Testimony of Kenneth W. Edwards
Center for Responsible Lending

Before the Public Meeting Panel
of the Federal Reserve Board

September 20, 2011

Good morning members of the Panel. Thank you for the opportunity to participate in this public meeting.

I serve as Policy Counsel at the Center for Responsible Lending (CRL), a nonprofit, nonpartisan research and policy organization dedicated to protecting homeownership and family wealth by working to eliminate abusive financial practices. Predatory lending, whether in the form of abusive subprime mortgage loans, payday loans, or overdraft fees, strip billions of dollars in wealth from low-wealth families and communities in the U.S. each year.

CRL is an affiliate of Self-Help, a nonprofit community development financial institution. For thirty years, Self-Help has focused on creating asset-building opportunities for low-income families, primarily through financing safe, affordable home loans.

I. Introduction and Summary.

CRL has done extensive research and policy work addressing checking account overdraft practices that cause significant harm to bank customers. We are concerned that Capital One's current overdraft practices are out of step with significant reforms other large institutions have recently implemented. These practices include continuing to charge high overdraft fees on debit card point-of-sale and ATM transactions, and posting transactions in order from largest to smallest, which maximizes overdraft fees. While other large banks have curbed these practices, Capital One has not.

This is particularly concerning in light of ING Direct's overdraft practices, which are industry leading and have earned the respect of the bank's customers and consumer groups. ING Direct does not charge high-cost overdraft fees. Instead, its customers are offered an overdraft line of credit, at a reasonable annual percentage rate, currently 11.25%,[1] with no additional fees. This responsible and fair program should be preserved.

[1] ING Direct, http://helpcenter.ingdirect.com/ingd/Topic.aspx?category=C3BNKEOOLD (last visited Aug. 18, 2011).

II. High Cost Overdraft Programs Cause Serious Financial Harm and Drive Customers Out of the Banking System.

High-fee overdraft loans cost Americans billions of dollars each year.[2] Overdrafts frequently are triggered by small debit card transactions, which could easily be declined at no cost when the account lacks sufficient funds.[3] Most institutions offer far lower cost alternatives, but too many institutions aggressively steer customers to their highest cost overdraft coverage.[4]

The FDIC's recent overdraft guidance acknowledged that repeat overdraft fees can result in "[s]erious financial harm" for "customers with a low or fixed income."[5] Some customers pay at least as much as $1,600 annually in overdraft fees;[6] the large majority of fees are paid by those who are overdrawn repeatedly and who are least able to recover from them.[7]

High-cost overdraft fees erode the assets of bank customers and, rather than promoting savings, make checking accounts unsafe for many them. Bank fees are the leading cause of involuntary bank account closures, driving many vulnerable consumers from the

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[2] *See* Leslie Parrish, *Overdraft Explosion: Bank fees for overdrafts increase 35% in two years,* Center for Responsible Lending (Oct. 6, 2009) (hereinafter *Overdraft Explosion*), *available at* http://www.responsiblelending.org/overdraft-loans/research-analysis/crl-overdraft-explosion.pdf.

[3] *See* 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*, Center for Responsible Lending, at 25 (Jan. 25, 2007) (hereinafter *Debit Card Danger*), *available at h*ttp://www.responsiblelending.org/overdraft-loans/research-analysis/Debit-Card-Danger-report.pdf.

[4] *See* Center for Responsible Lending Research Brief, *Banks Collect Opt-Ins Through Misleading Marketing*, April 2011 (hereinafter *Banks Collect Opt-Ins Through Misleading Marketing*), *available at* http://www.responsiblelending.org/overdraft-loans/policy-legislation/regulators/banks-misleading-marketing.html; Center for Responsible Lending Research Brief, "Banks Target, Mislead Consumers As Overdraft Deadline Nears," Aug. 5, 2010, *available at* http://www.responsiblelending.org/overdraft-loans/research-analysis/Banks-Target-And-Mislead-Consumers-As-Overdraft-Dateline-Nears.pdf.

[5] FDIC Supervisory Guidance for Overdraft Protection Programs and Consumer Protection, FIL-81-2010 (Nov. 24, 2010) (hereinafter *FDIC 2010 Guidance on Overdraft Programs*).

[6] FDIC Study of Bank Overdraft Programs (Nov. 2008) at iv. Note that this study included only FDIC-supervised banks, whose average overdraft fees at the time were $27 (*Id.* at v), compared to the average $34 fee that consumers overall paid at that time (*Debit Card Danger* at 8). This $34 average is influenced heavily by the fees charged at the largest banks, whose fees have averaged $34-$35 for several years. As a result, the FDIC's study may understate the amount that many bank customers pay annually in overdraft fees.

[7] Research from the FDIC, consistent with CRL's research, has found that account holders who overdrew their accounts five or more times per year paid 93 percent of all overdraft fees. FDIC Study of Bank Overdraft Programs at iv. Two CRL surveys, conducted in 2006 and 2008, found that 71 percent of overdraft fees were shouldered by only 16 percent of respondents who overdrafted, and those account-holders were more likely to be lower income, non-white, single, and renters when compared to the general population. Respondents reporting the most overdraft incidents were those earning below $50,000. Leslie Parrish, "Consumers Want Informed Choice on Overdraft Fees and Banking Options," CRL Research Brief (Apr. 16, 2008), *available at* http://www.responsiblelending.org/overdraft-loans/research-analysis/final-caravan-survey-4-16-08.pdf.

banking system, leading to greater numbers of unbanked households[8]—an outcome clearly inconsistent with the safety and soundness of financial institutions. By making these loans, banks also harm legitimate lenders and other legitimate businesses by putting themselves first in line for payment of debt and leaving their customers financially worse off.

III. Capital One's Overdraft Practices Are out of Step with Significant Reforms That Other Large Institutions Have Recently Implemented.

Other large financial institutions have discontinued charging overdraft fees on debit card transactions.[9] Bank of America and Citibank do not assess such fees on debit card transactions. These banks either decline debit card transactions that would overdraw the account—at no cost to the customer—or link the checking account to a savings account or a line of credit.[10] In announcing its decision to end debit overdraft fees, a Bank of America executive stated, "What our customers kept telling me is 'just don't let me spend money that I don't have'. . . ."[11]

Capital One, however, continues to charge overdraft fees on debit card transactions.

Also in recent months, some large banks have begun to process transactions chronologically or in order from lowest to highest to reduce the number of overdraft fees

[8] Overdraft fees are a significant reason that individuals who had bank accounts at one time are no longer banked. The FDIC's National Survey of Unbanked and Underbanked Households, FDIC (December 2009) found that one-third of previously banked households no longer had an account because they felt the cost was too high, including minimum balance requirements, overdraft fees, and other service charges. A survey in the Detroit area found that among those surveyed who formerly had a bank account, 70 percent chose to close the account themselves, citing moving, worrying about bouncing checks, and excessive fees as their reasons for closing the account. The remaining formerly banked, 30 percent, reported that their bank closed their account; the primary reason was bounced checks and overdrafts. Michael S. Barr, University of Michigan Law School, *Financial Services, Savings and Borrowing Among Low- and Moderate-Income Households: Evidence from the Detroit Area Household Financial Services Survey* (Mar.30, 2008). *See also* Dennis Campbell, Asis Martinez Jerez, and Peter Tufano, *Bouncing Out of the Banking System: An Empirical Analysis of Involuntary Bank Account Closures*, Harvard Business School (Jun. 6, 2008) (noting that virtually all involuntary bank account closures, when the financial institution closes a consumer's account, occur because the customer overdrew the account an excessive number of times).

[9] *See* Center for Responsible Lending Research Brief, *Debit Card Overdraft Abuse Continues*, Mar. 15, 2011 (hereinafter *Debit Card Overdraft Abuse Continues*), *available at* http://www.responsiblelending.org/media-center/press-releases/archives/Debit-Card-Overdraft-Abuse-Continues.html.

[10] *See Debit Card Overdraft Abuse Continues; see also* Bank of America Overdraft Protection, Frequently Asked Questions, http://www.bankofamerica.com/deposits/checksave/index.cfm?template=lc_faq_overdraft#question3 (last visited Sept. 14, 2011); Citibank Overdraft protection at-a-glance, https://online.citibank.com/US/JRS/pands/detail.do?ID=OverdraftProtect (last visited Sept. 14, 2011).

[11] Andrew Martin, *Bank of America to End Overdraft Fees*, N.Y. TIMES, Mar. 9, 2010, *available at* http://www.nytimes.com/2010/03/10/your-money/credit-and-debit-cards/10overdraft.html?pagewanted=print.

charged. Capital One, however, continues to post its customers' transactions, within each transaction type, in order from largest to smallest.

The proposed merger would make Capital One the fifth-largest financial institution, in the U.S. It would also propel the bank into a more influential position as a standard setter for the industry. As a result, safeguards should be put in place to ensure the preservation of ING Direct's model program as well as to encourage improvements in Capital One's current practices.

Thank you.