Proactive Steps to Reduce Overdraft Litigation Risk

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Financial institutions are aware that they have become targets of overdraft litigation, including class action lawsuits. While overdraft ligation has been around for a long time, the number of suits and threatened suits seems to be increasing. In recent years, allegations by plaintiffs have often focused on claims relating to breach of contract due to allegedly ambiguous account terms and conditions, violations of the Electronic Fund Transfer Act, and violations of consumer protection laws. This alert will provide general guidance on what actions financial institutions can take to proactively reduce their overdraft litigation risk.

1. **Account Terms and Conditions Should Accurately Reflect Actual Operations and be Consistent.** Financial institutions should thoroughly review account terms and conditions, disclosures, communications, and other customer documents against actual operations to ensure that they are accurate, complete, and not misleading. Further, financial institutions should ensure that all account terms and conditions, disclosures, communications, and other customer documents are consistent with one another. This may be of greater importance where a financial institution relies on general form documents provided by third-party vendors. Financial institutions should continue to conduct these reviews on at least an annual basis to ensure that any subsequent changes to policies and operations are addressed.
2. **Make Account Terms and Conditions Clear and Unambiguous.** Substantial overdraft litigation has included allegations relating to account terms and conditions, such as claims pertaining to a financial institution charging multiple non-sufficient fund fees on one item and the account balance calculation method used by a financial institution to determine overdraft fees. Account terms and conditions should be clearly and unambiguously described. Illustrative examples may also provide added clarity for customers. For instances, a financial institution may include examples of how and when a customer is and is not charged an overdraft fee. Particular attention should be directed to language that states that non-sufficient fund fees will be charged on a “per item” or “per transaction” basis as plaintiffs have alleged that this means that a customer will only be charged one fee. Moreover, financial institutions should go beyond merely stating that an overdraft occurs when an account has “insufficient funds” or does not have “enough money.” At minimum, these phrases should be explained, such as by describing the process and the specific account balance

calculation method used.

3. **Do Not Place Undue Reliance on the Regulation E Model Form.** At least one federal appellate court has held that a plaintiff's claim for violation of the Electronic Fund Transfer Act based on the substance of an overdraft opt-in agreement survived a motion to dismiss notwithstanding the financial institution's use of Model Form A-9 in Regulation E. *Tims v. LGE Community Credit Union*, 935 F.3d 1228 (11th Cir. 2019). *See also Salls v. Digital Fed. Credit Union*, 349 F. Supp. 3d 81 (D. Mass. 2018). It is recommended that financial institutions consult with legal counsel before making any changes to an overdraft opt-in agreement based on Model Form A-9 in Regulation E.
4. **Review and Comply with Federal Bank Regulator Guidance.** Federal bank regulators have issued guidance over the years on overdraft protection programs which financial institutions should review in connection with their respective programs. This guidance touches on both compliance concerns as well as best practices. *See, e.g., Joint Guidance on Overdraft Protection Programs (Feb. 18, 2005); FDIC Overdraft Payment Supervisory Guidance (Nov. 24, 2010).*
5. **Consider Adding an Arbitration Clause to Your Account Terms and Conditions.** In a recent case, a federal district court granted a financial institution's motion to compel arbitration based on an arbitration clause in a membership agreement in a case where the plaintiff alleged that the financial institution improperly charged overdraft fees. *Page v. Alliant Credit Union, No. 1:19-CV-5965, 2020 WL 2526488 (N.D. Ill. May 18, 2020). See also McGovern v. U.S. Bank N.A., 362 F. Supp. 3d 850 (S.D. Cal. 2019).* While there may also be drawbacks, arbitration may offer several benefits over a court proceeding, such as being less expensive, offering quicker resolution, the ability to choose the arbiter, and confidentiality. It is recommended that financial institutions consult with legal counsel before making any decision to add an arbitration clause.
6. **Refund Improperly Charged Fees.**Financial institutions should ensure that procedures are in place to refund non-sufficient fund fees or overdraft fees that were charged in error and/or where a customer complains about non-sufficient fund fees or overdraft fees or practices. Keep your customers happy!