
Coates' Canons Blog: Feds Reverse Course and Extend New Garnishment Procedures to Local Tax Collections

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It was big news for tax geeks like me back in early 2011 when the federal government released new regulations controlling garnishments of bank accounts that contain certain federal benefit payments. The regulations made banks responsible for determining if a garnished account contained Social Security payments or other protected federal benefits and, if so, to make sure that those benefits were not garnished. I blogged about the impact of these regulations on tax garnishments here. And I talked about them extensively in this attachment and garnishment webinar.

But soon after the regulations became effective the U.S. Treasury Department announced that the required garnishment procedures would not apply to local government tax garnishments. That surprise announcement led to this blog post letting local tax officials across the state know that it would still be their job to figure out which bank accounts were off limits to garnishment because of federal benefit deposits.

Well, guess what? Just this week the Treasury Department and four other agencies involved with this issue changed their minds and published new "final" regulations that extend the reach of the required garnishment procedures to cover all state and local tax garnishments.

I think this development is (belated) good news for local tax collectors and taxpayers alike because it eliminates existing uncertainty about when and how bank accounts containing certain federal benefits may be garnished for delinquent taxes.

A New Definition of "Garnishment"

The original regulations limited their reach to garnishment orders "issued by a court or a state child support enforcement agency." In North Carolina, garnishment orders for unpaid local taxes are issued directly by the taxing authority's tax collector. G.S. 105-368. Courts are not involved. The Treasury Department relied on a strict reading of the original regulations to conclude that they should not apply to local tax garnishments that are issued without court orders.

This decision upset consumer advocacy groups who argued during the regulations' public comment period that the narrow definition of garnishment left federal benefits "exposed to improper garnishment and freezing."

The Treasury Department must have agreed, because the new final regulations issued this week cover all garnishment orders "issued by a court, a state or state agency, a municipality or municipal corporation, or a state child support enforcement agency." This change and the accompanying explanation published along with the regulations make it clear that the required garnishment procedure now applies to garnishments and levies issued directly by a state or a city government.

What about counties? The regulations make no reference to garnishments issued by counties, but it seems illogical to include only certain local tax garnishments in the new garnishment procedures. A quick email to a Treasury Department attorney confirmed that the intent was not to exclude counties. For tax purposes, the Treasury Department considers counties to be "administrative units" of states and therefore covered by the reference to state garnishments.

What the Change Means for Local Tax Collectors

The new final regulations expand their reach but do not change the garnishment procedure that I described in this blog post from 2011. This procedure will apply to all local tax garnishments issued on or after June 28, 2013.

In a nutshell, the regulations require a bank that receives a garnishment order to first determine if the garnished account contains Social Security payments or other protected federal benefits. If so, then the bank must protect from garnishment those benefits that were deposited within a two-month “look-back” period. I encourage you to read my original post again to learn the details of the procedures now required of banks who receive tax garnishments. Also consider this attachment and garnishment webinar, available for purchase and on-demand viewing.

The mandatory garnishment procedure is good news for local tax collectors because it shifts the burden of determining whether a bank account holds protected federal benefits from the tax collector to the bank. It also limits the protection of federal benefits to two months of deposits; any funds remaining in a bank account over the total of two months of federal benefit deposits will be eligible for garnishment.

Taxpayers also benefit from the new procedure because it should result in far fewer improper garnishments. Under current law a tax collector normally doesn't learn about the existence of protected benefits until after a garnishment is complete. Then the tax collector and the taxpayer have to wrangle over exactly how much of the funds in the account, if any, should be subject to garnishment and how much must be returned to the taxpayer.

I think the only downside for local tax collectors concerning the new regulations is the delay between the issuance of a garnishment notice and the freezing of an account by a bank.

Under the Machinery Act, a bank is obligated to freeze a taxpayer's account immediately upon receipt of a tax garnishment notice. If the bank fails to do so, it will be liable for any funds withdrawn by the taxpayer after the garnishment notice was received.

But federal law trumps state law, and under the federal garnishment procedure a bank cannot freeze an account until after it conducts a review of that account to determine if it contains protected federal benefits. Banks have two days after receipt of the garnishment order to conduct this review. During that two-day delay the account holder must be provided full access to the account, meaning he or she could withdraw all of the funds in the account and avoid the garnishment entirely.

To avoid this result, a local tax collector should not give the taxpayer notice of garnishment until at least two days after serving the bank with notice. By that time the bank should have completed its account review and frozen any unprotected funds. The Machinery Act requires notice to the taxpayer before the garnishment is completed but does not require that the bank and the taxpayer receive notice simultaneously.

Links

- canons.sog.unc.edu/?p=4203
- www.sog.unc.edu/courses/webinars/attachment-and-garnishment-webinar-demand
- canons.sog.unc.edu/?p=4467
- www.gpo.gov/fdsys/pkg/FR-2013-05-29/pdf/2013-12567.pdf
- www.sog.unc.edu/courses/webinars/webinar-demand-attachment-and-garnishment-tax-collection