



National Credit Union Administration

Office of General Counsel

February 1, 2018

Faheem Masood, President/CEO
ESL FCU
225 Chestnut Street
Rochester, NY 14604

RE: Other Similar Escrow Account Share Insurance Coverage – New York Lease Security Account

Dear Mr. Masood:

You have asked if the below described “lease security account,” which ESL FCU is interested in offering to members, would qualify as an “other similar escrow account” under §745.14 of the NCUA’s regulations. If qualifying, the account would be eligible for pass-through share insurance coverage based on the credit union membership of the landlord/account holder. While not all accounts known as lease security accounts would qualify for pass-through share insurance coverage, we believe the subject account does.¹

Our determination that the subject lease security account, if offered in New York State by ESL FCU, would qualify to receive pass-through share insurance coverage as an “other similar escrow account” is based largely on ESL FCU’s factual representations regarding: (1) the nature of the lease security account and (2) New York State law with respect to such accounts. Accordingly, the availability of National Credit Union Share Insurance Fund insurance coverage for the subject account is dependent on the accuracy of ESL FCU’s representations.

The below analysis does not apply to other similarly named accounts where the factual and legal circumstances differ, even slightly, from those presented in the subject instance. Rather, the conclusions reached in this opinion are expressly limited to the specific facts and circumstances surrounding the subject account. This and any future determinations under §745.14 of the NCUA’s regulations are made strictly on a case-by-case basis. However, as discussed in NCUA’s Guidance on Enhanced Share Insurance (Guidance),² we are issuing this legal opinion to help federally insured credit unions: (1) better understand the concept of “other similar escrow accounts”; and (2) identify accounts eligible for pass-through share insurance coverage.

Analysis

Section 745.14 of the NCUA’s share insurance regulations provides for pass-through share insurance coverage for “interest on lawyers trust accounts” (IOLTAs) and “other similar escrow accounts.”³ Pass-through share insurance means, with respect to IOLTAs and other similar escrow accounts, that the insurance coverage is based on the interest of each person on whose

¹ As discussed below, New York State law plays a critical role in this determination.

² <https://www.ncua.gov/regulation-supervision/Documents/Regulatory%20Alerts/RA2016-02-enclosure.pdf>.

³ An IOLTA is an account opened as part of a system in which lawyers place certain client funds in interest-bearing or dividend-bearing accounts, with the interest or dividends then used to fund programs such as legal service organizations that provide services to clients in need. 12 C.F.R. §745.14.

behalf funds are held in the account by the attorney administering the IOLTA or the escrow agent administering the other similar escrow account.⁴

More specifically, to the extent membership requirements are satisfied, the shares in any IOLTA or other similar escrow account held in a federally insured credit union are insured on a “pass-through” basis, in an amount of up to the standard maximum share insurance amount of \$250,000⁵ for each client or principal on whose behalf funds are held in such accounts by either the attorney administering the IOLTA or the escrow agent administering a similar escrow account. Further, funds attributable to each client or principal will be insured on a pass-through basis in whatever right and capacity the client or principal owns the funds.

IOLTAs and other similar escrow accounts are considered member accounts⁶ and eligible for pass-through share insurance if the attorney administering the IOLTA or the agent administering the other similar escrow account is a member of the federally insured credit union in which the funds are held. In this circumstance, the membership status of the client or the principal is irrelevant.⁷

ESL FCU describes the subject account as allowing a landlord to deposit a tenant’s security deposit on rental property and to hold the funds in trust for the tenant in compliance with New York State law. In determining if the account is eligible for pass-through share insurance coverage, we must determine if the account, which clearly is not an IOLTA, satisfies all aspects of the definition of “other similar escrow account.”

Section 745.14(c)(1)(ii) of the NCUA’s regulations defines an “other similar escrow account” as an account where: (1) a licensed professional or other individual; (2) serving in a fiduciary capacity; (3) holds funds for the benefit of a client or principal as part of a transaction or business relationship. The definition also states that “[e]xamples of such accounts include, but are not limited to, real estate escrow accounts and prepaid funeral accounts.”⁸

A licensed professional or other individual

With respect to the first element of the definition of “other similar escrow account” that requires the account holder (agent) to be a member of the credit union and a “licensed professional or other individual,” the preamble to the IOLTA rule⁹ and subsequent guidance provide that the

⁴ The terms “interest on lawyers trust account”, “IOLTA”, and “pass-through share insurance” are given the same meaning in 12 C.F.R. Part 745 as in 12 U.S.C. 1787(k)(5) of the Federal Credit Union Act.

⁵ 12 CFR §745.1(e).

⁶ 12 C.F.R. §745.14(b).

⁷ This manner of satisfying the membership requirement is remarkable because, with few exceptions outside of the IOLTA and other similar escrow account context, the membership requirement is satisfied in the opposite manner. Specifically, in almost all other contexts, the membership status of the principal, as the true owner of the funds, is the key to obtaining insurance coverage and the membership status of the agent is irrelevant.

⁸ Whether the lease security account ESL FCU has described is eligible for pass-through share insurance coverage depends on if it is an other similar escrow account. If it is, insurance coverage would be available on a pass-through basis provided the account also is in compliance with all other relevant provisions of Part 745 and applicable law.

⁹ 80 FR 80635, 80639-40 (Dec. 28, 2015).

account holder is not strictly limited to being an individual to satisfy the definition. More specifically:

The enhanced pass-through coverage applies to IOLTAs and other similar escrow accounts opened and administered by individual attorneys and escrow agents as well as entities, such as law firms, real estate agencies, and funeral homes. However, these accounts must still satisfy the fiduciary relationship requirement, which may or may not require an individual lawyer or escrow agent to also be named on the account. That is subject to state law. Also, the [Credit Union Share Insurance Fund Parity Act] altered but did not eliminate the membership requirement to obtain share insurance. Accordingly, if the law firm or escrow agency itself does not qualify for membership in a particular credit union, but one of its lawyers or agents does, then the firm or agency may maintain an account in that credit union if the eligible lawyer or agent joins the credit union. It is the responsibility of the law firm or other entity wishing to establish an IOLTA or similar escrow account, however, to first determine if state and other applicable law and rules of professional conduct allow for such an arrangement.

Provided ESL FCU ensures the membership requirements as discussed above are satisfied, in accordance with applicable law and rules of professional conduct, the subject lease security account would satisfy this element of the definition.

Serving in a Fiduciary Capacity

The second element of the definition of “other similar escrow account” that must be satisfied includes whether the account holder is “serving in a fiduciary capacity.” As mentioned above, state law governs in this area. ESL FCU has represented that under New York State law: (1) a security deposit belongs to the tenant; (2) a security deposit paid by the tenant to the landlord must be held in trust by the landlord; and (3) New York courts have confirmed that the trustee relationship between landlord and tenant is a fiduciary relationship between the parties. Assuming ESL FCU’s representations are accurate, a fiduciary relationship exists under New York State law between landlord and tenant in this regard. As such, the fiduciary capacity requirement of the definition is satisfied if the funds in the lease security account are held pursuant to such a relationship and meet state and other applicable law requirements and rules of professional conduct.

Transaction or Business Relationship

The final element of the definition of “other similar escrow account” requires that the account holder/agent “hold[] funds for the benefit of a client or principal as part of a transaction or business relationship.” As discussed above, ESL FCU has represented that under New York State law, a landlord holds the security deposit in trust for a tenant, the actual owner of the funds, in a fiduciary capacity as part of their real estate related business relationship. Based on this

relationship, a New York lease security account, as described by ESL FCU, satisfies this final element of the definition.

Other Share Insurance Requirements

Although the subject account satisfies all of the elements of the definition of “other similar escrow account,” to be fully eligible for coverage, the subject lease security account must also comply with all applicable state and federal law. For instance, the recordkeeping requirements in §745.2(c)(1)-(2) of the NCUA’s regulations are particularly relevant. These requirements are summarized in the IOLTA Guidance:

Section 745.2(c)(1) of NCUA’s regulations provides that “the account records of an insured credit union shall be conclusive as to the existence of any relationship pursuant to which the funds in the account are deposited and on which a claim for insurance coverage is founded.” NCUA will not recognize a claim for insurance based on such a relationship in the absence of such disclosure. Additionally, §745.2(c)(2) provides that “if the account records of an insured credit union disclose the existence of a relationship which may provide a basis for additional insurance, the details of the relationship and the interests of other parties in the account must be ascertainable either from the records of the credit union or the records of the member maintained in good faith and in the regular course of business.” IOLTAs and escrow accounts are the kinds of accounts that are based on a relationship upon which a claim for insurance coverage could be founded. As such, for these accounts to receive pass-through coverage, the recordkeeping provisions of §745.2(c)(1)-(2) must be satisfied. NCUA did not impose any new recordkeeping requirements in the 2015 share insurance rule.

It is important to note that, for share insurance purposes, a tenant’s funds in the subject lease security account and any other funds the tenant happens to have in another account at ESL FCU could be aggregated and insured pursuant to Part 745 only to the standard maximum share insurance amount (\$250,000) depending on the legal capacity in which the tenant owns the various accounts.

Summary

To summarize, based on ESL FCU’s representations of the facts and New York State law, the subject lease security account at ESL FCU satisfies the definition of “other similar escrow account” and is eligible for pass-through share insurance coverage. Actual insurance coverage is, as always, dependent upon compliance with all other applicable state and federal law.

Sincerely,

/S/

Michael J. McKenna
General Counsel

GC/TIZ:bhs
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