PROFITABILITY AND ACCOUNT DESIGN

by Steve Brown

Product specialist and COOs at banks may feel like they need one of those oil leak arresting "Top Hat" contraptions to contain the hemorrhaging of red ink from many of their products. May is a particularly active month for bank deposit staff, as they are actively debating what to do about changes to Reg E that are set to take effect on Jul 1. In conjunction, banks are also rethinking what to do with both retail and business free checking. Let's take the latter question first.

This is an easy one - retail free checking costs banks about 3% per year on balances. Given the potential for lower OD/NSF fees, this level is about to increase to north of 3.5%. Business free checking, on the other hand, usually makes banks about 90bp on balances. As a result, banks should keep their business free checking accounts and take a 3 pronged attack for retail free checking. First, implement a service charge for the least profitable accounts. Next, for those just barely unprofitable accounts, levy a service charge unless they sign up for a profitable product/service (such as a goal oriented savings account, debit card or direct deposit). In the alternative, a minimum balance can be instituted. Finally, be prepared to let accounts go. This method is design to weed out those customers that are just using your bank for a free service and costing you money. While the average bank may lose a portion of their balances, replacing these funds with brokered or FHLB advances are far cheaper alternatives than keeping costly accounts around. Banks that can track profitability (see us if you can't) and institute the above tactics can recognize a 10%+ increase in fee income.

Next to deciding what to do with free checking, handling new Reg E changes is the next decision. Here, banks have several choices. The first choice is to do what Bank of America did and do away with electronic overdraft altogether for new customers. Here, the Bank found that it was too costly to handle tiered fees and disclosures across their multiple platforms and so it took the philosophical position that overdraft isn't appropriate given new legislation. Few banks have followed BofA's lead, but it should be noted that it does create a unique marketing position which all banks will have to counter. At the other end of the spectrum, banks are leaving their OD/NSF fee structures unchanged and just requiring new opt-in and notification procedures.

For the most part, community banks are choosing to not only require new opt-in procedures, but are restructuring their fees and tiers to better fit the customer. Some banks are charging a 1 or 2 tiered flat monthly (f.e. $5 per month) or annual fee for a set amounts of allowable ODs. Here, banks are attempting to recast their fees from one that is punitive in nature to one that is worthy of the "service" being performed. Other tactics banks are employing include discounting their fees, waiving fees for ODs under a set amount (usually $10) or allowing 1 or 2 overdrafts without charge per year. Variations on the above themes abound, but a clear path is too early to tell.

To help us get a quantitative view of the market, we ask for your help. If you have a retail operation, can you please take 3 minutes to complete a survey of what, if anything, your bank is doing (or plans to do) with respect to Reg E and overdraft protection and NSF charges? Even if you don't offer an OD program, your input would be helpful. In exchange for your time, we will send you the survey results and a case study of what one institution is doing that may be a good approach in terms of a combination of revenue, satisfaction, retention and profitability. To take the survey follow the link in the 'related links' section at the bottom of the page.

Related Links:
Overdraft/NSF Fee Survey

BANK NEWS

Federal Reserve

The Senate voted to uphold the FRB's oversight of smaller state-chartered banks in the financial reform bill.

2010 Customers

According to a ComScore survey, 64% of consumers use online bill pay, up from 45% last year. When searching for a new savings or checking account, 67% explicitly look for free checking, 37% seek out a low minimum balance, 36% look for a convenient branch or ATM and 24% examine bill pay options. Customer service is playing a larger part this year however, as 22% place customer service as a deciding factor, up from just 4% last year.

Tax Credit

The homebuyer tax credit ended last week and the results are starting to trickle in showing the impact of this event. One week later, mortgage applications are down 9.5% despite the fact that mortgage rates overall fell below 5%.

Corporate Earnings

About 85% of S&P 500 companies have reported 1Q results and earnings are up 56.5% compared to 1Q 2009. Cost cuts and higher productivity helped the average company to beat analyst estimates by about 16%.

Tax

We can complain against high taxes, but the fact is that Americans paid their lowest level of taxes since the days of Harry Truman. All taxes combined (including property, sales, etc.) consumed 9.2% of personal income in 2009, the lowest level since 1950 according to the Bureau of Economic Analysis. This is below the average of 12%. Of course, depending on your tax bracket, state you live in, etc. the taxes you paid could be substantially different than the "average."