CFPB Going After Checking Account Overdraft Fees

February 23, 2012 - Twenty five years ago, if you wanted to have overdraft protection on your checking account, you actually needed to have good credit. Banks used to issue Check Guarantee Cards that you would show a merchant when you were writing a check. Just imagine that. You actually had to be a responsible enough individual to warrant bank protection before the bank would guarantee your checks. And if I recall correctly, if you overdrew your account more than once in a 12 month period, the bank would cancel your guarantee card and end the protection. But all that changed when banks figured out that they could make more money by charging fees for bounced checks than they could for rewarding responsible customers. Now, the Consumer Financial Protection Bureau is taking a closer look at those fees.

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Overdraft protection on checking accounts is one of the last unregulated frontiers when it comes to bank fees. On average, banks charge consumers around $35 for every check that uses overdraft protection.

The benefit of overdraft protection is that consumers don't have to worry about bouncing a check; something that is illegal and can result in costly late penalties and ruined credit. For those who habitually bounce checks, overdraft protection can even help prevent prosecution.

But the downside of the protection is the cost. Overdrawing your account when you have multiple checks outstanding can run up hundreds of dollars in fees in very short order.

The protection has been abused by both consumers and banks. It is not uncommon for people to pay an important bill

knowing that they don't have the money in their account. They view the fee as being the more palatable of two bad alternatives.

But banks have also abused the service. For instance, when they process checks the bank may process the largest check first and each subsequent check in descending value. This practice results in unnecessarily high fees for consumers and the greatest possible profit for the banks.

Consumers who use debit cards now have to opt in to overdraft protection. And banks are now limited on the amount they can charge consumers for either overdrafts using a debit card, or purchase denials for consumers that have decided they don't want overdraft protection on their debit cards. A similar mechanism could be used with checking accounts but that is not what the CFPB is planning on.

Instead, the CFPB is considering a "penalty box" on bank statements. The box would contain in large print, the amount of overdraft fees that you have paid over the past month. While not an ideal solution, it may be better than following the route used on debit cards. The limitation and reduction of collected fees on debit card transactions has led banks to eliminate some services and to start charging for others which had been free in the past. The penalty box solution would not eliminate or cap fees, but it just might make account holders realize that it pays to balance their check books every single month.

byJim Malmberg
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