

# Overdraft Protection and Payday Advance Loans

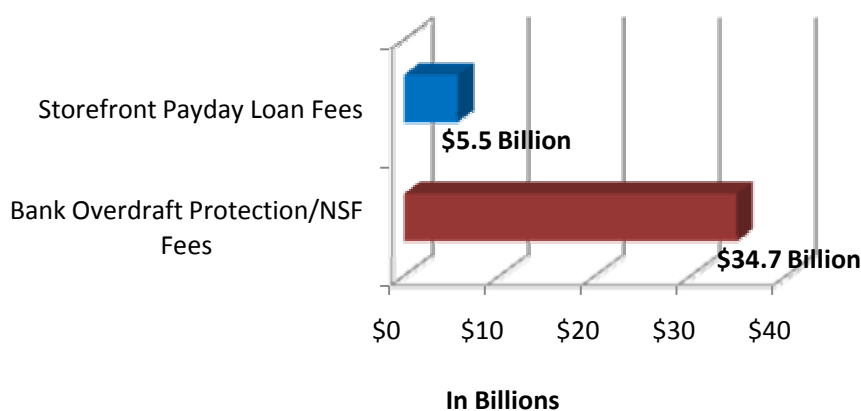
Short-term credit providers play a critical role in the U.S. financial services market by extending capital to a population in need of small-dollar loans. The demand to meet the need for immediate, unsecured, short-term credit has grown in the past decade with the market now exceeding \$115 billion<sup>1</sup>, including bounced check fees, late bill payment fees and payday loans. Bank overdraft protection and salary or payday advances are among a number of options available to consumers facing unexpected and unbudgeted expenses.

Confronting a budget shortfall, a consumer may overdraw their checking account, triggering a “bounced loan” through overdraft protection or choose an advance through a payday lender. While both options provide consumers with short-term access to funds, there are important differences between the two.

## **Payday advance fees paid by consumers pale in comparison to those paid in overdraft fees**

- In 2008, storefront payday lenders provided 120 million loan transactions and collected roughly \$5.5 billion in fees.<sup>2</sup>
- In comparison, it is estimated that consumers will overdraw their accounts 1.22 billion times this year, allowing banks and credit unions to collect more than \$34.7 billion in overdraft fees.<sup>3</sup>

### **Estimated Annual Fees Paid by U.S. Consumers**



## **Payday advances are highly regulated**

- State laws heavily regulate all aspects of payday lending, including limiting the number of loan transactions, placing caps on loan transaction amounts and the fees that can be charged. Payday loans are also subject to a number of federal laws that protect consumer credit borrowers, including full disclosure of the fees expressed both as a dollar amount and an annual percentage rate.<sup>4</sup>
- Bank and credit union overdraft transactions have no such regulations.

<sup>1</sup> [http://www.cfsa.net/policymakers/market\\_demand.html](http://www.cfsa.net/policymakers/market_demand.html)

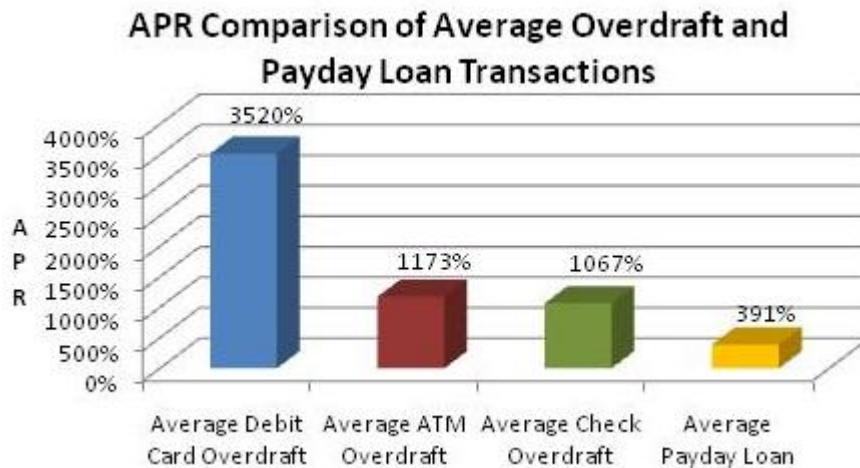
<sup>2</sup> Present and Future of the Payday Advance Industry, Dennis Telzrow, CFA, Managing Director, Research, Stephens Inc., March 5, 2009

<sup>3</sup> Overview NSF/OD National Analysis, Bretton Woods, March 2009

<sup>4</sup> <http://www.cfsa.net/knownyourfee/index.html>

## **Payday advances can be a less costly alternative to overdrawing a bank account**

- Payday lenders typically charge a flat fee of \$15 per \$100 borrowed, or 391% if quoted as an annual percentage rate.<sup>5</sup>
- FDIC reports that the average bank customer pays \$27 (median overdraft fee) to cover a transaction of \$36 (median transaction size), with annual percentage rates ranging from 1067% to 3520%.<sup>6</sup>



## **Payday advance fees are fully disclosed before customers enter into the transaction**

- Payday lending customers must make a conscious decision to apply for a payday advance, and take proactive action to do so. Before entering into the transaction, the fee and terms of the advance are fully disclosed. In addition to the information found in brochures and loan agreement forms, payday lenders post the fees, in both dollar amount and APR, in large type on poster-size displays in all stores.
- The majority (75%) of bank customers are automatically enrolled in overdraft programs when they first open their bank account. Even when overdrawing their account using a debit card or withdrawing cash at an ATM, customers are not alerted to the pending overdraft or fees associated with the transaction. Many banks offer a tiered fee structure, where the fee increases based on the customer history with overdrafts. And making it even more confusing, banks tend to process the largest debits first - which can increase the number of overdrafts.<sup>7</sup>

## **Payday lenders offer substantial, self-imposed consumer protections**

- Under Best Practices mandated by CFSA, the national trade association of payday lenders, any customer who cannot payback their loan when due has the option of entering into an extended payment plan, allowing them to repay the advance over a period of additional weeks. This option is provided to CFSA members' customers for any reason and at no additional cost.<sup>8</sup>
- Bank customers who have overdrawn their account risk being assessed additional fees daily or pay interest on accounts that remain in negative balance.<sup>9</sup> Other than depositing all of the funds necessary to cover the overdrawn balance, customers have no way to work out of their bounce-loan overdraft debt.

<sup>5</sup> Community Financial Services Association of America, [www.cfsa.net](http://www.cfsa.net)

<sup>6</sup> FDIC Study of Bank Overdraft Programs, December 2008, <http://www.fdic.gov/bank/analytical/overdraft/>.

<sup>7</sup> FDIC Study of Bank Overdraft Programs, December 2008, <http://www.fdic.gov/bank/analytical/overdraft/>.

<sup>8</sup> [http://www.cfsa.net/public\\_education\\_campaign/extended\\_payment\\_plan.html](http://www.cfsa.net/public_education_campaign/extended_payment_plan.html)

<sup>9</sup> FDIC Study of Bank Overdraft Programs, December 2008, <http://www.fdic.gov/bank/analytical/overdraft/>.