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Abstract

Overdrafts have been an ongoing concern of policymakers, and they are one of the main issues being considered for prepaid card rules that the Consumer Financial Protection Bureau (CFPB) is currently drafting. Despite regulatory interventions and heated debate between proponents and opponents of further intervention, little research has been conducted to understand the overdraft behavior of prepaid cardholders. This paper attempts to fill that gap by analyzing a large micro-level dataset of general purpose reloadable (GPR) prepaid cardholders. We find that a small percentage of GPR prepaid cardholders regularly make overdraft transactions and incur overdraft fees, but they tend to spend and load more funds on their card as well as use their card for a longer period of time than do cardholders who do not make overdraft transactions. Our results suggest that some cardholders may be making a deliberate decision to overdraw their account and pay overdraft fees.

JEL Classification: D12; E42; G21

Keywords: Overdrafts, General purpose reloadable prepaid cards, Unbanked and underbanked

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1. Introduction

Overdraft programs have been an ongoing concern of policymakers despite recent regulatory interventions. Between 2009 and 2011, the Federal Reserve Board amended its regulations regarding overdraft programs and other financial regulators issued supervisory guidance. Nevertheless, the Consumer Financial Protection Bureau (CFPB) pointed out in its recent study that several concerns previously identified by the Federal Deposit Insurance Corporation (FDIC) before the Fed's interventions continue to persist (CFPB 2013). Primary concerns include the ability of consumers to anticipate and avoid overdraft costs on their checking accounts and the fact that a small but significant segment of consumers continue to incur a large number of overdraft fees.

Concerns over overdrafts and associated overdraft fees also extend to prepaid cards, especially general purpose reloadable (GPR) prepaid cards. Indeed, overdrafts are one of the main issues being considered for prepaid card rules the CFPB is currently drafting. General purpose prepaid cards are the most rapidly growing payment instrument, with a 48 percent compound annual growth rate between 2006 and 2012 (Federal Reserve System). Among those cards, GPR prepaid cards are gaining the most traction among unbanked and underbanked consumers, who do not have access to or prefer not to use other forms of electronic payments, such as debit and credit cards.

Proponents of further intervention urge the CFPB and financial regulators to limit or ban overdraft fees charged to checking or prepaid card account holders because, they claim, those fees cause serious financial harm to account holders. Opponents of the interventions, in contrast, argue that overdraft programs provide liquidity-constrained consumers with access to short-term

loans relatively more conveniently and less expensively than do currently available alternatives such as payday and auto title loans.

Given regulatory interventions and heated debate, the literature on checking account overdrafts has been growing recently. However, little research has been conducted on overdrafts made by prepaid cardholders. This paper attempts to fill that gap by examining GPR prepaid cardholders' actual behavior. Questions unanswered regarding overdrafts on GPR prepaid cards include: How common are overdrafts on GPR prepaid cards? What amount of overdraft fees do cardholders who make overdraft transactions typically incur? What drives overdrafts on GPR prepaid cards? Does the overdraft fee burden crowd out cardholders' spending for goods and services on their card?

This paper examines these questions using a dataset provided by NetSpend, a leading prepaid card provider and one of a few providers that offer overdraft programs on GPR prepaid cards. We begin by describing NetSpend overdraft program and our dataset as well as reporting summary statistics regarding overdrafts: the shares of cardholders who are eligible for, and who actually make use of, overdraft programs, and the intensity of overdraft usage and associated fee payments. We then examine whether overdrafts are caused by cardholders' limited attention to their account balance, how overdraft fee payments affect spending on the card, and how overdrafts and card lifespan are related.

Our results suggest that a small percentage of GPR prepaid cardholders regularly make overdraft transactions and incur overdraft fees. Cardholders who make overdraft transactions tend to incur a higher fee amount, spend and load more funds on their card, and continue using their card for a longer period of time than those who do not make overdraft transactions. While mixed evidence is found regarding whether cardholders' limited attention on their account

balance is a cause of overdraft, some cardholders appear to be making a deliberate decision to overdraw their account and pay overdraft fees.

2. Background

2.1 Overdraft programs and regulations

Overdraft programs allow checking or prepaid card account holders to overdraw their account—a transaction that would bring the account balance below zero is approved by the financial institution or the prepaid card provider at which the account is held. Typically, an overdraft fee is assessed for an overdraft transaction. Overdraft fees from checking accounts have become an important revenue source for financial institutions. According to industry reports, overdraft fees generated \$32 billion in 2013, down from a peak of \$37 billion in 2009 (Moeb's Services 2010 and 2013a). The median fee per overdraft transaction on checking accounts has gradually increased from \$26 in 2009 to \$30 in 2013 (Moeb's Services 2013b). Although analogous statistics for prepaid cards are unavailable, total overdraft fee revenue in the prepaid card industry might have increased due to the growing popularity of prepaid cards.¹ The cost burden of overdraft programs on checking and prepaid card accounts for consumers has attracted regulatory scrutiny and controversy.

To address consumer protection concerns and to curb the costs of overdraft programs on checking accounts for consumers, the Federal Reserve Board amended Regulation E in 2009 to require financial institutions to obtain affirmative consent of consumers (opt-in) before charging overdraft fees on ATM and point-of-sale debit card transactions. In 2009 and 2011, the Federal Reserve Board also amended Regulation DD to require financial institutions to disclose total overdraft fees on periodic account statements. In 2010 and 2011, supervisory guidance was

¹ As explained later, only a few prepaid card products offer overdraft programs.

issued by other financial agencies, such as the FDIC, the Office of Thrift Supervision (OTS), and the Office of Comptroller of the Currency (OCC).

Right after these interventions, overdraft fee revenues from checking accounts fell, but more recently an upward trend has again emerged. To gain a deeper understanding of overdraft programs, the CFPB initiated an inquiry into financial institutions' overdraft programs for consumer checking accounts in 2012 and published the results in 2013 and 2014 (CFPB, 2013 and 2014). The CFPB's initial report noted that some progress has been made in overdraft practices in recent years, but it also observed that several concerns identified by the FDIC in its 2008 overdraft study—conducted well before these interventions—have continued to persist. In particular, the CFPB is concerned that a small but significant segment of consumers continued to incur a large number of overdraft fees and that a subset of consumers had their checking accounts closed involuntarily after overdrawing and sustaining negative account balances for an extended period of time.

These regulatory interventions, however, do not apply to GPR prepaid cards. In fact, only a few GPR prepaid card products actually offer overdraft programs.² Those that do offer overdraft programs typically do so on an opt-in basis.³ The CFPB is currently drafting rules on prepaid cards, and overdrafts are one of the main issues being considered.

Consumer-advocacy organizations urge the CFPB to limit or ban overdraft fees charged to checking accounts or prepaid cards.⁴ They argue that overdrafts, in general, are set disproportionately to the amount of the underlying transaction and to the cost borne by financial

² Only five of the 52 prepaid cards studied disclosed the availability of overdraft programs, according to the Pew Charitable Trusts (2012).

³ The authors find eight of 58 prepaid card products whose information is available as of August 2014 have overdraft programs. Seven of the eight products are offered by NetSpend. All eight products have opt-in based overdraft programs.

⁴ See, for example, Center for Responsible Lending, Consumer Federation of America, and National Consumer Law Center (2012a and 2012b).

institutions of covering the overdraft, and that high-cost overdraft loans are structured in a way likely to lead to repeated loans, causing a “cycle of debt.” Their concerns about overdrafts on prepaid cards in particular include: (1) the practice of advertising a card as “prepaid” while including post-paid features like overdraft is deceptive; (2) prepaid card users are vulnerable consumers, trying to control their spending within their means; and (3) consumers who can handle credit (such as overdraft) are more likely to have access to checking accounts, credit cards, or other credit products, instead of depending on prepaid cards, and thus prepaid cards should be left for vulnerable consumers who cannot handle credit.

Opponents of the interventions, in contrast, argue that the growth of the availability and use of overdraft programs is consistent with consumer preferences.⁵ Overdraft programs are beneficial for liquidity-constrained consumers by providing access to short-term loans relatively more conveniently and less expensively than do currently available alternatives such as payday and auto title loans.

2.2 Previous literature

In the past several years, research on overdrafts has gradually increased, especially on checking accounts. In a two-part study, the FDIC analyzed various overdraft programs offered to checking account customers by financial institutions, as well as micro-level customer account and transaction data to examine the occurrence of overdraft activity and the characteristics of customer accounts that tend to incur the higher volume of overdraft fees (FDIC 2008). Similar to the FDIC’s study, the CFPB collected both institution-level and micro-level data to examine overdraft practices by financial institutions and overdraft activity and the associated fee burden for checking account holders after the recent regulatory interventions (CFPB, 2013 and 2014). Both studies found that one in four (or five) consumer accounts had at least one overdraft fee or

⁵ See, for example, Zywicki (2012).

non-sufficient funds (NSF) fee during the 12-month period, and nine (or eight) percent of accounts were heavy users of overdraft, incurring more than 10 overdraft or NSF fees.

The Independent Community Bankers of America (ICBA) conducted a consumer survey to better understand the drivers of overdrafts, such as consumers' preferences for and knowledge of overdrafts and their alternatives and consumers' account monitoring behavior (ICBA 2012). The survey results suggest that consumers using overdraft programs (i) are among the most knowledgeable of alternative services to avoid overdrafts, (ii) monitor their account balance more frequently than consumers who had never used overdrafts, and (iii) tend to use payday loans.

A few studies examined whether overdrafts are substitutes for payday loans. Zinman (2010) examined the effects of a newly introduced cap on the financial charges assessed on payday loans in Oregon using survey data of consumers from two states, Oregon and Washington. He found overdrafts on checking accounts are imperfect substitutes for payday loan. Morgan, Strain and Seblani (2012) examined the effects of payday loan regulations in various states—whether payday loans are banned or enabled—on returned checks and overdraft fee income at financial institutions. They found that both the number of returned checks and the amount of overdraft fee income decline when payday credit supply expands.

Stango and Zinman (2014) explored the role of limited consumer attention for checking account overdrafts. They found that consumers who took overdraft-related surveys more recently are less likely to pay an overdraft fee, suggesting consumers have a limited, time-varying attention to day-to-day household finance. Their results also suggest that attention shocks (such as taking an overdraft-related survey) may have a stronger effect on consumers with less education and lower financial literacy.

In contrast to the growing literature on checking account overdrafts, little research has been conducted on prepaid card overdrafts. As GPR prepaid cards have gained popularity more recently, the literature on prepaid cards that analyzes card usage and fee payments in general has emerged (e.g., Rhine et. al., 2007; Wilshusen et. al., 2012; Hayashi and Cuddy, 2014). No studies have yet analyzed the use of overdraft by GPR prepaid cardholders, although Hayashi and Cuddy (2014) include overdraft in their analysis as a variable to explain card usage behavior. To the best of our knowledge, this is the first paper to examine the overdraft use and associated fee payments by GPR prepaid cardholders.

3. NetSpend overdraft program and data

The analysis in this paper is based on data furnished by NetSpend, a leading prepaid card provider and one of very few prepaid card providers who offer overdraft programs. No other leading prepaid card provider (e.g., Green Dot, American Express, Chase, and other large banks) offers an overdraft program.⁶ In this section, we begin by describing the overdraft program offered by NetSpend during the 2011-2012 period, which corresponds to the period of our dataset. We then explain our dataset and report key summary statistics regarding overdrafts.

3.1 Overdraft program offered by NetSpend

NetSpend offers its overdraft program to its GPR prepaid cardholders on an opt-in basis.⁷ Thus, cardholders who want the overdraft capability must review and accept the terms of the program and enroll in the program (opt-in).⁸

⁶ The authors find Insight Card Services provides an overdraft program on its prepaid cards. However, the market share of Insight prepaid cards is likely to be smaller than those of leading prepaid card providers. Insight prepaid cards offer a remarkably similar overdraft program to NetSpend's, which is described below.

⁷ The description in this section is applicable only to the overdraft program offered to NetSpend-branded GPR prepaid cardholders. A few depository institutions issue NetSpend-branded GPR cards but at least one of them does not offer an overdraft program.

⁸ NetSpend also provides a free-of-charge, non-enrollment based overdraft buffer for up to \$10 in a negative balance to accounts that meet certain criteria.

Not all NetSpend cardholders are eligible for the overdraft program. To qualify, a cardholder must (1) receive an ACH (direct) deposit of at least \$200 every 30 days and (2) provide a valid email address so that NetSpend can provide notice when an overdraft transaction is made.⁹ Eligibility for the program is determined on a monthly basis. If a cardholder cannot satisfy one or more conditions in a given month or has a negative balance for more than 30 days, the overdraft capability will be deactivated. Once deactivated, it can only be reactivated if the cardholder retakes all the aforementioned steps.

NetSpend's overdraft program is designed not only to allow cardholders to overdraw their account but also to prevent them from incurring overdraft fees as a result of overdrawing their account. To those who qualify for and opt in to the program, NetSpend does not assess an overdraft fee on any transaction that overdraws the cardholder account by \$10 or less.¹⁰ Further, they are given 24 hours to resolve any pending transaction that overdraws their account by more than \$10—in other words, bring their balance back to zero or positive. If they are unable to do so, they must pay an overdraft fee of \$15. NetSpend allows cardholders who opted in to the program to overdraw their account up to a maximum overdraft amount, which is set at its discretion.¹¹ Although a separate fee is assessed for each overdraft transaction, NetSpend caps these fees at three per month, or \$45.¹²

⁹ Cardholders also must consent to the delivery of electronic communications. One such communication is a notice of “excessive use of overdraft” sent by NetSpend via email to cardholders for each batch of six overdraft fee payments they make. Once eligible, a cardholder must wait an additional 36 days before the overdraft capability is activated.

¹⁰ In addition, NetSpend does not assess an overdraft fee on a transaction as long as the transaction keeps the account positive at the time of authorization even if it brings the balance negative at the time of settlement. NetSpend processes transactions in the order it receives them for settlement.

¹¹ The maximum overdraft amount also includes fees (such as overdraft fees).

¹² It is possible that a cardholder makes four or more overdraft transactions, each of which overdraws the cardholder account by more than \$10, in a month. But the cardholder is not charged more than \$45 overdraft fees in a month, due to the fee cap.

Once being assessed an overdraft fee, cardholders have a 30-day window in which to resolve their negative balance without further consequence. If it takes longer than 60 days, NetSpend permanently deactivates the overdraft capability on the account. Three negative-balance episodes each lasting more than 30 days also result in permanent deactivation of the overdraft capability.

3.2 Data

The data provided by NetSpend contain all GPR prepaid accounts that were active over the one-year period between July 1, 2011 and June 30, 2012. An active account is defined as an account that made at least one debit transaction during the one-year timeframe. Four types of debit transactions available for NetSpend account holders are (i) purchase transactions, (ii) cash withdrawal transactions, (iii) bill payments, and (iv) person-to-person transfers between NetSpend cardholders. More than three million accounts are included in the dataset.

The dataset is a rich source of account information. First, it includes overdraft information: how many overdraft transactions each account holder has made, how many overdraft fees the account holder has incurred, and when the account holder incurred the first overdraft fee. Second, it contains information about reloads: how the funds to the account were loaded (e.g., whether the account was ever reloaded, periodically vs. occasionally reloaded, and self-funded vs. direct deposits by third parties) and the total number and value of loads over the life of the account. A third set of information is about account characteristics, such as program types (i.e., whether enrolled in a monthly purchase fee program or a per-transaction fee program), types of card distributor (e.g., check casher, retail, tax refunds, etc.), and opt-in or utilized services (e.g., emails, text-message alerts, customer service calls, or online account access portal). A fourth set of information is aggregate transaction and fee payment information,

such as the total number and value of each of the four types of debit transactions and the total number and value of fee payments by each fee category. Fifth, the dataset contains important dates, such as the account creation date, the first dates of various types of load and debit transactions and fee payments, and the last date a debit transaction was made. Finally, it includes each account holder's zip code—no other information about the account holder is available.

3.3 Summary statistics: Use of overdraft and incurred overdraft fees

Relatively few NetSpend cardholders ever qualify for the overdraft program.¹³ Among the three million cardholders in the data, 14 percent are estimated to be eligible for the program for almost the entire lifespan of the account (Chart 1).¹⁴ Of these longer-term eligible cardholders, 31 percent overdraw their accounts by more than \$10 at least once (*overdrafters*). A little over 12 percent of overdrafters never incur overdraft fees. In total, a mere 4.5 percent of cardholders in the data ever overdraw their accounts by more than \$10 and 3.9 percent incur overdraft fees, suggesting that overdraft transactions (hereafter an overdraft transaction refers to the transaction that overdraws the account by more than \$10), as well as overdraft fee payments are relatively unusual phenomena among NetSpend cardholders.

Although overdraft transactions are relatively unusual among *all* cardholders, they are quite common for overdrafters. On average, overdrafters conduct 33 overdraft transactions over the course of the account lifespan and 1.7 overdraft transactions per month (Table 1).¹⁵ Compared to

¹³ As mentioned in Footnote 7, at least one NetSpend-branded GPR prepaid card issuer does not offer the overdraft program. Since our dataset does not include issuer information, we cannot distinguish cardholders based on their issuer. Thus, among eligible or ineligible cardholders we estimate in this section include cardholders who *would be* eligible or ineligible if they were offered the same overdraft program.

¹⁴ Four criteria used for the eligibility estimation are: (1) receiving direct deposits at least once a month; (2) \$200 or greater monthly average direct deposit amount; (3) email address provided to NetSpend; and (4) the card is active more than 36 days after the initial direct deposit date. For at least a short period, however, 21 percent of cardholders are estimated to be eligible. For this eligibility estimation, we use two criteria: (1) at least two direct deposits in the lifespan of the account and (2) email address provided to NetSpend.

¹⁵ The number of months from the account creation date to the last debit date is used to calculate the monthly overdraft transactions, because the card's eligible and ineligible months for the overdraft program is unobservable.

overdrafters who have incurred at least one overdraft fee, overdrafters who have never incurred an overdraft fee make fewer overdraft transactions per month on average (1.8 vs. 0.9 transactions). As mentioned above, not all overdraft transactions result in an overdraft fee. As Chart 2 depicts, for most overdrafters the number of overdraft fee payments is much smaller than the number of overdraft transactions. Even among overdrafters who pay overdraft fees, they do so for only 43 percent of their overdraft transactions on average; and only 2 percent pay an overdraft fee for each of their overdraft transactions made over the course of the account lifespan. Among all overdrafters, the average overdraft fee incurred on an adjusted monthly basis is \$9.12, and it increases to \$10.40 if excluding overdrafters who have never incurred overdraft fees.¹⁶

A few observations can be made from these statistics. First, as the average number of monthly overdraft transactions indicates, many overdrafters make overdraft transactions regularly rather than sporadically. Second, as the total number of overdraft transactions over the lifetime of the card account suggests, overdrafters keep using their prepaid cards for a longer period of time. Third, at least some overdrafters take advantage of the 24-hour window to resolve pending overdraft transactions so that they can avoid paying overdraft fees, as evidenced by the larger number of overdraft transactions than the number of overdraft fees.

These observations pose important questions to policymakers. To what extent can overdrafters' constant overdrawing their account be explained by their preference for using an overdraft as a short-term loan mechanism over available alternatives such as payday and auto title loans? To what extent is their constant overdrawing and incurring of overdraft fees causing a "cycle of debt," wherein the fee burden tightens the account's already constrained liquidity and

¹⁶ The average monthly overdraft fee during the eligible months is likely higher. Less than 1 percent of overdrafters pay more than two overdraft fees (\$30) per month, and less than 25 percent pay more than one (\$15) but less than two (\$30) overdraft fees per month.

leads the cardholder to repeatedly overdraw? Do very short-term (24 hour) loans help maintain cash flow for cardholders or can they be avoided if cardholders pay more attention to their card account balance? The next section sheds light on these questions by comparing the behavior of overdrafters and non-overdrafters.

4. Overdrafters vs. non-overdrafters

This section compares overdrafters and non-overdrafters, both of whom are eligible for the overdraft program, in three areas: (1) effort to keep track of account balance; (2) fee burden and its potential effects on card use; and (3) card lifespan.

4.1 Effort to keep track of account balance

Consumers' limited attention has been touted as one of the causes of overdrafts.¹⁷ From the NetSpend data, cardholders' monitoring of their account balance cannot be directly observed; however, whether cardholders opted in (or used) services which enable them to view their balance—other than via the default periodical paper statements—is observable. Besides email communication, which is, by requirement, used by all cardholders who are eligible for the overdraft program, NetSpend provides a text message alert service and an online account access portal (similar to online banking) to its cardholders at no charge. Cardholders can also call the customer service line. While a call to the automated balance inquiries is free, each balance inquiry call to a representative (i.e., in-person) costs \$0.50.

Somewhat surprisingly, the data show that the share of cardholders who opted in (or used) each of these services is higher among overdrafters than among non-overdrafters (Table 2). For the text message alert service, the share is significantly higher (95 vs. 86 percent, respectively).

¹⁷ See, for example, Stango and Zinman (2014).

For online account access and customer service calls, the share differences are small; nevertheless, relatively more overdrafters use these services than non-overdrafters.

The share differences remain statistically significant even after controlling for other account characteristics. To examine what factors explain a given service opted by cardholders, we estimate binomial probit models. The marginal effects are reported in Table 3. If all other characteristics are identical, the probabilities of overdrafters' opting in to (or using) the text alert service, online account access portal, and customer service call center are higher than those of non-overdrafters by 7.4 percentage points for text alert, by 1.2 percentage points for online account access, and by 0.4 percentage points for customer service calls. These results suggest that overdrafters are at least better armed with tools that help them keep track of their account balance than are non-overdrafters.

The NetSpend data also include various types of fee payments by cardholders, which reveal cardholders' balance inquiries via certain venues. Overdrafters make balance inquiries via ATM or by calling to a customer service representative slightly less often than do non-overdrafters (on average, 1.8 and 1.9 times per month by overdrafters and by non-overdrafters, respectively).¹⁸ However, the number of balance inquiries via text message and online account access, which cannot be observed from the data, could be greater for overdrafters than for non-overdrafters given that relatively more overdrafters opted in to those services.

On net, the data do not necessarily support the idea that overdrafters have limited attention relative to non-overdrafters. Further data and research on actual attention, however, are needed to answer this question definitively.

¹⁸ Even after controlling for other account characteristics, the difference in the number of balance inquiries via ATM and customer service calls between overdrafters and non-overdrafters is statistically significant.

4.2 Fee burden and its potential effects on card use

How much more do overdrafters pay in fees relative to non-overdrafters? Obviously, overdraft fees will significantly contribute to the fee amount difference because non-overdrafters do not incur overdraft fees. Other fees will also contribute to the fee difference but to a lesser degree than overdraft fees because of their relatively smaller value—at \$15, the overdraft fee is one of the largest fees assessed by NetSpend. Since a negative balance close to the maximum overdraft amount may trigger more transactions declined, overdrafters may incur more decline fees. As mentioned above, overdrafters incur fewer balance inquiry fees than do non-overdrafters. If overdrafters make more ATM transactions than non-overdrafters, then overdrafters must incur more ATM fees. Unlike ATM transactions, purchase transactions do not necessarily increase fees. For those enrolled in a monthly fee program, the fee amount per month is constant (either \$4.95 or \$9.95, depending on direct deposit amount). Those who do not enroll in a monthly fee program incur a per transaction fee of \$1 for a signature transaction and \$2 for a PIN transaction. Thus, behavioral differences between overdrafters and non-overdrafters will also affect the total fee amount they incur.

Not surprisingly, the monthly total fee amount incurred by overdrafters is greater than that of non-overdrafters. The average monthly total fee amount is \$28.32 for overdrafters and \$19.44 for non-overdrafters (Table 4). But, without overdraft fees, the amount is surprisingly similar for overdrafters and non-overdrafters (\$19.20 vs. \$19.44). Fee amounts of each fee category, however, vary between overdrafters and non-overdrafters. As expected, the decline fee amount is greater for overdrafters. The ATM fee amount is also greater for overdrafters due to their greater number of ATM transactions (3.4 vs. 2.9 per month for non-overdrafters) (Table 6). The fee amount related to purchase transactions (per transaction fees and monthly fee program fee) is

smaller for overdrafters, not because they make fewer purchase transactions but because relatively more overdrafters enroll in a monthly fee program than do non-overdrafters (82 vs. 63 percent) to avoid paying per transaction fees (Table 2).

To examine whether the fee amount differences remain qualitatively the same after controlling for other account characteristics, we conduct regression analysis using OLS models. The results are presented in Table 5. The sign of the coefficient for a dummy indicating overdrafters is consistent for all fee categories but “total – overdraft.” After controlling for other characteristics, overdrafters incur a slightly greater fee amount per month (\$0.88) than do non-overdrafters even when excluding overdraft fees. For decline, balance inquiry, ATM, and other fees, the magnitude of the coefficient of overdrafters is qualitatively similar to the average fee difference between overdrafters and non-overdrafters observed in Table 4. However, for purchase-related fees, the magnitude of the coefficient is smaller after controlling for other characteristics than the average fee difference (-\$0.16 vs. -\$1.93=\$9.01-\$10.94), while for total fees, the magnitude is larger (\$9.91 vs. \$8.88=\$28.32-\$19.44).

How does the fee burden affect card use, especially the debit amount? The monthly debit amount is positively correlated with the monthly overdraft fee amount as well as the monthly total fee amount. On average, overdrafters spend \$1,440 on their cards in a month, which is greater than \$1,215, the average monthly debit amount of non-overdrafters (Table 6). Overdrafters also load more funds on their cards per month than do non-overdrafters (\$1,508 vs. \$1,276, respectively). The excess monthly load amount after excluding the monthly debit and total fee amounts is about the same for overdrafters and non-overdrafters (\$39 and \$41).

Even after controlling for other account characteristics, the positive correlation between monthly debit/load amount and monthly total fee/overdraft fee amount holds, although the

difference of monthly debit or load amount between overdrafters and non-overdrafters is less pronounced. OLS regressions suggest that being an overdrafter would increase the monthly debit and load amounts by \$185 and \$188, respectively (Table 7), which are smaller than the difference in the average monthly debit and load amounts, \$225 ($=\$1,440-\$1,215$) and \$232 ($=\$1,508-\$1,276$), respectively. In contrast, the difference of average monthly balance becomes greater after controlling for other characteristics ($-\$6$ vs. $-\$2=\$39-\$41$).

Among overdrafters, those who incur more overdraft fees per month generally spend more and load more. The average monthly debit and load amounts for overdrafters who incur two or more overdraft fees per month are \$1,741 and \$1,823 while those for overdrafters who incur less than one overdraft fee per month (e.g., overdrafters who incur fewer than twelve overdraft fees in a year) are \$1,376 and \$1,441 (Table 6). The positive correlation between monthly debit/load amount and monthly overdraft fee amount is even stronger among overdrafters with negative average daily balances. The correlation coefficients exceed 0.35 among overdrafters with negative average daily balance whereas they are about 0.21 among overdrafters with positive average daily balance (Table 8).

The results suggest that the fee burden, in general, is not large enough to crowd out cardholders' spending on their card account for goods and services.¹⁹ Multiple overdraft fee payments (up to three) per month tend to be made by cardholders whose monthly load amounts are relatively higher. Those cardholders spend more on their cards for goods and services than do both overdrafters who make less than one overdraft fee payment per month and non-overdrafters.

¹⁹ NetSpend limits not just the number of overdraft fees assessed in a month but also the overdraft amount, inclusive of fees, in a month, which may help prevent cardholders from getting into a cycle of debt.

4.3 Card lifespan

Overdraft is positively correlated not only with load and debit amounts but also with card lifespan. Cardholders who are eligible for the overdraft program keep their cards longer than non-eligible cardholders. This is because receiving direct deposits—one of the requirements for overdraft capability—is strongly positively correlated with card lifespan.²⁰ Even among eligible cardholders, however, overdrafters' card lifespan is longer than non-overdrafters'. The median card lifespan after cardholders become eligible for overdraft is 630 days among overdrafters and 540 days among non-overdrafters (Table 9).²¹

However, the causality is unclear. On the one hand, the use of overdraft may increase card lifespan—cardholders who make use of the overdraft capability of their card may become more loyal customers and keep using their card longer than those who do not take advantage of it. On the other hand, cardholders who keep their card for a longer period of time may be more likely to have at least one overdraft incident and to incur at least one overdraft fee than cardholders who keep their card for only a short period of time.

The NetSpend data provide some evidence that supports the second conjecture, but the data cannot reject the first conjecture, either. Among overdrafters, those who incurred at least one overdraft fee keep their card longer than those who have never incurred such fee (the median lifespan after they became eligible for overdraft is 690 days for the former and 450 days for the latter). Furthermore, for 35 percent of overdrafters who incurred overdraft fees, there is at least a one-year lag from the date they become eligible for overdraft to the date they incur the first overdraft fee. The lag is less than one year for the rest (less than three months for 35 percent and between three to twelve months for the remaining 30 percent). These findings may support the

²⁰ The mean and median lifespan for all cards in the data are 347 days and 90 days, respectively. The mean and median lifespan for different account characteristics are shown in Hayashi and Cuddy (2014).

²¹ Conditional survival rates are used to calculate the median lifespan. For details, see Hayashi and Cuddy (2014).

second conjecture—the longer the cardholders keep their card, the more likely it is that they make an overdraft transaction and incur an overdraft fee.

The lag from the eligible date to the first overdraft fee date also affects card lifespan after the first overdraft fee. The longer the lag, the longer the card lifespan is. In particular, the median card lifespan after the first overdraft fee is 810 days for overdrafters with at least a one-year lag, 600 days for overdrafters with a three- to twelve-month lag, and 450 days for overdrafters with less than a three-month lag. There is no simple explanation for this behavioral difference. One might speculate that overdrafters who have not incurred an overdraft fee for more than one year after becoming eligible to overdraft are “accidental” users—they unknowingly make a debit transaction which pushes their account balance below zero—rather than habitual users who purposely use overdraft. However, over the course of their entire card lifespan, these overdrafters, on average, overdraw their account 41 times with 17 of these overdrafts resulting in overdraft fees, making the “accidental” hypothesis difficult to justify.²² In fact, their multiple overdraft transactions and longer account lifespan may instead support the first conjecture—cardholders who make use of the overdraft capability keep using their card longer.

5. Conclusion

Overdrafts are not common phenomena among GPR prepaid cardholders. Not many GPR prepaid cards offer overdraft programs. NetSpend is one of very few GPR prepaid card providers that offer overdraft programs, and its program has stringent eligibility requirements. Even among overdraft-eligible cardholders, a relatively small fraction of them ever actually overdraw their

²² The “cooling-off periods” imposed by NetSpend on repeated users of overdraft make it even more difficult to justify this hypothesis. Cooling-off periods are built into the overdraft program to discourage cardholders from making excessive overdrafts. Specifically, after the first 12 overdraft fee payments, NetSpend suspends the cardholder’s overdraft capability for 30 days. For each additional batch of 12 overdraft fee payments, a 90-day suspension is imposed.

account. Nevertheless, a small percentage of GPR prepaid cardholders regularly make overdraft transactions and incur overdraft fees. These so-called overdrafters tend to incur a larger amount of fees but spend and load more funds on their card than do non-overdrafters, indicating that the overdraft fee burden, in general, is not large enough to crowd out overdrafters' spending amount on their card account for goods and services. Moreover, overdrafters, especially those who incur overdraft fees, continue using their card for a longer period of time than do non-overdrafters.

Whether cardholders' limited attention to their account balance causes overdrafts is inconclusive, but our analysis indicates that overdrafters are at least better armed with tools that help them keep track of their account balance than are non-overdrafters. Furthermore, some overdrafters avoid overdraft fees by bringing their account balance back to zero or positive immediately after the overdraft transaction (within 24 hours). These results suggest that some cardholders may be making a deliberate decision to overdraw their account and pay overdraft fees. Further research is required to examine whether, in aggregate, overdraft programs on GPR prepaid cards enhance or diminish the welfare of cardholders, many of whom are financially underserved consumers.

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Chart 1: Overdraft eligible and actual users

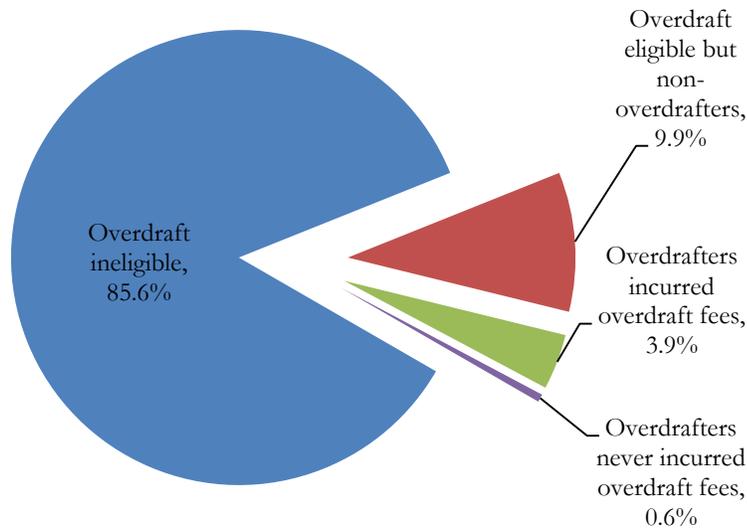


Chart 2: Number of overdraft fee payments versus overdraft transactions

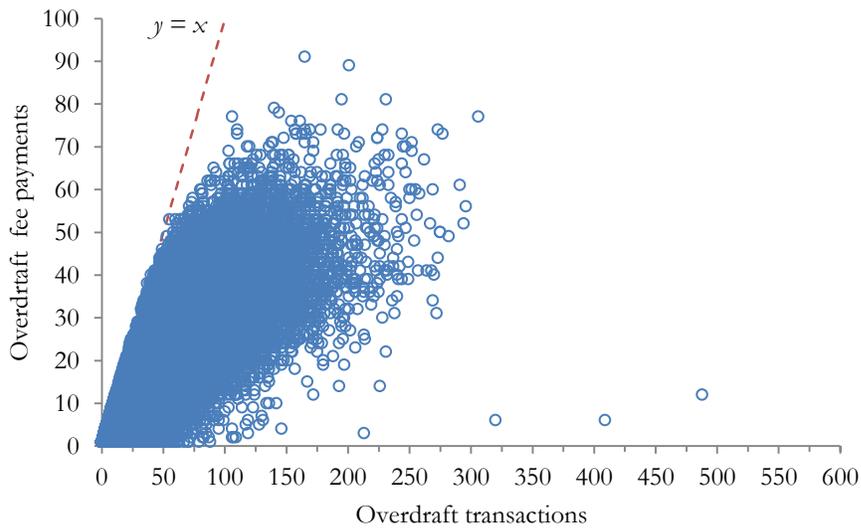


Table 1: Overdraft transactions and overdraft fees (average)

	All	Incurred overdraft fees	Never incurred overdraft fees
Overdraft transactions entire card lifespan (#)	32.6	36.2	7.7
Overdraft transactions per month (#)	1.7	1.8	0.9
Overdraft fee payments per month (#)	0.6	0.7	0.0
Overdraft fee payments per month (\$)	\$9.12	\$10.40	\$0.00

Table 2: Account characteristics

	Non-overdrafters	Overdrafters
Services opted-in or used		
Text alert	86%	95%
Online access	98%	100%
Customer service call	98%	99%
Fee program type		
Monthly fee program	63%	82%
Per-transaction fee	37%	18%
Source of direct deposit		
Government	24%	31%
Non-government	76%	69%
Card distributor type		
Check casher	52%	59%
Direct (NetSpend)	35%	40%
Retail	8%	0%
Disbursement	3%	0%
Tax	0%	0%
Other	2%	1%

Table 3: Binomial probit model: marginal effects

	Text alert		Online access		Customer service call	
Overdrafters	0.074***	(0.001)	0.012***	(0.000)	0.004***	(0.000)
Per-transaction fee	-0.064***	(0.001)	-0.008***	(0.000)	-0.003***	(0.000)
Government direct deposit	0.030***	(0.001)	-0.002***	(0.000)	0.013***	(0.000)
Card distributor type						
Direct (NetSpend)	-0.025***	(0.001)	0.005***	(0.000)	-0.009***	(0.000)
Retail	-0.079***	(0.002)	0.008***	(0.001)	-0.022***	(0.000)
Disbursement	-0.021***	(0.003)	0.003***	(0.001)	-0.006***	(0.001)
Tax	0.002	(0.008)	0.001	(0.002)	-0.001	(0.003)
Other	-0.039***	(0.003)	-0.003***	(0.001)	-0.009***	(0.001)
Log-likelihood	-147,249		-33,838		-32,877	

Notes: The marginal effects are estimated when all variables are at their means. The model includes an intercept term, the number of debit transactions per month and shares of ATM transactions, bill payments, and person-to-person transfers in the debit transactions in number as independent variables. Standard errors are in (). *** Significant at 0.01 level.

Table 4: Fee amount in a month (average)

	Non-overdrafters	Overdrafters
Overdraft	\$0.00	\$9.12
Decline	\$0.29	\$0.70
Balance inquiry	\$0.96	\$0.89
ATM	\$7.11	\$8.50
Purchase-related	\$10.96	\$9.02
Others	\$0.13	\$0.10
Total	\$19.46	\$28.33
Total - Overdraft	\$19.46	\$19.21

Table 5: OLS model: monthly fee amounts

	Decline		Balance inquiry	
Overdrafters	0.378***	(0.002)	-0.074***	(0.005)
Per-transaction fee	-0.054***	(0.002)	0.113***	(0.005)
Government direct deposit	-0.053***	(0.002)	0.478***	(0.005)
Card distributor type				
Direct (NetSpend)	0.095***	(0.002)	-0.693***	(0.005)
Retail	-0.011**	(0.004)	-0.242***	(0.010)
Disbursement	-0.014**	(0.006)	-0.201***	(0.014)
Tax	-0.055***	(0.020)	0.089*	(0.046)
Other	0.041***	(0.008)	-0.294***	(0.018)
Adjusted R-squared	0.182		0.142	

	ATM		Purchase-related		Others	
Overdrafters	0.749***	(0.019)	-0.162***	(0.031)	-0.178***	(0.009)
Per-transaction fee	-1.696***	(0.020)	8.872***	(0.032)	-4.496***	(0.009)
Government direct deposit	-3.006***	(0.020)	-2.253***	(0.031)	0.029***	(0.009)
Card distributor type						
Direct (NetSpend)	0.254***	(0.018)	-1.075***	(0.029)	-0.773***	(0.008)
Retail	-1.997***	(0.038)	-2.389***	(0.061)	-1.440***	(0.017)
Disbursement	-0.421***	(0.058)	-0.395***	(0.092)	0.058**	(0.028)
Tax	1.226***	(0.182)	-0.901***	(0.292)	-1.068***	(0.083)
Other	-0.118	(0.073)	-1.407***	(0.117)	-0.396***	(0.033)
Adjusted R-squared	0.297		0.119		0.418	

	Total		Total - Overdraft	
Overdrafters	9.913***	(0.047)	0.881***	(0.044)
Per-transaction fee	6.884***	(0.048)	7.237***	(0.045)
Government direct deposit	-5.562***	(0.048)	-4.891***	(0.045)
Card distributor type				
Direct (NetSpend)	1.612***	(0.045)	-1.373***	(0.042)
Retail	-4.765***	(0.094)	-4.544***	(0.088)
Disbursement	-1.121***	(0.141)	-1.025***	(0.132)
Tax	0.181	(0.447)	-0.379	(0.417)
Other	-1.827***	(0.179)	-1.771***	(0.167)
Adjusted R-squared	0.181		0.119	

Notes: The model includes an intercept term, dummies indicating opted-in text alert, online account access, and customer service calls and the shares of ATM transactions, bill payments, and person-to-person transfers in the debit transactions in number as independent variables. Standard errors are in (). *** Significant at 0.01 level; ** Significant at 0.05 level; and * Significant at 0.1 level.

Table 6: Monthly activities (average)

	Non-overdrafters	Overdrafters			
		Number of overdraft fees per month			
		All	2 or greater	1 to 2	Less than 1
Debits (\$)	\$1,215	\$1,440	\$1,741	\$1,673	\$1,376
Loads (\$)	\$1,276	\$1,508	\$1,823	\$1,750	\$1,441
Fees (\$)	\$19	\$28	\$61	\$43	\$24
Balance=Loads-Debits-Fees (\$)	\$41	\$39	\$20	\$34	\$41
ATM transactions (#)	2.9	3.4	6.2	4.6	3.1
Purchase transactions (#)	19.0	20.7	22.0	22.0	20.3

Table 7: OLS model: monthly debit amount, load amount, and balance

	Monthly debit amount		Monthly load amount		Monthly balance	
Overdrafters	184.56***	(2.81)	188.42***	(2.96)	-6.27***	(0.60)
Per-transaction fee	-279.93***	(2.90)	-283.26***	(3.06)	-10.22***	(0.62)
Government direct deposit	-332.34***	(2.90)	-338.85***	(3.05)	-1.21**	(0.62)
Card distributor type						
Direct (NetSpend)	-182.31***	(2.68)	-185.20***	(2.83)	-1.35**	(0.57)
Retail	-127.82***	(5.57)	-124.69***	(5.87)	8.11***	(1.21)
Disbursement	89.95***	(8.31)	84.41***	(8.77)	-3.55**	(1.81)
Tax	69.98***	(26.80)	61.89**	(28.25)	-8.10	(5.72)
Other	-174.64***	(10.67)	-175.27***	(11.25)	0.05	(2.29)
Adjusted R-squared	0.089		0.083		0.216	

Notes: The model includes an intercept term, dummies indicating opted-in text alert, online account access, and customer service calls and the shares of ATM transactions, bill payments, and person-to-person transfers in the debit transactions in number as independent variables. Standard errors are in (). *** Significant at 0.01 level; ** Significant at 0.05 level; and * Significant at 0.1 level.

Table 8: Correlation coefficients between fee amounts and debit/load amounts

	Non-overdrafters	Overdrafters		
		Average daily balance		
		All	Positive	Negative
With total fee amount				
Debit amount	0.36	0.35	0.36	0.47
Load amount	0.36	0.36	0.37	0.49
With overdraft fee amount				
Debit amount	n.a.	0.16	0.21	0.35
Load amount	n.a.	0.16	0.21	0.37

Note: For all correlation coefficients, p-value is smaller than 0.0001.

Table 9: Card lifespan (median days)

	After eligible date	After first overdraft fee
Non-overdrafters	540	n.a.
Overdrafters	630	n.a.
never incurred overdraft fees	450	n.a.
incurred overdraft fees	690	630
< 3-month lag*	480	450
3- to12-month lag*	780	600
>=1 year lag*	1,500	810

Notes: n.a.: not applicable. *: Lag from the eligible date to the first overdraft date.

Appendix: Detailed statistics

Table A1: Overdraft transactions and overdraft fees

		All	Incurred overdraft fees	Never incurred overdraft fees
Overdraft transactions entire card lifespan (#)				
	Mean	32.6	36.2	7.7
	75 th percentile	46.0	49.0	8.0
	50 th	25.0	28.0	4.0
	25 th	11.0	15.0	2.0
Overdraft transactions per month (#)				
	Mean	1.7	1.8	0.9
	75 th	2.3	2.4	1.1
	50 th	1.3	1.4	0.4
	25 th	0.7	0.8	0.2
Overdraft fee payments per month (#)				
	Mean	0.6	0.7	0.0
	75 th	0.9	1.0	0.0
	50 th	0.5	0.6	0.0
	25 th	0.2	0.3	0.0
Overdraft fee payments per month (\$)				
	Mean	\$9.12	\$10.40	\$0.00
	75 th	\$13.85	\$14.84	\$0.00
	50 th	\$7.85	\$9.12	\$0.00
	25 th	\$2.88	\$4.78	\$0.00

Table A2: Fee amount in a month

	Non-overdrafters			
	Mean	25 th percentile	50 th	75 th
Overdraft	\$0.00	\$0.00	\$0.00	\$0.00
Decline	\$0.29	\$0.00	\$0.14	\$0.38
Balance inquiry	\$0.96	\$0.10	\$0.37	\$1.17
ATM	\$7.11	\$2.42	\$5.57	\$9.92
Purchase-related	\$10.96	\$5.02	\$8.05	\$12.67
Others	\$0.13	\$0.00	\$0.00	\$0.01
Total	\$19.46	\$10.31	\$16.09	\$24.57
Total - Overdraft	\$19.46	\$10.31	\$16.09	\$24.57

	Overdrafters			
	Mean	25 th percentile	50 th	75 th
Overdraft	\$9.12	\$2.88	\$7.85	\$13.85
Decline	\$0.70	\$0.13	\$0.41	\$0.93
Balance inquiry	\$0.89	\$0.11	\$0.33	\$1.03
ATM	\$8.50	\$3.72	\$7.04	\$11.59
Purchase-related	\$9.02	\$4.90	\$6.82	\$9.94
Others	\$0.10	\$0.00	\$0.00	\$0.00
Total	\$28.33	\$17.55	\$25.70	\$36.15
Total - Overdraft	\$19.21	\$11.31	\$16.51	\$23.89

Table A3: Monthly activities

		Non-overdrafters	Overdrafters			
			All	2 or greater	1 to 2	Less than 1
Debits (\$)						
	Mean	\$1,215	\$1,440	\$1,741	\$1,673	\$1,376
	75 th percentile	\$1,576	\$1,878	\$2,160	\$2,120	\$1,795
	50 th	\$999	\$1,250	\$1,590	\$1,532	\$1,167
	25 th	\$639	\$784	\$1,220	\$1,041	\$734
Loads (\$)						
	Mean	\$1,276	\$1,508	\$1,823	\$1,750	\$1,441
	75 th percentile	\$1,645	\$1,957	\$2,260	\$2,207	\$1,807
	50 th	\$1,048	\$1,312	\$1,680	\$1,607	\$1,225
	25 th	\$673	\$830	\$1,290	\$1,099	\$775
Fees (\$)						
	Mean	\$19	\$28	\$61	\$43	\$24
	75 th percentile	\$25	\$36	\$70	\$49	\$30
	50 th	\$16	\$26	\$59	\$40	\$22
	25 th	\$10	\$18	\$51	\$33	\$16
Balance=Loads-Debits-Fees (\$)						
	Mean	\$41	\$39	\$20	\$34	\$41
	75 th percentile	\$24	\$36	\$6	\$29	\$38
	50 th	\$0	\$0	-\$8	-\$3	\$1
	25 th	-\$4	-\$10	-\$19	-\$15	-\$8
ATM transactions (#)						
	Mean	2.9	3.4	6.2	4.6	3.1
	75 th percentile	4.0	4.7	8.2	6.1	4.2
	50 th	2.3	2.8	5.7	4.1	2.6
	25 th	1.1	1.5	3.6	2.4	1.4
Purchase transactions (#)						
	Mean	19.0	20.7	22.0	22.0	20.3
	75 th percentile	26.3	28.4	29.6	30.0	27.9
	50 th	14.9	16.9	19.5	19.0	16.3
	25 th	7.7	8.9	11.3	10.7	8.5