



Neighborhood Economic Development Advocacy Project

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Submitted via <http://www.regulations.gov>

To: Department of the Treasury, Fiscal Service
Social Security Administration
Department of Veteran Affairs
Railroad Retirement Board
Office of Personnel Management

Re: Proposed Rule on Garnishment of Accounts Containing Federal Benefit Payments
RIN Nos. 3206-AM17, 3220-AB63, 0960-AH18, 1505-AC20, and 2900-AN67

Dear Sirs and Madams:

Thank you for the opportunity to submit comments regarding the Agencies' proposed rule addressing the problem of garnishment of exempt funds in bank accounts. I am Staff Attorney at the Neighborhood Economic Development Advocacy Project (NEDAP), where I work in our Consumer Law Project. NEDAP is a nonprofit resource and advocacy center that works with community groups in New York City's low-income neighborhoods and communities of color to promote economic justice and to eliminate discriminatory economic practices that harm communities and perpetuate inequality and poverty.

NEDAP's Consumer Law Project provides free legal information, advice, referrals, and representation to low-income New Yorkers who have problems concerning debt collection, credit reporting, and lending discrimination. We provide services through a legal hotline, a community legal clinic, and direct representation of consumers in state and federal court. We have helped thousands of low-income New Yorkers who are struggling with debt collection issues.

Until January 1, 2009, more than one quarter of our law project's time was spent assisting clients whose exempt funds had been unlawfully restrained by creditors and debt collectors. When our clients' Social Security, Supplement Security Income, or other benefits were frozen by debt collectors, they were unable to pay rent or buy food and medicine. They suffered incredible hardship, as the process for obtaining the release of their funds often took weeks.

In 2008, New York State passed the Exempt Income Protection Act (EIPA) to address this problem. Since EIPA took effect on January 1, 2009, New Yorkers no longer have significant problems with the restraint of exempt funds. Banks and other financial institutions are prohibited from restraining accounts that receive directly deposited exempt benefits and contain \$2,500 or less. Banks likewise may not freeze any account belonging to a natural person that contains \$1,740 – the current amount of minimum wage income that is protected under all circumstances – or less. New York also has a streamlined procedure for claiming an exemption

when accounts contain exempt funds in excess of the threshold amounts. For the most part, EIPA is functioning well and has made a tremendous difference for low-income, elderly, and disabled New Yorkers.

Our experience with New York's EIPA gives us a unique perspective from which to comment on the proposed rule. In general, we wholeheartedly support the proposed rule and would like to see it adopted as soon as possible. On one hand, we wish that the benefits of EIPA were available to all Americans, and we are thrilled to see the federal government take action to protect recipients of federal benefits from unlawful restraints and garnishments of their exempt funds. The proposed federal rule improves on EIPA in a few key respects. On the other hand, there are some aspects of the proposed rule that could be improved, and we urge the Treasury Department to incorporate in its final rule the recommendations set forth below.

Positive Aspects of the Proposed Rule

1. Establishment of a "protected amount"

EIPA establishes a protected amount of \$2,500 for all accounts that receive direct deposits of statutorily exempt benefits. The protected amount has been a key to EIPA's success. A protected amount provides banks with a clear mechanism for determining whether an account is subject to restraint. In addition, it eliminates debt collectors' ability to restrain exempt funds on bogus pretexts, such as false accusations of commingling and the like. With the rise in use of electronic banking and debit cards, it is common for small amounts of money to flow in and out of an account as consumers use their debit cards to buy and return items. These small flows should not affect the exempt status of Social Security, Supplemental Security Income, and other federal benefits.

The proposed rule uses a different mechanism than EIPA to determine the exempt amount, but the general idea is similar. It is essential that the final rule make clear that the protected amount is absolutely sacrosanct and may not be restrained under any circumstances.

2. Preemption issues

a. Higher protected amount (sec. 212.9(c))

Where a state law such as EIPA may provide for a higher protected amount than the proposed rule would provide, the state law's higher protected amount should prevail. We strongly support section 212.9(c) of the proposed rule, which explicitly provides that a state may by law or regulation establish a higher protected amount.

b. Protections under state law of non-federal exempt benefits and wage exemptions

EIPA has provided critical protections to low-income New Yorkers by protecting benefits that are statutorily exempt under both federal and state law. In addition, EIPA has made the New York's wage exemption a self-effectuating exemption (i.e., New York account holders are currently entitled to at least a \$1,740 protected amount for their account), thus extending a

critical protection to working poor New Yorkers.¹ The final rule should make explicit that financial institutions may not circumvent any greater protections provided by state law.

c. “Snapshot” rule (sec. 212.6(e))

We strongly support the partial preemption of New York law by section 212.6(e), which requires a financial institution that is served with a continuing garnishment to take a “snapshot” of an account and restrain only funds that exceed the protected amount as of that “snapshot” review, instead of maintaining the restraint for a period of one year as required by New York law.² Section 212.6(e) resolves a shortcoming unfortunately not addressed by EIPA. Because New York law requires “continuing” or “ongoing” restraints of bank accounts, many financial institutions have taken the approach in New York of freezing exempt funds that are deposited into an account after it has been restrained, even where those funds are readily identifiable by the financial institution as exempt. The “snapshot” approach, by contrast, would avert this problem of restraining future deposits of exempt federal benefits.

Recommendations

1. Define the “lookback period” as 65 days, not 60 days (sec. 212.3)

The lookback period should be 65 days, not 60 days. The notice of the proposed rule indicates that it is intended to protect two cycles of benefit payments from garnishment. The problem is that most 60-day lookback periods will not cover two cycles of benefit payments because: (1) seven months out of the year have 31 days; and (2) when benefit payments are due on a date that falls on a Saturday, Sunday, or holiday, the payment is actually deposited the business day before the due date. Because of these two factors, most 60-day lookback periods will in fact capture only one payment cycle.

2. Provide a safe harbor for banks that protect exempt funds deposited prior to the lookback period (sec. 212.10(b))

Section 212.10(b) should be modified to provide a safe harbor for financial institutions that recognize the exempt status of funds deposited prior to the lookback period and refuse to seize them. For example, recipients of federal benefits often set aside large back benefit payments in special savings or CD accounts, frequently leaving the accounts untouched for years, with no additional funds deposited. The funds are unquestionably exempt and should be protected from seizure under the proposed rule. Currently, many financial institutions receiving state garnishment orders that require only non-exempt funds to be seized will not seize funds in such accounts, because of the clearly exempt nature of the funds.

The current section 212.10(b) leaves such back payments of exempt benefits unprotected from seizure because the deposits would have been made well before the lookback period. In addition, the financial institution that recognizes the exempt status of funds deposited prior to the lookback period and refuses to seize them, or releases them to the account holder after the account holder demonstrates that the funds are exempt, would not be protected under the current version of the proposed rule.

¹ N.Y. C.P.L.R. § 5222(i).

² N.Y. C.P.L.R. § 5222(b).

Financial institutions should not only be permitted, but encouraged to release all exempt funds to the account holder, either on the institution's own initiative or after an inquiry prompted by the account holder. Modifying section 212.10(b) as suggested below would achieve this objective. Without requiring a financial institution to engage in this review, this modified safe harbor would simply protect the institution from creditor challenges when it did release to the account holder exempt funds that had been deposited prior to the lookback period.

We therefore recommend the following changes to section §212.10(b) (new language in bold):

“(b) General protection for financial institutions. A financial institution that complies in good faith with this part shall not be liable to a judgment creditor for any protected amounts, to an account holder for any frozen amounts, or for any penalties under state law, contempt of court, civil procedure, or other law for failing to honor a garnishment order in cases where

(1) A benefit agency has deposited a benefit payment into an account during the lookback period; ~~or~~

(2) The financial institution has determined that an order was obtained by the United States by following the procedures in Sec. 212.4(a)(1) and (2); **or**

(3) The financial institution, after a review of its own records, releases to the account holder benefit payments as defined by this Part.”

3. *Prohibit set-off by financial institutions against exempt funds (sec. 212.8(b)), including for garnishment fees (sec. 212.6(f))*

The proposed rule inappropriately provides support for bank set-offs against exempt funds. Section 212.8(b) currently states that “Nothing in this part shall be construed to invalidate any term of condition of an account agreement . . . that is not inconsistent with this part.” Most account agreements include terms permitting the financial institution to seize funds in the account for debts owed to the bank. A number of cases have held that this is not legal when exempt funds are seized.³

As written, section 212.8(b) could be used by a financial institution to legitimize what are currently illegal and inappropriate set-offs of exempt federal funds against debts owed to that institution. We therefore recommend that section 212.8(b) be deleted.

We also recommend that section 212.6(f), concerning when financial institutions may exact a garnishment fee, be deleted. This section states that a financial institution may take a garnishment fee from the funds in the account that are in excess of the protected amount. However, this might be interpreted as permitting financial institutions to take fees from exempt

³ Tom v. First Am. Credit Union, 151 F.3d 1289 (10th Cir. 1998) (noting that there is no relevant difference between set-off and garnishment and prohibiting set-off against exempt funds); Hambrick v. First Security Bank, 336 F. Supp.2d 890 (E.D.Ark. 2004) (Social Security's anti-assignment provision prohibited application of bank's set-off provisions in bank customer's agreements with bank); Marengo v. First Massachusetts Bank, N.A., 152 F.Supp.2d 92, (D.Mass. 2001) (bank's set-off against Social Security funds violated Social Security Act); In re Brewer, 2002 WL 32917680 (Bkrtcy. S.D.Ill., Aug. 15, 2002) (42 U.S.C. § 407(a) prohibits credit union from taking debtor's Social Security funds regardless of the prior agreement of the debtors that the subject funds would act as collateral for their loans from the credit union).

funds if those funds are not covered by the protected amount. Section 212.6(f) also conflicts with section 212.8(a), which states that nothing in the rule shall be construed to limit an individual's rights to assert the exempt status of funds in excess of the protected amount.

Section 212.6(f) is unnecessary and confusing in light of other provisions of the proposed rule. Section 212.6(g) states that financial institutions may not assess garnishment fees from the protected amount. Section 212.8(a) clarifies that funds in excess of the protected amount may nevertheless be exempt. Because section 212.6(f) could be used to justify the collection of the garnishment fee from exempt funds, we therefore recommend that section 212.6(f) be deleted. In addition, the rule should clarify that where it is later determined that any garnishment fees were taken from exempt funds, the financial institution must refund those fees to the account holder.

4. *Clarify that "access" to the protected amount means full, unfettered and customary access (sec. 212.6(a))*

In New York, some financial institutions have complied with the letter, but not the spirit, of the protections provided by the Exempt Income Protection Act. EIPA requires that when an account contains directly deposited exempt funds, \$2,500 in the account is automatically exempt. When the account has a balance greater than \$2,500, EIPA permits the financial institution to freeze the account, but explicitly prohibits the institution from restraining \$2,500 of the funds in the account. Despite this express prohibition, some financial institutions have not permitted the account holder to continue to write checks or make ATM withdrawals against that \$2,500, but instead have required the account holder to come into a branch to withdraw \$2,500 in cash. This practice, which a number of large national banks have adopted, has led to bounced rent, utility, and other checks; caused benefit recipients to incur substantial bounced-check, insufficient funds, and other fees; and has made elderly and disabled benefit recipients in particular vulnerable to theft and loss of their benefits while they are leaving a branch with so much cash in hand. We have seen that one of the large national banks even issues a check for the protected amount to the account holder and then closes the account. The rule should expressly prohibit such practices.

We therefore recommend making the following changes (changes in bold) – to section 212.6(a):

“(a) *Protected amount.* The financial institution shall immediately calculate and establish the protected amount for an account. The financial institution shall ensure that the account holder has **full, unfettered and customary** access to the protected amount, which the financial institution shall not freeze in response to the garnishment order. An account holder shall have no requirement to assert any right of garnishment exemption prior to accessing the protected amount **and the protected amount shall be conclusively considered to be exempt under state and federal law.**”

5. *Improve the Notice of Garnishment (§ 212.4(a)(2))*

The notice that financial institutions are required to send to account holders should include the following information:

- (1) The exact amount of money that has been restrained, with the name and account number in which the funds are located. This information will help an account holder determine how to deal with paying future bills and how to handle the potential bounced checks already drawn on the funds that have been restrained.
- (2) The amount of the garnishment fee, if any, that the bank has assessed against the recipient's account. This information is necessary so that the recipient understands what the current balance is in the account.
- (3) The date by which some action must be taken by the account holder in order to preserve the right to assert further exemptions.
- (4) The "snapshot" nature of the garnishment, including that future funds deposited in the account will not be subject to seizure as the result of the garnishment order.
- (5) How to contact local, free, legal aid and legal services programs.

In addition, the rule should require financial institutions to tailor the notice to the laws of the jurisdiction in which the account holder resides.

Thank you for your consideration of these comments. Please do not hesitate to contact me at 212-680-5100 with questions or for more information concerning these comments.

Sincerely,

Susan Shin
Staff Attorney