



Addressing **Consumer Needs** with a Responsible Overdraft Program

BY JOHN COHRON, CHIEF EXECUTIVE OFFICER

When a negative balance needs to be covered, overdraft services provide a number of benefits to the consumer

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***“I hear all of the time that members who
have Overdraft Privilege appreciate the
service and want to maintain it.”
– Northeastern financial institution, \$255MM assets***

ADDING CONSUMER **VALUE** TO YOUR OVERDRAFT PROGRAM

As you've likely seen, there has been discussion and speculation about overdraft programs in the news lately. What's more, the current back-and-forth about specific program details and fees among lawmakers and the media fails to recognize that sometimes, consumers don't have easy access to liquidity to cover financial shortfalls.

Of course, it's ideal for everyone to keep a positive account balance—but it's not always the reality. Sometimes bills and necessities need to be paid before the next paycheck is deposited, or emergencies occur unexpectedly, and the funds aren't there to cover them. In many cases, consumers may lack access to another account to draw from, such as another deposit account, a credit card or line of credit to cover an expense. It can leave them in quite a bind.

Every day it's possible for anyone to experience an overdraft for any number of reasons. A few examples include:

- » One person on a joint checking account forgets to tell the other about a cash withdrawal.
- » Meanwhile, the other person makes a car payment, thinking there's enough in the account. A family goes on vacation, relaxes and doesn't keep track of every expense, leading to balance confusion and over-purchasing.
- » A major home repair or other unexpected expense occurs and needs to be taken care of right away.
- » A hotel puts a temporary hold on a card to cover incidentals or for a deposit, and it takes longer than expected for the funds to be available.

These, and many others, are the exact types of situations where Overdraft Privilege provides a valuable service and fulfills consumers' needs.



In 2023, US active cardholders swiped their debit cards about 35 times a month.

With the average American making more than two payments per day, it's not difficult to see how an account can become overdrawn unintentionally.




Source: ABA banking journal 2024 survey

“Some of our members are living paycheck to paycheck. Overdraft Privilege helps them maintain their daily needs. It has been very beneficial for our member base.”

– Northeastern financial institution, \$33MM assets

OVERDRAFT PRIVILEGE: ANOTHER PART OF YOUR OVERDRAFT SOLUTION

Financial institutions can offer several services to help consumers stay in the black, including:

 Account-to-Account Transfers	 Overdraft Privilege	 Line of Credit or Credit Card
Consumers may not have another checking or savings account to link	No application is required, which offers convenience	Requires an application and approval
Some have a secondary account elsewhere, which may take additional time to complete a transfer of funds	There is no fee to have access to the safety net—a fee is only assessed if one or more paid items causes an overdraft	Some consumers may not qualify

WITHOUT OVERDRAFT PRIVILEGE, WHERE DO CONSUMERS TURN?

If your financial institution doesn't offer an Overdraft Privilege service, or it isn't easily accessible to consumers, you could be sending them elsewhere for a solution. Often, the alternatives come with higher fees, more risks, and potentially long-term consequences.

Source of Funds	The Consequences
Payday Loans	A short-term loan with a high-interest rate to be paid quickly makes it hard for consumers to get out of the cycle of debt. If defaulted, it may affect the consumer's credit score negatively, which can impact the cost of lending or insurance products in the future.
Pawn Loans	Another option is securing a short-term loan with a high interest rate using an item of value as collateral. If the loan isn't paid in a certain amount of time, the item can be sold. The borrower may not have items of value or may be forced to use something sentimental as collateral, with the chance of not getting it back if they can't repay the loan on time.
Family/Friends	Borrowing money from a family member or friend comes with whatever terms both parties agree on. Many times, this causes undue stress for both parties. The borrower risks damaging the relationship if unable to repay the loan in a timely manner or if borrowing becomes a common occurrence.
None	Suppose no other recourse exists to make an important payment on time and Overdraft Privilege isn't available. In that case, a person could face expensive late fees, insufficient funds fees, credit score decline and higher rates for lending or insurance products, in addition to personal embarrassment.



THE FINANCIAL DIVIDE

According to a recent financial health network report, about 17% of Americans are financially vulnerable; levels this high have not been seen since the pandemic. These consumers are struggling to meet expenses, have no emergency savings, and are likely in heavy debt. Less than half of all Americans (49%) report that they have disposable income.

In many cases, paying a one-time overdraft fee that's free from additional consequences makes more financial sense. It also provides an equitable and inclusive option for all consumers.

A RESPONSIBLE SERVICE FOR RESPONSIBLE USE

Being responsible means being dependable, keeping promises and honoring commitments. In the context of your financial institution, it also means being a trustworthy partner and providing consumers with the services they need.

In order for overdraft services to be a win-win for your financial institution and your consumers, responsibility is needed from both parties.

For your part, a responsible overdraft program should be:

- » **Fair.** The fee for using the service should be reasonable. And offering it to all eligible account holders creates inclusivity that treats them fairly.
- » **Easy to understand.** Having an established limit with simplified processes will ensure your staff can explain the service easily. Plus, when your consumers understand it to be free of any “gotchas” or special caveats, they will recognize the value you are offering.
- » **Well-communicated.** Your consumers need to know all of their options, including how the service works and the fees associated if it is used. Complete transparency is something they’ll appreciate. Plus, it empowers them to decide if Overdraft Privilege is the right option for them, should they need it.
- » **Properly managed.** Having a way to identify users along with access to reports and program data are critical must-haves. It means your staff can efficiently monitor activities and trends, such as pinpointing unusual patterns or irresponsible use, which may indicate the need for alternative solutions or financial counseling.

And on top of all of this, 100% compliance with regulations is always a must.

For the consumer, responsibly using Overdraft Privilege means exhausting other options first, such as transferring funds from another account or using a line of credit. When a consumer makes an informed decision to utilize Overdraft Privilege, they can cover a negative balance without it affecting their credit score or reputation, and they can avoid getting stuck in a cycle of high-interest, short-term loans.

Everybody wins with a responsible overdraft service. The consumer gets access to liquidity with convenience in a time of need, and your financial institution enhances the consumer relationship by offering greater value. This, in turn, organically leads to revenue growth through an ethical, consumer-centric service.

BRIDGING **THE DIVIDE**, INCLUSIVELY AND EQUITABLY

A good barometer for a product or service is if it is inclusive for all of your consumers and if it offers them equity.

Yet, some overdraft programs set eligibility and limits based on complicated algorithms involving consumer data, including specific deposit and overdraft activity, related balances and more. These “matrix” or “dynamic” programs result in changing limits for consumers, which naturally leads to confusion when a need to overdraft occurs. Will the payment clear? The user can never know for sure.

When program eligibility favors one group over others or restricts access to the service based on abstract data and difficult-to-explain factors, compliance violations (and damage to consumer relationships) can occur.

The more equitable and inclusive way to provide an overdraft service is to offer an established limit based on simplified eligibility criteria. That way, your consumers know exactly what to expect, and they can make an informed decision in the moment. Plus, a “fixed-limit” program is easy for employees to explain without actual or perceived discrimination, keeping all parties happy.

When your account holders have difficulty managing their checking account, having a responsible overdraft safety net can help them avoid the short- and long-term consequences that often come with utilizing other ways to borrow money.

Are you offering your consumers a fair, safe and reliable service they can count on? At ADVANTAGE, we can help you deliver a responsible overdraft solution so you can continue to offer more value to your account holders while fulfilling a vital consumer need.

“With fully transparent disclosures and ongoing communication resources, [consumers] have more confidence in what Overdraft Privilege offers. As a result, more are inclined to consider the program as an option to support their financial security.”

– Southwestern financial institution, \$134MM assets





ABOUT THE AUTHOR

John Cohron is CEO at ADVANTAGE. With over 20 years of experience managing consulting operations and technology development, he is a forward-thinking leader passionate about driving innovation and growth for community banks and credit unions to strengthen their competitive position.

ADVANTAGE, the experts in overdraft compliance, contract negotiations, and account growth, has earned the trust of the financial services industry by providing consumer-focused recommendations and data-driven results for four decades. We address the evolving needs of financial institutions and answer pressing questions on expense reduction, preserving revenue, increasing value and improving performance.

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