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Whose Safety Net? Reflections on "Untangling"

Henry L. Woodward*

I. Introduction

Allen Myers's Note, *Untangling the Safety Net: Protecting Federal Benefits from Freezes, Fees, and Garnishment*,¹ is the first serious academic scholarship to address the problem of garnishment of exempt benefits out of recipient bank accounts. Allen has given us remarkable detail on the variations of garnishment process, reasonable assessment of the interests of all the players, and excellent analysis of the potential solutions. I will add some comments on Allen's proposed solution, some recent developments, and brief reflections on how this travesty came to pass in the first place.

II. Looking at the Solutions

Acknowledging some potential for state statutory and federal regulatory solutions, Allen's Note recommends a relatively simple five-point federal statutory solution to the benefits garnishment problem.² His preference for a Congressional approach notes the universality of that approach compared to individual state garnishment reform, and the authoritative, less challengeable status of legislation compared to regulatory action.³ The uncertain footing and weakness shown in the recent collaborative effort of federal regulatory agencies, each with a finger in the pie, support that conclusion.⁴ The results of

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1. Allen C. Myers, Note, *Untangling the Safety Net: Protecting Federal Benefits from Freezes, Fees, and Garnishment*, 66 WASH. & LEE L. REV. 371 (2009).

2. *Id.* at 403-04.

3. *Id.* at 407-08.

4. Proposed Guidance on Garnishment of Exempt Federal Benefit Funds, 72 Fed. Reg. 55,273 (Sept. 28, 2007).

the 2008 federal elections may improve prospects on either the legislative or the regulatory front.

Looking at the substance of the five point proposal in Allen's Note, it addresses simply and well the major points of reform required. The interim protection afforded by proposed Section 101—a \$1,000 minimum⁵—is set too low for those benefit recipients wrestling with enormous subprime mortgage payments. In proposed Section 201,⁶ the Department of the Treasury should be expected to identify by ACH code not only the exempt benefits itemized and others within its discretion, but *all* federally exempt benefits. While proposed Section 204 fixes an accounting method to evaluate commingled accounts,⁷ the simpler solution favored by some state reform legislation⁸ would be easier for banks and courts to administer: a presumption that some fixed amount (such as \$2,500) of balance in a direct deposit account is exempt. Finally, the statute might specifically provide for simple state legislation authorizing benefits exempt under state law to enjoy the same protective regime without recreating the whole statutory structure.

III. New Variables

Although no proposed regulation has been published, testimony before a June 2008 Congressional hearing indicated that the Department of the Treasury had begun consideration of a regulation on garnishment of exempt benefits with many commendable features.⁹ On getting a garnishment order, a bank would be required to review electronic deposits in a 30–45 day look-back period, exempt some multiple—2X or 2.5X—of the benefits deposited for the duration of the garnishment, and ensure that no bank fees are charged against that exempt amount.¹⁰ Any greater amount from exempt sources could still be

5. Myers, *supra* note 1, at 409.

6. *Id.* at 409–10.

7. *Id.* at 411.

8. See, e.g., N.Y. C.P.L.R. 5205(l) (McKinney 1997 & Supp. 2009) (effective Jan. 1, 2009) (exempting \$2,500 in any account containing reasonably identifiable exempt benefits deposited within forty-five days of the garnishment order).

9. *Protecting Social Security Benefits from Predatory Lending and Other Harmful Financial Institution Practices: Hearing before the H.R. Ways and Means Comm.*, 110 Cong. (June 2008), <http://waysandmeans.house.gov/hearings.asp?formmode=detail&hearing=638> (Testimony of Margot Saunders, Counsel, National Consumer Law Center, 14–15) (describing draft Treasury regulation under discussion) (on file with the Washington and Lee Law Review).

10. *Id.* at 15.

reclaimed under state procedure.¹¹ New York has just passed a statute with some similar features.¹²

A second new development is a debit card called "Direct Express" that the Treasury Department has authorized for Social Security recipients.¹³ It can be used in lieu of a bank account deposit or a check in the mail, and is automatically refilled every month.¹⁴ It appears it would never be in reach of ordinary creditors. We are following several clients to see how well the debit card approach works in practice; unfortunately, such cards are not available for all forms of benefits at this time.

IV. Reflections on How We Got Here

The practice of garnishing exempt property out of the bank accounts of the elderly and disabled has important parallels to two other mucky swamps that afflict the most vulnerable—namely, the excesses of the credit card industry and the failings of the subprime mortgage market.

First, there is a perverted notion of contract in play. Recent testimony to Congress on exempt benefit loss tells of a 72-year-old resident of New York.¹⁵ She had her Social Security deposited in Chase Bank every month to write checks for her bills, as many of us do.¹⁶ At the onset of her crisis she got a notice from Chase that her account was restrained by a judgment creditor for \$920.15, slightly less than her \$929.54 on deposit.¹⁷ Two days later the bank refused a check for her cable bill, and charged her \$30 for refusing.¹⁸ A long chain of other refusal fees followed, the highlight of which may have been the day her two pre-authorized debits for some minor bank services, for amounts of \$4.15 and \$.95, came due: The bank treated both debits as refused, and heaped

11. *Id.*

12. See N.Y. C.P.L.R. 5205(*l*) (exempting \$2,500 in any account containing reasonably identifiable exempt benefits deposited within forty-five days of the garnishment order).

13. Press Release, Office of Legislative & Pub. Affairs, U.S. Dep't of the Treasury, U.S. Treasury Introduces Direct Express® Debit Card for Social Security Payments (June 10, 2008), http://www.fms.treas.gov/news/press/directexpress_launch.html (on file with the Washington and Lee Law Review). See also *How to Avoid Bank Account Freezes of Social Security, SSI Payments*, NCLC REPORTS, DEBT COLLECTION & REPOSSESSIONS EDITION (Nat'l Consumer Law Ctr., Boston, MA), May/June 2008, at 21–22.

14. *Id.*

15. *Saunders*, *supra* note 9, at 30.

16. *Id.*

17. *Id.*

18. *Id.*

on \$60 more in fees.¹⁹ By late November the bank fees had exhausted the entire amount frozen for the creditor, but the bank kept right on assessing fees until it closed out her account at \$637.79 *in the red*.²⁰ The bank had managed to rack up over \$1,500 in fees, while the judgment creditor got nothing,²¹ all from money which the law in its abstract majesty declares to be exempt from creditors.

When I describe such experiences as a perversion of contract, I am not referring to the contract at the basis of the creditor judgment, but rather the benefits recipient's contract with the bank. At some point the recipient came to the bank, plunked down some money, and said "I want to open an account." The bank said something like "Certainly, ma'am, you've got it, just sign here and here. We won't bore you with the fine print, because you're elderly or disabled and probably wouldn't understand it anyhow. And it really doesn't matter, because we can change the terms and conditions, and especially the fees for garnishment and refused checks, anytime we please. And since nobody can tell us our fees are too high, you'll just have to trust us." That contract formation is the basis on which a dishonored check or electronic draft incurs a \$30 fee each time it is presented. That contract is the only basis for gouging a \$100 or \$150 garnishment fee out of the exempt funds before relinquishing any leftovers to the judgment creditor.

This is very like unto the pretext of contract used by credit card lenders to change fees and penalties at whimsy,²² or the practice of subprime loan brokers of assuring borrowers that they would love the terms of the loans they are closing if only they had time to read through an inch and a half of documents written in an incomprehensible language.²³ Charles Dickens would love this stuff, and that by itself is a reason we should be paying a lot more attention.

19. *Id.*

20. *Id.*

21. *Id.*

22. See, e.g., Nancy Trejos, *Fed Drafting New Credit Card Rules; Regulations Would Ban "Unfair or Deceptive" Practices, Panel Is Told*, WASH. POST, Apr. 18, 2008, at D03 (identifying opposition to credit card practices such as retroactive rate increases, excessive fees, double-cycle billing, universal default, and "any time, any reason" repricing). The article quotes New York Congresswoman Carolyn B. Maloney as stating: "A credit card agreement is a contract between a card company and a cardholder, but what good is a contract when only one party has any power to make decisions?" *Id.*

23. See, e.g., Editorial, *Fuller Disclosure: HUD's Modest Step Toward a More Transparent Housing Market*, WASH. POST, Jan. 6, 2009, at A12 (discussing how the dream of homeownership "turns momentarily nightmarish when [the homebuyers] sit down at closing, take up a pen and nervously start signing a sheaf of complicated documents whose fine print only a seasoned real estate lawyer can comprehend").

A second point is that the economic transfer effect of garnishing exempt benefits is enormous. I will share a calculation that is only impressionistic, based on information from the deputy clerk of the Roanoke City General District Court which administers garnishments in this one modest city of under a hundred thousand residents. She estimates that her office receives five requests for exemption of federal benefits from account garnishment every week. That adds up to about 250 a year. We have not counted from court records what portion of garnished benefit recipients take advantage of their opportunity to request an exemption hearing, but considering that they are by definition disabled or elderly, let us optimistically assume 25% figure out how to claim the exemption. That leads us to a total of 1,000 bank account garnishments of exempt benefits in Roanoke City alone in a year's time. If the average recipient gets \$1,000 in benefits during a garnishment period, that amounts to *one million dollars* of exempt benefits a year that are frozen just by Roanoke garnishments. And if the garnished bank charges the prevailing local fee of \$100 each time—a fee which is not returned even if the court releases the garnishment—then that is *one hundred thousand dollars* in garnishment fees, and probably several more hundred thousand in bad check charges, that banks are reaping from just those 1,000 garnishments in Roanoke alone. Multiply that by the number of Roanokes in the country, and the hemorrhaging of exempt benefits is staggering.

What this suggests is a massive transfer of wealth from the poorest people in society to those at the other end. And we are not talking about money that is justly due by virtue of some underlying default of the poor debtors. We are talking about benefits that are protected by law precisely because they are essential to life and decency. The "safety net" of untouchable subsistence woven by Congress has become a golden goose for oppressive creditors and a deep well for excessive bank fees.

A third point: In a climate which honors the law, this practice Allen has exposed so thoroughly would never have happened because the exemption statutes could not be clearer.²⁴ We would never have seen this problem had not the federal agencies charged with regulating banks, social security, and federal funds distribution abdicated their responsibilities so completely. Only recently, when Congress is stirring and looking for scapegoats so as to escape the potential wrath of the AARP, have the regulatory bodies begun to respond. It is a credit to the pervasiveness of free market idolatry that the law can be so

24. 5 U.S.C. § 8346 (2006) (exempting Federal Retirement benefits); 38 U.S.C. § 5301(a)(1) (Supp. V 2005) (exempting Veterans' benefits); 42 U.S.C. § 407(a) (2000) (exempting Social Security benefits); 45 U.S.C. § 231m (2005 & LEXIS 2009 through Pub. L. No. 110-460) (exempting Railroad Retirement benefits).

cavalierly disregarded. Our last century was a long laboratory in how to keep the free market which most of us believe in from committing ritual suicide on a periodic basis, by imposing carefully selected regulatory limits on the excesses of entrepreneurial capitalism. By adopting the mantra of deregulation to the extreme, we have sentenced ourselves to watch the degradation of millions of poor pensioners and, in the current crisis of our times, perhaps sentenced ourselves to join them.