that the § 1026.4(c)(3) exception is overbroad for purposes of the current non-covered overdraft market. To address the issue, the CFPB proposes to add a new sentence to the end of § 1026.4(c)(3) that would provide that the paragraph no longer applies to ''above breakeven overdraft credit'' as that term is defined in proposed § 1026.62. As discussed in part V.A, the CFPB proposes to apply its proposed § 1026.4(c)(3) amendment only to very large financial institutions.

The CFPB proposes to define the term ''above breakeven overdraft credit'' at § 1026.62(b)(1) to mean overdraft credit extended by a very large financial institution to pay a transaction on which, as an incident to or a condition of the overdraft credit, the very large financial institution imposes a charge or combination of charges exceeding the average of its costs and charge-off losses for providing non-covered overdraft credit as described in § 1026.62(d). The CFPB proposes to establish above breakeven overdraft credit by reference to the average of a very large financial institution's cost and charge off losses for providing non-covered overdraft credit rather than the cost and estimated charge-off losses for providing non-covered overdraft credit for each separate transaction because the CFPB has preliminarily determined, based on its supervisory experience, that many financial institutions currently do not track their costs and charge-off losses at the transaction level, but generally can calculate their average costs and charge-off losses at the product level. Further, the CFPB expects that an institution-wide calculation would be easier for very large financial institutions to administer.

The CFPB is proposing these changes for several independent reasons.

First, the market for non-covered overdraft credit has changed in important ways—many financial institutions have automated their non-covered overdraft programs and expanded them to cover non-check transactions, while also adjusting their account pricing structure to more heavily emphasize overdraft fees.[152] These changes have caused the market for non-covered overdraft credit to move away from the historical courtesy model to the point that, for a significant number of consumers, non-covered overdraft credit is no longer an occasional accommodation for inadvertent overdrafts.

Unlike in 1969, when checks made up the lion's share of overdraft transactions,[153] recent CFPB analysis of account data from a number of large banks showed that on average overall only 10.36 percent of monthly debit transactions occurred by check, while 62.14 percent occurred by debit card (both one-time and recurring), 12.14 percent occurred by ACH, 6.43 percent occurred by ATM, 0.71 percent occurred by bank teller, and the remainder occurred by other means.[154]

This shift away from check transactions is significant because, as financial institutions have automated their non-covered overdraft programs and expanded them to cover non-check transactions, the sheer volume of overdraft transactions and associated fees has increased.[155] This trend especially is pronounced with respect to debit cards, where CFPB research shows that incidence of overdraft increases for consumers who use debit cards. For example, CFPB research shows that 92.3 percent of accounts that do not use debit cards have no overdrafts in a year of account use and only 0.6 percent of such accounts incur more than 10 overdrafts per year.[156] In contrast, accounts that use their debit cards more than 30 times per month have the lowest percentage of accounts with no overdraft (51.2 percent) and the highest percentage of accounts that overdraft more than 10 times per year (18.0 percent).[157] In other words, for many consumers who use debit cards frequently, non-covered overdraft credit services are no longer provided as an occasional accommodation.[158]

[141] 34 FR 2002, 2004 (Feb. 11, 1969); 73 FR 28904, 28927 (May 19, 2008) (''Historically, if a consumer engaged in a transaction that overdrew his or her account, depository institutions used their discretion on an ad hoc basis to pay the overdraft, usually imposing a fee. The Board recognized this longstanding practice when it initially adopted Regulation Z in 1969 to implement TILA.'').

[142] 34 FR 2002, 2004 (Feb. 11, 1969).

[143] 70 FR 29582, 29582 n.1 (May 24, 2005).

[144] *See* 12 CFR 1026.2(a)(17)(i).

[145] 42 FR 22360, 22362 (May 3, 1977).

[146] 46 FR 20848, 20855 (Apr. 7, 1981).

[147] *Id.*

[148] *Id.*

[149] *Id.*

[150] *Id.*

[151] In 2016, the CFPB added an additional sentence to the end of § 1026.4(c)(3) to clarify that the paragraph does not apply to credit offered in connection with a prepaid account as defined in § 1026.61. *See* 81 FR 83934, 84179 (Nov. 22, 2016). However, this amendment did not impact the text of the portion of § 1026.4(c)(3) adopted in 1981.

[152] 74 FR 5212 (Jan. 29, 2009); 81 FR 83934, 83950–51 (Nov. 22, 2016).

[153] Stephen Quinn & William Roberds, *The Evolution of the Check as a Means of Payment: A Historical Survey,* 93 Fed. Rsrv. Bank of Atlanta Econ. Rev. 1, at 21 (2008).

[154] CFPB 2014 Data Point at 17.

[155] 81 FR 83934, 83950–51 (Nov. 22, 2016).

[156] CFPB 2014 Data Point at 15 tbl.4c.

[157] *Id.*

[158] 42 FR 22360, 22362 (May 3, 1977) (''[Section 226.4(d) (now section 1026.4(c)(3)] relates only to regular demand deposit accounts which carry no credit features and in which a bank may occasionally, as an accommodation to its customer,

Continued

Moreover, financial institutions today routinely extend overdraft credit in circumstances where they stand to generate more direct revenue from extending overdraft credit to cover a transaction than they would from declining it (because, for example, consumers are rarely charged NSF fees for declined debit card transactions,[159] and nearly two-thirds of banks with over $10 billion in assets have eliminated NSF fees [160]).[161] As a result of these changes, non-covered overdraft programs now generate a substantial portion of the direct fee revenue that many financial institutions make from checking accounts (and much of the total revenue that financial institutions make from low-balance accounts), which has encouraged some financial institutions to promote consumers' use of non-covered overdraft credit and/or to calibrate their systems to increase overdraft fee revenue.[162] This shift represents a significant departure from the historical courtesy model, which provided an accommodation to consumers for the occasional inadvertent overdraft.

The proposed changes described in this section would return the exception to its original conception—excepting overdraft services from Regulation Z when offered as a courtesy or accommodation to customers—while adapting it to fit within the modern payments system. The concept of a courtesy or an accommodation is the provision of a service primarily for the convenience of a customer. A credit product that produces large amounts of revenue and profit, and is provided to many people who may not want the service, is not consistent with the concept of providing an additional service as a courtesy. The CFPB preliminarily finds that, where a financial institution sets its overdraft fees at or below its breakeven point, it provides a courtesy service to consumers who overdraw their accounts. Conversely, where a financial institution sets its overdraft fees above its breakeven point, and profits from those fees, it cannot be said to be providing a courtesy. The CFPB has preliminarily determined that the § 1026.4(c)(3) exception should continue to apply to overdraft fees set at or below the breakeven point, so that very large financial institutions have the option to recover their costs and losses associated with providing non-covered overdraft credit to consumers (without having to comply with Regulation Z), and thus, are not disincentivized from providing non-covered overdraft to consumers as a convenience.

In addition to returning the § 1026.4(c)(3) exception to its original courtesy conception, an independent justification for the proposed amendments to § 1026.4(c)(3) is that they would further TILA's purposes of promoting the informed use of credit and comparison shopping across credit products. Currently, most non-covered overdraft credit is subject to Regulations DD and E. Although Regulation DD and Regulation E require certain disclosures for overdraft services, neither regulation requires that such non-covered overdraft credit be disclosed as a credit product. Instead, both regulations use terms like overdraft fees, overdraft practices, or overdraft services that tend to obscure the fact that financial institutions are providing consumers a credit product. Applying the Regulation Z regulatory framework would benefit consumers by ensuring that above breakeven overdraft credit is disclosed as a credit product and treated like other credit products. Treating above breakeven overdraft credit like other credit would benefit consumers by helping them understand that they are entering into a contract for a credit product provided by a creditor. Unlike the disclosures required under Regulation DD and Regulation E, the disclosures required by Regulation Z are designed to set forth contractual terms for credit products clearly. Providing such disclosures will help promote the informed use of credit. In addition, treating above breakeven overdraft credit like other credit would benefit consumers by aligning the disclosures for such credit with other credit types and by applying Regulation Z's substantive credit protections consistently across similar credit products.

Further, disclosing above breakeven overdraft credit under the Regulation Z regulatory framework would make it easier for consumers to compare the cost of such credit with the cost of other credit products, such as linked credit cards, because financial institutions would present the credit terms for above breakeven overdraft credit in the same form that creditors present the credit terms of other credit products. In its November 2009 rulemaking finalizing the current Regulation E opt-in rule, the Board acknowledged that, based on its own consumer testing, consumers are interested in receiving more information about alternatives to non-covered overdraft credit services on ATM and one-time debit card transactions prior to deciding whether or not to opt in to such services.[163] Even though consumers generally are interested in alternatives to non-covered overdraft credit services, some consumers, including consumers who may even have alternative credit available to them,[164] continue to be frequent users of non-covered overdraft credit services despite its higher cost relative to other forms of credit. For example, CFPB research found that in 2012 the median overdraft fee was $34, the median size of a debit card transaction incurring an overdraft fee was $24, and that the majority of non-covered overdraft credit transactions were repaid within three days.[165] Putting these figures in lending terms, the annual percentage rate (APR) for such a non-covered overdraft credit transaction would be 17,000 percent (if transaction fees were included in the APR calculation).[166] By comparison, CFPB research found that the APR for a typical payday loan was 391 percent and APRs on credit cards can range between 12 and 30 percent.[167] The fact that frequent overdrafters continue to use non-covered overdraft credit services despite its higher cost relative to other credit suggests that some frequent overdrafters have difficulty comparing non-covered overdraft credit services with available alternatives. Disclosing above breakeven overdraft credit services under the Regulation Z regulatory framework would promote

honor a check which inadvertently overdraws that account.'').

[159] 74 FR 5212, 5217 (Jan. 29, 2009).

[160] *See* CFPB October 2023 Data Spotlight.

[161] This was not always the case. Historically, financial institutions charged no more for honoring an overdrawing check through non-covered overdraft credit than they did for returning the check unpaid. For example, a 1976 report on bank fees presented the results of a survey of banks in New York and Washington, DC. Of the 41 banks surveyed, 39 charged overdraft fees that were equal to or less than the amount of their NSF fees. *See* Senate Staff Report at 10–11.

[162] *See* 81 FR 83934, 83950–51 (Nov. 22, 2016); 70 FR 29582, 29583 (May 24, 2005); CFPB 2013 White Paper at 16–17; CFPB Winter 2015 Highlight at 8–9; FDIC 2018 Highlight at 12; FDIC 2019 Highlight at 2–3.

[163] 74 FR 59033, 59048 (Nov. 17, 2009).

[164] CFPB 2017 Data Point at 16 tbl. 2.

[165] CFPB 2013 White Paper at 52; CFPB 2014 Data Point at 5.

[166] Press Release, CFPB, *CFPB Finds Small Debit Purchases Lead to Expensive Overdraft Charges* (July 31, 2014), *https://www.consumerfinance.gov/about-us/newsroom/cfpb-finds-small-debit-purchases-lead-to-expensive-overdraft-charges/*. Recent supervisory data the CFPB has collected, reflecting transactions from 2022 and 2023, found that the median debit card overdraft resulted in an overdraft credit extension of approximately $25.50. Assuming a credit extension of $25.50, the $35 overdraft fee typical of very large financial institutions, and a three-day repayment period results in a similar APR of over 16,000 percent.

[167] CFPB, *Payday Loans and Deposit Advance Products,* at 9 (Apr. 24, 2013), *https://files.consumerfinance.gov/f/201304_cfpb_payday-dap-whitepaper.pdf;* CFPB, *Ask CFPB: What is a payday loan?, https://www.consumerfinance.gov/ask-cfpb/what-is-a-payday-loan-en-1567/* (last reviewed Jan. 17, 2022).

the informed use of credit by ensuring that credit terms were disclosed consistently across competing credit products, thereby helping consumers compare such credit with alternative credit options.

Moreover, the CFPB expects that applying the Regulation Z regulatory framework to above breakeven overdraft credit services would benefit consumers by applying the regulation's existing substantive protections to such credit services. For example, the CFPB's proposal, as discussed in additional detail in this notice, would apply the due date requirement in 1026.7(b)(11)(i)(A), the offset prohibitions in § 1026.12(d)(1), and the ability to pay provisions in § 1026.51 to covered overdraft credit accounts (including credit that currently is non-covered above breakeven overdraft credit) that can be accessed by a hybrid debit-credit card. Therefore, applying Regulation Z to above breakeven overdraft credit would prohibit very large financial institutions from immediately taking funds from any incoming deposit in repayment of the consumer's overdraft balance, would require very large financial institutions to establish due dates on the same day of each billing cycle, and would require very large financial institutions to assess the consumer's ability to pay for such credit—all protections that the current Regulation DD and Regulation E regulatory frameworks do not provide.

The CFPB acknowledges that the current § 1026.4(c)(3) exclusion has existed in its present form for decades and that very large financial institutions have undertaken efforts to ensure that their non-covered overdraft credit services comply with Regulations DD and E. The CFPB also recognizes that some consumers have come to rely on the availability of non-covered overdraft credit. The CFPB's proposal reflects, in part, an effort to balance these reliance interests against the other considerations discussed above in this section. The proposed changes to § 1026.4(c)(3) would require very large financial institutions to comply with Regulation Z when providing above breakeven overdraft credit services, but would allow them to continue to comply with Regulations DD and E when providing non-covered overdraft credit services at or below breakeven pricing. Thus, a very large financial institution that has invested in compliance with Regulations DD and E could maintain its current processes for providing consumers with non-covered overdraft credit so long as it priced such credit at or below breakeven pricing.

i. Alternatives to the Proposed § 1026.4(c)(3) Amendment Considered

During the development of its proposal, the CFPB considered alternatives to its proposed amendment to § 1026.4(c)(3) including (1) striking § 1026.4(c)(3) from Regulation Z in its entirety and (2) updating the opt-in disclosure requirements at § 1005.17 of Regulation E in a manner that would better disclose the costs associated with authorizing non-covered overdraft protection for ATM and debit card transactions.[168]

With respect to the first alternative, the CFPB has preliminarily determined that it should not eliminate all non-covered overdraft credit. The CFPB believes that the proposed amendment to § 1026.4(c)(3) is preferable because it would address the CFPB's concerns relating to consumers' informed use of above breakeven overdraft credit, including a consumer's ability to compare competing credit offers, and apply other substantive protections, including ability to pay requirements and offset restrictions, while allowing very large financial institutions to still offer non-covered overdraft credit as a courtesy if they chose to do so.

With respect to the second alternative, the CFPB preliminarily determined that Regulation E opt-in disclosures would not communicate the cost of above breakeven overdraft credit as effectively as Regulation Z disclosures. As discussed above, applying Regulation Z will ensure that above breakeven overdraft credit is disclosed as a credit product and treated like other credit products. In addition, Regulation E disclosures distinguish between overdraft transactions completed via electronic fund transfers and overdraft transactions completed via other funds transfer methods (such as checks), whereas Regulation Z disclosures would apply identically to above breakeven overdraft transactions regardless of fund transfer method. Modifying the opt-in disclosure requirements at § 1005.17 of Regulation E also would not provide other substantive protections available through Regulation Z, such as the ability to pay requirements and the offset prohibition discussed above. These substantive protections are important. For example, by requiring financial institutions to assess consumers' ability to pay, the proposed rule would ensure that financial institutions confirm that consumers could make the required minimum periodic payments under the terms of their account based on their income or assets and their current obligations. As another example, by prohibiting offset and requiring the due date to be on the same day each month for covered overdraft credit accessible by a hybrid debit-credit card, the proposed rule would give consumers more time to repay overdraft credit and greater control over how to structure those repayments. Therefore, the CFPB preliminarily believes that its proposal better protects consumers than an approach that merely updates the opt-in disclosure requirements at § 1005.17 of Regulation E.

ii. How To Calculate Whether Overdraft Credit Is Above Breakeven Overdraft Credit

To clarify the circumstances under which overdraft credit offered by a very large financial institution is ''above breakeven overdraft credit'' for purposes of proposed § 1026.62(b)(1), the CFPB also proposes to add a paragraph at § 1026.62(d).

Proposed § 1026.62(d)(1) would clarify that overdraft credit offered by a very large financial institution is ''above breakeven overdraft credit'' for purposes of proposed § 1026.62(b)(1) if the charge or combination of charges for such credit exceeds the greater of (1) the pro rata share of the very large financial institution's annual total direct costs and charge-off losses for providing non-covered overdraft credit calculated in accordance with § 1026.62(d)(2); or (2) an estimate published by the CFPB.

For purposes of proposed § 1026.62(d)(1), a ''combination of charges'' would include all revenue received in connection with an overdraft transaction when determining whether the charges for that transaction exceed its average costs and charge-off losses for providing non-covered overdraft credit, including any extended or sustained overdraft fees, any interest charges on outstanding overdraft balances, and any other payments the very large financial institution receives in connection with an overdraft transaction or transactions.

The approach outlined in proposed § 1026.62(d)(1) would provide a very large financial institution with two methods for determining whether its current charge for an overdraft transaction exceeds the average of its costs and charge-off losses for providing non-covered overdraft credit—the breakeven standard described at proposed § 1026.62(d)(1)(i) and the benchmark fee described at proposed

[168] Press Release, CFPB, *CFPB Unveils Prototypes of ''Know Before You Owe'' Overdraft Disclosure Designed to Make Costs and Risks Easier to Understand* (Aug. 4, 2017), *https://www.consumerfinance.gov/about-us/newsroom/cfpb-unveils-prototypes-know-you-owe-overdraft-disclosure-designed-make-costs-and-risks-easier-understand/.*

§ 1026.62(d)(1)(ii). To the extent that a very large financial institution does not determine or prefers not to calculate its average costs and charge-off losses for providing non-covered overdraft credit using the breakeven standard described at proposed § 1026.62(d)(1)(i), the proposal would permit the very large financial institution to determine whether it is offering above breakeven overdraft credit based solely on the benchmark fee at proposed § 1026.62(d)(1)(ii). The CFPB has preliminarily determined that this approach would decrease compliance costs for some very large financial institutions by providing them with a simple bright-line method for determining whether the overdraft credit they extend is above breakeven overdraft credit. Other very large financial institutions would be permitted the flexibility to calculate on their own whether the overdraft credit they extend is above breakeven pricing.

To employ the breakeven standard described at proposed § 1026.62(d)(1)(i), a very large financial institution would determine its total direct costs and charge-off losses for providing non-covered overdraft credit to all accounts open at any point during the previous 12 months and then divide that figure by the total number of non-covered overdraft transactions attributable to those accounts occurring the previous 12 months. The CFPB proposes to use figures from the prior 12 months because (1) reviewing annualized data would even out any seasonal variations that could occur with a shorter review period; (2) very large financial institutions likely already collect annualized cost and loss data; and (3) reviewing annualized data would require very large financial institutions to make average cost and loss calculations only once per year. When determining the total number of non-covered overdraft transactions occurring the previous 12 months, the financial institution may account for non-covered overdraft transactions that do not incur fees, including those that do not incur fees consistent with fee waiver policies, by excluding from its transaction total any non-covered overdraft transaction for which the financial institution either refunded or did not assess any fee or charge. The CFPB believes that allowing very large financial institutions to adjust their transaction totals to account for overdraft transactions that do not incur fees would give financial institutions flexibility to maintain or to implement fee waiver policies.

Under the proposal, when a very large financial institution applies the breakeven standard either for the first time or after transitioning from the benchmark fee described at proposed § 1026.62(d)(1)(ii), it may include direct costs and charge-off losses from any transaction that was a non-covered overdraft transaction during the prior 12-months even if, applying the breakeven standard, it would have been considered above breakeven overdraft credit during that period. When determining the total number of non-covered overdraft transactions occurring the previous 12 months, a very large financial institution applying the breakeven standard either for the first time or after transitioning from the benchmark fee described at proposed § 1026.62(d)(1)(ii) also may exclude from its transaction total any non-covered overdraft transaction for which the financial institution either refunded or did not assess any fee or charge.

To provide additional guidance regarding the types of costs and charge-off losses a very large financial institution could consider when calculating the breakeven standard, the CFPB also proposes to add a paragraph at § 1026.62(d)(2). Proposed § 1026.62(d)(2) would provide that, when calculating the breakeven standard, a very large financial institution could consider costs and charge-off losses that are specifically traceable to its provision of non-covered overdraft credit in the previous year. The CFPB proposes to allow very large financial institutions to consider only costs and charge-off losses that are specifically traceable to their provision of non-covered overdraft credit to prevent very large financial institutions from employing the breakeven standard in a manner that would circumvent § 1026.62(b)(1). For example, without the specifically traceable restriction, very large financial institutions might include in their average cost and loss calculations costs and charge-off losses that are more appropriately attributable either to other segments of their deposit business or to their deposit business overhead.

Based on its previous experience collecting overdraft cost data from financial institutions, the CFPB has preliminarily determined that specifically traceable costs and charge-off losses would include a very large financial institution's cost of funds for providing non-covered overdraft credit, its charge-off losses for non-covered overdraft credit, and any operational costs that are directly attributable to its non-covered overdraft program. For example, if a very large financial institution uses issue tagging in its call center to reasonably and accurately gauge the number of customer service calls it receives relating to non-covered overdraft credit, direct costs relating to those customer service calls would be specifically traceable and the very large financial institution could include the direct costs relating to those calls in its calculation of costs under the breakeven standard. Conversely, the CFPB preliminarily believes that both general overhead costs and charge-off losses resulting from unauthorized use, EFT errors, billing errors, returned deposit items, or rescinded provisional credit are not specifically traceable to a very large financial institution's provision of non-covered overdraft credit and must not be included in its calculation of costs under the breakeven standard. For example, if a very large financial institution purchases office equipment to support its depository business generally, such costs would not be specifically traceable to its provision of overdraft services and the very large financial institution could not include the cost of such office equipment in its calculation of costs under the breakeven standard.

Under the benchmark fee approach outlined at proposed § 1026.62(d)(1)(ii), a very large financial institution may presume that any charge or combination of charges it imposes for paying a transaction that overdraws an account does not exceed its costs and charge-off losses for providing non-covered overdraft credit if the charge or combination of charges is less than or equal to any benchmark fee established by the CFPB. The CFPB is considering four alternatives for this benchmark fee—$3, $6, $7, and $14. The CFPB views each of these options as potentially viable because, as discussed in additional detail in the following paragraphs, they each apply the calculation method proposed by the breakeven standard to alternative data sets and/or alternative approaches for calculating the total number of non-covered overdraft transactions. (As highlighted at the end of this section, the CFPB seeks comment on each of these alternatives.)

The CFPB requested data, information, and documents from eight financial institutions relating to, among other things, their costs and charge-off losses for providing non-covered overdraft credit in the 2022 calendar year.[169] Each of these eight financial institutions would qualify as very large financial institutions for purposes of

[169] CFPB, *Discretionary Overdraft and NSF Practices at Very Large Financial Institutions* (Jan. 2024), *https://files.consumerfinance.gov/f/documents/cfpb_overdraft-nsf-practices-very-large-financial-institutions_2024-01.pdf* (CFPB 2024 Overdraft NSF Report).

proposed § 1026.62(b)(8) and, collectively, these eight institutions account for over 30 percent of the total assets of very large financial institutions and represent a diverse set of geographic footprints, asset sizes, and business models.[170] The CFPB received data from all eight institutions, but some institutions were unable to provide all the requested data at the level of detail requested.[171] As a result, the CFPB referenced data from five financial institutions to calculate the four alternatives for the proposed benchmark fee.

The CFPB used the same general formula to calculate all four of the proposed alternative benchmark fees but relied on different datapoints to derive each fee amount. To calculate each benchmark fee, the CFPB first determined the total charge-off losses (excluding losses attributable to unauthorized use, billing errors, rescinded provisional credit, returned deposit items, and other sources not attributable to overdraft transactions) for the financial institutions included in its estimate calculation and then divided that figure by the total number of non-covered overdraft transactions (*i.e.,* overdraft transactions currently excepted from Regulation Z) in the relevant dataset for each estimate. Next, the CFPB adjusted this charge-off loss per transaction figure by adding to it $1 per transaction to account for the CFPB's estimate of a financial institution's cost of funds and operational costs, which the CFPB estimates does not exceed $0.50 per transaction each.[172] To calculate the $0.50 cost of funds figure, the CFPB estimated that financial institutions would pay interest of 5 percent per year to obtain funds and would lend an average of $120 to consumers per transaction for a period of one month. The CFPB preliminarily believes that this cost of funds estimate would cover most institutions' costs given that the median overdraft amount per transaction is $50 and that consumers typically repay overdraft transactions within three days.[173] Based on its supervisory and enforcement experience, the CFPB preliminarily believes that call center expenses represent the bulk of the operational costs associated with providing non-covered overdraft programs at very large financial institutions. To calculate the figure for operational costs, the CFPB estimated that 10 percent of non-covered overdraft transactions would require 10 minutes of a customer service representative's time and that 20 percent of these customer service contacts also would require 10 minutes of a supervisor's time.[174] Based on this estimate, the CFPB determined that at an average hourly wage of $21.07 and $30.81 for customer service representatives and supervisors in the financial sector, respectively, financial institutions would incur roughly $0.45 per non-covered overdraft transaction on call center expenses.[175] The CFPB then rounded this figure up to $0.50 to account for other potential operational costs.

To calculate the $3 benchmark fee figure, the CFPB first added together the charge-off losses for the five financial institutions in its sample that produced sufficient data to analyze. Next, the CFPB calculated a charge-off loss per transaction figure by dividing the total charge-off loss figure by the total number of non-covered overdraft transactions paid by those five financial institutions. When tallying the total number of non-covered overdraft transactions for the charge-off loss per transaction figure, the CFPB counted both non-covered overdraft transactions that resulted in an overdraft fee and non-covered overdraft transactions that did not result in an overdraft fee. This approach yielded a charge-off loss per transaction figure of $2 per transaction after rounding to the nearest dollar. The CFPB then added $1 per transaction to this figure to account for the CFPB's estimate of a financial institution's cost of funds and operational costs.

To calculate the $6 benchmark fee figure, the CFPB used the same approach it used to calculate the $3 benchmark fee figure, but changed how it tallied the total number of non-covered overdraft transactions for the charge-off loss per transaction figure. Instead of counting both non-covered overdraft transactions that resulted in an overdraft fee and non-covered overdraft transactions that did not result in an overdraft fee, the CFPB counted only non-covered overdraft transactions that resulted in an overdraft fee. This change increased the charge-off loss per transaction figure to $5 per transaction after rounding to the nearest dollar. The CFPB then added $1 dollar per transaction to this figure to account for the CFPB's estimate of a financial institution's cost of funds and operational costs.

To calculate the $7 benchmark fee figure, the CFPB first identified the financial institution in its sample with the highest charge-off losses. Next, the CFPB calculated a charge-off loss per transaction figure by dividing total charge-off losses by the total number of non-covered overdraft transactions paid by the financial institution. When tallying the total number of non-covered overdraft transactions for the charge-off loss per transaction figure, the CFPB counted both non-covered overdraft transactions that resulted in an overdraft fee and non-covered overdraft transactions that did not result in an overdraft fee. This approach yielded a charge-off loss per transaction figure of $6 per transaction after rounding to the nearest dollar. The CFPB then added $1 dollar per transaction to this figure to account for the CFPB's estimate of a financial institution's cost of funds and operational costs.

To calculate the $14 benchmark fee figure, the CFPB used the same approach it used to calculate the $7 benchmark fee figure (*i.e.,* identifying the financial institution in its sample with the highest charge-off losses) but changed how it tallied the total number of non-covered overdraft transactions for the charge-off loss per transaction figure. Instead of counting both non-covered overdraft transactions that resulted in an overdraft fee and non-covered overdraft transactions that did not result in an overdraft fee, the CFPB only counted non-covered overdraft transactions that resulted in an overdraft fee. This change increased the charge-off loss per transaction figure to approximately $13 per transaction after rounding to the nearest dollar. The CFPB then added $1 dollar per transaction to this figure to account for the CFPB's estimate of a financial institution's cost of funds and operational costs.

In addition to amending § 1026.4(c)(3), the proposed rule also would revise the commentary to § 1026.4(c)(3) by adding proposed comment 4(c)(3)–3. Proposed comment 4(c)(3)–3 would direct readers to see proposed § 1026.4(b)(12) for guidance on when fees imposed on a covered asset account as defined in § 1026.62 are finance charges.

The CFPB seeks comment on all aspects of the proposed amendments to § 1026.4(c)(3) and its commentary and on its proposal to add § 1026.62(b)(1) and (d). In particular, the CFPB seeks comment on the following issues:

[170] *Id.* at 4.

[171] *Id.*

[172] *Id.* at 8–9.

[173] *Id.* at 8.

[174] *Id.* at 9.

[175] U.S. Bureau of Labor Stat., *Occupational Employment and Wage Statistics: May 2022 National Industry-Specific Occupational Employment and Wage Estimates NAICS 5220A1—Credit Intermediation and Related Activities (5221 and 5223 only), https://www.bls.gov/oes/current/naics4_5220A1.htm (last modified Apr. 25, 2023).*

1. Should the CFPB eliminate the § 1026.4(c)(3) exception for very large financial institutions rather than amend its application to above breakeven overdraft credit?

2. What alternative formulae, if any, should the CFPB consider for calculating costs and charge-off losses for the breakeven standard and the proposed alternative benchmark fee? For example, instead of requiring a very large financial institution to calculate its average costs and charge-off losses for non-covered overdraft across its entire depository account portfolio, should the breakeven standard allow a very large financial institution to make separate calculations of its average costs and charge-off losses for non-covered overdraft within subsets of its depository account portfolio, such as account relationship tiers or average account balance ranges?

3. What are the pros and cons of permitting very large financial institutions to adjust their non-covered overdraft transaction totals to account for their fee waiver policies under the breakeven standard described at proposed § 1026.62(d)(1)(i)?

4. What alternative approaches, if any, should the CFPB consider for calculating the breakeven standard described at proposed § 1026.62(d)(1)(i)? For example, should the CFPB consider an approach that allows very large financial institutions to estimate their costs as a flat dollar amount per transaction, as a percentage of their total asset account costs, or as a percentage of losses?

5. What alternative figures should the CFPB consider, if any, for its cost of funds and operational cost estimates?

6. Which of its proposed benchmark fee figures—$3, $6, $7, and $14—should the CFPB adopt? What alternative figures should the CFPB consider, if any?

7. Should the breakeven standard require the same calculation used to calculate the benchmark fee? For example, if the CFPB finalizes a benchmark fee based on all non-covered overdraft transactions, whether or not the very large financial institution collected a fee in connection with the transaction, should the breakeven standard also require the very large financial institution to calculate their costs based on all non-covered overdraft transactions, whether or not the very large financial institution collected a fee in connection with the transaction?

D. Changes to Covered Overdraft Credit Offered by Very Large Financial Institutions

As discussed below, the CFPB is proposing to change requirements that apply to covered overdraft credit offered by a very large financial institution by: (1) requiring covered overdraft credit to be structured as a separate account; (2) applying additional credit card provisions to covered overdraft credit that can be accessed by a hybrid debit-credit card; and (3) applying Regulation E's compulsory-use prohibition to covered overdraft credit. For existing open-end covered overdraft credit products, the proposed new designation as covered overdraft credit accounts would not impose duplicative or additional account opening requirements.

1. Structure of Covered Overdraft Credit (§ 1026.62(c))

The CFPB proposes in § 1026.62(c) to prohibit a very large financial institution from structuring covered overdraft credit as a negative balance on a checking or other transaction account. Conversely, the CFPB proposes to require such institution to structure covered overdraft credit as a separate credit account.

The CFPB has preliminarily determined that this structural prohibition and requirement will make it easier for creditors and consumers to implement and understand, respectively, covered overdraft credit. Regulation Z's open-end credit rules generally address independent credit products that do not have substantial positive (asset) funds associated with them. For example, existing § 1026.11(a) generally provides that creditors must refund any asset balances on a credit account to the consumer within six months.

In contrast, overdraft credit, whether or not subject to Regulation Z's requirements, by its nature involves both consumer assets and consumer credit, the purpose of the latter being to cover shortfalls in the former. In the context of overdraft credit, the CFPB has preliminarily determined that requiring the separation of a consumer's asset balance, such as a checking or other transaction account that is a ''covered asset account'' as defined in proposed § 1026.62(b)(2), from the consumer's credit balance, such as a credit account that is a ''covered overdraft credit account'' as defined in proposed § 1026.62(b)(4), is an appropriate addition to Regulation Z under its TILA section 105(a) authority, as it is necessary or proper to facilitate creditor compliance and to effectuate the purposes of TILA by helping to avoid the uninformed use of credit and protecting consumers against inaccurate and unfair credit billing and credit card practices. Existing § 1026.61(b), which was established by the Bureau's 2016 Prepaid Final Rule, similarly prohibits credit accounts tied to prepaid accounts from being structured as negative balances on the prepaid accounts and requires that the prepaid account and the tied credit account be separate.[176] Further, commenters that addressed this aspect of the Bureau's 2014 prepaid accounts proposed rule universally supported the separate asset account and credit account structure that the 2016 rule adopted.[177]

In the context of overdraft credit that is not subject to Regulation Z's requirements, financial institutions today typically provide overdraft credit to consumers through negative balances on consumers' asset accounts. That is, institutions typically provide one account to a consumer, which is regulated as an asset account such as a checking or other transaction account, with an asset balance being a positive balance in the account and an overdraft credit balance being a negative balance in the account. Further, institutions typically obtain repayment of a consumer's negative overdraft credit balance by immediately taking any incoming deposit to the asset account, such as an electronic direct deposit, as repayment (or ''offset'') of the account's negative balance. For example, if a consumer's asset account balance is a negative $100 overdraft credit balance and an institution receives a $150 electronic direct deposit which is to be credited to the consumer's account, the institution immediately takes the first $100 of the electronic deposit to repay the consumer's overdraft credit balance, such that the consumer's account balance subsequent to the institution's receipt of the electronic direct deposit is a positive asset balance of $50.

This practice by institutions of immediately taking incoming deposits as repayment of overdrafts is known as ''offset.'' Regulation Z generally prohibits offset in connection with covered overdraft credit, as defined in proposed 1026.62(b)(3), which can typically be accessed by a ''credit card'' as defined in 1026.2(a)(15).[178] That is, the institution providing the covered overdraft credit is generally prohibited from immediately taking funds from

[176] *See* 12 CFR 1026.61(b).

[177] *See* 81 FR 83934, 84264 (Nov. 22, 2016).

[178] *See* TILA section 169(a) (15 U.S.C. 1666h(a)) and 12 CFR 1026.12(d)(1).

incoming deposits in repayment of consumers' outstanding overdraft credit balances. Thus, continuing the above example of an outstanding overdraft credit balance of $100, when Regulation Z applies and the institution receives a $150 deposit to be credited to the consumer's account, the institution is prohibited from immediately taking the funds of the incoming deposit, but must instead credit the funds to the consumer's asset account and give the consumer the use of the funds. In other words, when Regulation Z applies, the regulation's offset prohibition requires that the institution make it such that the consumer has *both* an overdraft credit balance of $100 (the money the consumer continues to owe the institution) and an asset balance of $150 (the money from the incoming deposit) at the same time.[179]

Accordingly, the CFPB has preliminarily determined that the proposed requirement in § 1026.62(c) to structure covered overdraft credit as a separate credit account that is separate from the checking or other transaction account will enable institutions to comply with the TILA and Regulation Z offset prohibition. Specifically, the CFPB has preliminarily determined that that proposed requirement would facilitate compliance with the TILA and Regulation Z offset prohibition by requiring an institution to retain at the same time both an outstanding overdraft credit balance and an outstanding asset balance for a consumer. Conversely, the CFPB has preliminarily determined that it is difficult or impossible for an institution to maintain both an asset (positive) balance and a credit (negative) balance at the same time for a consumer within a single asset account and that it is therefore difficult or impossible for the institution to provide overdraft credit to the consumer in a manner that complies with Regulation Z without providing the consumer with an asset account and a credit account that are separate from each other.

In addition, the CFPB has preliminarily determined that the proposed requirement to structure covered overdraft credit as a separate credit account would (1) protect consumers against inaccurate and unfair credit billing and credit card practices by enabling them to exercise control over their funds and (2) avoid the uninformed use of credit by enabling consumers to better understand their asset and credit balances. With respect to protecting consumers by enabling them to control their funds, the requirement will facilitate consumers' ability to control incoming deposits to their accounts and use them for purposes other than immediately repaying an overdraft balance, as the offset prohibition requires institutions to permit consumers to do. For example, continuing the example above, rather than the institution immediately using the incoming $150 electronic direct deposit to eliminate the $100 negative overdraft balance in the single account, under the proposed separate-account structure the consumer might use the electronically deposited funds to pay a phone or electric bill and to retain the unpaid $100 balance in the separate credit account (*i.e.,* to repay the credit balance to the institution at a later time).

With respect to avoiding the uninformed use of credit by enabling consumers to understand their asset and credit balances, the requirement for separate accounts will enable consumers to better monitor their account balances and trace how their funds are being used through the better disclosures (*e.g.,* entries on periodic statements) that institutions will provide to consumers in compliance with Regulations E and DD for asset accounts and in compliance with Regulation Z, which effectuates the informed use of credit, for the credit accounts. Continuing the above example of a $150 incoming deposit and $100 overdraft balance, with a separate asset account and credit account (as would be required by proposed § 1026.62(c)), the consumer whose asset account receives an electronic direct deposit would see disclosed on the periodic statements a $150 credit entry to the asset account and, at that time, a $150 balance in the asset account and a $100 balance in the credit account.

Further, if the consumer were to subsequently choose to use the $150 asset funds to repay the overdraft, the consumer would at that later point in time see on the statements the following data points on the asset account and credit account: (1) a debit entry of $100 to the asset account for repayment of the overdraft credit balance, (2) a resulting balance in the asset account of $50, (3) a credit entry of $100 to the credit account, and (4) a resulting balance in the credit account of $0. In contrast, *without* the separate credit account, where overdrafts are represented as negative balances on the asset account, the same consumer would see disclosed only the following: a $150 credit to the asset account for the incoming electronic deposit and a resulting balance of $50 in the asset account. The CFPB has preliminarily determined that this latter approach may result in the uninformed use of credit by the consumer, because the consumer may not readily appreciate how the credit and asset aspects of their asset account have interacted. The CFPB has therefore also preliminarily determined that the former approach of requiring that the asset account and the credit account be separate from each other—and the better periodic-statement disclosures that necessarily accompany that approach—will help avoid the uninformed use of credit by the consumer.

Credit account opening. Opening an open-end consumer credit plan, such as a covered overdraft credit account, that is subject to Regulation Z may trigger certain requirements and protections, including account opening disclosures pursuant to §§ 1026.5 and 1026.6 and, if a credit card is involved, ability to pay requirements in § 1026.51 and fee limitations in § 1026.52(a). Consistent with existing requirements, for purposes of determining compliance with provisions of Regulation Z that are tied to credit account opening, an account opening with respect to covered overdraft credit occurs on the date a consumer may first engage in a transaction for which covered overdraft credit can be extended under the account.

If the CFPB finalizes the rule as proposed, very large financial institutions that offer overdraft services on existing accounts may need to take steps to come into compliance with Regulation Z. For example, assume that prior to the effective date of this proposed rule, a very large financial institution through negative balances on a deposit account provides above breakeven overdraft credit that is not subject to Regulation Z to a consumer, and assume further that the institution seeks to continue to provide above breakeven overdraft credit to the consumer subsequent to the effective date of the proposed rule. After the proposed rule's effective date, such above breakeven overdraft credit would be covered overdraft credit, and proposed § 1026.62(c) of the proposed rule (discussed in the preceding paragraphs) would require the institution to provide the covered overdraft credit to the consumer through a separate covered overdraft credit account. Therefore, to provide above

[179] While TILA and Regulation Z prohibit offset, the statute and regulation do permit periodic deductions pursuant to the consumer's written agreement. *See* 12 CFR 1026.12(d)(3). These periodic deductions must occur at regular intervals and therefore cannot occur immediately whenever deposit funds are received to be credited to the consumer's account. Thus, the permissibility of periodic deductions does not change the requirement that the institution make it such that the consumer has both an overdraft credit balance of $100 and an asset balance of $150 at the same time.

breakeven, covered overdraft credit to the consumer subsequent to the effective date of this proposed rule, the institution would need to open a covered overdraft credit account for the consumer. Further, the institution would be required by § 1026.5(b)(1)(i) to provide to credit account opening disclosures to the consumer for the covered overdraft credit account before the consumer makes the first transaction under the covered overdraft credit plan. This is so regardless of whether there was any change in the terms or conditions of the previously existing deposit account under which the above breakeven non-covered overdraft credit was previously extended.[180]

Disclosure requirements. Subsequent to the effective date of the CFPB's proposed rule, when a very large financial institution seeks to provide above breakeven overdraft credit to a consumer through a covered overdraft credit account, the institution will need to comply with the existing disclosure requirements in Regulation Z. The CFPB seeks comment on whether any specific disclosure requirements should be clarified and on whether any adjustments should be made to existing disclosure requirements to help better promote the informed use of covered overdraft credit.

Credit subaccounts. Like the CFPB's current proposal, section 1026.61(b), established by the CFPB's 2016 Prepaid Final Rule, prohibits a covered separate credit feature from being structured as a negative balance on a prepaid account. Section 1026.61(b) requires that the covered credit feature be provided ''as a separate credit feature, either as a separate credit account, or as a credit subaccount of a prepaid account that is separate from the asset feature of the prepaid account.'' Further, comment 61(b)–1 requires that ''the credit feature [] be set up as a separate balance on the prepaid account such that there are at least two balances on the prepaid account—the asset account balance and the credit account balance.''

In light of these requirements that the prepaid accounts rule attaches to covered credit subaccounts tied to prepaid asset accounts (*i.e.,* the same requirements that it attaches to covered credit accounts tied to prepaid asset accounts) the CFPB has preliminarily determined that there would be no meaningful distinction between a covered overdraft credit account tied to a covered asset account and a covered overdraft credit subaccount tied to a covered asset account. For clarity in this regard, proposed § 1026.62(b)(4) would establish that a credit subaccount is a type of covered overdraft credit account. Nonetheless, the CFPB seeks comment on whether any distinctions should be made between covered overdraft credit subaccounts and other types of covered overdraft credit accounts. The CFPB also seeks comment on whether any additional requirements should be adopted to specify how covered overdraft credit accounts should be disclosed to consumers.

Existing overdraft lines of credit. Many very large financial institutions currently provide overdraft lines of credit subject to Regulation Z. Subsequent to the effective date of the CFPB's proposed rule, these lines of credit would be covered overdraft credit accounts, regardless of whether they are above or below breakeven pricing. However, under the proposed rule the institution would not be opening a new credit account (*i.e.,* would not be newly opening an account that is subject to Regulation Z) because a credit account—the overdraft line of credit—already existed prior to the effective date of the proposed rule. Thus, Regulation Z requirements triggered by credit-account opening (such as §§ 1026.5, 1026.6, 1026.51, and § 1026.52(a) mentioned above) would not apply to these previously existing overdraft lines of credit. However, other Regulation Z requirements such as change-in-terms requirements would continue to apply to them. Further, as discussed under proposed § 1026.4(b)(2) and (12), fees for transferring funds from the overdraft line of credit to the tied deposit account, which are currently excepted from being finance charges under Regulation Z, would be finance charges under the CFPB's proposed changes to § 1026.4(b)(2) and (12). Accordingly, very large financial institutions may need to provide change-in-terms notices in connection with many of the overdraft lines of credit that they currently provide. The CFPB seeks comment on whether additional guidance would be helpful for understanding the disclosure and other requirements that under the proposed rule would be applicable to very large financial institutions in these circumstances. If so, what examples should be addressed and added?

2. Credit Card Changes

Credit cards and card issuers are generally subject to additional requirements in Regulation Z. The requirements that apply generally depend on whether the credit account can be accessed by a ''credit card,'' ''credit card account under an open-end (not home-secured) consumer credit plan,'' or ''charge card'' under Regulation Z. Currently, a covered overdraft credit account that can be accessed by a debit card or other device that qualifies as a credit card (including certain account numbers) is subject to some Regulation Z requirements that apply to ''credit cards.'' Such covered overdraft credit is not subject to requirements that apply to a ''credit card account under an open-end (not home-secured) consumer credit plan.'' It is also specifically excepted from some of the requirements that apply to ''credit cards.'' As discussed in more detail below, the CFPB is proposing to apply all credit card provisions generally to covered overdraft credit accounts if the credit can be accessed by a hybrid debit-credit card, as defined in this proposal, such as a debit card offered by a very large financial institution.

i. Applying CARD Act Provisions of Regulation Z to Covered Overdraft Credit

The CFPB is proposing to subject all covered overdraft credit to the CARD Act provisions of Regulation Z in subparts G and B (the CARD Act provisions) if that credit is (1) open-end credit; (2) accessible by a credit card; and (3) offered by a very large financial institution. Currently, covered overdraft credit accessible by a debit card is considered a credit card under Regulation Z and generally is subject to the Regulation Z provisions that apply to credit cards, but, because of two non-statutory exceptions, such overdraft credit is not subject to the CARD Act provisions.[181] The proposal would

[180] The only change in the terms of the previously existing deposit account that would be required by the CFPB's proposed rule would be a reduction in the dollar amount of the overdraft fee the institution charges for negative-balance (non-covered) overdraft. Because that changed term would be a change in the consumer's favor, a change-in-terms notice would not be required in advance of the change. *See* Regulation E § 1005.8(a)(1) and Regulation DD § 1030.5(a)(1).

[181] 12 CFR 1026.2(a)(15)(i), (iv) and comment 2(a)(15)–2.i.B. Non-covered overdraft credit is not subject to Regulation Z, which includes the provisions applicable generally to credit cards and the provisions implementing the CARD Act, because (1) it is not subject to a finance charge or repayable by a written agreement in more than four installments and (2) a debit card that can access non-covered overdraft credit is not considered a credit card because, as current comment 2(a)(15)–2.ii.A explains, a debit card with no credit feature or agreement is not a credit card even if the creditor occasionally honors an inadvertent overdraft. As discussed in the changes to the definition of finance charge section above, the CFPB is proposing to amend the definition of ''finance charge'' to expand the scope of covered overdraft credit, such that certain overdraft credit that is currently non-covered overdraft credit would be considered covered overdraft credit if this proposal is finalized

subject such credit to the CARD Act provisions when it is offered by very large financial institutions. To implement these changes, the proposal would add a new definition of ''hybrid debit-credit card,'' amend the definitions of ''credit card'' and ''credit card account under an open-end (not home-secured) consumer credit plan,'' and make other clarifying changes to the rule text and associated commentary.

The CARD Act and Overdraft

The CARD Act amended TILA to institute new substantive and disclosure requirements to establish fair and transparent practices for open-end consumer credit card plans. The CARD Act addressed multiple aspects of the credit card market, regulating, among other things, rate increases, the imposition of penalty fees, the timing of payments, the issuance of subprime credit cards, ability to pay assessments, the specifics of certain credit card disclosures, the marketing of credit reports, and the marketing of credit cards to young consumers.[182] These provisions indicate that Congress was particularly concerned with protecting vulnerable populations of consumers—like students and individuals with subprime credit—and with regulating high-cost consumer credit card products subject to burdensome fees.[183]

The statutory language of the CARD Act applies the protections broadly to credit card products that can access open-end consumer credit. The CARD Act generally applies to any ''credit card account under an open-end consumer credit plan.'' Absent two non-statutory exceptions, this broad language generally would apply to open-end covered overdraft credit that is accessed by a credit card, including a debit card.

The Board implemented this statutory language in Regulation Z in 2010 through the term ''credit card account under an open-end (not home-secured) consumer credit plan.'' [184] That term is defined in current § 1026.2(a)(15)(ii) to generally mean an open-end credit account that is accessed by a credit card. The Board then used the term ''credit card account under an open-end (not home-secured) consumer credit plan'' in provisions of Regulation Z in subpart G and subpart B that were promulgated or amended to implement the CARD Act. Like the statutory definition, absent non-statutory exceptions, this regulatory definition would be broad enough so that the CARD Act provisions generally would apply to covered overdraft credit that is accessed by a credit card, including a debit card.

However, overdraft lines of credit are not subject to the CARD Act provisions in subpart G and subpart B that apply to a ''credit card account under an open-end (not home-secured) consumer credit plan'' because the Board adopted two exceptions that exclude overdraft lines of credit from that definition. Current § 1026.2(a)(15)(ii)(B) and (C), respectively, except from this definition (1) an overdraft line of credit that is accessed by a debit card; and (2) an overdraft line of credit that is accessed by an account number other than an account number that is a hybrid prepaid-credit card and that can access a covered separate credit feature as defined in § 1026.61. Although Regulation Z does not define ''overdraft line of credit,'' the term is generally understood to refer to an open-end credit product tied to an asset account. Funds are advanced from the credit product to pay for a withdrawal when the consumer withdraws more money than they have in the asset account.

Aside from the CARD Act provisions in subpart G and subpart B, currently these overdraft line of credit products are generally subject to Regulation Z's open-end credit rules when the fees and other charges imposed on this product are finance charges.[185] To the extent these overdraft line of credit products can be accessed by a debit card or other single credit device, they are thus also a ''credit card'' and are generally subject to provisions in Regulation Z that apply to a ''credit card.'' [186]

The Board acknowledged in its February 2010 Rule that it believed that, as a general matter, Congress intended the CARD Act to apply broadly to products that meet the definition of a credit card.[187] The Board also acknowledged that a debit card that accesses an overdraft line of credit is a ''credit card.'' [188]

Nevertheless, the Board relied on its authority under TILA section 105(a) and section 2 of the CARD Act to create two exceptions for overdraft lines of credit, including one for debit cards that can access an overdraft line of credit. As a result of the exceptions, such accounts are not subject to the various CARD Act provisions in subpart G and subpart B, as discussed below, that apply to a ''credit card account under an open-end (not home-secured) consumer credit plan.'' In creating the exceptions, the Board stated that, at the time, Regulation Z-covered overdraft lines of credit were not in wide use and that, as a general matter, creditors who offered overdraft lines of credit did not engage in some of the practices regulated by the CARD Act provisions with respect to those products.[189] The Board cited three examples of practices regulated by the CARD Act that were not currently present in the market: (1) increasing annual percentage rates, (2) applying different rates to different balances, and (3) allowing grace periods before charging interest. The Board did not specifically address other provisions, such as limitations on penalty fees and the requirement to assess ability to pay, which may have had an impact on practices involving overdraft lines of credit. Because of its assessment that the small market for overdraft lines of credit did not present substantial consumer protection concerns similar to those addressed by the CARD Act, the Board concluded that ''alternative forms of regulation'' such as Regulation E were ''better suited'' to protect consumers from harm with respect to those products.[190]

The CFPB is proposing to amend the non-statutory overdraft-related exceptions so that a very large financial institution that offers open-end covered overdraft credit that can be accessed by a ''credit card'' must comply with provisions that apply to a ''credit card account under an open-end (not home-secured) consumer credit plan.'' As a result, open-end covered overdraft credit that can be accessed by a ''credit card,'' including a debit card, would be

as proposed. This newly covered overdraft credit generally would be subject to the Regulation Z provisions applicable to credit cards if the covered overdraft credit can be accessed by a credit card. However, without further changes, the non-statutory exceptions that exclude covered overdraft from being subject to the CARD Act provisions would prevent covered overdraft credit, including newly covered overdraft credit, from being subject to the CARD Act provisions. As discussed in this section, the CFPB is proposing to update these non-statutory exceptions, which would subject certain covered overdraft credit, including certain newly covered overdraft credit, to the CARD Act provisions.

182 *See* CARD Act sections 101, 102, 105, 106, 109, 201, 301.

183 *See* CARD Act sections 102, 105, 109, 301.

184 *See* 75 FR 7658, 7663–65 (Feb. 22, 2010). The Board first implemented the statutory term ''credit card account under an open-end consumer credit plan'' in its July 2009 interim final rule, which, in relevant part, exempted home equity lines of credit from certain requirements of the CARD Act. 74 FR 36077, 36083 (July 22, 2009). The Board added the new term ''credit card account under an open-end (not home-secured) consumer credit plan'' in its 2010 final rule.

185 *See* 12 CFR 1026.4. The current overdraft-related exception in 12 CFR 1026.4(c)(3), which the CFPB is proposing to narrow in this rulemaking, does not apply to overdraft products where ''the payment of [overdrawing] items and the imposition of the charge were previously agreed upon in writing.''

186 *See* Regulation Z comment 2(a)(15)–2.i.B.

187 *See* 75 FR 7658, 7664 (Feb. 22, 2010).

188 *Id.*

189 *Id.* at 7665.

190 *Id.*

subject to the CARD Act provisions in subpart G and subpart B if it is offered by a very large financial institution. This would include existing covered overdraft credit (currently commonly referred to as ''overdraft lines of credit'') and overdraft credit that would become covered overdraft credit, such as above breakeven overdraft credit, if the rule is finalized.

The CFPB has preliminarily determined that the exceptions are no longer appropriate. While the Board created those exceptions based on the understanding that overdraft lines of credit were not in ''wide use'' at the time and did not include features common to other credit cards, the CFPB has preliminarily determined that the prevalence or nature of a particular type of credit card should not render it beyond the scope of the CARD Act. By its plain terms, the CARD Act applies to all ''credit card account[s] under an open-end consumer credit plan,'' which, as noted above, would include open-end overdraft credit accessible by a credit card. In any event, the CFPB anticipates that the market for covered overdraft credit could react to the proposed changes in this rulemaking, if finalized, in several ways, including by offering covered overdraft credit to many consumers who currently receive non-covered overdraft credit, including subprime consumers.

Very large financial institutions could also react to the proposed changes by offering different terms on covered overdraft credit than those that have historically been offered. For example, financial institutions could start marketing covered overdraft credit as a long-term credit solution and could begin imposing different rates on different balances. In addition, consistent with the current non-covered overdraft credit market, financial institutions could allow for grace periods before imposing finance charges. Similarly, other protections, such as the requirement to assess ability to pay, the fee limitations provision, and the limits on penalty fees, may become even more important if covered overdraft credit is offered to more subprime consumers.

The CFPB also has preliminarily determined that the CARD Act provisions would provide important consumer protections to those consumers most likely to use covered overdraft credit accounts. Today, a small subset of consumers (approximately 10 percent of consumers), whom the CFPB has in the past referred to as ''frequent overdrafters,'' incur most overdraft fees. In light of the CFPB's proposed treatment of the overdraft fee that a very large financial institution may charge for non-covered overdraft, the CFPB expects that some very large financial institutions will have reduced incentives to provide non-covered overdraft credit to the subprime consumers who are frequent overdrafters and today incur the preponderance of overdraft fees. Instead of providing these consumers with non-covered overdraft credit, some very large financial institutions may provide these consumers with covered overdraft credit accounts—the accounts to which the CFPB is proposing to apply the CARD Act provisions—which would allow them the flexibility to charge more than the threshold that cannot be exceeded to remain non-covered overdraft credit.

The CFPB also has preliminarily determined that applying the CARD Act provisions as proposed could provide important benefits to subprime consumers. Many of the provisions of the CARD Act target credit card practices affecting subprime consumers. To the extent that some financial institutions would offer covered overdraft credit to more subprime consumers if the proposed rule were adopted, these CARD Act provisions would offer additional protections to consumers with a debit card that accesses overdraft credit. This will result in a consumer who uses a debit card to access overdraft credit—who often is a subprime consumer—receiving the same protections that a subprime credit card consumer receives today, consistent with the broad statutory language in the CARD Act.

To prevent the market for Regulation Z-covered overdraft from posing consumer risks after the rule goes into effect, and to carry out the purposes of TILA by promoting the informed use of credit and protecting consumers against unfair credit card practices pursuant to TILA section 105(a), and to carry out the CARD Act pursuant to section 2 of the CARD Act, the CFPB is proposing to subject covered overdraft credit to the CARD Act provisions in subpart G and subpart B when such credit can be accessed by a credit card and is offered by a very large financial institution. This would revise non-statutory exceptions so that Regulation Z's coverage more closely aligns with the plain language of the CARD Act.

The CFPB invites comment on the proposal to subject covered overdraft credit to the CARD Act provisions in subpart G and subpart B. In particular, the CFPB seeks comment on potential impacts of a finalized rule, if any, on the market for covered overdraft credit and the resulting effects of market changes on consumers. The CFPB also seeks comment on the costs and benefits to these consumers of the CARD Act protections in subpart G and subpart B. The CFPB also requests comment on whether clarification is needed or whether there are operational challenges regarding the application of specific CARD Act provisions to covered overdraft credit. The CFPB also seeks comment on what, if any, operational costs might arise as a result.

The proposed rule would subject all covered overdraft credit to the CARD Act provisions in subparts G and B if that credit is (1) open-end credit; (2) accessible by a credit card; and (3) offered by a very large financial institution. The proposed rule would also add a new definition of ''hybrid debit-credit card,'' and amend the definitions of ''credit card,'' and ''credit card account under an open-end (not home-secured) consumer credit plan.'' The proposal would also make other clarifying changes to the rule text and associated commentary. These technical and clarifying changes are discussed in more detail below.

Hybrid Debit-Credit Card (§ 1026.62(b)(5))

In proposed § 1026.62(b)(5), the CFPB is proposing to define the new term ''hybrid debit-credit card'' for clarity and ease of reference. The CFPB proposes to define ''hybrid debit-credit card'' to mean any card, plate, or other single credit device that a consumer may use to obtain covered overdraft credit from a very large financial institution. This proposed definition describes a type of credit card that has two defining characteristics: (1) the credit card must be able to access covered overdraft credit; and (2) the covered overdraft credit must be offered by a very large financial institution. This definition would include, for example, a debit card that a consumer can use to complete transactions using funds drawn from an asset account held at a very large financial institution when that device can also be used to access covered overdraft credit.

Credit Card (§ 1026.2(a)(15)(i))

TILA defines ''credit card'' as ''any card, plate, coupon book or other credit device existing for the purpose of obtaining money, property, labor, or services on credit.'' [191] Section 1026.2(a)(15)(i) defines credit card as ''any card, plate, or other single credit device that may be used from time to time to obtain credit,'' which includes

[191] 15 U.S.C. 1602(l).

''a hybrid prepaid-credit card as defined in § 1026.61.'' The CFPB is proposing to amend the definition of ''credit card'' to clarify what is and is not a credit card when certain credit devices can access covered overdraft credit. These amendments would clarify that when a debit card can access covered overdraft credit, the debit card would be a credit card subject to the CARD Act provisions.

First, the CFPB is proposing various non-substantive wording revisions in § 1026.2(a)(15)(i) to clarify that a debit card that can access a covered overdraft credit account is a credit card. These changes are non-substantive because, under Regulation Z today, a debit card that can access an overdraft line of credit is a credit card.[192] Nonetheless, to make this fact—that a debit card that can access covered overdraft credit is a credit card—as clear as possible, the CFPB is proposing two textual changes for clarity. First, in § 1026.62, the CFPB proposes to define a ''hybrid debit-credit card'' as any card (including a debit card) that can access covered overdraft credit offered by a very large financial institution. Second, the CFPB proposes to amend § 1026.2(a)(15)(i) to explain that the definition of ''credit card'' includes a hybrid debit-credit card. Thus, under the proposal, a debit card that can access a covered overdraft credit account is a hybrid debit-credit card, a hybrid debit-credit card is a credit card, and a debit card that can access a covered overdraft credit account is a credit card. This is not a substantive change from the extant regulation because, as noted, under the extant regulation a debit card that can access an overdraft line of credit is a credit card.

Similarly, the CFPB is proposing to revise comment 2(a)(15)–2.i.B to clarify that a hybrid debit-credit card is a type of debit card that also accesses a credit account, such as a covered overdraft credit account.

To further clarify what is and is not a ''credit card'' in light of proposed definitions and proposed changes to the definition of ''finance charge,'' the CFPB is also proposing to amend several examples in the commentary to § 1026.2(a)(15)(i) and (ii). In comment 2(a)(15)–2.i.A, the CFPB is proposing to replace the undefined term ''overdraft line of credit'' with a new proposed term ''covered overdraft credit.'' In comment 2(a)(15)–2.ii.C, the CFPB is proposing amendments to clarify that an account number is a credit card when it can access covered overdraft credit if the account number can use the credit accessed to purchase goods and services.

The CFPB is also proposing to amend comment 2(a)(15)–2.ii.A and add comment 2(a)(15)–2.ii.E to ensure that the examples of what is not a credit card clarify that allowing a card, plate, or other single credit device to access non-covered overdraft credit does not trigger Regulation Z's credit card requirements. As explained in current § 1026.1(c)(2), where a credit card is involved, certain provisions of Regulation Z apply even if the credit is not subject to a finance charge or is not payable by a written agreement in more than four installments. However, comment 2(a)(15)–2.ii.A clarifies that a check-guarantee or debit card with no credit feature or agreement is not a credit card ''even if the creditor occasionally honors an inadvertent overdraft.'' In other words, a financial institution that allows a debit card or check-guarantee card to access non-covered overdraft—including overdraft where the financial institution does not impose a ''finance charge,'' either because it does not impose a fee or because any fee charged is not considered a finance charge under § 1026.4(c)(3)—does not have to comply with Regulation Z's credit card provisions, even though such cards would otherwise meet the definition of ''credit card.'' As discussed above, currently, § 1026.4(c)(3) provides that overdraft charges are not finance charges if the payment of such items and the imposition of the charge were not previously agreed upon in writing. Thus, financial institutions may pay an inadvertent overdraft and charge for it without complying with Regulation Z as long as the payment of the overdraft and associated charges are consistent with the provision. The CFPB is proposing to modify the exception from the definition of finance charge in § 1026.4(c)(3) so that certain overdraft-related charges are finance charges even if the financial institution does not agree in advance to pay the items. If finalized, some charges for paying overdrafts that may otherwise be characterized as occasional or inadvertent would be considered finance charges. To ensure the commentary aligns with the exception in § 1026.4(c)(3) and clarify that allowing a consumer to access non-covered overdraft credit using a debit card does not trigger credit card requirements in Regulation Z, the CFPB is proposing to: (1) amend comment 2(a)(15)–2.ii.A by deleting the phrase ''even if the creditor occasionally honors an inadvertent overdraft;'' and (2) add comment 2(a)(15)–2.ii.E to clarify that a check-guarantee or debit card that can only access non-covered overdraft credit is not a ''credit card''.

Credit Card Account Under an Open-End (Not Home-Secured) Consumer Credit Plan (§ 1026.2(a)(15)(ii))

The CFPB is proposing to amend the definition of ''credit card account under an open-end (not home-secured) consumer credit plan'' in § 1026.2(a)(15)(ii) by narrowing the two overdraft-related exceptions so that open-end covered overdraft credit offered by a very large financial institution would no longer be excepted from the definition of a ''credit card account under an open-end (not home-secured) consumer credit plan.'' Such credit offered by a very large financial institution would be subject to the CARD Act provisions in subpart G and subpart B.

Discussion of the Effect of Applying Regulation Z's CARD Act Provisions to Covered Overdraft Credit Accounts Accessed by a Hybrid Debit-Credit Card

These changes would subject all covered overdraft credit to the CARD Act provisions in subparts G and B if that credit is accessible by a credit card and offered by a very large financial institution.

The CARD Act provisions that the CFPB is proposing to apply to hybrid debit-credit cards include the following:

- The requirement in § 1026.51 to assess the consumer's ability to pay the credit extended, such as covered overdraft credit, including special rules regarding the extension of credit to persons under the age of 21. This may provide an incentive for institutions to structure and price covered overdraft credit such that consumers are better able to repay it, relative to current non-covered overdraft credit.
- The restriction in § 1026.52(a) on the amount of certain fees, such as overdraft fees, that an issuer can charge during the first year after opening of a credit account, such as a covered overdraft credit account, to 25 percent of the credit limit. This restriction does not apply to charges assessed as periodic rates. This may provide an incentive for institutions to reduce or eliminate flat fees for overdraft and to instead apply periodic rates that must be disclosed as APRs. The CFPB has preliminarily determined that this change in the manner and disclosure of overdraft credit pricing would improve consumers' ability to understand the price of the credit, and to compare it to

[192] *See* current Regulation Z comment 1026.2(a)(15)–2.i.B (stating that examples of credit cards include a debit card that also accesses a credit account).

the pricing of other forms of credit that consumers might wish to consider.

- The limit in § 1026.52(b)(1) on the amount card issuers can charge for ''back-end'' penalty fees, such as when a consumer makes a late payment or exceeds their credit limit. This may provide an incentive for institutions to rely more on non-penalty charges that are disclosed as part of the upfront price of the covered overdraft credit.
- The prohibition in § 1026.52(b)(2) on ''declined transaction fees'' and other penalty fees where there is no cost to the card issuer associated with the violation of the account agreement. As discussed below, applying this provision to a covered overdraft credit account accessed by a hybrid debit-credit card would prohibit declined debit card transaction fees on accounts with a covered overdraft credit account accessed by a hybrid debit-credit card. This provision would also prohibit declined ACH transaction fees where the card issuer declines an attempted ACH payment and would otherwise impose a fee on the cardholder for doing so. Consistent with comment 52(b)(2)(i)–4, this provision would permit a card issuer to impose a fee for declining a check that attempts to access a covered overdraft credit account because such a check is ''a check that accesses a credit card account.'' Such a fee would still be limited by § 1026.52(b)(1). The CFPB has preliminarily determined that this prohibition on declined transaction fees limit could lead institutions to shift away from back-end fees and toward upfront pricing in the form of periodic rates disclosed as APRs.
- The provisions in § 1026.53 regarding how a card issuer must allocate payments in excess of the minimum periodic payment.
- The limitation in § 1026.54 on card issuers imposing a finance charge as a result of the loss of a grace period.
- The prohibition in § 1026.55 on increases in any APR, fee, or finance charge applicable to any outstanding balance on a credit card account, with exceptions where advance notice is provided, with a requirement that the promotional rate generally cannot expire earlier than six months, and the requirement in § 1026.59 that card issuers reevaluate rate increases.
- The restriction in § 1026.56 on fees for over-the-limit transactions to one per billing cycle and the requirement that the consumer opt-in to payment of such transactions in order for the fee to be charged.
- The requirement in § 1026.57 that institutions of higher education publicly disclose agreements with card issuers and limit the marketing of credit cards on or near college campuses.
- The requirement in § 1026.58 that card issuers submit credit card agreements to the CFPB on a quarterly basis.

This proposal would also require very large financial institutions to comply with the following CARD Act-derived disclosure-related requirements in subpart B with respect to covered overdraft credit accounts accessed by a hybrid debit-credit card:

- The timing requirements in § 1026.5(b)(2)(ii)(A) for disclosures sent with respect to a credit card account under an open-end (not home-secured) consumer credit plan.
- The rate-disclosure requirements in § 1026.6(b)(2)(i)(F) for account-opening statements specific to a credit card account under an open-end (not home-secured) consumer credit plan.
- The due date disclosure, repayment disclosure, and format requirements for periodic statements specific to a credit card account under an open-end (not home-secured) consumer credit plan in § 1026.7(b)(11)(i), (b)(12)(i), (b)(13).
- The subsequent disclosure requirements specific to a credit card account under an open-end (not home-secured) consumer credit plan in § 1026.9(c)(2)(iv)(A)(8), (c)(2)(iv)(B)–(C), (g)(3)(i)(A)(*6*), (g)(3)(i)(B), (h).
- The payments-related requirements specific to a credit card account under an open-end (not home secured) consumer credit plan in § 1026.10(b)(3), (e).
- The requirements in § 1026.11(c)(1)(i) related to the timely settlement of estate debts for a credit card account under an open-end (not home-secured) consumer credit plan.

In addition to the proposed amendments to the definition of ''credit card'' and ''credit card account under an open-end (not home-secured) consumer credit plan,'' the CFPB is also proposing conforming and clarifying changes to the commentary for §§ 1026.55 and 1026.57 to reflect the changes discussed in this section. In particular, the CFPB is proposing to add comment 55(a)–5 to clarify that the limitations on increasing annual percentage rates, fees, and charges apply to fees imposed in connection with covered overdraft credit whether those fees are imposed on the covered overdraft credit account or the associated covered asset account. Finally, the CFPB is proposing to amend comment 57(a)(1)–1 so that it would continue to accurately reflect the exceptions from the definition of credit card issued under a credit card account under an open-end (not home-secured) consumer credit plan if changes to that definition are finalized as proposed.

Limitations on Penalty Fees

Among the CARD Act provisions discussed above, one of them, § 1026.52(b), raises complex policy considerations that the CFPB believes are important to address in more detail. Section 1026.52(b) regulates the imposition of penalty fees on a credit card account under an open-end (not home secured) consumer credit plan. TILA refers to a ''penalty fee'' as a fee imposed ''in connection with any omission with respect to, or violation of, the cardholder agreement,'' and it permits only a penalty fee that is ''reasonable and proportional to the amount of such omission or violation.'' [193] Consistent with this statutory language, Regulation Z defines a ''penalty fee'' as ''any charge imposed by a card issuer based on an act or omission that violates the terms of the account or any other requirements imposed by the card issuer with respect to the account, other than charges attributable to periodic interest rates.'' [194] Section 1026.52(b)(1) permits a card issuer to impose a penalty fee as long as that fee represents a ''reasonable proportion of the total costs incurred by the card issuer as a result of that type of violation'' or complies with dollar amounts specified in a safe harbor provision.[195] Section 1026.52(b)(2), meanwhile, prohibits a penalty fee that exceeds the dollar amount associated with the violation or where there is no dollar amount associated with the violation.[196] In particular, § 1026.52(b)(2)(i)(B)(*1*) prohibits any fee charged in connection with a ''transaction that a card issuer declines to authorize.''

When applied to a covered overdraft credit account accessed by a hybrid debit-credit card, § 1026.52(b)(2)(B)(*1*) would prohibit most declined transaction fees imposed with respect to a declined transaction that, if paid, would have overdrawn a particular consumer's asset account. When covered overdraft credit is accessible by a hybrid debit-credit card, the CFPB has preliminarily determined that a fee imposed when a potentially overdrawing transaction is declined, such as an nonsufficient funds (NSF) fee, is a penalty fee. A potentially overdrawing transaction initiated on a

[193] CARD Act section 102, TILA section 149, 15 U.S.C. 1665d(a).

[194] Regulation Z comment 52(b)–1.

[195] 12 CFR 1026.52(b)(1)(i)–(ii).

[196] Section 1026.52(b)(2) also bans the imposition of multiple fees for the same violation. 12 CFR 1026.52(b)(2)(ii).

consumer's asset account, would, if authorized, result in the extension of overdraft credit. Declining such a transaction, and then imposing a fee for such an attempt, is a penalty fee because, under the statutory language, it is a fee that ''a card issuer may impose with respect to a credit card account . . . in connection with any omission with respect to, or in violation of, the cardholder agreement.'' [197] Likewise, under Regulation Z, it is a fee ''imposed by a card issuer based on an act . . . that violates the terms'' of the covered overdraft credit account ''or any other requirements imposed by the card issuer with respect to'' that overdraft credit account, including any requirements relating to when overdraft credit can and cannot be accessed from an asset account.[198] Because such a transaction has been declined, no credit has been extended and there is therefore no dollar amount associated with the violation.[199] Finally, because the card issuer is the entity declining this transaction, any fee imposed with respect to this declined transaction is a fee for a ''transaction that the card issuer declines to authorize.'' [200] This is true whether the penalty is charged to the covered overdraft credit account or the covered asset account.

Thus, for a covered overdraft account accessed by a hybrid debit-credit card, 15 U.S.C. 1665d(a) and § 1026.52(b) would prohibit any fee for a potentially overdrawing transaction that the card issuer declines to authorize. This would include declined debit card transactions as well as declined ACH transactions. However, as explained in comment 52(b)(2)(i)–4, the prohibition on fees for transactions that a card issuer declines to authorize does not extend to fees imposed for declining a ''check that can access a credit card account.'' [201] The CFPB has preliminarily determined that applying § 1026.52(b) to a covered overdraft credit account accessed by a hybrid debit-credit card similarly would permit fees imposed when a card issuer declines a check on an asset account with an attached covered overdraft credit account as long as those fees satisfy the restrictions in § 1026.52(b)(1).

With respect to declined transactions other than declined check transactions, the CFPB has preliminarily determined that the Board's rationale in adopting § 1026.52(b)(2) continues to apply. That is, it appears that there is no dollar amount associated with a declined transaction and the imposition of the fee does not appear to be related to costs incurred by the card issuer. The CFPB recognizes that it may be possible that such fees could have a deterrent effect or could affect the consumer's conduct in certain limited situations. However, there does not appear to be any need for the financial institution to attempt to deter or influence the consumer's conduct in this situation, particularly in light of minimal costs and risks to the card issuer. With respect to costs, because the mechanism for authorizing or declining a transaction is generally automated, the CFPB understands that declining transactions imposes very minimal or no costs, which would not support imposing a penalty fee. The CFPB understands this to be the case across several payment channels, including for payments initiated via debit card, payments occurring on an ACH network, and other online payments. To the extent there are certain minimal costs associated with the automated authorization and declination of transactions generally, card issuers can consider whether other sources of revenue might allow them to recoup those costs.

The CFPB notes that these considerations may apply equally to declined checks. However, the CFPB is not proposing at this time to reconsider the Board's prior decision to permit some amount of a fee in connection with declining to pay a check that accesses a credit card account and would apply the same approach to checks issued in connection with a checking or other transaction account with a connected covered overdraft credit account accessible by a hybrid debit-credit card.

Accordingly, after considering the factors in 15 U.S.C. 1665d, the CFPB is not proposing any amendments to § 1026.52(b).

ii. Special Credit Card Provisions (§ 1026.12)

Existing § 1026.12 contains special rules applicable to credit cards and credit card accounts, including rules regarding the conditions under which a credit card may be issued, liability of cardholders for unauthorized use, cardholder rights to assert merchant claims and defenses against the card issuer, and the prohibition on offsets by issuers.

The proposal would revise the commentary to § 1026.12 to clarify how the special card provisions of § 1026.12 apply to hybrid debit-credit cards. Specifically, the proposal would add a sentence to comment 12–1 clarifying that paragraphs (a) through (f) of § 1026.12 apply to hybrid debit-credit cards notwithstanding paragraph (g). Paragraph (g) addresses whether Regulation Z or Regulation E controls in instances where a transaction involves both credit and electronic fund transfer aspects. The proposed revision to comment 12–1 is intended to clarify that the provisions of § 1026.12 relating to card issuance and liability apply to hybrid debit-credit cards.

As discussed in greater detail below, the proposal would provide additional guidance on unsolicited issuance in § 1026.12(a) and the right of a cardholder to assert claims or defenses against a card issuer in § 1026.12(c).

iii. Clarification to Issuance of Credit Cards (§ 1026.12(a))

TILA section 132 generally prohibits creditors from issuing credit cards except in response to a request or an application. TILA section 132 explicitly exempts credit cards issued as renewals of or substitutes for previously accepted credit cards from this prohibition.[202]

Section 1026.12(a) of Regulation Z implements TILA section 132 and provides that ''[r]egardless of the purpose for which a credit card is to be used, including business, commercial, or agricultural use, no credit card shall be issued to any person except: (1) In response to an oral or written request or application for the card; or (2) As a renewal of, or substitute for, an accepted credit card.'' The proposal would provide guidance on how the prohibition on issuing unsolicited credit cards applies to hybrid debit-credit cards.

Clarification to Explicit Request Requirement (§ 1026.12(a)(1))

Comment 12(a)(1)–1 states that ''[a] request or application for a card must be explicit'' and that ''a request for an overdraft plan tied to a checking account does not constitute an application for a credit card with overdraft checking features.'' However, as discussed in greater detail in part [IV.E.2.i], under the proposal, a hybrid debit-credit card would be a credit card that a consumer may use from time to time to obtain covered overdraft credit from a very large financial institution. Therefore, the prohibition on issuing unsolicited credit cards set forth in § 1026.12(a)(1) would apply to hybrid debit-credit cards. As a result, a request for covered overdraft credit from a very large financial institution would constitute an application for a credit card with overdraft features to the extent such credit would be accessible

[197] 15 U.S.C. 1665d(a).

[198] *See* Regulation Z comment 52(b)–1.

[199] *See* 12 CFR 1026.52(b)(2)(i)(B).

[200] *See* 12 CFR 1026.52(b)(2)(i)(B)(1).

[201] Regulation Z comment 52(b)(2)(i)–4.

[202] 15 U.S.C. 1642.

through a hybrid debit-credit card. The proposal would revise comment 12(a)(1)–1 to clarify that a very large financial institution cannot issue a hybrid debit-credit card to a person without first receiving an oral or written request or application from that person for the hybrid debit-credit card.

The proposed rule also would amend comment 12(a)(1)–2. Comment 12(a)(1)–2 explains that the addition of a credit feature or plan to a non-credit card that would turn that card into a credit card constitutes issuance of a credit card. The comment then provides two examples of scenarios that would constitute issuance of a credit card. The proposed rule would amend comment 12(a)(1)–2 by adding a third example relating to hybrid debit-credit cards as comment 12(a)(1)–2.iii. Proposed comment 12(a)(1)–2.iii would state that extending covered overdraft credit through a hybrid debit-credit card as defined in § 1026.62 would constitute issuance of a credit card. For example, if a very large financial institution initially allowed a consumer to use a debit card to access overdraft credit that is not ''covered overdraft credit'' as defined in § 1026.62, the very large financial institution would be issuing a credit card if it then allowed the consumer to use the same card to access covered overdraft credit. Under that scenario, the debit card would convert into a hybrid debit-credit card subject to the requirements of § 1026.12(a).

Clarifications to Replacement Card Requirements (§ 1026.12(a)(2))

Comment 12(a)(2)–5 (the so-called ''one for one'' rule) explains that an accepted card generally may be replaced by no more than one renewal or substitute card. For example, the card issuer may not replace a credit card permitting purchases and cash advances with two cards, one for the purchases and another for the cash advances. However, comment 12(a)(2)–6 provides three exceptions to this general ''one for one'' rule. First, comment 12(a)(2)–6.i explains that the unsolicited issuance rule in § 1026.12(a) does not prohibit the card issuer from replacing a debit/credit card with a credit card and another card with only debit functions (or debit functions plus an associated overdraft capability), since the latter card could be issued on an unsolicited basis under Regulation E. Second, comment 12(a)(2)–6.ii explains that § 1026.12(a) does not prohibit a card issuer from replacing a single card that is both a prepaid card and a credit card with a credit card and a separate prepaid card where the latter card is not a hybrid prepaid-credit card as defined in § 1026.61. Finally, comment 12(a)(2)–6.iii explains that § 1026.12(a) does not prohibit a card issuer from replacing an accepted card with more than one renewal or substitute card, provided that: ''(A) No replacement card accesses any account not accessed by the accepted card; (B) For terms and conditions required to be disclosed under § 1026.6, all replacement cards are issued subject to the same terms and conditions, except that a creditor may vary terms for which no change in terms notice is required under § 1026.9(c); and (3) Under the account's terms the consumer's total liability for unauthorized use with respect to the account does not increase.''

The proposal would amend comment 12(a)(2)–6 by revising comment 12(a)(2)–6.i in two respects. First, it would explain that a hybrid debit-credit card is an example of a single card that is both a debit card and a credit card. Second, it would remove the phrase ''an associated overdraft capability'' in the parenthetical and replace it with the phrase ''an associated capability to extend overdraft credit that is not covered overdraft credit as defined in § 1026.62.'' The purpose of these proposed changes is to clarify that a very large financial institution may replace a hybrid debit-credit card with a credit card and a separate debit card so long as the separate debit card does not provide the capability to extend covered overdraft credit (*i.e.,* overdraft that is subject to a finance charge or payable by written agreement in more than four installments). Replacing the phrase ''an associated overdraft capability'' with the phrase ''an associated capability to extend overdraft credit that is not covered overdraft credit as defined in § 1026.62'' in the parenthetical would not change how the provision applies to card issuers, but rather would align terminology relating to overdraft credit across Regulation Z.

iv. Right of Cardholder To Assert Claims or Defenses Against Card Issuer (§ 1026.12(c))

When a cardholder has a dispute with a person honoring the credit card, TILA section 170 generally provides that the cardholder may assert against the card issuer all claims (other than tort claims) and defenses arising out of the transaction.[203] The claim or defense applies only as to unpaid balances for the goods or services and any finance or other charges imposed on that amount if the merchant honoring the card fails to resolve the dispute. The right is further limited generally to disputes exceeding $50 for purchases made in the consumer's home State or within 100 miles of the cardholder's address. Regulation Z § 1026.12(c), implements this section of TILA.

TILA does not except overdraft credit from the scope of cardholders' right to assert claims or defenses against card issuers. However, in 1981 the Board created a non-statutory exception for the use of a debit card in connection with an overdraft credit plan.[204] In doing so, the Board noted ''serious operational problems cited by commenters as arising from applying the claims and defenses provisions to check guarantee and debit card transactions.''[205] This exception is in current comment 12(c)–3.

As discussed above, the CFPB has preliminarily determined that it would be appropriate to update exceptions in Regulation Z and thus increase consumer protections that apply to covered overdraft credit offered by very large financial institutions. The proposed rule would not change the current overdraft exceptions for financial institutions with total assets of $10 billion or less.

Accordingly, the CFPB proposes to narrow the overdraft exception in comment 12(c)–3 by adding the phrase ''other than a hybrid debit-credit card.'' As discussed above, under proposed § 1026.62(b)(5) a ''hybrid debit-credit card'' would include a debit card that a consumer may use from time to time to obtain covered overdraft credit from a very large financial institution. Such cards would be covered by the consumer protections in § 1026.12(c). The CFPB has preliminarily determined that operational concerns alluded to by the Board in 1981 may no longer justify the overdraft exception in comment 12(c)–3, particularly for very large financial institutions, given advances in information technology systems over the last 40 years. The current exception would not change for financial institutions with total assets of $10 billion or less.

The CFPB further proposes conforming revisions to the commentary for § 1026.12(c)(1). First, the CFPB would revise comment 12(c)(1)–1. The current comment explains that the scope of cardholders' right to assert claims or defenses against card issuers only includes situations where the goods or services are ''purchased with the credit card.'' The comment provides examples of situations that are included and excluded. To facilitate compliance with the proposed rule, the CFPB would

[203] 15 U.S.C. 1666i.

[204] 46 FR 20848, 20865 (Apr. 7, 1981).

[205] *Id.*

revise comment 12(c)(1)–1 to provide an example illustrating that the phrase ''purchased with the credit card'' includes a purchase using a hybrid debit-credit card to access a covered overdraft credit account as defined in § 1026.62.

Second, the CFPB would revise comment 12(c)(1)–1.ii. The current comment explains that credit card protections in § 1026.12(c) do not apply to the purchase of goods or services by use of a check accessing an overdraft account and a credit card used solely for identification of the consumer. The current comment further illustrates that, if the credit card is used to make partial payment for the purchase and not merely for identification, the right to assert claims or defenses would apply to credit extended via the credit card (although not to credit extended by the overdraft line). The current comment also provides that the right would apply to credit extended through a covered separate credit feature accessible by a hybrid prepaid-credit card. To facilitate compliance with the proposed rule, the CFPB would revise comment 12(c)(1)–1.ii to provide an example illustrating that if partial payment for the purchase is made with a hybrid prepaid-credit card or a hybrid debit-credit card, the right to assert claims or defenses would apply to credit accessed from a covered separate credit feature or covered overdraft credit account, respectively.

Third, the CFPB would revise comment 12(c)(1)–1.iv. Current comment 12(c)(1)–1.iv cross-references comment 12(c)–3 and explains that credit card protections in § 1026.12(c) do not apply to purchases effected by use of either a check guarantee card or a debit card when used to draw on overdraft credit plans. The current comment further illustrates that, if a card serves both as an ordinary credit card and also as a check guarantee or debit card, a transaction will be subject to the provisions on asserting claims and defenses when used as an ordinary credit card, but not when used as a check guarantee or debit card. As discussed above, the CFPB proposes to narrow the overdraft exception in comment 12(c)–3. To reflect that proposed change, CFPB also proposes conforming revisions to comment 12(c)(1)–1.iv, which would provide that the right to assert claims or defenses would apply to purchases effected by use of a hybrid debit-credit card to access a covered overdraft credit account. The CFPB would also revise comment 12(c)(1)–1.iv to provide an example illustrating that for purchases effected by use of a hybrid debit-credit card where the transaction is partially paid with funds from the asset account, and partially paid with covered overdraft credit, the provisions of § 1026.12(c) apply only to the credit portion of the purchase transaction. The CFPB would also correct a typographical error in comment 12(c)(1)–1.iv by inserting the article ''a'' that is currently missing before ''check guarantee or debit card.''

The CFPB seeks comment on the proposed narrowing of the overdraft exception in comment 12(c)–3, including what, if any, operational issues might arise as a result. The CFPB also seeks comment on the proposed conforming revisions to the commentary for § 1026.12(c)(1).

v. Credit Card Applications and Solicitations (§ 1026.60)

Existing § 1026.60 includes certain requirements related to applications and solicitations for credit cards. Among other things, it requires certain disclosures in connection with credit card applications and solicitations and prescribes content and format of the application or solicitation. Existing § 1026.60(a)(5) excepts certain types of credit from the requirements of § 1026.60, including § 1026.60(a)(5)(ii), which excepts overdraft lines of credit tied to asset accounts accessed by check-guarantee cards or by debit cards; § 1026.60(a)(5)(iii), which excepts lines of credit accessed by check-guarantee cards or by debit cards that can be used only at automated teller machines; and § 1026.60(a)(5)(iv), which excepts lines of credit accessed solely by account numbers except for a covered separate credit feature solely accessible by an account number that is a hybrid prepaid-debit card as defined in § 1026.61.

The requirements in § 1026.60 implement provisions of the Fair Credit and Charge Card Disclosure Act of 1988.[206] The purpose of the law was to provide for more detailed and uniform disclosures of rates and other cost information in applications and in solicitations to open credit and charge card accounts. The statute applies the disclosure requirements broadly to any application to open a credit card account for any person under an open-end consumer credit plan or to a solicitation to open such an account without requiring an application. In implementing the statutory requirements, the Board narrowed the scope of coverage by adopting the exceptions in what is now § 1026.60(a)(5), determining that the requirements should apply only to ''traditional'' credit or charge accounts that are used primarily to purchase goods and services.[207]

The CFPB has preliminarily determined that, as with the CARD Act provisions, covered overdraft offered by a very large financial institution that is accessible by a card, including a debit card, should be subject to the requirements of § 1026.60. In excepting certain types of credit from those requirements, the Board noted only that the requirements should apply only to ''traditional'' credit cards that are used to purchase goods and services. However, given the expanded use of debit cards to purchase goods and services, many of which are linked to accounts that offer overdraft credit, the distinction between ''traditional'' credit cards and debit cards that can access overdraft credit appears far less clear. The CFPB has preliminarily determined that the requirements of § 1026.60 should be applied consistent with the broad statutory language to cards that can access covered overdraft credit, and that doing so will carry out the purposes of TILA by assuring a meaningful disclosure of credit terms and avoiding the uninformed use of credit.

Accordingly, the CFPB is proposing to amend § 1026.60 to narrow the exception for overdraft lines of credit. Specifically, the proposal would amend § 1026.60(a)(5)(ii), (iii), and (iv) so that those exceptions would not apply to covered overdraft credit accessed by a hybrid debit-credit card. As explained above, the CFPB is proposing to define a ''hybrid debit-credit card'' as any card (including a debit card) that can access covered overdraft credit offered by a very large financial institution. Accordingly, the proposed amendments to § 1026.60(a)(5)(ii), (iii), and (iv) would narrow the exception so that the requirements of § 1026.60 would apply to covered overdraft credit offered by a very large financial institution when that credit can be accessed by any card, including a debit card.

vi. Charge Card (§ 1026.2(a)(15)(iii))

The CFPB proposes to amend the definition of ''charge card'' in § 1026.2(a)(15)(iii) to exclude a hybrid debit-credit card from the definition. Under the proposed amendment, a hybrid debit-credit card would be subject to the same disclosure and other rules as other credit cards, rather than certain special rules for charge cards. The CFPB has preliminarily determined that consumers using hybrid debit-credit cards would benefit from the

[206] Public Law 100–583, 102 Stat. 2960 (Nov. 3, 1988).

[207] 54 FR 13855, 13856–57 (Apr. 6, 1989).

TILA and Regulation Z provisions that apply to credit cards generally.

TILA defines ''charge card'' as ''a card, plate, or other single credit device that may be used from time to time to obtain credit which is not subject to a finance charge.'' [208] Because hybrid debit-credit cards would generally access credit that is subject to a finance charge, they do not fit within the statutory definition of charge card. The term ''charge card'' was introduced into TILA with the Fair Credit and Charge Card Disclosure Act of 1988, which amended TILA to define ''charge card'' as ''a card, plate, or other single credit device that may be used from time to time to obtain credit *which is not subject to a finance charge*'' (emphasis added).[209] In its rule implementing the 1988 act, the Board expanded the definition of ''charge card'' such that, in Regulation Z, the definition includes any card on which *there is no periodic rate*.[210] In other words, a card with a finance charge that is not a periodic rate is excluded from the statutory charge card definition but is included within the Regulation Z definition of that term. The Board sought to address a perceived inconsistency between that statutory definition and the fact that some disclosure provisions that apply to charge cards reference finance charges.

Under both the statutory and regulatory definitions, a charge card is a type of credit card. Thus, where Regulation Z provisions apply to credit cards, the provisions also apply to charge cards. However, in specific provisions, which are listed in comment 2(a)(15)–3.i, the term charge card is distinguished from credit card such that different requirements apply. One example of such a provision is § 1026.7(b)(11), which, in accordance with TILA, requires on credit card periodic statements the disclosure of a payment due date and requires that that date be the same day of the month for each billing cycle. The Board in Regulation Z excluded charge cards from these requirements.[211] The CFPB has preliminarily determined, however, that these requirements should apply to a debit card that can access a covered overdraft credit account (*i.e.,* a hybrid debit-credit card). The CFPB accordingly is proposing to exclude hybrid debit-credit cards from the Regulation Z definition of charge card. This approach is consistent with TILA; in proposing to apply the TILA and Regulation Z credit card provisions to debit cards that can access covered overdraft, the CFPB is merely declining to exercise its regulatory authority to implement TILA with respect to hybrid debit-credit cards in the ways that the Board previously did with respect to charge cards.

The proposed definition of hybrid debit-credit card would encompass devices that can access overdraft credit and are subject to finance charges, including devices that are subject to fees but not a periodic interest rate. Hybrid debit-credit cards would therefore *not* fit the statutory definition of a ''charge card,'' because they are subject to finance charges. Further, the CFPB preliminarily determines that consumers using hybrid debit-credit cards would benefit from the TILA and Regulation Z provisions that apply to credit cards generally, such as § 1026.7(b)(11).

The CFPB understands that charge cards are typically offered to higher income individuals with prime or super-prime credit, and they often have no set credit limit.[212] In contrast, current users of non-covered overdraft credit often are lower-income consumers with lower credit scores.[213] Subsequent to the CFPB's proposal, many of these consumers may be offered hybrid debit-credit cards. Accordingly, consistent with TILA, and to ensure that consumers who use covered overdraft credit may benefit from the full protection of the Regulation Z credit card rules, the CFPB is proposing to amend the regulatory definition of ''charge card'' such that a 'hybrid debit-credit card' would *not* be within the credit card subset ''charge card'' but would nonetheless remain in the larger set ''credit card.'' This would ensure that a hybrid debit-credit card that accesses covered overdraft credit offered by a very large financial institution would be subject to the same disclosure and other rules as other credit cards.

3. Compulsory Use of Preauthorized Transfers (§ 1005.10(e)(1))

The CFPB proposes to apply the Regulation E compulsory-use prohibition to covered overdraft credit extended by very large financial institutions—*i.e.,* when a very large financial institution provides overdraft credit that is subject to Regulation Z. Under this proposal, a very large financial institution that provides covered overdraft credit to a consumer could not condition the extension of such covered overdraft credit on the consumer's agreement to repay it solely by preauthorized electronic fund transfer (EFT). In other words, the proposal would require a very large financial institution that provides covered overdraft credit to a consumer to offer the consumer at least one alternative repayment option in addition to a preauthorized EFT.

EFTA section 903(10) defines the term ''preauthorized electronic fund transfer'' as ''an [EFT] authorized in advance to recur at substantially regular intervals.'' [214] Regulation E § 1005.2(k) restates the statutory definition. EFTA's compulsory-use prohibition, EFTA section 913(1), prohibits any person from conditioning the extension of credit to a consumer on the consumer's repayment by means of preauthorized EFTs.[215] However, Regulation E § 1005.10(e)(1) currently includes a non-statutory exception. Specifically, that section states that ''[n]o financial institution or other person may condition an extension of credit to a consumer on the consumer's repayment by preauthorized electronic fund transfers, *except for* credit extended under an overdraft credit plan or extended to maintain a specified minimum balance in the consumer's account'' (emphasis added).[216] The commentary explains that, as a result of the exception, a financial institution may require the automatic repayment of an overdraft credit plan.[217]

Regulation Z section 1026.12(d)(3) permits a card issuer, who obtains written authorization from the cardholder, to deduct periodically a cardholder's credit card debt from a deposit account held with the card issuer. Therefore, under the current rules, if a financial instution were to provide a consumer with overdraft credit accessible by a credit card, the financial institution could, with the consumer's written authorization, make automatic periodic deductions from the consumer's deposit account. Because periodic deductions by a creditor to obtain repayment of an overdraft credit balance occur at regular intervals, they are a form of preauthorized EFT and would be subject to the Regulation E compulsory-use prohibition, absent the extant exception for an overdraft credit plan provided by current

[208] 15 U.S.C. 1637(c)(4)(E).

[209] *See* Public Law 100–583, section 2, 102 Stat. 2960 (Nov. 3, 1988).

[210] 54 FR 13855, 13856 (Apr. 4, 1989).

[211] *See* § 1026.7(b)(11)(ii)(A); 75 FR 7658, 7672–73 (Feb. 22, 2010).

[212] *See* Fed. Trade Comm'n, *Comparing Credit, Charge, Secured Credit, Debit, or Prepaid Cards* (Dec. 2021), *https://consumer.ftc.gov/articles/comparing-credit-charge-secured-credit-debit-or-prepaid-cards.*

[213] *See* CFPB 2017 Data Point at 6.

[214] 15 U.S.C. 1693a(10).

[215] 15 U.S.C. 1693k(1).

[216] 12 CFR 1005.10(e)(1).

[217] Regulation E comment 10(e)(1)–2.

§ 1005.10(e)(1).[218] It is this exception that the CFPB is proposing to eliminate for covered overdraft credit provided by a very large financial institution.

In adopting the exception from the compulsory-use prohibition in 1981, the Board used its EFTA exception authority to exclude ''overdraft credit plans'' (*i.e.,* covered overdraft credit) from the general EFTA compulsory-use prohibition.[219] The CFPB's proposal would revise § 1005.10(e)(1) and associated commentary to update that non-statutory exception. Under the CFPB's proposal, the exception in § 1005.10(e)(1) for overdraft credit plans would no longer apply to covered overdraft credit provided by a very large financial institution, as those terms would be defined in proposed § 1026.62.

Because under the proposal the exception would no longer apply to covered overdraft credit provided by a very large financial institution, the institution would be required to offer a consumer at least one method of repaying an overdraft credit balance other than automatic repayment by preauthorized EFT. For example, in addition to the automatic repayment option, the institution could offer consumers an option to repay their outstanding overdraft credit balances by expressly authorizing (*e.g.,* on the institution's website or smartphone application) a one-time transfer of funds from the consumer's asset account.

Under the CFPB's proposal, this requirement to offer additional repayment methods would apply to any existing covered overdraft credit offered by a very large financial institution, including products that often are referred to as Regulation Z overdraft lines of credit. In other words, where such an institution today provides a consumer with an overdraft line of credit subject to Regulation Z, the institution, upon the compliance date of the CFPB's proposal (if finalized), would need to begin to offer the consumer a way for the consumer to repay the consumer's overdraft credit balances other than by preauthorized EFT. While the institution would be required to offer a repayment option other than automatic repayment, the institution (as today) may offer a reduced APR or other cost-related incentive for the consumer to choose the option of automatic repayment.[220]

Congress enacted the compulsory-use prohibition to prevent financial institutions and other persons that are creditors from mandating repayment of credit by preauthorized EFTs, such as automatic periodic deductions from consumers' accounts. In turn, in adopting an exception to that prohibition for overdraft in the early 1980s, the Board stated its belief that overdraft credit plans were popular with those consumers who had them and that those plans almost universally involved an automatic payment feature.[221] The Board also stated that it believed that the cost to institutions of providing and maintaining a nonautomatic payment option was substantial and that requiring institutions to incur that cost could have an adverse impact on consumers, such as through reduced service levels or the termination of the overdraft service altogether.[222]

Covered overdraft credit plans are currently relatively rare.[223] The CFPB has no reason to believe that these plans were available to a wider set of consumers in 1981 than they are now. Accordingly, the CFPB generally understands the Board's 1981 preamble to indicate that covered overdraft credit plans were well liked at that time by those consumers who had access to them. In addition, the CFPB has preliminarily determined that advances in information technology since the early 1980s (when the Board adopted the compulsory-use exception for overdraft) have reduced institutions' costs of obtaining repayment by means other than automatic repayment by preauthorized EFT. For example, an institution can establish at reasonable cost an internet computer or smartphone interface through which consumers may easily initiate—such as by tapping a ''button'' on a smartphone screen—monthly repayment of credit balances. Further, because applying the compulsory-use prohibition should not substantially increase institutions' costs, applying the prohibition would not necessarily reduce consumers' access to covered overdraft credit plans. At the same time, applying the compulsory-use prohibition to covered overdraft credit may allow consumers at very large financial institutions to retain better control over the funds in their asset accounts at those institutions. Specifically, applying the prohibition would better enable consumers to prioritize which of their obligations to pay. For example, when funds are deposited into the consumer's asset account (such as electronic direct deposit of the consumer's paycheck), the consumer would be able to choose to use those funds to pay their rent before subsequently repaying the consumer's overdraft balance at the institution (using additional funds from the electronic direct deposit or subsequently deposited funds). Giving the consumer this choice could also help to reduce the consumer's costs if the consumer is charged for each overdraft transaction and delaying repayment of the overdrawn amounts would allow the consumer to avoid a subsequent overdraft transaction and its associated charge.

For these reasons, the CFPB has preliminarily determined that applying the compulsory-use prohibition to covered overdraft credit provided by a very large financial institution will carry out the purposes of EFTA by safeguarding consumers' rights in electronic fund transfer systems. This preliminary determination to apply the compulsory-use prohibition is consistent with Congress's original intent. Congress passed a broad compulsory-use prohibition, which the Board then narrowed due to concerns about costs, and which the CFPB is now proposing to restore in light of changed market circumstances (*i.e.,* substantially reduced costs of alternative means of repayment).

Non-Covered Overdraft Credit

As noted, the Regulation E compulsory-use prohibition prohibits conditioning *credit* extensions on consumers' repayment by preauthorized EFT. As discussed in this proposal, *all* overdraft is credit, irrespective of whether the overdraft is or is not subject to Regulation Z. Nonetheless, the compulsory-use prohibition has historically been interpreted as not applying to overdraft credit that is not subject to the requirements of Regulation Z (notwithstanding that non-covered overdraft credit *is* credit). Specifically, in 1980 the Board stated its belief that the compulsory-use prohibition does not apply to overdraft credit that is not covered by Regulation Z because, with respect to that overdraft, banks take consumers' repayments through immediate offset (which does not occur at regular intervals), rather than through preauthorized EFTs that consumers authorize in advance to recur at

[218] *See* § 1005.3(c)(5)(iii), which excludes from the Regulation E EFT definition a transfer of funds between a consumer's account and an account of the consumer's financial institution, but which also states that these transfers remain subject to the § 1005.10(e) compulsory-use prohibition.

[219] *See* 46 FR 2972, 2973 (Jan. 13, 1981).

[220] *See* Regulation E comment 10(e)(1)–4.

[221] 46 FR 2972, 2973 (Jan. 13, 1981).

[222] *Id.*

[223] 75 FR 7657, 7664 (Feb. 22, 2010). *See also* 79 FR 77102, 77208 (Dec. 23, 2014).

substantially regular intervals.[224] Under the Board's historical reasoning, a financial institution providing non-covered overdraft credit does not need access to the above-described exception for overdraft credit plans from the compulsory-use prohibition, because the institution's non-covered overdraft credit is not subject to the compulsory-use prohibition in the first place (because the institution takes repayment at irregular intervals, whenever the next deposit is received, rather than at regular intervals).

The CFPB is not proposing to revisit this longstanding interpretation. That is, under the CFPB's proposal, it will remain the case that non-covered overdraft credit that obtains repayment through offset, such as the typical overdraft service as defined in § 1005.17(a), is not subject to the compulsory-use prohibition. Therefore, a very large institution providing non-covered overdraft at or below breakeven pricing may continue to take repayment of a consumer's overdraft balance immediately upon the institution's receipt of the next deposit to the consumer's account, just as institutions typically do today, if done in compliance with applicable law.

Under the CFPB's proposal, however, overdraft credit, including an overdraft service as that term is defined in Regulation E, that is provided by a very large financial institution, would *only* remain not covered by Regulation Z's requirements—and thus outside the Regulation E compulsory-use prohibition—if the institution provides its overdraft credit to consumers for a price that is at or below the institution's breakeven price for providing the credit. In other words, if the price of such institution's overdraft credit is *above* its costs and losses, then, under the CFPB's proposal, the credit is covered overdraft credit that is *not* excepted from Regulation Z and is therefore subject to the Regulation Z offset prohibition. Accordingly, under the CFPB's proposal, the institution would be required to obtain repayment only periodically (pursuant to the offset prohibition) and to comply with the Regulation E compulsory-use prohibition (in addition to complying with Regulation Z). As previously noted, the CFPB's proposal does not apply to non-covered or covered overdraft credit provided by an institution other than a very large financial institution. As now, where such an institution provides non-covered overdraft credit, including an overdraft service, the overdraft credit is not subject to the Regulation E compulsory-use prohibition. Further, as now, where such an institution provides an overdraft credit plan that *is* subject to Regulation Z, the institution's overdraft credit plan retains access to the current § 1005.10(e)(1) exception from the compulsory-use prohibition for overdraft credit plans.

i. The Offset Prohibition in 12 CFR 1026.12(d)(1)

While the CFPB is not proposing to amend the Regulation Z prohibition against offset, it is closely related to the Regulation E compulsory-use prohibition discussed above; thus, the CFPB briefly discusses it here for clarity.

''Offset'' is a term used to describe a practice whereby a depository institution uses funds from an incoming deposit to a consumer's asset account at the institution to immediately obtain repayment of the consumer's debt to the institution, such as an overdraft.[225] ''Offset'' is a permitted practice in the context of non-covered overdraft that is *not* subject to Regulation Z. In that context, as described above, an institution may use deposited funds immediately upon receipt to obtain repayment of, or ''offset'' against, the consumer's overdraft balance owed to the institution.

Offset is prohibited by TILA section 169(a) (15 U.S.C. 1666h(a)) and 12 CFR 1026.12(d)(1). The statutory and regulatory offset prohibition applies to a ''card issuer,'' [226] which is a person that issues a ''credit card.'' [227] When an institution offers an overdraft credit plan subject to Regulation Z, that plan is covered overdraft credit. If the covered overdraft credit is accessible by a debit card, the debit card is a credit card, the institution that provides the card is a card issuer, and the covered overdraft credit is subject to the Regulation Z prohibition against offset.

The CFPB is not proposing to amend the offset prohibition in Regulation Z. Thus, when a very large financial institution provides a covered overdraft credit account that is accessible by a card (*i.e.,* a hybrid debit-credit card), the institution must comply with the offset prohibition. In particular, 12 CFR 1026.12(d)(1) prohibits the institution (as a card issuer) from taking any action, either before or after termination of credit card privileges, to offset a consumer's indebtedness (such as an overdraft balance) that arises from a credit card plan (such as a covered overdraft credit account) against the consumer's funds (such as funds in a covered asset account) held on deposit with the institution.

Further, per comment 12(d)(1)–3, the offset prohibition applies to any indebtedness arising from transactions under a credit card plan (such as a covered overdraft credit account accessible by a hybrid debit-credit card), including accrued finance charges and other charges on the account. The prohibition also applies to balances arising from transactions not using the card itself but taking place under plans that involve a credit card. For example, if the consumer writes a check that accesses an overdraft line of credit (which is a type of covered overdraft credit account), the resulting indebtedness is subject to the offset prohibition since it is incurred through a credit card plan.[228]

ii. Periodic Deductions Permitted by 12 CFR 1026.12(d)(3)

Periodic deductions are a different practice than offset. TILA section 169(a)(1) (15 U.S.C. 1666h(a)(1)) permits a card issuer to periodically deduct all or part of a consumer's credit card debt from the consumer's asset account if the periodic deductions are in accordance with the consumer's preauthorized written agreement. This TILA provision is implemented in 12 CFR 1026.12(d)(3).

The CFPB is not proposing to amend 12 CFR 1026.12(d)(3). Thus, when a very large financial institution provides covered overdraft credit that is accessible by a card, the institution (as a card issuer) must comply with the offset prohibition (§ 1026.12(d)(1), discussed above), but may obtain a consumer's preauthorized written agreement to periodic deductions of the consumer's overdraft balances from the consumer's asset balances held at the institution. These deductions must be ''periodic'' to be permitted under

[224] *See* 45 FR 66348, 66348 (Oct. 6, 1980) (''Other [*i.e.,* non-covered] plans have automatic debiting whenever funds are deposited into the consumer's account, and do not have a fixed periodic or recurring payment schedule. It is the Board's opinion that these [non-covered] plans are already in compliance with section 913, because they do not require the consumer to agree to repayment by preauthorized transfers, which are defined in the act and regulation as transfers 'authorized in advance to recur at substantially regular intervals.''').

[225] *See* Regulation Z comment 12(d)(1)–2 (describing offset as when ''the consumer tenders funds as a deposit . . . [and] the card issuer . . . appl[ies] the funds to repay indebtedness on the consumer's credit card account'').

[226] The term ''card issuer'' is defined in 12 CFR 1026.2(a)(7) as ''a person that issues a credit card or that person's agent with respect to the card.''

[227] The term ''credit card'' is defined in 12 CFR 1026.2(a)(15)(i) as ''any card, plate, or other single credit device that may be used from time to time to obtain credit.''

[228] *See* Regulation Z comment 12(d)(1)–3.

§ 1026.12(d)(3); that is, the deductions must occur at regular intervals. Because the deductions must occur at regular intervals, they are, as discussed above, a form of preauthorized EFT and are subject to the Regulation E compulsory-use prohibition. Further, because the deductions are subject to that prohibition, under the CFPB's proposal, as discussed, a very large financial institution providing covered overdraft credit must offer consumers a means of repayment other than periodic deduction. In other words, even when a very large institution (as a card issuer) obtains a consumer's written agreement to periodic deductions as permitted by § 1026.12(d)(3), the institution may not adopt a practice of immediately taking funds from any incoming deposit in repayment of the consumer's overdraft balance, because doing so would run afoul of the offset prohibition in § 1026.12(d)(1). Moreover, when obtaining written agreement for periodic deductions, the very large financial institution must offer the consumer another repayment option, consistent with the prohibition against compulsory use discussed earlier in this section.

iii. Summary of Compliance With the Compulsory-Use Prohibition, Offset Prohibition, and Permitted Periodic Deduction Under the CFPB's Proposal

As discussed above, the CFPB is proposing to apply the Regulation E compulsory-use prohibition to covered overdraft credit provided by a very large financial institution. Further, the CFPB is not proposing to amend the Regulation Z prohibition against offset, nor is the CFPB proposing to amend the Regulation Z provision permitting periodic deductions. Therefore, when such an institution provides covered overdraft credit that is accessible by a card, the institution must comply with the Regulation E compulsory-use prohibition and the Regulation Z offset prohibition, and may obtain the consumer's voluntary agreement to repayment by periodic deduction from the consumer's asset account at the institution.

Pursuant to the Regulation Z offset prohibition, the institution may not adopt a practice of immediately taking funds from any incoming deposit in repayment of the consumer's overdraft balance. Pursuant to the Regulation Z provision permitting periodic deductions, the institution may obtain the consumer's written agreement to the institution's obtaining repayment of the consumer's overdraft balance through automatic periodic deductions from the consumer's covered asset account. However, pursuant to the Regulation E compulsory-use prohibition, the institution must provide the consumer with a repayment option *other than* automatic periodic deduction. For example, the institution could provide the repayment option of permitting the consumer to authorize one-time EFTs to make payments against their overdraft balance. Also pursuant to the compulsory-use prohibition, the institution may provide a reduced APR or other cost-related incentive for the consumer to choose the option of repayment by periodic deduction.

Request for Comment—Defining ''Periodic''

In its 2016 Prepaid Final Rule, the CFPB defined ''periodically'' in § 1026.12(d)(3) for purposes of a credit feature accessible by a hybrid prepaid-credit card to mean no more frequently than once per calendar month. The CFPB stated that it was concerned that some issuers of hybrid prepaid-credit cards would attempt to circumvent the offset prohibition in § 1026.12(d)(1) by obtaining a consumer's written authorization to deduct all or part of the cardholder's credit card debt on a daily or weekly basis from the prepaid account to help ensure that the debt is repaid.[229] The CFPB stated that issuers of hybrid prepaid-credit cards might obtain a consumer's written authorization to daily or weekly debits given the overall creditworthiness of prepaid accountholders who rely on covered separate credit features. In addition, the CFPB believed that prepaid consumers might grant the authorization more readily than other credit cardholders because these consumers may believe that providing such authorization is required. While the CFPB acknowledged that an appropriate interval for periodic deductions may depend on the facts and circumstances, the CFPB determined that § 1026.12(d)(3)—defining periodically as no more frequently than once per calendar month—would fully effectuate the intent of the compulsory-use and offset prohibitions and would allow consumers to retain control over the funds in their prepaid accounts even when a covered separate credit feature accessible by a hybrid prepaid-credit card becomes associated with that account.

The CFPB believes that similar issues are also present in the context of covered overdraft credit accounts tied to covered asset accounts. In particular, the CFPB believes that institutions providing such accounts might attempt to circumvent the offset prohibition by obtaining a consumer's written authorization to deduct all or part of the consumer's debt on a daily or weekly basis to help ensure that the debt is repaid. Further, the CFPB believes that consumers using these accounts, such as frequent overdrafters, would generally be more vulnerable than other consumers and that, in light of their vulnerability, these consumers might grant such authorization more readily than other consumers, because they believe that the authorization is required to obtain the accounts. At the same time, the CFPB acknowledges that it is possible that a periodic deduction period shorter than one month might be appropriate in some circumstances. Specifically, it is possible that some consumers might have difficulty managing repayment of credit balances and that these consumers might benefit from periodic deductions that occur more frequently than once per month.

The CFPB requests comment on whether in its final rule it should define ''periodically'' to mean no more frequently than once per calendar month or some other interval for covered overdraft credit accounts tied to covered asset accounts.

4. Definition of Overdraft Services in Regulation E (§ 1005.17(a))

Section 1005.17(a) currently defines ''overdraft service'' to mean 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. Section 1005.17(a)(1) also provides that the term ''overdraft service'' does not include any payment of overdrafts pursuant to a line of credit subject to Regulation Z, including transfers from a credit card account, home equity line of credit, or overdraft line of credit. The CFPB is proposing to add comment 17(a)–2 to clarify that the newly defined terms under this proposal do not change the scope of the definition of overdraft services under § 1005.17(a). Specifically, the proposed comment would clarify that covered overdraft credit, which includes above breakeven overdraft credit, is not an overdraft service under § 1005.17(a) because it is a line of credit subject to Regulation Z. When consumers at very large financial institutions are offered covered overdraft credit, that covered overdraft credit would not be subject to the Regulation E opt-in requirement for non-covered debit card overdraft.

[229] 81 FR 83934, 84213 (Nov. 22, 2016).

VI. Proposed Effective Date

Consistent with TILA section 105(d), the CFPB proposes that a final rule relating to this proposal would have an effective date of the October 1 which follows by at least six months the date it is published in the **Federal Register**.[230] The Bureau seeks comment on the proposed effective date including whether it should be at a different time, and if so, when and why.

As discussed above, the CFPB's proposed rule would, if finalized, apply only to very large financial institutions. Accordingly, financial institutions that are not very large institutions would not need to make any changes in response to the proposed rule were it to be finalized.

With respect to very large financial institutions, the changes that the proposed rule would require, if finalized, would vary depending on the very large financial institution's activities. If a very large financial institution currently offered non-covered overdraft services in compliance with existing regulations and, in response to the rule, it chose to provide those services at or below its breakeven price, it could continue to provide such services without making any operational changes in response to the rule apart from developing a process to confirm that its pricing for such services complied with either the rule's benchmark fee or breakeven standard provisions.

If a very large financial institution currently offered non-covered overdraft services in compliance with existing regulations and, in response to the rule, chose to provide above-breakeven overdraft credit, it would need to ensure that such credit complied with Regulation Z. However, if the very large financial institution were unable to bring a Regulation Z compliant above-breakeven overdraft credit program to market before the effective date of a final rule, the institution still could comply with the rule by delaying, for as long as it wishes, the point in time at which it began to offer above-breakeven overdraft credit to consumers. Finally, if a very large financial institution currently offered covered overdraft credit in compliance with Regulation Z and, in response to the rule, chose to continue offering such credit, the very large financial institution would need to comply with the rule by: (1) treating transfer fees as finance charges, or eliminating those fees, (2) offering consumers a means of repaying their overdrafts other than by preauthorized EFTs, and (3) beginning to comply with the regulatory provisions in Regulation Z that apply to credit cards that would newly apply to certain types of covered overdraft credit.

The CFPB believes that the proposed effective date should be sufficient for a very large financial institution to make these changes.

VII. Severability

The CFPB preliminarily intends that, if any provision of the proposed rule, if adopted as final, or any application of a provision, is stayed or determined to be invalid, the remaining provisions or applications are severable and shall continue in effect.

VIII. CFPA Section 1022(b) Analysis

A. Overview

In developing this proposed rule, the CFPB has considered the proposed rule's potential benefits, costs, and impacts per section 1022(b)(2)(A) of the Consumer Financial Protection Act of 2010 (CFPA). The CFPB requests comment on the preliminary analysis presented below and submissions of more data that could inform the CFPB's analysis of the potential benefits, costs, and impacts. In developing the proposed rule, the CFPB has consulted or offered to consult with the appropriate prudential regulators and other Federal agencies, including about the consistency of this proposed rule with any prudential, market, or systemic objectives administered by those agencies, in accordance with section 1022(b)(2)(B) of the CFPA. The CFPB also consulted with agencies described in TILA section 149.

The goal of this proposed rule is to allow more consumers to better compare certain overdraft credit to other types of credit and to provide consumers with several substantive protections that already apply to other consumer credit, while still encouraging the availability of overdraft coverage. The section proceeds as follows. First, it describes data limitations and the quantification of benefits, costs, and impacts. Second, it presents the baseline for its analysis. Third, it goes through the potential benefits and costs, first to consumers and then to covered persons, of the proposed changes that affect charges for non-covered and covered overdraft. Fourth, the section turns to the benefits, costs, and impacts of further provisions of the proposed rule. Fifth and sixth, it summarizes specific impacts on financial institutions with $10 billion in assets or less and on consumers in rural areas, respectively.

B. Data Limitations and Quantification of Benefits, Costs, and Impacts

The discussion below relies on information that the CFPB has obtained from industry, other regulatory agencies, and publicly available sources, including reports published by the CFPB. These sources form the basis for the CFPB's consideration of the likely impacts of the proposed rule. The CFPB provides estimates, to the extent possible, of the potential benefits and costs to consumers and covered persons of this proposal given available data.

Specifically, this discussion is based on the CFPB's analysis of public Call Reports and other publicly available data sources, internal data from multiple supervisory information requests, as described in part II above, as well as research reports published by the CFPB. The CFPB also consulted the academic literature and policy analyses of United Kingdom and State regulators.

The CFPB acknowledges several important limitations that prevent a full determination of benefits, costs, and impacts. Quantifying the benefits, costs, and impacts requires quantifying consumer and depository institution responses to the proposed changes, and the CFPB finds the body of knowledge on relevant behavioral responses and elasticities incomplete. In particular, the CFPB is not aware of evidence that could be used to predict how changes to overdraft pricing would affect negative balance periods or the expected substitution effects across asset accounts and between deposit accounts with overdraft coverage and other forms of credit, including the consumer harm from delaying or forgoing some transactions. Similarly, the CFPB believes there is little reliable quantitative evidence available on the cost and effectiveness of steps financial institutions might take to facilitate clients' money management or timely repayment on overdrawn accounts; reprice any of their services; remunerate their staff, suppliers, or sources of capital differently; or enter or exit any or all segments of the checking account market. Thus, while the data and research available to the CFPB provide an important basis for understanding the likely effects of the proposal, the data and research are insufficient to fully quantify the potential effects of the proposal for consumers and very large financial institutions. This reflects, in part, the fact that the effects of the proposal would depend on choices made by independent actors in response to the proposal, and the data and research available to the CFPB do not

[230] 15 U.S.C. 1604(d).

allow reliable predictions of those choices.

In light of these data limitations, the analysis below provides quantitative estimates where possible and a qualitative discussion of the proposed rule's benefits, costs, and impacts. General economic principles and the CFPB's expertise, together with the available data, provide insight into these benefits, costs, and impacts. The CFPB requests additional data or studies that could help quantify the benefits and costs to consumers and covered persons of the proposed rule.

C. Baseline for Analysis

To evaluate the proposal's benefits, costs, and impacts, the CFPB measures the proposal's benefits, costs, and impacts against a baseline in which the CFPB would take no action. This baseline assumes existing regulations remain in place and that market conditions in the overdraft market do not change from their current state.

The discussion below assumes that, without action, both the overdraft credit market and the broader consumer checking market would function in the manner understood through past CFPB research, external academic literature, and supervisory activity. The CFPB bases its prediction for the baseline on market conditions and market data from the 2022 calendar year. As a result, its baseline reflects changes to the overdraft market through 2022, including changes to checking account pricing (both fee and net interest revenue) and changes to the speed, cost, availability, and prevalence of payment systems. The CFPB sees that the market is changing rapidly and might continue to do so absent the rule, but for purposes of the baseline the CFPB generally uses data from the most recent full calendar year to characterize the status quo.

D. Potential Benefits and Costs to Consumers and Covered Persons of the Proposed Changes That Affect Charges for Non-Covered and Covered Overdraft Credit

1. Potential Benefits and Costs to Consumers

In addition to other changes discussed later in this section and to the further changes discussed in the following section, the proposal would apply Regulation Z to above breakeven overdraft credit that is currently excepted from the regulation (*i.e.,* it is currently non-covered overdraft credit). Overdraft credit is above breakeven overdraft credit when a very large financial institution imposes a charge or combination of charges for such credit that exceeds the greater of either the average of the institution's costs and losses for providing non-covered overdraft credit (as defined in the proposal) or the benchmark fee published by the CFPB. The CFPB anticipates that its proposal generally would benefit consumers in two ways. First, some very large financial institutions may reduce their fees so that they can continue offering non-covered overdraft credit. In general, lower overdraft fees for non-covered overdraft credit would benefit consumers by reducing the amount they pay through these fees. Second, some financial institutions may continue offering above breakeven overdraft credit and apply the Regulation Z regulatory framework. In general, applying the Regulation Z regulatory framework to above breakeven overdraft credit would benefit consumers by promoting their informed use of such credit and by applying TILA's substantive protections. The CFPB's analysis may underestimate or overestimate the proposal's benefits to consumers depending on how various market participants, such as financial institutions covered by the proposal, entities not covered by the proposal, and consumers, respond to the proposal. The discussion below begins with an analysis of the proposal's direct benefits to consumers assuming that very large financial institutions comply with the proposal by lowering their fees for non-covered overdraft credit. The discussion then considers how other potential responses by very large financial institutions could impact the proposal's direct benefits to consumers. Next, the discussion considers how the proposal might impact consumer behavior, including demand for both covered and non-covered overdraft credit, demand for alternative credit products, and deposit behavior. Finally, the discussion briefly considers how institutions not covered by the proposal may respond to the proposal.

i. Estimated Savings to Consumers if Very Large Financial Institutions All Use the CFPB's Proposed Benchmark Fee or Breakeven Standard

Under the proposal, overdraft credit offered by very large financial institutions that currently is non-covered overdraft credit could remain non-covered overdraft credit if the per-transaction price for such credit were less than or equal to the benchmark fee established by the CFPB. Consequently, if all very large financial institutions were to use the benchmark fee to comply with the rule, the proposal's direct benefits to consumers, assuming no change in overdraft frequency, could be as high as the difference between the total fees currently paid by consumers for non-covered overdraft credit and the total fees they would pay if non-covered overdraft credit were priced at the benchmark fee.

Today, fees for non-covered overdraft credit are generally greater than $30 per transaction.[231] Under the proposal, fees for any non-covered overdraft product provided by a very large financial institution would be substantially lower. From Call Report data, the CFPB estimates that consumers paid $5.98 billion in overdraft fees to very large banks and thrifts in 2022. For this estimate, the CFPB started with CFPB-supervised banks' total reported consumer overdraft-related service charges levied on those transaction account and non-transaction savings account deposit products intended primarily for individuals for personal, household, or family use.[232] This amount was $6.42 billion in 2022, including fee revenue from both overdraft and NSF transactions. In prior work, the CFPB has estimated that, between January 2011 through June 2012, 18.9 percent of such revenue at several very large financial institutions was NSF fee revenue.[233] However, most of the largest banks eliminated NSF fees during 2022; the CFPB estimates that nearly two-thirds of supervised banks had eliminated NSF fees by mid-2023, representing an estimated 97 percent of annual NSF fee revenue earned by those institutions.[234] For purposes of this analysis, the CFPB estimates that the NSF fee share in 2022 was half as large as the earlier 18.9 percent share, so supervised banks' overdraft fees would be 90.55 percent of the 2022 fee total, or $5.81 billion. This total does not include fee revenue from credit unions that are very large financial institutions, since credit union call reports do not include data on overdraft fee

[231] In narrative responses to supervisory information requests, financial institutions generally stated that discretionary overdraft fees are set using factors such as: (1) the direct and indirect cost of offering OD services, (2) deterrence effects, (3) positioning with respect to other competitors, (4) customer feedback, experiences, and utility, (5) regulatory requirements and (6) safety and soundness concerns. CFPB 2024 Overdraft NSF Report at 11.

[232] This information is reported in Schedule RI, Memorandum item 15.a on the FFIEC 031 and 041 forms, as of September 2023. For most institutions, this definition also includes fees associated with sustained negative balances. Few charges related to overdraft transactions are reported as net interest revenue, if any.

[233] CFPB 2014 Data Point at 10 tbl.2.

[234] CFPB October 2023 Data Spotlight.

revenue.[235] To estimate overdraft revenue earned by CFPB-supervised (very large) credit unions, the CFPB estimates the overdraft revenue earned by all credit unions and distributes that estimated revenue to credit unions above and below $10 billion in assets based on those groups' relative share of member shares and deposits. The CFPB has estimated that overdraft revenue reported by banks with over $1 billion in assets comprises approximately 77 percent of the total overdraft/NSF revenue earned by banks and credit unions combined, while credit union overdraft/NSF revenue comprises approximately 15 percent of such revenue (overdraft/NSF revenue of banks under $1 billion in assets comprises approximately 7 percent of such revenue).[236] Banks with more than $1 billion in assets reported $7.72 billion in overdraft/NSF revenue in 2022, 90.55 percent or $7.00 billion of which the CFPB estimates is overdraft revenue for reasons explained above. Assuming this $7.00 billion represents 77 percent of the market total overdraft revenue, the CFPB estimates that credit unions earned 15 percent of the total, or $1.43 billion in overdraft revenue in 2022. At the end of 2022, very large credit unions held 24.1 percent of all member shares and deposits held by federally insured credit unions. Applying this 24.1 percent to $1.43 billion, the CFPB estimates that very large credit unions earned $0.34 billion in overdraft fees in 2022, and that very large financial institutions collectively earned $6.16 billion.

From information requests by the CFPB, it estimates the average overdraft fee amount to be $32.50.[237] The CFPB initially assumes that a reduction in the fee for non-covered overdraft credit would affect neither the quantity of credit demanded nor the quantity supplied, meaning that the application of the benchmark fee across the entire market would imply mechanical savings for consumers, unaffected by behavioral responses.[238] As discussed in part V(D)(2)(v), the CFPB has proposed four alternative values for the benchmark fee—$3, $6, $7, and $14. Assuming each proposed value would effectively be the new average fee across the market, the decline of the market total revenue would be proportional to the decline in the average fee amount. Thus, using a 2022 baseline, a $3 fee would have saved consumers $5.6 billion (90.8 percent of the 2022 total) annually, a $6 fee $5.0 billion (81.5 percent of the total), a $7 fee $4.8 billion (78.5 percent of the total), and a $14 fee $3.5 billion (56.9 percent of the total) in a calendar year.

Savings from lower fees would be particularly valuable in cases when they protect liquidity at times when the consumer needs it most. Consumers with low balances may deplete their asset account less frequently if they have paid less in overdraft fees in the past, and thus their asset account recovered to a higher balance after a sufficiently large deposit. Moreover, if fees, in particular multiple or cascading fees, deplete less of the buffer the depository institution is willing to lend to the consumer (*i.e.,* the shadow line of their non-covered overdraft credit), the consumer might be able to cover more or larger transactions with it when they have depleted their asset account. The same shadow line would permit more consumption. Current users of non-covered overdraft credit would enjoy similar benefits even if they end up with substitute products like covered overdraft credit, or linked asset or credit accounts, as long as the new source of liquidity is cheaper than non-covered overdraft is currently.

A large reduction in fees for non-covered overdraft could reduce some operating costs associated with complaints, collections, and account closures. Such benefits to covered persons do not need to reflect an equal but opposite pecuniary cost to consumers. Fewer complaints, collections, or account closures can save money for both the accountholder and the depository institution, who somehow split the value that would have been spent otherwise. These gains would mitigate some losses covered persons suffer from lower fee revenue, so they lose less on net, in total. The CFPB understands from its general monitoring activities that complaints fell by 70 percent or more at depository institutions that radically decreased overdraft fees recently. With lower fees and charges, the CFPB expects more non-covered or covered overdraft credit accounts to recover from negative balance episodes.

Very large financial institutions with per-incident costs and losses traceable to overdrawing transactions above the benchmark fee would have an incentive to set fees for non-covered overdraft using the breakeven standard described at proposed § 1026.62(d)(1)(i). Consumer gains when very large financial institutions with per-incident costs and losses above the benchmark fee use the breakeven standard would be less as their fee would not drop all the way to the benchmark fee. The gains for consumers would be even smaller if the application of the breakeven standard imposes additional administrative costs on the institutions who use it, and, in turn, those institutions shift some of these costs to their customers. However, the CFPB expects these administrative costs to be small compared to revenue.

[235] Some state-charted credit unions reported substantial overdraft revenue under California's Financial Code Section 521. *See* Dep't of Fin. Prot. & Innovation, *Annual Report of Income from Fees on Nonsufficient Funds and Overdraft Charges* (Mar. 2023), *https://dfpi.ca.gov/wp-content/uploads/sites/337/2023/04/Annual-Report-of-Income-from-Fees-on-Nonsufficient-Funds-and-Overdraft-Charges_2023.pdf* (DFPI 2023 Report).

[236] *See* CFPB 2021 Data Point at 7 (estimating combined overdraft/NSF revenue for credit unions and for banks with less than $1 billion in assets using 2014 data collected from core processors for the number of accounts by asset size and the overdraft/NSF revenue per account, and from 2014 call report data for distribution of institutions by asset size, and then assuming that overdraft/NSF revenue at small institutions saw the same growth from 2014 to 2019 as at large banks to arrive at the 2019 estimates). For purposes of this analysis, we assume that banks with assets over $1 billion, banks with assets below $1 billion, and all credit unions represent the same relative portions of total marketwide overdraft/NSF revenue in 2022 as they did in 2019.

[237] The CFPB requested information about some very large financial institutions' 2022 overdraft practices. For those institutions with available data on the number of instances of non-covered overdraft when the institution charged a fee, the reported weighted average fee amount was $32.50. CFPB 2024 Overdraft NSF Report. Based on the CFPB's review of publicly available information between December 2022 and July 2023, the unweighted median non-covered overdraft fee amount across all very large financial institutions was $35. Past CFPB research publications have reported the median non-covered overdraft fee as $35; this median was also based on data from very large financial institutions. A $35 fee is higher than the $25.77 fee recently reported by the New York State Department of Financial Services for 2022 based on a surveyed entities, most of which would not be subject to this proposal. *See* N.Y. State Dep't of Fin. Servs., *Consumer Fee Practices in New York* (July 14, 2023), *https://www.dfs.ny.gov/system/files/documents/2023/07/rpt_20230714_consumer_fee_practices_nys.pdf.* The Department of Financial Protection and Innovation of the State of California annually tabulates State-chartered banks' and credit unions' revenue from overdraft charges but not the fee amounts. *See* DFPI 2023 Report Note that to the extent market revenue or fees for very large financial institutions were lower by the effective date of the proposed rule, the proportional drop from a smaller market total would amount to less than these extrapolations from 2022 market revenue totals and fees. Bankrate's 2023 checking account and ATM fee survey reports that the average overdraft fee was 11 percent lower than a year before, *https://www.bankrate.com/banking/checking/checking-account-survey/* (last visited Jan. 7, 2024).

[238] This assumption approximates the situation where overdraft transactions are inadvertent (a fixed quantity demanded) and always met at the prevailing price, even after the supply curve shifts downward with the benchmark fee. As discussed elsewhere, this outcome is unlikely to hold exactly. Consumers might be less attentive to avoid overdraft when it is cheaper, though many might have larger buffers if earlier fees have depleted their account balances less than they would under the baseline. Financial institutions might also meet demand only at higher prices, applying the breakeven standard approach or offering covered overdraft credit instead.

Data produced in response to the CFPB's supervisory information requests on 2022 overdraft practices suggest that, for benchmark fee levels less than $14, at least some very large financial institutions would have traceable costs and losses per overdraft fee charged greater than the benchmark fee level, such that they could find it more advantageous to use the breakeven standard. The CFPB has less data on the costs and losses of other very large financial institutions, whose costs and losses (mostly their charge-off losses) may be higher than for some institutions in its supervisory information request collection. However, because the costs and losses of providing non-covered overdraft are driven largely by credit losses, and because these losses depend on underwriting policies, which, as discussed below, very large financial institutions likely would change in response to the proposed rule, current cost and loss levels may not be a reliable indicator of future cost and loss levels assuming the proposed rule were finalized.

Overdraft fees are incurred by consumers in an estimated 17 percent of households annually.[239] Among these, the consumers who would benefit most from the proposal are those that incur the largest number of overdraft fees. Thus, a change in fee amounts would have an outsized impact on specific groups of consumers. The CFPB collected 2022 calendar year information from entities it supervises (the group that would be affected by the proposed rule), which reinforced patterns of disparity that prior research of the CFPB and others established: [240] Overdraft and NSF fees comprised 53 percent of all fees that the institutions charged to consumer checking accounts, nearly three quarters of all fees charged to accounts with an average balance below $500 (lower balance accounts), and nearly three quarters of all fees charged to accounts where accountholders opted to authorize overdraft fees on debit card and ATM overdraft transactions (opted-in accounts). While overdraft-related fees averaged approximately $65 per year over all accounts, accountholders of opted-in accounts and accountholders of lower-balance accounts paid over $165 and $220, respectively, in total of overdraft fees per year on average. Therefore, the benefits of any fee changes driven by the proposal would be predominantly experienced by the small fraction of accountholders who had either opted-in accounts or lower-balance accounts because those accountholders paid the majority of overdraft fees. Indeed, in aggregate, across all institutions represented in the CFPB's Supervisory Information collection, one-fifth of accounts were lower-balance accounts, but these accounts paid 68 percent of per-item overdraft fees assessed. In fact, at least one institution charged over half of per-item overdraft fees to accounts that were both lower-balance accounts and opted-in accounts, even though only five percent of accounts fell into this category. Furthermore, accounts that paid for overdraft most often (twelve or more overdraft fees per year) were nearly five times as prevalent among opted-in accounts than not-opted-in accounts.

Overdraft use, and therefore the potential benefit from reduced fees, is also correlated with other consumer characteristics. As lower-income accountholders pay more fees, and minorities pay more fees even after controlling for income, these groups are more likely to benefit from the proposed changes.[241]

ii. Responses by the Depository Institutions Covered by the Proposal

Consumer gains would likely differ from the mechanical effect of lower fees on non-covered overdraft as described in the section above if some depository institutions would tailor their offering to the new environment as the proposed rule allows. The discussion in this subsection starts with the possibility that institutions might adjust underwriting standards or overdraft coverage limits for non-covered overdraft credit when the marginal profit on each non-covered overdraft transaction falls. Then the text turns to the decision of whether to waive the fees on some overdraft transactions. Next is the analysis of decisions about whether to instead extend products that substitute for non-covered overdraft, primarily covered overdraft credit but also transfers from linked asset accounts. Finally, the subsection discusses repricing of financial products, like maintenance fees on the underlying checking account.

The Availability of Non-Covered Overdraft Credit

Assuming that very large financial institutions comply with the proposal by lowering their fees for non-covered overdraft credit, these lower fees may change very large financial institutions' decisions about whether to extend non-covered overdraft credit for a given transaction on a given account. Financial institutions generally have discretion in setting overdraft policies.[242] When a financial institution decides whether to cover an overdraft transaction, it generally trades off the revenue from charging a fee against expected marginal costs and charge-off losses, although decisions about extending credit and charging or waiving a fee may also take into account their impact on the lifetime value of the customer as well as its reputation.[243] Lower potential fee revenue could impact the decision to extend non-covered overdraft credit. In addition, very large financial institutions often offer services that are substitutes for non-covered overdraft credit, including covered overdraft credit and the option of linking other asset accounts to a checking account such that those other accounts can, sometimes for a fee, be accessed in the event of a shortfall. If fees for non-covered overdraft credit were limited for very large financial institutions, they could have incentives to limit access to non-covered overdraft credit but encourage consumers to take advantage of these substitute services. Having said that, firms that use the breakeven standard and not the benchmark fee could be disincentivized from reducing overdraft transactions because to do so would necessarily reduce the firms' cost and loss basis for the next year's fee calculation for remaining overdraft customers but not yield profits over the long run.

In principle, very large financial institutions could respond to the

[239] FinHealth Spend Research Reports from 2021, 2022 and 2023 have estimated that 17 percent of responding households have paid an overdraft fee in the prior twelve months between November 2021 and January 2023. *See generally,* FHN, *Market Analysis: FinHealth Spend Research—Latest Research, https://finhealthnetwork.org/finhealth-spend-research/* (last visited Jan. 7, 2024).

[240] *See* CFPB Fall 2023 Highlight; *see also* CFPB 2014 Data; CFPB 2017 Data Point.

[241] Oz Shy & Joanna Stavins, *Who Is Paying All These Fees? An Empirical Analysis of Bank Account and Credit Card Fees* (Fed. Rsrv. Bank of Bos., Working Paper No. 22–18, 2022), *https://www.bostonfed.org/-/media/Documents/Workingpapers/PDF/2022/wp2218.pdf.*

[242] Institutions authorize and pay transactions that they are contractually obligated to, such as ''authorize positive, settle negative'' (APSN) transactions, since under applicable payment system rules, once a transaction is authorized, the financial institution must pay the transaction. Pursuant to the CFPA, charging an overdraft fee on such transactions can be unfair.

[243] In response to supervisory information requests, financial institutions said that when setting limits for discretionary overdraft they consider factors that could be relevant both to the risk of charge off and to the lifetime value of the customer, including (1) age of the account, (2) available balance, (3) account transaction activity and history, (4) standing of the account, and (5) existence of direct deposits. CFPB 2024 Overdraft NSF Report at 8.

proposed rule's changes by underwriting non-covered overdraft credit more conservatively, by reducing credit limits (whether or not disclosed to the accountholder) for accountholders with higher expected credit losses, or even by eliminating access to non-covered overdraft credit for some consumers who currently qualify for such credit, though as discussed later, the firms may offer other products instead. Limited access to non-covered overdraft could be beneficial to consumers with access to cheaper credit options they mistakenly forgo or to consumers who would have preferred that a transaction was declined rather than incurring an overdraft fee. Consumers often overdraw their account when they have liquid funds or available cheaper credit. In these cases, consumers might benefit from using those options instead of overdraft credit. However, there are scenarios, even when there are other credit options available and overdraft is more expensive, that the prompt completion of the transaction would be more valuable to consumers than the fee charged.

The CFPB is aware of an empirical study finding that relaxing restrictions to overdraft fees may result in increased access to deposit accounts with overdraft coverage.[244] The work, not yet peer-reviewed, analyzed an episode in 2001 in which national banks' sudden exemption from State fee caps permitted some banks to increase their fees for non-covered overdraft. The study attempts to identify the effect of the regulatory change by comparing national banks (which became exempt from State fee restrictions) to State banks (which did not), and also comparing banks in States that had such restrictions to States that did not.

The authors find that the analyzed change to fee caps seems to have led to higher overdraft fees at national banks in these States, expanded overdraft coverage at these banks, and more low-income households opening deposit accounts. In the setting studied, about 56 percent of consumers in the lowest income quartile did not have checking accounts before the regulatory change, and the authors estimate that this share fell by about five percentage points after the change. The findings are consistent with the regulatory change making it more profitable, in those States affected, for national banks to provide accounts to consumers who maintain low balances. The authors do not find evidence that the newly banked consumers regretted (or at least reverted) their choice or that they suffered worse financial health.

As with most modern empirical research in economics, the study focuses attention on the internal validity of the findings, *i.e.,* the measurement of the causal effect of the policy change at the time and place that it took effect. The study design relies on relatively strong assumptions to establish causation. The study's methodology requires establishing that differential trends at national and State institutions in affected States would have continued to diverge (or converge) at the same linear rate in the absence of the rule, and establishing this is made more difficult by the relatively short five-year window that the study uses from its data source.

Even assuming the internal validity of the findings, several differences in both the economic context and the nature of the regulatory change make it unlikely that the study's findings would apply directly if the proposed rule were finalized. The authors report that for the households in their data from 2001, 34 percent of households did not have a checking account,[245] whereas the FDIC reports that the share of households without a checking or savings account has fallen steadily over the last decade and that in 2021 only 4.5 percent of households are unbanked.[246] Even if new opportunities to earn overdraft revenue gave banks meaningful incentives to expand the types of checking accounts they offered in 2001, that does not necessarily mean that reductions in overdraft revenue in the current market would lead to similar reductions in overall bank account access. The study authors concluded that while their research suggested relaxing caps was beneficial to consumers without bank accounts in 2001, they did not reach the conclusion that relaxing the caps was beneficial to consumers who already had bank accounts, which, as noted above, since the time studied, has since become an even greater proportion of the population. Moreover, the proposal would not impose limits on all overdraft fees but rather would require very large financial institutions to comply with Regulation Z when offering covered overdraft credit.

A prominent precedent for a U.S. policy change affecting overdraft fee revenue was the implementation of the opt-in rule of Regulation E in August 2010. The CFPB is not aware of a careful empirical study that isolates the effect of this change in the market. That said, there was a substantial decrease in marketwide overdraft revenue following the introduction of the opt-in rule and a smaller decrease in total service charges, which suggests less than fully offsetting price responses.[247] However, isolating the effect of the opt-in rule is made more difficult by the fact that the implementation of the cap on very large financial institutions' interchange fees on debit cards came a mere three months later, and the Great Recession might also confound the effects of the opt-in rule alone. The CFPB's market monitoring activities also indicate that some institutions ceased to offer "free checking" after the 2010 changes.[248] The downward trend in the share of American adults without a bank account does not seem to have broken around the time of these changes in the long-running series of the Survey of Consumer Finances, and the FDIC's Survey of Household Use of Banking and Financial Services, which started in 2009, shows a small increase in the unbanked share in 2011 before steady declines thereafter.[249]

According to the CFPB's market monitoring, recent voluntary decreases in overdraft revenue at many large American depository institutions have not coincided with conspicuous restrictions of checking offerings or increases in other fees, though this period corresponded to increases in net interest revenue on deposits resulting from a changing interest rate environment.[250]

In some cases, in response to the proposed rule, the above referenced more conservative underwriting may lead lenders to reject transactions they

[244] Jennifer L. Dlugosz et al.,*Who Pays the Price? Overdraft Fee Ceilings and the Unbanked* (Fed. Rsrv. Bank of N.Y., Staff Rep. No. 9073, June 2021), *https://www.newyorkfed.org/medialibrary/media/research/staff_reports/sr973.pdf* (revised July 2023).

[245] *Id.* at 40 tbl.7.

[246] FDIC Tables at 3 tbl.A.2.

[247] As discussed in part II above, marketwide overdraft revenue (for both banks and credit unions) is estimated at approximately $25 billion in 2009, and fell to an estimated $12 billion in 2011. According to bank call report data, total bank deposit service charges fell from $41.7 billion in 2009 to $33.1 billion in 2011 and remained at a similar level in following years. While other factors may explain part of the reduction in deposit service charges, the large and persistent decrease suggests that banks did not make up all of the lost overdraft revenue from the 2009 opt-in rule by increasing other prices.

[248] *See, e.g.,* E. Scott Reckord, *At many big banks, no more free checking,* L.A. Times (Feb. 4, 2011), *https://www.latimes.com/archives/la-xpm-2011-feb-04-la-fi-free-checking-20110204-story.html.*

[249] Paola Boel & and Peter Zimmerman. *Unbanked in America: A Review of the Literature.* Econ. Comment. 2022–07 (Fed. Rsrv. Bank of Clev.), May 26, 2002, *https://www.clevelandfed.org/publications/economic-commentary/2022/ec-202207-unbanked-in-america-a-review-of-the-literature.* Note that the increase in the FDIC measure may have been impacted by the Financial Crisis.

[250] *See* CFPB May 2023 Data Spotlight.

would not have rejected under the baseline where consumers do not have other viable options. In such cases, some consumers would no longer have the option to use non-covered overdraft as credit, which means transactions would be declined, but also, the consumers would not incur its high cost and potential risks of account closure.

Overdraft use can also decrease due to financial institution responses that cause no consumer harm. With smaller profits on each transaction, very large financial institutions could have more of an incentive to educate their depositors and help them avoid negative balance episodes.[251] Financial institutions would also have less of an incentive to inflate the number of overdraft transactions with transaction posting orders designed to increase the number of overdraft fees.

Waiver Policies

Currently, a substantial fraction of overdraft fees is waived by financial institutions, either because regulation does not allow fees on transactions that are payed per contractual obligations (such as debit APSN transactions without opt-in), pursuant to an automatic policy like a daily maximum, or at the discretion of a customer service representative or manager, often called a discretionary waiver or a reversal after the fact. Lower fee amounts would change institutions' incentives related to whether to waive the fee by policy or discretion, which is a subset of overall waivers. For this decision, the depository institution trades off the net revenue from charging the fee against the expected value of a marginally better relationship with the customer. Lower fee amounts would affect both parts of this tradeoff. Lower potential fee revenue would mean that depository institutions would have less to lose by waiving a fee, while they also imply that there is less at stake for the consumer, likely making fee waivers less important to maintaining good customer relationships.

As discussed in part V(D)(2)(v), the $3 benchmark fee, in particular, would not have covered charge-off losses for the institution with the lowest credit losses in the CFPB's data for 2022 had they applied their current waiver policy so that they charged $3 only in instances where they actually charged their current higher fee in 2022. This suggests that institutions that currently waive or reverse fees might reconsider their policies if a benchmark fee did not allow them to recoup their costs and losses on their non-covered overdraft credit product, if product-specific profit targets were more important in practice than the marginal incentives for individual waivers. Were an institution to adopt the breakeven standard, it would charge higher fees but could waive the fee on fewer or more instances than in the baseline without any impact on its profit. Institutions adopting the breakeven standard would have an incentive to tailor their waiver policies to foster customer goodwill and retention according to the accountholder's lifetime value to the institution.

A decrease in the chance of a waiver would shift the consumer experience from higher overdraft fees (as much as $35) that might be waived discretionarily, to lower overdraft fees (as low as $3) that are more predictable. On net, the CFPB expects that shift to lower costs and create more predictability for consumers. In addition, the discretionary nature of some fee waivers can lead to the potential for disparate treatment of customers, as some customers may be more likely to get an overdraft fee waived than others. This disparate treatment would amount to what has been called ''contractual inequality.''[252] A substantial decrease in discretionary waivers is likely to move towards more equality of waiver rates across underprivileged and more privileged groups.

Expanding Covered Overdraft Credit or Other Substitutes for Non-Covered Overdraft

Financial institutions may choose to offer covered overdraft credit in addition to or instead of non-covered overdraft credit. Whether consumers would choose to apply for and use covered overdraft products, and whether very large financial institutions would find it profitable to offer them, depends on a number of factors, and available evidence does not permit the CFPB to confidently predict whether or how such products would develop. In particular, it would depend on the price that the market will bear for these products in new segments, as well as the cost and time required to develop reliable underwriting and consumer acquisition systems to support such products.

Lines of credit on any such new covered overdraft product might be smaller than on existing covered overdraft lines of credit, which generally focus on premium market segments.

If underwriting these covered overdraft credit lines on the new accounts would require extensions of existing systems or new installations at many institutions, transitioning a new customer base to covered overdraft credit would take time and experimentation, even at institutions with experience underwriting credit cards or extant overdraft lines of credit. The frequent overdrafter population might be profitable to underwrite with small lines, but few financial institutions would have experience underwriting such small lines of credit for this population (either for a credit card or extant overdraft lines of credit). The effective date proposed would leave time for very large financial institutions to experiment before implementation, which could facilitate development of new covered overdraft credit offerings.

If frictions slowed the transition of consumers from non-covered to covered overdraft credit, fewer consumers would receive the new coverage at institutions that try to move some of their overdraft customers into a covered product.

Past experience offers little guidance on the extent to which very large

[251] Various pieces of evidence have bolstered the view that overdraft is a mistake for many. Stango and Zinman document that surveying consumers about overdraft makes them use it less, strongly suggesting that they overuse the service when they are paying less attention. *See* Victor Stango & Jonathan Zinman, *Limited and Varying Consumer Attention: Evidence from Shocks to the Salience of Bank Overdraft Fees,* 27 Rev. Fin. Stud. 990–1030 (2014), *https://academic.oup.com/rfs/article/27/4/990/1603971*). Alan et al. ran an experiment in Turkey, where overdraft fee discounts lowered use while messages about availability raised it, suggesting that consumers are overdrawing their account without regard to the actual fees and even a discounted price is too high for them when it draws their attention. Sule Alan et al., *Unshrouding: Evidence from Bank Overdrafts in Turkey,* 73 J. Fin. 481–522 (2018), *https://onlinelibrary.wiley.com/doi/full/10.1111/jofi.12593*). Grubb modeled the direct and indirect consequences of just-in time ''bill-shock alerts'' (*e.g.,* for debit card transactions) on consumers and finds that the overdraft market is ripe for such reminders, as people differ in how much attention they pay to their available balance. Michael D. Grubb, *Consumer Inattention and Bill-Shock Regulation,* 82 Rev. Econ. Stud. 219–57 (2015), *https://academic.oup.com/restud/article/82/1/219/1543467*). Grubb et al. indeed report on field experiments in the UK where timely text message alerts saved consumers 11 to 27 percent of overdraft fees, which also shows that many had available funds elsewhere. Michael D. Grubb et al., *Sending Out an SOS: Automatic Enrollment Experiments for Overdraft Alerts* (forthcoming in the Journal of Finance), *https://sites.google.com/bc.edu/michael-grubb/research.* Heidhues and Koszegi use overdraft as their prime example of markets where providers exploit the mistakes of some consumers. Paul Heidhues & Botond Koszegi, *Naïveté-Based Discrimination,* 132 The Q. J. of Econ. 1019, 1019–1054 (May 2017), *https://academic.oup.com/qje/article/132/2/1019/2724551?searchresult=1.* Gathergood and Olafsson find in granular administrative data some overdraft behaviors impossible to rationalize. John Gathergood & Arna Olafsson, *The Co-holding Puzzle: New Evidence from Transaction-Level Data* (Oct 10, 2023), *https://ssrn.com/abstract=3607560.*

[252] Manisha Padi, *Contractual Inequality,* 120 Mich. L. Rev. 825, at 834–40 (2021).

financial institutions would attempt to transition current non-covered overdraft transactions into a covered product. As depository institutions generally target existing covered overdraft credit as a premium product at customers with low charge-off risks and high expected lifetime value to the institution, inertia might imply that customers who are more likely to struggle to recover from a negative balance episode continue to access a non-covered overdraft product subject to the new breakeven or benchmark limits, keeping non-covered overdraft fees higher under the breakeven standard than otherwise.[253] When overdraft credit is covered overdraft credit, institutions may find it harder to quickly adjust credit limits, an advantage to institutions of non-covered overdraft credit that is more important for institutions when extending overdraft credit that is less likely to be repaid.

The disclosure provisions of Regulation Z might result in more competitive pressure on the pricing of covered overdraft credit products than currently exists for non-covered overdraft credit. An increase in competitive pressure could mean that new covered overdraft products would be less expensive than existing non-covered overdraft products for the same consumers and coverage.[254]

Consumers would also stand to gain from the availability of covered overdraft credit because meeting periodic minimum payments, which are generally lower than the full balance, would allow them to revolve their overdraft debt and cover more extended needs for liquidity. They could also pay less in per-transaction fees if their asset account, not depleted by full repayment of prior overdrafts, would cover more transactions while the credit account carries a balance. Periodic repayment saves consumers some per-transaction finance charges at the cost of somewhat higher periodic charges resulting from a credit balance remaining outstanding for longer. Furthermore, consumers who cannot repay the overdrawn amount within 60 days, when non-covered overdraft credit balances are typically charged off, might benefit from revolving their covered overdraft credit balance for a longer period of time.

Consumers who go delinquent on new covered overdraft credit accounts would have their credit negatively impacted if the delinquency is reported to consumer reporting agencies, though not necessarily with more dire consequences than with a negative report to checking account reporting companies after involuntary account closure due to a negative balance on the original asset account that would have resulted from similar behavior with non-covered overdraft credit in the absence of the proposed rule.

When consumers at very large financial institutions are offered covered overdraft credit, that covered overdraft credit would not be subject to the Regulation E opt-in requirement for non-covered debit card overdraft. However, it would be subject to Regulation Z's application and solicitation requirements and limitations on the issuance of credit cards if it can be accessed by a hybrid debit-credit card. Consumers would not separately consent, the same way as Regulation E currently requires, to overdraft charges on one-time debit card and ATM transactions. A very large financial institution would be permitted, instead, to simply give the consumer the choice to apply for covered overdraft credit that would be extended to cover any overdrawing transaction (whether it be check, ACH, debit card, ATM, or any other form). Once the account is established, the CFPB expects those covered overdraft accounts to be presented to consumers as a credit account on phone applications, accounts on websites, and periodic statements, which would call attention to the fact that covered overdraft credit is a credit product.

Consumers who choose to have covered overdraft credit that is accessible by a hybrid debit-credit card might be better off than those who are opted into non-covered overdraft credit on one-time debit card and ATM transactions today if the same amount of credit for the same transactions costs less, as discussed above, or because of the other protections included in this proposed rule. Where a financial institution only offers covered overdraft credit bundled for all transaction types, consumers who are not opted in today would gain the right to, effectively, refrain from opting into overdraft on transactions other than one-time debit and ATMs. They would lose, however, the ability to refrain from opting into overdraft for one-time debit and ATMs while intentionally keeping overdraft for other transactions. It is unclear how many consumers would prefer the default of Regulation E, particularly given evidence that consumer understanding of the Reg E opt-in right is low.[255] Loss of this choice would be an issue where the financial institution is offering covered overdraft credit and does not give consumers a choice on which transactions can access the covered overdraft.

If very large financial institutions chose to offer closed-end covered overdraft credit, such closed-end covered overdraft credit would not be subject to the substantive protections discussed above. Instead, it would be subject to the disclosure requirements that apply to closed-end credit. The CFPB believes it is unlikely that this product would be provided.

With non-covered overdraft credit less profitable for financial institutions and available to fewer consumers, both institutions and consumers would have greater incentive to take advantage of linked accounts. Institutions might offer and promote more of these opportunities. Transfer fees on linked asset accounts to cover overdrawing checking account debits can result in costs for consumers but protect them from unnecessary borrowing if they indeed have liquid assets elsewhere. Links to existing credit lines like credit cards would not have this benefit but give more control to consumers to shop for rates and decide on repayment, with potentially still lower transfer fees than fees on non-covered overdraft credit under the proposal. Transfer fees for transfers from both savings accounts and credit accounts have been less common among the largest banks in recent years than they were prior.[256]

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[253] Interest rates are similar on arranged and unarranged overdrafts in the United Kingdom, following recent regulation setting a comparable pricing structure on both. *See* Danail Vasilev et al., Fin. Conduct Auth., *Evaluation Paper 23/1: An evaluation of our 2019 overdrafts intervention* (Apr. 2023), *https://www.fca.org.uk/publications/corporate-documents/evaluation-paper-23-1-evaluation-our-2019-overdrafts-intervention* (FCA 2023)). This could suggest similar pricing for covered overdraft credit as for current non-covered overdraft credit, even if it becomes better disclosed and the credit limits are clearer than current shadow lines. However, the same British reform also resulted in expanding arranged overdraft lines and smaller unarranged lines in addition, which suggests that covered overdraft credit could also become competitive or even prevalent in the United States.

[254] Regulatory constraints may also affect the fees charged for covered overdraft credit. For example, for open-end covered overdraft credit accounts accessible with a hybrid debit credit card, the fee-harvesting provisions in § 1026.52(a) would limit some fees that very large financial institutions can charge in the first year of a new account to 25 percent of the approved credit line. Section 1026.52(a) does not, however, limit charges that are assessed as periodic rates.

[255] Pew Charitable Tr., *Overdraft Does Not Meet the Needs of Most Consumers* (Dec. 2017), *https://www.pewtrusts.org/-/media/assets/2017/12/cb_overdraft_does_not_meet_the_needs_of_most_consumers.pdf* (3 of 4 consumers do not understand they have a right to not opt in to overdraft on debit card transactions).

[256] Based on the CFPB's review of publicly available information in June 2023, of the 20 banks reporting the most in overdraft/NSF revenue in 2021, 18 were not charging a transfer fee to transfer funds from a savings account to cover an overdraft,

Offsetting Changes to Other Deposit Account Prices

As discussed above, the proposed rule would lead to reductions in non-covered overdraft revenue at many financial institutions, and it is uncertain whether that revenue would be replaced, potentially by revenue from covered overdraft or other substitute products. Overdraft provider responses to this lost revenue would affect both the sum of consumer gains and their distribution across market segments and populations. Total consumer gains will be lower if very large financial institutions make up for lost overdraft fee revenue and any potential increase in costs by raising revenue by increasing other checking account prices or decreasing rates paid on deposit accounts. Whether financial institutions would offset lost overdraft fee revenue in this way for some or all deposit accounts would depend on a number of factors, including overall profitability of deposit accounts and the nature of competition among financial institutions.

To give an upper bound on how much lost revenue might be offset on a per-account basis, the CFPB estimates the mechanically lost revenue per account from non-covered overdraft fees without any behavioral responses. While full offset of the revenue loss is not a likely scenario, calculating this upper bound provides some quantitative context for understanding the limits of potential lost revenue and corresponding changes that might result. The CFPB does not have current information on the number of active checking accounts at all very large financial institutions but requested such information for 2022 from eight very large financial institutions in a supervisory capacity. For these institutions, the overall average overdraft fee revenue from any active account-month was $3.77. Of course, the proposed rule would not eliminate all overdraft fee revenue. Were the CFPB to finalize with a $3 benchmark (and again, assuming for analytical purposes full adoption of the benchmark), financial institutions would lose approximately 90.8 percent in weighted average fee revenue (from $32.50 average fees to the $3 benchmark proposal), totalling a revenue loss of $3.42 per account per month. An 81.5 percent drop in average fee revenue (assuming a $6 benchmark) would be result in $3 of lost revenue per account per month. For a $7 benchmark, that figure is $2.96. For the $14 benchmark, that figure is $2.15.

The magnitude of these extreme upper bounds on lost revenue per account reassures the CFPB that any potential losses to banking access can remain limited. In fact, there are large financial institutions for which this proposed rule is unlikely to result in substantial reductions in revenue.[257] Furthermore, this decrease in overdraft revenue is likely to be on-par with, if not lower than, the voluntary decrease in revenue many large financial institutions already absorbed between 2019 and 2022, without apparent disruptions to checking and overdraft access.[258] The proposed fee reductions are in some ways similar to new regulations of the overdraft market in the United Kingdom in 2019, whose impacts the Financial Conduct Authority evaluated ex-post with a careful causal analysis. Their findings are generally consistent with the CFPB's expectations about limited disruption to checking and credit access and no complete offset of lost overdraft revenue.[259]

Offsetting changes in prices, if any, would limit the benefits consumers gain from the proposal (as well as the corresponding costs to covered persons), but also redistribute the burden of paying for consumer checking services in the United States. Those consumers who are currently frequent users of high-cost non-covered overdraft credit would benefit substantially from lower fees even if checking account APY or maintenance fees adjust, as those adjustments are unlikely to be similarly concentrated. Consumers who currently receive cross-subsidies from frequent (or just occasional) overdrafters, but might now receive lower net interest or pay higher maintenance fees to their checking provider, would incur only modest losses under the proposal relative to the baseline.

Under the baseline scenario for this analysis, very large financial institutions generally do not charge nonsufficient fund fees for transactions that consumers attempt to authorize in close to real time, which could include non-recurring debit card transactions or certain person-to-person transactions. Consumers with less access to overdraft credit due to this proposal would not pay fees on these types of transactions that they attempted but that were not authorized. However, the CFPB recognizes that financial institutions under the baseline could start to charge such fees in the future if they are not subject to the penalty fees limitation in § 1026.52(b). Other types of transactions can and might continue to trigger NSF fees when declined, although, as noted earlier, the significant majority of supervised entities subject to the proposal eliminated such fees during 2022 and early 2023.

iii. Responses by Consumers

A lower price for non-covered overdraft credit would lead some consumers to use the product more on the margin, assuming it remains available to them. For those who are attentive to the price of the product, who are also likely to use the product deliberately and experience liquidity and convenience benefits outweighing the cost, any additional utilization would likely provide net benefits. Inattentive consumers, for whom overdraft has already often been a mistake, would continue to be unlikely to pay attention to and rationally consider the lower cost of overdrawing their balance, and would thus be unlikely to use overdraft more even at a lower price.

Some consumers might keep a lower deposit balance as long as their overdraft protection seems sufficient but is now cheaper. As consumers with checking account balances forgo a net interest margin of 250 basis points[260] relative to short-term Treasury bill yields, on average, every $500 in deposits shifted from a checking account to an account with short-term Treasury bill yields would earn each consumer an additional average $12.50 over a year. Others might keep higher balances in their checking accounts if the proposed rule were to reduce their access to overdraft credit or if more salient use of overdraft credit made them try harder to avoid it. The cost-of-credit disclosures required for covered overdraft credit make its use more salient for the switchers than non-covered overdraft used to be. Consumers

and 16 were not charging a fee to transfer funds from a credit account.

[257] *See* CFPB, Chart of *Overdraft/NSF metrics for Top 20 banks based on overdraft/NSF revenue reported* (Feb. 2022), *https://files.consumerfinance.gov/f/documents/cfpb_overdraft-chart_2022-02.pdf.* At least one of these banks charges overdraft fees that are already less than fee benchmarks under consideration in this proposed rule.

[258] CFPB May 2023 Data Spotlight.

[259] *See* FCA 2023.

[260] The FDIC has been reporting national average interest rates on checking accounts since 2009, separately for non-jumbo and jumbo accounts until 2021. For much of this history, nominal interest rates hit the zero lower bound. For months with four-week Treasury yields below one hundred basis points, the national average (non-jumbo) checking account paid 8.3 basis points less. In other times, partly because checking account APYs have not risen as fast as short-term nominal interest rates, checking accounts paid 251.7 basis points below the four-week Treasury bill yield, on average.

who keep more in their checking account may forgo more interest on their savings if they would have otherwise kept it in higher-yielding accounts.

Some consumers may also choose different depository institutions, as account terms change as a result of the proposed rule. The ability to do so will generally increase consumer benefits and reduce consumer costs. For example, consumers who frequently overdraft at banks that are not very large financial institutions could switch to an account at a very large financial institution if non-covered overdraft credit is available there at lower cost. Conversely, a consumer at a very large financial institution that loses access to non-covered overdraft credit as a result of the rule could switch their account to another institution that is not covered by the proposed rule.

To the extent that marginal consumers could expect to pay a predictable and lower amount for checking overall, the proposal would encourage unbanked or underbanked customers to return to the banking system and gain access to FDIC insurance and the low cost payments system banks provide.

Overdraft use might also change because very large financial institutions would need to better disclose newly covered overdraft credit to consumers, which can only help them. For consumers who would use overdraft more because of this, their increased use may suggest that they would be deliberately taking advantage of a product worth its price for them. For consumers who would use overdraft less after these changes, better information might correct prior misunderstandings and prevent further mistakes.

Better disclosure would also help consumers compare the costs of different forms of credit (or other options to delay or forgo transactions), which provides direct benefits to those who are able to make more informed choices, and also provides indirect benefits to other potential users as more intensive comparison shopping would bring down prices among competitors.

Consumers currently not opting into one-time debit card transaction coverage by their non-covered overdraft service under Regulation E may be more likely to opt into such coverage under lower prices. To the extent these consumers pay particular attention to the fee and how it might affect them, they are less likely to regret when they use non-covered overdraft credit than others and are thus more likely to benefit from the proposed rule.

iv. Responses by Financial Institutions Not Covered by the Proposal

The proposal would only apply to very large financial institutions, and if finalized, would not lead to any new compliance costs for financial institutions not covered by the proposal.

The CFPB recognizes that a bank or credit union's demand for deposits (including demand and time deposits) derives from a multitude of factors, including, but not limited to, meeting expected loan demand and liquidity needs. In addition, when consumers select a deposit product, they rely on many factors unrelated to the overdraft pricing, including ATM and branch availability, interest rate, and expected customer service.

As the proposal outlines, many large financial institutions have already substantially reduced overdraft fees. During this time, there was no major shift in the total share of deposits from small financial institutions to very large financial institutions.

The CFPB acknowledges that is difficult to predict with certainty as to how very large financial institutions would evolve their business models over time. Of course, as with any change in business strategies by market participants with substantial market shares, this may ultimately lead to evolving industry dynamics with uncertain benefits and costs.

2. Potential Benefits and Costs to Covered Persons

This proposed rulemaking would affect the consumer business of certain depository institutions with more than $10 billion in assets. At the end of calendar year 2022, used for some tabulations here, this list included 176 depository institutions.

For covered persons, costs and benefits mostly mirror the existence and extent of each respective pecuniary benefit or cost to their customers, as detailed above, net of offsetting changes. By the very nature of this relationship, the CFPB has considered the various causes, mediating channels and modulating responses affecting costs and benefits to covered persons as carefully as for consumers, and much of the discussion of the factors and mechanisms affecting potential consumer pecuniary benefits and costs in the previous section also applies to the potential costs and benefits, respectively, of the proposed rule for covered persons.

In particular, the proposed rule would reduce the revenue of very large financial institutions from non-covered overdraft credit, and these institutions may be able to offset this lost revenue in various ways, including expanding their offerings of covered overdraft or other services that substitute for non-covered overdraft credit. The extent to which depository institutions will be able to pass the price changes of checking accounts under the proposed rule onto input prices depends on the pricing pressures on capital, labor, and intermediary goods, and services that very large financial institutions pay for. Due to their complexity, the CFPB has not modeled them in detail.

The operating cost of offering covered overdraft may be higher than the cost of providing similar non-covered overdraft credit. This arises from the costs of complying with Regulations Z and E, and potentially other laws. The covered persons might bear these costs if market forces do not let them pass some of them on to the consumer.

Very large financial institutions already have to provide disclosures per Regulations DD and E for non-covered overdraft credit. If they chose to continue offering non-covered overdraft credit, they would need to update these systems to make sure they accurately disclose and charge the new lower fees. If they decided to offer covered overdraft credit instead to any customer, then the disclosures would follow Regulation Z. The one-time cost of setting up a new covered overdraft program or transitioning consumers to existing covered overdraft programs could be substantial. The compulsory use prohibition would impose an administrative burden on the institution to offer another form of payment to the covered overdraft credit customer, as well as the operating cost of collecting the payment.

As discussed in the previous section, mechanical application of the benchmark fee amount to existing non-covered overdraft could reduce revenue of very large financial institutions by $3.5 billion to $5.6 billion, depending on the benchmark fee amount. This revenue impact on covered persons is limited by the proposal's design, which allows depository institutions to collect their costs and losses in overdraft fees. Part V.C.3.ii details why the CFPB believes that the benchmark fee number would allow some very large financial institutions to cover their costs and losses. Where the benchmark fee number would not allow this, fees set based on the breakeven standard would allow institutions to recover their costs and losses over time. This mechanism ensures that even entities that would see less revenue due to this proposal need not take losses on overdraft credit, unless they charge lower fees than the proposal would allow. And financial institutions whose per-transaction traceable costs and losses are lower than the benchmark fee could charge that fee and thereby make a profit on overdraft.

The CFPB finds it plausible that a different revenue model for checking in the U.S. that may result from the proposed rule will have broader implications on counterparties, competitors, or new entrants, or elsewhere in the economy. Such considerations would be too speculative for this impact analysis.

E. Potential Benefits and Costs to Consumers and Covered Persons of Further Provisions of the Proposed Rule

The CFPB is also proposing to apply the Regulation E compulsory-use prohibition to covered overdraft credit provided by a very large financial institution. The CFPB is not proposing to amend the Regulation Z prohibition against offset, nor is the CFPB proposing to amend the Regulation Z provision permitting periodic deductions. The proposal's approach to these provisions would affect the costs and benefits for consumers and covered persons of consumers potentially switching from non-covered overdraft to covered overdraft. Consumers who have access to covered overdraft credit but consciously avoid pre-authorized EFTs to repay covered overdraft credit are likely to benefit from the compulsory use prohibition, which would give them additional control over their finances, though they might be overoptimistic about their future repayment discipline, and mistakenly turn down automatic payments, to their detriment. Consumers who forget to repay can incur additional costs, including late fees, default interest rates or negative credit reporting after a period of delinquency. Some consumers might not be able to switch to covered overdraft credit if their depository institution was on the margin of offering it and they deem the consumer too prone to delinquency without a pre-authorized EFT for repayment. It is less likely that existing users of covered overdraft credit would be impacted for the same reason, as they are typically premium customers not on the margin of profitability.

Covered persons should not incur substantial cost from establishing repayment options in addition to a preauthorized EFTs. They can feasibly establish processes for consumers to have the repayment option of authorizing individual EFTs. Covered overdraft credit accounts that are not accessible via a hybrid debit-credit card would not be subject to the no-offset provision of Regulation Z.

Consumers with covered overdraft who do not repay their balance with frequent preauthorized EFTs pay either more interest from debt held longer or the hassle cost of making unscheduled repayments more often.

On covered overdraft credit accounts accessible via a debit card (a hybrid debit-credit card), financial institutions cannot automatically offset the credit balance against a positive balance on the associated asset account after a deposit. Therefore, consumers would be able to pay new debit transactions from the asset account before they repay the credit account. As discussed above, this flexibility in when to repay debt will generally give consumers better opportunities to manage their finances, although in practice the extent of any benefit to consumers from being able to delay repayment depends on finance charges for the credit and whether delaying repayment out of the asset account allows them to avoid higher additional credit charges for new transactions.

Consumers making purchases by using hybrid debit-credit cards that access covered overdraft credit would also benefit from the proposed rule's effect on dispute resolution for such purchases. The CFPB expects the burden on covered persons from this occasional service to be minimal.

The CFPB is also proposing to require very large financial institutions that provide covered overdraft credit to do so through a credit account that is separate from the associated asset account. These provisions would clarify that a very large financial institution must treat existing deposit accounts with overdraft credit that is currently non-covered overdraft credit, but that the institution chooses to provide as above breakeven covered overdraft credit subsequent to the rule, as a new credit account for purposes of Regulation Z. Consumers with hybrid debit-credit cards able to access a covered overdraft credit account, and the very large financial institutions that provide these accounts, would then be subject to the CARD Act protections in subpart G of Regulation Z.

Section 1026.51 would require card issuers to consider consumers' ability to make the required minimum periodic payments under the terms of the account. This could generally reduce the amount of credit available to some consumers, and some consumers may benefit from this requirement if it makes it less likely that they are burdened with covered overdraft debt for which they are unlikely to be able to make required minimum periodic payments. Because the safe harbor requires lenders to estimate whether consumers can repay the minimum payment and all fees assuming full use of the credit line, this could result in firms setting more concrete and less fluid credit limits, could result in lower credit limits, and firms might institute minimum payment formulas that do not require full payment of overdrafted amounts every month.

Section 1026.52(a) would limit fees charged in the first year a covered overdraft credit account is open to 25 percent of the account's credit limit. (Section 1026.52(a) does not restrict charges attributable to periodic interest rates; see comment 1026.52(a)(2)–1.) This could benefit consumers with hybrid debit-credit cards able to access a covered overdraft credit account in the first year the account is open. Any reduction in fees paid by consumers as a result of 1026.52(a) would result in a corresponding cost to covered persons from decreased fee revenue. Developing and implementing pricing strategies for covered overdraft products that comply with these requirements could impose costs on the covered persons providing these products, though the CFPB does not expect these costs to impose a substantial direct burden.

Penalty fees, like declined transaction fees, for violating the terms of the covered overdraft credit account would be subject to limitations under § 1026.52(b), providing further benefits to consumers who would have paid such fees. For example, § 1026.52(b) would restrict NSF fees from being charged on ACH transactions on accounts that have covered overdraft credit that is accessible by a hybrid debit-credit card. Consumers that would have been charged penalty fees, including NSF fees on debit card or ACH transactions, would benefit by not being charged these fees. Similarly, financial institutions that would have received NSF fee revenue from these transactions would see a decrease in revenue. Yet, the CFPB understands that NSF fees are currently rarely charged on debit card transactions and, as discussed above, most of the largest banks have already eliminated all NSF fees. This suggests that the benefits to consumers and costs to covered persons from this restriction are likely to be limited.

Very large financial institutions would be required to provide credit account opening disclosures and comply with other requirements of credit account opening in connection with tying covered overdraft credit to deposit accounts that already exist.

Applying new credit account opening requirements in connection with deposit accounts of consumers who already have existing non-covered overdraft credit that the institution chooses to replace with covered overdraft credit under the proposal will impose some costs on the depository institution.

Under the proposed rule, above breakeven overdraft credit would no longer qualify as ''incidental credit'' under § 1002.3 and thus would be newly subject to certain requirements under Regulation B, including with respect to providing notice and record-keeping. These obligations would have costs to covered persons.

The proposed changes, including proposed changes to the definition of finance charge, may affect other legal requirements under various Federal and State laws, including the Military Lending Act, usury limits, capital requirements, and interchange fees. The CFPB acknowledges that some or all of these legal requirements might also affect charges for non-covered and covered overdraft credit indirectly. However, the CFPB has not attempted to quantify the effects of such changes because it is not responsible for interpreting those laws and regulations and therefore cannot provide the detailed predictions about their effects that would be required for quantification; moreover, the CFPB does not predict the extent to which very large financial institutions will choose to offer covered overdraft credit that is subject to those rules. The CFPB seeks comment on the extent to which these considerations should affect its analysis.

F. Potential Specific Impacts of the Proposed Rule on Depository Institutions and Credit Unions With $10 Billion or Less in Total Assets, as Described in CFPA Section 1026

As this proposed rule applies only to financial institutions with more than $10 billion in total assets, the CFPB expects no specific impact on small entities directly. Subsection VIII.D.1.iv above discusses how the CFPB understands the proposed rule's indirect impact on these entities.

G. Potential Specific Impacts of the Proposed Rule on Consumer Access to Credit and on Consumers in Rural Areas

As discussed above, the proposed rule would likely lead to an increase in overdraft credit regulated by TILA and Regulation Z, and for remaining non-covered overdraft credit, a decrease in the fee.

To the extent that consumers in rural areas bank with institutions other than very large financial institutions, the impact of the proposed rule on these areas will be limited.

The CFPB has limited insight into overdraft practices in rural areas specifically. It is not aware of reasons to suggest more adverse or particular impacts in rural areas.

The CFPB has tabulated the share of the unbanked in lowest fifth of the income distribution in ZIP codes that the Census classified as urban, rural, or with a fraction rural.[261] With this precise measurement, both fully urban or fully rural areas see 74 percent of those with lowest incomes with a bank account, with slight variations in the ratio for the mixed ZIP codes in between. This makes the CFPB expect that urban and rural areas have similar exposure to overdraft fees, and would likely experience similar impacts from the proposed rule.

The CFPB has also tabulated the average credit score in each ZIP code, in the latest year available in a public dataset released by researchers at the Federal Reserve Board.[262] Fully rural ZIP codes have higher credit scores (719.6 on average) than fully urban ZIP codes (713.7), though with even higher averages scores in mostly urban areas and the lowest averages for fairly rural areas. This again suggests that on average, rural areas would have as much access to newly underwritten covered overdraft credit as the rest of the United States.

IX. Regulatory Flexibility Act Analysis

The Regulatory Flexibility Act (RFA) generally requires an agency to conduct an initial regulatory flexibility analysis (IRFA) and a final regulatory flexibility analysis of any rule subject to notice-and-comment rulemaking requirements unless the agency certifies that the rule will not have a significant economic impact on a substantial number of small entities (SISNOSE). The CFPB is also subject to specific additional procedures under the RFA involving convening a panel to consult with small business representatives before proposing a rule for which an IRFA is required. An IRFA is not required for this proposal because the proposal, if adopted, would not have a SISNOSE.

Small institutions, for the purposes of the Small Business Regulatory Enforcement Fairness Act (SBREFA) of 1996, are defined by the Small Business Administration. Effective March 17, 2023, financial institutions with less than $850 million in total assets are determined to be small.[263]

As this proposed rule only applies to financial institutions with more than $10 billion in total assets, it affects no small entities.

Accordingly, the Director hereby certifies that this proposal, if adopted, would not have a significant economic impact on a substantial number of small entities. Thus, neither an IRFA nor a small business review panel is required for this proposal. The CFPB requests comment on the analysis above.

X. Paperwork Reduction Act

Under the Paperwork Reduction Act of 1995 (PRA), Federal agencies are generally required to seek the Office of Management and Budget's (OMB's) approval for information collection requirements prior to implementation.

Under the PRA, the CFPB may not conduct or sponsor and, notwithstanding any other provision of law, a person is not required to respond to an information collection unless the information collection displays a valid control number assigned by OMB.

The proposed rule amends 12 CFR 1005 (Regulation E), which implements the Electronic Funds Transfer Act, which is assigned OMB control number 3170–0014, which expires 5/31/2025, as well as 12 CFR 1026 (Regulation Z), which implements the Truth in Lending Act and is assigned OMB Control number 3170–0015, which expires 05/31/2025. However, this proposed rule may, in addition to the information collection requirements of Regulation Z, affect the information collection requirements contained in 12 CFR part 1002 (Regulation B), which implements ECOA, which is assigned OMB Control number 3170–0013 which expires 08/31/2026. A full description of those changes and the estimated burdens thereof can be found in the Supporting Statements for each affected regulation that have been filed with OMB in connection with this proposed rule and are available as part of its public docket.

The CFPB has a continuing interest in the public's opinions regarding this determination. At any time, comments regarding this determination may be

[261] Cox et al. (2022) identified the unbanked in the universe of tax records as those not listing an account for rebates or payment over a ten-year period, focusing on the 50–59 age group in 2019 (Cox et al., *Financial Inclusion Across the United States,* available for download at *https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3934498* (last revised Apr. 24, 2023)). The Census links ZCTAs to an urban area (or none).

[262] *See* Jesse Bricker & Geng Li, FRS, Finance and Economics Discussion Series, 2023–048, *Your Friends Your Credit: Social Capital Measures Derived From Social Media and the Credit Market* (2023), *https://www.federalreserve.gov/econres/feds/files/2023048pap.pdf.*

[263] *See* U.S. Small Bus. Admin., *Table of size standards, https://www.sba.gov/document/support-table-size-standards* (last updated Oct. 25, 2023).

sent to: The Consumer Financial Protection Bureau (Attention: PRA Office), 1700 G Street NW, Washington, DC 20552, or by email to *CFPB_Public_PRA@cfpb.gov.*

List of Subjects

12 CFR Part 1005

Banks, Banking, Consumer protection, Credit unions, Electronic fund transfers, National banks, Reporting and recordkeeping requirements, Savings associations.

12 CFR Part 1026

Advertising, Banks, Banking, Consumer protection, Credit, Credit unions, Mortgages, National banks, Reporting and recordkeeping requirements, Savings associations, Truth-in-lending.

Authority and Issuance

For the reasons set forth in the preamble, the CFPB proposes to amend Regulation E, 12 CFR part 1005, and Regulation Z, 12 CFR part 1026, as set forth below:

PART 1005—ELECTRONIC FUND TRANSFER ACT (REGULATION E)

■ 1. The authority citation for part 1005 continues to read as follows:

Authority: 12 U.S.C. 5512, 5581; 15 U.S.C. 1693b. Subpart B is also issued under 12 U.S.C. 5601 and 15 U.S.C. 1693o–1.

Subpart A—General

■ 2. Section 1005.10 is amended by revising paragraph (e)(1) to read as follows:

§ 1005.10 Preauthorized transfers.

* * * * *

(e) *Compulsory use*—(1) *Credit.* No financial institution or other person may condition an extension of credit to a consumer on the consumer's repayment by preauthorized electronic fund transfers, except for credit extended under an overdraft credit plan or extended to maintain a specified minimum balance in the consumer's account. This exception does not apply to a covered separate credit feature accessible by a hybrid prepaid-credit card as defined in Regulation Z, 12 CFR 1026.61. This exception also does not apply to covered overdraft credit extended by very large financial institutions as those terms are defined in Regulation Z, 12 CFR 1026.62.

* * * * *

■ 3. In Supplement I to Part 1005—Official Interpretations:

■ a. Under *Section 1005.10—Preauthorized Transfers, 10(e)(1) Credit* is revised.

■ b. Under *Section 1005.17—Requirements for Overdraft Services, 17(a) Definition* is revised.

The revisions read as follows:

Supplement I to Part 1005—Official Interpretations

* * * * *

Section 1005.10—Preauthorized Transfers

* * * * *

10(e) Compulsory Use

10(e)(1) Credit

1. *General rule for loan payments.* Creditors may not require repayment of loans by electronic means on a preauthorized, recurring basis.

2. *Overdraft credit plans not accessible by hybrid prepaid-credit cards and covered overdraft credit extended by very large financial institutions.*

i. Section 1005.10(e)(1) provides an exception from the general rule for an overdraft credit plan other than for a covered separate credit feature accessible by a hybrid prepaid-credit card as defined in Regulation Z, 12 CFR 1026.61 and for covered overdraft credit extended by very large financial institutions as those terms are defined in Regulation Z, 12 CFR 1026.62. A financial institution may therefore require the automatic repayment of an overdraft credit plan, other than a covered separate credit feature accessible by a hybrid prepaid-credit card or covered overdraft credit extended by very large financial institutions, even if the overdraft extension is charged to an open-end account that may be accessed by the consumer in ways other than by overdrafts.

ii. Credit extended through a negative balance on the asset feature of a prepaid account that meets the conditions of Regulation Z, 12 CFR 1026.61(a)(4), is considered credit extended pursuant to an overdraft credit plan for purposes of § 1005.10(e)(1). Thus, the exception for overdraft credit plans in § 1005.10(e)(1) applies to this credit.

3. *Applicability to covered separate credit features accessible by hybrid prepaid-credit cards.*

i. Under § 1005.10(e)(1), creditors may not require by electronic means on a preauthorized, recurring basis repayment of credit extended under a covered separate credit feature accessible by a hybrid prepaid-credit card as defined in Regulation Z, 12 CFR 1026.61. The prohibition in § 1005.10(e)(1) applies to any credit extended under such a credit feature, including preauthorized checks. See Regulation Z, 12 CFR 1026.61, and comment 61(a)(1)–3.

ii. Under Regulation Z, 12 CFR 1026.12(d)(1), a card issuer may not take any action, either before or after termination of credit card privileges, to offset a cardholder's indebtedness arising from a consumer credit transaction under the relevant credit card plan against funds of the cardholder held on deposit with the card issuer. Under Regulation Z, 12 CFR 1026.12(d)(3), with respect to covered separate credit features accessible by hybrid prepaid-credit cards as defined in 12 CFR 1026.61, a card issuer generally is not prohibited from periodically deducting all or part of the cardholder's credit card debt from a deposit account (such as a prepaid account) held with the card issuer under a plan that is authorized in writing by the cardholder, so long as the card issuer does not make such deductions to the plan more frequently than once per calendar month. A card issuer is prohibited under Regulation Z, 12 CFR 1026.12(d), from automatically deducting all or part of the cardholder's credit card debt under a covered separate credit feature from a deposit account (such as a prepaid account) held with the card issuer on a daily or weekly basis, or whenever deposits are made to the deposit account. Section 1005.10(e)(1) further restricts the card issuer from requiring payment from a deposit account (such as a prepaid account) of credit card balances of a covered separate credit feature accessible by a hybrid prepaid-credit card by electronic means on a preauthorized, recurring basis.

4. *Incentives.* A creditor may offer a program with a reduced annual percentage rate or other cost-related incentive for an automatic repayment feature, provided the program with the automatic payment feature is not the only loan program offered by the creditor for the type of credit involved. Examples include:

i. Mortgages with graduated payments in which a pledged savings account is automatically debited during an initial period to supplement the monthly payments made by the borrower.

ii. Mortgage plans calling for preauthorized biweekly payments that are debited electronically to the consumer's account and produce a lower total finance charge.

* * * * *

Section 1005.17—Requirements for Overdraft Services

17(a) Definition

1. *Exempt securities- and commodities-related lines of credit.* The definition of ''overdraft service'' does not include the payment of transactions in a securities or commodities account pursuant to which credit is extended by a broker-dealer registered with the Securities and Exchange Commission or the Commodity Futures Trading Commission.

2. *Covered overdraft credit.* Under § 1005.17(a)(1), a line of credit subject to Regulation Z (12 CFR 1026) is not an overdraft service. Covered overdraft credit as that term is defined in 12 CFR 1026.62, is a line of credit subject to Regulation Z and is therefore not an overdraft service. Covered overdraft credit includes above breakeven overdraft credit extended by a very large financial institution as those terms are defined in 12 CFR 1026.62. Above breakeven overdraft credit extended by a very large financial institution is therefore not an overdraft service under § 1005.17(a).

* * * * *

PART 1026—TRUTH IN LENDING (REGULATION Z)

■ 4. The authority citation for part 1026 continues to read as follows:

Authority: 12 U.S.C. 2601, 2603–2605, 2607, 2609, 2617, 3353, 5511, 5512, 5532, 5581; 15 U.S.C. 1601 *et seq.*

Subpart A—General

■ 5. Section 1026.2 is amended by revising paragraph (a)(15) to read as follows:

§ 1026.2 Definitions and rules of construction.

(a) * * *

(15)(i) *Credit card* means any card, plate, or other single credit device that may be used from time to time to obtain credit. The term *credit card* includes both a hybrid prepaid-credit card as defined in § 1026.61 and a hybrid debit-credit card as defined in § 1026.62.

(ii) *Credit card account under an open-end (not home-secured) consumer credit plan* means any open-end credit account that is accessed by a credit card, except:

(A) A home-equity plan subject to the requirements of § 1026.40 that is accessed by a credit card; or

(B) A covered overdraft credit account as defined in § 1026.62 offered by a creditor other than a very large financial institution as defined in § 1026.62 that is accessed by a debit card or account number.

(iii) *Charge card* means a credit card on an account for which no periodic rate is used to compute a finance charge. The term does not include a hybrid debit-credit card as defined in § 1026.62.

(iv) *Debit card* means any card, plate, or other single device that may be used from time to time to access an asset account other than a prepaid account as defined in § 1026.61. The term *debit card* does not include a prepaid card as defined in § 1026.61.

* * * * *

■ 6. Section 1026.4 is amended by revising paragraph (b)(2), adding paragraph (b)(12), and revising paragraph (c)(3) to read as follows:

§ 1026.4 Finance charge.

* * * * *

(b) * * *

(2) Service, transaction, activity, and carrying charges, including any charge imposed on a checking or other transaction account (except a prepaid account as defined in § 1026.61 or a covered asset account as that term is defined in § 1026.62) to the extent that the charge exceeds the charge for a similar account without a credit feature.

* * * * *

(12) With regard to a covered asset account as that term is defined in § 1026.62(b)(2):

(i) Any service, transaction, activity, or carrying charge imposed on the separate credit account required by § 1026.62(c); and

(ii) Any service, transaction, activity, or carrying charge imposed on the covered asset account to the extent that the charge exceeds a comparable charge imposed on a checking or other transaction account that does not have overdraft credit.

(iii) For purposes of paragraph (b)(12)(ii) of this section, the following charges imposed on a checking or other transaction account without covered overdraft credit are not comparable to charges imposed on a covered asset account. Thus, to determine pursuant to paragraph (b)(12)(ii) of this section the amount of a charge on a covered asset account that is a finance charge, the following fees and charges on a checking or other transaction account that does not have covered overdraft credit may not be subtracted from the amount of the charge on the covered asset account.

(A) A charge for authorizing or paying a transaction that overdraws the checking or other transaction account.

(B) A charge for declining to authorize or pay a transaction.

(C) A charge for returning a transaction unpaid.

(D) A charge for transferring funds into the checking or other transaction account from any credit account.

(E) A charge for transferring funds into the checking or other transaction account from any other asset account.

* * * * *

(c) * * *

(3) Charges imposed by a financial institution for paying items that overdraw an account, unless the payment of such items and the imposition of the charge were previously agreed upon in writing. This paragraph (c)(3) does not apply to credit offered in connection with a prepaid account as defined in § 1026.61. This paragraph (c)(3) also does not apply to above breakeven overdraft credit as defined in § 1026.62.

* * * * *

Subpart G—Special Rules Applicable to Credit Card Accounts and Open-End Credit Offered to College Students

* * * * *

■ 7. Section 1026.60 is amended by revising paragraph (a)(5) to read as follows:

§ 1026.60 Credit and charge card applications and solicitations.

(a) * * *

(5) *Exceptions.* This section does not apply to:

(i) Home-equity plans accessible by a credit or charge card that are subject to the requirements of § 1026.40;

(ii) Covered overdraft credit as defined in § 1026.62 tied to asset accounts accessed by check-guarantee cards or by debit cards other than hybrid debit-credit cards as defined in § 1026.62;

(iii) Lines of credit accessed by check-guarantee cards or by debit cards, other than covered overdraft credit accessed by hybrid debit-credit cards, that can be used only at automated teller machines;

(iv) Lines of credit accessed solely by account numbers except for a covered separate credit feature solely accessible by an account number that is a hybrid prepaid-credit card as defined in § 1026.61 or covered overdraft credit accessible by an account number that is a hybrid debit-credit card;

(v) Additions of a credit or charge card to an existing open-end plan;

(vi) General purpose applications unless the application, or material accompanying it, indicates that it can be used to open a credit or charge card account; or

(vii) Consumer-initiated requests for applications.

* * * * *

■ 8. Section 1026.62 is added to read as follows:

§ 1026.62 Overdraft Credit.

(a) *In general*—(1) Overdraft credit is subject to this section and this part as specified below.

(2) *Overdraft credit* is any consumer credit extended by a financial institution to pay a transaction from a checking or other transaction account (other than a prepaid account as defined in § 1026.61) held at the financial institution when the consumer has insufficient or unavailable funds in that account. The term overdraft credit includes, but is not limited to, any such consumer credit extended through a transfer from a credit card account or overdraft line of credit. The term does not include credit exempt from this part pursuant to § 1026.3.

(b) *Definitions.* For purposes of this section and this part, the following definitions apply:

(1) *Above Breakeven Overdraft Credit* means overdraft credit extended by a very large financial institution to pay a transaction on which, as an incident to or a condition of the overdraft credit, the very large financial institution imposes a charge or combination of charges exceeding the average of its costs and charge-off losses for providing non-covered overdraft credit as described in § 1026.62(d).

(2) *Covered Asset Account* means a checking or other transaction account (other than a prepaid account as defined in § 1026.61) provided by a very large financial institution that is tied to overdraft credit provided by the very large financial institution.

(3) *Covered Overdraft Credit* means overdraft credit that is subject to a finance charge or is payable by written agreement in more than four installments.

(4) *Covered Overdraft Credit Account* means a credit account through which a financial institution extends or can extend covered overdraft credit. For example, the term includes any line of credit, credit card account, credit feature, credit plan, or credit subaccount through which the financial institution extends or can extend covered overdraft credit.

(5) *Hybrid Debit-Credit Card* means any card, plate, or other single credit device that a consumer may use from time to time to obtain covered overdraft credit from a very large financial institution.

(6) *Non-Covered Overdraft Credit* means overdraft credit that is not subject to a finance charge and is not payable by written agreement in more than four installments.

(7) *Overdraft credit* has the meaning set out in § 1026.62(a)(2).

(8) *Very Large Financial Institution* means an insured depository institution or an insured credit union that has total assets of more than $10,000,000,000 and any affiliate thereof, as determined under 12 U.S.C. 5515(a).

(c) *Structure of covered overdraft credit.* A very large financial institution shall not structure covered overdraft credit as a negative balance on a checking or other transaction account. The very large financial institution shall structure covered overdraft credit as a separate credit account. The separate credit account is a covered overdraft credit account. The tied checking or other transaction account is a covered asset account.

(d) *Charges exceeding the average of its costs and charge-off losses for providing non-covered overdraft credit*—(1) *General rule.* For purposes of paragraph 62(b)(1) of this section, any charge or combination of charges to pay a transaction exceeds the average of a very large financial institution's costs and charge-off losses for providing non-covered overdraft credit if the charge or combination of charges exceeds the greater of:

(i) The pro rata share of the very large financial institution's total direct costs and charge-off losses for providing non-covered overdraft credit in the previous year, calculated in accordance with this paragraph; or

(ii) [$3/$6/$7/$14].

(2) *Cost and loss calculation.* When calculating the pro rata share of the very large financial institution's total direct costs and charge-off losses for providing non-covered overdraft credit in the previous year, a very large financial institution may consider only those costs and charge-off losses specifically traceable to its provision of non-covered overdraft credit in the previous year. Such costs and charge-off losses include, but are not limited to, its cost of funds, its net charge-off losses, and operating expenses for its non-covered overdraft credit program. Such costs and charge-off losses do not include general overhead costs or charge-off losses due to unauthorized use, EFT errors, billing errors, returned deposit items, or rescinded provisional credit.

■ 9. In Supplement I to Part 1026—Official Interpretations:

■ a. Under *Section 1026.2—Definitions and Rules of Construction:*

■ i. *2(a)(14) Credit* is revised.

■ ii. *Paragraph 2(a)(15)* is revised.

■ iii. *2(a)(20) Open-End Credit* is revised.

■ b. Under *Section 1026.4—Finance Charge:*

■ i. *Paragraph 4(b)(2)* is revised.

■ ii. *Paragraph 4(b)(12)* is added.

■ iii. *Paragraph 4(c)(3)* is revised.

■ c. Under *Section 1026.12—Special Credit Card Provisions:*

■ i. Introductory paragraph 1 is revised.

■ ii. *12(a)(1)* is revised.

■ iii. *12(a)(2)* is revised.

■ iv. *12(c)* is revised.

■ v. *12(c)(1) General Rule* is revised.

■ d. Under *Section 1026.55—Limitations on increasing annual percentage rates, fees, and charges,* revise *55(a).*

■ e. Under *Section 1026.57—Reporting and Marketing Rules for College Student Open-End Credit,* revise *57(a)(1).*

The revisions and addition read as follows:

Supplement I to Part 1026—Official Interpretations

* * * * *

Subpart A—General

* * * * *

Section 1026.2—Definitions and Rules of Construction

* * * * *

2(a)(14) Credit

1. *Exclusions.* The following situations are not considered credit for purposes of the regulation:

i. Layaway plans, unless the consumer is contractually obligated to continue making payments. Whether the consumer is so obligated is a matter to be determined under applicable law. The fact that the consumer is not entitled to a refund of any amounts paid towards the cash price of the merchandise does not bring layaways within the definition of credit.

ii. Tax liens, tax assessments, court judgments, and court approvals of reaffirmation of debts in bankruptcy. However, third-party financing of such obligations (for example, a bank loan obtained to pay off a tax lien) is credit for purposes of the regulation.

iii. Insurance premium plans that involve payment in installments with each installment representing the payment for insurance coverage for a certain future period of time, unless the consumer is contractually obligated to continue making payments.

iv. Home improvement transactions that involve progress payments, if the consumer pays, as the work progresses, only for work completed and has no contractual obligation to continue making payments.

v. Borrowing against the accrued cash value of an insurance policy or a pension account, if there is no independent obligation to repay.

vi. Letters of credit.

vii. The execution of option contracts. However, there may be an extension of credit when the option is exercised, if there is an agreement at that time to defer payment of a debt.

viii. Investment plans in which the party extending capital to the consumer risks the loss of the capital advanced. This includes, for example, an arrangement with a home purchaser in which the investor pays a portion of the downpayment and of the periodic mortgage payments in return for an ownership interest in the property, and shares in any gain or loss of property value.

ix. Mortgage assistance plans administered by a government agency in which a portion of the consumer's monthly payment amount is paid by the agency. No finance charge is imposed on the subsidy amount, and that amount is due in a lump-sum payment on a set date or upon the occurrence of certain events. (If payment is not made when due, a new note imposing a finance charge may be written, which may then be subject to the regulation.)

2. *Payday loans; deferred presentment.* Credit includes a transaction in which a cash advance is made to a consumer in exchange for the consumer's personal check, or in exchange for the consumer's authorization to debit the consumer's deposit account, and where the parties agree either that the check will not be cashed or deposited, or that the consumer's deposit account will not be debited, until a designated future date. This type of transaction is often referred to as a ''payday loan'' or ''payday advance'' or ''deferred-presentment loan.'' A fee charged in connection with such a transaction may be a finance charge for purposes of § 1026.4, regardless of how the fee is characterized under state law. Where the fee charged constitutes a finance charge under § 1026.4 and the person advancing funds regularly extends consumer credit, that person is a creditor and is required to provide disclosures consistent with the requirements of Regulation Z. (*See* § 1026.2(a)(17).)

3. *Transactions on the asset features of prepaid accounts when there are insufficient or unavailable funds.* Credit includes authorization of a transaction on the asset feature of a prepaid account as defined in § 1026.61 where the consumer has insufficient or unavailable funds in the asset feature of the prepaid account at the time the transaction is authorized to cover the amount of the transaction. It also includes settlement of a transaction on the asset feature of a prepaid account where the consumer has insufficient or unavailable funds in the asset feature of the prepaid account at the time the transaction is settled to cover the amount of the transaction. This includes a transaction where the consumer has sufficient or available funds in the asset feature of a prepaid account to cover the amount of the transaction at the time the transaction is authorized but insufficient or unavailable funds in the asset feature of the prepaid account to cover the transaction amount at the time the transaction is settled. See § 1026.61 and related commentary on the applicability of this regulation to credit that is extended in connection with a prepaid account.

4. *Overdraft credit.* Funds extended by a financial institution to a consumer to pay transactions that overdraw a checking or other transaction account held at the financial institution are credit whenever the consumer has a contractual obligation to repay the funds.

Paragraph 2(a)(15)

1. *Usable from time to time.* A credit card must be usable from time to time. Since this involves the possibility of repeated use of a single device, checks and similar instruments that can be used only once to obtain a single credit extension are not credit cards.

2. *Examples.*

i. Examples of credit cards include:

A. A card that guarantees checks or similar instruments, if the asset account is also tied to covered overdraft credit or if the instrument directly accesses a line of credit.

B. A debit card (other than a debit card that is solely an account number) that also accesses a credit account (that is, a debit-credit card or hybrid debit-credit card as defined in § 1026.62). See comment 2(a)(15)–2.ii.C for guidance on whether a debit card that is solely an account number is a credit card.

C. An identification card that permits the consumer to defer payment on a purchase.

D. An identification card indicating loan approval that is presented to a merchant or to a lender, whether or not the consumer signs a separate promissory note for each credit extension.

E. A card or device that can be activated upon receipt to access credit, even if the card has a substantive use other than credit, such as a purchase-price discount card. Such a card or device is a credit card notwithstanding the fact that the recipient must first contact the card issuer to access or activate the credit feature.

F. A prepaid card that is a hybrid prepaid-credit card as defined in § 1026.61.

ii. In contrast, credit card does not include, for example:

A. A check-guarantee or debit card with no credit feature or agreement.

B. Any card, key, plate, or other device that is used in order to obtain petroleum products for business purposes from a wholesale distribution facility or to gain access to that facility, and that is required to be used without regard to payment terms.

C. An account number that accesses a credit account, unless the account number can access an open-end line of credit to purchase goods or services or as provided in § 1026.61 with respect to a hybrid prepaid-credit card. An account number that can access an open-end line of credit to purchase goods or services includes an account number that can access a covered overdraft credit account offered by a very large financial institution. For example, if a creditor provides a consumer with an open-end line of credit that can be accessed by an account number in order to transfer funds into another account (such as an asset account with the same creditor), the account number is not a credit card for purposes of § 1026.2(a)(15)(i). However, if the account number can also access the line of credit to purchase goods or services (such as an account number that can be used to purchase goods or services on the internet), the account number is a credit card for purposes of § 1026.2(a)(15)(i), regardless of whether the creditor treats such transactions as purchases, cash advances, or some other type of transaction. Furthermore, if the line of credit can also be accessed by a card (such as a debit card), that card is a credit card for purposes of § 1026.2(a)(15)(i).

D. A prepaid card that is not a hybrid prepaid-credit card as defined in § 1026.61.

E. A check-guarantee or debit card that can access non-covered overdraft credit as defined in § 1026.62 and cannot access any other form of credit.

3. *Charge card.*

i. Charge cards are credit cards where no periodic rate is used to compute the finance charge. The term *charge card* does not include a hybrid debit-credit card as defined in § 1026.62. Thus, covered overdraft credit extended by a very large financial institution through a hybrid debit-credit card is not subject to special charge card rules.

A. Under the regulation, a reference to credit cards generally includes charge cards. In particular, references to credit card accounts under an open-end (not home-secured) consumer credit plan in subparts B and G generally include charge cards.

B. The term *charge card* is, however, distinguished from credit card or credit card account under an open-end (not home-secured) consumer credit plan in §§ 1026.6(b)(2)(xiv), 1026.7(b)(11) (except as described in comment 2(a)(15)–3.ii below), 1026.7(b)(12), 1026.9(e), 1026.9(f), 1026.28(d), 1026.52(b)(1)(ii)(C), 1026.60, and appendices G–10 through G–13.

ii. A hybrid prepaid-credit card as defined in § 1026.61 is a charge card with respect to a covered separate credit feature if no periodic rate is used to compute the finance charge in connection with the covered separate credit feature. Unlike other charge card accounts, the requirements in § 1026.7(b)(11) apply to a covered separate credit feature accessible by a hybrid prepaid-credit card that is a charge card when that covered separate credit feature is a credit card account under an open-end (not home-secured) consumer credit plan. Thus, under § 1026.5(b)(2)(ii)(A), with respect to a covered separate credit feature that is a credit card account under an open-end (not home-secured) consumer credit plan, a card issuer of a hybrid prepaid-credit card that meets the definition of a charge card because no periodic rate is used to compute a finance charge in connection with the covered separate credit feature must adopt reasonable procedures for the covered separate credit feature designed to ensure that

(1) periodic statements are mailed or delivered at least 21 days prior to the payment due date disclosed on the statement pursuant to § 1026.7(b)(11)(i)(A); and

(2) the card issuer does not treat as late for any purposes a required minimum periodic payment received by the card issuer within 21 days after mailing or delivery of the periodic statement disclosing the due date for that payment.

4. *Credit card account under an open-end (not home-secured) consumer credit plan.*

i. An open-end consumer credit account is a credit card account under an open-end (not home-secured) consumer credit plan for purposes of § 1026.2(a)(15)(ii) if:

A. The account is accessed by a credit card, as defined in § 1026.2(a)(15)(i); and

B. The account is not excluded under § 1026.2(a)(15)(ii)(A) or (B).

ii. The exclusion from credit card account under an open-end (not home-secured) consumer credit plan provided by § 1026.2(a)(15)(ii)(B) for covered overdraft credit offered by a creditor that is not a very large financial institution does not apply to a covered separate credit feature accessible by a hybrid prepaid-credit card (including a hybrid prepaid-credit card that is solely an account number) as defined in § 1026.61.

* * * * *

2(a)(20) Open-End Credit

1. *General.* This definition describes the characteristics of open-end credit (for which the applicable disclosure and other rules are contained in Subpart B), as distinct from closed-end credit. Open-end credit is consumer credit that is extended under a plan and meets *all 3* criteria set forth in the definition.

2. *Existence of a plan.*

i. The definition requires that there be a plan, which connotes a contractual arrangement between the creditor and the consumer.

ii. With respect to a covered separate credit feature accessible by a hybrid prepaid-credit card as defined in § 1026.61, a plan means a program where the consumer is obligated contractually to repay any credit extended by the creditor. For example, a plan includes a program under which a creditor routinely extends credit from a covered separate credit feature offered by the prepaid account issuer, its affiliate, or its business partner where the prepaid card can be used from time to time to draw, transfer, or authorize the draw or transfer of credit from the covered separate credit feature in the course of authorizing, settling, or otherwise completing transactions conducted with the card to obtain goods or services, obtain cash, or conduct person-to-person transfers, and the consumer is obligated contractually to repay those credit transactions. Such a program constitutes a plan notwithstanding that, for example, the creditor has not agreed in writing to extend credit for those transactions, the creditor retains discretion not to extend credit for those transactions, or the creditor does not extend credit for those transactions once the consumer has exceeded a certain amount of credit. See § 1026.61(a) and related commentary for guidance on the applicability of this regulation to credit accessible by hybrid prepaid-credit cards.

iii. Some creditors offer programs containing a number of different credit features. The consumer has a single account with the institution that can be accessed repeatedly via a number of sub-accounts established for the different program features and rate structures. Some features of the program might be used repeatedly (for example, an overdraft line) while others might be used infrequently (such as the part of the credit line available for secured credit). If the program as a whole is subject to prescribed terms and otherwise meets the definition of open-end credit, such a program would be considered a single, multifeatured plan.

iv. With respect to covered overdraft credit as defined in § 1026.62, a plan means a program where the consumer is obligated contractually to repay any credit extended by the creditor. Such a program constitutes a plan notwithstanding that, for example, the creditor has not agreed in writing to extend credit for those transactions, the creditor retains discretion not to extend credit for those transactions, or the creditor does not extend credit for those transactions once the consumer has exceeded a certain amount of credit.

3. *Repeated transactions.* Under this criterion, the creditor must reasonably contemplate repeated transactions. This means that the credit plan must be usable from time to time and the creditor must legitimately expect that there will be repeat business rather than a one-time credit extension. The creditor must expect repeated dealings with consumers under the credit plan as a whole and need not believe a consumer will reuse a particular feature of the plan. The determination of whether a creditor can reasonably contemplate repeated transactions requires an objective analysis. Information that much of the creditor's customer base with accounts under the plan make repeated transactions over some period of time is relevant to the determination, particularly when the plan is opened primarily for the financing of infrequently purchased products or services. A standard based on reasonable belief by a creditor necessarily includes some margin for judgmental error. The fact that particular consumers do not return for further credit extensions does not prevent a plan from having been properly characterized as open-end. For example, if much of the customer base of a clothing store makes repeat purchases, the fact that some consumers use the plan only once would not affect the characterization of the store's plan as open-end credit. The criterion regarding repeated transactions is a question of fact to be decided in the context of the creditor's type of business and the creditor's relationship with its customers. For example, it would be more reasonable for a bank or depository institution to contemplate repeated transactions with a customer than for a seller of aluminum siding to

make the same assumption about its customers.

4. *Finance charge on an outstanding balance.*

i. The requirement that a finance charge may be computed and imposed from time to time on the outstanding balance means that there is no specific amount financed for the plan for which the finance charge, total of payments, and payment schedule can be calculated. A plan may meet the definition of open-end credit even though a finance charge is not normally imposed, provided the creditor has the right, under the plan, to impose a finance charge from time to time on the outstanding balance. For example, in some plans, a finance charge is not imposed if the consumer pays all or a specified portion of the outstanding balance within a given time period. Such a plan could meet the finance charge criterion, if the creditor has the right to impose a finance charge, even though the consumer actually pays no finance charges during the existence of the plan because the consumer takes advantage of the option to pay the balance (either in full or in installments) within the time necessary to avoid finance charges.

ii. With regard to a covered separate credit feature and an asset feature on a prepaid account that are both accessible by a hybrid prepaid-credit card as defined in § 1026.61, any service, transaction, activity, or carrying charges imposed on the covered separate credit feature, and any such charges imposed on the asset feature of the prepaid account to the extent that the amount of the charge exceeds comparable charges imposed on prepaid accounts in the same prepaid account program that do not have a covered separate credit feature accessible by a hybrid prepaid-credit card, generally is a finance charge. *See* § 1026.4(a) and (b)(11). Such charges include a periodic fee to participate in the covered separate credit feature, regardless of whether this fee is imposed on the credit feature or on the asset feature of the prepaid account. With respect to credit from a covered separate credit feature accessible by a hybrid prepaid-credit card, any service, transaction, activity, or carrying charges that are finance charges under § 1026.4 constitute finance charges imposed from time to time on an outstanding unpaid balance as described in § 1026.2(a)(20) if there is no specific amount financed for the credit feature for which the finance charge, total of payments, and payment schedule can be calculated.

iii. Regardless of whether the financial institution assesses such charges on the deposit account itself or a separate credit account, any service, transaction, activity, or carrying charges imposed by a financial institution for paying a transaction that overdraws a consumer's deposit account held at the financial institution are finance charges unless they are excluded from the definition of finance charge by § 1026.4(c). *See* § 1026.4(a), (b)(12), and (c). Additionally, such charges would constitute finance charges imposed from time to time on an outstanding unpaid balance, as described in § 1026.2(a)(20), if there is no specific amount financed for the plan for which the finance charge, total of payments, and payment schedule can be calculated.

5. *Reusable line.* The total amount of credit that may be extended during the existence of an open-end plan is unlimited because available credit is generally replenished as earlier advances are repaid. A line of credit is self-replenishing even though the plan itself has a fixed expiration date, as long as during the plan's existence the consumer may use the line, repay, and reuse the credit. The creditor may occasionally or routinely verify credit information such as the consumer's continued income and employment status or information for security purposes but, to meet the definition of open-end credit, such verification of credit information may not be done as a condition of granting a consumer's request for a particular advance under the plan. In general, a credit line is self-replenishing if the consumer can take further advances as outstanding balances are repaid without being required to separately apply for those additional advances. A credit card account where the plan as a whole replenishes meets the self-replenishing criterion, notwithstanding the fact that a credit card issuer may verify credit information from time to time in connection with specific transactions. This criterion of unlimited credit distinguishes open-end credit from a series of advances made pursuant to a closed-end credit loan commitment. For example:

i. Under a closed-end commitment, the creditor might agree to lend a total of $10,000 in a series of advances as needed by the consumer. When a consumer has borrowed the full $10,000, no more is advanced under that particular agreement, even if there has been repayment of a portion of the debt. (*See* § 1026.2(a)(17)(iv) for disclosure requirements when a credit card is used to obtain the advances.)

ii. This criterion does not mean that the creditor must establish a specific credit limit for the line of credit or that the line of credit must always be replenished to its original amount. The creditor may reduce a credit limit or refuse to extend new credit in a particular case due to changes in the creditor's financial condition or the consumer's creditworthiness. (The rules in § 1026.40(f), however, limit the ability of a creditor to suspend credit advances for home equity plans.) While consumers should have a reasonable expectation of obtaining credit as long as they remain current and within any preset credit limits, further extensions of credit need not be an absolute right in order for the plan to meet the self-replenishing criterion.

6. *Verifications of collateral value.* Creditors that otherwise meet the requirements of § 1026.2(a)(20) extend open-end credit notwithstanding the fact that the creditor must verify collateral values to comply with Federal, state, or other applicable law or verifies the value of collateral in connection with a particular advance under the plan.

7. *Open-end real estate mortgages.* Some credit plans call for negotiated advances under so-called open-end real estate mortgages. Each such plan must be independently measured against the definition of open-end credit, regardless of the terminology used in the industry to describe the plan. The fact that a particular plan is called an open-end real estate mortgage, for example, does not, by itself, mean that it is open-end credit under the regulation.

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Section 1026.4—Finance Charge

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Paragraph 4(b)(2)

1. *Checking or transaction account charges.* A charge imposed in connection with a credit feature on a checking or transaction account (other than a prepaid account as defined in § 1026.61 or a covered asset account as that term is defined in § 1026.62) is a finance charge under § 1026.4(b)(2) to the extent the charge exceeds the charge for a similar account without a credit feature and the charge is not addressed by § 1026.4(b)(12). If a charge for an account with a credit feature does not exceed the charge for an account without a credit feature, the charge is not a finance charge under § 1026.4(b)(2). To illustrate:

i. A $5 service charge is imposed on an account with an overdraft line of credit (where the institution has agreed in writing to pay an overdraft), while a $3 service charge is imposed on an account without a credit feature; the $2 difference is a finance charge. (If the difference is not related to account activity, however, it may be excludable as a participation fee. See the commentary to § 1026.4(c)(4).)

ii. A $5 service charge is imposed for each item that results in an overdraft on an account with an overdraft line of credit, while a $25 service charge is imposed for paying or returning each item on a similar account without a credit feature; the $5 charge is not a finance charge.

2. *Prepaid accounts.* Fees or charges related to credit offered in connection with prepaid accounts as defined in § 1026.61 are discussed in §§ 1026.4(b)(11) and 1026.61 and related commentary.

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Paragraph 4(c)(3)

1. *Assessing interest on an overdraft balance.* Except with respect to credit offered in connection with a prepaid account as defined in § 1026.61, a charge on an overdraft balance computed by applying a rate of interest to the amount of the overdraft is not a finance charge, even though the consumer agrees to the charge in the account agreement, unless the financial institution agrees in writing that it will pay such items.

2. *Credit accessed in connection with a prepaid account.* See comment 4(b)(11)–1 for guidance on when fees imposed with regard to credit accessed in connection with a prepaid account as defined in § 1026.61 are finance charges.

3. *Credit accessed in connection with a covered asset account.* See 12 CFR 1026.4(b)(12) for guidance on when fees imposed on a covered asset account as defined in § 1026.62 are finance charges.

* * * * *

Section 1026.12—Special Credit Card Provisions

1. *Scope.* Sections 1026.12(a) and (b) deal with the issuance and liability rules for credit cards, whether the card is intended for consumer, business, or any other purposes. Sections 1026.12(a) and (b) are exceptions to the general rule that the regulation applies only to consumer credit. (See §§ 1026.1 and 1026.3.) Notwithstanding paragraph (g) of this section or Regulation E, 12 CFR 1005.12(a), paragraphs (a) through (f) of this section apply to hybrid debit credit cards.

2. *Definition of ''accepted credit card''*. For purposes of this section, ''accepted credit card'' means any credit card that a cardholder has requested or applied for and received, or has signed, used, or authorized another person to use to obtain credit. Any credit card issued as a renewal or substitute in accordance with § 1026.12(a) becomes an accepted credit card when received by the cardholder.

12(a) Issuance of Credit Cards

Paragraph 12(a)(1)

1. *Explicit request.* A request or application for a card must be explicit. For example, a request for an overdraft plan tied to a checking account does not constitute an application for a credit card with overdraft checking features. Therefore, a very large financial institution cannot issue a hybrid debit-credit card to a person without first receiving an oral or written request or application for the hybrid debit-credit card. The term *hybrid debit-credit* card has the same meaning as provided in § 1026.62.

2. *Addition of credit features.* If the consumer has a non-credit card, including a prepaid card, the addition of a credit feature or plan to the card that would make the card into a credit card under § 1026.2(a)(15)(i) constitutes issuance of a credit card. For example, the following constitute issuance of a credit card:

i. Granting overdraft privileges on a checking account when the consumer already has a check guarantee card; or

ii. Allowing a prepaid card to access a covered separate credit feature that would make the card into a hybrid prepaid-credit card as defined in § 1026.61 with respect to the covered separate credit feature.

iii. Extending covered overdraft credit through a hybrid debit-credit card as defined in § 1026.62.

3. *Variance of card from request.* The request or application need not correspond exactly to the card that is issued. For example:

i. The name of the card requested may be different when issued.

ii. The card may have features in addition to those reflected in the request or application.

4. *Permissible form of request.* The request or application may be oral (in response to a telephone solicitation by a card issuer, for example) or written.

5. *Time of issuance.* A credit card may be issued in response to a request made before any cards are ready for issuance (for example, if a new program is established), even if there is some delay in issuance.

6. *Persons to whom cards may be issued.* A card issuer may issue a credit card to the person who requests it, and to anyone else for whom that person requests a card and who will be an authorized user on the requester's account. In other words, cards may be sent to consumer A on A's request, and also (on A's request) to consumers B and C, who will be authorized users on A's account. In these circumstances, the following rules apply:

i. The additional cards may be imprinted in either A's name or in the names of B and C.

ii. No liability for unauthorized use (by persons other than B and C), not even the $50, may be imposed on B or C since they are merely users and not cardholders as that term is defined in § 1026.2 and used in § 1026.12(b); of course, liability of up to $50 for unauthorized use of B's and C's cards may be imposed on A.

iii. Whether B and C may be held liable for their own use, or on the account generally, is a matter of state or other applicable law.

7. *Issuance of non-credit cards.*

i. *Issuance of non-credit cards other than prepaid cards.*

A. Under § 1026.12(a)(1), a credit card cannot be issued except in response to a request or an application. (See comment 2(a)(15)–2 for examples of cards or devices that are and are not credit cards.) A non-credit card other than a prepaid card may be sent on an unsolicited basis by an issuer that does not propose to connect the card to any credit plan; a credit feature may be added to a previously issued non-credit card other than a prepaid card only upon the consumer's specific request.

B. *Examples.* A purchase-price discount card may be sent on an unsolicited basis by an issuer that does not propose to connect the card to any credit plan. An issuer demonstrates that it proposes to connect the card to a credit plan by, for example, including promotional materials about credit features or account agreements and disclosures required by § 1026.6. The issuer will violate the rule against unsolicited issuance if, for example, at the time the card is sent a credit plan can be accessed by the card or the recipient of the unsolicited card has been preapproved for credit that the recipient can access by contacting the issuer and activating the card.

ii. *Issuance of a prepaid card.* Section 1026.12(a)(1) does not apply to the issuance of a prepaid card where an issuer does not connect the card to any covered separate credit feature that would make the prepaid card into a hybrid prepaid-credit card as defined in § 1026.61 at the time the card is issued and only opens a covered separate credit feature, or provides an application or solicitation to open a covered separate credit feature, or allows an existing credit feature to become a covered separate credit feature accessible by a hybrid prepaid-credit card as defined in § 1026.61 in compliance with § 1026.61(c). A covered separate credit feature may be added to a previously issued prepaid card only upon the consumer's application or specific request and only in compliance with § 1026.61(c). An issuer does not connect a prepaid card to a covered separate credit feature that would make the card into a credit card simply by providing the disclosures required by Regulation E, 12 CFR 1005.18(b)(2)(x), (b)(4)(iv), and (vii), with the prepaid card. See § 1026.12(a)(2) and related commentary for when a hybrid prepaid-credit card as defined in § 1026.61 may be issued as a replacement or substitution for another hybrid prepaid-credit card. See also Regulation E, 12 CFR 1005.5 and 1005.18(a), and related commentary, governing issuance of access devices under Regulation E.

8. *Unsolicited issuance of PINs.* A card issuer may issue personal identification numbers (PINs) to existing credit cardholders without a specific request from the cardholders, provided the PINs cannot be used alone to obtain credit. For example, the PINs may be necessary if consumers wish to use their existing credit cards at automated teller machines or at merchant locations with point of sale terminals that require PINs.

Paragraph 12(a)(2)

1. *Renewal.* Renewal generally contemplates the regular replacement of existing cards because of, for example, security reasons or new technology or systems. It also includes the re-issuance of cards that have been suspended temporarily, but does not include the opening of a new account after a previous account was closed.

2. *Substitution—examples.* Substitution encompasses the replacement of one card with another because the underlying account relationship has changed in some way—such as when the card issuer has:

i. Changed its name.

ii. Changed the name of the card.

iii. Changed the credit or other features available on the account. For example, the original card could be used to make purchases and obtain cash advances at teller windows. The substitute card might be usable, in addition, for obtaining cash advances through automated teller machines. (If the substitute card constitutes an access device, as defined in Regulation E, then the Regulation E issuance rules would have to be followed.) The substitution of one card with another on an unsolicited basis is not permissible, however, where in conjunction with the substitution an additional credit card account is opened and the consumer is able to make new purchases or advances under both the original and the new account with the new card. For example, if a retail card issuer replaces its credit card with a combined retailer/bank card, each of the creditors maintains a separate account, and both accounts can be accessed for new transactions by use of the new credit card, the card cannot be provided to a consumer without solicitation.

iv. Substituted a card user's name on the substitute card for the cardholder's name appearing on the original card.

v. Changed the merchant base, provided that the new card is honored by at least one of the persons that honored the original card. However, unless the change in the merchant base is the addition of an affiliate of the existing merchant base, the substitution of a new card for another on an unsolicited basis is not permissible where the account is inactive. A credit card cannot be issued in these circumstances without a request or application. For purposes of § 1026.12(a), an account is inactive if no credit has been extended and if the account has no outstanding balance for the prior 24 months. (See § 1026.11(b)(2).)

3. *Substitution—successor card issuer.* Substitution also occurs when a successor card issuer replaces the original card issuer (for example, when a new card issuer purchases the accounts of the original issuer and issues its own card to replace the original one). A permissible substitution exists even if the original issuer retains the existing receivables and the new card issuer acquires the right only to future receivables, provided use of the original card is cut off when use of the new card becomes possible.

4. *Substitution—non-credit-card plan.* A credit card that replaces a retailer's open-end credit plan not involving a credit card is not considered a substitute for the retailer's plan—even if the consumer used the retailer's plan. A credit card cannot be issued in these circumstances without a request or application.

5. *One-for-one rule.* An accepted card may be replaced by no more than one renewal or substitute card. For example, the card issuer may not replace a credit card permitting purchases and cash advances with two cards, one for the purchases and another for the cash advances.

6. *One-for-one rule—exceptions.* The regulation does not prohibit the card issuer from:

i. Replacing a single card that is both a debit card and a credit card, such as a hybrid debit-credit card as defined in § 1026.62, with a credit card and a separate debit card with only debit functions (or debit functions plus an associated capability to extend overdraft credit that is not covered overdraft credit as defined in § 1026.62), since the latter card could be issued on an unsolicited basis under Regulation E.

ii. Replacing a single card that is both a prepaid card and a credit card with a credit card and a separate prepaid card where the latter card is not a hybrid prepaid-credit card as defined in § 1026.61.

iii. Replacing an accepted card with more than one renewal or substitute card, provided that:

A. No replacement card accesses any account not accessed by the accepted card;

B. For terms and conditions required to be disclosed under § 1026.6, all replacement cards are issued subject to the same terms and conditions, except that a creditor may vary terms for which no change in terms notice is required under § 1026.9(c); and

C. Under the account's terms the consumer's total liability for unauthorized use with respect to the account does not increase.

7. *Methods of terminating replaced card.* The card issuer need not physically retrieve the original card, provided the old card is voided in some way, for example:

i. The issuer includes with the new card a notification that the existing card is no longer valid and should be destroyed immediately.

ii. The original card contained an expiration date.

iii. The card issuer, in order to preclude use of the card, reprograms computers or issues instructions to authorization centers.

8. *Incomplete replacement.* If a consumer has duplicate credit cards on the same account (Card A—one type of bank credit card, for example), the card issuer may not replace the duplicate cards with one Card A and one Card B (Card B—another type of bank credit card) unless the consumer requests Card B.

9. *Multiple entities.* Where multiple entities share responsibilities with respect to a credit card issued by one of them, the entity that issued the card may replace it on an unsolicited basis, if that entity terminates the original card by voiding it in some way, as described in comment 12(a)(2)–7. The other entity or entities may not issue a card on an unsolicited basis in these circumstances.

* * * * *

12(c) Right of Cardholder To Assert Claims or Defenses Against Card Issuer

1. *Relationship to § 1026.13.* The § 1026.12(c) credit card ''holder in due course'' provision deals with the consumer's right to assert against the card issuer a claim or defense concerning property or services purchased with a credit card, if the merchant has been unwilling to resolve the dispute. Even though certain merchandise disputes, such as non-delivery of goods, may also constitute ''billing errors'' under § 1026.13, that section operates independently of § 1026.12(c). The cardholder whose asserted billing error involves undelivered goods may institute the error resolution procedures of § 1026.13; but whether or not the cardholder has done so, the cardholder may assert claims or defenses under § 1026.12(c). Conversely, the consumer may pay a disputed balance and thus have no further right to assert claims and defenses, but still may assert a billing error if notice of that billing error is given in the proper time and manner. An assertion that a particular transaction resulted from unauthorized use of the card could also be both a ''defense'' and a billing error.

2. *Claims and defenses assertible.* Section 1026.12(c) merely preserves the consumer's right to assert against the card issuer any claims or defenses that can be asserted against the merchant. It does not determine what claims or defenses are valid as to the merchant; this determination must be made under state or other applicable law.

3. *Transactions excluded.* Section 1026.12(c) does not apply to the use of a check guarantee card or a debit card (other than a hybrid debit-credit card) in connection with an overdraft credit plan, or to a check guarantee card used in connection with cash-advance checks.

4. *Method of calculating the amount of credit outstanding.* The amount of the claim or defense that the cardholder may assert shall not exceed the amount of credit outstanding for the disputed transaction at the time the cardholder first notifies the card issuer or the person honoring the credit card of the existence of the claim or defense. However, when a consumer has asserted a claim or defense against a creditor pursuant to § 1026.12(c), the creditor must apply any payment or other credit in a manner that avoids or minimizes any reduction in the amount subject to that claim or defense. Accordingly, to determine the amount of credit outstanding for purposes of this section, payments and other credits must be applied first to amounts other than the disputed transaction.

i. For examples of how to comply with §§ 1026.12 and 1026.53 for credit card accounts under an open-end (not home-secured) consumer credit plan, see comment 53–3.

ii. For other types of credit card accounts, creditors may, at their option, apply payments consistent with § 1026.53 and comment 53–3. In the alternative, payments and other credits may be applied to: Late charges in the order of entry to the account; then to finance charges in the order of entry to the account; and then to any debits other than the transaction subject to the claim or defense in the order of entry to the account. In these circumstances, if more than one item is included in a single extension of credit, credits are to be distributed pro rata according to prices and applicable taxes.

5. *Prepaid cards.*

i. Section 1026.12(c) applies to property or services purchased with the hybrid prepaid-credit card that accesses a covered separate credit feature as defined in § 1026.61. The following examples illustrate when a hybrid prepaid-credit card is used to purchase property or services:

A. A consumer uses a hybrid prepaid-credit card as defined in § 1026.61 to make a purchase to obtain goods or services from a merchant and credit is drawn directly from a covered separate credit feature accessed by the hybrid prepaid-credit card without transferring funds into the asset feature of the prepaid account to cover the amount of the purchase. For example, assume that the consumer has $10 of funds in the asset feature of the prepaid account and initiates a transaction with a merchant to obtain goods or services with the hybrid prepaid-credit card for $25. In this case, $10 is debited from the asset feature and $15 of credit is drawn directly from the covered separate credit feature accessed by the hybrid prepaid-credit card without any transfer of funds into the asset feature of the prepaid account to cover the amount of the purchase. In this case, the consumer is using credit accessed by the hybrid prepaid-credit card to purchase property or services where credit is drawn directly from the covered separate credit feature accessed by the hybrid prepaid-credit card to cover the amount of the purchase.

B. A consumer uses a hybrid prepaid-credit card as defined in § 1026.61 to make a purchase to obtain goods or services from a merchant and credit is transferred from a covered separate credit feature accessed by the hybrid prepaid-credit card into the asset feature of the prepaid account to cover the amount of the purchase. For example, assume the same facts as above, except that the $15 will be transferred from a covered separate credit feature to the asset feature, and a transaction of $25 is debited from the asset feature of the prepaid account. In this case, the consumer is using credit accessed by the hybrid prepaid-credit card to purchase property or services because credit is transferred to the asset feature of the prepaid account to cover the amount of a purchase made with the card. This is true even though the $15 credit transaction is treated as ''nonsale credit'' under § 1026.8(b). *See* comments 8(a)–9.ii and 8(b)–1.vi.

ii. For a transaction at point of sale where a hybrid prepaid-credit card is used to obtain goods or services from a merchant and the transaction is partially paid with funds from the asset feature of the prepaid account, and partially paid with credit from the covered separate credit feature, the amount of the purchase transaction that is funded by credit generally would be subject to the requirements of § 1026.12(c). The amount of the transaction funded from the prepaid account would not be subject to the requirements of § 1026.12(c).

12(c)(1) General Rule

1. *Situations excluded and included.* The consumer may assert claims or defenses only when the goods or services are ''purchased with the credit card.'' This would include when the goods or services are purchased by a consumer using a hybrid prepaid-credit card to access a covered separate credit feature as defined in § 1026.61 or using a hybrid debit-credit card to access a covered overdraft credit account as defined in § 1026.62. This could include mail, the internet or telephone orders, if the purchase is charged to the credit card account. But it would exclude:

i. Use of a credit card to obtain a cash advance, even if the consumer then uses the money to purchase goods or services. Such a transaction would not involve ''property or services purchased with the credit card.''

ii. The purchase of goods or services by use of a check accessing an overdraft account and a credit card used solely for identification of the consumer. (On the other hand, if the credit card is used to make partial payment for the purchase and not merely for identification, the right to assert claims or defenses would apply to credit extended via the credit card, although not to credit extended by the overdraft line. If partial payment for the purchase is made with a hybrid prepaid-credit card or a hybrid debit-credit card, the right to assert claims or defenses would apply to credit accessed from a covered separate credit feature or covered overdraft credit account, respectively.)

iii. Purchases made by use of a check guarantee card in conjunction with a cash advance check (or by cash advance checks alone). (*See* comment 12(c)–3.) A cash advance check is a check that, when written, does not draw on an asset account; instead, it is charged entirely to an open-end credit account.

iv. Purchases effected by use of either a check guarantee card or a debit card (other than a hybrid debit-credit card) when used to draw on overdraft credit plans. (*See* comment 12(c)–3.) The debit card exemption applies whether the card accesses an asset account via point of sale terminals, automated teller machines, or in any other way, and whether the card qualifies as an ''access device'' under Regulation E or is only a paper based debit card. If a card serves both as an ordinary credit card and also as a check guarantee or debit card, a transaction will be subject to this rule on asserting claims and defenses when used as an ordinary credit card (including when used as a hybrid debit-credit card to access a covered overdraft credit account), but not when used as a check guarantee or debit card. For purchases effected by use of a hybrid debit-credit card where the transaction is partially paid with funds from the asset account, and partially paid with covered overdraft credit, the provisions of § 1026.12(c) apply only to the credit portion of the purchase transaction.

* * * * *

Section 1026.55—Limitations on Increasing Annual Percentage Rates, Fees, and Charges

55(a) General Rule

1. *Increase in rate, fee, or charge.* Section 1026.55(a) prohibits card issuers from increasing an annual percentage rate or any fee or charge required to be disclosed under § 1026.6(b)(2)(ii), (b)(2)(iii), or (b)(2)(xii) on a credit card account unless specifically permitted by one of the exceptions in § 1026.55(b). Except as specifically provided in § 1026.55(b), this prohibition applies even if the circumstances under which an increase will occur are disclosed in advance. The following examples illustrate the general application of § 1026.55(a) and (b). Additional examples illustrating specific aspects of the exceptions in § 1026.55(b) are provided in the commentary to those exceptions.

i. *Account-opening disclosure of non-variable rate for six months, then variable rate.* Assume that, at account opening on January 1 of year one, a card issuer discloses that the annual percentage rate for purchases is a non-variable rate of 15% and will apply for six months. The card issuer also discloses that, after six months, the annual percentage rate for purchases will be a variable rate that is currently 18% and will be adjusted quarterly by adding a margin of 8 percentage points to a publicly-available index not under the card issuer's control. Furthermore, the card issuer discloses that the annual percentage rate for cash advances is the same variable rate that will apply to purchases after six months. Finally, the card issuer discloses that, to the extent consistent with § 1026.55 and other applicable law, a non-variable penalty rate of 30% may apply if the consumer makes a late payment. The payment due date for the account is the twenty-fifth day of the month and the required minimum periodic payments are applied to accrued interest and fees but do not reduce the purchase and cash advance balances.

A. *Change-in-terms rate increase for new transactions after first year.* On January 15 of year one, the consumer uses the account to make a $2,000 purchase and a $500 cash advance. No other transactions are made on the account. At the start of each quarter, the card issuer may adjust the variable rate that applies to the $500 cash advance consistent with changes in the index (pursuant to § 1026.55(b)(2)). All required minimum periodic payments are received on or before the payment due date until May of year one, when the payment due on May 25 is received by the creditor on May 28. At this time, the card issuer is prohibited by § 1026.55 from increasing the rates that apply to the $2,000 purchase, the $500 cash advance, or future purchases and cash advances. Six months after account opening (July 1), the card issuer may begin to accrue interest on the $2,000 purchase at the previously-disclosed variable rate determined using an 8-point margin (pursuant to § 1026.55(b)(1)). Because no other increases in rate were disclosed at account opening, the card issuer may not subsequently increase the variable rate that applies to the $2,000 purchase and the $500 cash advance (except due to increases in the index pursuant to § 1026.55(b)(2)). On November 16, the card issuer provides a notice pursuant to § 1026.9(c) informing the consumer of a new variable rate that will apply on January 1 of year two (calculated using the same index and an increased margin of 12 percentage points). On December 15, the consumer makes a $100 purchase. On January 1 of year two, the card issuer may increase the margin used to determine the variable rate that applies to new purchases to 12 percentage points (pursuant to § 1026.55(b)(3)). However, § 1026.55(b)(3)(ii) does not permit the card issuer to apply the variable rate determined using the 12-point margin to the $2,000 purchase balance. Furthermore, although the $100 purchase occurred more than 14 days after provision of the § 1026.9(c) notice, § 1026.55(b)(3)(iii) does not permit the card issuer to apply the variable rate determined using the 12-point margin to that purchase because it occurred during the first year after account opening. On January 15 of year two, the consumer makes a $300 purchase. The card issuer may apply the variable rate determined using the 12-point margin to the $300 purchase.

B. *Account becomes more than 60 days delinquent during first year.* Same facts as above except that the required minimum periodic payment due on May 25 of year one is not received by the card issuer until July 30 of year one. Because the card issuer received the required minimum periodic payment more than 60 days after the payment due date, § 1026.55(b)(4) permits the card issuer to increase the annual percentage rate applicable to the $2,000 purchase, the $500 cash advance, and future purchases and cash advances. However, § 1026.55(b)(4)(i) requires the card issuer to first comply with the notice requirements in § 1026.9(g). Thus, if the card issuer provided a § 1026.9(g) notice on July 25 stating that all rates on the account would be increased to the 30% penalty rate, the card issuer could apply that rate beginning on September 8 to all balances and to future transactions.

ii. *Account-opening disclosure of non-variable rate for six months, then increased non-variable rate for six months, then variable rate; change-in-terms rate increase for new transactions after first year.* Assume that, at account opening on January 1 of year one, a card issuer discloses that the annual percentage rate for purchases will increase as follows: A non-variable rate of 5% for six months; a non-variable rate of 10% for an additional six months; and thereafter a variable rate that is currently 15% and will be adjusted monthly by adding a margin of 5 percentage points to a publicly-available index not under the card issuer's control. The payment due date for the account is the fifteenth day of the month and the required minimum periodic payments are applied to accrued interest and fees but do not reduce the purchase balance. On January 15 of year one, the consumer uses the account to make a $1,500 purchase. Six months after account opening (July 1), the card issuer may begin to accrue interest on the $1,500 purchase at the previously-disclosed 10% non-variable rate (pursuant to § 1026.55(b)(1)). On September 15, the consumer uses the account for a $700 purchase. On November 16, the card issuer provides a notice pursuant to § 1026.9(c) informing the consumer of a new variable rate that will apply on January 1 of year two (calculated using the same index and an increased margin of 8 percentage points). One year after account opening (January 1 of year two), the card issuer may begin accruing interest on the $2,200 purchase balance at the previously-disclosed variable rate determined using a 5-point margin (pursuant to § 1026.55(b)(1)). Section 1026.55 does not permit the card issuer to apply the variable rate determined using the 8-point margin to the $2,200 purchase balance. Furthermore, § 1026.55 does not permit the card issuer to subsequently increase the variable rate determined using the 5-point margin that applies to the $2,200 purchase balance (except due to increases in the index pursuant to § 1026.55(b)(2)). The card issuer may, however, apply the variable rate determined using the 8-point margin to purchases made on or after January 1 of year two (pursuant to § 1026.55(b)(3)).

iii. *Change-in-terms rate increase for new transactions after first year; penalty rate increase after first year.* Assume that, at account opening on January 1 of year one, a card issuer discloses that the annual percentage rate for purchases is a variable rate determined by adding a margin of 6 percentage points to a publicly-available index outside of the card issuer's control. The card issuer also discloses that, to the extent consistent with § 1026.55 and other applicable law, a non-variable penalty rate of 28% may apply if the consumer makes a late payment. The due date for the account is the fifteenth of the month. On May 30 of year two, the account has a purchase balance of $1,000. On May 31, the card issuer provides a notice pursuant to § 1026.9(c) informing the consumer of a new variable rate that will apply on July 16 for all purchases made on or after June 15 (calculated by using the same index and an increased margin of 8 percentage points). On June 14, the consumer makes a $500 purchase. On June 15, the consumer makes a $200 purchase. On July 1, the card issuer has not received the payment due on June 15 and provides the consumer with a notice pursuant to § 1026.9(g) stating that the 28% penalty rate will apply as of August 15 to all transactions made on or after July 16 and that, if the consumer becomes more than 60 days late, the penalty rate will apply to all balances on the account. On July 17, the consumer makes a $300 purchase.

A. *Account does not become more than 60 days delinquent.* The payment due on June 15 of year two is received on July 2. On July 16, § 1026.55(b)(3)(ii) permits the card issuer to apply the variable rate determined using the 8-point margin disclosed in the § 1026.9(c) notice to the $200 purchase made on June 15 but does not permit the card issuer to apply this rate to the $1,500 purchase balance. On August 15, § 1026.55(b)(3)(ii) permits the card issuer to apply the 28% penalty rate disclosed at account opening and in the § 1026.9(g) notice to the $300 purchase made on July 17 but does not permit the card issuer to apply this rate to the $1,500 purchase balance (which remains at the variable rate determined using the 6-point margin) or the $200 purchase (which remains at the variable rate determined using the 8-point margin).

B. *Account becomes more than 60 days delinquent after provision of § 1026.9(g) notice.* Same facts as above except the payment due on June 15 of year two has not been received by August 15. Section 1026.55(b)(4) permits the card issuer to apply the 28% penalty rate to the $1,500 purchase balance and the $200 purchase because it has not received the June 15 payment within 60 days after the due date. However, in order to do so, § 1026.55(b)(4)(i) requires the card issuer to first provide an additional notice pursuant to § 1026.9(g). This notice must be sent no earlier than August 15, which is the first day the account became more than 60 days' delinquent. If the notice is sent on August 15, the card issuer may begin accruing interest on the $1,500 purchase balance and the $200 purchase at the 28% penalty rate beginning on September 29.

2. *Relationship to grace period.* Nothing in § 1026.55 prohibits a card issuer from assessing interest due to the loss of a grace period to the extent consistent with § 1026.5(b)(2)(ii)(B) and § 1026.54. In addition, a card issuer has not reduced an annual percentage rate on a credit card account for purposes of § 1026.55 if the card issuer does not charge interest on a balance or a portion thereof based on a payment received prior to the expiration of a grace period. For example, if the annual percentage rate for purchases on an account is 15% but the card issuer does not charge any interest on a $500 purchase balance because that balance was paid in full prior to the expiration of the grace period, the card issuer has not reduced the 15% purchase rate to 0% for purposes of § 1026.55.

3. *Fees in connection with covered separate credit features accessible by hybrid prepaid-credit cards.* With regard to a covered separate credit feature and an asset feature on a prepaid account that are both accessible by a hybrid prepaid-credit card as defined in § 1026.61 where the credit feature is a credit card account under an open-end (not home-secured) consumer credit plan, § 1026.55(a) prohibits card issuers from increasing an annual percentage rate or any fee or charge required to be disclosed under § 1026.6(b)(2)(ii), (iii), or (xii) on a credit card account unless specifically permitted by one of the exceptions in § 1026.55(b). This is true regardless of whether these fees or annual percentage rates are imposed on the asset feature of the prepaid account or on the credit feature.

4. *Fees imposed on the asset feature of a prepaid account that are not charges imposed as part of the plan.* Section 1026.55(a) does not apply to any fee or charge imposed on the asset feature of the prepaid account that is not a charge imposed as part of the plan under § 1026.6(b)(3). See § 1026.6(b)(3)(iii)(D) and (E) and related commentary regarding fees imposed on the asset feature of the prepaid account that are not charges imposed as part of the plan under § 1026.6(b)(3) with respect to covered separate credit features accessible by hybrid prepaid-credit cards and non-covered separate credit features as those terms are defined in § 1026.61.

5. *Fees in connection with covered overdraft credit.* With regard to covered overdraft credit accessible by a hybrid debit-credit card, § 1026.55(a) prohibits card issuers from increasing an annual percentage rate or any fee or charge required to be disclosed under § 1026.6(b)(2)(ii), (iii), or (xii) on a credit card account unless specifically permitted by one of the exceptions in § 1026.55(b). This is true regardless of whether these fees or annual percentage rates are imposed on the covered asset account associated with the covered overdraft credit or on the covered overdraft credit account.

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Section 1026.57—Reporting and Marketing Rules for College Student Open-End Credit

57(a) Definitions

57(a)(1) College Student Credit Card

1. *Definition.* The definition of college student credit card excludes home-equity lines of credit accessed by credit cards and covered overdraft credit accounts as defined in 1026.62 offered by a creditor other than a very large financial institution as defined in 1026.62 that is accessed by a debit card or account number. A college student credit card includes a college affinity card within the meaning of TILA section 127(r)(1)(A). In addition, a card may fall within the scope of the definition regardless of the fact that it is not intentionally targeted at or marketed to college students. For example, an agreement between a college and a card issuer may provide for marketing of credit cards to alumni, faculty, staff, and other non-student consumers who have a relationship with the college, but also contain provisions that contemplate the issuance of cards to students. A credit card issued to a student at the college in connection with such an agreement qualifies as a college student credit card. The definition of college student credit card includes a hybrid prepaid-credit card as defined by § 1026.61 that is issued to any college student where the card can access a covered separate credit feature that is a credit card account under an open-end (not home-secured) consumer credit plan. The definition of college student credit card also includes a prepaid account as defined in § 1026.61 that is issued to any college student where a covered separate credit feature that is a credit card account under an open-end (not home-secured) consumer credit plan accessible by a hybrid prepaid-credit card as defined by § 1026.61 may be added in the future to the prepaid account.

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