â€˜Opt inâ€™ to fairness on bank overdraft fees

by The St. Louis Post-Dispatch

Banks levy about $17.5 billion each year in fees for overdrawn accounts, whether by bounced check, debit card purchase, cash withdrawal from an ATM or electronic payments of bills. Thatâ€™s chump change compared to the hundreds of billions of dollars banks have received from various federal bailout programs.

But both are a product of greed run amok.

Bank customers are abused by fee structures that are as dishonorable as the AIG bonuses. But that may be about to change, thanks to rules changes being proposed by the Board of Governors of the Federal Reserve System. The board wants customers to be given the choice of signing up for overdraft programs, instead of being enrolled automatically and not given advance notice that a transaction will result in an overdraft and extra fee.

Banks charge $30 or more for each overdraft and design their programs to maximize the number of overdrafts. The most notorious practice: When clearing an account on a given day, banks debit the largest payments first â€” regardless of the chronological order of transactions.

Say a customer with $450 in her account withdraws $20 from the ATM; uses her debit card to make a $6 purchase at a fast-food restaurant; writes a $30 check to pay her light bill and then, thinking her paycheck has cleared, pays her rent with a $475 check. The bank debits the $475 first so that it can charge its customer four overdraft fees.

Banks sometimes are the direct cause of an overdraft by holding checks for unreasonably long periods before crediting them to the customersâ€™ accounts.

Banks say overdraft protection provides customers a valuable service, protecting their credit ratings and the embarrassment of a bounced payment. The reality, though, is that banks have chosen the most expensive and onerous means of providing such a â€œservice.â€•

If banks genuinely were interested in serving customers, they would steer customers toward linking overdrafts to a credit card account. But that would mean much less profit for the bank.

The Fed has proposed two options to deal with this problem:

â€¢ One would give customers the right to opt out of a bankâ€™s overdraft program. The bank would have to give customers clear notice of this right and how to exercise it before they could charge for any overdraft.

â€¢ The other would require that customers specifically opt-in to the overdraft program with full knowledge of the programâ€™s terms and fee structure.

The opt-in approach is by far superior. It makes customers take full responsibility for their decision, instead of letting the overdraft program take over by default.

But the opt-in option can improved. Banks should be denied overdraft fees on existing customersâ€™ accounts until the customers specifically opt in to the program. Banks also should be required to inform customers of less costly options for protecting accounts from overdrafts, such as linking them to a credit card. They should disclose the fact that an overdraft fee actually is a short term loan with interest rates that would make a loan shark blush.

Bank customers tired of being ripped off can have a say. The Fed is soliciting consumer comments on how best to reform the system. The deadline is March 30.

E-mail comments to regs.comments@federalreserve.gov. Put â€œDocket No. R-1343â€• in the subject line.