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**DEPARTMENT OF THE TREASURY**

**Office of the Comptroller of the Currency**

**[Docket ID OCC-2013-0005]**

**Guidance on Supervisory Concerns and Expectations Regarding Deposit Advance**

**Products**

**AGENCY:** Office of the Comptroller of the Currency, Treasury (OCC).

**ACTION:** Final guidance.

**SUMMARY:** The OCC is issuing final supervisory guidance entitled “Guidance on Supervisory Concerns and Expectations Regarding Deposit Advance Products” (Guidance), which addresses safe and sound banking practices and consumer protection in connection with deposit advance products.

**FOR FURTHER INFORMATION CONTACT:**

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**SUPPLEMENTARY INFORMATION:**

## **I. Introduction**

The Office of the Comptroller of the Currency (OCC) is issuing the Guidance to clarify the OCC's application of principles of safe and sound banking practices and consumer protection in connection with deposit advance products. The Guidance details the OCC's supervisory expectations in connection with any deposit advance product offered by OCC-supervised financial institutions (banks) to address potential credit, reputation, operational, and compliance risks. The OCC expects a bank to apply the principles set forth in this Guidance to any deposit advance product it offers.

## **II. Description of Guidance**

A deposit advance product is a small-dollar, short-term loan or line of credit that a bank makes available to a customer whose deposit account reflects recurring direct deposits. The customer obtains a loan, which is to be repaid from the proceeds of the next direct deposit. These loans typically have high fees, are repaid in a lump sum in advance of the customer's other bills, and often are not subject to fundamental and prudent banking practices through which a bank can determine the customer's ability to repay the loan and meet other necessary financial obligations.

The OCC continues to encourage banks to respond to customers' small-dollar credit needs; however, banks should be aware that deposit advance products can pose a variety of credit, reputation, operational, compliance, and other risks. The OCC is issuing the Guidance to ensure that any bank offering these products does so in a safe and sound manner and does not engage in practices that would increase these risks.

## **III. Comment Letters Received**

The OCC received over 100 official comments on the proposal<sup>1</sup>. After consideration of all such comments, the OCC is issuing the Guidance substantially as proposed, but with certain amendments. The amendments to the Guidance are meant to provide further clarification of certain provisions, including those raised by the commenters.

Several commenters stated they believed the OCC issued the Guidance to address consumer protection issues, not safety and soundness concerns. Additionally, some commenters stated the Guidance would create new rules and regulations within the consumer protection arena, which the OCC does not have the jurisdiction to promulgate. The Guidance, like other supervisory guidance issued by the prudential banking regulators, highlights supervisory expectations based on applicable laws and regulations. It is intended to make a bank aware of the risks related to deposit advance products and provide guidelines to follow, based on safety and soundness principles, if it offers, or is considering offering, deposit advance products. The Guidance, in part, is also designed to help a bank understand which specific consumer compliance laws and regulations may be applicable to these types of loans.

Many commenters also questioned whether guidance relating to a determination of a customer's financial capacity and the level of effort necessary to complete such an analysis may be overly burdensome. The OCC, however, believes analyzing recurring deposits (inflows) and checks/credits/customer withdrawals (outflows) over at least a six-month period is appropriate because it would afford a bank the opportunity to use readily available information to determine whether the customer has the ability to repay the loan

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<sup>1</sup> See "Proposed Guidance on Deposit Advance Products; Withdrawal of Proposed Guidance on Deposit-Related Consumer Credit Products," 78 FR 25353 (April 20, 2013).

without needing to borrow repeatedly from any source, including re-borrowing, to meet necessary expenses. When determining the appropriate credit limit for a customer, there is no expectation in the Guidance that the bank do any additional analysis of inflows and outflows to determine ability to repay other than the specific transactions occurring within the account being used to repay the deposit advance product. However, as a matter of policy, a bank may consider other factors in determining overall eligibility for the product, including performance related to other accounts at the bank.

Several commenters also expressed concerns that this Guidance would have a “chilling effect” on the overall small-dollar, short-term credit market, and potentially drive consumers to illegal and/or unregulated lenders. However, the OCC is aware of a number of banks offering affordable small-dollar loans at reasonable terms to their customers.

Certain other commenters expressed concerns with the underwriting requirements as they relate to classified credits. Specifically, commenters interpreted the proposal to mean it was necessary to look outside of their bank (e.g., obtaining a credit report) to determine whether the customer had any delinquent or adversely classified credits, and was therefore ineligible for their product. This was never the intent of the Guidance. The OCC has added language to clarify that the eligibility and underwriting expectations described in the Guidance do not require the use of credit reports.

A number of other commenters questioned whether the Guidance would be applicable to deposit advance products that are designed to resemble “lines of credit” given that the proposal uses the term “loan.” To address this concern, language has been

added to state that the Guidance is applicable to all deposit advance products regardless of how the extension of credit is structured.

Some commenters, primarily state regulatory agencies, raised the concern that the Guidance would preempt applicable state laws, including usury laws, and potentially limit the ability of states to regulate these types of products. This was never the intent of the Guidance. Therefore, to address these concerns, the OCC has added a footnote to the section on Compliance and Consumer Protection Related Concerns clarifying that the Guidance does not impinge on state usury laws, to the extent they are applicable.

Commenters also raised concerns about banks using the proceeds of certain government benefits (e.g., Social Security) in determining a customer's ability to repay a deposit advance loan. The commenters suggested that, because government benefits are "designed to cover basic living expenses," the Guidance should discourage a bank from using proceeds from these benefits to determine a customer's ability to repay deposit advance loans. The Guidance does not distinguish between types of inflows, but more generally cautions a bank against making a loan that cannot be repaid to any customer, including Social Security and other government benefit recipients.

A related concern raised by commenters had to do with the impact of the "cooling off" period. For example, the commenters felt a required cooling off period might result in some customers obtaining larger advances than they might otherwise, because their access to additional advances would be delayed by the cooling off period.

The Guidance makes clear that an OCC-supervised bank is expected to assess the customer's ability to repay a loan while allowing the customer to continue to meet typical recurring and other necessary expenses such as food, housing, transportation, and

healthcare, as well as other outstanding debt obligations. Additionally, the bank's underwriting criteria should ensure the appropriate deposit advance limit is established and that customers can meet these criteria without needing to borrow repeatedly. The underwriting standards detailed in the Guidance, along with the cooling off provision, should prevent customers from taking out loans they cannot repay.

#### **IV. Guidance**

The text of the Guidance follows:

##### **OCC Guidance on Supervisory Concerns and Expectations Regarding Deposit Advance Products**

The Office of the Comptroller of the Currency (OCC) is issuing this “Guidance on Supervisory Concerns and Expectations Regarding Deposit Advance Products” (Guidance) to OCC-supervised financial institutions (banks) that offer deposit advance products. The Guidance is intended to ensure that banks are aware of the significant risks associated with deposit advance products and supplements the OCC's existing guidance on payday loans and subprime lending.<sup>2</sup> Although the OCC encourages banks to respond to customers' small-dollar credit needs in a responsible manner and with reasonable terms and conditions, deposit advance products pose a variety of credit, reputation, operational, and compliance risks to banks.<sup>3</sup>

**Background:** A deposit advance product is a type of small-dollar, short-term credit product offered to customers maintaining a deposit account, reloadable prepaid

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<sup>2</sup> OCC Advisory Letter AL 2000-10, “Payday Lending” (November 27, 2000); OCC Bulletin 2001-6, “Expanded Guidance for Subprime Lending Programs” (Subprime Lending Guidance) (January 31, 2001), jointly signed by the OCC, the Board of Governors of the Federal Reserve (Board), the Federal Deposit Insurance Corporation (FDIC), and the Office of Thrift Supervision (OTS).

<sup>3</sup> This Guidance does not apply to banks' overdraft lines of credit. Overdraft lines of credit typically do not have repayment characteristics similar to deposit advance products.

card, or similar deposit-related vehicle at a bank. The bank provides a credit feature that allows the customer to obtain a loan in advance of the customer's next direct deposit. The deposit advance is based on the customer's history of recurring deposits. Typically, the advance is offered as an open-end line of credit.<sup>4</sup> While the specific details of deposit advance products vary from bank to bank, and also may vary over time, those currently offered incorporate some or all of the characteristics described below.

**Cost:** The cost of the deposit advance is typically based on a fee structure, rather than an interest rate. Generally advances are made in fixed dollar increments and a flat fee is assessed for each advance. For example, a customer may obtain advances in increments of \$20 with a fee of \$10 per every \$100 advanced. The cost of the deposit advance can be more expensive than other forms of credit, such as a credit card or a traditional line of credit.

**Eligibility, Loan Limits, and Ability to Repay:** Typically, a customer is eligible for a deposit advance if the deposit account has been open for a certain period of time and the customer receives recurring deposits. Banks typically require a minimum sum to be directly deposited each month for a certain period of time in order for the customer to be eligible for a deposit advance loan. Currently, some banks permit a recurring deposit as low as \$100.

The maximum dollar amount of the advance is typically limited to a percent or amount of the recurring monthly deposit. For example, some banks permit the deposit advance to be the lesser of \$500 or 50 percent of the scheduled direct deposits from the preceding statement cycle, rounded up to the nearest \$10. The advance limit does not

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<sup>4</sup> This Guidance applies to *all* deposit advance products, regardless of whether the deposit advance product is structured as open- or closed-end credit.

include the fee associated with the advance. In addition, some banks will allow the advance even if the customer's account is currently overdrawn. Some banks also permit a customer to exceed the advance limit, at the bank's discretion.

Typically, the bank does not analyze the customer's ability to repay the loan based on recurring debits or other indications of a need for residual income to pay other bills. The decision to advance credit to customers, based solely on the amount and frequency of their deposits, stands in contrast to banks' traditional underwriting standards for other products, which typically include an assessment of the ability to repay the loan based on an analysis of the customer's finances.

**Repayment:** Repayment is generally required through an electronic payment of the fee and the advance with the next direct deposit. Typically, the bank is paid first before any other transactions are paid. In some cases, a bank will apply a time limit on how soon it will take the fee and the advance from the direct deposit, but the time limit is minimal, usually one or two days. If the first deposit is insufficient to repay the fee and the advance, the repayment will be obtained from subsequent deposits. If the deposits are insufficient to repay the fee and the advance within a certain time period, typically 35 days, then the bank executes a forced repayment by sweeping the underlying deposit account for the remaining balance. Unlike a payday lender, the bank has automatic access to the underlying deposit account. In some cases, customers may be able to access program features that allow for a longer repayment period than 35 days; however, this is not usually allowed.

If the deposit account funds are insufficient to repay the fee and the advance, then the account goes into overdraft status. Some banks will charge an overdraft fee based on

the deposit advance overdrawing the account. Other banks will only charge overdraft fees based on any subsequent transactions that overdraw the account.

Although the deposit advance limit is based on an amount or percentage of the monthly deposit, the repayment can be based on a shorter time period. For example, if a customer receives direct deposits of \$500 every other Friday from her employer, her monthly direct deposit would be \$1000. Under the typical bank's advance limit, she could receive an advance of \$500 with a fee of \$50. If she obtains the deposit advance on the Thursday before her payday, then the bank will obtain repayment on Friday. The bank will take the entire \$500 paycheck. In addition, the customer will still owe \$50 in principal because the deposit was only sufficient to pay the \$50 fee and \$450 in principal. Assuming the customer has no other source of income, the customer will need to rely on savings to pay bills until the next paycheck. At the next paycheck, the bank will take the remaining \$50 in principal and the customer will have \$450 to pay all outstanding bills.

Some banks have implemented alternative repayment methods that provide more flexibility to the customer. For example, some banks will permit repayment to extend through to the second direct deposit if the first direct deposit falls below a specific dollar threshold. In addition, some banks allow payment by mail rather than electronic transfer, but may charge a fee for this option. Finally, some banks offer an installment loan option, but may also charge an additional fee or may only offer this option if the customer cannot repay the advance and fee from the monthly deposits.

**Repeat Usage Controls:** Banks often have repeat usage limits that trigger a “cooling off” period during which the customer cannot take out a deposit advance, or the credit limit is reduced. For example, some banks may prevent an advance for 35 days if

the customer has used the service at least once each month in the previous six-month period. However, the customer can resume use of the product after the 35-day period is completed. Other banks may prevent an advance for one full billing cycle if the customer borrows the entire amount of the advance each month in the previous six months. However, the customer can avoid this limit by taking out something less than the maximum advance.

**Marketing and Access:** Banks market deposit advance products as intended to assist customers through a financial emergency or to meet short-term needs. These advances, however, are typically not included with the bank's list of available credit products, but are instead listed as a deposit account "feature." Customers are alerted to the availability of the products by a reference on their account statements or a "button" or hot link on their personal accounts' webpages, but it is not clear that the customers are made equally aware of less expensive alternatives.

## **SUPERVISORY CONCERNS WITH DEPOSIT ADVANCE LOANS**

Although the OCC encourages a bank to respond to customers' small-dollar credit needs, deposit advance products pose supervisory risks. These products share a number of characteristics seen in traditional payday loans, including: high fees; very short, lump-sum repayment terms; and inadequate attention to the consumer's ability to repay. As such, a bank needs to be aware of these products' potential to harm consumers, as well as elevated credit, reputation, operational, and compliance risks.

The combined impact of both an expensive credit product and short repayment periods increases the risk that customers may end up using what is marketed as a short-

term credit product that results in debt over an extended period of time. Specifically, deposit advance customers may repeatedly take out loans because they are unable to fully repay the balance in one pay period while also meeting typical recurring and other necessary expenses (e.g., housing, food, and transportation). Customers may feel compelled to take out another loan very soon thereafter to make up for the shortfall. This is similar to the practice of “loan flipping,” which the OCC, the FDIC, and the Board have previously noted to be an element of predatory lending.<sup>5</sup> Though deposit advance products are often marketed as intended for emergency financial assistance, and as unsuitable for meeting a customer’s recurring or long-term obligations, the OCC believes the product’s design results in consumer behavior that is frequently inconsistent with this marketing and is detrimental to the customer.

To address concerns that certain customers become dependent on deposit advance products to meet their daily expenses (as evidenced by their repeated borrowings), certain lenders now require customers who have taken out a specified number of deposit advance loans within a certain time frame to wait for a specified period before they are eligible to take out a new loan. However, the OCC is concerned these cooling off periods can be easily avoided and are ineffective in preventing repeated usage of these high-cost, short-term loans, for longer-term borrowing needs.

Weak underwriting increases the risk that the customer’s account may become overdrawn and result in multiple overdraft fees when subsequent transactions are presented for payment. Some banks assess overdraft fees when the automatic repayment of the deposit advance loan causes the associated account to reflect a negative balance.

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<sup>5</sup> *Subprime Lending Guidance*, jointly signed by the OCC, the Board, the FDIC, and the OTS (January 31, 2001).

## **Safety and Soundness Risks**

**Credit Risk:** Customers who obtain deposit advance loans may have cash flow difficulties or blemished or insufficient credit histories that limit other borrowing options. The high aggregate cost of numerous and repeated extensions of credit that may be a consequence of this product further increases credit risk. Lenders that offer deposit advance loans typically focus on the amount of the customer's monthly deposit for underwriting purposes. Failure to consider whether the income sources are adequate to repay the debt while covering typical living expenses and other debt payments presents safety and soundness risks.

Numerous and repeated extensions of credit to the same individual may be substantially similar to continuous advances and subject the bank to increased credit risk. While re-aging, extensions, deferrals, renewals, and rewrites of lending products can be used to help customers overcome temporary financial difficulties, such practices, if repeated, can cloud the true performance and delinquency status of the portfolio.<sup>6</sup> Further, a bank should ensure customers do not use deposit advances to make payments on other loans at the bank, as this could mask a lack of repayment ability and delinquencies on other loans at the bank.

Relying on the amount of the customer's incoming deposits without consideration of expected outflows does not allow for a proper assessment of the customer's ability to repay the loan and other necessary expenses. This failure to properly assess the customer's financial capacity, a basic underwriting principle, increases default risk.

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<sup>6</sup> See "Federal Financial Institutions Examination Council's Uniform Retail Credit Classification and Account Management Policy," 65 FR 36903 (June 12, 2000). This policy is addressed more fully in the "Credit Quality" section of this Guidance. See also OCC Bulletin 2000-20, "Uniform Retail Credit Classification and Account Management Policy" (June 20, 2000).

**Reputation Risk:** Reputation risk is the risk arising from negative public opinion. Deposit advance products are receiving significant levels of negative news coverage and public scrutiny. This increased scrutiny includes reports of high fees and customers taking out multiple advances to cover prior advances and everyday expenses. Engaging in practices that are perceived to be unfair or detrimental to the customer can cause a bank to lose community support and business.

**Operational Risk:** Banks remain responsible for compliance with all applicable laws and regulations, including the activities of a third party.<sup>7</sup> The OCC is aware of banks working with third parties to develop, design and service the deposit advance product. The existence of third-party arrangements may, when not properly managed, significantly increase banks' reputation, compliance, and, operational risks. Some of the risks are associated with the underlying activity itself, similar to the risks faced by a bank directly conducting the activity. Consequently, third-party arrangements may expose the bank to regulatory action and may impact the bank's ability to establish new or service existing customer relationships.

**Compliance Risk:** The significant risks associated with deposit advance lending products may subject banks to the risk of litigation - both from private lawsuits and regulatory enforcement actions.

### **Compliance and Consumer Protection Related Concerns**

Deposit advance products must comply with all applicable federal laws and regulations, some of which are outlined below. In some circumstances, certain state laws

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<sup>7</sup> See OCC Bulletin 2013-29, "Third-Party Relationships: Risk Management Guidance" (October 30, 2013).

may be applicable.<sup>8</sup> It is important that a bank's deposit advance products be reviewed by counsel for compliance with all applicable laws prior to implementation. Furthermore, although the guidance below outlines federal laws and regulations as of the date this Guidance is published, applicable laws and regulations are subject to amendment. In addition, statutes and regulations will have different applications depending on how a deposit advance product is structured. A bank offering deposit advances should carefully consider whether and how these laws and rules will apply to the particular version of the deposit advance product it is providing. Accordingly, a bank should monitor applicable laws and regulations for revisions and to ensure that its deposit advance product is fully compliant. Federal laws and regulations applicable to deposit advance products include the following:

**The Federal Trade Commission Act (FTC Act):** Section 5 of the FTC Act prohibits unfair or deceptive acts or practices (UDAP).<sup>9</sup> The OCC enforces this section pursuant to its authority in Section 8 of the Federal Deposit Insurance Act, 12 U.S.C. 1818.<sup>10</sup> An act or practice is unfair where it: (1) Causes or is likely to cause substantial injury to consumers; (2) cannot be reasonably avoided by consumers; and (3) is not outweighed by countervailing benefits to consumers or to competition. Public policy may also be considered. An act or practice is deceptive if: (1) There is a representation, omission, or practice that misleads or is likely to mislead a consumer; (2) the consumer's interpretation is reasonable under the circumstances; and (3) the misleading representation, omission, or practice is material.

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<sup>8</sup> This Guidance has no bearing on state usury laws or existing federal laws regarding usury. *See* 12 U.S.C. 85, 1831d(a).

<sup>9</sup> 15 U.S.C. 45(a) and (n).

<sup>10</sup> *See* OCC Advisory Letter 2002-3, "Guidance on Unfair or Deceptive Acts or Practices" (March 22, 2002).

Deposit advance products may raise issues under the FTC Act depending upon how the products are marketed and administered. Any FTC Act analysis will be dependent on the facts and circumstances in a particular matter.

The prohibition on UDAP applies not only to the product, but to every stage and activity, from product development to the creation and rollout of marketing campaigns, and to servicing and collections. For example, marketing materials and disclosures should be clear, conspicuous, accurate, and timely and should describe fairly and adequately the terms, benefits, potential risks, and material limitations of the product.

**Truth in Lending Act (TILA):** TILA and Regulation Z require creditors to provide cost disclosures for extensions of consumer credit.<sup>11</sup> Different rules apply to Regulation Z disclosures depending on whether the loan is an open- or closed-end credit product. A bank should ensure the product's disclosures comply with the applicable requirements. TILA advertising rules for open-end credit require that, if an advertisement states any periodic rate that may be applied, it must state the rate as an Annual Percentage Rate, using that term.<sup>12</sup> Similarly, TILA advertising rules for closed-end credit require that, if an advertisement states a rate of finance charge, it must state the rate as an Annual Percentage Rate, using that term.<sup>13</sup>

**Electronic Fund Transfer Act (EFTA):** A program that involves the use of electronic fund transfers must meet the applicable disclosure and other requirements of EFTA and Regulation E.<sup>14</sup> EFTA requires disclosures,<sup>15</sup> prohibits creditors from

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<sup>11</sup> 15 U.S.C. 1601 *et seq.* TILA is implemented by Regulation Z, 12 CFR Part 1026.

<sup>12</sup> *See* 12 CFR 1026.16(b)(1).

<sup>13</sup> *See* 12 CFR 1026.24(c).

<sup>14</sup> 15 U.S.C. 1693 *et seq.* EFTA is implemented by Regulation E, 12 CFR Part 1005.

<sup>15</sup> *See, e.g.,* 12 CFR 1005.7, 1005.8, and 1005.9.

mandating that loans be repaid by “preauthorized electronic fund transfers,”<sup>16</sup> and allows customers to withdraw authorization for “preauthorized fund transfers.”<sup>17</sup>

**Truth in Savings Act (TISA):** A program that involves a consumer’s deposit account must meet the disclosure requirements of TISA and Regulation DD.<sup>18</sup> Under TISA, deposit account disclosures must include the amount of any fee that may be imposed in connection with the account and the conditions under which the fee may be imposed.<sup>19</sup> TISA also prohibits a bank from making any advertisement, announcement, or solicitation relating to a deposit account that is inaccurate or misleading or that misrepresents their deposit contracts.<sup>20</sup> TISA disclosures enable consumers to make informed decisions about their deposit accounts at a bank. A consumer is entitled to receive TISA disclosures at account opening, when the terms of the consumer’s account are changed, and when a periodic statement is sent.

**Equal Credit Opportunity Act (ECOA):** Under ECOA and Regulation B, creditors are prohibited from discriminating against an applicant on a prohibited basis in any aspect of a credit transaction.<sup>21</sup> This prohibition applies to deposit advance products. The creditor’s discretion, for example in determining the application of eligibility requirements, loss mitigation options, and fee waivers, may raise fair lending risk.<sup>22</sup> Steering or targeting certain customers on a prohibited basis toward deposit advance

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<sup>16</sup> See 12 CFR 1005.10(e).

<sup>17</sup> See 12 CFR 1005.10(c).

<sup>18</sup> 12 U.S.C. 4301 *et seq.* TISA is implemented by Regulation DD at 12 CFR Part 1030 for banks and federal savings associations.

<sup>19</sup> See 12 CFR 1030.4(b)(4).

<sup>20</sup> See 12 CFR 1030.8.

<sup>21</sup> 15 U.S.C. 1691 *et seq.* ECOA is implemented by Regulation B, 12 CFR Part 1002. ECOA prohibits discrimination on the basis of race, color, religion, national origin, sex, marital status, age (provided the applicant has the capacity to contract), the fact that all or part of the applicant’s income derives from a public assistance program, and the fact that the applicant has in good faith exercised any right under the Consumer Credit Protection Act.

<sup>22</sup> See Interagency Fair Lending Examination Procedures (August 2009) at 9-13.

products while offering other customers more favorable credit products may also raise fair lending risk. Additionally, providing different product terms or conditions and different servicing or loss mitigation options to similarly situated customers on a prohibited basis may also violate ECOA.

In addition to the general prohibition against discrimination, ECOA and Regulation B contain specific rules concerning procedures and notices for credit denials and other adverse actions. Regulation B defines the term “adverse action,” and generally requires a creditor who takes an adverse action to send a notice to the consumer providing, among other things, the reasons for the adverse action.<sup>23</sup>

## **SUPERVISORY EXPECTATIONS**

Deposit advance lending presents significant consumer protection and safety and soundness concerns, irrespective of whether the products are issued by a bank directly or by a third party. The OCC will take appropriate supervisory action to address any unsafe or unsound banking practices associated with these products, to prevent harm to consumers, and to ensure compliance with all applicable laws. Examinations will focus on potential safety and soundness issues and compliance with applicable consumer protection statutes.

Examiners will assess credit quality, including underwriting and credit administration policies and practices. In addition, examiners will assess the adequacy of capital, reliance on fee income, and adequacy of the allowance for loan and lease losses (ALLL). Compliance with applicable federal consumer protection statutes, management’s oversight, and relationships with third parties will also be assessed.

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<sup>23</sup> See 12 CFR 1002.2(c) and 1002.9.

**Credit Quality:** The Uniform Retail Credit Classification and Account Management Policy (Retail Classification Policy) establishes guidelines for classifying consumer loans, such as deposit advance loans, based on delinquency, but also grants examiners the discretion to classify individual retail loans that exhibit signs of credit weakness, regardless of delinquency status. An examiner also may classify consumer portfolios, or segments thereof, in which underwriting standards are weak and present unreasonable credit risk.

Deposit advance loans often have weaknesses that may jeopardize the liquidation of the debt. Customers often have limited repayment capacity. A bank should adequately review repayment capacity to assess whether a customer will be able to repay the loan without needing to incur further deposit advance borrowing.

Deposit advance loans that have been accessed repeatedly or for extended periods of time could be evidence of inability to repay and inadequate underwriting. A bank should monitor for repeated or extended use, as will be discussed in greater detail in the discussion of underwriting expectations below.

**Underwriting and Credit Administration Policies and Practices:** As part of the credit quality review, examiners will assess underwriting and administration policies and practices for deposit advance loan products. Eligibility and underwriting criteria for deposit advance loans, consistent with eligibility and underwriting criteria for other bank loans, should be well documented in the bank's policy. The criteria should be designed to assure that the extension of credit, including all associated fees and expenses, can be repaid according to its terms while allowing the customer to continue to meet typical recurring and other necessary expenses such as food, housing, transportation, and

healthcare, as well as other outstanding debt obligations. Additionally, criteria should ensure that customers can meet these requirements without needing to borrow repeatedly. Banks should maintain appropriate criteria to prevent churning and prolonged use of these products. Underwriting for deposit advance products should occur prior to opening such accounts and should be monitored on an ongoing basis. Repetitive deposit advance borrowings could indicate weak underwriting and may be criticized in the Report of Examination and then taken into account in a bank's ratings, as appropriate.

Bank policies regarding the underwriting of deposit advance loan products should be written and approved by the bank's board of directors, and be consistent with the bank's general underwriting standards and risk appetite. Factors a bank should address in its written underwriting policies for deposit advance products include the following:

- The Length of a Customer's Deposit Relationship With the Bank. A bank should ensure that the customer relationship is of sufficient duration to provide the bank with adequate information regarding the customer's recurring deposits and expenses in order to prudently underwrite deposit advance loans. The OCC will consider sufficient duration to evaluate a customer's deposit advance eligibility to be no less than six months.
- Classified Credits. Customers with delinquent or adversely classified credits with the bank that is offering the deposit advance product should be ineligible.
- Financial Capacity. In addition to any eligibility requirements, the bank should conduct an analysis of the customer's financial capacity including income

levels.<sup>24</sup> Underwriting assessments should consider the customer's ability to repay a loan without needing to borrow repeatedly from any source, including re-borrowing, to meet necessary expenses. The financial capacity assessment should include:

- An analysis of the customer's account for recurring deposits (inflows) and checks/credit/customer withdrawals (outflows) over at least six consecutive months. Lines of credit of any sort, including overdrafts, and drafts from savings should not be considered inflows. In reviewing a customer's transactions to determine deposit advance eligibility, the bank should consider the customer's net surplus or deficit at the end of each of the preceding six months, and not rely on a six-month transaction average.
- After conducting the above-described analysis, determine whether an installment repayment is more appropriate.
- Cooling Off Period. Each deposit advance loan, along with all applicable fees, should be repaid in full before the extension of a subsequent deposit advance loan, and a bank should not offer more than one loan per monthly statement cycle.<sup>25</sup> A cooling off period of at least one monthly statement cycle after the repayment of a deposit advance loan should be completed before another advance may be extended in order to avoid repeated use of the short-term product.

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<sup>24</sup> While a bank may choose to obtain and review a customer's credit report for the purposes of assessing financial capacity or ongoing eligibility, obtaining a customer's credit report to assess ability to repay is not expected pursuant to this Guidance.

<sup>25</sup> The Interagency "Expanded Guidance for Subprime Lending Programs" (2001) states that loans to borrowers who do not demonstrate the capacity to repay the loan, as structured, from sources other than the collateral pledged, in this case the customer's direct deposit, are generally considered unsafe and unsound. Such lending practices should be criticized in the Report of Examination as imprudent.

- Increasing Deposit Advance Credit Limits. The amount of credit available to a customer should not be increased without a full underwriting reassessment in compliance with the bank's underwriting policies and in accordance with the factors discussed in this Guidance. Additionally, any increase in the credit limit should not be automatic and should be initiated by a request from the customer.
- Ongoing Customer Eligibility. As part of underwriting for this product, a bank should, no less than every six months, reevaluate the customer's eligibility and capacity for this product. Additionally, a bank should identify risks that could negatively affect a customer's eligibility to receive additional deposit advances.

For example:

- Repeated overdrafts (establish/set a certain number during a specified number of months).
- Evidence that the customer is overextended with respect to total credit obligations.

Additionally, a bank should monitor for repeated customer usage, which may indicate a need for alternative credit arrangements or other services, and inform customers of these available options when appropriate.

**Capital Adequacy:** Higher capital requirements generally apply to loan portfolios that exhibit higher-risk characteristics and are subject to less stringent loan underwriting requirements. Loans exhibiting subprime credit characteristics are higher-risk loans and may require higher levels of capital.

**Over-Reliance on Fee Income:** Fees associated with deposit advance products should be based on safe and sound banking principles. A bank should monitor for any undue reliance on the fees generated by such products for its revenue and earnings.

**ALLL:** Examiners will assess whether the ALLL is adequate to absorb estimated credit losses within the deposit advance loan portfolio. Examiners will also determine whether a bank engaged in deposit advance lending has methodologies and analyses in place that demonstrate and document that the level of the ALLL is appropriate.

**Consumer Compliance:** A bank should implement effective compliance management systems, processes and procedures to mitigate risks appropriately. Examiners will review a bank's program with respect to deposit advance products for compliance with applicable consumer protection statutes and regulations, including TILA, EFTA, TISA, ECOA, and Section 5 of the FTC Act.

**Operational Risk and Third-Party Relationships:** A bank is responsible for ensuring that the processes and systems, and the associated internal controls are appropriate for the delivery of products to the customer in a safe and sound manner, and in compliance with laws and regulations, whether performed by the bank or a third party. In the review of a bank's relationships with third parties, the OCC's primary supervisory concern is whether the bank is assuming more risk than it can identify, monitor, and manage. Management should allocate sufficient qualified staff to monitor for significant third-party relationships, excessive usage by customers, and excessive risk taking by the bank. Therefore, examiners will review the risks associated with all material third-party relationships and activities together with other bank risks. In certain high-risk situations,

examiners may conduct on-site third-party reviews under specific authorities granted to the OCC.

**Management Oversight:** Examiners will assess bank management’s ability to administer a deposit advance program and board oversight of the program. Furthermore, examiners will determine whether bank management has established controls and implemented a rigorous analytical process to identify, measure, monitor, and manage the risks associated with deposit advance products.

A bank should maintain adequate oversight of deposit advance programs and adequate quality control over those products and services to minimize exposure to potential significant financial loss, reputation damage, and supervisory action. The bank’s compliance management system should ensure continuing compliance with applicable federal and state laws, rules and regulations, as well as internal policies and procedures.

Management should provide the appropriate oversight and allocate sufficient qualified staff to monitor deposit advance programs. Results of oversight activities – including identified weaknesses that, should be documented and promptly addressed - should be reported periodically to the bank’s board of directors or designated committee.

## **RESPONSIBLE PRODUCTS TO MEET SMALL-DOLLAR CREDIT NEEDS**

The OCC recognizes consumers’ need for responsible small-dollar credit products. A number of banks are currently offering reasonably priced small-dollar loans at reasonable terms to their customers. If such loans are structured properly, they can provide a safe and affordable means for customers to transition from reliance on high-cost debt products that do not appropriately serve their needs. The OCC encourages banks to continue to offer these products, in a manner consistent with safety and

soundness and other supervisory considerations, and encourages other banks to consider offering such products. Properly managed small-dollar loan products offered with reasonable terms and at a reasonable cost do not pose the same level of supervisory risk as deposit advance products. The OCC encourages banks to develop new or innovative programs to effectively meet the need for small-dollar credit that do not exhibit the risks associated with deposit advance products and payday loans.

End of Guidance.

**[THIS SIGNATURE PAGE RELATES TO THE GUIDANCE ENTITLED  
“GUIDANCE ON SUPERVISORY CONCERNS AND EXPECTATIONS  
REGARDING DEPOSIT ADVANCE PRODUCTS”]**

Dated: November 20, 2013.

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Thomas J. Curry,  
Comptroller of the Currency.

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