

## **INTERPRETIVE LETTER 95-3 (JUNE 3, 1995)**

**Illinois Department of Employment Security may visit state bank despite exclusive visitation provision of Section 48 solely for purpose of verifying unemployment tax records.**

This letter is in response to your inquiry on behalf of \* ("Bank"), an Illinois state bank, concerning a notice that it received from the Illinois Department of Employment Security ("IDES") and in particular, whether the Bank is subject to audit by IDES. The notice stated that IDES would commence an audit of the Bank's employment records on June 15, 1995, to verify compliance with the Illinois Unemployment Insurance Act ("Unemployment Act"), 820 ILCS 405/100 et seq. For the reasons set forth in this letter, the Commissioner of Banks and Trust Companies ("Agency") concludes that IDES may audit records of the Bank relating to the Bank as an employer and those records that relate to the Bank's payment of the proper amount of unemployment tax.

The Unemployment Act taxes employers of a certain size based upon their payroll. The money is then used by the state and federal governments to fund compensation for individuals who are laid off or otherwise lose their jobs. IDES auditors are required by federal regulations to audit a selected sample of employers to determine compliance with the requirements for reporting, record keeping and payment of unemployment taxes. IDES audits focus upon employers to determine whether they have persons functioning as employees who are being paid by the employer as "independent contractors" with a corresponding underpayment of unemployment taxes. In conversations with the IDES employees, they stated that IDES does not intend to review the items that the Agency customarily reviews--capital, asset quality, management, earnings or liquidity. Rather their focus will be upon the W-4's, W-2's, 1099's and the portions of the general ledger and books and accounts of the Bank that would reflect disbursements for vendor services that are likely to disguise employees as independent contractors for whom unemployment taxes were not paid.

The Commissioner's authority to examine state banks is provided in Section 48 of the Illinois Banking Act ("Act"), 205 ILCS 5/48 (1994), which states that:

a State bank shall not be subject to any other visitorial power other than as authorized by this Act, except those vested in the courts. (emphasis added)

A nearly identical "exclusive visitation" provision is included in the National Bank Act. While the literal language of these statutes would suggest that no other entity can visit an Illinois state bank, this is not true in practice. Examiners from the Federal Deposit Insurance Corporation ("FDIC"), the Federal Reserve System ("Fed") and Illinois Department of Financial Institutions (unclaimed property) regularly visit state banks. Also the federal Department of Labor examines banks as trustees for compliance with the federal Employee Retirement Income Security Act and the Internal Revenue Service

visits banks in connection with tax audits of the banks and of bank customers. Other governmental authorities are empowered by law to visit a bank for a specific purpose, usually a purpose other than examination of the banking business. The Fed and the FDIC are granted authority under federal law to visit state banks **as bank regulators**. Other agencies that visit banks have more narrowly defined regulatory missions and the scope of their visits should be more limited. A building inspector could appropriately inspect new building construction, plans for the construction and work in progress, but would be clearly out of bounds if the inspector asked to see a loan file, customer account information or financial data relative to the bank's performance. The Fire Marshall could inspect for fire hazards and for safety and evacuation routes, but should similarly be excluded from bank operations in the visit. Therefore, the exclusive visitation language does not actually preclude other entities from visiting a state bank.

The exclusive visitation issue was litigated in N.L.R.B. v. Northern Trust Co. 148 F. 2d 24 (1945, 7th C.C.A.), in which Northern Trust Co. ("Northern"), an Illinois state bank, asserted that it was not subject to an administrative subpoena by the National Labor Relations Board ("NLRB") because of the provisions of 12 U.S.C. 484 which read:

No bank shall be subject to any visitorial powers other than such as are authorized by law, or vested in the courts of justice or such as shall be or shall have been exercised or directed by Congress, or by either House thereof or by any committee of Congress or of either House duly authorized.

Northern also asserted that NLRB visitation was also precluded by the similar provision in the Banking Act of Illinois, Ill. Rev. Stat. 1943, ch. 16 1/2, Sec. 8 which stated that:

banks organized this Act shall not be subject to any other visitorial powers than such as are authorized by the Act or such as are vested by the law in the several courts of law and chancery.

The provisions of the 1943 Illinois law have continued in the previously quoted portion of Section 48. The court concluded in response to Northern's assertion of an exemption that "[t]heir assertion is untenable, because the Board's action falls within the meaning of the stated exceptions in the statute..." The Court of Appeals proceeded to sustain the District Court and the NLRB subpoenas because:

the subpoenas were not unlimited and the records were particularized to such records as would show certain specific information. Hence they did not amount to a fishing expedition; rather, they specified with as much precision as was fair and feasible the records to be examined and the information to be obtained from such records.

Because of the limitations placed on the order, we are far from convinced that the 'essential business of the bank and of its customers will be interfered with and confidential information subjected to public scrutiny.'

Thus his opinion stated that the 'order requiring compliance with the subpoena should provide a convenient method of compliance, one which will not interfere with the business of the bank,' and 'in so far as the bank will permit inspection of the books and papers at its place of business it need not be required to produce them before the Examiner.'

148 F.2d 24, 29. (emphasis added)

The Northern case has been followed in other instances and has not been overruled.

We have also confirmed with Regional Counsel for the Office of the Comptroller of the Currency, regulator of national banks, that they interpret the exclusive visitation provision consistently with the Northern case--they only oppose other visitations aimed at supervision of a national bank's banking business, not visitations for a limited purpose.

We therefore conclude that IDES may properly visit the Bank to audit its employment records. We are, however, concerned that, in the words of the court in Northern, IDES conduct its visitation to "provide a convenient method of compliance, one which will not interfere with the business of the bank." The Records Request already provided to the Bank, for instance, requests copies of "Check Stubs and Cancelled Checks." We were informed by the Bank that for calendar year 1994 check stubs and cancelled checks alone would total at least 1,000,000 items. We hope and trust that IDES will provide a supplemental "Records Request" that more narrowly focuses upon the records that the Bank needs to provide. What may be reasonable to request from a small business may "amount to a fishing expedition" as the court stated in Northern.