



Comptroller of the Currency
Administrator of National Banks

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Interpretive Letter #1041
October 2005
12 USC 24(7)
12 CFR 7.5002
12 CFR 7.5001

September 28, 2005

Re: Performance of Escrow Activities by a National Bank

Dear []:

This is in response to your letter on behalf of []
(the "Bank") regarding the proposed performance of escrow agent activities by the Bank.

Proposal

More specifically, []¹ and the Bank propose to enter into a master agreement whereby the Bank will act in one of two capacities. The master agreement will govern the terms of the relationship between [] and the Bank. First, in those situations where [] acts as the funds control agent and [] has determined that it is not necessary to have a bank as a party to the escrow agreement, the Bank will act solely as the depository for the monies collected by []. In those situations, the Bank will follow its standard depository account practices and procedures. Second, in those situations where [] determines that it is necessary to have a bank as party to the escrow agreement, [] will continue and act as funds control agent, but the Bank will become a party to the escrow agreement as "escrow agent."² The Bank will also

¹ [] ("[]") performs funds control activities for construction projects throughout the United States. [] acts as funds control agent on construction contracts where the surety will not issue a bond with respect to a contractor unless the funds paid to the contractor by the owner are "controlled" by a third party (i.e., []), so that the surety can be confident that subcontractors of, and material suppliers to, the contractor will be paid.

² The Bank expects that it will be acting as an escrow agent in most situations since they expect that the surety will likely require it.

act as a depository bank. [] will make the determination whether it is necessary to have the Bank become a party to the escrow agreement. In either case, the Bank will act as a depository bank for funds to be placed in escrow.

When acting in its capacity as an escrow agent, the Bank's obligations will be limited to: (1) receiving funds from the project owner or contractors; (2) depositing the funds into a separate non-interest bearing account for each project; (3) honoring checks written against the account; (4) mailing monthly account statements; and (5) providing on-line access to the necessary parties. All other services and work associated with the escrow agreement will be performed by [] as an independent party to the Agreement.³

In order to limit the exposure of the Bank, [] will: (1) indemnify the Bank for any of []' actions in performing its duties under an escrow agreement; (2) will utilize the Bank's Positive Pay service (or indemnify the Bank for losses arising from counterfeit, fraudulent or forged checks); and (3) will maintain Commercial General Liability ("CGL") and Errors and Omissions ("E&O") insurance of at least \$1,000,000 per occurrence and a fidelity bond of at least \$500,000 per occurrence. Further the majority shareholder of [] has agreed to sign a separate guaranty agreement covering all obligations of [] to the Bank under the master agreement and all escrow agreements. Perhaps the most important way in which the Bank's liability is limited is that the Bank's duties under the escrow agreement are limited to what in essence are purely bank functions. The Bank takes no role in the funds control process, and essentially acts solely as depository bank.

In situations where the Bank will not act as escrow agent, the Bank will receive its standard depository fees. In exchange for the Bank acting as the escrow agent (i.e., for funds control projects where the Bank is a party to the escrow agreement), it will receive 0.15% of the amount of the contractor's construction contract and \$250 for account set up. The term of the master agreement will be for three (3) years initially with the option to renew for successive one (1) year terms. Finally, all deposits made to a particular escrow account will be made via wire transfer, ACH, or check at the Bank's established offices in [*State*]. The Bank will review its operating procedures to determine compliance with the Bank Secrecy Act when acting as an escrow agent.

Discussion

The Bank will provide escrow services in the context of its other depository services available to its customers. As an escrow agent, the Bank will: 1) receive funds from the project owner or contractor, 2) deposit funds into a separate non-interest bearing account, 3) honor checks written against the account, 4) mail monthly account statements, and 5) provide on-line access to the necessary parties. The five activities described above are traditional banking activities that are either expressly permitted by statute or incidental to those services.

³ If [] will be acting as agent or a service provider to the Bank, please be mindful of the risk management guidance set forth in OCC Bulletin 2001-47 (November 1, 2001) on "Third-Party Relationships".

The OCC has approved banks providing escrow services in a variety of contexts. The OCC has approved escrow services in the context of mortgage banking where a bank subsidiary would originate, arrange, make, hold, purchase, sell, warehouse, and service mortgage loans, as well as conduct loan closing, escrow, appraisal management, property inspection, and related activities.⁴ Further, the OCC has approved national banks providing escrow services in the context of collecting real estate taxes.⁵ Both the general escrow services associated with mortgage banking and the real estate tax escrow services have been approved when they are provided to the bank, its subsidiaries, other affiliates and other unrelated entities. Finally, there is older OCC precedent that permitted the provision of escrow services by a national bank and its subsidiaries for itself or other banks, as “a proper activity for national banks.”⁶ Therefore, we believe that the Bank’s proposed activities are consistent with existing OCC precedent.

Further, the first three activities listed when the Bank acts as escrow agent constitute depository and check cashing functions that are enumerated powers set forth in statutory law. Among other activities, a national bank may exercise:

...all incidental powers as shall be necessary to carry on the business of banking; by discounting and negotiating promissory notes, drafts, bills of exchange and other evidences of debt; by receiving deposits; by buying and selling exchange, coin, and bullion; by loaning money on personal security; and by obtaining, issuing, and circulating notes....

12 USC § 24(Seventh). The provision of monthly account statements to customers is also part of the Bank’s powers to receive deposits and a safe and sound banking practice. Finally, we believe that the provision of on-line access to customers is the functional equivalent to providing non-electronic account statements and account access. Since national banks must be able to make use of modern technology in performing their business, the OCC’s regulation, 12 C.F.R. § 7.5002(a), permits national banks to “perform, provide, or deliver through electronic means and facilities any activity, function, product, or service that [they are] otherwise authorized to perform, provide, or deliver....” Pursuant to 12 C.F.R. 7.5001(c), in determining whether an electronic activity is considered part of the business of banking, the OCC considers, among other things, whether the activity: is the functional equivalent to or a logical outgrowth of a recognized banking activity, benefits the customers, involves similar risks to those already assumed by banks, and is authorized for state-chartered banks. Providing on-line access to accounts is clearly part of the business of banking as it is the functional equivalent of providing a customer with non-electronic access to accounts, benefits customers, involves similar risks already assumed by banks, and is authorized for state-chartered banks. Therefore, providing on-line

⁴ See, e.g., OCC Conditional Approval No. 338 (November 10, 1999); OCC Corporate Decision No. 99-33 (September 28, 1999). Also, please note that “real estate settlement, closing, escrow, and related services....” are activities listed as requiring only “notice” to the OCC for national bank operating subsidiaries, pursuant to 12 C.F.R. § 5.34(e)(5)(v)(V).

⁵ See, e.g., OCC Conditional Approval No. 322 (July 30, 1999); OCC Conditional Approval No. 276 (May 8, 1998).

⁶ See Interpretive Letter (May 13, 1975).

access to parties is a permissible activity pursuant to 12 C.F.R. § 7.5002 and considered part of the business of banking. It is also an activity that has been previously approved by the OCC.⁷

In summary, we believe that the proposed provision of escrow services by the Bank in connection with the proposed depository services is part of the Bank's depository function.⁸

If you have any questions regarding this issue, please contact Christina Trojan-Masnyk at (312) 360-8805.

Sincerely,

signed

Coreen S. Arnold
District Counsel
Central District

⁷ See, e.g., Interpretive Letter No. 742, reprinted in [1996-1997 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 81,106 (August 19, 1996).

⁸ I note that the Bank will be a party to the escrow agreement(s), but its duties will be limited to those described above. Further, it appears the Bank has taken steps to indemnify itself and limit its exposure. From the materials provided and from our conversations with the Bank, it is our understanding that the Bank would not be in a partnership or joint venture with any of the other parties, but will be acting solely as a depository and engaging in those activities described.