



# Is Your Overdraft Program **UNMANAGED?**

*You Might Be Surprised!*





There are many proverbs about the consequences of “standing still” and how the concept connotes the lack of progress or growth. One well-known example is attributed to author Timothy Ferriss: “Many a false step was made by standing still.” While the concept is applicable to many things: everyday life decisions, risk-taking, business models, it can also be accurately attributed to overdraft limits. Is your overdraft program standing still? In other words, are you offering only static, one-size-fits-all limits? Giving every account holder the same overdraft limit means that your program is really unmanaged, because you’re not actively addressing the biggest lever for managing charge offs and addressing risk.

American consumers differ dramatically in their income levels, deposit behavior, transactional activity and ability to repay. So why would you offer the same limit to all your account holders?

## *DID YOU KNOW?*

You don’t have to be a mega bank or one of the largest credit unions to offer a managed overdraft program with customizable limits based on ability to repay!

Why offer a managed overdraft program? Here are the top 3 reasons you should:

- 1** → **Provide a higher level of service to account holders**
- 2** → **Meet compliance demands now - and in the future**
- 3** → **Drive incremental overdraft revenue**

## First, let's define the difference between a managed and unmanaged overdraft program.

Both strategies enable your institution to automatically allow or disallow overdrafts for those account holders who utilize your service – it's just that you may think your program is managed today when it really isn't!



**UNMANAGED** programs provide a “one-size-fits-all” approach that is determined at account opening. All account holders who qualify to be in the program, receive the same overdraft limit; OR the limit varies based on account type (i.e., \$500 for Free Checking and \$750 for Premier Checking). And then, you never actively manage these limits going forward.



**MANAGED** programs assign limits calculated automatically based on a myriad of account holder data points, including specific deposit and overdraft activity. This data enables your institution to establish a risk profile for each account and assign individualized overdraft limits based on the account holder's ability to repay the overdraft, and is updated in response to changing conditions.

Both types of programs have been in use for many years, although community-sized banks utilize unmanaged programs more widely due to the previously high cost of developing or purchasing the tools required to offer more sophisticated managed programs.

However, times have changed and so must financial institutions. Software which can set overdraft limits based on the account holder's ability to repay—the hallmark of a modern, automated discretionary overdraft program—is now affordable to implement and can help institutions provide a higher level of service, meet compliance demands and drive incremental income better than unmanaged programs with the same overdraft limits across the board for everyone based solely on account type.

Now, we'll explain the top three reasons why your financial institution should be offering a managed program, regardless of your size or assets.



## **You'll Provide a Higher Level of Service to Your Account Holders**

Although unmanaged programs with fixed overdraft limits may sufficiently serve the broad base of account holders, they can be a disservice to two types of consumers: 1) Those who overdraw their account more than the fixed overdraft limit and have the ability to repay their overdrafts; and 2) Those whose economic circumstances prevent them from being able to repay the overdraft.

Data shows that in the first group, the majority of these consumers typically can afford to repay the overdrafts and fees. They are living a convenience-driven lifestyle and they rely on the service to help them when their funds fall short.

Institutions with unmanaged programs generally set an overdraft limit which was designed to cover the middle of the bell curve (for example, a \$500 limit for everyone with your basic checking account). Doing this subjects your higher-income account holders to more denied transactions and returned items—resulting in greater dissatisfaction, especially since they have demonstrated their ability to repay an overdraft.

Conversely, allowing the second group of consumers with lower incomes to overdraw within the fixed limit while their transactional behavior suggests they do not have the ability to repay is also a disservice, but one that can have devastating consequences for the affected, including potentially being driven out of the banking system because of a history of charge offs.

With a MANAGED program, your institution provides account holders a personalized overdraft service—one that pays more items for those account holders who appreciate and can afford the service, while pulling back on overdraft limits for those account holders whose ability to repay has diminished. Not only does this translate into better service to your account holders, it also manages risk by assigning limits based on an account holder's ability to repay.

Federal regulatory guidance requires that financial institutions monitor the credit risk of each account holder.

In the Federal Financial Institutions Examination Council (FFIEC) 2005 Joint Guidance on Overdraft Protection Programs, the FFIEC wrote: "Institutions also should monitor these accounts on an ongoing basis and be able to identify consumers who may represent an undue credit risk to the institution. Overdraft protection programs should be administered and adjusted, as needed, to ensure that credit risk remains in line with expectations. This may include, where appropriate, disqualification of a consumer from future overdraft protection. Reports sufficient to enable management to identify, measure, and manage overdraft volume, profitability, and credit performance should be provided to management on a regular basis."

This ongoing monitoring requires a managed program, one using advanced algorithms that analyze account holder data on a daily basis and alert you to take action such as adjusting overdraft limits, suspending the service, suggesting counseling, etc.

Outdated unmanaged overdraft systems with fixed limits simply cannot provide this level of sophistication. However, without it, your institution is at risk for higher charge-offs and at a loss when justifying overdraft limits to regulators.



**You'll Meet  
Current Compliance  
Demands and Better  
Respond to Future  
Regulation Changes**

With an overdraft program lacking managed limits, your financial institution does not have the ability to increase an account holder's overdraft limit when that person's capacity to repay changes. As a result, your institution forgoes income while your account holder suffers.

Is your institution aware of the number of debit/ATM transactions denied for reason of non-sufficient funds (NSF)? A large percentage of these denials may happen to your account holders who have opted in to your overdraft service for one-time debit and ATM transactions (Reg. E). These customers have proactively requested that you allow them to overdraft at these channels and they are willing to pay you a fee, but their transactions are being denied. Not only does this present a service dilemma, but it represents a missed opportunity for additional income.

MANAGED programs allow your institution to generate additional revenue by honoring more overdrafts, including Reg. E transactions, and helping more account holders meet their short-term funding needs, while giving you the ability to better manage charge off levels.

If you're ready to move to a truly managed overdraft program that upgrades your service, compliance and revenue, [contact Velocity Solutions](#) to learn how we can help!



## **Managed Limits Lead to Additional Overdraft Revenue**



Founded in 1995 and servicing the transaction accounts of over 30 million consumers and business owners, Velocity Solutions has unparalleled expertise in using data to optimize revenue, risk and service for banks and credit unions. Velocity's solutions use the power of digitization and big data to drive new accounts, generate new non-interest income, responsibly offer overdraft services, digitize consumer and business lending, and manage risk and compliance.

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