



Overdraft Fact Sheet

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(2010)

What is an overdraft?

An overdraft is a situation that occurs when a bank pays a transaction that a customer has authorized even though the customer doesn't have enough money in the account to cover it.

What is overdraft service?

Most banks will pay the overdraft as an accommodation, trusting that the customer will repay the amount of the overdraft. Usually, there is a fee associated with that service that varies depending on the bank.

Can customers avoid overdraft fees?

Yes. There are a number of options to avoid paying overdraft fees. Many banks allow customers to link their checking account to another account such as a saving account. In the case of an overdraft, the money would be taken from the other account. If eligible, customers can also link the checking account to an overdraft line of credit or a credit card account. Fees and interest are usually charged, but they are usually less than paying an overdraft fee. The easiest way to avoid overdrafts is to keep track of your transactions and balance. You are also less likely to overdraw if you keep extra money – a cushion -- in the account. Many banks will also offer to send you an alert by phone, email, or text message that your balance has fallen below an amount you established.

Why do banks pay overdrafts?

Banks pay overdrafts because studies have shown that people want important payments to be paid and they are willing to pay a fee for the service. Generally, people want important bills such as a mortgage or rent paid even when they don't have enough money in their account in order to avoid inconvenience, additional fees, and embarrassment. For example, you may want the bank to pay a check(or an electronic or automatic payment) made to a store, mortgage company, or landlord because if it's returned, you might have to pay a penalty fee to the payment recipient and because in the future, your checks (or electronic and automatic payments) may no longer be accepted.

People may also want their ATM and other debit card transactions paid in order to avoid embarrassment, get help in an emergency or get through a temporary cash-flow problem.

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Do all banks do this?

Most banks pay check (and electronic and automatic bill payments) that cause an overdraft. Some banks also pay ATM and other debit card overdrafts.

Why aren't overdrafts just free?

Overdraft fees are intended to be a deterrent to customers so they keep track of transactions and are careful not to overdraw their account on a regular basis. It is much like a parking ticket. And, just like any other business, banks have to cover their costs and any risk. The fees for overdrafts cover the risk the bank is taking when it pays a transaction for someone who doesn't have enough money in their account, in case they don't pay it back – and sometimes they don't.

What does the new rule do?

The new rule affects most debit card transactions: specifically ATM transactions and everyday debit card transactions made for purchases at a store or on the internet. The new rule provides that customers must expressly agree, or “opt in,” before the bank can charge an overdraft fee for paying an ATM or everyday debit card transaction that will cause an overdraft.

What about automatic bill payments that have been arranged to be paid through a debit card? If the customer doesn't opt in, will the payments always be returned when there isn't enough money in the account?

The bank may, at its discretion, pay automatic bill payments charged to a debit card, but a fee will be charged even if the customer has not “opted-in” and agreed to pay a fee to have ATM and everyday debit card overdrafts paid. The reason is that consumer testing found that consumers want these bills paid and are willing to pay something for it.

If the customer opts in, will the bank always pay ATM and everyday debit card transactions even when there is not enough money in the account?

No. Unless the customer has signed up to link the checking account to another account such as an overdraft line of credit, the bank does not guarantee that ATM and everyday debit card overdrafts will be paid even if the customer has opted in. These standard overdraft services are an accommodation provided at the bank's discretion.

If the customer does NOT opt in, does it mean that they will never overdraw their account using a debit card for ATM and everyday transactions?

No. There are limited circumstances when it will not be possible for the bank to avoid paying an ATM or other debit card transaction, even if there is not enough money in the account. Customers should not assume that because the ATM or other debit card transaction goes through that there is enough money in their account to cover it. In

these cases, the bank may not charge an overdraft fee, but the customer still must repay the bank to cover the overdraft.

How do customers opt in?

It depends on the bank. If the bank normally pays overdrafts for ATM and everyday debit card transactions (and then charges a fee), customers will receive an opt-in notice with directions. The rule permits banks to let customers opt in online, by phone, or in writing. They must also be able to revoke the opt-in in the same fashion.

Can customers opt in at the time of the debit card transaction?

Generally, customers will not be able to opt in at the time of the transaction though some banks may be able to allow customers to opt in at an ATM. If they think they will want their ATM and everyday debit card overdrafts paid and are willing to pay for it, they should opt in before they need it.

How do banks determine the price of an overdraft fee?

Determining the price of an overdraft fee is a proprietary decision that each bank makes for itself, taking into consideration the risks and costs of providing the service, as well as competitive forces.

Why can't the fee be proportional to the amount of the overdraft?

Again, determining the price of an overdraft fee is a proprietary decision that each bank makes for itself, taking into consideration the risks and costs of providing the service as well as competitive forces. Additionally, the fee is intended to be a deterrent to customers so they are careful not to overdraw their account on a regular basis. Like a parking ticket, the fine has to be high enough to keep drivers from parking in a fire lane. Same goes for overdraft fees.

Why are banks opposed to limits on overdraft fees?

If the number or amount of overdraft fees is limited, banks won't be able to cover the risk of providing the service and may cut it altogether. Then, even customers who want it won't be able to get it.

How many people overdraw their accounts?

According to ABA's annual overdraft survey conducted by an independent market research firm (Ipsos-Ried) in August 2009, 82 percent of bank customers did not pay an overdraft fee in the previous twelve months. That's up two percent from 2008.