

**FEDERAL RESERVE SYSTEM****12 CFR Part 205****[Regulation E; Docket No. R-1343]****Electronic Fund Transfers****AGENCY:** Board of Governors of the Federal Reserve System.**ACTION:** Proposed rule; request for public comment.

**SUMMARY:** The Board is proposing to amend Regulation E, which implements the Electronic Fund Transfer Act, and the official staff commentary to the regulation, which interprets the requirements of Regulation E. The proposal would limit the ability of a financial institution to assess an overdraft fee for paying automated teller machine (ATM) withdrawals and one-time debit card transactions that overdraw a consumer's account, unless the consumer is given notice of the right to opt out of the payment of such overdrafts, and the consumer does not opt out. As an alternative approach, the proposal would limit the ability of a financial institution to assess an overdraft fee for paying ATM withdrawals and one-time debit card transactions that overdraw a consumer's account, unless the consumer affirmatively consents, or opts in, to the institution's payment of overdrafts for these transactions. In addition, the proposal would prohibit financial institutions from assessing an overdraft fee if the overdraft would not have occurred but for a debit hold placed on funds in the consumer's account that exceeds the actual amount of the transaction.

**DATES:** Comments must be received on or before March 30, 2009.**ADDRESSES:** You may submit comments, identified by Docket No. R-1343, by any of the following methods:

- *Agency Web Site:* <http://www.federalreserve.gov>. Follow the instructions for submitting comments at <http://www.federalreserve.gov/generalinfo/foia/ProposedRegs.cfm>.

- *Federal eRulemaking Portal:* <http://www.regulations.gov>. Follow the instructions for submitting comments.

- *E-mail:* [regs.comments@federalreserve.gov](mailto:regs.comments@federalreserve.gov). Include the docket number in the subject line of the message.

- *FAX:* (202) 452-3819 or (202) 452-3102.

- *Mail:* Jennifer J. Johnson, Secretary, Board of Governors of the Federal Reserve System, 20th Street and Constitution Avenue, NW., Washington, DC 20551.

All public comments are available from the Board's Web site at <http://www.federalreserve.gov/generalinfo/foia/ProposedRegs.cfm> as submitted, unless modified for technical reasons. Accordingly, your comments will not be edited to remove any identifying or contact information. Public comments may also be viewed electronically or in paper form in Room MP-500 of the Board's Martin Building (20th and C Streets, NW.) between 9 a.m. and 5 p.m. on weekdays.

**FOR FURTHER INFORMATION CONTACT:** Ky Tran-Trong, Counsel, Dana Miller, Attorney, or Vivian Wong, Senior Attorney, Division of Consumer and Community Affairs, Board of Governors of the Federal Reserve System, Washington, DC 20551, at (202) 452-2412 or (202) 452-3667. For users of Telecommunications Device for the Deaf (TDD) only, contact (202) 263-4869.

**SUPPLEMENTARY INFORMATION:****I. Statutory Background**

The Electronic Fund Transfer Act (15 U.S.C. 1693 *et seq.*) (EFTA or Act), enacted in 1978, provides a basic framework establishing the rights, liabilities, and responsibilities of participants in electronic fund transfer (EFT) systems. The EFTA is implemented by the Board's Regulation E (12 CFR part 205). Examples of the types of transactions covered by the Act and regulation include transfers initiated through an ATM, point-of-sale (POS) terminal, automated clearinghouse (ACH), telephone bill-payment plan, or remote banking service. The Act and regulation provide for the disclosure of terms and conditions of an EFT service; documentation of EFTs by means of terminal receipts and periodic account activity statements; limitations on consumer liability for unauthorized transfers; procedures for error resolution; and certain rights related to preauthorized EFTs. Further, the Act and regulation restrict the unsolicited issuance of ATM cards and other access devices.

The official staff commentary (12 CFR part 205 (Supp. I)) interprets the requirements of Regulation E to facilitate compliance and provides protection from liability under Sections 915 and 916 of the EFTA for financial institutions and other persons subject to the Act. 15 U.S.C. 1693m(d)(1). The commentary is updated periodically to address significant questions that arise.

**II. Background***Overview of Overdraft Services*

Historically, if a consumer sought to engage in a transaction that would overdraw his or her deposit account, the consumer's financial institution used its discretion on an ad hoc basis to determine whether to pay the overdraft. If an overdraft was paid, the institution usually imposed a fee on the consumer's account. In recent years, many institutions have largely automated the overdraft payment process. Automation is used to apply specific criteria for determining whether to honor overdrafts and to set limits on the amount of coverage provided.

Overdraft services vary among institutions but often share certain common characteristics. In most cases, consumers that meet a depository institution's criteria are automatically enrolled in overdraft services. While institutions generally do not underwrite on an individual account basis when enrolling the consumer in an overdraft service, most institutions will review individual accounts periodically to determine whether the consumer continues to qualify for the service and the amount of overdraft coverage provided. Most institutions disclose that the payment of overdrafts is discretionary, and that the institution has no legal obligation to pay any overdraft.<sup>1</sup>

In the past, institutions generally provided overdraft coverage only for check transactions. In recent years, however, the service has been extended to cover overdrafts resulting from non-check transactions, including ATM withdrawals, debit card transactions at POS, online transactions, preauthorized transfers, and ACH transactions.<sup>2</sup>

<sup>1</sup> These transactions are generally not covered under Regulation Z (Truth in Lending) if there is no written agreement between the consumer and institution to pay an overdraft and impose a fee. See 12 CFR 226.4(c)(3).

<sup>2</sup> According to the FDIC's Study of Bank Overdraft Programs, nearly 70 percent of banks surveyed implemented their automated overdraft program after 2001. In addition, 81 percent of banks surveyed that operate automated programs allow overdrafts to be paid at ATMs and POS debit card terminals. See FDIC Study of Bank Overdraft Programs 8, 10 (November 2008) (hereinafter, *FDIC Study*) (available at: [http://www.fdic.gov/bank/analytical/overdraft/FDIC138\\_Report\\_FinalTOC.pdf](http://www.fdic.gov/bank/analytical/overdraft/FDIC138_Report_FinalTOC.pdf)). See also *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) (hereinafter, *Overdraft Protection Hearing*) (available at [http://www.house.gov/apps/list/hearing/financialsvcs\\_dem/hr0705072.shtml](http://www.house.gov/apps/list/hearing/financialsvcs_dem/hr0705072.shtml)) (stating 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).

A flat fee is charged each time an overdraft is paid, regardless of the amount of the overdraft. Institutions commonly charge the same amount for paying the overdraft as they would if they returned the item unpaid. Some institutions may also impose a fee for each day the account remains overdrawn.

According to a recent report from the Government Accountability Office (GAO), the average cost of overdraft and insufficient funds fees was just over \$26 per item in 2007.<sup>3</sup> The GAO also reported that large institutions on average charged between \$4 and \$5 more for overdraft and insufficient fund fees compared to smaller institutions.<sup>4</sup> In addition, the GAO noted that a small number of institutions (primarily large banks) apply tiered fees to overdrafts, charging higher fees as the number of overdrafts in the account increases.<sup>5</sup>

#### *Industry and Consumer Group Perspectives*

From the industry's perspective, automated overdraft services enable institutions to reduce the cost of manually reviewing individual items, and also ensure that all consumers are treated consistently with respect to overdraft payment decisions. Industry representatives observe that whether an overdrawn check is paid or returned, the consumer will be charged the same amount by the consumer's financial institution. Industry representatives also assert, however, that when an overdrawn check is paid, consumers receive significant benefits because they can avoid additional fees that would be charged by the merchant if the item was

returned unpaid, and other adverse consequences, such as the furnishing of negative information to a consumer reporting agency.<sup>6</sup>

In contrast, consumer groups assert that overdraft transactions are a high-cost form of lending that trap low- and moderate-income consumers into paying high fees. Consumer groups also state that consumers are often enrolled in overdraft services automatically without their request or consent. In addition, consumer groups believe that by honoring overdrafts, institutions encourage consumer reliance on the service and therefore, consumers incur greater costs in the long run than they would if the transactions were not honored. Consumer groups note, for example, that historically, institutions declined a consumer's request for an ATM withdrawal or debit card transaction if the consumer did not have sufficient funds in his or her account.<sup>7</sup> Today, however, institutions are more likely to cover those overdrafts and assess a fee on the consumer's account for doing so.<sup>8</sup> According to consumer groups, this practice can be particularly costly in connection with debit card overdrafts because the dollar amount of the fee is likely to considerably exceed the dollar amount of the overdraft.<sup>9</sup> In addition, multiple fees may be assessed in a single day for a series of small-dollar transactions. Because of these costs, consumer groups assert that most consumers would prefer that their bank decline debit card transactions if the transactions would overdraw their account.<sup>10</sup>

#### *Previous Agency Actions*

In February 2005, the Board, Federal Deposit Insurance Commission (FDIC), Office of the Comptroller of the Currency (OCC), and National Credit Union Administration (NCUA) (collectively, the federal banking agencies) issued guidance on overdraft protection programs in response to the increased availability and customer use of overdraft protection services (Joint Guidance).<sup>11</sup> The Joint Guidance addresses three primary areas—safety and soundness considerations, legal risks, and best practices. The Office of Thrift Supervision (OTS) issued separate guidance (OTS Guidance) that focuses on safety and soundness considerations and best practices.<sup>12</sup> The best practices described in the Joint Guidance and the OTS Guidance address the marketing and communications that accompany the offering of overdraft services, as well as the disclosure and operation of program features, including the provision of consumer choice to opt out of the overdraft service.<sup>13</sup>

In May 2005, the Board revised Regulation DD and the staff commentary pursuant to its authority under the Truth in Savings Act (TISA) to address concerns about institutions' disclosure of overdraft fees generally, and the advertisement of overdraft services.<sup>14</sup> The goal of the Regulation DD revisions was to improve the uniformity and adequacy of disclosures provided to consumers about overdraft and returned-item fees to assist consumers in better understanding the costs associated with the payment of overdrafts. In addition, the final rule addressed some of the Board's concerns about institutions' marketing practices with respect to overdraft services.

#### *May 2008 FTC Act and Regulation DD Proposals*

In May 2008, the Board, along with the OTS and the NCUA (collectively, the Agencies), proposed to exercise their authority under the Federal Trade Commission Act (FTC Act) to prohibit institutions from assessing any fees on a consumer's account in connection

<sup>3</sup> See *Bank Fees: Federal Banking Regulators Could Better Ensure That Consumers Have Required Disclosure Documents Prior to Opening Checking or Savings Accounts*, GAO Report 08-281, at 14 (January 2008) (hereinafter, *GAO Bank Fees Report*). See also *Bankrate 2008 Checking Account Study*, posted October 27, 2008 (available at: <http://www.bankrate.com/brm/news/chk/chkstudy/20081027-bounced-check-fees-a1.asp?caret=2>) (reporting an average overdraft fee of approximately \$29 per item).

<sup>4</sup> See *GAO Bank Fees Report* at 16. A recent survey suggests that the cost difference in overdraft fees between small and large institutions may be larger than reported by the GAO, however. See also "Disparities in Checking Overdraft Fees by Geography and Size," Press release, Moeb\$ Services (October 25, 2008) (*Moeb\$ 2008 Pricing Survey Press Release*) (available at: <http://moeb.com/AboutUs/Pressreleases/tabid/58/ctl/Details/mid/380/ItemID/29/Default.aspx>) (reporting that banks with more than \$20 billion in assets charged on average \$33.43 per overdrawn check compared to \$24.28 per overdrawn check for banks and credit unions with less than \$100 million in assets).

<sup>5</sup> According to the GAO, of the financial institutions that applied up to three tiers of fees in 2006, the average overdraft fees were \$26.74, \$32.53 and \$34.74, respectively. See *GAO Bank Fees Report* at 14.

<sup>6</sup> See, e.g., *Overdraft Protection Hearing* at 44.

<sup>7</sup> See, e.g., *Overdraft Protection Hearing* at 72 (stating 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).

<sup>8</sup> See, e.g., *FDIC Study* at 10 (reporting that 81 percent of banks surveyed that operate automated programs allow overdrafts to be paid at ATMs and POS debit card terminals).

<sup>9</sup> See, e.g., *Overdraft Protection Hearing* at 72.

<sup>10</sup> See Leslie Parrish, *Consumers Want Informed Choice on Overdraft Fees and Banking Options*, Ctr. for Responsible Lending (April 16, 2008) (reporting the results of a survey indicating that 80 percent of consumers would prefer that a debit card transaction be declined if a \$5 purchase would result in an overdraft and an accompanying \$34 fee) (available at: <http://www.responsiblelending.org/pdfs/final-caravan-survey-4-16-08.pdf>). But see *80 Percent of Consumers Have Not Paid Overdraft Fees in Past Year, Says ABA Survey*, Press Release, American Bankers Association (August 30, 2007) (reporting survey results indicating that of those consumers who had paid an overdraft fee in the past 12 months, 88 percent had wanted the payment covered) (available at: <http://www.aba.com/Press+Room/083007ABASurvey.htm>).

<sup>11</sup> See Interagency Guidance on Overdraft Protection Programs, 70 FR 9127, Feb. 24, 2005.

<sup>12</sup> See OTS Guidance on Overdraft Protection Programs, 70 FR 8428, Feb. 18, 2005.

<sup>13</sup> The federal banking agencies have also published a consumer brochure on overdraft services. The brochure, entitled "Protecting Yourself from Overdraft and Bounced-Check Fees," can be found at: <http://www.federalreserve.gov/pubs/bounce/default.htm>.

<sup>14</sup> 70 FR 29582, May 24, 2005. A substantively similar rule applying to credit unions was issued separately by the NCUA. 71 FR 24568, Apr. 26, 2006.

with an overdraft service, unless the consumer is given notice and the right to opt out of the institution's overdraft service, and the consumer does not opt out. 73 FR 28904, May 19, 2008. The proposed opt-out right would have applied to overdrafts resulting from all methods of payment, including checks, ACH transactions, ATM withdrawals, recurring payments, and POS debit card transactions. The proposal also would have required institutions to provide consumers with the option of opting out only of the payment of overdrafts for ATM withdrawals and debit card transactions at POS. In addition, the proposal would have prohibited institutions from assessing overdraft fees where the overdraft would not have occurred but for a debit hold placed on funds in the consumer's account in excess of the actual transaction amount.

Concurrent with the issuance of the May 2008 FTC Act Proposal, the Board separately issued a proposal under Regulation DD (Truth in Savings), which set forth proposed form, content, and timing requirements for providing the opt-out notice. 73 FR 28730, May 19, 2008. To facilitate compliance, the Regulation DD proposal contained a model form that institutions could use to satisfy the opt-out notice requirement. Collectively, the two proposals on overdraft services were intended to ensure that consumers understand how overdraft services operate generally and have the opportunity to avoid the associated costs where such services do not meet their needs.

In addition to the proposed requirements regarding the form and content of the opt-out notice, the Regulation DD proposal set forth proposed revisions that would require all institutions to provide aggregate totals for overdraft fees and for returned item fees for the statement period and the year-to-date. Currently, only institutions that promote the payment of overdrafts are subject to this requirement. The Regulation DD proposal also addressed balance disclosures provided to consumers through automated systems, such as ATMs and online banking services. These provisions are adopted in final form under Regulation DD elsewhere in today's **Federal Register**.

#### *Overview of Comments Received*

The Agencies received approximately 1,500 comment letters on the proposed opt-out right for overdraft services under the May 2008 FTC Act Proposal. Consumer groups, members of Congress, the FDIC, and individual consumers supported the Agencies' proposal, but

urged the Agencies to require institutions to obtain a consumer's affirmative consent (that is, an opt-in) before any fees could be charged for paying an overdraft. Some of these commenters also argued that overdraft services provide extensions of credit that should be subject to the Truth in Lending Act (TILA) so that consumers would be better able to compare the cost of overdraft services to the cost of other credit alternatives.

In contrast, the majority of industry commenters opposed the proposed rule. Industry commenters asserted that consumers derive substantial benefit from overdraft services, particularly in connection with check transactions. While institutions generally assess the same fee whether a check is paid or returned, industry commenters observed that the payment of overdrafts for checks enables consumers to avoid other adverse consequences, such as merchant fees, the furnishing of negative information for credit reports, and violations of bad check laws. Some industry commenters urged the Board to instead use other regulatory authority, such as Regulations DD or E, to address concerns about overdraft services.

Industry commenters also asserted that consumers may not fully understand the implications of opting out, and that those who elect to do so might unintentionally incur significant costs. In this regard, industry commenters and the OCC stated that if the opt-out right applied to check transactions, more checks would be returned unpaid. Industry commenters and the OCC also noted a potential unintended consequence of the proposal could be that institutions would lengthen their availability schedules to the extent permitted by the Board's Regulation CC, 12 CFR part 229, to ensure that there are sufficient funds in the payor's account to cover a deposited check. As a result, they argued, consumers may experience a longer waiting period before gaining access to deposited funds than currently is the case today.

With respect to implementing the proposed opt-out requirement, industry commenters raised a number of operational issues. These commenters were most concerned about the feasibility of limiting the opt-out right only to overdrafts paid in connection with ATM withdrawals and POS debit card transactions. Some industry commenters, however, argued that if the Agencies deemed it necessary to create a consumer opt-out right, it should be limited to ATM withdrawals and POS debit card transactions. These commenters noted that the majority of

complaints about overdraft services arise in connection with debit card transactions in which the amount of the overdraft fee is substantially higher than the amount of the overdraft. Industry commenters also questioned the merits of requiring institutions to provide an opt-out notice following the assessment of an overdraft fee in light of the costs of printing and mailing additional opt-out notices.

With respect to the debit hold provision, individual consumers and consumer groups generally supported the Agencies' proposal. Industry commenters, in contrast, expressed concern about the operational burdens associated with the proposal because it could require institutions to retroactively monitor, and adjust, overdraft fees that have been assessed to a consumer's account. Industry commenters also urged the Agencies to instead adopt a disclosure-based rule applying to merchants that are responsible for placing the hold.

The Board also received over 600 comments in response to the Regulation DD proposal regarding the timing, format and content of the opt-out notice. Most of the comments came from individual consumers, who supported the proposed rule. The remaining comments came from financial institutions, industry trade associations, consumer groups, members of Congress, other federal banking agencies, state and local governments, and others.

Consumer groups supported the proposed content and model form for notifying consumers of their right to opt out of an overdraft service, but urged the Board to enhance the model form in various ways, including making the opt-out notice more prominent. Several industry commenters argued that the proposed model form was unduly biased towards encouraging consumers to opt out, and did not sufficiently explain that the payment of overdrafts was discretionary. Some industry commenters also urged the Board to eliminate the requirement to provide notice of the opt-out right following the assessment of an overdraft fee, stating that an initial notice was sufficient to apprise consumers of that right.

#### *Consumer Testing*

In addition to reviewing the comments received on the two proposals, the Board worked with a testing consultant, Macro International, Inc. (Macro), to revise the proposed model opt-out notice and conduct consumer testing of the revised notice. Two rounds of one-on-one interviews with a diverse group of consumers were completed in the fall of 2008. In general,

after reviewing the model disclosures, test participants generally understood the concept of overdraft coverage, and that they would be charged fees if their institution paid their overdrafts.

Participants also appeared to understand that if they opted out of overdraft coverage, this meant their checks would not be paid and they could be charged fees by both their institution and by the merchant.

During the first round of testing, Macro tested an opt-out form that allowed consumers to opt out of the payment of overdrafts for all transaction types, including checks and recurring debits. In the second round of testing, Macro tested an opt-out form that limited the opt-out right to ATM withdrawals and one-time debit card transactions made at POS and online. The majority of participants during both rounds indicated that they likely would not opt out if the opt-out also applied to checks. However, when asked if they would opt out if the choice was limited to opting out of overdrafts in connection with ATM withdrawals and one-time debit card purchases, half of the participants indicated that they would consider doing so.<sup>15</sup>

### III. Summary of Proposal

#### *Overdrafts*

The Board is proposing amendments to Regulation E and the staff commentary to assist consumers in understanding how overdraft services provided by their institutions operate and to ensure that consumers have the opportunity to limit the overdraft costs associated with ATM withdrawals and one-time debit card transactions where such services do not meet their needs. The Board is proposing two alternative approaches in proposed § 205.17 of Regulation E. In addition, as stated elsewhere in today's **Federal Register**, the Board is not taking action on the May 2008 FTC Act (Regulation AA) and Regulation DD Proposals regarding consumers' right to opt out of overdraft services.

Under the first approach, institutions would be required to provide consumers with notice of the right to opt out of the institution's overdraft service for ATM withdrawals and one-time debit card transactions. The notice must be provided to the consumer before the institution may assess any fees or charges to a consumer's account for paying such overdrafts. Under this approach, the opt-out notice would generally be given at account opening (or any time before any overdraft fees

are assessed) and subsequently for each periodic statement cycle in which the institution assesses a fee or charge to the consumer's account for paying an overdraft.

Under the second approach, institutions would be required to provide consumers with notice of the right to opt in, or affirmatively consent, to the institution's overdraft service for ATM withdrawals and one-time debit card transactions. The notice must be provided, and the consumer's affirmative consent obtained, before the institution could assess a fee or charge on the consumer's account for paying such overdrafts. Under this approach, additional notices following the assessment of a fee or charge for paying an ATM or one-time debit card overdraft would not be required once the consumer has opted in to the overdraft service.

Both approaches would permit institutions to implement the consumer's choice by providing an account that would not permit the payment of overdrafts for ATM withdrawals and one-time debit card transactions. The proposal provides two alternatives for implementing the consumer's choice for both of the opt-out and opt-in approaches. Under one alternative, the proposal would require an institution to provide an account that has the same terms, conditions, or features that are provided for consumers who do not opt out, except for features that limit the institution's payment of such overdrafts. Under another alternative, the proposal would allow institutions to vary the terms, conditions, or features for the account that does not permit the payment of ATM and one-time debit card overdrafts, provided that the differences are not so substantial that they discourage a reasonable consumer from exercising his or her right to opt out of the payment of such overdrafts (or compel a reasonable consumer to opt in).

To facilitate compliance, the proposal provides model forms that institutions may use to satisfy their disclosure obligations. The Board intends to conduct additional consumer testing of the proposed model forms following issuance of this proposal.

#### *Debit Holds*

The Board is also proposing to prohibit institutions from assessing an overdraft fee where the overdraft would not have occurred but for a debit hold placed on funds in an amount that exceeds the actual transaction amount and where the merchant can determine the actual transaction amount within a

short period of time after authorization of the transaction (for example, fuel purchases at a gas station). The prohibition, set forth in proposed § 205.19, would not apply if the institution adopts procedures designed to release the hold within a reasonable period of time.

In light of this proposal, and as discussed elsewhere in today's **Federal Register**, the Board is not taking action on the proposed FTC Act (Regulation AA) amendments regarding debit holds.

### IV. Legal Authority

The Board is issuing the proposed opt-out (and opt-in) and debit hold provisions of this proposal pursuant to its authority under Sections 904(a) and 904(c) of the EFTA (15 U.S.C. 1693b). Section 904(a) of the EFTA authorizes the Board to prescribe regulations necessary to carry out the purposes of the title. The express purposes of the EFTA are to establish "the rights, liabilities, and responsibilities of participants in electronic fund transfer systems" and to provide "individual consumer rights." See EFTA Section 902(b); 15 U.S.C. 1693. In addition, Section 904(c) of the EFTA provides that regulations prescribed by the Board may contain any classifications, differentiations, or other provisions, and may provide for such adjustments or exceptions for any class of electronic fund transfers, that the Board deems necessary or proper to effectuate the purposes of the title, to prevent circumvention or evasion, or to facilitate compliance.

The legislative history of the EFTA makes clear that the Board has broad regulatory authority. The Senate Report states that section 904 of the EFTA "authorizes the Federal Reserve Board to promulgate regulations to carry out the act's purposes" and notes that the Senate Committee on Banking, Housing, and Urban Affairs "regards regulations as essential to the act's effectiveness."<sup>16</sup> According to the Senate Report, such regulations "will add flexibility to the act by permitting the Board 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."<sup>17</sup> The Senate Report states that the intent was to give the Board "flexibility in determining whether new or developing electronic services should be covered by

<sup>16</sup> S. Rep. No. 95-1273, 95th Cong., 2d Sess., at 26 (Oct. 4, 1978).

<sup>17</sup> S. Rep. No. 95-1273, at 26.

<sup>15</sup> See *Review and Testing of Overdraft Notices*, Macro International, December 8, 2008.

the act and, if so, to what extent.”<sup>18</sup> “This delegation of authority to the Board is an important aspect of this legislation as it would enable the Board to examine new services on a case-by-case basis and would contribute substantially to the act’s overall effectiveness.”<sup>19</sup>

The proposed opt-out (and opt-in) rules are intended to carry out the express purposes of the EFTA by: (a) Establishing notice requirements to help consumers better understand the cost of overdraft services for certain EFTs; and (b) providing consumers with a choice as to whether they want overdraft services for ATM withdrawals and one-time debit card transactions in light of the costs associated with those services. The proposed opt-out (and opt-in) rules include provisions designed to prevent circumvention or evasion of the requirement to provide the consumer with choice regarding these overdraft services. These rules also include provisions, including exceptions, designed to facilitate compliance by financial institutions in light of certain operational constraints.

The proposed debit hold rule is intended to carry out the express purposes of the EFTA by ensuring that consumers generally are not assessed fees for overdrafts that would not have occurred but for the placement of the hold. The proposed debit hold rule contains classifications, differentiations, and other provisions, including adjustments and exceptions, designed to facilitate compliance by financial institutions in light of certain operational constraints.

The proposed disclosures that would implement the proposed opt-out (and opt-in) requirements are issued pursuant to the Board’s authority under Sections 904, 905 and 906(b) of the EFTA. 15 U.S.C. 1693b, 1693c and 1693d(c).

## V. Section-by-Section Analysis

### *Section 205.12 Relation to Other Laws*

Section 205.12(a) explains the relationship between Regulation E and Regulation Z when an access device permits a consumer to obtain an extension of credit incident to an EFT. In general, Regulation E governs the issuance of access devices and the addition of an EFT service to an accepted credit card, and Regulation Z governs the issuance of a combined credit card and access device and the addition of a credit feature to an accepted credit card. *See* § 205.12(a).

The proposal would amend Regulation E to clarify that both the issuance of an access device with an overdraft service and the addition of an overdraft service to an accepted access device are governed by Regulation E.

Currently, § 205.12(a)(1)(ii) states that the EFTA and Regulation E govern the “issuance of an access device that permits credit extensions (under a preexisting agreement between a consumer and a financial institution) only when the consumer’s account is overdrawn or to maintain a specified minimum balance in the consumer’s account.” As the Board stated in the original March 1979 final rule, this provision was intended to clarify that Regulation E, rather than Regulation Z, applies to the issuance of “access devices that are also credit cards solely by virtue of their capacity to access an existing overdraft credit line attached to the consumer’s account.” 61 FR 18468, 18472, March 28, 1979 (adopting § 205.4(c) where this provision originally appeared).

When the rule was originally adopted, the primary means of covering overdrafts incurred in connection with EFTs was through an overdraft line of credit linked to a debit card or other access device. Today, however, consumers are more likely to have these overdrafts covered by their institution’s overdraft service, rather than by a separate overdraft line of credit. In both cases, the Board believes that Regulation E should apply to ensure consistent treatment.

Accordingly, the Board is proposing to amend § 205.12(a)(1)(ii) to provide that Regulation E governs the issuance of an access device that permits extensions of funds under an overdraft service (as defined below under proposed § 205.17) when the consumer’s account is overdrawn. Proposed § 205.12(a)(1)(iii) provides that Regulation E also covers the addition of an overdraft service to a previously accepted access device. *See* also comment 12(a)–2, as proposed to be revised. Proposed comment 12(a)–3 clarifies that the addition of an overdraft service to an accepted access device does not constitute the addition of a credit feature under Regulation Z.

In addition, the Board is also proposing to amend § 205.12(a)(1)(i) to conform the regulation to reflect the redesignation of the definition of the term “accepted credit card” under Regulation Z, adopted elsewhere in today’s **Federal Register**. *See* 12 CFR 226.12, comment 2. Current § 205.12(a)(1)(iii), which provides that Regulation E’s liability limits and error resolution rules also apply to extensions

of credit under an overdraft line of credit, would be redesignated as § 205.12(a)(1)(iv) and revised to include a reference to overdraft services.

### *Section 205.17 Requirements for Overdraft Services*

#### Background

In the February 2005 Joint Guidance on overdraft protection services, the federal banking agencies recommended as a best practice that institutions obtain a consumer’s affirmative consent to receive overdraft protection. Alternatively, the Joint Guidance stated that where overdraft protection is automatically provided, institutions should provide consumers the opportunity to “opt out” of the overdraft program and provide consumers with a clear disclosure of this option. 70 FR at 9132.<sup>20</sup>

Although it appears that most institutions provide consumers the right to opt out of overdraft services, this practice is not uniform across all institutions.<sup>21</sup> Moreover, even where an opt-out right is provided, this right may not be clearly disclosed to consumers. For example, some institutions may disclose the opt-out right in a clause in their deposit agreement, which many consumers may not notice or may not consider relevant because they do not expect to overdraw their accounts. In other cases, the clause may not be written in clearly understandable language. Accordingly, to ensure that all consumers are given a meaningful choice regarding overdraft services, the May 2008 FTC Act Proposal would have established notice and opt-out requirements for institutions providing such services. The content and format of the opt-out notice were set forth in the Board’s Regulation DD Proposal.

#### Discussion

Based on the comments received in response to the May 2008 FTC Act and Regulation DD Proposals, the results of limited consumer testing, and its own analysis, the Board believes that concerns about overdraft services can be appropriately addressed under its rulemaking authority under the EFTA

<sup>20</sup> The OTS made similar recommendations in its separate guidance. *See* 70 FR at 8431.

<sup>21</sup> According to the FDIC’s Study of Bank Overdraft Programs, 75.1% of institutions surveyed permit consumers to opt out of their automated overdraft program, while 11.1% of institutions require consumers to opt in. According to the FDIC, banks that do not promote automated programs were less likely to give consumers either the option to opt in or to opt out of the automated overdraft program. *See FDIC Study at 27. See also MoebS 2008 Pricing Survey Press Release* (reporting that 89.9% of institutions offer some form of a consumer opt-out).

<sup>18</sup> S. Rep. No. 95–1273, at 25.

<sup>19</sup> S. Rep. No. 95–1273, at 26.

and Regulation E. The Board has a number of reasons for reaching this conclusion.

First, the Board has considered the benefits to consumers of covering check transactions under an overdraft service. In particular, while a consumer will generally be charged the same fee by the financial institution whether or not a check is paid, if the institution covers an overdrawn check, the consumer may avoid other adverse consequences, such as the imposition of additional merchant returned item fees.<sup>22</sup> Such benefits are not evident, however, with regard to the payment of overdrafts for certain types of EFTs, specifically ATM withdrawals and one-time debit card transactions. For those types of transactions, if the transaction is declined because of insufficient funds in the consumer's account, the consumer would not incur any merchant returned item fees and typically would avoid any fees assessed by the financial institution. Accordingly, the Board believes it is unnecessary to apply an opt-out (or opt-in) rule to check transactions in the proposed rule and that a more targeted rule covering overdraft services is appropriate.

Second, the Board has considered the cost impact to consumers from overdraft fees assessed in connection with ATM and debit card overdrafts.<sup>23</sup> For one-time debit card transactions in particular, the amount of the fee assessed may substantially exceed the amount overdrawn.<sup>24</sup> Given the costs

<sup>22</sup> According to one survey, the average merchant fee for a returned check is \$27.78. See *Moeb's 2008 Pricing Survey Press Release*. See also *FDIC Study* at 16 n.18 (stating that the fee amounts for paying an overdraft and for returning an item unpaid were the same for 98.1 of the surveyed institutions operating automated overdraft programs that reported the two fees).

<sup>23</sup> According to the FDIC's Study of Bank Overdraft Programs, the median dollar amount for debit card transactions resulting in an overdraft is \$20. The FDIC's study also reported that POS/debit overdraft transactions accounted for the largest share of all insufficient funds transactions (41.0%). See *FDIC Study* at 78–79. This compares to the average cost of overdraft and insufficient funds fees of over \$26 per item in 2007, as reported by the GAO. See *Bank Fees: Federal Banking Regulators Could Better Ensure That Consumers Have Required Disclosure Documents Prior to Opening Checking or Savings Accounts*, GAO Report 08–281, at 14 (January 2008). See also *FDIC Study* at 15, 18 (reporting a median per item overdraft fee of \$27 for banks surveyed); Eric Halperin, Lisa James and Peter Smith, *Debit Card Danger: Banks Offer Little Warning and Few Choices as Customers Pay a High Price for Debit Card Overdrafts*, Ctr. for Responsible Lending at 8 (January 25, 2007) (estimating that the median amount by which a consumer overdraws his or her account for a debit card purchase is \$17).

<sup>24</sup> See *Overdraft Protection Hearing* at 72 (stating that consumers pay \$1.94 in fees for every one dollar borrowed to cover a debit card POS overdraft).

associated with overdraft services in these circumstances, consumers may prefer not to have these overdrafts paid. In the Board's limited consumer testing, some participants stated that they would prefer to have ATM withdrawals and debit card transactions declined if they had insufficient funds, rather than incur an overdraft fee.

Third, the Board notes that addressing overdrafts under its authority under the EFTA and Regulation E would ensure that if finalized, the rule would apply to all depository institutions, including state-chartered credit unions which would not have been covered by the NCUA's FTC Act authority.

Thus, for the reasons discussed above, the Board is proposing to prohibit account-holding financial institutions from assessing overdraft fees or charges on a consumer's account for paying an overdraft on an ATM withdrawal or one-time debit card transaction (whether at POS, online or by telephone), unless the consumer is given notice and a reasonable opportunity to opt out of the institution's overdraft service in connection with those transactions, and the consumer does not opt out. As discussed below, the Board is also proposing an alternative approach that would prohibit an account-holding financial institution from assessing any fees on a consumer's account for paying an ATM withdrawal or one-time debit card transaction that overdraws the account, unless the consumer opts in, or affirmatively consents, to the service.

#### 1. First Alternative Approach—Opt-Out Requirement

##### A. Definition—§ 205.17(a)

Proposed § 205.17(a) 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. The term is intended to cover circumstances when an institution assesses a fee for paying an overdraft pursuant to any automated program or service, whether promoted or not, or as a non-automated, ad hoc accommodation. The term does not include an institution's payment of overdrafts pursuant to a line of credit subject to the Board's Regulation Z, including transfers from a credit card account, a home equity line of credit, or an overdraft line of credit. The term also does not include any overdrafts paid pursuant to a service that transfers funds from another account of the

consumer (including any account that may be jointly held by the consumer and another person) held at the institution. The Board is not proposing to include these methods of covering overdrafts under this proposal because they require the express agreement of the consumer.

##### B. Opt-Out Requirement—§ 205.17(b)

*General rule and scope of opt-out.* Proposed § 205.17(b)(1) sets forth the general rule prohibiting an account-holding institution from assessing a fee or charge on a consumer's account for paying an overdraft on an ATM withdrawal or a one-time debit card transaction pursuant to the institution's overdraft service, unless the consumer is given notice and a reasonable opportunity to opt out of the service, and the consumer does not opt out.<sup>25</sup> The proposed opt-out would apply to any ATM withdrawal, including withdrawals made at proprietary or foreign ATMs. The proposed opt-out would also apply to any one-time debit card transaction, regardless of whether the consumer uses a debit card at a point-of-sale (for example, at a merchant or a store), in an online transaction, or in a telephone transaction.

Proposed comment 17(b)–1 clarifies that a consumer's election to opt out of a financial institution's overdraft service does not prohibit the institution from paying any overdrafts for ATM withdrawals or one-time debit card transactions. If the institution pays an overdraft for these transactions, however, it would generally be prohibited from assessing an overdraft fee or charge, except as permitted under the exceptions set forth in proposed § 205.17(b)(5), discussed below. The rule would not, however, limit the institution's ability to debit the consumer's account for the amount of the overdraft, if the institution is permitted to do so under applicable law.

The proposed opt-out would not apply to other types of transactions, including check transactions and preauthorized EFTs.<sup>26</sup> As discussed above with respect to checks, the payment of overdrafts for these transactions may enable consumers to avoid other possible adverse consequences that might result if such items are returned unpaid, such as merchant returned item fees. Consumers may also be more likely to use checks

<sup>25</sup> As further discussed below under proposed § 205.17(c), notice must be provided both before the institution's assessment of any fees or charges for paying an overdraft, and subsequently after the consumer has incurred any such fees or charges.

<sup>26</sup> The EFTA and Regulation E generally do not apply to check transactions. See § 205.3(c).

and preauthorized EFTs to pay for significant household expenses, such as utilities and rent. In the Board's limited consumer testing, participants indicated that they were more likely to pay important bills using checks and preauthorized EFTs, and to use debit cards for their discretionary purchases.

The opt-out also generally would not apply to ACH transactions. For example, if the consumer provides his or her checking account number to authorize an ACH transfer online or by telephone, the institution would be permitted to pay the item if it overdraws the consumer's account and assess a fee for doing so. The Board notes that in many cases, ACH transactions serve as a replacement for check transactions, such as where a check is converted to a one-time ACH debit to the consumer's account.<sup>27</sup> In addition, the payment of an overdraft for an ACH transaction could enable consumers to avoid merchant returned item fees.

*Operational considerations.* As discussed above, the May 2008 FTC Act Proposal would have required institutions to offer consumers the option of opting out of the payment of overdrafts only for ATM withdrawals and POS debit card transactions in addition to the option to opt out of the payment of overdrafts for all transaction types. In response, industry commenters stated that many processors do not currently have systems set up to distinguish paying overdrafts for some, but not all, payment channels, and that the reprogramming costs would be significant. Specifically, industry commenters stated that most systems today could either pay overdrafts for all transaction types or pay overdrafts for none; however, these systems were not set up to pay overdrafts for certain transaction types (e.g., checks and ACH), but not others (e.g., ATM and POS debit card transactions). Some industry commenters also asserted that most systems today are unable to readily differentiate between POS debit card transactions and other types of debit card transactions, such as a preauthorized transfer. A few industry commenters, however, argued that any opt-out right should be limited to ATM withdrawals and POS debit card transactions because the majority of complaints about overdraft services arise in connection with these transactions.

Notwithstanding the programming changes that would be required by the

proposed rule, the benefits of enabling consumers to have a choice regarding the payment of overdrafts for ATM withdrawals and one-time debit card transactions may outweigh the associated reprogramming costs. From a consumer's perspective, any benefits from overdrawing the consumer's account for ATM withdrawals and one-time debit card transactions may be substantially outweighed by the costs associated with the overdraft. Unlike for check and ACH transactions where the consumer could be assessed fees by both the institution and the merchant or other payee, the consequence of not having overdraft services for ATM and one-time debit card transactions is to have a transaction denied with no fees assessed. If a one-time debit card transaction is denied, the consumer can provide another form of payment, such as cash or a credit card. For ATM transactions, consumers may reasonably expect that their withdrawal request will be denied if they do not have sufficient funds in their accounts.

For these reasons, the Board is proposing to limit the scope of the opt-out to ATM withdrawals and one-time debit card transactions. To minimize the cost impact on institutions, however, the Board anticipates allowing substantial lead time for institutions to implement the necessary programming changes. Comment is requested on whether the proposed opt-out should also apply to recurring debit card transactions and ACH transactions. Comment is also solicited on an appropriate implementation period for the proposed rule.

*Reasonable opportunity for opt-out.* Proposed § 205.17(b)(1)(ii) provides that once a consumer has received an opt-out notice, the consumer must be given a reasonable opportunity to opt out of an institution's overdraft service for ATM withdrawals and one-time debit card transactions. Proposed comment 17(b)-2 provides examples to illustrate what would constitute a reasonable opportunity to opt out, including reasonable methods for opting out.

The first three examples provide a generally applicable safe harbor for opt-out periods of 30 days after the consumer is provided an initial notice informing the consumer of the opt-out right. During this period, an institution generally would be prohibited from assessing any fees or charges for paying an overdraft for an ATM withdrawal or a one-time debit card transaction. Although 30 days would be a safe harbor, an institution may decide that a shorter waiting period could be adequate depending on the circumstances. Comment is requested

regarding whether a shorter time frame, such as 15 or 20 days, may be more appropriate.

Proposed comment 17(b)-2.i contains an example of a reasonable method of opting out when the institution provides a written form that the consumer can fill out and mail to opt out. See proposed Model Form A-9(A) in Appendix A, discussed below. Proposed comment 17(b)-2.ii provides that an institution could also provide a toll-free telephone number that the consumer may call to exercise the opt-out. Proposed comment 17(b)-2.iii provides that an institution may provide an electronic means to opt out, such as a form that can be accessed and processed at an Internet Web site, provided that the institution directs the consumer to the specific Web site address where the form may be located, rather than solely referring to the institution's home page.

The fourth example provides that an institution may provide an opt-out notice prior to or at account-opening and require the consumer to decide whether to opt out as a necessary step to opening the account. See proposed comment 17(b)-2.iv. For operational reasons, an institution may not want to set up an account for the consumer with overdraft services, only to have to implement a consumer's opt-out a short time later when the consumer opts out within 30 days after receiving an initial opt-out notice.

Comment is requested whether the Board should require institutions to provide a toll-free telephone number to ensure that consumers can easily opt out. Participants in the Board's consumer testing indicated that even if the institution provided a form with a check-off box for the consumer's convenience, participants would still prefer to call their institution to opt out. Comment is also requested regarding whether the Board should add examples of methods of opting out that would not satisfy the requirement to provide a reasonable opportunity to opt out, such as requiring the consumer to write a letter to opt out.

*Conditioning the opt-out.* Proposed § 205.17(b)(2) provides that a financial institution shall not condition a consumer's right to opt out of the institution's payment of ATM withdrawals and one-time debit card transactions pursuant to the institution's overdraft service on the consumer also opting out of the institution's overdraft service with respect to checks, ACH transactions or other types of transactions (such as preauthorized EFTs). The Board is concerned that consumers may be discouraged from exercising their opt-out rights with

<sup>27</sup> See Geoffrey Gerdes, "Recent Payment Trends in the United States," *Federal Reserve Bulletin* at A79 (October 2008) (noting that the number of checks converted to electronic payments in 2006 was 2.6 billion up from 0.3 billion in 2003).

respect to the institution's payment of ATM and debit card overdrafts if the consumer's opt-out choice would also preclude the consumer from having overdrafts paid for checks, ACH transactions, and other types of transactions.<sup>28</sup>

To prevent circumvention of the opt-out right, the proposed rule also would prohibit an institution from declining to pay checks, ACH transactions, or other types of transactions that overdraw the consumer's account because the consumer has opted out of the institution's overdraft service for ATM and one-time debit card transactions. Although the payment of overdrafts is generally at the discretion of the institution, the Board is concerned that some institutions may exercise that discretion in a manner that effectively prevents consumers from exercising a meaningful choice regarding overdraft services. Thus, the proposed rule generally would require an institution to apply the same criteria for deciding whether to pay overdrafts on checks, ACH transactions, or other types of transactions regardless of the consumer's opt-out choice with respect to ATM and one-time debit card overdrafts. For example, if an institution's internal criteria would lead the institution to pay a check overdraft if the consumer had not opted out of the institution's overdraft service, it must also apply that same criteria in a consistent manner in determining to pay the check overdraft if the consumer has opted out.

This provision is not intended to create a contractual requirement for the institution to pay overdrafts on checks, ACH transactions, or other types of transactions. Comment is requested on whether there are other, more effective means of ensuring that consumers are not discouraged from opting out of an institution's overdraft service for ATM withdrawals and one-time debit card transactions.

Notwithstanding the Board's concerns about potential chilling effects, the Board is also proposing a modified version of proposed § 205.17(b)(2) that would expressly permit institutions to condition the consumer's ability to opt out of an institution's overdraft service for ATM withdrawals and one-time

<sup>28</sup> In the Board's limited consumer testing, participants indicated that they would likely not opt out if checks and preauthorized EFTs would be returned because they used these methods of payment to pay important household bills, such as rent and utilities. In contrast, several participants stated that they would prefer that their institution decline their ATM withdrawals and one-time debit card transactions if they did not have sufficient funds in their accounts in order to avoid overdraft fees.

debit card transactions on the consumer also opting out of the institution's overdraft service for checks and other transaction types. Under this alternative approach, an institution could also decline checks, ACH transactions, and other types of transactions because the consumer has opted out of the service for ATM withdrawals and one-time debit card transactions. This alternative would address the potential operational issues associated with implementing a partial opt-out rule.

The Board solicits comment on the merits of both alternatives. The Board also seeks comment on other approaches that may sufficiently balance concerns about the potential chilling effects from institutions declining to pay overdrafts for checks and other transactions if a consumer opts out of the payment of overdrafts for ATM withdrawals and one-time debit card transactions against the operational difficulties of implementing a partial opt-out rule.

*Implementation of opt-out.* Some institutions may choose to implement a consumer's decision to opt out at the account level and decline to pay overdrafts for ATM withdrawals and one-time debit card transactions for those consumers that have opted out. Other institutions for operational reasons may prefer to implement the consumer's choice at the product level and offer two different accounts, one account that allows the institution to pay overdrafts for ATM withdrawals and one-time debit card transactions, and another that is specifically designed for consumers who opt out ("opt-out" account). Proposed § 205.17(b)(3) is intended to provide operational flexibility to financial institutions to implement an opt-out using either approach.

This provision would not, however, permit an institution to discourage, or chill, a reasonable consumer's exercise of the right to opt out. The Board is concerned that institutions may circumvent the proposed opt-out requirement and discourage consumers from opting out by, for example, imposing higher fees, paying lower interest rates, or limiting the features of the opt-out account. Thus, the proposal sets forth two alternative approaches to address this concern.

Under the first alternative, if the institution is providing an opt-out account that does not permit the payment of ATM and one-time debit card overdrafts, the account must have the same terms, conditions, and features, including interest rates paid and fees assessed, as an account that permits the payment of such overdrafts,

except for features that limit the institution's payment of such overdrafts.<sup>29</sup>

Under the second alternative, an institution may alter some of the terms, conditions, or features of an account that does not permit the payment of overdrafts on ATM withdrawals and one-time debit card transactions. For example, the institution may wish to price some account services differently for the opt-out account. In light of the Board's concern about possible chilling effects, however, the second alternative permits an institution to vary the terms, conditions, or features of the opt-out account, provided that the differences in the terms, conditions, or features are not so substantial that they would discourage a reasonable consumer from exercising his or her right to opt out of the payment of overdrafts on ATM withdrawals and one-time debit card transactions.<sup>30</sup> For example, an institution may not decline to provide ATM and debit card services altogether because the consumer has opted out of the institution's overdraft service for ATM withdrawals and one-time debit card transactions. See proposed comment 17(b)(3)-1 to this second alternative.

The Board requests comment on both approaches. Specifically, the Board requests comment on whether institutions that currently offer an opt-out implement an opt-out at the account level (*i.e.*, within the same type of account) or at the product level (*i.e.*, by placing the consumer in a separate opt-out account). The Board also requests comment on whether institutions that currently offer an opt-out vary any other terms, conditions, or features of a separate opt-out account, and if so, which terms, conditions, or features are varied and why.

*Exceptions to the notice and opt-out requirements.* In response to the May 2008 FTC Act Proposal, several commenters urged the Agencies to exclude institutions that require consumers to opt into the institution's overdraft service from the requirement to provide opt-out notices to consumers. These commenters stated that the Agencies' proposed rule would impose

<sup>29</sup> As discussed in proposed comment 17(b)-1, a consumer's election to opt out of an institution's overdraft service for ATM and one-time debit card transactions does not prohibit the institution from paying overdrafts in such cases. However, the institution generally would not be permitted to assess a fee or charge for paying the overdraft.

<sup>30</sup> An institution that varies a term, condition, or feature of an account if a consumer opts out of the institution's overdraft service would have to comply with the change-in-terms notice requirements in § 205.8 and 12 CFR 230.5, as applicable.

unnecessary costs on such institutions. Moreover, these commenters stated that consumers would likely be confused by notices informing them of their right to opt out of a service that they have affirmatively requested.

In addition, some institutions may have a policy and practice of declining any ATM withdrawals or debit card transactions when the institution has a reasonable belief that the consumer does not have sufficient funds available in his or her account to cover the requested transaction at the time of authorization. An opt-out requirement would serve little purpose in these circumstances, and could lead to potential consumer confusion.

The Board is proposing to create exceptions to the notice and opt-out requirements in the circumstances described above. Proposed § 205.17(b)(4) contains the two proposed exceptions. First, institutions that have a policy and practice of declining to pay ATM withdrawals or one-time debit card transactions for which authorization is requested if the institution has a reasonable belief that the consumer does not have sufficient funds available to cover the transaction at the time of the authorization request would not have to provide consumers with notice and the right to opt out of overdraft services. Second, institutions that require the consumer's affirmative consent, or opt-in, before assessing any fees or charges for paying an ATM or one-time debit card overdraft also would not be subject to § 205.17.<sup>31</sup>

Proposed comment 17(b)(4)-1 states that institutions that qualify for either of the exceptions in § 205.17(b)(4) would not be required to provide consumers notice and a reasonable opportunity to opt out of the institution's payment of overdrafts for ATM withdrawals and one-time debit card transactions. Proposed comment 17(b)(4)-2 clarifies that an institution is not required to obtain the consumer's affirmative consent prior to each transaction that may overdraw the consumer's account to qualify for the opt-in exception in § 205.17(b)(4)(ii).

*Exceptions allowing assessment of overdraft fees when a consumer opts out.* In limited circumstances, an institution may be unable to avoid paying a transaction that would overdraw a consumer's account. The proposal sets forth two exceptions that would permit an institution to assess a fee or charge to a consumer's account

for paying an overdraft for an ATM withdrawal or one-time debit card transaction, even if the consumer has opted out of the institution's overdraft service.

*FTC Act Proposal.* The May 2008 FTC Act Proposal would have permitted fees to be charged for an overdraft in two circumstances, notwithstanding the consumer's decision to opt out. The first circumstance was where the purchase amount presented at settlement by a merchant for a debit card transaction exceeded the amount originally requested for pre-authorization. The second circumstance was where a merchant or other payee presented a debit card transaction for payment by paper-based means, rather than electronically using a card terminal, and where the payee did not obtain authorization from the card-issuing financial institution at the time of the transaction.

In the supplementary information accompanying the May 2008 FTC Act Proposal, the Agencies stated that they had considered, but did not propose, an exception that would allow an institution to impose an overdraft fee despite a consumer's opt-out election as long as the institution did not "knowingly" authorize a transaction that resulted in an overdraft. The Agencies expressed concern that given the difficulty in determining a consumer's real-time account balance, such an exception could undercut the protections provided by a consumer's election to opt out. Nonetheless, the Agencies sought comment on other circumstances in which an exception may be appropriate to allow an institution to impose a fee or charge for paying an overdraft even if the consumer has opted out of the institution's overdraft service.

Industry commenters urged the Board to consider additional exceptions. Some industry commenters urged the Board to adopt a broad principles-based exception allowing fees to be charged when overdrafts are paid despite a consumer's decision to opt out. These commenters suggested the following principles-based exceptions: if an institution does not "knowingly" authorize the transaction that would overdraw the consumer's account; or if the institution authorizes a transaction on the "good faith belief" that there are sufficient funds in the consumer's account.

Other industry commenters listed specific exceptions that the Agencies should consider. Several commenters urged the Agencies to allow fees to be assessed if an overdraft was paid when the institution used a stand-in processor

to authorize the transaction because the card network was temporarily off-line. Industry commenters also stated that the rule should permit fees to be assessed for "force-post" or "must pay" debit card transactions where an institution authorizes payment at the time of the transaction based on a determination that the consumer had sufficient funds. Under these circumstances, card network rules require institutions to honor or pay the transaction even if intervening transactions (for example, checks that are presented for payment or ATM withdrawals) causes the consumer to have insufficient funds when the transaction is presented for settlement. In addition, industry commenters supported exceptions permitting fees to be charged where a consumer subsequently has a deposited item returned, and where the transaction is not submitted for authorization by the merchant.

*Reasonable belief exception.* Proposed § 205.17(b)(5)(i) would permit a financial institution to assess an overdraft fee or charge for paying an ATM withdrawal or one-time debit card transaction, notwithstanding the consumer's opt-out, if the institution has a reasonable belief that there are sufficient funds available in the consumer's account at the time the institution authorizes the transaction. Thus, an institution could assess an overdraft fee if the institution has authorized a transaction on the reasonable belief that there were sufficient funds available to cover the transaction, but sufficient funds were not, in fact, available at settlement.

This could occur, for instance, where an authorization balance is not updated in real-time. For example, some institutions use a daily batch balance method for authorizing transactions and authorization decisions may be based upon a balance which is not updated during the day to reflect other account activity that occurred before the authorization request. In such cases, the institution may authorize a debit card transaction even though prior transactions that have posted or otherwise taken place during the day may cause the consumer's account to have insufficient funds for the debit card transaction. The proposed exception would permit the institution to pay the debit card transaction and assess an overdraft fee on the consumer's account because the institution authorized the transaction on the reasonable belief that there were sufficient available funds in the account to cover the transaction.

An institution could also assess an overdraft fee if it authorizes a

<sup>31</sup> This exception assumes that the Board adopts a rule requiring consumer opt-out, rather than opt-in, as is proposed under the second alternative approach discussed below.

transaction on the reasonable belief that a previously deposited check or other item was deposited on good funds, and the item is subsequently returned, causing the transaction to overdraw the consumer's account. For example, an institution may provide immediate availability for a \$100 check that a consumer has deposited, and subsequently authorize a \$75 debit card transaction on the belief that the check was written on sufficient funds. However, if the check is later returned due to insufficient funds in the check writer's account, the institution could permissibly charge the account of the consumer that had deposited that check if the debit card transaction overdraws the account because of the returned deposit.

The proposed exception would also apply where the settlement amount exceeds the amount submitted for pre-authorization. For example, a consumer may use his or her debit card at a pay-at-the-pump fuel dispenser to purchase \$50 of fuel. At the time of authorization, the gas station may request a pre-authorization hold of \$1 to verify the validity of the card. Assuming the card-issuing financial institution does not increase the amount of the hold, if the consumer has less than \$50 in his or her account when the transaction is presented for settlement, the institution would be permitted to pay the transaction and assess a fee, even if the consumer has opted out of the institution's overdraft service.

Finally, an institution could assess an overdraft fee or charge in connection with force-post, or must-pay, debit card transactions that the institution is required to honor even if, at settlement, intervening transactions by the consumer have reduced the consumer's available balance below the authorized amount of the transaction. For example, a consumer may use his debit card to make a \$50 purchase, which the institution authorizes based on the consumer's available balance at the time of authorization. However, because settlement may not occur for some period of time after completion of the transaction, intervening transactions may post to the consumer's account before the \$50 transaction is presented for settlement. If there are insufficient funds in the consumer's account at the time of settlement, this exception would allow the institution to assess a fee to the consumer's account for paying the overdraft even if the consumer has opted out of the institution's overdraft service. Proposed comment 17(b)(5)-1 sets forth examples illustrating this exception.

The proposed exception in § 205.17(b)(5)(i) is not intended to permit an institution to assess an overdraft fee where a merchant has not submitted the transaction to the institution for authorization. A transaction may not be submitted for authorization, for example, because it is below the floor limits established by card network rules requiring authorization. Similarly, a merchant may decide not to submit the transaction for authorization because the small dollar amount of the transaction does not pose significant payment risk to the merchant. In either case, the consumer's financial institution would be unable to decline the transaction if the consumer did not have sufficient funds in the consumer's account. Nevertheless, the Board believes that institutions should not be permitted to assess a fee on the consumer's account in these cases when the consumer has opted out. From the perspective of a consumer who has opted out, it is reasonable to expect that the transaction would be declined if he or she did not have sufficient funds in the account. The merchant's decision not to seek authorization for small dollar transactions generally is not transparent to the consumer. In addition, because small-dollar transactions are those most frequently not submitted for authorization, prohibiting institutions from assessing overdraft fees in these circumstances would reduce the possibility that the consumer will incur overdraft fees that exceed the amount of the overdraft. An institution may, however, debit the consumer's account for the amount of the overdraft if permitted to do so under applicable law.

Similarly, the proposal would not permit the institution to assess a fee if the institution uses a stand-in processor to authorize the transaction and an overdraft was paid as a result. A stand-in processor may be used by an institution when the debit card network is temporarily unavailable. In such cases, the authorization decision may be made by the processor based on the institution's pre-determined amount, rather than the consumer's account balance. The Board is concerned about the appropriateness of permitting an institution to assess an overdraft fee on the consumer's account in these rare circumstances because a consumer who has opted out would reasonably expect the transaction to be declined if he or she did not have sufficient funds in the account. The institution may, however, debit the consumer's account for the amount of the overdraft if permitted to

do so under applicable law. Proposed comment 17(b)(5)-2 provides examples of circumstances where an institution would not be permitted to assess a fee for paying an overdraft if the consumer has opted out because a transaction was never submitted to the institution for authorization.

*Paper-based debit card transaction exception.* Proposed § 205.17(b)(5)(ii) would permit an institution to assess an overdraft fee or charge, notwithstanding the consumer's opt-out election, where a merchant or other payee presents a debit card transaction for payment by paper-based means, rather than electronically using a card terminal, and the institution has not previously authorized the transaction. For example, the merchant may use a card imprinter to take an imprint of the consumer's card and later submit the sales slip to its acquirer for payment.

The Board believes this circumstance is analogous to a check transaction that is later returned for insufficient funds. In this case, the institution cannot authorize the transaction because of the way in which the transaction is processed. The consumer should be aware that the merchant is not obtaining authorization from the financial institution when the merchant takes an imprint of the consumer's card. Thus, the consumer could reasonably expect that he or she would be charged a fee if there are not sufficient available funds to pay for the transaction. In contrast, where a merchant swipes a consumer's card to capture the card information, but chooses not to submit the transaction for authorization, the merchant's decision not to seek authorization is not transparent to the consumer. Therefore, in the latter circumstance, the consumer may reasonably expect that if he or she did not have sufficient funds in his or her account that the transaction would be declined. Proposed comment 17(b)(5)-3 illustrates this exception.

#### C. Timing—§ 205.17(c)

The May 2008 FTC Act and Regulation DD Proposals would have required institutions to provide notice of the opt-out both before the institution's assessment of any fees or charges for paying an overdraft, and subsequently after the consumer has incurred any such fees or charges. The subsequent notice could be given on each periodic statement reflecting any fees or charges imposed in connection with an overdraft service, or at least once per statement cycle on any notice sent promptly after the institution's payment of an overdraft under an overdraft service. Proposed § 205.17(c)

sets forth essentially the same requirements under Regulation E.

In response to the May 2008 FTC Act and Regulation DD Proposals, the majority of industry commenters stated that the rule should only require notices to be provided at account opening. These commenters argued that the subsequent notice requirement would impose unnecessary costs on institutions based on the expense of producing and mailing the additional notices. In the alternative, industry commenters recommended that the Board permit institutions to provide a shorter opt-out notice on periodic statements to limit statement costs.

Consumer groups urged the Board to require institutions to provide initial opt-out notices at account opening, segregated from other account documents, to ensure that the notice would be noticeable. In addition, consumer groups urged the Board to require institutions to provide subsequent notice of the opt-out right both on the periodic statement as well as on any notices the institution may send immediately after an overdraft so that if the consumer failed to read the opt-out language on the notice sent after an overdraft, it would also appear on the periodic statement.

Proposed § 205.17(c)(1) would require an institution to provide an opt-out notice before the institution assesses a fee or charge for paying an ATM withdrawal or one-time debit card transaction pursuant to the institution's overdraft service for accounts opened after the effective date of the final rule. For example, notice may be given at account opening, either within the deposit account agreement or in a stand-alone document. Institutions may also choose to provide the opt-out notice closer to the time the overdraft service is available, so long as the notice is provided before the institution assesses any fees or charges for paying an ATM withdrawal or one-time debit card transaction that overdraws the consumer's account. Proposed § 205.17(c)(1) also provides that the consumer must be given a reasonable opportunity to exercise the opt-out right after receiving the notice before such fees or charges may be assessed to the consumer's account. *See* proposed comment 17(b)-2 (providing that a consumer has a reasonable opportunity to opt out if the consumer is given 30 days after receiving an opt-out notice before an overdraft fee is assessed). Comment is requested whether institutions should be required to segregate the opt-out notice from other account disclosures to help ensure that the notice can be seen by the consumer.

Under the proposal, initial opt-out notices would not have to be provided to accounts that are opened prior to the effective date of the final rule. In response to the May 2008 Regulation DD proposal, consumer groups urged the Board to require institutions to provide initial opt-out notices to existing accountholders. The Board is concerned, however, that the costs of mailing initial opt-out notices to the millions of existing accountholders may exceed any consumer benefit. As further discussed below, existing consumers will still be alerted to their right to opt out of the overdraft service because they will receive an opt-out notice if and when they are assessed a fee or charge by their financial institution for paying an ATM or debit card overdraft.

If a consumer has not opted out (in the case of a joint account, where no joint account holder has opted out) or the consumer has revoked a prior opt-out election, proposed § 205.17(c)(2) would require institutions to provide an opt-out notice following the assessment of any overdraft fees or charges for paying an ATM withdrawal or one-time debit card transaction. The subsequent notice requirement would apply to all accounts, including existing accounts as of the effective date of the final rule.

The requirement to provide an opt-out notice following the assessment of an overdraft fee or charge is designed to ensure that consumers are given notice of their right to opt out at a time that may be most relevant to them, that is, after they have been assessed fees or other charges for the service. Consumers receiving an opt-out notice only at account opening may not focus on the significance of the information at that time because they may assume that they will not overdraw the account. Or, consumers may not notice the opt-out information provided with other account-opening documents.

Under the proposal, institutions would have the option of placing an opt-out notice on the periodic statement reflecting an overdraft fee or charge assessed to the consumer's account or on any notice sent promptly after the ATM or debit card overdraft. If the subsequent notice is included on the periodic statement, proposed § 205.17(c)(2)(i) would require the notice to be placed in close proximity to any aggregate totals for overdraft and returned item fees required to be disclosed by 12 CFR 230.11(a), as adopted under the Board's final rules under Regulation DD, published elsewhere in today's **Federal Register**. During consumer testing, a version of the opt-out form was placed directly below the cost totals associated with

overdrawing the account. This placement enabled consumers to easily notice the information about their opt-out right.

The requirement to provide subsequent notice of the opt-out terminates once the consumer has opted out. That is, once the consumer has opted out, an institution need not provide notice of the opt-out right following the assessment of any overdraft fees or charges to the consumer's account (for example, under one of the exceptions in § 205.17(b)(5)). Of course, if the consumer opts out after having incurred an overdraft fee, the opt-out applies only to subsequent transactions and the institution could permissibly assess an overdraft fee without violating the general rule in § 205.17(b). Similarly, if the consumer has opted out but incurs an overdraft before the opt-out has been implemented, the institution would be permitted to assess a fee for paying the overdraft. *See also* proposed comment 17(g)-1 (stating that a consumer's subsequent opt-out does not require the institution to waive or reverse any overdraft fees assessed to the consumer's account prior to the institution's implementation of the opt-out).

Comment is requested as to whether the rule should permit institutions to include the opt-out notice on periodic statements in any cycle in which the consumer has been assessed an overdraft fee or charge, even if that fee or charge was not incurred in connection with an ATM withdrawal or a one-time debit card transaction. For example, the rule could permit institutions to provide an opt-out notice on a periodic statement if the consumer incurred an overdraft fee in connection with a check transaction. Comment is also requested as to whether institutions should be permitted to include the opt-out notice on the periodic statement if the consumer did not incur any overdraft fees or charges during the statement cycle. Prohibiting institutions from including the opt-out notice on each periodic statement where no fee has been assessed could impose additional costs on institutions because it would require a dynamic statement process that only permits the opt-out notice to appear on statements that reflect an overdraft fee. The Board is concerned, however, that consumers may dismiss the opt-out notice as boilerplate language if the opt-out notice were included on every periodic statement.

Proposed comment 17(c)(1)-1 contains guidance regarding the applicability of the notice requirements

in § 205.17(c) to existing consumers. As discussed above, the requirement to provide notice before overdraft fees are assessed would apply only to accounts opened on or after the effective date of the final rule, that is, on or after the mandatory compliance date. However, the requirement to provide subsequent notice of the opt-out right after the consumer has overdrawn the account and assessed a fee or charge on the account would apply to all accounts on or after the effective date of the final rule, including existing accounts.

#### D. Content and Format—§ 205.17(d)

Proposed § 205.17(d) specifies the information that an institution would be required to include in its opt-out notices. In general, the proposal includes information similar to what would have been required under the May 2008 Regulation DD proposal, with certain revisions to reflect industry and consumer group comments, as well as the Board's consumer testing.

Two different notices are set forth in the proposal. First, the proposal contains a detailed notice about the institution's overdraft service and the consumer's opt-out right that would be provided before an institution can assess any fees or charges for paying an ATM or one-time debit card transaction that overdraws the consumer's account. Second, the proposal includes a shorter notice which could be provided to the consumer after an overdraft fee has been assessed (for example, on a periodic statement) that generally informs the consumer of his or her opt-out right and instructs the consumer to contact the institution for more information.<sup>32</sup> Model forms that institutions may use to comply with the rule are also included in this proposal. See proposed Model Forms A-9(A) and A-9(B) in Appendix A.

**Initial notice content.** Proposed § 205.17(d)(1) sets forth the information that must be included in the initial opt-out notice provided to consumers before an institution may assess any fees or charges for paying an overdraft. Proposed § 205.17(d)(1) would also require that the initial opt-out notice be in a form substantially similar to Model Form A-9(A) in Appendix A.

Proposed § 205.17(d)(1)(i) would require the institution to provide a general description of the financial institution's overdraft services and the types of EFTs for which an overdraft fee may be imposed, including ATM

withdrawals and one-time debit card transactions.

Proposed § 205.17(d)(1)(ii) would require the initial notice to include information about the dollar amount of any fees or charges assessed on the consumer's account for paying an ATM withdrawal or a one-time debit card transaction pursuant to the institution's overdraft service. Some institutions may vary the fee amount that may be imposed based upon the number of times the consumer has overdrawn his or her account, the amount of the overdraft, or other factors. Under these circumstances, the institution must disclose the maximum fee that may be imposed or a range of fees. Proposed comment 17(d)(1)-1 provides that the institution may indicate that the consumer may be assessed a fee "up to" the maximum fee or provide the range of fees. Comment is requested whether additional guidance is necessary if an overdraft fee is determined by other means, such as a percentage of the overdraft or the transaction that caused the overdraft.

Proposed § 205.17(d)(1)(iii) would require institutions to disclose any daily dollar limits on the amount of overdraft fees or charges that may be assessed. If the institution does not limit the amount of fees that can be imposed, it must disclose this fact. The May 2008 Regulation DD Proposal contained a similar disclosure, but also would have required institutions to state any dollar limits on the amount of fees that may be imposed in a statement period. Upon further analysis, however, a requirement to state any limits on the amount of fees that may be imposed in a statement cycle is not included in this proposal because the Board believes that this information is unlikely to be relevant or helpful to consumers.

Proposed § 205.17(d)(1)(iv) would require institutions to inform consumers of the right to opt out of the institution's payment of overdrafts for ATM and one-time debit card transactions, including the method(s) that the consumer may use to exercise the opt-out right and how to contact the institution for more information. See also proposed § 205.17(b)(1)(ii); comment 17(b)-2. An institution may also include an explanation regarding the type of transactions that would not be covered by the opt-out. See proposed comment 17(d)(1)-2, discussed below.

Several industry commenters in response to the Regulation DD proposed model forms urged the Board to add language to the forms stating that the payment of overdrafts is discretionary even if the consumer does not opt out. In addition, industry commenters urged

the Board to include language stating that the consumer's decision to opt out would not ensure that overdrafts would not be paid. The proposed model form does not include specific language regarding the discretionary nature of overdraft services. However, institutions would be permitted to include in their opt-out notices language indicating that the payment of overdrafts is at their discretion. See proposed comment 17(d)(1)-2.

Proposed § 205.17(d)(1)(v) provides that institutions must state whether they offer any alternatives for the payment of overdrafts. Specifically, if an institution offers an overdraft line of credit or a service that transfers funds from another account of the consumer held at the institution to cover the overdraft (including an account held jointly with another consumer), the institution must state that fact and how to obtain more information about these alternatives. Institutions may also, but are not required to, list any additional alternatives they may offer to overdraft services. This provision incorporates a recommendation from the February 2005 Joint Guidance that institutions should inform consumers generally of other overdraft services and credit products, if any, that are available when describing an overdraft protection program.<sup>33</sup>

In some cases, these alternatives for paying overdrafts may be less costly than the overdraft service offered by the institution.<sup>34</sup> Consequently, requiring disclosures regarding these alternatives may enable consumers to make an informed decision about the merits of the overdraft service or whether other alternatives would be more appropriate to their needs. Consumer testing indicated that participants found information about alternatives helpful. Participants also generally understood that they would have to qualify for an overdraft line of credit, without a reference in the notice to any qualification requirements.

Some institutions may wish to explain to consumers the consequences of opting out of overdraft services. Proposed comment 17(d)(1)-2 provides that institutions may briefly describe these consequences. For example, the institution may state that if a consumer opts out of the institution's overdraft service for ATM withdrawals and one-time debit card transactions, the

<sup>33</sup> See 70 FR at 9131.

<sup>34</sup> The FDIC Study on Bank Overdraft Programs indicated that the median per usage fee charged by banks for automated overdraft programs was \$27. In contrast, the median per usage fee for linked-account programs and overdraft lines of credit was \$5. FDIC Study at 15, 20 and 23.

<sup>32</sup> Alternatively, after assessing an overdraft fee or charge to the consumer's account, the institution could provide a notice containing the same content as the initial notice.

institution may decline such transactions if the consumer's account does not have sufficient funds. Institutions that include an explanation of the consequences of opting out, the type of transactions that would not be covered by the opt-out, or that the payment of overdrafts is at the institution's discretion, would not violate the requirement that opt-out notices be substantially similar to Model Forms A-9(A) or A-9(B), as applicable. *But see* proposed § 205.17(b)(3) (prohibiting institutions from declining to pay checks, ACH transactions, or other types of transactions that overdraw a consumer's account because the consumer opted out of the institution's overdraft service for ATM withdrawals and one-time debit card transactions). Comment is requested regarding whether the rule should permit or require any other information to be included in the overdraft notice.

*Notice following assessment of overdraft fee.* Proposed § 205.17(d)(2) sets forth the content requirements for the short form notice that institutions may provide to consumers following an institution's assessment of a fee or charge to the consumer's account for paying an ATM withdrawal or one-time debit card transaction pursuant to the institution's overdraft service (assuming that the consumer has not opted out).

The May 2008 Regulation DD Proposal would have required both the initial notice and subsequent notice of the opt-out right to contain the same content. Industry commenters urged that the Board to eliminate the subsequent notice requirement to reduce compliance burdens and costs. Alternatively, industry commenters urged the Board to permit institutions to provide an abbreviated notice on periodic statements that would generally remind consumers of their opt-out right and instruct them to contact the institution for additional information. Consumer group commenters supported the Board's proposal to require the same content on all notices informing consumers of their opt-out right to ensure that consumers can make an informed decision at the time they review the opt-out notice.

Upon further analysis, the Board believes that permitting institutions to provide a short-form opt-out notice may strike an appropriate balance between including sufficient information to inform consumers of their options regarding overdraft services and keeping such notices short, simple, and cost-effective. The Board recognizes that requiring institutions to provide the same amount of detail in the subsequent notice as provided in the initial notice

could impose significant statement production and mailing costs. In addition, participants during consumer testing indicated that it was sufficient for them to receive all of the required information about the institution's overdraft service at account opening. Nevertheless, test participants indicated that it would be helpful to receive a concise reminder of their right to opt out after they were assessed an overdraft fee or charge.

Thus, proposed § 205.17(d)(2) provides institutions with the flexibility to provide either a notice containing the same content as the initial opt-out notice or an abbreviated notice that is substantially similar to Model Form A-9(B) in Appendix A. The proposed abbreviated model notice generally states the consumer's right to opt out, the availability of alternatives to the institution's overdraft service, and how to contact the institution for more information.

*Model forms.* As noted above, proposed § 205.17(d)(1) would require the initial opt-out notice to be substantially similar to Model Form A-9(A) in Appendix A. The model form has been revised from the model form in the May 2008 Regulation DD proposal to reflect the more limited opt-out right and to highlight near the top of the notice key information about the consumer's opt-out right, including the information about alternatives to the institution's overdraft service. To comply with the subsequent notice requirement, proposed § 205.17(d)(2) permits institutions to use a notice substantially similar to proposed Model Form A-9(A) or an abbreviated notice substantially similar to proposed Model Form A-9(B). The Board expects to conduct additional consumer testing of both proposed model forms following issuance of this proposal.

*E. Additional provisions addressing consumer opt-out right—§ 205.17(e)-(h)*

*Joint accounts.* Proposed § 205.17(e) would require a financial institution to treat an opt-out direction by any joint holder of an account as an opt-out for the account from all of the joint consumers. This provision takes into account recognizes the operational difficulties that would otherwise arise if an institution had to determine which account holder was responsible for a particular transaction and then decide whether to authorize that transaction based on that account holder's opt-out choice. Thus, if one joint consumer notifies the institution that he or she wishes to opt out of the institution's overdraft service, the institution must treat the choice as applying to all

overdrafts triggered by an ATM withdrawal or debit card transaction for that account.

*Continuing right to opt-out and time to implement opt-out.* Proposed § 205.17(f) provides that a consumer may opt out of an institution's overdraft service at any time in the manner described in the institution's opt-out notice. Proposed § 205.17(g) provides that institutions must comply with a consumer's opt-out request as soon as reasonably practicable after the institution receives it. Comment is requested regarding the need for additional guidance on the "as soon as reasonably practicable" standard. Proposed comment 17(g)-1 would clarify that an institution is not required to waive or reverse any overdraft fees or charges assessed to the consumer's account prior to the institution's implementation of the consumer's opt-out request.

*Duration of opt-out.* Proposed § 205.17(h) provides that once a consumer opts out, the opt-out remains in effect until revoked by the consumer in writing or electronically. Comment is requested on whether consumers should also be permitted to revoke prior opt-out elections orally, whether by telephone or in-person.

#### F. Request for Comment

The Board requests comment on all aspects of the opt-out proposal, including the various alternatives set forth in the proposal. Comment is also requested on the costs and benefits of the proposed opt-out rule to consumers and financial institutions.

#### 2. Second Alternative Approach—Opt-In Requirement

The Board is also soliciting comment on an alternative—an opt-in approach. An opt-in requirement may be appropriate where the rule is limited to the payment of overdrafts for ATM withdrawals and one-time debit card transactions, and would not apply to the payment of overdrafts for other types of transactions, including checks and ACH transactions. While a check or ACH transaction that is returned for insufficient funds may cause the consumer to incur possible merchant fee(s) for the returned item or late payment penalties, as well as an insufficient funds fee assessed by the consumer's financial institution, a declined ATM or debit card transaction does not result in the same adverse consequences.

Under an opt-out approach, consumers who may prefer to have ATM and debit card transactions declined if they would result in an

overdraft may nonetheless incur overdraft fees simply because they fail to act on the notice.<sup>35</sup> For such consumers, establishing an opt-in rule that generally does not allow institutions to impose fees for paying these overdrafts unless a consumer affirmatively consents to the overdraft service would enable consumers to avoid fees for a service that they did not request or were unaware they had. An opt-in rule would also provide an incentive for institutions to persuade consumers of the benefits of the overdraft service and enable the consumer to make an informed choice about the merits of the service before he or she incurs any overdraft fees.

However, for consumers who rarely, if ever, overdraw their accounts, the occasional coverage of overdrafts by their institutions may be a positive benefit.<sup>36</sup> For such consumers, an opt-in regime may result in more declined transactions even though the consumer may have preferred to have the overdraft paid, despite the overdraft fee that may be charged by the consumer's financial institution. Such a consumer could be precluded from completing an important transaction when there are insufficient funds in the consumer's account and the consumer does not have another means of payment. For example, a consumer may need emergency funds and attempt to withdraw such funds from an ATM using a debit card. Or, the consumer may use a debit card to purchase essential groceries or medicine and have no other means of payment. In such cases, if the consumer has not opted in, the consumer would not be able to complete the transaction if the

<sup>35</sup> Various studies suggest that consumers are likely to adhere to the established default rule, that is, the outcome that would apply if the consumer takes no action, even if the default rule may not always be in their best interest. For example, studies of automatic enrollment in 401(k) savings plans indicate a significant increase in employee participation if the default rule provides that a consumer is automatically enrolled in the plan unless they opt out, instead of requiring employees to affirmatively agree to participate in the plan. See, e.g., Brigitte Madrian and Dennis Shea, *The Power of Suggestion: Inertia in 401(k) Participation and Savings Behavior*, 116 Quarterly Journal of Economics 1149 (2001).

<sup>36</sup> Available data indicates that the majority of account holders do not overdraw their accounts in a given year. In its Study of bank Overdraft Programs, the FDIC reported that almost 75 percent of consumer accounts for banks that had an automated overdraft program had no overdrafts during the 12-month period examined. See *FDIC Study at 76. See also 80 Percent of Consumers Have Not Paid Overdraft Fees in Past year, Says ABA Survey*, Press release, American Bankers Association (August 30, 2007) (available at <http://www.aba.com/Press+Room/083007ABASurvey.htm>).

consumer does not have another form of payment.

Thus, while an opt-in approach may benefit some consumers, it may not be the optimal outcome for others. In addition, an opt-in rule could result in greater inefficiency for processing systems due to the potential increase in transactions that are declined. Accordingly, because there are both benefits and costs associated with the opt-in and opt-out approaches, the Board is soliciting comment on both approaches.

#### A. Definition—§ 205.17(a)

The proposed definition of “overdraft service” is the same under both the opt-out and the opt-in approaches, and means 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. See § 205.17(a). The term would cover circumstances when an institution assesses a fee for paying an overdraft pursuant to any automated program or service, whether promoted or not, or as a non-automated, ad hoc accommodation. The term does not include an institution's payment of overdrafts pursuant to a line of credit subject to the Board's Regulation Z, including transfers from a credit card account, a home equity line of credit, or an overdraft line of credit. The term also does not include any overdrafts paid pursuant to a service that transfers funds from another account of the consumer (including any account that may be jointly held by the consumer and another person) held at the institution. The Board is not proposing to include these methods of covering overdrafts in this proposal because they require the express agreement of the consumer.

#### B. Opt-In Requirement—§ 205.17(b)

*General rule and scope of opt-in.* Proposed § 205.17(b)(1) sets forth the general rule prohibiting an account-holding institution from assessing a fee or charge on a consumer's account held at the institution for paying an ATM withdrawal or a one-time debit card transaction pursuant to the institution's overdraft service, unless the consumer is provided with notice explaining the institution's overdraft service for such transactions and a reasonable opportunity to affirmatively consent, or opt in, to the service, and the consumer affirmatively consents, or opts in, to the service. If the consumer opts in, the

institution must provide written confirmation of the consumer's consent.

The proposed opt-in would apply to any ATM withdrawal, including withdrawals made at proprietary or foreign ATMs. The proposed opt-in would also apply to any one-time debit card transaction, regardless of whether the consumer uses a debit card at a point-of-sale (for example, at a merchant or a store), in an online transaction, or in a telephone transaction.

Proposed comment 17(b)–1 clarifies that a financial institution may pay overdrafts for ATM withdrawals and one-time debit card transactions even if a consumer has not affirmatively consented or opted in to the institution's overdraft service. If an institution pays an overdraft for these transactions and the consumer has not opted in to the service, however, the financial institution would generally be prohibited from assessing a fee or charge for doing so, except as permitted under the exceptions set forth in proposed § 205.17(b)(5). The rule would not, however, limit the institution's ability to debit the consumer's account for the amount of the overdraft, provided that the institution is permitted to do so by applicable law.

Proposed comment 17(b)–2 clarifies that § 205.17 does not require an institution to pay or honor any overdrafts on an ATM withdrawal or a one-time debit card transaction even if a consumer affirmatively consents to the institution's overdraft service for such transactions.

Similar to the opt-out approach, the proposed rule requiring consumer opt-in would not apply to other types of transactions, such as checks, ACH transactions or preauthorized EFTs. In many of these cases, the institution would assess the same fee amount whether the item is paid or returned, but payment pursuant to the overdraft service would enable the consumer to avoid other adverse consequences, such as merchant returned item fees. In contrast, if a consumer does not opt in to the payment of overdrafts for ATM withdrawals or one-time debit card transactions, the transaction would generally be declined and the consumer would not be assessed any fees either by the financial institution or the merchant.

To enable consumers to make an informed choice about an institution's overdraft service, proposed § 205.17(b)(1)(i) would require the institution to provide a consumer a notice explaining the institution's overdraft service for ATM withdrawals and one-time debit card transactions that is segregated from everything else,

including other account disclosures. In addition, the proposal would provide that the notice may not contain any information that is not specified or otherwise permitted by this section (see proposed § 205.17(d) and comment 17(d)-2, discussed below). The separate notice requirement is designed to ensure that this information is not buried within other account documents and overlooked by the consumer. Otherwise, institutions could include information about the overdraft service in preprinted language in an account-opening disclosure, and a consumer might inadvertently consent to the institution's overdraft service merely by signing a signature card or other account-opening document acknowledging acceptance of the account terms.

*Reasonable opportunity to opt in.* Proposed § 205.17(b)(1)(ii) requires an institution to provide a reasonable opportunity for the consumer to affirmatively consent to the institution's overdraft service for ATM withdrawals and one-time debit card transactions. Proposed comment 17(b)-3 contains examples to illustrate what would constitute a reasonable opportunity to affirmatively consent, including the provision of reasonable method(s) to provide affirmative consent.

Proposed comment 17(b)-3.i contains an example of a reasonable method of opting in when the institution provides a written form that the consumer can fill out and mail to opt in. See proposed § 205.17(b)(1)(i) and proposed Model Form A-9 in Appendix A, discussed below. The institution may not, however, obtain a consumer's affirmative consent in writing by including preprinted language about the overdraft service in an account disclosure provided with a signature card or contract that the consumer must sign to open the account and that acknowledges the consumer's acceptance of the account terms. Nor may an institution obtain a consumer's affirmative consent by providing a signature card that contains a pre-selected check box indicating that the consumer is requesting the service.

Proposed comment 17(b)-3.ii illustrates that an institution could also provide a toll-free telephone number that the consumer may call to provide affirmative consent. Proposed 17(b)-3.iii illustrates that an institution may provide an electronic means for the consumer to affirmatively consent, such as a form that can be accessed and processed at an Internet Web site, provided that the institution directs the consumer to the specific Web site address where the form is located,

rather than solely referring to the institution's home page.

Proposed comment 205.17(b)-4 states that an institution may provide an opt-in notice prior to or at account opening and require the consumer to decide whether to opt in to the payment of ATM withdrawals or one-time debit card transactions pursuant to the institution's overdraft service as a necessary step to opening an account. For example, the institution could require the consumer prior to or at account opening to choose between an account that does not permit the payment of ATM withdrawals or one-time debit card transactions pursuant to the institution's overdraft service or an account that permits the payment of such overdrafts.

*Written confirmation.* Proposed § 205.17(b)(1)(iii) requires that upon obtaining the consumer's affirmative consent to the institution's overdraft service, the institution must provide the consumer with written confirmation documenting the consumer's choice, to help ensure that the consumer intended to opt in to the service. An institution could comply with the proposed written confirmation requirement, for example, by providing a copy of a consumer's completed opt-in form or sending a letter to the consumer acknowledging that the consumer has elected to opt in to the institution's service if the consumer has opted out by telephone or in person.

*Conditioning payment of overdrafts on consumer's affirmative consent.* Proposed § 205.17(b)(2) of the opt-in approach provides that an institution shall not condition the payment of any overdrafts for checks, ACH transactions, or other types of transactions on the consumer also affirmatively consenting to the institution's payment of overdrafts for ATM withdrawals and one-time debit card transactions. The Board is concerned that some institutions may seek to tie the ability of a consumer to have overdrafts paid for checks, ACH transactions, and other types of transactions to the consumer affirmatively consenting to the institution's payment of ATM and debit card overdrafts. As discussed above, many consumers may prefer that their account-holding financial institution cover overdrafts by check. These consumers may elect to opt in to an institution's overdraft service if not doing so would mean that checks would be returned unpaid.

To prevent circumvention of the opt-out right, the proposed rule also would prohibit an institution from declining to pay checks, ACH transactions, or other types of transactions because the

consumer has not also affirmatively consented to the institution's overdraft service for ATM and one-time debit card transactions. The proposed provision is designed to ensure that institutions do not exercise their discretion regarding the payment of overdrafts in such a manner as to prevent consumers from exercising a meaningful choice regarding overdraft services. Thus, the proposed rule generally would require an institution to apply the same criteria for deciding when to pay overdrafts for checks, ACH transactions, and other types of transactions, whether or not the consumer has affirmatively consented to the institution's overdraft service with respect to ATM and one-time debit card overdrafts. For example, if an institution's internal criteria would lead the institution to pay a check overdraft if the consumer had affirmatively consented to the institution's overdraft service, it must also apply that same criteria in a consistent manner in determining to pay the check overdraft if the consumer has not opted in. This provision is not intended to create a contractual requirement for the institution to pay overdrafts on checks, ACH transactions, or other types of transactions in any circumstances. See also proposed comment 17(b)-2. Comment is requested on whether there are other, more effective means of ensuring that consumers are not effectively compelled to opt in to an institution's overdraft service for ATM withdrawals and one-time debit card transactions.

Notwithstanding the Board's concerns about potential consumer compulsion to opt in, the Board is proposing a modified version of proposed § 205.17(b)(2) that would expressly permit institutions to condition the payment of any overdrafts for checks, ACH transactions, and other types of transactions on the consumer also affirmatively consenting to the institution's payment of ATM withdrawals and one-time debit card transactions pursuant to the institution's overdraft service. Under the alternative approach, an institution could also decline checks, ACH transactions, and other types of transactions because the consumer has not affirmatively consented to the institution's overdraft service for ATM withdrawals and one-time debit card transactions. See proposed § 205.17(b)(2). This alternative would address the potential operational issues associated with implementing an opt-in that would apply to ATM withdrawals and one-time debit card transactions, but not to other types of transactions.

The Board solicits comment on the merits of both alternatives. The Board also seeks comment on other approaches that may sufficiently balance concerns about consumers being effectively compelled to opt in to an institution's overdraft service for ATM withdrawals and one-time debit card transactions in order to have overdrafts paid for checks and other transactions against the operational difficulties of implementing a rule that enables consumers to decide whether to have overdrafts paid for some but not all types of transactions.

*Implementation of opt-in.* Some institutions may choose to implement a consumer's affirmative consent at the account level and pay overdrafts for ATM withdrawals and one-time debit card transactions for those consumers that have opted in. Other institutions for operational reasons may prefer to implement the consumer's choice at the product level and open different accounts for consumers depending on whether the consumer has provided affirmative consent to the institution's overdraft service for ATM withdrawals and one-time debit card transactions ("opt-in" account) or not ("no opt-in" account). Proposed § 205.17(b)(3) is intended to provide operational flexibility to institutions to implement a consumer's affirmative consent using either approach.

The Board is concerned, however, that institutions could circumvent the proposed opt-in right and effectively compel the consumer to affirmatively consent to the institution's payment of overdrafts for ATM withdrawals and one-time debit card transactions by providing a "no opt-in" account with significantly less favorable terms, conditions, or features compared to the opt-in account. Thus, the proposal sets forth two alternative approaches to address this concern.

Under the first alternative, an institution must provide to consumers who do not affirmatively consent to the institution's overdraft service for ATM withdrawals and one-time debit card transactions an account with the same terms, conditions, and features, including interest rates paid and fees assessed, as it provides to consumers who do affirmatively consent, except for the features that limit the institution's payment of such overdrafts.

Under the second alternative, an institution may wish to alter some of the terms, conditions, or features of the account that does not permit the payment of overdrafts on ATM withdrawals and one-time debit card transactions. For example, the institution may wish to price some

account services differently for the "no opt-in" account. In light of the Board's concern about possible chilling effects, however, the second alternative permits an institution to vary the terms, conditions, or features of the "no opt-in" account only if the differences in the terms, conditions, or features are not so substantial as to effectively compel a reasonable consumer to affirmatively consent to the institution's payment of overdrafts on ATM withdrawals and one-time debit card transactions. For example, an institution may not decline to provide ATM and debit card services altogether if the consumer has not affirmatively consented to the institution's overdraft service for ATM withdrawals and one-time debit card transactions. See proposed comment 17(b)(3)-1 of this second alternative.

The Board requests comment on both approaches. For institutions that require consumers to opt in to the institution's overdraft service, the Board requests comment on whether the consumer's choice is implemented at the account level (*i.e.*, within the same type of account) or at the product level (*i.e.*, by placing the consumer in a different type of account). The Board also requests comment on whether institutions that currently require an opt-in for overdraft services, or that offer accounts to certain subsets of consumers (such as high-risk consumers) that limit the consumer's ability to overdraw the account, vary any other terms, conditions, or features of the account depending upon whether the consumer opts in or not. If so, comment is solicited on which terms, conditions or features are varied and why.

*Exception to the notice and opt-in requirements.* Proposed § 205.17(b)(4) creates an exception to the proposed notice and opt-in requirement. Specifically, no notice would be required (nor affirmative consent obtained) when the institution has a policy and practice of declining to pay any ATM withdrawals or one-time debit card transactions for which authorization is requested if the institution has a reasonable belief that if the consumer's account does not have sufficient funds available to cover the transaction at the time of the authorization request.

*Exceptions to the fee prohibition.* Proposed § 205.17(b)(5) contains two exceptions to the fee prohibition that are identical to the exceptions proposed under the opt-out approach. These exceptions would allow institutions to assess a fee or charge for paying an ATM or debit card overdraft in certain circumstances even if the consumer has

not affirmatively consented to the overdraft service.

Under the first exception, an institution would be permitted to assess an overdraft fee or charge for paying an ATM withdrawal or one-time debit card transaction, notwithstanding the absence of the consumer's affirmative consent, if the institution has a reasonable belief that there are sufficient funds available in the consumer's account at the time it authorizes a transaction. See proposed § 205.17(b)(5)(i). Under the second exception, an institution would be permitted to assess an overdraft fee or charge, notwithstanding the absence of the consumer's affirmative consent, where a merchant or payee presents a debit card transaction for payment by paper-based means, rather than electronically using a card terminal, and the institution has not previously authorized the transaction. See proposed § 205.17(b)(5)(ii). These exceptions, and the reasons for proposing them, are discussed in greater detail in the section regarding the proposed opt-out approach. Proposed comments 17(b)(5)-1 through -3 contain examples illustrating the proposed exceptions for the opt-in approach.

#### C. Timing—§ 205.17(c)

Proposed § 205.17(c) would generally require that a financial institution provide an opt-in notice to the consumer about the institution's overdraft service before the institution assesses any fee or charge on the consumer's account for paying an ATM withdrawal or one-time debit card transaction pursuant to the institution's overdraft service. However, once a consumer has opted in, financial institutions would not be required to provide a notice regarding the institution's overdraft service following the assessment of any overdraft fees or charges to the consumer's account. The Board believes such a requirement is not necessary when the consumer has affirmatively elected to enroll in the overdraft service.

The proposed provision would apply differently depending on when the account is opened. For new accounts opened on or after the effective date of the final rule, the opt-in notice must be provided prior to the assessment of any fee or charge on the consumer's account for paying an ATM withdrawal or one-time debit card transaction pursuant to the institution's overdraft service.

In contrast to the opt-out approach, the opt-in rule would not require institutions to provide a notice after a consumer has been assessed an overdraft fee or charge. Thus, existing

consumers may be unaware of their right to determine whether to enroll in their institution's overdraft service for ATM withdrawals and one-time debit card transactions, absent being given an "initial" opt-in notice. Accordingly, the proposed opt-in approach would require institutions to provide notices regarding their opt-in right to existing customers.

For existing accounts, that is, accounts opened prior to the effective date of the final rule, an institution may elect to provide an opt-in notice to all of its account holders on or with the first periodic statement sent after the effective date of the final rule. Alternatively, the institution may provide an opt-out notice to existing consumers following the first assessment of an overdraft fee or charge to the consumer's account on or after the effective date of the final rule.

The notice requirements for existing accounts would apply only for accounts for which overdraft services are provided as of the effective date of the final rule. Thus, institutions would not be required to provide notices to consumers that have previously opted out of, or, for those institutions that require an opt-in, to consumers that have not affirmatively consented to, the service. Institutions that elect to provide notices to consumers prior to the effective date of the final rule also would not be required to provide new notices once the rule becomes effective for consumers that have not affirmatively consented to the service (provided that the consumer was given a reasonable amount of time to opt in).

As discussed below under proposed § 205.17(g), if an existing consumer has not opted in within 60 days of receiving the opt-in notice, the institution must cease assessing any fees or charges to existing consumer accounts for paying an ATM withdrawal or one-time debit card transaction pursuant to the institution's overdraft service, except for fees that are permitted by the exceptions in § 205.17(b)(5).

The Board solicits comment on whether another approach may be more appropriate for existing customers. Specifically, the Board requests comment on whether it should adopt a hybrid approach consisting of an opt-out rule for existing accounts and an opt-in rule for new accounts. Under this approach, an institution could continue to pay overdrafts (and assess fees) for ATM withdrawals and one-time debit card transactions for existing consumers who have not opted out, but would be prohibited from paying such overdrafts and assessing an overdraft fee or charge on new consumers who have not

affirmatively consented to the institution's overdraft service.

#### D. Content and Format—§ 205.17(d)

Proposed § 205.17(d) sets forth content requirements for the notice that must be provided to the consumer before the consumer may affirmatively consent to the institution's overdraft service. In addition, proposed § 205.17(d) requires that the opt-in notice be in a form substantially similar to Model Form A-9 in Appendix A. The content requirements are discussed in greater detail in the section regarding the proposed opt-out approach. However, the Board has modified these content requirements (and the accompanying proposed commentary) from the proposed opt-out approach to reflect the requirement to obtain the consumer's affirmative consent. See proposed § 205.17(d) and proposed comments 17(d)-1 and -2.

The Board expects to conduct consumer testing of this proposed model form (and the proposed model forms for the opt-out) following issuance of this proposal.

#### E. Additional Provisions Addressing Consumer Opt-in Right—§ 205.17(e)-(g)

*Joint accounts.* Proposed § 205.17(e) requires a financial institution to treat affirmative consent provided by any joint consumer of an account as affirmative consent for the account from all of the joint consumers. As also discussed above with regard to the opt-out approach, this provision takes into account the operational difficulties that would otherwise arise if an institution had to determine which account holder was responsible for a particular transaction and then make an authorization decision based on whether the consumer had affirmatively consented to the institution's overdraft service. Thus, if one joint consumer opts in to the institution's overdraft service, the institution must treat the consent as applying to all overdrafts triggered by an ATM withdrawal or debit card transaction for that account.

*Continuing right to opt-in.* Proposed § 205.17(f) provides that a consumer may affirmatively consent to a financial institution's overdraft service at any time in the manner described in the opt-in notice. This provision allows consumers to decide later in the account relationship that they wish to have overdrafts paid for ATM withdrawals and one-time debit card transactions.

*Time to comply for existing customers.* As discussed above under § 205.17(c), institutions would have the option of implementing the opt-in requirement for existing accounts either

by providing a notice to all existing accounts on or with the first periodic statement sent on or after the effective date of the final rule. Alternatively, an institution could provide an opt-in notice to existing accounts after the first assessment of an overdraft fee or charge for an ATM or one-time debit card overdraft on or after the effective date of the final rule. In either case, under proposed § 205.17(g), if a consumer has not affirmatively consented to the service within 60 days after the institution sends the opt-in notice, the institution shall cease assessing any fees or charges on the consumer's account for paying such overdrafts, except if permitted by the exceptions in § 205.17(b)(5).

The 60-day period is intended to provide sufficient time for the consumer to respond to the opt-in notice, and for the institution to implement the consumer's decision. During this time, an institution may continue to assess overdraft fees for paying ATM withdrawals and one-time debit card transactions. Comment is requested on the 60-day period, and whether the period should be longer or shorter.

*Duration of opt-in.* Proposed § 205.17(h) provides that a consumer's affirmative consent to the institution's overdraft service is generally effective until revoked by the consumer. An institution may also terminate the consumer's access to the overdraft service at its discretion, for example, if the institution determines that there is excessive usage of the service by the consumer.

#### F. Request for Comment

The Board requests comment on all aspects of the opt-in proposal, including the various alternatives set forth in the proposal. Comment is requested on the costs and benefits of the proposed opt-in rule to consumers and financial institutions. Comment is also solicited on which approach (opt-out or opt-in) may be optimal for both consumers, and whether one approach may present unique operational or cost issues that would not be associated with the other approach.

#### Section 205.19 Debit Holds

##### Background

When a consumer uses a debit card to make a purchase, a block, or hold, may be placed on funds in the consumer's account to ensure that the consumer has sufficient funds in his or her account when the transaction is presented for settlement. This type of block or hold is commonly referred to as a "debit hold." During the time the debit hold remains

in place, which may be up to three days after authorization, those funds may be unavailable for the consumer's use in other transactions.

In some cases, the actual purchase amount is not known at the time the transaction is authorized, such as when a consumer uses a debit card to pay for gas at the pump, check into a hotel room, or pay for a meal at a restaurant. Consequently, the debit hold may be placed for an estimated amount that exceeds the actual transaction amount. The consumer may engage in subsequent transactions reasonably assuming that his or her account has only been debited for the actual transaction amount. Or, prior transactions may be presented for settlement after the hold is placed. Because of the excess hold, however, the consumer may incur overdraft fees for those transactions.

For example, a consumer with \$100 in a deposit account may swipe his or her debit card at a pay-at-the-pump dispenser to purchase \$20 worth of fuel. When this transaction is authorized, the consumer's financial institution may increase the merchant's \$1 pre-authorization hold<sup>37</sup> to \$75 to cover the maximum amount the institution guarantees to pay the gas station under card network rules.<sup>38</sup> Because the final \$20 transaction amount is not settled immediately, the \$75 debit hold amount may remain in place for some period of time, up to three days for signature-based debit card transactions.<sup>39</sup> However, the consumer would be unaware that \$55 more than the purchase amount has been temporarily made unavailable for use until the merchant presents the transaction for settlement. Thus, prior to settlement of the transaction, the consumer may make subsequent purchases assuming that his or her account has been debited by only \$20, and inadvertently spend more than the available amount in his or her

account. As a result, the consumer could be charged an overdraft fee even though the account contained sufficient funds to pay for all of the consumer's purchases.

*May 2008 FTC Act Proposal.* The Agencies proposed in the May 2008 FTC Act Proposal to prohibit institutions from assessing an overdraft fee where the overdraft would not have occurred but for the placement of an excess debit hold. While consumer groups endorsed the Agencies' proposal, industry commenters expressed strong opposition, stating that it would present significant operational difficulties.

Several industry commenters asserted the rule would require banks to monitor retroactively, and manually adjust, transactions and fees that have posted to the account. A few of these commenters believed that the proposal would have a disproportionate cost impact on smaller institutions that do not have the systems or staff to handle the research and manual adjustments necessary to correct the consumer's account. Alternatively, institutions would have to stop placing debit holds altogether which, industry commenters argued, would raise potential safety and soundness concerns. Nonetheless, a few financial institution commenters stated that they either do not currently place holds on authorizations from gas stations, hotels, or rental car companies, or do not increase the \$1 merchant pre-authorization amount in connection with fuel purchases.

Rather than adopting a substantive FTC Act rule, industry commenters urged the Agencies to use other existing regulatory authority. For example, industry commenters recommended that the Board exercise its authority under Regulation E to require merchants to disclose at the point-of-sale when holds may be placed on debit card transactions. Many industry commenters also stated that the Agencies' concerns were already largely addressed by recent card network initiatives intended to reduce the length of the hold time for debit holds. For example, one payment card network has recently implemented changes intended to reduce the hold times for pay-at-the-pump fuel dispensers. Under these new rules, fuel merchants would be encouraged to transmit a transaction for settlement within two hours of authorization. If the merchant does so, the card-issuing institution will be required to drop the hold within the two-hour time frame, thus reducing the hold times to a matter of hours, instead of days.

## Discussion

### A. General Rule—§ 205.19(a)

After reviewing the comments received on the May 2008 FTC Act Proposal and based on its own analysis, the Board is proposing to address debit holds under the EFTA and Regulation E. Proposed § 205.19(a) generally would prohibit financial institutions from assessing a fee or charge for paying an overdraft pursuant to the institution's overdraft service if the overdraft would not have occurred but for a debit hold placed in a consumer's account if the amount of the hold exceeds the actual transaction amount. The proposed rule would not apply to transactions in which the amount of the hold equals or is less than the actual amount of the transaction. Similarly, the proposed rule would not apply if the actual amount of the transaction would also have caused the overdraft to occur.

Under the proposal, the scope of the debit hold provision would be limited to debit card transactions in which the actual transaction amount generally can be determined by the merchant or other payee within a short period of time after the institution authorizes the transaction. For example, in pay-at-the-pump fuel purchases, the actual transaction amount can be calculated once the consumer has finished pumping fuel. Similarly, when a consumer uses a debit card to pay a restaurant bill, the actual transaction amount can be determined once the consumer has signed the receipt and added a service tip. According to data submitted by one card network on the Board's May 2008 FTC Act Proposal, restaurant and fuel purchases comprise over 95 percent of all transactions in which the settlement amount typically does not match the authorization amount.<sup>40</sup>

The proposed rule would not apply, however, to debit holds in other retail environments where the actual transaction amount generally cannot be determined for a considerable period of time after the merchant has submitted a transaction for authorization. For example, when a consumer provides his or her debit card at check-in for a multi-night hotel stay, the transaction will not be submitted for settlement until the end of the consumer's stay. In this case, a hold may be placed on funds in the consumer's account at check-in, but will not be released until the consumer completes his or her stay (or when the hold is required to be released under card network rules, whichever comes first). Similarly, if a consumer uses his

<sup>37</sup> Pre-authorization describes the dollar amount of funds that are held on a consumer's account when a card is swiped to initiate a transaction.

<sup>38</sup> In a signature-based debit card transaction at a pay-at-the-pump dispenser, the merchant typically obtains a \$1 pre-authorization to activate the pump. The card issuer may increase this amount to the maximum amount guaranteed to the merchant (currently \$75 in most cases under card network rules) to protect itself against risk of loss. In contrast, in a PIN-based debit card transaction where the cardholder enters his or her personal identification number (PIN) to complete the transaction, the merchant obtains pre-authorization for an estimated transaction amount, which under current card network rules generally may not exceed \$75.

<sup>39</sup> Unlike signature-based debit card transactions, PIN-based debit card transactions that take place before the processing cut-off time for that day will typically settle soon after completion of the transaction.

<sup>40</sup> See Visa comment letter at 8.

or her debit card to reserve or pick up a rental car, the actual amount of the transaction will not be known until the car is returned. In these circumstances, the general rule would not apply because the actual amount of the transaction generally cannot be determined within a short period of time after. It seems impracticable to craft a rule in such cases because it would be impossible to determine a reasonable hold period in all such circumstances.

Moreover, the Board believes that overdraft fees are less likely to occur for hotel and car rental transactions because consumers tend to use credit cards for these transactions. In addition, data provided by one commenter indicates that even where debit cards are used in hotel and car rental transactions, they comprise a very small proportion of transactions overall involving a debit hold. The Board has received few complaints regarding overdraft fees incurred as a result of debit holds placed in connection with hotel and car rental transactions.

For these reasons, the Board is proposing a targeted rule for debit holds that would apply only in circumstances when the actual transaction amount can be determined within a short period of time after the institution authorizes the transaction. As stated above, the proposed rule would appear to cover approximately 95 percent of all transactions (pay-at-the-pump and restaurants) in which the actual transaction amount and the authorization amount do not match. Thus, the proposed rule would cover the areas of greatest concern regarding overdraft fees incurred because of a debit hold. Proposed comment 19(a)–1 provides examples of transactions covered by the proposed rule.

The prohibition against assessing an overdraft fee in connection with a debit hold applies only if the overdraft is caused solely by the existence of the hold. Proposed comment 19(a)–2 provides that an institution may assess an overdraft fee or charge if the consumer's account is overdrawn for other reasons. These reasons may include prior debit card transactions that may have been authorized but not yet presented for settlement, or when a deposited check in the consumer's account is returned.

Proposed comment 19(a)–3 clarifies that a financial institution does not violate the prohibition in § 205.19 if it promptly waives or refunds any overdraft fees assessed on a consumer's account caused by a debit hold placed on funds in the consumer's account that is in excess of the actual amount of the

transaction. However, the institution may not require the consumer to provide notice or other information that an overdraft fee was caused by a debit hold on funds in the consumer's account before waiving or refunding the fee. Proposed comment 19(a)–3 includes an example illustrating this provision.

Proposed comments 19(a)–4 through –7 set forth examples to illustrate application of the rule.

#### B. Safe Harbor—§ 205.19(b)

The proposed rule provides a safe harbor that would allow a financial institution to assess a fee or charge for paying an overdraft that is caused solely by a debit hold in certain cases. Specifically, proposed § 205.19(b) permits an institution to assess an overdraft fee or charge to the consumer's account in connection with a debit hold if the institution has adopted procedures and practices designed to remove the hold within a reasonable period of time. This safe harbor is intended to mitigate the potential compliance burden on institutions. Thus, an institution would not be required to recalculate each transaction which may appear to be overdrawn due to an excess hold to determine whether an overdraft fee was properly assessed if the hold is removed within a reasonable period of time following authorization. Proposed § 205.19(b) provides that an institution has procedures and practices designed to release the hold within a reasonable period of time if the institution releases debit holds for the transactions covered by the proposed rule within two hours of authorization.<sup>41</sup> Proposed comment 19(b)–1 illustrates the safe harbor.

The two-hour time period for removing a hold is consistent with industry efforts to minimize current hold times in certain retail environments. As discussed above, one payment card network has recently implemented changes designed to significantly reduce the hold times at pay-at-the-pump fuel dispensers. This industry initiative, however, is voluntary and, by itself, may not be sufficient to protect consumers from being assessed overdraft fees caused by an excess hold. In addition, this initiative is currently limited to pay-at-the-pump debit card transactions, and would not apply in other circumstances in which the actual transaction amount can be determined within a short period

of time after authorization was obtained, such as at restaurants. Nonetheless, the introduction of a two-hour hold period, even on a voluntary basis, suggests that such a standard is feasible.

The Board recognizes that the proposed safe harbor in § 205.19(b) would not prevent in all cases the assessment of overdraft fees caused by a debit hold even though the consumer had sufficient funds in the account. For example, a consumer may use his or her debit card to purchase groceries an hour after completing a fuel purchase. The proposed safe harbor would not preclude the consumer's financial institution from assessing an overdraft fee or charge for the grocery purchase where an excess hold placed in connection with the fuel purchase causes the consumer to have insufficient funds at the time of authorization for the grocery purchase. (However, if the consumer has opted out under § 205.17 (or not opted in), the institution would not be permitted to assess a fee or charge for paying the debit card overdraft. See proposed comment 19(b)–2, discussed below.) The Board nonetheless believes that in the vast majority of cases, consumers would not be assessed a fee for an overdraft that was caused by an excess debit hold in light of the short time period (2 hours) that the hold would be in place before it would be released by institutions that follow the safe harbor. However, the Board solicits comment on this approach.

Proposed comment 19(b)–2 illustrates the interaction between the debit hold provision in § 205.19 and the opt-out (or opt-in) requirements in § 205.17. Specifically, if a consumer is not enrolled in the institution's overdraft service for ATM withdrawals and one-time debit card transactions (because the consumer has opted out or not opted in), the institution may not assess any overdraft fees incurred in connection with a debit hold even if the institution otherwise is not prohibited from doing so by the debit hold provision. For example, assume a consumer has \$100 in his or her deposit account and has opted out of the institution's overdraft service. The consumer uses his or her debit card to purchase \$30 of fuel at a pay-at-the-pump fuel dispenser. At the time of authorization, the financial institution increased the gas station's \$1 preauthorization hold to \$75. One hour after completing the fuel purchase, the consumer makes a \$60 debit card purchase at a grocery store. Notwithstanding the fact that the consumer made the purchase within the two-hour safe harbor, the institution would not be permitted to assess an

<sup>41</sup> Where an institution has released a debit hold before the transaction is presented for payment in order to take advantage of the safe harbor, it would be permitted to assess an overdraft fee if the actual transaction amount presented for settlement causes the consumer to overdraw his or her account.

overdraft fee because the consumer had opted out of (or not opted in to) the institution's overdraft service.

### C. Other Potential Approaches

The proposal does not require merchants to disclose debit holds as a substitute for a substantive rule, as some industry commenters had suggested. The Board does not believe that a disclosure-based approach would be effective in pay-at-the-pump and restaurant transactions. For example, a notice posted at a gas pump or in a restaurant is unlikely to be noticed by the consumer. Even if the consumer were to notice a point-of-sale disclosure about debit holds, the consumer would not know how long the hold will remain in place. Moreover, for signature-based pay-at-the-pump debit card purchases, the merchant does not know whether the financial institution will increase the \$1 pre-authorization hold. Therefore, merchant disclosures at point-of-sale regarding debit holds do not appear to provide a workable solution in most circumstances.

### D. Request for Comment

The Board requests comment on all aspects of the debit hold proposal, including whether additional guidance is necessary regarding transactions in which the actual purchase amount is determined within "a short period of time." Comment is also requested on the costs and benefits of the proposed rule to consumers and financial institutions.

Comment is requested on the appropriateness of the proposed safe harbor, including whether other time periods may be more appropriate in light of operational constraints at smaller institutions which may only receive authorization and settlement information periodically during the day.

In addition, comment is requested whether the Board should exercise its authority under Section 904 of the EFTA to also require merchants (or their acquirers or processors) to promptly submit transactions covered by this rule for settlement. Specifically, the Board seeks comment on whether the final rule should also require merchants (or their acquirers or processors) to submit such transactions for settlement within the safe harbor period.

## VI. Initial Regulatory Flexibility Analysis

The Regulatory Flexibility Act (5 U.S.C. 601 *et seq.*) (RFA) generally requires an agency to perform an assessment of the impact a rule is expected to have on small entities.

However, under section 605(b) of the RFA, 5 U.S.C. 605(b), the regulatory

flexibility analysis otherwise required under section 604 of the RFA is not required if an agency certifies, along with a statement providing the factual basis for such certification, that the rule will not have a significant economic impact on a substantial number of small entities. Based on its analysis and for the reasons stated below, the Board believes that this proposed rule is likely to have a significant economic impact on a substantial number of small entities. A final regulatory flexibility analysis will be conducted after consideration of comments received during the public comment period.

1. *Statement of the need for, and objectives of, the proposed rule.* The Board is proposing revisions to Regulation E to prohibit financial institutions that hold a consumer's account from assessing a fee or charge for paying ATM withdrawals and one-time debit card transactions pursuant to the institution's overdraft service, unless the consumer is given the right to opt out of the service, and the consumer does not opt out. The proposal also sets forth an alternative approach that would require that a consumer affirmatively consent to the institution's overdraft service before overdraft fees could be assessed for these transactions. Under the proposal, financial institutions would be prohibited from assessing a fee or charge for certain debit card transactions that overdraw the consumer's account if the overdraft would not have occurred but for a hold placed on funds in the consumer's account in excess of the actual transaction, unless the institution has adopted procedures and practices designed to release the hold within a reasonable period of time. A safe harbor is provided if an institution has adopted procedures to release the hold within two hours after the institution authorized the transaction.

The EFTA was enacted to provide a basic framework establishing the rights, liabilities, and responsibilities of participants in electronic fund transfer systems. The primary objective of the EFTA is the provision of individual consumer rights. 15 U.S.C. 1693. The EFTA authorizes the Board to prescribe regulations to carry out the purpose and provisions of the statute. 15 U.S.C. 1693b(a). The Act expressly states that the Board's regulations may contain "such classifications, differentiations, or other provisions, . . . as, in the judgment of the Board, are necessary or proper to effectuate the purposes of [the Act], to prevent circumvention or evasion [of the Act], or to facilitate compliance [with the Act]." 15 U.S.C. 1693b(c). The Board believes that the

revisions to Regulation E discussed above are within Congress's broad grant of authority to the Board to adopt provisions that carry out the purposes of the statute. These revisions facilitate a consumer's ability to avoid overdrawing his or her account in connection with an electronic fund transfer the consumer has requested.

2. *Small entities affected by the proposed rule.* The number of small entities affected by this proposal is unknown. Account-holding institutions would be required to provide consumers with a notice of their right to opt out of the payment of overdrafts at ATMs and for one-time debit transactions, and a reasonable opportunity to opt out, before assessing any overdraft fee. These institutions would also be required to provide notice of the opt-out right subsequent to any overdraft fee assessment, whether on the consumer's periodic statement or on a notice provided promptly after the occurrence of the overdraft. Under the alternative proposed approach, account-holding institutions would be required to obtain affirmative consent to the institution's overdraft service before assessing overdraft fees for ATM withdrawals and one-time debit card transactions. According to the FDIC's Study of Bank Overdraft Programs, 75.1 percent of banks with an automated overdraft program currently provide some form of an opt-out right to consumers, and 11.1 percent provide an opt-in right.<sup>42</sup> Thus, institutions that already have an opt-out or an opt-in process in place would have to reprogram their systems to provide the notices required by the proposal. Institutions would also have to reprogram their systems to differentiate between overdrafts for different transaction types. As some industry commenters noted, some systems are not currently set up to pay overdrafts for certain transaction types (e.g., checks and ACH), but not others (e.g., ATM and one-time debit card transactions).

The Board is aware that some small institutions do not pay overdrafts at ATMs or for one-time debit card transactions.<sup>43</sup> These institutions would not be subject to the proposed opt-out (or opt-in) requirements. With respect to the opt-out approach, the Board believes that many institutions are already providing customers a method to opt out of their overdraft service, or an affirmative opt-in. These institutions would need to conform their opt-out (or

<sup>42</sup> See *FDIC Study* at 27.

<sup>43</sup> See *FDIC Study* at 10 (reporting that 81 percent of institutions surveyed provide overdraft services for ATM and POS/debit card transactions).

opt-in) procedures to the proposal. Also, those institutions that currently provide a form of opt-out or opt-in notice would need to review and revise this disclosure. Further, the Board believes that many institutions currently notify consumers who have incurred overdrafts promptly following an overdraft. Under the proposed opt-out approach, these institutions may need to review and perhaps revise this notification to add the opt-out notice.

In addition, financial institutions would be prohibited from assessing a fee or charge for certain debit card transactions that overdraw the consumer's account if the overdraft would not have occurred but for a hold placed on funds in the consumer's account in excess of the actual transaction, unless they have adopted procedures designed to release the hold within a reasonable period of time. A safe harbor is provided if an institution has adopted procedures to release the hold within two hours after the institution authorized the transaction. The Board believes the proposed safe harbor will significantly decrease the burden of compliance with the rule.

3. *Other federal rules.* The Board has not identified any federal rules that duplicate, overlap, or conflict with the proposed revisions to Regulation E.

4. *Significant alternatives to the proposed revisions.* The Board solicits comment on any significant alternatives that would reduce regulatory burden associated with this proposed rule on small entities.

## VII. Paperwork Reduction Act

In accordance with the Paperwork Reduction Act (PRA) of 1995 (44 U.S.C. 3506; 5 CFR Part 1320 Appendix A.1), the Board reviewed the rule under the authority delegated to the Board by the Office of Management and Budget (OMB). The collection of information that is subject to the PRA by this proposed rule is found in 12 CFR part 205. The Federal Reserve may not conduct or sponsor, and an organization is not required to respond to, this information collection unless the information collection displays a currently valid OMB control number. The OMB control number is 7100-0200.

This information collection is required to provide benefits for consumers and is mandatory (15 U.S.C. 1693 *et seq.*). Since the Board does not collect any information, no issue of confidentiality arises. The respondents/recordkeepers are for-profit financial institutions, including small businesses. Institutions are required to retain records for 24 months, but this

regulation does not specify types of records that must be retained.

The EFTA and Regulation E are designed to ensure adequate disclosure of basic terms, costs, and rights relating to electronic fund transfer (EFT) services debiting or crediting a consumer's account. The disclosures required by the EFTA and Regulation E are triggered by certain specified events. The disclosures inform consumers about the terms of the electronic fund transfer service, activity on the account, potential liability for unauthorized transfers, and the process for resolving errors. To ease institutions' burden and cost of complying with the disclosure requirements of Regulation E (particularly for small entities), the Board publishes model forms and disclosure clauses.

Regulation E applies to all financial institutions, not just state member banks (SMBs). In addition, certain provisions in Regulation E apply to entities that are not financial institutions, including those that act as service providers or ATM operators, as well as merchants and other payees that engage in electronic check conversion transactions, the electronic collection of returned item fees, or preauthorized transfers. The Federal Reserve accounts for the paperwork burden associated with Regulation E only for the financial institutions it supervises<sup>44</sup> and that meet the criteria set forth in the regulation. Other federal agencies account for the paperwork burden imposed on the entities for which they have regulatory enforcement authority.

As mentioned in the **SUPPLEMENTARY INFORMATION** above, under Alternative 1, the proposed rule (§ 205.17) would prohibit account-holding financial institutions from assessing a fee or charge for paying ATM withdrawals and one-time debit card transactions pursuant to the institution's overdraft service, unless the consumer is given the right to opt out of the service, and the consumer does not opt out. Alternative 1 would also require these institutions to provide notice of the opt-out right subsequent to any overdraft fee assessment, whether on the consumer's periodic statement or on a notice provided promptly after the occurrence of the overdraft. The proposal also sets forth an alternative approach, Alternative 2, that would require that a

<sup>44</sup> State member banks, branches and agencies of foreign banks (other than Federal branches, Federal agencies, and insured state branches of foreign banks), commercial lending companies owned or controlled by foreign banks, and Edge and agreement corporations, organizations operating under section 25 or 25(a) of the Federal Reserve Act.

consumer affirmatively consent, or opt-in, to the institution's overdraft service before overdraft fees could be assessed for these transactions.

Under alternative 1 the Federal Reserve estimates that, to comply with the proposed opt-out notice requirement, 1,205 respondents regulated by the Federal Reserve would take, on average, 16 hours (two business days) to revise and update initial disclosures (§ 205.7(b)) for new customers and that 327 respondents<sup>45</sup> regulated by the Federal Reserve would take, on average, 16 hours (two business days) to revise and update periodic statements (§ 205.9(b)) for existing customers.

The Federal Reserve estimates the total annual one-time burden for respondents to be 24,512 hours and believes that, on a continuing basis, there would be no additional increase in burden as the disclosures would be sufficiently accounted for once incorporated into the current initial account disclosure (§ 205.7(b)) and periodic statements (§ 205.9(b)). This would increase the total annual burden to 84,414 hours for Federal Reserve-regulated financial institutions that are required to comply with Regulation E. To ease the burden of compliance model forms that institutions may use are available in Appendix A (*See* proposed Model Forms A-9(A) and A-9(B)).

Under alternative 2 the Federal Reserve estimates that, to comply with the proposed opt-in notice requirement, 1,205 respondents regulated by the Federal Reserve would again take, on average, 16 hours (two business days) to revise and update initial disclosures (§ 205.7(b)) for new customers. The Federal Reserve estimates that 1,205 respondents regulated by the Federal Reserve would take, on average, 16 hours (two business days) to prepare and send new opt-in notices for existing customers.

The Federal Reserve estimates the total annual one-time burden for respondents to be 38,560 hours and believes that, on a continuing basis, there would be no additional increase in burden as the disclosure would be sufficiently accounted for once incorporated into the current initial account disclosure (§ 205.7(b)). This would increase the total annual burden to 98,462 hours for Federal Reserve-regulated financial institutions that are required to comply with Regulation E. To ease the burden of compliance a

<sup>45</sup> To avoid double counting and to be consistent with the current burden associated with periodic statements, burden for the 878 state member banks will be taken under Regulation DD.

model form that institutions may use is available in Appendix A (See proposed Model Forms A–9).

The Federal Reserve estimates that on average 5,136,693 consumers would spend as much as 5 minutes reviewing and responding to an opt-in or opt-out notice. This would increase the total annual burden for this information collection by 428,058 hours.

Overall, the burden could increase, depending on the alternative implemented, between 452,570 hours for alternative 1 and 466,618 hours for alternative 2 (for 512,472 hours or 526,520 hours total, respectively).

The other federal financial agencies are responsible for estimating and reporting to OMB the total paperwork burden for the institutions for which they have administrative enforcement authority. They may, but are not required to, use the Federal Reserve's burden estimation methodology. Using the Federal Reserve's method, the total estimated annual burden for all financial institutions subject to Regulation E, including Federal Reserve-supervised institutions, would be approximately 1,041,011 hours.<sup>46</sup> The above estimates represent an average across all respondents and reflect variations between institutions based on their size, complexity, and practices. All covered institutions, including depository institutions (of which there are approximately 17,200), potentially are affected by this collection of information, and thus are respondents for purposes of the PRA.

Comments are invited on: a. whether the proposed collection of information is necessary for the proper performance of the Federal Reserve's functions including (a) Whether the information has practical utility; (b) the accuracy of the burden of the proposed information collection, including the cost of compliance; (c) ways to enhance the quality, utility, and clarity of the information to be collected; and (d) ways to minimize the burden of information collection on respondents, including through the use of automated collection techniques or other forms of information technology. Comments on the collection of information should be sent to Michelle Shore, Federal Reserve Board Clearance Officer, Division of Research and Statistics, Mail Stop 151–A, Board of Governors of the Federal Reserve System, Washington, DC 20551, with copies of such comments sent to the Office of Management and Budget,

Paperwork Reduction Project (7100–0200), Washington, DC 20503.

### Text of Proposed Revisions

Certain conventions have been used to highlight the proposed changes to the text of the regulation and staff commentary. New language is shown inside bold-faced arrows, while language that would be deleted is set off with bold-faced brackets.

### List of Subjects in 12 CFR Part 205

Consumer protection, Electronic fund transfers, Federal Reserve System, Reporting and recordkeeping requirements.

For the reasons set forth in the preamble, the Board proposes to amend 12 CFR part 205 and the Official Staff Commentary, as follows:

### PART 205—ELECTRONIC FUND TRANSFERS (REGULATION E)

1. The authority citation for part 205 continues to read as follows:

**Authority:** 15 U.S.C. 1693b.

2. Section 205.12 is amended by revising paragraph (a) to read as follows:

#### § 205.12 Relation to other laws.

(a) *Relation to truth in lending.* (1) The Electronic Fund Transfer Act and this part govern—

(i) The addition to an accepted credit card as defined in Regulation Z (12 CFR 226.12)(a)(2), footnote 21▶, comment 12–2◀, of the capability to initiate electronic fund transfers;

(ii) The issuance of an access device that permits credit extensions (under a preexisting agreement between a consumer and a financial institution▶ or an overdraft service, as defined in § 205.17(a)◀) only when the consumer's account is overdrawn or to maintain a specified minimum balance in the consumer's account; [and]

▶(iii) The addition of an overdraft service, as defined in § 205.17(a), to an accepted access device; and◀

[(iii)]▶(iv)◀ A consumer's liability for an unauthorized electronic fund transfer and the investigation of errors involving an extension of credit that occurs under an agreement between the consumer and a financial institution to extend credit▶ or an overdraft service, as defined in § 205.17(a),◀ when the consumer's account is overdrawn or to maintain a specified minimum balance in the consumer's account.

(2) The Truth in Lending Act and Regulation Z (12 CFR▶ part◀ 226), which prohibit the unsolicited issuance of credit cards, govern—

(i) The addition of a credit feature to an accepted access device; and

(ii) Except as provided in paragraph (a)(1)(ii) of this section, the issuance of a credit card that is also an access device.

\* \* \* \* \*

3. Section 205.17 is added to read as follows:

#### Alternative 1

#### ▶§ 205.17 Requirements for overdraft services.

(a) *Definition.* For purposes of this section, the term “overdraft service” means 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. The term “overdraft service” does not include any payment of overdrafts pursuant to—

(1) A line of credit subject to the Federal Reserve Board's Regulation Z (12 CFR part 226), including transfers from a credit card account, home equity line of credit, or overdraft line of credit; or

(2) A service that transfers funds from another account held individually or jointly by a consumer.

(b) *Opt-out requirement.* (1) *General.* Except as provided under paragraphs (b)(4) and (b)(5) of this section, a financial institution holding a consumer's account shall not assess a fee or charge on a consumer's account for paying an ATM withdrawal or a one-time debit card transaction pursuant to the institution's overdraft service, unless:

(i) The institution provides notice to the consumer explaining that it may pay overdrafts on such transactions pursuant to the institution's overdraft service and assess a fee or charge on the consumer's account for doing so;

(ii) The consumer is given a reasonable opportunity to opt out of the institution's overdraft service for such transactions; and

(iii) The consumer has not opted out.

(2) *Conditioning the opt-out.* If a consumer opts out of a financial institution's overdraft service for ATM withdrawals and one-time debit card transactions, the institution [shall not/may]:

(i) Condition the consumer's right to opt out of the institution's overdraft service for ATM withdrawals and one-time debit card transactions on the consumer also opting out of the institution's overdraft service with respect to the payment of checks, ACH transactions, and other types of transactions; or

<sup>46</sup>This estimate does not include consumer burden.

(ii) Decline to pay checks, ACH transactions, or other types of transactions that overdraw the consumer's account because the consumer has opted out of the institution's overdraft service for ATM withdrawals and one-time debit card transactions.

**Alternative A—Paragraph (b)(3)**

(3) *Implementation of opt-out.* A financial institution shall implement the consumer's election to opt out of the institution's overdraft service for ATM withdrawals and one-time debit card transactions by providing to the consumer an account that has the same terms, conditions, and features, including interest rates paid and fees assessed, as are provided to consumers who do not opt out, except for features that limit the institution's payment of such overdrafts as provided in this section.

**Alternative B—Paragraph (b)(3)**

(3) *Implementation of opt-out.* A financial institution shall implement the consumer's election to opt out of the institution's overdraft service for ATM withdrawals and one-time debit card transactions by providing an account on the same or reasonably comparable terms. The institution may vary the terms, conditions, and features for the account that does not permit the payment of overdrafts on ATM withdrawals and one-time debit card transactions, provided that the differences in the terms, conditions, or features are not so substantial that they would discourage a reasonable consumer from exercising his or her right to opt out of the payment of such overdrafts.

(4) *Exceptions to the notice and opt-out requirement.* The requirements of this section do not apply to any financial institution that:

(i) Has a policy and practice of declining to pay any ATM withdrawals or one-time debit card transactions for which authorization is requested if the institution has a reasonable belief that the consumer's account does not have sufficient funds available to cover the transaction at the time of the authorization request; or

(ii) Requires consumers to affirmatively consent to the institution's overdraft service for the payment of any ATM withdrawals or one-time debit card transactions before the institution assesses any fees or charges to the consumer's account for paying such overdrafts.

(5) *Exceptions to the fee prohibition.* Notwithstanding a consumer's election to opt out, a financial institution may

assess a fee or charge on a consumer's account for paying an ATM withdrawal or a one-time debit card transaction pursuant to the institution's overdraft service if:

(i) The institution has a reasonable belief that there are sufficient funds available in the consumer's account at the time the institution authorizes the transaction; or

(ii) In the case of a debit card transaction, the transaction is presented for payment by the merchant through paper-based means, rather than electronically through a card terminal, and the institution has not previously authorized the transaction.

(c) *Timing.* The notice described in paragraph (b)(1)(i) of this section shall be provided:

(1) For accounts opened on or after [the effective date of the final rule], prior to the financial institution's assessment of any fee or charge on the consumer's account for paying an ATM withdrawal or a one-time debit card transaction pursuant to the institution's overdraft service, so long as the consumer has a reasonable opportunity to exercise the opt-out right before the assessment of any such fee or charge; and

(2) For any account for which an opt-out has not been exercised or for which a prior opt-out has been revoked, following the assessment of any fee or charge assessed on the consumer's account for paying an ATM withdrawal or a one-time debit card transaction pursuant to the institution's overdraft service:

(i) On each periodic statement that reflects any such fee or charge, in close proximity to the disclosures required to be disclosed by 12 CFR 230.11(a); or

(ii) At least once per statement cycle on any notice sent promptly after the institution's payment of an overdraft for an ATM withdrawal or a one-time debit card transaction during that statement cycle.

(d) *Content and format.* (1) *Initial notice.* The notice required by paragraph (c)(1) of this section shall be substantially similar to Model Form A-9(A) set forth in Appendix A of this part, and include all applicable items in this paragraph.

(i) *Overdraft policy.* A general description of the financial institution's overdraft service, and the types of electronic fund transfers for which a fee or charge for paying an overdraft may be imposed, including ATM withdrawals and one-time debit card transactions.

(ii) *Fees imposed.* The dollar amount of any fees or charges assessed on the consumer's account by the financial institution for paying an ATM

withdrawal or a one-time debit card transaction, as applicable, pursuant to the institution's overdraft service. If the amount of the fee is determined on the basis of the number of times the consumer has overdrawn the account, the amount of the overdraft, or other factors, the institution must disclose the maximum fee that may be imposed or provide a range of fees that may be imposed.

(iii) *Limits on fees charged.* The maximum amount of overdraft fees or charges that may be assessed for transactions per day, or, if applicable, that there is no limit to the fees that can be imposed.

(iv) *Disclosure of opt-out right.* An explanation of the consumer's right to opt out of the financial institution's payment of overdrafts for ATM withdrawals and one-time debit card transactions pursuant to the institution's overdraft service, including the method(s) by which the consumer may exercise that right and how to contact the institution for more information.

(v) *Alternative payment options.* A statement that the financial institution offers other alternatives for the payment of overdrafts, if applicable. If the institution offers a line of credit subject to the Board's Regulation Z (12 CFR part 226) or a service that transfers funds from another account of the consumer (including joint accounts) held at the institution to cover the overdraft, the institution shall also state that fact and how to obtain more information about these alternatives. An institution may, but is not required to, list additional alternatives for the payment of overdrafts.

(2) *Subsequent notice.* The notice required by paragraph (c)(2) of this section shall be substantially similar to either Model Form A-9(A) in Appendix A of this part, or Model Form A-9(B) in Appendix A of this part.

(e) *Joint relationships.* If two or more consumers jointly hold an account, the financial institution shall treat an opt-out direction by any of the joint consumers as an opt-out for that account.

(f) *Continuing right to opt-out.* A consumer may opt out of the institution's future payment of overdrafts at any time in the manner described in the notice required by paragraph (b)(1)(i) of this section.

(g) *Time to comply with opt-out.* A financial institution shall comply with a consumer's opt-out request as soon as reasonably practicable after the institution receives it.

(h) *Duration of opt-out.* A consumer's opt-out is effective until revoked by the consumer in writing or electronically.

**Alternative 2****§ 205.17 Requirements for overdraft services.**

(a) *Definition.* For purposes of this section, the term “overdraft service” means 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. The term “overdraft service” does not include any payment of overdrafts pursuant to—

(1) A line of credit subject to the Federal Reserve Board’s Regulation Z (12 CFR part 226), including transfers from a credit card account, home equity line of credit, or overdraft line of credit; or

(2) A service that transfers funds from another account held individually or jointly by a consumer.

(b) *Opt-in requirement.* (1) *General.* Except as provided under paragraphs (b)(4) and (b)(5) of this section, a financial institution holding a consumer’s account shall not assess a fee or charge on a consumer’s account for paying an ATM withdrawal or a one-time debit card transaction pursuant to the institution’s overdraft service, unless the institution:

(i) Provides the consumer with a notice explaining the institution’s overdraft service for such transactions that is segregated from everything else, and does not contain any information not specified in or otherwise permitted by paragraph (d) of this section;

(ii) Provides a reasonable opportunity for the consumer to affirmatively consent, or opt in, to the service for such transactions; and

(iii) Obtains the consumer’s affirmative consent, or opt-in, to the institution’s payment of ATM withdrawals or one-time debit card transactions pursuant to the institution’s overdraft service, and provides the consumer with written confirmation of the consumer’s consent.

(2) *Conditioning payment of other overdrafts on consumer’s affirmative consent.* A financial institution [shall not/ may]:

(i) Condition the payment of any overdrafts for checks, ACH transactions, and other types of transactions on the consumer also affirmatively consenting to the institution’s payment of ATM withdrawals and one-time debit card transactions pursuant to the institution’s overdraft service; or

(ii) Decline to pay checks, ACH transactions, and other types of transactions that overdraw the

consumer’s account because the consumer has not affirmatively consented to the institution’s overdraft service for ATM withdrawals and one-time debit card transactions.

**Alternative A—Paragraph (b)(3)**

(3) *Implementation of opt-in.* A financial institution shall provide to consumers who do not affirmatively consent to the institution’s overdraft service for ATM withdrawals and one-time debit card transactions an account with the same terms, conditions, and features, including interest rates paid and fees assessed, as it provides to consumers who affirmatively consent, except for features that limit the institution’s payment of such overdrafts as provided in this section.

**Alternative B—Paragraph (b)(3)**

(3) *Implementation of opt-in.* A financial institution shall implement the consumer’s affirmative consent to the institution’s overdraft service for ATM withdrawals and one-time debit card transactions by providing an account on the same or reasonably comparable terms. The institution may vary the terms, conditions, and features for the account that does not permit the payment of overdrafts on ATM withdrawals and one-time debit card transactions, provided that the differences in the terms, conditions, or features are not so substantial that they would compel a reasonable consumer to affirmatively consent to the payment of such overdrafts.

(4) *Exception to the notice and opt-in requirements.* The requirements of this section do not apply to any financial institution that has a policy and practice of declining to pay any ATM withdrawals or a one-time debit card transactions for which authorization is requested when the institution has a reasonable belief that the consumer’s account does not have sufficient funds available to cover the transaction at the time of the authorization request.

(5) *Exceptions to the fee prohibition.* Notwithstanding the absence of a consumer’s affirmative consent, a financial institution may assess a fee or charge on the consumer’s account for paying an ATM withdrawal or a one-time debit card transaction pursuant to the institution’s overdraft service if:

(i) The institution has a reasonable belief that there are sufficient funds available in the consumer’s account at the time the institution authorizes the transaction; or

(ii) In the case of a debit card transaction, the transaction is presented for payment by the merchant through paper-based means, rather than

electronically through a card terminal, and the institution has not previously authorized the transaction.

(c) *Timing.* The notice required by paragraph (b)(1)(i) of this section shall be provided:

(1) For accounts opened and for which an overdraft service is provided prior to [the effective date of the final rule], at the institution’s option—

(i) On or with the first periodic statement sent on or after [the effective date of the final rule]; or

(ii) Following the first assessment on or after [the effective date of the final rule] of any fee or charge on the consumer’s account for paying an ATM withdrawal or a one-time debit card transaction pursuant to the institution’s overdraft service; or

(2) For accounts opened on or after [the effective date of the final rule], before the financial institution assesses any fee or charge on the consumer’s account for paying an ATM withdrawal or a one-time debit card transaction pursuant to the institution’s overdraft service.

(d) *Content and format.* The notice required by paragraph (b)(1)(i) of this section shall be substantially similar to Model Form A–9 set forth in Appendix A of this part, and include all applicable items in this paragraph.

(1) *Overdraft policy.* A general description of the financial institution’s overdraft services and the types of electronic fund transfers for which a fee or charge for paying an overdraft may be imposed, including ATM withdrawals and one-time debit card transactions.

(2) *Fees imposed.* The dollar amount of any fees or charges assessed on the consumer’s account by the financial institution for paying an ATM withdrawal or a one-time debit card transaction pursuant to the institution’s overdraft service. If the amount of the fee is determined on the basis of the number of times the consumer has overdrawn the account, the amount of the overdraft, or other factors, the institution must disclose the maximum fee that may be imposed or provide a range of fees that may be imposed.

(3) *Limits on fees charged.* The maximum amount of overdraft fees or charges that may be assessed per day, or, if applicable, that there is no limit to the fees that can be imposed.

(4) *Disclosure of opt-in right.* An explanation of the consumer’s right to affirmatively consent to the financial institution’s payment of overdrafts for ATM withdrawals and one-time debit card transactions pursuant to the institution’s overdraft service, including the method(s) by which the consumer

may consent to the service and how to get more information; and

(5) *Alternative payment options.* A statement that the financial institution offers other alternatives for the payment of overdrafts, if applicable. If the institution offers a line of credit subject to the Board's Regulation Z (12 CFR part 226) or a service that transfers funds from another account of the consumer (individual or joint) held at the institution to cover the overdraft, the institution must also state that fact and how to obtain more information about these alternatives. An institution may, but is not required to, list additional alternatives for the payment of overdrafts.

(e) *Joint relationships.* If two or more consumers jointly hold an account, the financial institution shall treat the affirmative consent of any of the joint consumers as affirmative consent for that account.

(f) *Continuing right to opt-in.* A consumer may affirmatively consent to the financial institution's overdraft service at any time in the manner described in the notice required by paragraph (b)(1)(i) of this section.

(g) *Time to comply for existing customers.* For accounts opened prior to [the effective date of the final rule], if

a consumer has not affirmatively consented to a financial institution's overdraft service within 60 days after the institution sends the notice required under paragraph (c)(1) of this section, the institution shall cease assessing any fees or charges on a consumer's account for paying an ATM withdrawal or a one-time debit card transaction pursuant to the service.

(h) *Duration of opt-in.* A consumer's affirmative consent to the institution's overdraft service is effective until revoked by the consumer, or until the financial institution decides for any reason to terminate the service for the consumer, such as due to the consumer's excessive usage of the service. ◀

4. Section 205.19 is added to read as follows:

▶ **§ 205.19 Debit holds.**

(a) *General rule.* A financial institution shall not assess a fee or charge for paying an overdraft pursuant to the institution's overdraft service, as defined in § 205.17(a), if the overdraft would not have occurred but for a hold placed on funds in the consumer's account in connection with a debit card transaction if the actual amount of the transaction can be determined by the merchant or other payee within a short

period of time after the financial institution authorizes the transaction. A financial institution may, however, assess a fee or charge for paying an overdraft for a debit card transaction incurred in connection with a hold placed on funds for that transaction if the amount of the hold is less than or equal to the actual amount of the transaction.

(b) *Safe harbor.* Notwithstanding paragraph (a) of this section, a financial institution may assess an overdraft fee if the institution has procedures and practices in place designed to release a debit hold subject to this section within a reasonable period of time. An institution is deemed to have procedures and practices designed to release the hold within a reasonable period of time if the institution releases the hold within two hours of the institution's authorization of the transaction. ◀

5. In Appendix A to Part 205, Appendix A-9 Model Forms for Overdraft Services (§ 205.17) is added to read as follows:

**Appendix a to Part 205—Model Disclosure Clauses and Forms**

\* \* \* \* \*

BILLING CODE 6210-01-P

## A-9 – MODEL FORMS FOR OVERDRAFT SERVICES (§ 205.17)

## ALTERNATIVE 1 – MODEL FORM A-9(A)

## A-9(A) Model Opt-Out Form for Account Opening (ALTERNATIVE 1 ONLY)

## EXPLANATION OF OVERDRAFT COVERAGE

Overview of Coverage

We currently provide overdraft coverage for your account. This means that if you attempt to spend or withdraw more money than you have in your account, we may decide to pay the overdrawn amount. Having overdraft coverage does not guarantee that we will pay your overdrafts. If we do, we will charge you fees. This coverage differs from other overdraft services we offer, such as linking your account to another account with us or an overdraft line of credit.

Your Right to Opt Out of Overdraft Coverage

You may tell us **not** to pay overdrafts for ATM withdrawals and debit card purchases you make at a store, online, or by telephone. [If you do, we will decline these transactions if you do not have enough money in your account to cover them.] As a result, you may pay fewer overdraft fees.

Your decision to opt out will not affect whether we pay overdrafts for other types of transactions, including checks. We may still cover these transactions and charge you a fee. See below for more information about your overdraft coverage, including how to contact us to opt out.

Overdraft Fees

- We will charge you a fee of [up to] [\$\_\_] each time that we pay an overdraft.
- We will also charge you a fee of [\$\_\_] for each day your account remains overdrawn.
- [There is no limit on the daily fees we can charge you for overdrawing your account.]

Other Ways We Can Cover Your Overdrafts

We offer other ways of covering your overdrafts that may be less expensive, such as linking your account to another account with us or an overdraft line of credit. Contact us to learn more about these options.

How to Opt Out or Get More Information

To opt out of our overdraft coverage, or for information about alternatives we offer for covering overdrafts, please: [include as applicable]

- Contact us at 1-8xx-xxx-xxxx.
- Contact us at [insert Internet address].
- Complete the form below and mail it to [insert address].

-----  
 \_\_\_ I do not want overdraft coverage for my ATM withdrawals and debit card purchases.

Printed Name: \_\_\_\_\_

Date: \_\_\_\_\_

Account Number: \_\_\_\_\_

## A-9(B) Model Opt-Out Form for Periodic Statements (ALTERNATIVE 1 ONLY)

You have the right to tell us **not** to pay overdrafts for ATM withdrawals and debit card purchases you make at a store, online, or by telephone. [If you do, we will decline these transactions if you do not have enough money in your account to cover them.] As a result, you may pay fewer overdraft fees.

To opt out of our overdraft coverage, or for information about alternatives we offer for covering overdrafts (including linking this account to another account with us), contact us at 1-8xx-xxx-xxxx or [insert Internet address].

ALTERNATIVE 2 – MODEL FORM A-9

A-9 Model Consent Form for Overdraft Services (ALTERNATIVE 2 ONLY)

EXPLANATION OF OVERDRAFT COVERAGE

Your Right to Request Overdraft Coverage

We will not pay your overdrafts for ATM withdrawals and debit card purchases you make at a store, online, or by telephone, unless you tell us you want overdraft coverage for these transactions. Even if you do not request overdraft coverage for ATM withdrawals and debit card purchases, we may still pay your overdrafts for other types of transactions, including checks.

Having overdraft coverage does not guarantee that we will pay your overdrafts. If we decide to pay an overdraft, you will be charged fees as described below.

Overdraft coverage differs from other overdraft services we offer, such as linking your account to another account with us or an overdraft line of credit. See below for more information, including how to contact us if you want overdraft coverage to apply to your ATM withdrawals and debit card purchases.

Overdraft Fees

- We will charge you a fee of [up to] [\$\_] each time we pay an overdraft.
We will also charge you a fee of [\$\_] for each day your account remains overdrawn.
[There is no limit on the daily fees we can charge you for overdrawing your account.]

Other Ways We Can Cover Your Overdrafts

We offer other ways of covering your overdrafts that may be less expensive, such as linking your account to another account with us or an overdraft line of credit. Contact us to learn more about these options.

How to Request Overdraft Coverage or Get More Information

To request overdraft coverage for your ATM withdrawals and debit card purchases, or for information about other alternatives we offer for covering overdrafts, please:

- Contact us at 1-8xx-xxx-xxxx.
Contact us at [insert Internet address].
Complete the form below and mail it to [insert address].

\_\_\_ I want overdraft coverage for my ATM withdrawals and debit card purchases.

Printed Name: \_\_\_\_\_

Date: \_\_\_\_\_

Account Number: \_\_\_\_\_

BILLING CODE 6210-01-C

- 6. In Supplement I to part 205,
a. Under Section 205.12 Relation to other laws, under 12(a) Relation to truth in lending, paragraph 2. is revised, and paragraph 3. is added.
b. Section 205.17—Requirements for Overdraft Services is added.
c. Section 205.19—Debit Holds is added.

Supplement I to Part 205—Official Staff Interpretations

\* \* \* \* \*

Section 205.12—Relation to Other Laws

12(a) Relation to Truth in Lending

\* \* \* \* \*

2. Issuance rules. For access devices that also constitute credit cards, the issuance rules of Regulation E apply if the only credit feature is a preexisting

credit line attached to the asset account to cover overdrafts (or to maintain a specified minimum balance) or an overdraft service, as defined in § 205.17(a). Regulation Z (12 CFR part 226) rules apply if there is another type of credit feature, for example, one permitting direct extensions of credit that do not involve the asset account.

3. Overdraft service. The addition of an overdraft service, as that term is defined in § 205.17(a), to an accepted access device does not constitute the addition of a credit feature subject to Regulation Z. Instead, the provisions of Regulation E apply, including the liability limitations (§ 205.6) and the requirement to provide consumers an opportunity to opt out of the service before any fees or charges for paying an

overdraft may be assessed to the account (§ 205.17).

\* \* \* \* \*

Section 205.17—Requirements for Overdraft Services

Alternative 1

17(b) Opt-Out Requirement

1. Effect of opt-Out. A consumer's election to opt out of a financial institution's overdraft service does not prohibit the institution from paying overdrafts for ATM withdrawals and one-time debit card transactions. If the institution pays such an overdraft, however, it may not impose a fee or charge for doing so if the consumer has opted out, except as permitted under the exceptions set forth in § 205.17(b)(5). These provisions do not limit the

institution's ability to debit the consumer's account for the amount of the overdraft if permitted to do so under applicable law.

2. *Examples of reasonable opportunity to opt out.* A financial institution gives a consumer a reasonable opportunity to opt out if:

i. *By mail.* The institution provides a form for the consumer to fill out and mail to opt out. The consumer is given 30 days from the date the consumer is provided the initial opt-out notice to opt out before an overdraft fee or charge is assessed to the consumer's account.

ii. *By telephone.* The institution provides a toll-free telephone number that consumers may call to opt out. The consumer is given 30 days from the date the consumer is provided the initial opt-out notice to opt out before an overdraft fee or charge is assessed to the consumer's account.

iii. *By electronic means.* The institution provides an electronic means to opt out, such as a form that can be accessed and processed at an Internet Web site, provided that the institution directs the consumer to the specific Web site address where the form is located, rather than solely referring to the institution's home page. The consumer is given 30 days from the date the consumer is provided the initial opt-out notice to opt out before an overdraft fee or charge is assessed to the consumer's account.

iv. *At the time of account-opening.* The institution provides the opt-out notice prior to or at account-opening and requires the consumer to decide whether to opt out of the institution's payment of ATM withdrawals and one-time debit card transactions pursuant to the institution's overdraft service as a necessary step to opening the account.

Paragraph 17(b)(3)—Implementation of Opt-out

#### Alternative B Only

1. *Example of impermissible variation in account terms.* A financial institution may not vary the terms, conditions, or features of an account that does not permit the payment of overdrafts for ATM withdrawals and one-time debit card transactions such that the differences in the terms, conditions, or features are so substantial that they would discourage a reasonable consumer from opting out of the institution's overdraft service. For example, an institution may not decline to provide ATM and debit card services altogether because the consumer has opted out of the institution's overdraft service for ATM and one-time debit card transactions.

Paragraph 17(b)(4)—Exceptions to the Notice and Opt-out Requirement

1. *Compliance.* A financial institution that qualifies for either of the exceptions in § 205.17(b)(4) is not subject to the requirements to provide a consumer notice and a reasonable opportunity to opt out of the institution's payment of overdrafts for ATM withdrawals and one-time debit card transactions.

2. *Opt-in.* A financial institution that requires the consumer's affirmative consent before paying overdrafts on the consumer's behalf need not obtain the consumer's affirmative consent prior to each transaction that may cause the consumer to overdraw the account. It is sufficient for the institution to require that the consumer affirmatively consent to the institution's overdraft service prior to the institution's assessment of any fees or charges for paying an overdraft.

Paragraph 17(b)(5)—Exceptions to the Fee Prohibition

1. *Examples of transactions authorized on an institution's reasonable belief.*

i. *Balances not updated in real-time.* A consumer has opted out of a financial institution's overdraft service. The financial institution uses a daily batch balance method for authorizing transactions, and updates the balance used for authorization at the end of the processing day. The consumer has \$100 in her deposit account after the institution has finished processing transactions at the end of the day. The next day, the consumer makes two \$40 debit card purchases followed by a \$25 debit card purchase. Because the institution does not update the authorization balance during the day, each transaction, including the \$25 debit card purchase, is authorized by the institution based on the same \$100 balance that was calculated at the end of the prior day's processing. Under these circumstances, the institution may assess a fee for paying or honoring the \$25 debit card purchase because the institution authorized the transaction on the reasonable belief that the consumer had sufficient funds available in her account to cover the transaction.

ii. *Returned deposit.* A consumer has opted out of a financial institution's overdraft service. The consumer has \$30 in his deposit account and deposits a \$100 check. The institution provides immediate availability to the consumer for the deposited funds. Subsequently, the consumer makes a \$75 debit card purchase which is authorized by the institution based on a balance of \$130. The \$100 check is later returned on

insufficient funds. Under these circumstances, the institution may assess a fee for paying or honoring the \$75 debit card transaction because the institution authorized the transaction on the reasonable belief that the consumer had sufficient funds available in his account to cover the transaction.

iii. *Settlement amount exceeds authorization amount.* A consumer has opted out of an institution's overdraft service. The consumer has \$30 in her deposit account and uses a debit card to purchase fuel. Before permitting the consumer to use the fuel pump, the merchant verifies the validity of the card by requesting a pre-authorization hold from the institution for \$1. The institution does not increase the amount of the hold. The consumer purchases \$50 of fuel. If the institution pays or honors the transaction, it may assess an overdraft fee because the actual amount of the transaction exceeds the amount requested for authorization and causes the consumer to overdraw her account.

iv. *Intervening transactions between authorization and settlement of a "force pay" debit card transaction.* A consumer has opted out of a financial institution's overdraft service. The consumer has \$100 in his deposit account and uses his debit card to make a \$50 purchase at a store, and the institution authorizes the transaction. Before the transaction is presented for settlement, however, checks written by the consumer totaling \$75 are posted to the consumer's account. Under these circumstances, and assuming no intervening deposits are made by the consumer, the institution may assess a fee or charge for paying or honoring an overdraft when the \$50 is presented for settlement because the institution authorized that transaction on the reasonable belief that the consumer had sufficient funds available in his account to cover the transaction.

2. *Examples of transactions not submitted for authorization.* The exception under § 205.17(b)(5)(i) permitting an overdraft fee to be charged to a consumer's account when a financial institution has a reasonable belief that the consumer has sufficient funds available for the requested transaction does not apply where the transaction is not submitted to the institution for authorization. Under these circumstances, the general rule in § 205.17(b)(1) prohibits the institution from assessing a fee on the consumer's account for paying or honoring an ATM withdrawal or one-time debit card transaction that overdraws the consumer's account if the consumer has opted out of the institution's overdraft service. If otherwise permitted under

applicable law, the institution may debit the consumer's account for the amount of the overdraft.

i. *Small-dollar transactions not submitted for authorization.* A consumer has opted out of a financial institution's overdraft service. The consumer purchases a \$3 cup of coffee using his debit card. Because of the small dollar amount of the transaction, the merchant does not submit the transaction to the consumer's financial institution for authorization. At the time of the transaction, the consumer's account does not have sufficient available funds to cover the transaction. The institution may not assess an overdraft fee to the consumer's account for paying or honoring the debit card transaction. If otherwise permitted under applicable law, the institution may debit the consumer's account for the amount of the overdraft.

ii. *Stand-in processing.* A consumer has opted out of a financial institution's overdraft service. The consumer withdraws \$20 from an ATM. At the time the consumer initiates the withdrawal request, the card network is temporarily unavailable and the request is not submitted to the institution for authorization. Instead, the consumer's financial institution uses a "stand-in" processor to authorize transactions based on the institution's pre-determined amount, rather than the consumer's account balance. The consumer's account does not have sufficient available funds at settlement to cover the transaction. The institution may not assess an overdraft fee to the consumer's account for paying or honoring the debit card transaction. If otherwise permitted under applicable law, the institution may debit the consumer's account for the amount of the overdraft.

3. *Example of a transaction presented by paper-based means.* A consumer has opted out of a financial institution's overdraft service. The consumer has \$50 in her deposit account and presents her debit card to make a \$60 purchase. At that time, the merchant takes an imprint of the card but does not submit the transaction for authorization. Later that day, the merchant submits a sales slip with the card imprint to its processor for payment. If the transaction overdraws the consumer's account and the consumer's institution pays the transaction, the institution may assess a fee or charge for paying or honoring the overdraft.

#### 17(c) Timing

##### Paragraph 17(c)(1)

1. *Existing customers.* The requirement to provide notice before overdraft fees are assessed for payment of an ATM withdrawal or one-time debit card transaction pursuant to a financial institution's overdraft service is applicable only to accounts opened on or after [the effective date of the final rule]. However, the requirement to provide notice of the opt-out right following the institution's assessment of a fee or charge for paying an ATM withdrawal or a one-time debit card transaction pursuant to the institution's overdraft service applies on or after [the effective date of the final rule], unless the consumer has previously opted out and the consumer has not revoked the opt-out.

#### 17(d) Content and Format

##### Paragraph 17(d)(1)—Initial Notice

1. *Range of fees.* If the amount of a fee will vary from transaction to transaction, the financial institution may indicate that the consumer may be assessed a fee "up to" the maximum fee or provide the range of fees.

2. *Additional opt-out notice content.* Section 205.17(b)(1) requires an opt-out notice that is substantially similar to Model Forms A-9(A) and A-9(B). A financial institution, may, however, briefly describe in its notice the consequences of the consumer's election to opt out of the institution's payment of overdrafts. For example, the institution may state that if a consumer opts out of the institution's overdraft service for ATM withdrawals and one-time debit card transactions, the institution may decline such transactions if the consumer's account does not have sufficient funds. An institution may also include language describing other types of transactions that are not subject to the opt-out right or indicating that the institution pays overdrafts at its discretion.

#### 17(g) Time to Comply With Opt-Out

1. *Fees or charges assessed prior to implementing opt-out.* Section 205.17(g) provides that a consumer may opt out of a financial institution's future payment of overdrafts at any time. If a consumer, who has not initially opted out, later elects to exercise his or her opt-out right, this provision does not require the institution to waive or reverse any overdraft fees or charges assessed to the consumer's account prior to the institution's implementation of the consumer's opt-out request.

#### Alternative 2

##### 17(b) Opt-In Requirement

1. *No affirmative consent.* A financial institution may pay overdrafts for ATM withdrawals and one-time debit card transactions even if a consumer has not affirmatively consented or opted in to the institution's overdraft service. If the institution pays such an overdraft, however, it may not impose a fee or charge for doing so without the consumer's affirmative consent, except as permitted under the exceptions set forth in § 205.17(b)(5). These provisions do not limit the institution's ability to debit the consumer's account for the amount of the overdraft if the institution is permitted to do so under applicable law.

2. *Overdraft transactions not required to be paid or honored.* Section 205.17 does not require a financial institution to pay or honor an overdraft on an ATM withdrawal or a one-time debit card transaction even if the consumer has affirmatively consented to an institution's overdraft service for such transactions.

3. *Examples of reasonable opportunity to provide affirmative consent.* A financial institution provides a reasonable opportunity for the consumer to affirmatively consent to the institution's overdraft service if—

i. *By mail.* The institution provides a form for the consumer to fill out and mail to affirmatively request the service.

ii. *By telephone.* The institution provides a toll-free telephone number that consumers may call to provide affirmative consent.

iii. *By electronic means.* The institution provides an electronic means for the consumer to affirmatively consent, such as a form that can be accessed and processed at an Internet Web site, provided that the institution directs the consumer to the specific Web site address where the form is located, rather than solely referring to the institution's home page.

4. *Implementing opt-in at account-opening.* A financial institution may provide a notice regarding the institution's overdraft service prior to or at account-opening and, as a necessary step to opening an account, require a consumer to choose whether to opt in to the payment of ATM withdrawals or one-time debit card transactions pursuant to the institution's overdraft service. For example, the institution could require the consumer at account opening to choose between an account that does not permit the payment of ATM withdrawals or one-time debit card transactions pursuant to the institution's overdraft service or an

account that permits the payment of such overdrafts.

Paragraph 17(b)(3)—Implementation of Opt-In

#### Alternative B Only

1. *Example of impermissible variation in account terms.* A financial institution may not vary the terms, conditions, or features of an account that does not permit the payment of overdrafts for ATM withdrawals and one-time debit card transactions such that the differences in the terms, conditions, or features are so substantial that they would compel a reasonable consumer to opt in to the institution's overdraft service. For example, an institution may not decline to provide ATM and debit card services altogether unless the consumer affirmatively consents to the institution's overdraft service for ATM withdrawals and one-time debit card transactions.

Paragraph 17(b)(5)—Exceptions to the Fee Prohibition

1. *Examples of transactions authorized on an institution's reasonable belief.*

i. *Balances not updated in real-time.* A consumer has not affirmatively consented to a financial institution's overdraft service. A financial institution uses a daily batch balance method for authorizing transactions, and updates the balance used for authorization at the end of the processing day. The consumer has \$100 in her deposit account after the institution has finished processing transactions at the end of the day. The next day, the consumer makes two \$40 debit card purchases followed by a \$25 debit card purchase. Because the institution does not update the authorization balance during the day, each transaction, including the \$25 debit card purchase, is authorized by the institution based on the same \$100 balance that was calculated at the end of the prior day's processing. Under these circumstances, the institution may assess a fee for paying or honoring the \$25 debit card purchase because the institution authorized the transaction on the reasonable belief that the consumer had sufficient funds available in her account to cover the transaction.

ii. *Returned deposit.* A consumer has not affirmatively consented to a financial institution's overdraft service. The consumer has \$30 in his deposit account and deposits a \$100 check. The institution provides immediate availability to the consumer for the deposited funds. Subsequently, the consumer makes a \$75 debit card purchase which is authorized by the

institution based on the \$130 balance. The \$100 check is later returned on insufficient funds. Under these circumstances, the institution may assess a fee for paying or honoring the \$75 debit card transaction because the institution authorized the transaction on the reasonable belief that the consumer had sufficient funds available in his account to cover the transaction.

iii. *Settlement amount exceeds authorization amount.* A consumer has not affirmatively consented to a financial institution's overdraft service. The consumer has \$30 in her deposit account and uses a debit card to purchase fuel. Before permitting the consumer to use the fuel pump, the merchant verifies the validity of the card by requesting a pre-authorization hold from the institution for \$1. The institution does not increase the amount of the hold. The consumer purchases \$50 of fuel. If the institution pays or honors the transaction, it may assess an overdraft fee because the actual amount of the transaction exceeds the amount requested for authorization and causes the consumer to overdraw her account.

iv. *Intervening transactions between authorization and settlement of a "force pay" debit card transaction.* A consumer has not affirmatively consented to a financial institution's overdraft service. The consumer has \$100 in a deposit account and uses his debit card to make a \$50 purchase at a store. The institution authorizes the transaction. Before the transaction is presented for settlement, however, checks written by the consumer totaling \$75 are posted to the consumer's account. Under these circumstances, and assuming no intervening deposits are made by the consumer, the institution may assess a fee or charge for paying or honoring an overdraft when the \$50 is presented for settlement because the institution authorized that transaction on the reasonable belief that the consumer had sufficient funds available in his account to cover the transaction.

2. *Examples of transactions not submitted for authorization.* The exception under § 205.17(b)(5)(i) permitting an overdraft fee to be charged to a consumer's account when a financial institution has a reasonable belief that the consumer has sufficient funds available for the requested transaction does not apply where the transaction is not submitted to the institution for authorization. Under these circumstances, the general rule in § 205.17(b)(1) prohibits an institution from assessing a fee to the consumer's account for paying or honoring an ATM withdrawal or one-time debit card

transaction that overdraws the consumer's account if the consumer has not affirmatively consented to the institution's overdraft service. If otherwise permitted under applicable law, the institution may debit the consumer's account for the amount of the overdraft.

i. *Small-dollar transactions not submitted for authorization.* A consumer has not affirmatively consented to a financial institution's overdraft service. The consumer purchases a \$3 cup of coffee using his debit card. Because of the small dollar amount of the transaction, the merchant does not submit the transaction to the consumer's financial institution for authorization. At the time of the transaction, the consumer's account does not have sufficient available funds to cover the transaction and the consumer has not affirmatively consented to the institution's overdraft service. The institution may not assess an overdraft fee to the consumer's account for paying or honoring the debit card transaction. If otherwise permitted under applicable law, the institution may debit the consumer's account for the amount of the overdraft.

ii. *Stand-in processing.* A consumer has not affirmatively consented to a financial institution's overdraft service. The consumer withdraws \$20 from an ATM. At the time the consumer initiates the withdrawal request, the card network is temporarily unavailable and the request is not submitted to the consumer's financial institution for authorization. Instead, the institution uses a "stand-in" processor to authorize transactions based on the institution's pre-determined amount, rather than the consumer's account balance. The consumer's account does not have sufficient available funds at settlement to cover the transaction. The institution may not assess an overdraft fee to the consumer's account for paying or honoring the debit card transaction. If otherwise permitted under applicable law, the institution may debit the consumer's account for the amount of the overdraft.

3. *Example of a transaction presented by paper-based means.* A consumer has not affirmatively consented to a financial institution's overdraft service. The consumer has \$50 in her deposit account and presents her debit card to make a \$60 purchase. At that time, the merchant takes an imprint of the card but does not submit the transaction for authorization. Later that day, the merchant submits a sales slip with the card imprint to its processor for payment. If the transaction overdraws the consumer's account and the

consumer's institution pays the transaction, the institution may assess a fee or charge for paying or honoring the overdraft.

#### 17(d) Content and Format

1. *Range of fees.* If the amount of a fee may vary from transaction to transaction, the financial institution may indicate that the consumer may be assessed a fee "up to" the maximum fee or provide the range of fees.

2. *Additional consent notice content.* Section 205.17(d)(1) requires an opt-in notice that is substantially similar to Model Form A-9. A financial institution may, however, briefly describe in its notice the benefits of the institution's payment of ATM withdrawals or debit card transactions. For example, the institution may state that if a consumer does not affirmatively consent to the institution's overdraft service in connection with ATM withdrawals and one-time debit card transactions, the institution may decline such transactions if the consumer's account does not have sufficient funds. An institution may also include language describing other types of transactions that are not subject to the opt-in right or indicating that even if the consumer affirmatively consents to the overdraft service, the institution pays overdrafts at its discretion. ◀

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#### ▶ Section 205.19—Debit Holds

##### 19(a) General Rule

1. *Transactions for which the actual transaction amount can be determined shortly after authorization.* Examples of transactions involving a hold in connection with a debit card transaction for which the actual transaction amount can be determined within a short period of time after authorization is obtained include:

- i. A fuel purchase at a pay-at-the-pump dispenser.
- ii. The payment of a restaurant bill where an estimated amount is added to the amount of the requested authorization to account for service tips.

2. *Additional reasons for overdraft.* Section 205.19 does not limit a financial institution from assessing an overdraft fee or charge for paying a particular transaction pursuant to the institution's overdraft service if the consumer would have incurred an overdraft for other reasons, such as a prior debit card transaction that may have been authorized but not yet presented for settlement or if a deposited check is returned.

3. *Waiver of overdraft fees caused by debit holds.* A financial institution does

not violate § 205.19 if it promptly waives or refunds any overdraft fees or charges assessed to the consumer's account caused by a debit hold in excess of the actual amount of the transaction. For example, assume that a consumer has \$50 in a deposit account. An institution does not violate § 205.19 if it assesses an overdraft fee on the consumer's account as a result of a \$75 hold placed in connection with a pay-at-the-pump fuel transaction, but promptly waives or refunds the overdraft fee after determining that the consumer has only purchased \$40 worth of fuel. The institution may not require the consumer to provide notice or other information that an overdraft fee was caused by a debit hold on funds in the consumer's account before the institution waives or refunds the fee.

4. *Example of prohibition in connection with a debit hold placed for same transaction.* A consumer has \$50 in a deposit account and is enrolled in a financial institution's overdraft service. The consumer makes a fuel purchase using his debit card. Before permitting the consumer to use the fuel pump, the merchant obtains a pre-authorization hold for \$1 to verify that the consumer's account is valid. The institution increases the amount of the hold to \$75, or the maximum amount it guarantees to the merchant for the authorized transaction under card network rules. The \$75 hold exceeds the consumer's funds. The consumer purchases \$20 of fuel. Under these circumstances, the financial institution is prohibited from assessing a fee or charge in connection with the debit hold because the overdraft would not have occurred but for the excess amount of the debit hold. However, if the consumer had purchased \$60 of fuel, the institution could assess a fee or charge for an overdraft because the transaction exceeds the funds in the consumer's account.

5. *Example of prohibition in connection with a debit hold placed for another transaction.* A consumer has \$100 in a deposit account and is enrolled in a financial institution's overdraft service. The consumer makes a fuel purchase using her debit card. Before permitting the consumer to use the fuel pump, the merchant obtains a pre-authorization hold for \$1, which the institution increases to \$75, or the maximum amount it guarantees to the merchant for the authorized transaction under card network rules. The consumer purchases \$20 of fuel, but the transaction is not presented for settlement for two days. The next day, the consumer withdraws \$75 at an ATM. Under these circumstances,

§ 205.19 prohibits the institution from assessing a fee or charge for paying an overdraft with respect to the \$75 withdrawal because the overdraft would not have occurred but for the \$75 hold.

6. *Example of prohibition when authorization and settlement amounts are held for the same transaction.* A consumer has \$100 in a deposit account and is enrolled in a financial institution's overdraft service. The consumer makes a \$50 fuel purchase using his debit card. Before permitting the consumer to use the fuel pump, the merchant obtains a pre-authorization hold for \$1, which the institution increases to \$75, or the maximum amount it guarantees to the merchant for the authorized transaction. The consumer purchases \$50 of fuel. When the merchant presents the \$50 transaction for settlement, it uses a different transaction code to identify the transaction than it had used for the pre-authorization, causing both the \$75 hold and the \$50 purchase amount to be temporarily posted to the consumer's account at the same time. As a result, the consumer's account becomes overdrawn. Under these circumstances, and assuming no other transactions, § 205.19 prohibits the institution from assessing a fee or charge for paying an overdraft because the overdraft would not have occurred but for the \$75 hold.

7. *Example of permissible overdraft fees in connection with a debit hold.* A consumer has \$100 in a deposit account and is enrolled in a financial institution's overdraft service. The consumer makes a fuel purchase using her debit card. Before permitting the consumer to use the fuel pump, the merchant obtains a pre-authorization hold for \$1, which the institution increases to \$75, or the maximum amount it guarantees to the merchant for the authorized transaction. The consumer purchases \$35 of fuel, but the transaction is not presented for settlement for two days. The next day, the consumer withdraws \$75 at an ATM. Notwithstanding the existence of the hold, the consumer's financial institution may charge the consumer an overdraft fee for the \$75 ATM withdrawal because the consumer would have incurred the overdraft even if the debit hold had been for the actual amount of the fuel purchase.

##### 19(b) Safe Harbor

1. *Example of two-hour safe harbor.* A consumer has \$100 in his deposit account and is enrolled in a financial institution's overdraft service. The consumer makes a \$35 fuel purchase using his debit card. Before permitting the consumer to use the fuel pump, the

merchant obtains pre-authorization hold for \$1, which the institution increases to \$75, or the maximum amount it guarantees to the merchant for the authorized transaction. One hour after the transaction is completed, but before the transaction is presented for settlement, the consumer withdraws \$55 at an ATM. Notwithstanding the existence of the debit hold, the consumer's financial institution may charge the consumer an overdraft fee for the \$55 ATM withdrawal even though the overdraft was caused by the hold, because the institution has procedures and practices to release the hold within two hours and the ATM withdrawal occurred within the two-hour safe harbor period.

*2. Relationship between § 205.17 and § 205.19.* If a consumer is not enrolled in the institution's overdraft service for ATM withdrawals and one-time debit card transactions (because the consumer has opted out or not opted in), the institution may not assess any fees or charges to the consumer's account for paying a debit card overdraft even if the institution is not otherwise prohibited from doing so by the debit hold provision in § 205.19. For example, assume a consumer has \$100 in her deposit account and has opted out of the institution's overdraft service. The consumer uses her debit card to purchase \$30 of fuel at a pay-at-the-pump fuel dispenser. At the time of authorization, the financial institution

increased the gas station's \$1 preauthorization hold to \$75. One hour after completing the fuel purchase, the consumer makes a \$60 debit card purchase at a grocery store. Notwithstanding the fact that the consumer made the purchase within the two-hour safe harbor, the institution would not be permitted to assess an overdraft fee because the consumer had opted out of the institution's overdraft service. ◀

By order of the Board of Governors of the Federal Reserve System, December 18, 2008.

**Jennifer J. Johnson,**

*Secretary of the Board.*

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