

Alert | Financial Regulatory & Compliance



January 2024

CFPB Proposes Rule to Reclassify Overdraft Fees Under TILA

Go-To Guide:

- The proposed rule, if finalized in its present form, would require very large financial institutions to treat commonly used overdraft protection as credit, thus subjecting the current practice to disclosure requirements and other protections that apply to credit cards and loans.
- The proposed rule would also give covered institutions two options on how to approach overdrafts. First, institutions could offer overdraft loans, treating them as lines of credit, that comply with Truth in Lending Act (TILA) requirements. Second, they could offer overdrafts as a courtesy service where fees do not exceed costs and losses, using a “breakeven standard” calculation or, alternatively, a “benchmark fee” which options under consideration include \$3, \$6, \$7, or \$14.
- The new rules would apply to banks and credit unions with \$10 billion or more in assets and, if finalized in its present form, would not go into effect until October 2025.

In a move that could reshape the landscape of consumer finance, on Jan. 17, 2024, the Consumer Financial Protection Bureau (CFPB) proposed a new rule that aims to redefine overdraft fees as credit products subject to TILA. This proposal is part of the CFPB’s ongoing efforts to curb what it identifies as “junk fees” and enhance transparency in consumer financial products.

If finalized in its present form, the proposed rule would eliminate a current exemption to TILA that broadly allows financial institutions to streamline honoring checks of their depositors who have inadvertently overdrawn their accounts.

Background

In 1968, Congress enacted TILA. In 1969, the Federal Reserve Board wrote rules to implement the new law, which generally required lenders to disclose the cost of credit to a borrower. Many families received and sent checks through the mail at the time and needed more certainty about when their deposits and withdrawals would clear. When a bank processes a check transaction, and the consumer doesn't have funds in the account to cover such payment, the bank may cover the difference and honor payment of the check. The Federal Reserve Board exempted TILA requirements if the bank honored a check when their depositor "inadvertently" overdraw their account.

Traditionally, overdraft fees have been treated as service charges by financial institutions. However, the CFPB's proposed rule seeks to categorize these fees under TILA, thereby imposing on large financial institutions the obligation to provide detailed disclosures and obtain explicit consumer consent akin to unsecured consumer loans and lines of credit.

Potential Implications

- **Legal Challenges:** Large financial institutions may challenge the rule, arguing it oversteps the CFPB's regulatory authority or creates undue burdens. The success of such a challenge would likely hinge, in part, on the Supreme Court's rulings in *Consumer Financial Protection Bureau v. Community Financial Services Association of America, Limited*, challenging the constitutionality of the CFPB's funding structure, and *Loper Bright Enterprises v. Raimondo, Relentless, Inc. v. Department of Commerce* potentially overruling *Chevron*, which grants deference to an agency's reasonable interpretation of an ambiguous statute.
- **Consumer Credit Reporting:** Treating overdrafts as credit under TILA may necessitate their inclusion in consumer credit reports, impacting credit scores and borrowing capacity.
- **State Law Interactions:** The reclassification could activate additional requirements under state consumer credit laws, complicating compliance efforts.

Takeaways

The proposed rule represents a pivotal development in consumer finance regulation. Large financial institutions should consider initiating an immediate and thorough evaluation of their overdraft fee structures and policies. This step would ensure alignment with the proposed rule's exclusion (breakeven standard or benchmark fee) or TILA's enhanced disclosure requirements and consumer consent mandates. Additionally, financial institutions should prepare for significant operational changes, including modifications to IT systems, customer service protocols, and staff training programs to adapt to these possible new regulatory demands. The potential inclusion of overdrafts in consumer credit reports necessitates a strategic approach to maintain compliance with applicable credit reporting laws. Covered financial institutions under the rule also must be aware of the additional complexities involving applicable state consumer credit laws, which this proposed rule could further complicate.

Equally important is the development of a comprehensive client communication strategy. If the proposed rule is finalized in its present form, covered financial institutions should proactively inform and educate customers about the impending changes to overdraft services. Risk management frameworks should also

be updated to reflect these potential regulatory changes, and contingency plans should be established to address various scenarios, including increased enforcement scrutiny in this area.

Authors

This GT Alert was prepared by:

- **Benjamin M. Saul** | +1 202.331.3123 | saulbe@gtlaw.com
- **Shane Foster** | +1 602.445.8000 | Shane.Foster@gtlaw.com
- **Tarrian L. Ellis** | +1 202.533.2351 | Tarrian.Ellis@gtlaw.com

Albany. Amsterdam. Atlanta. Austin. Berlin. Boston. Charlotte. Chicago. Dallas. Delaware. Denver. Fort Lauderdale. Houston. Kingdom of Saudi Arabia. Las Vegas. London. Long Island. Los Angeles. Mexico City. Miami. Milan. Minneapolis. New Jersey. New York. Northern Virginia. Orange County. Orlando. Philadelphia. Phoenix. Portland. Sacramento. Salt Lake City. San Diego. San Francisco. Seoul. Shanghai. Silicon Valley. Singapore. Tallahassee. Tampa. Tel Aviv. Tokyo. United Arab Emirates. Warsaw. Washington, D.C.. West Palm Beach. Westchester County.

This Greenberg Traurig Alert is issued for informational purposes only and is not intended to be construed or used as general legal advice nor as a solicitation of any type. Please contact the author(s) or your Greenberg Traurig contact if you have questions regarding the currency of this information. The hiring of a lawyer is an important decision. Before you decide, ask for written information about the lawyer's legal qualifications and experience. Greenberg Traurig is a service mark and trade name of Greenberg Traurig, LLP and Greenberg Traurig, P.A. Greenberg Traurig's Berlin office is operated by Greenberg Traurig Germany, an affiliate of Greenberg Traurig, P.A. and Greenberg Traurig, LLP. Khalid Al-Thebity Law Firm in affiliation with Greenberg Traurig, P.A. is applying to register a joint venture in Saudi Arabia. Operates as a separate UK registered legal entity. Greenberg Traurig's Mexico City office is operated by Greenberg Traurig, S.C., an affiliate of Greenberg Traurig, P.A. and Greenberg Traurig, LLP. Greenberg Traurig's Milan office is operated by Greenberg Traurig Santa Maria, an affiliate of Greenberg Traurig, P.A. and Greenberg Traurig, LLP. Operates as Greenberg Traurig LLP Foreign Legal Consultant Office. Greenberg Traurig's Singapore office is operated by Greenberg Traurig Singapore LLP which is licensed as a foreign law practice in Singapore. Greenberg Traurig's Tel Aviv office is a branch of Greenberg Traurig, P.A., Florida, USA. Greenberg Traurig's Tokyo Office is operated by GT Tokyo Horitsu Jimusho and Greenberg Traurig Gaikokuhojimbengoshi Jimusho, affiliates of Greenberg Traurig, P.A. and Greenberg Traurig, LLP. Greenberg Traurig's United Arab Emirates office is operated by Greenberg Traurig Limited. Greenberg Traurig's Warsaw office is operated by GREENBERG TRAURIG Nowakowska-Zimoch Wysokiński sp.k., an affiliate of Greenberg Traurig, P.A. and Greenberg Traurig, LLP. Certain partners in GREENBERG TRAURIG Nowakowska-Zimoch Wysokiński sp.k. are also shareholders in Greenberg Traurig, P.A. Images in this advertisement do not depict Greenberg Traurig attorneys, clients, staff or facilities. No aspect of this advertisement has been approved by the Supreme Court of New Jersey. ©2024 Greenberg Traurig, LLP. All rights reserved.