
CA Supreme Court Approves Bank Recovery of Overdrafts and Fees from Accounts Containing Public Benefit Direct Deposits

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Miller v. Bank of America, No. S149178, __ Cal. 4th __ (2009), issued June 1, 2009, authorizes banks to recoup overdrafts and bank fees occurring within a single account and confirms that these setoffs are not governed by Kruger v. Wells Fargo Bank, 11 Cal. 3d 352, 356 (1974).

On June 1, 2009, the California Supreme Court held in *Miller v. Bank of America* that a bank may recover overdrawn amounts and bank fees from an account containing supplemental security income ("SSI") or other public benefit direct deposits. Plaintiffs' theory of liability was premised on the 1974 holding in *Kruger* that a bank may not satisfy a credit card debt by deducting the amount due from an independent account containing unemployment compensation and state disability benefits. The *Miller* Court held that *Kruger* was not controlling.

***Kruger* Set the Stage for *Miller* by Prohibiting Banks from Using Public Benefit Funds to Satisfy Credit Card Delinquencies**

In *Kruger*, plaintiff Jean Kruger deposited her unemployment compensation and state disability benefits into a Wells Fargo checking account. She also maintained a Wells Fargo credit card account. When Kruger's credit card account became delinquent, without notice to Kruger, Wells Fargo deducted the entire balance in Kruger's checking account and applied it towards the delinquency and to satisfy service charges on dishonored checks issued from the checking account.

In prohibiting Wells Fargo's conduct, the *Kruger* Court pointed out that funds derived from state disability insurance and unemployment compensation are exempt from attachment and execution. The *Kruger* Court found that it follows that these benefits should also be immune to a bank's right of setoff, otherwise state policy of preserving such deposits for the depositor's daily living expenses would be completely defeated. It then held that, if Kruger's account consisted of monies derived from unemployment compensation or state disability benefits, the bank may not set off its claims against those accounts.

Miller Sought to Extend the Holding of *Kruger* to Repayment of Bank Account Delinquencies and Require Remittance of Upwards of \$284 Million in Overdraft Amounts and Fees

Miller v. Bank of America was brought by class representative Paul Miller, who maintained a Bank of America (“B of A”) account containing SSI deposits. Miller overdrew his account several times, and each time B of A deducted the overdrawn amount and the associated fees (up to \$104 per day) from Miller’s subsequent SSI deposits. In 1998, Miller, relying heavily on *Kruger*, filed a class action against B of A. He alleged B of A could not cover overdrafts and overdraft fees with SSI benefits and other public benefit payments directly deposited into his checking account. The trial court certified a class of all California residents who were affected similarly to Miller. The amount of overdrafts and fees from accounts of the class totaled upwards of \$284 million.

In a split jury and bench trial, both the jury and the court concluded that B of A was prohibited from recovering overdrafts and fees from accounts containing direct deposit public benefits. A judgment was entered for the class of nearly \$360 million plus \$1,000 to qualified class members. In addition, the trial court issued an injunction against B of A.

The Court of Appeal reversed the trial court’s judgment, and the Supreme Court granted review.

The Supreme Court Limits *Kruger* to Prohibit Setoff of Exempt Funds to Satisfy Independent Debt

In affirming the Court of Appeal’s reversal, the Supreme Court acknowledged that B of A’s practice implicates to some extent the policy considerations at issue in *Kruger*, but it was ultimately persuaded that the practice of recouping overdrafts and charging fees is not prohibited by California Finance Code Section 864 or *Kruger*. The Supreme Court relied on the plain meaning and legislative history of Section 864, which limits a bank’s right to set off debts but defines “debt” to exclude “a charge for bank services or a debit for uncollected funds or for an overdraft of an account imposed by a bank on a deposit account.” A plain reading of Section 864 reveals that a bank may recoup overdrafts and associated fees without regard to the limitations imposed by Section 864 and *Kruger*. The *Miller* Court also noted the legislative intent to treat charges for overdrafts and associated fees different from the satisfaction of independent debt by restricting a bank’s ability to set off using other accounts and not its “internal balancing practices” within a single account.

The Supreme Court distinguished the policy issues at play in *Kruger*. The Court said it was “far from clear” that the public policy to provide subsistence income to the recently unemployed or the disabled would be undermined: “Indeed, an overdraft may be the result of the bank honoring, rather than bouncing, a rent or utility payment made prior to the deposit of benefit funds.” In contrast, dishonoring checks could harm the customer’s credit rating, result in additional fees and affect the customer’s relationship with merchants. Thus, the Court concluded that policy concerns at issue in *Kruger* were not present where the credits and debits occur in a single account.

Finally, the *Miller* Court relied on a June 2007 Interpretive Letter issued by the United States Office of the Comptroller of the Currency (the “OCC”), which concluded that a bank’s recoupment of overdrawn amounts and associated fees is part of a bank’s “routine maintenance” of its accounts. The OCC agreed that “[f]undamentally, the [b]ank is not creating a ‘debt’ that it then collects by recovering the overdraft and the overdraft fee from the account.”

Ultimately, the *Miller* Court held that *Kruger* does not prohibit B of A's recoupment of overdrafts and bank charges occurring within a single account containing directly deposited public benefit funds.

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