

Comments on Proposed Guidance Garnishment of Federal Benefit Payments

The Golden 1 Credit Union objects to the proposed guidance in general. It is the position of the Credit Union that the proposed guidance will not achieve the required purpose of reducing the need to freeze accounts and reducing costs to garnishees. The guidance will provide little benefit to consumers in California and will actually increase the cost of handling levies. Furthermore, segregated accounts for federal funds will be very expensive to establish and to maintain.

The basis for the objections is discussed in detail hereinafter. In the first portion of the discussion the Credit Union has identified specific best practices that it objects to. In the second portion of the discussion the Credit Union has responded briefly to the four issues set forth in the Request for Comment. The last portion of the discussion is a detailed discussion which explains in detail the basis for the position of the Credit Union and its responses to the Request for Comment.

Discussion

(1) Objections to specific proposed best practices.

The Golden 1 Credit Union objects to the following proposed best practices:

1. Providing the member with information about what types of federal benefit funds are exempt.

The Credit Union objects to this proposal because it is duplicative of notices currently provided in state court levies and more limited in scope than the notices currently provided by the Sheriff.

2. Notifying the creditor, collection agent, or relevant state court that the account contains exempt funds.

This notice will require extra time by personnel to ascertain the name and address of the party and to manually generate a letter. Thus, the cost of processing a levy will increase. Also, notice would duplicate notice already required to be given to the levying officer if the account has direct deposit of Social Security funds. Furthermore, notice by the financial institution will not result in release of the funds.

3. Allowing the member access to funds that are documented exempt federal funds.

This proposed best practice does not take into account state law. In California the financial institution will be liable for any funds withdrawn by the member if the member fails to properly claim the exemption.

4. Offer segregated accounts that contain only federal benefit funds.

In California segregating accounts will not obviate the need to freeze the funds and it will result in substantial costs to the financial institution, and ultimately increased costs for the consumer.

(2) *Response to Request for Comment.*

1. Are there practices that would enable a financial institution to avoid freezing an account that contains exempt federally protected funds?

No. A change in California state law would be required.

2. Are there alternative practices available?

Are there ways to provide access to funds during the garnishment process?

The answer is no to both questions.

3. Are members adequately notified of their rights?

Yes.

4. How do fees for levies compare to fees for insufficient funds?
Is there justification for both fees?

The fee for processing a levy is higher than the fee for insufficient funds. The processing of the levy and the processing of insufficient checks are separate functions handled in different manners. Furthermore, insufficient funds may occur even when there is not a levy and do not always occur when there is a levy. There is justification for both fees.

The processing of insufficient funds is primarily an automated feature that requires little manual intervention. The computer system ascertains that funds are not available. Notice to the consumer is generated to the system address and the item is returned through the Federal Reserve System.

The processing of a levy requires manual processing from the first receipt of the levy, through the freezing of the funds and ultimately the release or remittance of the funds.

(3) *Detailed discussion of basis for objections to proposed best practices and for response to Request for Comment.*

California law recognizes federal exemptions as it is required to do. Generally, the funds are exempt prior to payment by the paying entity. California Code of Civil Procedure § 703.080 permits a recipient to trace exempt funds into share accounts. The burden is on the claimant to trace the funds. California Civil Code § 703.020 provides who may make the claim.

Said section does not include the financial institution holding the share account.

Pursuant to California Code of Civil Procedure § 704.080 there is a limited amount of direct deposit Social Security funds that are exempt without claim. Subsection (d) specifically provides in part that “the financial institution that holds the share account **shall** either place the amount that exceeds the exemption provided in subdivision (b) in a suspense account or otherwise prohibit withdrawal of that amount . . .” (Emphasis added.) The section then requires that the financial institution give notice to the levying officer.

For all other funds, the financial institution is bound by California Code of Civil Procedure § 700.140. It must prohibit withdrawal of any funds up to the amount levied upon. Thus, placing the funds in a segregated account will not prevent the funds from being frozen nor allow the garnishee access to the funds.

Since segregated accounts would still be subject to a freeze, any advice by a financial institution to segregate accounts may give the recipient a false sense of security. The limited benefit of segregated accounts is the ease of tracing any funds.

Segregated accounts pose a significant cost to the financial institution. The Golden 1 Credit Union currently has 84666 accounts with members over age 62. If each member opened one additional account, the initial cost just to set up the segregated account would be \$592,662. For each account, there is a host system storage cost of \$0.85 or \$71,966. Each account would require a separate statement. The cost of processing each statement is \$0.50 with a minimum of 4 statements per year or a yearly total of \$169,332.

However, many account holders receive benefits from more than one source and have a joint checking account with a spouse. In those situations, two additional accounts may be needed in place of the one joint checking account. The recipient would have one account for federal exempt funds, a separate account for other funds that may be exempt under state law and a third account for nonexempt funds. If everyone opened two accounts, the initial set up costs would be \$1,185,324. Host system storage costs would increase to \$143,932 and statement processing costs would double.

The set up costs and statement costs do not include the cost of monitoring accounts or preparing new disclosures for members. Many members when they retire notify directly the agency paying retirement benefits of their existing account number. The funds are then sent by the paying agency to the financial institution. If best practices require the financial institution to offer a segregated account, then the institution would be required to establish a system to flag accounts receiving direct deposit and to notify the account holders to obtain a segregated account.

If a member has two or more accounts instead of one account, then the levy costs would also increase. The Credit Union must now locate and review more accounts. Also, it will be required to send letters for each separate account. Currently, many financial institutions waive fees or offer reduced fees for accounts that receive direct deposit. When parties deposit additional funds to these accounts, they are receiving the benefit of the reduced fees.

If parties have a separate account for nonfederal funds, then there will be additional costs to the consumer for these accounts. Also, the consumer will lose the benefit of having all funds deposited into one account from which they may pay their bills.

Thus, significant costs and minimal benefit will result from segregated accounts in order to try to minimize the impact on consumers who are the subject of the garnishment. In the comments of the proposed guidance, there is concern that state courts permit levies on an ex parte basis. In California levies may be obtained on an ex parte levy without an order from a judge if a judgment or court order has been previously obtained. In order to obtain a judgment a creditor must have served the member with the complaint or claim. The consumer has the opportunity to contest the validity of the creditor's claim. Furthermore, a court has made a determination that the moneys are owed by the consumer to the creditor. Thus, the consumer is afforded due process prior to the levy. The consumer is also notified by the Sheriff or person serving the garnishment of all exemptions federal and state that may be available. (See California Code of Civil Procedure § 700.010.)

It is ironic that federal law requires that the creditor must treat income from federally exempt funds in the same manner as income from nonexempt funds and the lender cannot discriminate based on the source of income, but the federal government now wants to provide extra protection to the consumer to prevent the creditor from collecting the moneys owed to it.

It appears that the paradox created here is the same dilemma that the Ninth Circuit Court of Appeals faced in the case entitled Lopez v Washington Mutual (Lopez I) 284 F.3d 990 (9th Cir. 2002), when it decided to grant the rehearing and issue a revised opinion in Lopez II, i.e., Lopez v Washington Mutual 302 F.3d 900 (9th Cir. 2002). If lenders are unable to collect debts, then the cost of loans will rise.

The Golden 1 Credit Union submits that the practical solution would be to expand California Civil Code Procedure § 704.080 to all exempt direct deposit federal funds to provide a minimum level of funds that are exempt from levy.

If NCUA or any other agency or entity has any questions regarding the comments of The Golden 1 Credit Union, please contact Barbara Heming, NCCO, Compliance Officer at bheming@golden1.com.