Overdraft Protection: An Overview of Practices and Disclosures Available to Consumers and Potential Implications for Family Financial Management

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Over the past few years bank fees have evolved as banking technology and services have changed the way many Americans take care of their financial business. Two fees in particular, overdraft protection fees and non-sufficient funds (NSF) fees, have changed significantly and have been brought to the attention of many. In their 2005 report, Consumer Federation of America (CFA) cited a Moebs Services analyst's estimate that consumers paid $33 billion in overdraft protection and NSF fees (Fox & Woodall, 2005). These fees are assessed in a variety of ways when a customer's check or debit is presented and the funds are not available. Not all consumers fully understand how the fees are assessed nor do they fully understand how these services might impact their daily resource management practices.

The purpose of this project is to look at the various types of overdraft fees associated with accounts available Athens, GA, a town of roughly 100,000 residents. This project explores many of the same issues as the CFA report. However, instead of looking only at the larger depository institutes, smaller local/community banks are included to determine if there are any significant differences in overdraft protection practices. Information was also collected from the bank's website, if one was available.

A total of ten banks were visited, four banks multi-state banking institutes and six banks located only in Athens or northeast Georgia. The four multi-state banks included are Bank of America, Regions Bank, SunTrust Bank, and Wachovia. Websites visited for these banks include personal banking pages on the following websites: www.bankofamerica.com, www.regions.com, www.suntrust.com, and www.wachovia.com. The six local/community banks included are Athens First Bank & Trust, Main St. Bank, First American Bank & Trust, Bank of Athens, National Bank of Georgia, and Oconee State Bank. Again, the banks' websites and personal banking pages were visited to gather additional information. These sites include: www.athensfirstbank.com, www.mainstreetbank.com, www.fabonline.com, www.bankathens.com, www.tnbg.net, and www.oconeestatebank.com.

At each bank, an account representative was asked several questions relating to available accounts and overdraft protection services. Promotional pamphlets were also collected from each branch to determine differences between information available for in-branch pick-up and information available online. Each account representative was asked about the available checking accounts and if fee schedules varied for each account. Nine banks offered some form of free checking with no monthly maintenance or usage fees. All banks offered some form of checking with monthly maintenance fees. Accounts often had slightly different fee schedules for varying services.

The next set of questions focused on how accounts were handled in the event that an item was presented and funds were not available in the account. All ten banks had some form of overdraft protection to keep from returning such items. Many banks offer what is considered traditional overdraft protection. Traditional overdraft services involve linking the checking account to either the individual's savings account with the bank, an approved credit card with the bank, or an approved line-of-credit (LOC) with the bank. Traditional overdraft protection is set up when opening accounts or it may be added to or dropped from the account at a later time. Other banks had what they called "bounce protection." Bounce protection services provide the account holder with a predetermined amount by which their account may be overdrawn to cover items being presented against their account. Often this bounce protection amount is added to the "funds available" balance an account holder would see when visiting the automated teller machine (ATM). Bounce protection is usually made available automatically after the account has been open for a certain time period. If the account holder does not wish to have this protection, they must opt-out with an account representative.

The four multi-state banks all provided the traditional overdraft protection. All banks provided the account holder with the option to link their account with their savings account. Three banks transferred amounts to cover the item in $100 increments, and one bank transferred the next full dollar amount needed to cover the transaction. Fees for this transfer ranged from $5 to $10 per transfer, with one bank having a maximum limit of one transfer per day. Three banks also allowed the account holder to have funds transferred from a preexisting credit card with the bank. These transfers become subject to the terms of the credit card. All four banks also allowed for transfers from pre-approved LOC accounts for a fee of $5 to $10. Each bank had their own specific procedures for these transfers; however, most LOC transfers resulted in immediate interest charges and were accompanied by automatic monthly payments from the checking account at the end of the month.

The six local/community banks provide a wide variety of overdraft protection services. Four banks offer the traditional overdraft service of linked savings accounts and LOC transfers as their multi-state counterparts. The terms of the transfer are much the same as the multi-state banks, with associated fees ranging from $5 to $10. Only two banks offer the linked credit card as an option. This is primarily due to the fact that these smaller local banks do not have their own in-house credit cards. Three banks offer the bounce protection services. The bounce protection permits items in excess of the funds available to clear and draw the account negative in amounts up to $300, $500, or $1,500, depending on the type of checking account. Each time this protection is utilized a fee, generally around $30, is assessed. Two of these banks offer both the bounce protection and traditional overdraft services.

Account representatives also were asked about instances in which traditional overdraft protection or bounce protection had been fully utilized. Would NSF items be returned to the merchant or would the account be overdrawn, possibly in addition to the bounce protection? At each bank, save one, the account representative indicated there was the possibility the item would be paid and an additional fee would be charged. In fact, most all banks indicated that debit card transactions would be processed and the account would be overdrawn. At two of the multi-state banks and one of the local/community banks, the decision to pay an NSF item and charge a fee to overdraw the account was made automatically by software programs (C. Conway and J. Mellow, personal communications, January 10, 2006). At one of the multi-state banks and five of the local/community banks, this decision is made in-house on a case-by-case process, usually based on the history of the account (L. Cooksey, T. Lanier, K. Nix, A. Revell, C. Ross, S. Viola, personal communications, January 10, 2006).

In addition to speaking with account representatives, the information available in pamphlets and on the banks' website was compared. All ten banks had a website and pamphlets with at least some basic information available about checking accounts offered. However, information on overdraft protection on the websites and in the pamphlets varied considerably. In total six banks, four multi-states and two local/community offered some information about overdraft protection on their websites. All four multi-state banks' and one local/community bank's websites included information on what overdraft protection is and how it works. In pamphlets available for pick-up in the lobbies, all but two local banks, mentioned overdraft protection. The pamphlets generally provide only a line item with the fee amount associated with the service.

There are many potential implications on family financial management associated with the above-mentioned overdraft practices. These practices may lead to significantly increased costs for any consumer who is not careful with their checking account. Consumer advocates are claiming overdraft fees associated with bounce protection or drawing an account negative represent a short-term loan and need to be covered by the same Truth-in-Lending Act as regular loans (Conrad, 2005). The interest rates on these short-term loans often equate to triple digit interest rates, considerably higher than any personal loan. The CFA report includes several policy recommendations for protecting consumers, including limiting assessed fees to the bank's actual costs and warning consumers when ATM or debit card transactions will pull the account negative (Fox & Woodall, 2005).

Consumers will also have to be more diligent with their checking accounts. If the trend becomes one such that smaller local/community banks all provide the bounce protection instead of traditional overdraft services, those who only have access to local/community banks will face higher costs associated with NSF items. These consumers will be responsible for asking their banks if available fund balances include the bounce protection and for remembering the additional funds are only an extension of credit. For those who struggle with day-to-day money management, seeking out educational resources might be warranted. Educators and community outreach partners ought to include in financial education programs, particularly money management sessions, information on specific options available for the community.

Another implication is that those who are not banking savvy may not find the most suitable account. They may not know what to look for or what questions to ask when opening a bank account. The responsibility of finding the banking institution and account that best suites the individual's needs now lies with the consumer. Finding the appropriate bank and product requires the consumer to understand what is offered as well as their financial needs. Some individuals may find the in-house decision-making more common in local banks better suits their needs because they have the occasional NSF item come through and would prefer the decision to be made on a case-by-case basis. However, some individuals may find the more traditional overdraft protection services more commonly offered at the multi-state banks work better for their financial management. Again, the burden of understanding the changes in banking is falling predominately on the shoulders of the consumer.

There are plenty of articles raising awareness about the evolving overdraft protection. A future area of study could be to determine if the differences between multi-state banks and local/community banks in the Athens area are also found in other small to mid-size towns. If so, do those most adversely affected by certain overdraft services have access to multiple banking options? The ever-changing banking industry greatly affects consumer financial management and it is imperative that consumers understand the options available to them.

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Endnotes

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