CUNA & Affiliates

Credit Union National Association, Inc.
601 Pennsylvania Avenue NW
South Building, Suite 600
Washington, D.C. 20004
(202) 638-5777

TESTIMONY
OF
RODNEY STAATZ
PRESIDENT AND CEO
STATE EMPLOYEES CREDIT UNION OF MARYLAND
ON BEHALF OF
THE CREDIT UNION NATIONAL ASSOCIATION
BEFORE THE
COMMITTEE ON FINANCIAL SERVICES
UNITED STATES HOUSE OF REPRESENTATIVES

OCTOBER 30, 2009

"THE OVERDRAFT PROTECTION ACT OF 2009"

TESTIMONY
OF
RODNEY STAATZ
PRESIDENT AND CEO
STATE EMPLOYEES CREDIT UNION OF MARYLAND
ON BEHALF OF
THE CREDIT UNION NATIONAL ASSOCIATION
BEFORE THE
COMMITTEE ON FINANCIAL SERVICES
UNITED STATES HOUSE OF REPRESENTATIVES

OCTOBER 30, 2009

"THE OVERDRAFT PROTECTION ACT OF 2009"

Mr. Chairman, Ranking Member Bachus, Members of the Committee, thank you very much for the invitation to testify before the Committee today to express the views of the Credit Union National Association (CUNA)[1] on the Overdraft Protection Act of 2009. My name is Rod Staatz and I am President and Chief Executive Officer of State Employees Credit Union of Maryland (SECU).[2] I am also a member of CUNA's Board of Directors.

The Impact of Proposed Overdraft Legislation

CUNA strongly supports the ability of credit unions to offer overdraft protection plans as a means to help their members resolve short-term financial problems. While the terms of credit union overdraft protection programs may vary, they are structured to help to pay, rather than return, non-sufficient funds transactions in exchange for fees that are similar to those charged for returned items. This spares members the embarrassment of returned checks, as well as additional fees charged by merchants and other payees. Such programs, when used appropriately by consumers, serve as a valuable back-up to overdrawing checking accounts or relying on payday lenders or check-cashing businesses, and are fully consistent with the philosophy and principles of the credit union system.

However, CUNA recognizes concerns exist about how some overdraft protection programs operate and is sympathetic to Congressional interest in enacting a law to address abusive

[1] CUNA is the nation's largest credit union advocacy organization representing nearly 90% of America's 8,000 state and federally chartered credit unions and their 90 million members.
[2] Founded in Baltimore in 1951, SECU is the largest credit union in Maryland and serves 248,000 members. SECU's total assets were $2.06 billion as of June 2009.

practices. CUNA is convinced that the provisions in H.R. 3904, particularly the provisions that would limit the number of overdraft fees that could be charged per month and per year, would simply end overdraft programs -- to the detriment of many consumers who truly value these programs. Consumers will incur more non-sufficient fund (NSF) fees with none of the benefits of having many transactions honored. They will pay more merchant return check fees and have more bad checks reported to consumer reporting agencies. Merchants will deal with more bounced checks and have more bills that are currently paid under automated bill-paying services rejected. Inevitably, other adjustments will be made in checking account services and maintenance fees that will impact a wide range of accountholders. All consumers lose under this scenario.

Credit Unions' Best Practices

While there is certainly an exception to every rule, we believe most credit unions approach overdraft protection in a manner that is in the best interest both of the individual member using the service as well as the overall membership of the credit unions, who put their own money behind the program.

Several years ago, CUNA's Board of Directors adopted policy calling on every credit union that is a member of CUNA and offering overdraft protection services to adopt overdraft protection standards and ethical guidelines to emphasize credit unions' consumer-orientation. Our policy states:

> *Credit unions recognize that the following practices are not consistent with the credit union philosophy and principles and publicly affirm that they will not engage in any of these practices:*
>
> - ***Deceptive Advertisement***
>
>   *Advertising, representing, or implying that the member should expect that all overdrafts will be paid but then stating in other documents that the paying of overdrafts is discretionary, which is a standard feature of overdraft protection plans. Such advertising may lead members to rely on the service in expectation that all overdrafts will be paid, which would be detrimental if any overdrafts are not ultimately paid by the financial institution.*

- ***Enticing Members to Overdraw Accounts Repeatedly***
  Advertising or promoting the overdraft protection plan in a manner that encourages the member to overdraw repeatedly his or her share draft account, ***as opposed to*** *such a plan being used as an occasional convenience for the member. The frequent overdraw of accounts is a practice that financial education programs, such as those offered by credit unions, generally discourage.*

- ***Structuring Programs that Mislead Members***
  Including a feature that records the amount of coverage being offered to cover overdrawn share drafts as part of the "available funds," such as on ATM receipts, online statements and telephone balance statements.

- ***Failure to Inform Heavy Users of Overdraft Protection Programs of Alternatives***
  Overdraft protection programs may not be appropriate for members who heavily use and rely on overdraft protection programs as a means to pay a significant proportion of every day living expenses. For these members, credit unions may offer a number of other products and services that would be more appropriate. These may include transfers from a savings account to the share draft account, as well as other types of less expensive secured and unsecured loans that the credit union offers to all its members.

- ***Failure to Provide Financial Counseling Information***
  Credit unions recognize that they have a role in helping their members use overdraft protection services in a responsible manner. In addition to providing adequate disclosures regarding the features and fees associated with the programs, credit unions should also provide information regarding counseling services provided by the credit union or other reputable counseling services.

SECU's Overdraft Program

Mr. Chairman, please allow me to describe how SECU's overdraft protection program, "Courtesy Pay," works. The objective of Courtesy Pay is to permit members to have many transactions completed even when they lack sufficient funds in their checking accounts and to spare them from merchant and collection agency fees incurred for returned checks. Courtesy Pay is <u>not</u> factored into available balances for approval of debit card, ATM or teller transactions. I am sure that many elements of my program are similar to overdraft programs used by credit unions throughout the United States.

Here is how our program works. A member can pre-arrange to have funds drawn from a selected savings account or establish a line of credit, and if he or she writes a check without enough funds in his checking account, the necessary funds are automatically drawn from the other account or line of credit. There is no fee for this overdraft service. Courtesy Pay for qualified members allows SECU to pay an item after all other funds from a member's accounts have been exhausted or a pre-arrangement transfer plan has not been established.

SECU covers the necessary amount up to the member's Courtesy Pay limit established by SECU ($500, $750, $1,000 depending on the member's standing.) The member's checking account is debited that amount plus a $27 fee. The member is sent a non-sufficient funds notice explaining that the account is negative and a deposit is required to bring the account to a positive status. If the account is not positive within 30 days, all future items will be returned "NSF" with a $27 NSF fee assessed.

SECU does not allow members to draw their balance into the negative at the teller line, ATM, or through their debit card. Courtesy Pay only pertains to written checks and approved ACH debits.

SECU does not market Courtesy Pay because we do not want to encourage members to live beyond their means -- knowing Courtesy Pay is an option to cover overdrafts may lead them to view it as available funds. Approximately 90% of our members qualify for Courtesy Pay. To be eligible, the account must be open for at least 30 days, and the member must be in good standing with no current delinquencies and no previous charge-offs.

Guidelines for Refunds

If a member contacts SECU for a fee refund, we review the account and consider the specific circumstances. SECU makes full fee refunds without question if the fee was assessed through a SECU error or if the member is in good standing and has had no non-sufficient funds/overdraft refunds in the past.

If the member is in good standing with unusual circumstances that warrant a refund of some kind, we consider a full or partial refund based on the member's situation. Examples include a job loss, merchant holds, deposit holds, a single mathematical error that triggers a series of incoming items to create overdrafts, and payday lending where lenders repeatedly withdraw from the account. Additionally, we refer them to free financial counseling.

Program Abuse

SECU monitors overdraft protection abuse. Even those members who honor the terms of our agreement to restore their balance to a positive balance within 30 days but demonstrate repeated overdraft behavior will have progressive notification from warnings to account closure for overuse of Courtesy Pay. In 2008, SECU closed 486 checking accounts for abuse.

Why Overdraft Programs Assist Working America

While we have several concerns with H.R. 3904, our primary concern is the provision that limits the number of overdrafts that can be provided by a credit union to a member. H.R. 3904 prohibits a credit union from charging more than one overdraft fee per month and no more than six in a calendar year per transaction account.

Any arbitrary limit would basically end credit unions' overdraft programs and cause member dissatisfaction and even potential hardships. Overdraft fees are obviously assessed both because covering an overdraft is a service and because the fee is there to control overuse of the service. Members cannot necessarily predict when they will need the help – what if they already incurred an overdraft fee early in the month and then needed our Courtesy Pay to help cover the car payment due later in the month?

I can give you many examples of how the SECU Courtesy Pay program is of value to our membership everyday. But when a smaller credit union yesterday heard I was testifying, it sent me an email, imploring that I make a strong case to Congress about how important overdraft programs are to credit union members. So while I can give you similar examples from SECU's file, let me share some real world examples that credit union sent to me, a credit union with 18,000 members who are mostly blue- collar workers and their families:

1. A scenario that arises time and again is the member using the overdraft program so the rent check doesn't bounce, which avoids late payment fees and possible problems with the landlord.
2. An elderly member who received her Social Security check early in the month used the overdraft program to pay her electric bill.
3. A few days before payday, a member's child got sick and funds were low in her account, but she could cover the cost of the doctor's visit by relying on the overdraft program.
4. A similar example was provided about the member who needed to rely upon the overdraft program to buy groceries for the family before payday.
5. A member used the overdraft program to make his car payment when his checking account was a little short of what was owed, which prevented a late payment fee and a report to the credit bureau for being 30 days late.
6. And a member who had opted out of the overdraft protection service -- certainly something allowed by credit unions – called back a few weeks later and wanted to resume the overdraft protection service, deciding that it wasn't worth paying NSF fees to the credit union plus the returned check charge to merchants.

As these examples show, overdraft programs at credit unions are there primarily to serve working America, the people who basically live paycheck to paycheck. To put arbitrary limits on overdraft programs offered by depository institutions will only undermine these programs and drive people to alternative money providers who will undoubtedly charge more.

Merits of a Regulatory Approach

Instead of the legislation before the Committee, CUNA strongly believes that concerns should be addressed through the federal regulatory system, which allows for a notice-and-comment process to evaluate what regulations may be appropriate and to hopefully protect from unintended consequences of federal restrictions on overdraft programs. We note that just over a week ago, the Committee approved legislation to create a robust federal consumer protection regulator, which would have the authority to promulgate rules governing overdraft protection programs. Moreover, the Federal Reserve and other banking regulators, which currently have the authority to issue these rules, have rulemaking processes underway which address key concerns with overdraft programs.

The periodic statement disclosure requirement proposed in Section 4 of H.R. 3904 is already scheduled to go into effect on January 1, 2010. The Federal Reserve Board (Regulation DD) and the National Credit Union Administration (NCUA) (Section 707) earlier this year amended their implementing regulations to the Truth in Savings Act to require the dollar amounts charged for overdraft fees and returned item fees, both for the month and year-to-date, to be disclosed on the periodic statements of transaction accounts, starting nine weeks from now. Currently, only financial institutions that advertise or otherwise promote their payment of overdrafts are required to provide these disclosures. I should add that SECU does not market our overdraft Courtesy Pay program because we do not want to encourage members to live beyond their means – knowing that there is an option to cover overdrafts may lead them to view it as available funds. We think disclosure of dollars spent, rather than the proposed disclosure of the fee as a "finance charge" under the Truth in Lending Act (TILA) is of more practical meaning to the consumer.

Another Truth in Savings amendment effective January 1, 2010 mandates that financial institutions providing account balance information through an automated system only disclose the amount of funds available for withdrawal *without* including the additional funds that would be available under an overdraft program. We believe this new regulatory requirement is what will be expected under Section 4 of the bill on "Exclusion from Account Balance Information." Even without this regulatory mandate, available checking balances at SECU do not reflect availability of courtesy pay amounts.

A third possible change to overdraft programs is under active consideration by the Federal Reserve using its Regulation E implementing authority of the Electronic Funds Transfer Act. In its January 2009 proposal, the Federal Reserve outlined two approaches for providing consumers a choice regarding the payment of ATM and one-time debit card overdrafts by their financial institutions, asking for comments on which approach should be adopted by regulation. Under an "opt out" approach, an institution would be prohibited from imposing an overdraft fee unless the accountholder is given an initial notice and a reasonable opportunity to opt-out of the overdraft service, and the consumer does not opt out. Under the "opt in" approach, the institution would be prohibited from imposing an overdraft fee if it chooses to pay an overdraft unless the accountholder affirmatively consents to the overdraft service.

In CUNA's comment to the Federal Reserve last spring, we generally supported action in this area if limited to ATM and one-time debit services. If an opt-in approach were to be adopted, CUNA strongly urged the Fed to permit financial institutions to continue to use an opt-out system for existing accounts. CUNA raised many other operational concerns and considerations in our comment letter on implementing possible new Regulation E requirements on overdraft programs. This proposal provides a good example of why the regulatory process, not the legislative process, should be used to address consumer disclosures and protections.

In 2005, NCUA and the other federal financial institution regulators issued guidelines on overdraft protection plans that addressed safety and soundness considerations, legal risks and best practices. These guidelines are still in effect, and attached to this testimony is a two-page chart that summarizes the agencies' best practices and SECU's Courtesy Pay program. I feel our program measures very favorably to what the regulators have laid out in their guidelines and provides a valuable service to our membership.

CUNA is uncertain about what other TILA requirements may be triggered if overdrafts are brought under TILA and Regulation Z, something that needs further analysis. While we are certainly pleased that the bill's sponsors acknowledge the problem that would be created for federal credit unions without an exception to the federal usury ceiling (Section 3 in the bill), we strongly believe that overdraft protection programs are not lending programs but rather are accommodation services provided at the discretion of the credit union, not based on any loan underwriting standards CUNA continues to believe that overdraft programs are appropriately regulated by Truth in Savings rules.

Additional Credit Union Concerns Regarding H.R. 3904

Prompt Notification

H.R. 3904 would require prompt notification of the consumer when an overdraft occurs including the date of the transaction, the type of transaction, the overdraft amount, the overdraft coverage fee, the amount necessary to return the account to a positive balance, and whether the participation of the consumer in the program will be terminated if the balance is not returned to positive within a given period of time. The bill requires the credit union to use a notification method requested by the consumer.

Credit unions would have significant concern with any requirement for same-day or "real time" notification of an overdraft occurrence given the fact that many of them do not have the technological capacity to provide such a notification to their members in a short period of time.

Additionally, while larger financial institutions may have a greater capacity to provide this type of notification via email or text messaging, we are concerned that credit unions would not be able to provide this type of notification. Moreover, there would increased burden associated with keeping track of which members want which types of notification.

ATM Notification

H.R. 3904 would require credit unions to warn consumers at ATM machines if the transaction would trigger overdraft coverage fees and provide the consumer the opportunity to cancel the transaction. While this provision would appear to be well-intentioned, we do believe that this requirement would represent a compliance burden that we do not believe can be met given current technology and the structure of the payment system.

There are other ways to notify consumers that the transaction that they are about to complete may cause an overdraft event. A "sticker" on the side of any ATM – which has been used in the past for other warnings – or a first screen general notice alerting the consumer that a withdrawal from the ATM may trigger an overdraft fee by his own institution, may be appropriate notice for consumers. At some point, however, we do think the consumer has the responsibility to know how much money he has in his checking account. We are also mindful of the fact that there is no warning given when a consumer writes that check which puts him in an overdraft position.

Treatment of Debit Holds

H.R. 3904 would prohibit charging an overdraft fee on any transaction if the overdraft results solely from a debit hold that exceeds the actual dollar amount of the transaction. The significant problem with debit holds is that financial institutions have little control over the holds placed by merchants and are unable to determine the exact amount of the transaction or control how long the hold is in place. We believe merchants should be subject to additional rules that require them to submit debit card transactions promptly for settlement as this will significantly reduce the overall amount of overdraft fees that are assessed as a result of debit holds.

Government Accountability Office Study

The Committee will undoubtedly hear conflicting information with respect to consumer opinion of overdraft protection programs. We encourage Congress to ask the Government Accountability Office to study consumer opinion with respect to these programs, specifically if consumers prefer overdraft protection services to having their checks bounce and other debits denied.

Conclusion

Mr. Chairman, credit unions generally agree that consumers of financial products—especially those consumers of financial products provided by for-profit and unregulated entities—need greater protections. That is why we have said for the last several months that a consumer financial protection agency *could* be a good way of providing those protections; however, in order for such an agency to work, consumer protection regulation must be consolidated and streamlined. For the better part of the last two decades, many of the consumer protection statutes that Congress has enacted actually resembled regulations, in terms of level of specificity. While we do not believe that H.R. 3904 should become law under any circumstances, the bill is another example of Congress attempting to legislate a question that may be better answered by a regulator responsible for consumer protection working in conjunction with a safety and soundness regulator.

Mr. Chairman, thank you very much for the opportunity to testify at today's hearing. I look forward to answering questions from the Members of the Committee.

Comparison of SECU to Federal Financial Institution Regulators' Guidance on Best Practices for Courtesy Pay

Best Practice	SECU Practice
Avoid promoting poor account management.	Discussion of no-fee options (savings overdraft, LOC) occurs at account opening and is repeated in every paid item notice. Three step NSF abuse program applied to members who carry YTD NSF counts of 20 or more for periods of 6, 9 and 12 months.
Fairly represent overdraft protection programs and alternatives.	Every paid item notice includes the message "Avoid NSF fees – apply for a line of credit or use savings for overdraft protection on your account" with the corresponding phone number and web address for application.
Train staff to explain program features and other choices.	No-fee options are explained consistently at account opening. SECU does not promote Courtesy Pay; however staff are trained to explain the program features in response to member inquires.
Clearly explain discretionary nature of program.	SECU does not represent that the payment of items is guaranteed. Courtesy Pay is a privilege.
Distinguish overdraft protection services from "free" account features.	SECU does not market Courtesy Pay as part of free services.
Clearly disclose program fees.	Overdraft/Non-Sufficient Funds/Uncollected Funds (whether paid or not paid) = $27. Disclosed on fee schedule provided to all members at account opening.
Clarify that fees count against the disclosed overdraft protection dollar limit.	SECU has standard limits ranging between $500 and $1,000 based upon account type. SECU does not disclose the limits as to not promote the program and the ability to utilize the limits. Therefore we do not clarify that the fees count against the disclosed overdraft protection limit. Yes, both the dollar amount of the item and the associated fee are combined to count towards the dollar limit.
Demonstrate when multiple fees will be charged.	Each overdraft occurrence incurs one fee. There are no multiple fees.
Explain impact of transaction clearing policies.	SECU does not currently disclose the process or the impact of transaction clearing policies.
Illustrate the type of transactions covered.	Yes, we disclose that Courtesy Pay covers in-clearing checks and previously approved ACH debits only.
Provide election or opt-out of service.	Opt out service is offered.
Alert consumers before a transaction triggers any fees.	Courtesy Pay is NOT considered for approval of electronic transactions (card purchases and ATM withdrawals) or for cashing over the counter checks in branches. It is therefore impossible for the member to accidentally trigger fees in situations where advance notification could be provided.
Prominently distinguish balances from overdraft	The amount of overdraft protection is not included in checking available balance. Available checking balances do not reflect

Best Practice	SECU Practice
protection funds availability.	savings balances, available Line of Credit or available courtesy pay amounts. Knowing Courtesy Pay is an option to cover overdrafts may lead members to view it as available funds.
Promptly notify consumers of overdraft protection program usage each time used.	Daily notices are sent by mail and populated in online banking whenever a check and/or ACH debit triggers either a paid or returned NSF fee.
Consider daily limits on the consumer's costs.	We do not have a daily cap.
Monitor overdraft protection program usage.	SECU monitors overdraft protection abuse. For those who honor the terms of our agreement but demonstrate repeated overdraft behavior, we have three levels of progressive notification from warnings to account closure. Level 1: First letter is triggered when the member has carried 20 or more NSF's for six consecutive months. Member is warned that courtesy pay may be revoked with continued abuse. Level 2: Second letter is triggered when the member has carried 20 or more NSF's for nine consecutive months. The member's courtesy pay is revoked and the member is warned that their checking account will be closed with continued abuse. Level 3: Final letter is triggered when the member has carried 20 or more NSF's for twelve consecutive months. Account is reviewed and may be closed unless the member has had extenuating circumstances. In 2008, SECU closed 486 checking accounts for abuse.
Fairly report program usage.	SECU does not report negative information to consumer reporting agencies when the overdrafts are paid under the terms of the overdraft protection programs.