

New Fed Rules Limit Debit Card Overdrafts

Are the days of the pesky overdraft fee drawing to a close? The Federal Reserve announced new rules Thursday that would restrict banks' ability to charge fees on debit card transactions that would result in a negative balance.

The rules were not designed to bail out habitual check-bouncers. Rather, they were created to curb fees on everyday purchases – say, an ill-timed cup of coffee at **Starbucks** that ends up costing \$38 (or three in one day that end up costing more than \$100). “Because of these costs, consumer advocates contend that most consumers would prefer that their bank decline ATM or debit card transactions if the transactions would overdraw their account,” the Fed wrote.

But unless legislation currently making its way through Congress becomes law, consumers may be stuck paying for their mistakes. Without a law, overdraft fees – which average \$34, according to the Center for Responsible Lending -- will continue to pop up on bank statements and put consumers in a cycle of debt, says Ed Mierzewski, the consumer program director for the consumer advocacy U.S. Public Interest Research Groups.

The new Fed rules, which go into effect July 1, 2010, would prohibit banks from charging overdraft fees on A.T.M. withdrawals or purchases made using debit cards, unless customers opt into their overdraft protection programs.

Currently, the majority of banks (75%, according to a study of these programs by the Federal Deposit Insurance Corporation) enroll their customers automatically and give them the option to opt out.

But the Fed's rules come too little too late, Mierzewski says. The heat to address overdraft fees is already on the banking industry. Last month, Sen. Christopher Dodd (D., Conn.), who is the chairman of the Senate Banking Committee, introduced legislation that would require banks to implement an opt-in rule for overdraft programs and prohibit banks from manipulating the order in which they post transactions. Similar legislation has been introduced to the House of Representatives by Rep. Carolyn Maloney (D., N.Y.).

Bank of America and **JP Morgan Chase** announced changes to their overdraft programs in September, which included an opt-in requirement and limiting the number of overdraft fees charged each day. The Fed rules will make some of those changes a requirement for all banks, but they do not offer most of the other consumer protections embedded in the Dodd and Maloney's proposed legislation.

Here's what consumer protections the Fed rules introduce, and where they come up short:

1. Opt-in approach for ATM and debit-card transactions...

Banks will be required to provide new and existing customers with the right to opt in to the institution's overdraft service for ATM and one-time debit-card transactions.

2. ... but no such requirements for checks and recurring electronic payments

The assumption here is that because consumers typically pay by check when making larger purchases, they should be better able to plan these purchases and avoid overdraft fees, Mierzwinski says. Likewise for so-called ACH transactions, such as the automatic electronic payment of utility or other monthly bills set up by the consumer.

3. All customers must be treated equally

Banks are prohibited from offering better terms of service (say, accounts with lower fees or the same fees but more bells and whistles) for customers who opt in to their overdraft programs. So if the bank has a \$30 overdraft fee for checks, it cannot offer a \$20 fee for its opt-in customers only.

4. Banks cannot decline payment of checks or ACH transactions that overdraw accounts

So even if you do not opt into the bank's overdraft protection program, you will still be hit with an overdraft fee if a check or ACH payment causes an overdraft.

5. No action on debit-hold concerns

When a merchant places a hold on funds in a consumer's checking account (a common scenario for those using their debit cards to book car rentals, hotel rooms or even pay at the gas station), that debit hold may cause an overdraft on the consumer's account. But the Fed rules have not adopted the proposed provisions on debit holds, which would obligate financial institutions to address such concerns. According to the final rules document, "the Board believes that a more comprehensive approach that involves financial institutions, card networks, and merchants may be required to effectively address these problems. The Board will continue to monitor developments with respect to debit holds and assess whether to take further action."

6. No limit on the number of overdraft fees

The bills introduced by Dodd and Maloney would limit the number of overdraft coverage fees banks can charge to one per month and six per year. The Fed rules do not address that issue.