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SCOTT J. HELFAND
CHICAGO:
312.341.9876
SCOTT.HELFAND@
HUSCHBLACKWELL.COM

SUSAN M. SEAMAN
MADISON:
608.255.4440
SUSAN.SEAMAN@
HUSCHBLACKWELL.COM

Federal Court Allows Class Action on Deposit Account Fees to Proceed

A New York federal court has largely denied a state credit union's motion to dismiss a class action lawsuit regarding non-sufficient funds (NSF) fees, overdraft fees, and out-of-network ATM fees. *See Fairchild-Cathey v. American Credit Union*, No. 21-cv-01173 (N.D.N.Y. Jan. 17, 2023). While the court dismissed the plaintiffs' allegation that the credit union breached the implied covenant of good faith and fair dealings, the court permitted the bulk of the plaintiffs' claims to proceed. In particular, the court denied dismissal of the plaintiffs' claims for breach of contract and violation of a New York deceptive practices statute.

Fee assessment practices at issue

In October 2021, the plaintiffs filed a lawsuit challenging three fee assessment practices. First, the plaintiffs alleged that the credit union charged multiple NSF fees on a single transaction in violation of their membership account agreement and fees schedule. The credit union charged a \$28 NSF fee each time a payment request by a merchant failed and was returned because of a lack of sufficient funds in an account. A member incurred multiple NSF fees for a single transaction if a merchant re-presented the payment request multiple times to the credit union.

Next, the plaintiffs argued that the account agreement and fees schedule did not permit the credit union to charge an overdraft fee when a deposit account had sufficient funds at the time of payment authorization but lacked sufficient funds at the time of settlement. This "authorize positive, settle negative" situation can occur with debit cards. The plaintiffs contended that the account agreement requires the credit union to determine overdraft status and fee assessment at the time of payment authorization. According to the plaintiffs, no overdraft fees should have been assessed to members who had insufficient funds in an account at the time of settlement.

The third fee at issue is an out-of-network ATM fee. The plaintiffs claimed that the account agreement and fees schedule did not permit the credit union to charge a separate ATM fee for each function (e.g., withdrawal, deposit, balance inquiry) the member conducted at an out-of-network ATM. Instead, the plaintiffs argued that the credit union was permitted to charge members only one ATM fee for all the functions performed at a single visit to an out-of-network ATM.

In addition to breach of contract claims, the plaintiffs argued that the credit union violated Section 349 of the New York General Business Law, i.e., the state's deceptive-practices statute. Specifically, plaintiffs alleged that—by not clearly explaining that multiple NSF fees, multiple ATM fees, and overdraft fees would be charged in the aforementioned situations—the credit union engaged in “materially misleading” conduct. The plaintiffs also claimed that the credit union violated the implied covenant of good faith and fair dealings by charging deposit account fees contrary to what members would expect under the account documents.

The credit union moved to dismiss. In so doing, the credit union argued, among other things, that the membership agreements and fees schedules unambiguously permitted the credit union to charge the challenged fees. Therefore, the credit union argued that the plaintiffs' breach of contract claim failed. The credit union also argued that, because the account documents properly disclosed the challenged fees, the plaintiffs' deceptive practices claim failed. Finally, the credit union argued that, because the federal Truth-in-Savings Act permitted the credit union to use the fee structure it used, the plaintiffs' state-law claims were preempted.

The court's decision

The court denied the credit union's motion to dismiss the breach of contract claims because the court found that the language in the membership account agreement and fees schedule is ambiguous. The court found both parties' interpretations of the agreement tenable. The court's decision parsed through the account agreement to explain how the language could be read to support each party's argument. The court also rejected the preemption argument, finding that the federal Truth-in-Savings Act does not preempt the question whether the credit union had properly disclosed the fees. The court also found that the plaintiffs pled sufficient facts to support a deception claim under the New York deceptive practices statute. However, the court granted the credit union's motion to dismiss the alleged violation of the implied covenant of good faith and fair dealings because it was duplicative of the breach of contract claim.

Notably, the parties disagreed on which version of the membership account agreement and fees schedule should be considered with the motion to dismiss. The credit union argued that the court should consider later versions of the membership account agreement (presumably with more favorable language). But the plaintiffs disputed the relevance of those documents. Moreover, the plaintiffs argued that—at the motion-to-dismiss stage—the court could consider only those documents

attached to or relied on in the complaint. The court agreed. Thus, rather than convert the credit union's motion to dismiss into a motion for summary judgment, the court refused to consider the later versions of the membership account agreement.

What this means for you: litigation and regulatory risks with deposit account fees

Deposit account fees pose increasing litigation risk and regulatory risk to depository institutions. Customers have filed numerous cases nationwide alleging that depository institutions charged overdraft, NSF, and other deposit account fees in violation of the terms of the deposit account agreement and state trade practices statutes.

Importantly, as the *Fairchild-Cathey* case illustrates, defendants must make careful strategic decisions at the outset of these cases. For example, defendants must consider whether—based on differences in potentially relevant documents—their arguments are best presented on a motion to dismiss (where courts generally put their thumbs on the scale for the plaintiff) or at a later stage of litigation (*e.g.*, summary judgment). Defendants must also consider whether, even though the plaintiffs' claims in theory implicate “form” documents (*e.g.*, account agreements sent to all customers), there are other differences—either in the documents themselves, or in how individual class members might have understood different disclosures in different places—that could defeat class certification (either as to all claims or at least as to statutory-deceptive-practices claims with fee-shifting provisions).

In addition to the litigation risk illustrated above, federal regulators have also increased their scrutiny of overdraft, NSF, and other deposit account fees as part of the Biden administration's larger war on “junk” fees. For example, the Federal Deposit Insurance Corporation issued supervisory guidance in August 2022 highlighting risks to banks charging multiple NSF fees on re-presented transactions. The Consumer Financial Protection Bureau warned in October 2022 that unanticipated overdraft fees are likely “unfair” under the Consumer Financial Protection Act. In January 2023, the National Credit Union Administration sent a letter to federal credit unions indicating that it will conduct expanded examinations of overdraft programs. Required reform of overdraft programs and overdraft/NSF fee practices could be on the horizon.

Contact us

For more information on litigation and regulatory risks with overdraft and NSF fees, contact Scott Helfand, Susan Seaman or your Husch Blackwell attorney.