CONSUMER CONCERNS

Information for Advocates Representing Older Adults

National Consumer Law Center®

Protecting Social Security and other Federal Benefits in Bank Accounts from Garnishment by Debt Collectors

Federal law provides that Social Security benefits, Veteran's benefits and SSI payments are all protected from seizure for debts owed to banks and other creditors. Despite the law, these benefits have often been seized right out of bank accounts to satisfy judgments in a process called "garnishment." (Garnishment occurs after a creditor brings a lawsuit and obtains a judgment against a debtor; it is used to seize the debtor's property to pay the judgment.) Now, because of the U.S. Department of Treasury's rule (effective May 1, 2011), banks are not permitted to seize these exempt federal benefits in response to garnishment orders in most instances.

The rule only protects federal funds that were electronically deposited directly into the recipient's bank account. In addition to Social Security, SSI, and VA benefits, the rule protects federal Railroad Retirement, federal Railroad Unemployment and Sickness, federal Civil Service Retirement System, and federal Employee Retirement System benefits. We will refer to these types of benefits as "exempt funds" or "exempt federal benefits." The rule does not protect military retirement payments or other military benefits, nor does it protect benefits provided by the states – such as welfare benefits or unemployment compensation. Those benefits are generally exempt from garnishment under state law, but the Treasury Rule does not cover them.

The Treasury Rule requires all banks and credit unions to follow a certain procedure after receiving a garnishment order from a debt collector. Once the garnishment order against a debtor comes to the bank, the bank must review all accounts owned by debtor to determine whether any of the federal benefits were electronically deposited during the preceding ***two months*** (the "look back period"). If yes, then the bank must calculate the "protected amount." The protected amount is the lesser of the sum of all exempt benefits electronically deposited into the debtor's account during the look-back period, or the balance of the account on the day the review is conducted. If the account contains a protected amount, the bank cannot freeze, or otherwise restrict the account holder's "full and customary" access to that amount.

Once the bank has determined that the account contains protected, exempt federal funds, the bank must send the account holder a notice describing what the bank has done and giving some basic information about how to protect exempt benefits that exceed the protected amount.

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Exceptions for Debts Owed to Federal Government or State Child Support

The account review is not required and there is no automatic protection of any amount, however, if either the federal government or a state child support agency issued the garnishment order. These orders must contain a special notice. In these cases, the debtor can still assert exemptions, but must do so through the usual state procedures. (See box on state exemption procedures.) However, garnishment orders issued to collect child support owed to private parties are still subject to the Treasury Rule – federal benefits will be protected from those orders.

Commingled Funds, Co-Owners & Lump-Sum Payments

In some states, the law has been that exempt funds lose their protected status whenever they are deposited into a bank account that contains non-exempt funds. The Treasury Rule applies to the exempt federal benefits whether or not the protected funds have been mixed with other funds. As long as the specified federal benefits were electronically deposited into the account during the two-month period before the garnishment order, they are protected regardless of what other funds might be in the account.

It also makes no difference if there is a co-owner on the account. Whatever amount of benefits was deposited during the look-back period is exempt, even if it was deposited in the name of the non-debtor co-owner.

The rule does not contain any cap on the amount of benefits that are protected. If the beneficiary received a lump-sum payment by electronic deposit within the two-month look-back period, it is protected regardless of its amount. However, a lump-sum payment that remains unspent in an account will lose the rule's automatic protection after two months. If a garnishment order arrives, the recipient will need to invoke state procedures to protect the remainder of the lump-sum payment.

Also, if the exempt funds were electronically deposited into one account and then transferred into another account, the funds are not protected. The "protected amount" under the rule is limited to funds that were electronically deposited into each account the bank holds in the name of the debtor.

How to Make the Most of the New Protections

Exempt funds delivered by paper checks are not protected under the new rule, and can only be protected through the applicable state process. Beneficiaries who are receiving paper checks should consider switching to electronic deposit or to the Direct Express prepaid card (See, Consumer Facts: *Your Right to Know: Direct Express Prepaid Debit Card for Social Security, SSI and Other Federal Payments,* available at http://www.nclc.org/images/pdf/high_cost_small_loans/direct-express-2pager.pdf).

The rule will not provide full protection for benefit recipients who accumulate more than two months of benefit payments in their accounts, or who are expecting or have not yet spent down a lump-sum payment. These recipients are vulnerable to garnishment of whatever amount exceeds the

STATE EXEMPTION LAWS

Every state has laws that protect some property owned by debtors from seizure by creditors – these laws are called "exemption laws." Garnishment is when a creditor takes a debtor's property to satisfy a debt. Generally, creditors cannot garnish – or seize – a debtor's property until the creditor has filed an action in court and obtained a judgment from the court.

The purpose of the exemption laws is to ensure that debtors are not made completely destitute from the payment of debts and to preserve some small amount of property for the debtor to use. State laws require that debtors be told about the judgment and their right to claim exemptions before the garnishment, and that debtors have the right to go to court and claim the exemptions to protect their property. In some states, the exemptions are automatic – the debtor need do nothing for the property to be protected. However, in most states debtors must respond in a timely way to the garnishment notice to be able to claim the state permitted exemptions and protect their property.

State exemption laws generally protect:

1. Some amount of home equity. Home equity is the difference between what is owed on a home and what the home is worth. If a home is worth $125,000 and the amount owed on the loans secured by the home is $105,000, the homeowner has $20,000 in equity.

2. Necessary household goods.

3. A small amount of value in automobiles.

4. Some money in bank accounts.

5. The debtor's tools of the trade, up to a specific value. These would be the tools the debtor uses to earn a living.

6. A portion of the debtor's wages.

7. State benefits, such as welfare (TANF), unemployment and worker's compensation.

8. Pensions and retirement benefits, IRA balances and insurance benefits and annuities, at least partially.

9. Some states have a "wild card" amount that can be applied to any property.

These are just some examples. *Every state's law, procedures and protections are different.* Debtors who have a judgment taken against them should contact the Clerk of Court in their county to find out the procedures for claiming exemptions.

“protected amount.” For example, if an account contains $5,000, which reflects that two $2,000 federal benefit payments were deposited within the last two months, the two payments are protected but the remaining $1,000 is vulnerable. Although already-paid benefits cannot be transferred onto the card, switching to the Direct Express card will protect the full amount of future benefits. In the alternative, the beneficiary can withdraw cash or spend down the bank account to protect the full amount, or can rely on asserting the exemption through state court procedures.

Recipients should not transfer funds from one account to another, as the protections of the new rule will not follow the transferred funds. For example, if a recipient receives a $1,500 electronic deposit of federal benefits, and transfers $1,000 to a different account, leaving $500 in the first account, only the remaining $500 in the first account is protected by the rule. The $1,000 transferred to the second account is vulnerable, although state law may protect this sum if it can be traced to the exempt benefits.

If there is any chance that a beneficiary will need to rely on state exemption procedures, the account should include *just* exempt benefits, not any other amounts, as some courts have denied state exemptions when the exempt funds were commingled with non-exempt funds.

For more information see, NCLC e-Report: New Treasury Rule Protects Exempt Federal Benefits from Garnishment: http://www.nclc.org/images/pdf/preemption/nclc-rpts-repo-jan-feb-2011.pdf.

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