

REGULATORY UPDATE

New CFPB Guidance on Illegal Junk Fees on Deposit Accounts

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On October 26, 2022, the CFPB announced that it was issuing formal guidance regarding the legality of certain fees, which they have deemed “*Surprise Fees*,” also referred to as “*Junk Fees*,” associated with deposit accounts.

In the [Press Release](#), the CFPB detailed two distinct “*Surprise fees*” that they consider violations of the Consumer Protection Act, which prohibits unfair practices when consumers cannot reasonably avoid them. One fee is associated with Courtesy Overdraft programs, and another is simply labeled as a “*depositor*” fee. The two fees in summary are:

- **The Surprise Depositor Fee - The Depositor is charged a fee for the return to the depositor of a deposit (credit) deemed NSF (Non-Sufficient Funds).**
- **The Surprise Overdraft Fee – A Debit card item is Approved when the account is Positive, but the customer is charged a fee when the item Posts Negative or Settles when Negative, also referred to as APPN (approved/authorized positive, posts negative) or APSN (approved positive, settles negative) items.**

Delving into each of these individually, we first look at the –

Surprise Depositor Fee

Overview:

The [October 2022 CFPB Bulletin 2022-06: Unfair Returned Deposited Item Fee Assessment Practices](#) clearly defines the fees charged by financial institutions (FIs) when returning a check deposited to the depositor’s account that is subsequently returned from the payor’s bank for insufficient funds (or another valid reason beyond the depositor’s control), as likely unfair. The charging of such fees is now considered to be a violation by the CFPB, which has the authority to make such a determination under the Consumer Protection Act.

This statement of policy was issued under the Administrative Procedures Act, which dictates the process by which federal agencies, including the CFBP, develop and issue regulations. The new statement provides background information about applicable law, articulates considerations relevant to the Bureau’s exercise of its authorities, and establishes guidance for the other regulatory agencies charged with enforcement of consumer protection laws as established by the CFPB. Since it is a statement of policy and not considered a new rule, it does not require the formal process followed by a new or amended regulation, which includes comment periods and effective dates. As such, it may be considered effective as of the date of the notification.

Corrective Action Recommended:

Institutions should strongly consider the prompt termination of such fees, weighing the risk of non-compliance with consideration given to any possible extenuating circumstances the FI may put up as a defense.

Effective Date Correction Required By:

Since this is an administrative action under an existing regulation or authority granted to the agency, the effective date would appear to be when issued. Corrective action should be required immediately.

Surprise Overdraft Fee – APPN/APSN

Overview:

The October 26, 2022, CFPB [“Consumer Financial Protection Circular 2022-06 - Unanticipated Overdraft Fee Assessment Practices”](#) provides 13 pages of extensive detail explaining why overdraft fees charged on Debit items -- that had been approved when the available balance was positive -- are considered unanticipated or “surprise” fees by the consumer when they are subsequently charged for these items. The following excerpt explains:

“Unanticipated overdraft fees can occur on “authorize positive, settle negative” or APSN transactions, when financial institutions assess an overdraft fee for a debit card transaction where the consumer had sufficient available balance in their account to cover the transaction at the time the consumer initiated the transaction and the financial institution authorized it, but due to intervening authorizations, settlement of other transactions (including the ordering in which transactions are settled), or other complex processes, the financial institution determined that the consumer’s balance was insufficient at the time of settlement. These unanticipated overdraft fees are assessed on consumers who are opted-in to overdraft coverage for one-time debit card and ATM transactions, but they likely did not expect overdraft fees for these transactions.”

This situation has been noted in several past Pinnacle Regulatory Updates as the basis for numerous successful class action lawsuits where the claim argued that the practice was “Deceptive” and not clearly disclosed to the consumer. Pinnacle provided clear disclosure language for brochures and recommended FIs review their account agreements for transparency and full and clear disclosure as to how fees are charged with specific reference to this type of situation. Given this latest pronouncement, in addition to similar presentations and statements of the potential for UDAP claims by other agencies as early as 2018, this practice is no longer solely an issue of inadequate disclosure. It should now be considered a prohibited practice, similar to the Reg E regulatory prohibition of charging for the payment of a debit item that, when the customer has not opted in, is approved against a positive balance, but that settles when negative. Now, even when the customer has opted in, if a debit item approved positive settles negative, no charge can be assessed. Only when debit items that have been approved when the account balance disclosed was negative, can the subsequent clearing item be assessed a charge. The Circular also has examples of systems that use an available balance and a ledger balance for the calculation of fees. As noted in several past articles by the CFPB and in the examples shown, the use of available balance for fee calculations

results in higher fee assessments to consumers compared to fees assessed by institutions using ledger balance. Many of these higher fee amounts can be the direct result of these APSN items. When these additional fees are attributable to the charging of APSN items and fees, they can be included when calculating restitution.

Corrective Action Recommended:

This can only be corrected by implementing a change to the core banking deposit systems' item processing. Because of earlier regulatory scrutiny, most core providers have already provided a solution, but it may be a request item. We are aware of one core that implemented their corrective item by default with an update. All FIs with a courtesy overdraft program where customers are allowed to opt-in under Reg E for the payment of additional one-time debit card and ATM transactions, if they have not previously done so, should promptly contact their core provider to have their item processing operations reset to correctly handle these items.

Each core may call this corrective process by a variation of names, and it may require more than one change or update. Some of the named references have included the terms "OD fee enhancements," "Good Funds Enhancements," and "Next Day Fee Enhancements." If your core support is unaware of their corrective action from these descriptions, request they research and provide a solution for the deposit processing and fee assessment component that will provide compliance with the requirements set forth in the "CFPBs Consumer Financial Protection Circular 2022-06 - Unanticipated Overdraft Fee Assessment Practices."

Effective Date Correction Required By:

Since this is an administrative action under an existing regulation or authority granted to the agency, the effective date would appear to be when issued. Should an institution be found to be in noncompliance, the enforcement agency may request reimbursement of fees for consumers going back to any time periods as determined by the agency for the specific FI, with potential additional Civil Monetary Penalties. Please refer to the [Regions Bank enforcement example](#) presented by the CFPB within the circular.

About CFPB Financial Circulars and Bulletins:

While direct examination by the CFPB is limited to FIs over \$10 Billion in assets, CFPB regulations and guidance apply broadly to all financial institutions, including those examined only by State authorities.

Consumer Financial Protection Circulars are issued to all parties with authority to enforce federal consumer financial law. The CFPB is the principal federal regulator responsible for administering federal consumer financial law, see 12 U.S.C. 5511, including the Consumer Financial Protection Act's prohibition on unfair, deceptive, and abusive acts or practices, 12 U.S.C. 5536(a)(1)(B), and 18 other "enumerated consumer laws," 12 U.S.C. 5481(12). However, these laws are also enforced by state attorneys general and state regulators, 12 U.S.C. 5552, and prudential regulators including the Federal Deposit Insurance Corporation (FDIC), the Office of the Comptroller of the Currency, the Board of Governors of the Federal Reserve System, and the National Credit Union Administration. See, e.g., 12 U.S.C. 5516(d), 5581(c)(2) (exclusive enforcement authority for banks and credit unions with \$10 billion or less in assets). Consumer Financial Protection Circulars are general statements of policy under the Administrative Procedure Act. 5 U.S.C. 553(b).

FDIC GUIDANCE ON ILLEGAL OVERDRAFT FEES ON DEPOSIT ACCOUNTS

As reported in our earlier November Regulatory Update, the FDIC has provided several communications warning FDIC insured and regulated State-Non-Member banks of overdraft related fees that it considers possibly unfair or deceptive.

In its publicly broadcast FDIC Advisory Committee of State Regulators (ACSR) Meeting on October 24, 2022, two days prior to the CFPB Junk Fee press release and bulletin on APSN, the FDIC informed its State Regulators that it was focused on certain practices associated with courtesy overdraft programs. This focus included the aforementioned APSN fees, as well as an additional situation, not mentioned in the CFPB press release, where multiple Return Fees may be assessed for multiple presentments of the same item.

The Surprise Overdraft Fee - Multiple Fees charged for the Same ACH item - Returned Multiple Times.

Overview:

As explained in our earlier Fall 2022 Regulatory Update, the FDIC sent out a financial institution letter (FIL) "["FIL-40-2022 Supervisory Guidance on Multiple Re-Presentation NSF Fees."](#) In the FIL, the FDIC reiterated a message provided earlier in their "["FDIC Consumer Compliance Supervisory Highlights for March 2022."](#) Both FDIC documents cite the practice of charging successive return item fees on the same electronic item that has been returned and successively resubmitted as excessive, and possibly citable as a UDAP violation, unless clearly and transparently disclosed. Pinnacle has provided earlier guidance and suggested language for its Overdraft program, and the subject was covered in more detail in the "Pinnacle Fall 2019 Regulatory Update." In that update, we noted that there have recently been several class action lawsuits filed against FIs for charging an NSF fee multiple times on the same item. In one example, which was cited in a lawsuit, a transaction in the amount of \$25.00 was presented five times for payment, resulting in an NSF fee of \$36.00 to the accountholder each time, for a total of \$180.00 in fees. We suggested that when reviewing and updating overdraft program brochures and return policies in related disclosures for compliance, FIs should review all documents for all accounts, including the FIs' own deposit agreements and schedule of fees.

Given the CFPB's emphasis on Junk fees and Surprise fees, it is important to revisit the FDIC's position on multiple re-presentation fees.

In the [current guidance](#), * the FDIC references two Compliance Risks – **Deceptive Practices** and **Unfair Practices** – and two additional risks -- **Third Party Risks** and **Litigation Risks**.

In our earlier Regulatory Update, we covered the **Deceptive Practices Risk** and the related **Litigation Risk** from Class Action Lawsuits with several successful class action lawsuits summarized. On the regulatory side, these deceptive practices are also the result of disclosures that do not adequately advise customers of this practice, and the misrepresentation and omission of this information from the institutions' disclosures that is considered material. This then leads to a UDAP violation of Section 5 of the FTC Act.

In this same FIL, the FDIC appears to have upped the level of scrutiny within the confines of Section 5 of the Act, stating that "In particular, a risk of **unfairness** may be present if multiple NSF fees are assessed for the same transaction in a short period of time without sufficient notice or opportunity for

customers to bring their account to a positive balance in order to avoid the assessment of additional NSF fees." They then conclude this section with the following key language:

"While revising disclosures may address the risk of deception, doing so may not fully address the unfairness risks. "

What the FDIC is saying here is that while clear disclosures may be a defense against UDAP regarding the deceptive nature of the program, the inability of the customer to stop the continuing charges in a reasonable period of time may bring back into question the issue of the unfairness test found within the Act. While they stop short in the assertion that this leads to a violation, they are clearly stating that they consider this to be unfair and "may" be determined to be so, and thus a violation, on a case-by-case basis, may be found during an exam. This is also the message that was signaled in the discussion with state bank regulators.

Also discussed in the meeting in more detail is the issue of **Third-Party Risk**. In this section of the FIL, the FDIC clearly puts the responsibility on the FI for understanding the FI's core capabilities. "Institutions are encouraged to review and understand the risks presented from their core processing system settings related to multiple NSF fees, as well as understand the capabilities of their core processing system(s), such as identifying and tracking re-presented items and maintaining data on such transactions."

The FDIC said it has received many comments, is engaged in discussions with the banking associations, and is in touch with many of the core processors, encouraging them to automate the identification and reduction of these multiple presentments to eliminate multiple charges. While the FDIC appears to be aware that there are systems that do not provide the automation needed, they are encouraging other means of making customers whole for these multiple charges, with the recognition that it may be a manual commitment.

Not discussed in the FIL are the related procedures and merchant processing rules for presentment by the merchant and the originator bank that allowed these multiple present items to be sent to the receiving banks. Pinnacle recommends receiving banks may have some success in controlling these resubmissions by coordinating with their originator banks. While the FDIC puts the responsibility on the receiving bank and their core processor, it may be an issue for further discussion and coordination with NACHA, as merchants can change identifying traits of the transaction that would make it difficult to identify as a repeated submission.

When asked during the ACSR Meeting what the current examination procedures would be for identifying these practices, the response was that the FDIC has a risk-based approach and would not be looking for them at every exam. When pressed on what may constitute risk indicators, the response was "evidence of it," most probably based on complaint letters. (These could be to the FDIC or CFPB, but they might also be ones received by the FI and found during a standard review of complaints received by the institution and actions taken as part of the regular compliance examination procedures.)

Corrective Action Recommended:

Our past Regulatory Updates have clearly pushed for proper disclosures and emphasized the need for considering practices and reforms as presented in this FIL and other guidance. Given the ongoing emphasis on this practice and the FDIC's strong discouragement of these charges even when clearly disclosed, Pinnacle recommends that these fees are not charged whenever the core can prevent them. When the core has no solution, the FI should first document the inquiry and request made to its core, and then establish an internal process to identify such representation fees with a subsequent reversal. We also note that many competitor FIs are eliminating NSF return fees altogether, especially in very large institutions, as an effective risk mitigation practice, which was suggested in the FIL.

Effective Date Correction Required By:

Since this is also an administrative action under an existing regulation or authority granted to the agency, the effective date would appear to be when issued. However, the FIL suggests that institutions should act promptly to self-correct to avoid further regulatory action, and that self-correction includes making consumers who were harmed whole.

As covered in the ACSR Meeting and as stated in the FIL in the footnote on page 4, we find the question and discussion on how far back an FI must go to look for fees that have been inappropriately charged. The answer for a self-correcting institution was a two year look back from the date of the FIL.

* Note: On June 16, 2023 the FDIC published a revision to this guidance making a slight change to its regulatory approach with due consideration being given to the likelihood of substantial consumer harm in their assessment of the institution's practice. Your attention is directed to page 3 of the revised guidance as well as the revised footnote, number 4.

[June 16, 2023 | FIL-32-2023 - FDIC Clarifying Supervisory Approach Regarding Supervisory Guidance on Multiple Re-Presentation NSF Fees](#)

Additional Considerations:

The corrective actions contained in this update are not intended as legal advice but are provided as recommendations and guidance for clients as part of Pinnacle's best practices for running a regulatory compliant and fair program for all consumers. Readers are advised to consult with internal compliance officers and bank counsel for their interpretation of these recent pronouncements and action to be taken by the FI.

An additional PDF document containing all the referenced agency documents is provided for download on the Pinnacle Website – [Nov 2022 Reg Update Supplementary Documents](#).