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U.S. House of Representatives
Committee on Financial Services
2129 Rayburn House Office Building
Washington, DC 20515
June 21, 2007

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The Honorable Ben S. Bernanke, Chairman
Federal Reserve Board
20th Street and Constitution Avenue, NW
Washington, DC 20551

The Honorable John C. Dugan
Comptroller
Office of the Comptroller of the Currency
250 E Street, SW
Washington, DC 20219

The Honorable John M. Reich, Director
Office of Thrift Supervision
1700 G Street, NW
Washington, DC 20552

The Honorable Sheila Bair, Chairman
The Federal Deposit Insurance Corporation
550 17th Street, NW
Washington, DC 20429-9990

The Honorable JoAnn Johnson, Chairman
National Credit Union Administration
1775 Duke Street
Alexandria, VA 22314-3428

Dear Chairman Bernanke, Comptroller Dugan, Director Reich, Chairman Bair, and Chairman Johnson:

I am writing to inquire what actions your agency is taking to ensure that the financial institutions that you regulate comply with the Social Security Act's explicit prohibition on the garnishment of federal benefits to Veterans, the elderly and the disabled. I am also concerned about the use of the practice of "set off" when banks remove funds owed the financial institution from these accounts. Finally, I have been made aware that some debt collectors have made use of the national banking system to circumvent state and federal law protecting consumers. While my primary concern is enforcement of the garnishment prohibition, I would like to know what

guidance or other instruction your agency has provided to the institutions you regulate regarding these related practices.

Financial Institutions Are Illegally Freezing Accounts Containing Federal Benefits

I have received some information that some banks routinely freeze accounts containing these benefits when they receive garnishment or attachment orders. The consumer is generally denied access to the funds in the frozen account. New deposits into the account are subject to the freeze and checks previously drawn on the account (before the consumer knew it was frozen) are returned unpaid, garnering NSF fees. The bank generally charges an attachment fee for freezing the account, from \$100-\$150, and any preauthorized electronic transfers from the account will result in additional NSF fees unless canceled.

I am very concerned about this problem, which was the subject of articles in the Wall Street Journal earlier this spring. It is not enough merely to correct this problem and refund fees after the account has been frozen. Please advise me regarding the actions your agency is taking to prevent accounts with funds exempt from collection from being frozen in violation of federal law.

Financial Institutions Are "Setting Off" Funds Owed Them From Exempt Accounts

In addition to facilitating the collection of third party debts from accounts that contain exempt funds, I have also been made aware that many banks also routinely seize funds from these accounts to pay debts owed to the bank under the practice of "set-off," in which banks take money that is owed them out of customer accounts, rather than sending a separate bill (for example, for a monthly account maintenance fee). It is my understanding that banks are increasingly setting off significant NSF or other fees on these exempt accounts and in some cases are seizing these funds to pay debts for auto or other loans owed to the bank.

Regulatory Guidance Appears to be Limited to Electronic Transfer Accounts

The number of people affected by all of these practices has risen significantly in recent years, largely due to the increase in the number of recipients whose benefits are electronically deposited into bank accounts. This is the result of federal policy mandating electronic payment of all federal funds (EFT 99), as well as the ability of debt collectors to search more efficiently for funds in bank accounts electronically.

There appears to be little direct regulatory guidance for banks and their customers on the issue of garnishment and setting off of exempt funds. However, on September 14, 1999, Treasury issued regulations regarding Electronic Transfer Accounts (ETAs), deposit accounts designed to provide access for individuals receiving federal benefits at a reasonable cost. These regulations indicated that federal benefits in the ETA accounts are generally protected from garnishment and required financial institutions who receive garnishment orders to "immediately send a copy of the order

and the name of the creditor and contact person, if any, to the name of the recipient.” Treasury also required that account holders receive the following disclosure:

Many Federal benefit payments, including Social Security benefits, Supplemental Security Income benefits, Veteran's benefits, and Railroad Retirement benefits, are protected from attachment under Federal law. This means that your creditors do not have the right to have these funds taken out of your ETA. There are a few exceptions, however. For example, funds in your ETA can be taken to satisfy child support or alimony obligations you owe. If you deposit funds other than Federal benefit payments to your ETA, your creditors may be able to have those funds taken out of your account, but your Federal benefits would still be protected. ¹ If we/[name of Institution] receive an order of attachment, garnishment, or levy, we will immediately send you a copy of the order and the name of the creditor and contact person, if any. If you have questions about a creditor's right to remove funds from your ETA, contact your benefit agency or your local legal services organization.

These regulations also limited the ability of banks to exercise the right to set off against an ETA, with the exception of the monthly account fee (which is limited to \$3.00), any other maintenance fees, fees mistakenly credited to the account, any amount for which the recipient is liable under Regulation E, and overdraft fees. Overdraft fees were also limited to \$10.00 and financial institutions were prohibited from charging more than one overdraft fee during a 24 hour settlement period, even if several items were returned during that period.

Unfortunately, of more than 62 million federal benefits recipients (48 million of whom are paid electronically),² only 91,061 have ETA accounts with these protections clearly delineated in regulation. I believe that additional guidance is needed to ensure that the millions of other federal benefit recipients receive the protections they are entitled to under federal law. Why should the vast majority of federal beneficiaries not receive 1) clear protection of the federal benefits; 2) a notice of any garnishment order; 3) a disclosure of their rights under the law; and 4) limitations of banks' ability to set off against exempt funds?

I am concerned that an additional consequence of banks' failure to obey the law could cause consumers to opt out of receiving their federal benefits via direct deposit, resulting in increased costs to the Treasury.

¹This sentence must be included only if the financial institution permits the recipient to deposit into the ETA funds other than Federal benefit, wage, salary, and retirement payments.

²As of October 26, 2005.

Some Collectors Pursue Debts Through the National Banking System, Which May Circumvent State and Federal Laws

Finally, I understand that some debt collectors are using the national banking system to evade consumer protections in the states, by collecting exempt funds from debtors through their bank's branch in another state where the debt collector has obtained judgment.

For example, when a debt collector obtains a judgment in New York against a person who lives in Florida (who may have lived in New York in the past), he then electronically serves that judgment with every bank in the state of New York. If the Florida resident is a Social Security recipient who has established a bank account with a Florida branch of a national bank and has direct deposit, the New York branch of the national bank accepts the New York judgment and freezes the exempt funds in the Florida bank account of the Florida resident. The consumer will receive notice of this freeze at her Florida address, including information regarding making a claim that funds in the account are exempt using a New York procedure, which requires the resident of Florida to go to New York. However, it would likely take weeks for the Florida recipient to unfreeze her funds, leaving her without access to her own money during that time. The bank, absent guidance to the contrary, believes it must honor a New York court order, even though the bank account is established in Florida. This process circumvents the well established principles for executing on judgments across state lines, which are agreed to by all of the states through the Uniform Enforcement of Foreign Judgments Act. This Act requires that a judgment obtained in one state against a resident of another state must be registered in the state in which the person lives, and then the enforcement of the judgment (along with protections from the enforcement of judgment) must proceed pursuant to the rules of person's home state.

This use of the interstate nature of national banks to collect judgments against exempt funds is very troubling. Whereas the initial problem is very serious -- banks freezing exempt funds -- this issue adds an extra layer of difficulty for the recipient. These recipients must not only deal with the banks' freezing their exempt funds, they must do so using a foreign state's procedures. Please advise me as to what actions you are taking to ensure that the financial institutions you regulation are not engaged in circumventing the law in this manner.

Please inform me as soon as possible about the measures your agency has taken to ensure that the institutions you regulate are aware of the laws that were enacted to protect the funds of federal beneficiaries and that these laws are being rigorously enforced.


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October 1, 2007

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The Honorable Henry M. Paulson
Secretary
Department of the Treasury
1500 Pennsylvania Avenue, NW
Washington, DC 20220

Dear Secretary Paulson:

I understand that you are considering moving to a system that would require universal direct deposit for all federal beneficiaries with bank accounts, eliminating the current waivers. As you may be aware, I am very concerned that these funds, which are protected from garnishment under federal law, are frequently frozen by banks due to the lack of guidance on this issue. As illustrated in *Wall Street Journal* articles this spring, some banks routinely freeze accounts containing these benefits when they receive garnishment or attachment orders. The consumer is generally denied access to the funds in the frozen account. New deposits into the account are subject to the freeze and checks previously drawn on the account (before the consumer knew it was frozen) are returned unpaid, garnering NSF fees. The bank generally charges an attachment fee for freezing the account, from \$100-\$150, and any preauthorized electronic transfers from the account will result in additional NSF fees unless canceled.

I am very concerned about this problem. It is not enough merely to correct the error and refund fees after the account has been frozen. I wrote to the banking regulatory agencies in June, and they formed an interagency task force, which has begun to make efforts in this area. The Senate Finance Committee recently held a hearing on this issue, and the Social Security Administration has also requested OMB's assistance in coordinating an interagency approach to clarifying and resolving the issues.

Until this garnishment problem is resolved, I request that you refrain from moving forward with this proposal, which will exacerbate the problem for new recipients of federal benefits by requiring them to receive their benefits electronically. Under the new system, the only way for new recipients to protect their existing accounts from being frozen is to close the bank accounts so that they can receive paper checks. Clearly, this is not an ideal solution. I would also appreciate your assistance in clarifying that accounts containing exempt funds should not be frozen in the first place, so that seniors and other federal beneficiaries can receive their checks electronically without fear of being denied access to their funds or being subject to unwarranted fees.


BARNEY FRANK
Chairman