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A Closer Look: Overdraft and the Impact of Opting-In

1. **What is overdraft?** An overdraft happens when a consumer does not have enough available funds in her account to cover a payment or withdrawal and the bank or credit union pays the transaction. When the bank or credit union pays the transaction, the transaction is an overdraft and the account balance becomes negative (or "overdrawn"). Institutions typically charge per-transaction fees for overdrafts. The median overdraft fee among the retail banks that rank in the top 50 in terms of U.S. deposit market share is $34, while the median fee among a sample of smaller banks and credit unions is $31.[1]

   Alternatively, a bank or credit union could return a check or ACH transaction unpaid. Most institutions would then charge a "non sufficient funds" or NSF fee. The NSF fee is typically the same amount as an overdraft fee. Institutions generally do not charge NSF fees when declining to authorize a debit card-based transaction.

2. **How much do consumers pay in overdraft and NSF fees?** Overdraft and NSF fees constitute the biggest single cost for consumers of owning a checking account. The CFPB estimates that consumer overdraft and NSF fee revenues total as much as $17 billion annually. Bank revenue from consumer overdraft and NSF fees are 65.4% of all consumer deposit fees paid for those banks that report this revenue for the 12 months ending September 30, 2016. For these same banks, overdraft and NSF fees are 4.76% of bank net income before taxes and discontinued operations[2] for that same time period. Further, the CFPB estimates that close to 80% of what banks report as overdraft and NSF fee revenues are accounted for by overdraft

[1] Analysis of data obtained from Informa Research Services, Inc. (Dec. 2016), Calabasas, CA. www.informars.com. Although the information has been obtained from the various financial institutions, the accuracy cannot be guaranteed.

[2] "Discontinued operations" includes disposals of businesses that represent strategic shifts that have a major effect on an organization's operations and financial results.

fees.[3]

A small group of consumers pay most of these fees. In a given year, only 30% of consumers overdraw their checking account. The 8% of consumers who overdraft more than 10 times per year pay 74% of overdraft fees. These consumers are charged $380 in overdraft fees on average annually.[4]

3. **What does it mean when a consumer "opts in?"** A bank or credit union may not charge a fee when a consumer overdraws her account on a one-time debit card or ATM transaction unless the consumer has affirmatively consented (or "opted in") to fees on such transactions.[5] Consumers who have opted in can revoke their opt in at any time.

   If a consumer opts in, the consumer is charged an overdraft fee on an ATM or debit card transaction if, when the transaction settles and is posted to the consumer's account, there are insufficient funds in the account to cover the transaction.

   If the consumer does not opt in, the bank or credit union typically will not authorize any ATM or debit card transactions if there are insufficient funds at the time the transaction is authorized.

4. **How often do consumers make debit card payments or ATM withdrawals?** Over the last two decades, debit cards have become the most popular form of payment among consumers. The CFPB estimates that the average U.S. household made 6.3 debit card payments per month in 2000; in 2011, this number stood at 33.5 per month.[6] The CFPB further estimates that the average U.S. household made 5.5 ATM withdrawals per month in 2011.[7] In 2015, debit cards accounted for the largest share of U.S. non-cash payments and, at

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[3] CFPB, "Data Point: Checking Account Overdraft," (July 2014), available at http://files.consumerfinance.gov/f/201407_cfpb_report_data-point_overdrafts.pdf.

[4] Ibid.

[5] Regulation E requires banks and credit unions to obtain a consumer's affirmative consent before charging overdraft fees on debit card-based transactions.

[6] CFPB, "CFPB Study of Overdraft Programs: A White Paper of Initial Data Findings," (June 2013), available at http://files.consumerfinance.gov/f/201306_cfpb_whitepaper_overdraft-practices.pdf.

[7] Ibid.

about 60 billion transactions, were nearly twice as popular as credit cards.[8] The CFPB found that consumers averaged almost twice as many debit card transactions per month than all other forms of payment (check, ACH, ATM, teller, and other) combined.[9] The ratio was higher for consumers who were opted in than for consumers who were not. Consumers overdraw their accounts more often via debit card transactions than by any other means.[10]

5. **How many financial institutions offer consumers the option of opting in to debit card and ATM overdraft programs?** Most large banks[11] have overdraft programs and allow consumers to opt-in; however, several large institutions also offer a separate type of transaction account without overdraft. Sixteen percent of large banks do not allow ATM or debit card point-of-sale overdrafts.[12]

6. **How frequently do consumers opt-in?** For the first two years following the implementation of the rule requiring banks and credit unions to obtain consumer opt in to charge overdraft fees on debit card transactions, the average opt-in rate was 19.4% at large banks that offered opt-in, when taking a weighted average across portfolio accounts at these institutions.[13] However, opt-in rates vary considerably from institution to institution. As of the end of 2011, across all accounts at the banks with the highest opt-in rates, 24.8% of accounts were opted in, while at banks with the lowest opt-in rates, 7.4% were opted in. For recently-opened accounts (i.e., those opened after the implementation of the opt-in rule), the opt-in rate was 44.5% at banks with the highest opt-in rates and 13.2% at banks with the lowest opt-in

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[8] Federal Reserve Board, "The Federal Reserve Payments Study 2016," (Dec. 2016), at p. 12, available at https://www.federalreserve.gov/newsevents/press/other/2016-payments-study-20161222.pdf.

[9] Supra, note 3. Credit cards were not included in the forms of possible payment in this analysis.

[10] Supra, note 3.

[11] The term "large banks" is generally used here to refer to a sample of banks with $10 billion or more in total assets.

[12] The Pew Charitable Trusts, "Checks and Balances: 2015 Update," (May 2015), available at http://www.pewtrusts.org/~/media/Assets/2015/05/Checks_and_Balances_Report_FINAL.pdf?la=en. .

[13] Calculations using the same large bank data that were used in CFPB, "Data Point: Checking Account Overdraft," (July 2014), available at http://files.consumerfinance.gov/f/201407_cfpb_report_data-point_overdrafts.pdf.

rates.[14] The difference in opt-in rates may result from variations in marketing approaches or customer preferences across institutions.

7. **What is the impact to consumers of opting in to debit card and ATM overdraft?**
Consumers who opt-in to debit card and ATM overdraft risk paying more overdraft fees. This risk is higher for consumers that routinely have low account balances. The CFPB was able to better understand this impact by comparing the overdraft and NSF fees paid by consumers before and after implementation of the rule that required financial institutions to obtain opt-ins before charging overdraft fees on one-time debit card and ATM transactions. Among those consumers who had more than 10 overdrafts or NSFs in the first half of 2010, those who chose NOT to opt in saw their annual overdraft and NSF expenses drop by around $350 relative to those who opted in.[15]

The CFPB found that consumers who opted in pay more fees than consumers who do not opt in. Specifically, opted-in consumers paid on average $22 per month in overdraft and NSF fees while non-opted-in consumers paid on average $3 per month.[16] Opted-in consumers averaged 7.78 overdrafts per year while non-opted-in consumers averaged just 1.99 overdrafts.[17] Nearly one-in-five (17.8%) of opted-in consumers overdrew their account more than 10 times per year, compared to just 5.9% of consumers who did not opt in.[18] Relatedly, the CFPB found that debit card and ATM transactions accounted for 70% of all overdraft fees among opted-in consumers.[19] Had the same consumers chosen not to opt in, they likely would have avoided these fees, but some of the purchases or withdrawals that overdrew their accounts would have been declined by the institution at the point of sale or at the ATM since institutions typically only authorize payment or withdrawal attempts that would take the account's balance negative at the time of the authorization for accounts that are opted-in.

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[14] Supra, note 6.

[15] Supra, note 6.

[16] Supra, note 3.

[17] Supra, note 13.

[18] Supra, note 3.

[19] Supra, note 13.

Finally, opted-in consumers are more likely than consumers not opted in to have their accounts involuntarily closed in a given year due to unrecovered negative balances (6.2% vs. 2.5%).[20]

[20] Ibid.