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Practice Tips to Comply with the Final Rule on Garnishment of Federal Benefit Payments

The Department of Treasury recently issued its final rule regarding procedures financial institutions must undertake to protect directly deposited federal benefit payments from garnishment.[1] Although the final rule takes effect on June 28, 2013, because the interim rule[2] went into effect over two years ago, financial institutions likely already have most of the necessary procedures in place to comply with the final rule. Only minor tweaking to existing procedures should be required. Below are the major areas that were changed by the final rule and tips to help financial institutions focus on what changes they need to make to their existing procedures to ensure they are in compliance with the new final rule.

1. Broader Definition of "Garnishment Order"

The interim rule defined "garnishment order" as "a writ, order, notice, summons, judgment, or similar written instruction issued by a court or a State child support enforcement agency." The final rule broadens the definition of "garnishment order" to include orders or levies issued by a state or a state agency or municipality, as well as "an order to freeze an account," which includes restraining orders. The "garnishment order" may be issued by someone other than a court, including a clerk of a court, an attorney acting in his or her capacity as an officer of a court, or as noted above, a state or municipality. In other words, a "garnishment order" includes any legal process that demands the payment of deposited funds belonging to another.

2. "Protected Amount" Takes into Account Intraday Transactions

The final rule, like the interim rule, uses the XX notification method in determining what funds are exempt from garnishment and as a result should be included in the "protected amount." However, the definition of "protected amount" has been revised to include the account balance at the time the account review is performed, so that the balance will include any intraday transactions like ATM or cash withdrawals. This is a change from the interim rule which defined the "protected amount" as the balance at the open of business on the date of the account review.

3. Limiting Notices Required to be Sent to Accountholders

The interim rule requires a financial institution to send a notice to an accountholder if the balance in the account on the date of the account review is more than zero dollars and the institution establishes a "protected amount." This requirement forced financial institutions to send notices to customers even if no account funds were frozen, particularly in the case where there are no funds in excess of the "protected amount." The Treasury recognized that this requirement resulted in financial institutions sending notices with little benefit to accountholders, and created much confusion where funds were not actually frozen or

[1] Garnishments of Accounts Containing Federal Benefit Payments, Final rule, 78 Fed. Reg. 32099 (May 29, 2013), to be codified in the U.S. Treasury Regulations at 31 C.F.R. Part 212.

[2] Garnishment of Accounts Containing Federal Benefit Payments, Interim final rule, 76 Fed. Reg. 9939 (Feb. 23, 2011).

even available to be frozen. Therefore, the final rule amended this obligation to require financial institutions to send a notice to an accountholder only if (1) the balance in the account on the date of the account review is above zero dollars, (2) the institution establishes a "protected amount," and (3) there are funds in the account above the "protected amount."

4. Financial institutions may Charge a Garnishment Fee in Limited Situations

A financial institution may charge its normal and customary garnishment fee as allowed by the customer agreement and state law if there are non-protected funds available. Both the interim and final regulation prohibit a financial institution from collecting a garnishment fee from the "protected amount" in an account. However, if non-benefit funds are deposited into the account during the five business days following the account review, the financial institution may collect its normal garnishment fee from those funds so long as the fee does not exceed the amount of the non-benefit funds.

5. Practice Tips for Tweaking Procedures to Comply with the Final Rule

- Update the procedures whether automated or manual used to determine when a garnishment order has been received by the financial institution to include all legal processes that fit within the broader definition of "garnishment order."

- Revise the procedures used to determine the "protected amount" to ensure that they take into account intraday transactions.

- Change the notice procedures to ensure that notice is only sent if there are funds in the account above and beyond the "protected amount."

- If the financial institution seeks to charge a garnishment fee, make sure that the customer agreement and state and local law allow such a fee. If after the review process is complete, there are no available funds available to cover the garnishment fee, set up a procedure to monitor the account, whether automated or manually, over the next five business days to determine if non-benefit funds are deposited that can be used to cover the garnishment fee.

- If the financial institution has not already done so, revise the customer agreement to include a form that accountholders fill out noting whether they receive any type of protected benefit income, including Social Security benefits, SSI benefits, VA benefits, Federal Railroad retirement benefits, Federal Railroad unemployment and sickness benefits, Civil Service Retirement System benefits, and Federal Employee Retirement System benefits. The customer agreement should also require the accountholder to notify the financial institution if they begin receiving any of the above benefits after opening an account.

- The final rule preempts only inconsistent state and local regulation. Check state and local regulations to ensure compliance with those regulations that do not contradict the final rule.

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