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Comptroller of the Currency  
Administrator of National Banks

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Washington, DC 20219

**Conditional Approval #322**  
**August 1999**

July 30, 1999

Courtney D. Allison, Esq.  
Vice President and Assistant General Counsel  
First Union Corporation  
Charlotte, North Carolina 28288

**Subject:** Application by First Union National Bank to acquire through an existing operating subsidiary a 50-percent voting interest in a limited liability company engaged in title insurance agency and loan-related activities – Application Control No. 99-ML-08-007

Dear Ms. Allison:

This responds to the application filed by First Union National Bank, Charlotte, North Carolina (“the Bank”), requesting approval to make, through an existing operating subsidiary, a 50-percent, non-controlling equity investment in a limited liability company (“the LLC”) that will engage in title insurance agency, real estate appraisal, loan closing, and other real estate loan-related and finder activities. The LLC will be jointly owned by the Bank’s operating subsidiary and (either directly or indirectly) a vendor (“the Vendor”) that currently provides the services to be engaged in by the LLC. For the reasons set forth below, the application is approved, subject to the specified conditions.

**I. DESCRIPTION OF THE PROPOSAL**

**A. Organization and Management of the LLC**

First Union Insurance Agency of NC, Inc. (“the Operating Subsidiary”), is a licensed insurance agency subsidiary of the Bank authorized to act as a general insurance agent from a place of less than 5,000. Two subsidiaries of the Vendor have established the LLC, and upon receiving regulatory approval, the Operating Subsidiary will purchase its interest in the LLC from one of the subsidiaries of the Vendor. The Operating Subsidiary is incorporated in North Carolina and is authorized to make an equity investment in a title insurance agency under North Carolina insurance regulatory laws.<sup>1</sup> The LLC is organized under Delaware law but will be located in Pineville, North Carolina, a place of less than 5,000 (as measured by the 1990 census), in which the Bank operates a branch.

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<sup>1</sup> N.C. Gen. Stat. § 58-27-5 (1994).

The Operating Subsidiary and the Vendor will enter into an operating agreement (the “Operating Agreement”) that will govern the management, operations and affairs of the LLC,<sup>2</sup> and they will be its only members. They will manage the LLC, and they each will have an equal number of votes (based on owning an equal number of membership units). All decisions relating to the LLC, including any delegation of decision-making responsibilities, will require approval by a majority-in-interest of the members. Because there will be only two members with equal voting rights who will exercise management control of the LLC, each member effectively will have a veto power over the other and no action will be taken unless it is unanimously approved. The members may appoint officers who will be responsible for the day-to-day management and administration of the LLC.

The Operating Subsidiary will make 49-percent of the initial capital contribution to the LLC, and the Vendor will contribute 51-percent of the capital. Nevertheless, as stated above, they will have equal voting interests. The Operating Subsidiary and the Vendor will share equally in the profits, losses, and the management and control of the LLC. Certain employees of the Vendor will be hired by the LLC with the assistance of the Vendor and will qualify for benefits under existing Vendor employee plans. The Vendor will receive a monthly management fee in return for overseeing the LLC’s activities.

#### B. Description of the Activities to be Engaged in by the LLC

The LLC will leverage the expertise and systems of the Bank and the Vendor to the benefit of both parties. The initial objective of the LLC is to provide title insurance agency, loan closing, commercial real estate finder services, and other services in connection with commercial real estate lending. The LLC may provide services with respect to residential real estate lending in the future, and accordingly, you have requested authority for the LLC to engage in services related to residential title insurance agency activities.<sup>3</sup>

The following services will be provided for the Bank and other lenders in connection with loans secured by real property (whether the lien has first priority or a subordinate lien position) (the “Mortgage Loans”): (1) title insurance agency; (2) appraisal management; (3) loan closing services; (4) flood insurance; (5) credit reporting; (6) property inspections; (7) property preservation; (8) loan document preparation; (9) census tract information; (10) portfolio audit; and (11) real estate tax services. In addition, the LLC will act as a finder for an intermediary in like-kind exchanges of commercial real estate. (These will be collectively referred to as “the Services”). All of the Services have been previously approved for national banks and their operating subsidiaries.

##### 1. Title Insurance Agency Activities

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<sup>2</sup> Currently, the Operating Agreement is in draft form. Information contained herein is based on this draft.

<sup>3</sup> Initially, the LLC will provide services for the Bank and its affiliates only. At some future time, the LLC may market its services to unaffiliated lenders, much as the Bank itself provides certain other services to unaffiliated institutions as correspondent.

Creditors making Mortgage Loans, and obligors on such loans, will often obtain title insurance to protect their interests in the collateral. In some cases, creditors will not obtain title insurance but will want to know of liens, judgments, and other clouds on the title of the collateral prior to making a credit decision. The LLC will provide title insurance agency services in North Carolina and other states. Services will be performed outside of North Carolina by the LLC receiving a license to act as a nonresident agent or by forming a subsidiary insurance agency in states that require resident agents. The LLC will act as a title insurance agent only; in no event will it become obligated as a title insurer. Services typically available through title insurance agencies will be provided by the LLC, and will conform to the conditions set forth in OCC Interpretive Letter No. 753, *reprinted in* [1996-1997 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 81-107 (November 4, 1996) (“the First Union Letter”).

## 2. Appraisal Management

Appraisals to determine the value of collateral generally are prepared when creditors make a Mortgage Loan. Federally regulated depository institutions must comply with appraisal regulations and guidelines issued by their primary regulators. *See, e.g.*, OCC appraisal regulations at 12 C.F.R. Part 34, Subpart C; Federal Reserve Board appraisal regulations at 12 C.F.R. Part 225, Subpart G; and Office of Thrift Supervision appraisal regulations at 12 C.F.R. Part 564. Even in the absence of a legal requirement to do so, prudent lenders will routinely take appropriate steps to determine the value of the property securing the loan when making a credit decision. The LLC will provide typical appraisal services.

## 3. Closing Management

When a creditor finds it inconvenient or impossible to close a loan at its office or using its own employees, *e.g.*, to out-of-area obligors, or when special expertise or documents are required, creditors typically engage a closing agent to conduct the closing. Often, title insurance agencies perform closing services as the functions may overlap, *e.g.*, recording of mortgages, UCC-1 financing statements, and similar documents. In some cases, closing services include the disbursement of loan proceeds. When such closings occur, the LLC will ensure disbursement will be made in compliance with the OCC’s interpretive rulings regarding the origination and making of loans at banking and other than banking offices. Specifically, the closing of loans will occur either at a branch of the Bank or at the office of an unaffiliated entity, such as a lawyer’s office or other location, that is not owned by the Bank or any of its affiliates.

## 4. Flood Insurance

The National Flood Insurance Act of 1968 and the Flood Disaster Protection Act of 1973, as amended (42 U.S.C. §§ 4001-4129) (collectively, the “FDPA”), require federally insured depository institutions to obtain flood insurance in connection with Mortgage Loans in certain circumstances. While the LLC will not act as a flood insurance underwriter, it will provide services to creditors who must comply with the FDPA requirements, such as determining if the

real estate collateral is located within a flood hazard area and providing a flood certificate and borrower disclosure notice as contemplated by the Acts.

#### 5. Credit Reporting

The LLC will provide lenders with credit reports on consumers (such reports will often qualify as “consumer reports” under the Fair Credit Reporting Act, 15 U.S.C. §§ 1681, *et seq.*), corporations, partnerships and other entities.

#### 6. Property Inspections

In connection with the collateral for Mortgage Loans, at the request of the lender or borrower, the LLC will arrange for inspections to determine the condition of collateral securing Mortgage Loans. This will include inspections of commercial or construction loan collateral during the construction phase, inspections of real estate held as Other Real Estate Owned (“OREO”), as well as inspections of property that will secure a Mortgage Loan for which an application has been made. The LLC will provide lenders, borrowers, and servicers with reports of such inspections, including damage reports and photographs. Where special expertise is warranted, such inspections will be carried out by qualified third-party vendors and LLC employees will not be engaged in such inspections.

#### 7. Property Preservation

On real estate held as OREO, the LLC will arrange for the maintenance and preservation of the property, including winterization, lock change, board-up, debris removal, lawn service, pool covering, and preparation for conveyance.

#### 8. Loan Document Preparation

Upon being advised by a lender of the terms of a loan, the LLC will prepare and complete the necessary loan documents appropriate to close the loan. It is anticipated the LLC will develop and maintain a database of standardized and customized loan documents.

#### 9. Census Tract and Related Information

Creditors must have census tract data for their required Home Mortgage Disclosure Act (“HMDA”) filings. The LLC will provide to lenders census tract metropolitan statistical area, county code and state code information applicable to Mortgage Loans.

#### 10. Portfolio Audit

The LLC will design or assist lenders to design and execute an audit of their Mortgage Loan portfolio to assess compliance with the FDPA requirements.

### 11. Real Estate Tax Service

In connection with the collateral for Mortgage Loans, the LLC will provide complete real estate tax services, including, *e.g.*, procuring state and local tax bills, reporting such information to the servicers in time for establishing escrow accounts and paying tax bills, and data processing and administration services with respect to escrows, taxes, and delinquencies.

### 12. Finder for an Intermediary in Like-Kind Exchanges

A “1031” or “like-kind” exchange is the sale of one property followed by the purchase of another where the transaction is treated as a tax-free exchange for federal income tax purposes. In order to qualify for tax-free treatment (i) the funds must be held by a qualified intermediary; (ii) both properties must be of “like kind;” and (iii) the exchange time period requirements must be met. In addition, the properties must be either held for productive use in a trade or business, or held for investment. An affiliate of the Vendor currently acts as an intermediary for like-kind exchanges. The LLC will bring together parties who are interested in pursuing a 1031 exchange of property and then refer them to the Vendor affiliate, in return for a fee. The parties themselves, together with the intermediary, will negotiate and consummate the 1031 exchange.

### C. Relationship Between the Bank and the LLC

To the extent that the LLC provides Services to bank holding company subsidiary affiliates of the Bank, the LLC and such affiliates will enter into a contract providing for the LLC to furnish the Services on an arm's length basis as required by Section 23B of the Federal Reserve Act, 12 U.S.C. § 371c-1. The Bank has no current plans to provide credit to or enter into a guarantee on behalf of the LLC.

## II. ANALYSIS

In a variety of circumstances, the OCC has authorized a national bank to make a non-controlling investment in an enterprise, either directly, or indirectly through an operating subsidiary. The enterprise might be a corporation, a limited partnership, or a limited liability company.<sup>4</sup> Such an investment is permissible provided that four criteria or standards are satisfied. These standards, which have been distilled from our previous decisions in this area, are:

1. the activities of the enterprise in which the investment is made must be limited to activities that are part of, or incidental to, the business of banking;

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<sup>4</sup> See, *e.g.*, Conditional Approval No. 307 (Mar. 19, 1999) (corporation); Conditional Approval No. 295 (Dec. 3, 1998) (limited partnership); Conditional Approval No. 308 (Apr. 8, 1999) (limited liability company). *See also* 12 C.F.R. § 5.36(b) (national banks are permitted to make various types of equity investments pursuant to 12 U.S.C. § 24(Seventh) and other statutes).

2. the bank must be able to prevent the enterprise from engaging in activities that do not meet the foregoing standard, or be able to withdraw its investment;
3. the bank's loss exposure must be limited, as a legal and an accounting matter, and the bank must not have open-ended liability for the obligations of the enterprise; and
4. the investment must be convenient or useful to the bank in carrying out its business and not a mere passive investment unrelated to that bank's banking business.

As explained below, the proposed investment in the LLC satisfies all of these requirements.

1. *The activities of the enterprise in which the investment is made must be limited to activities that are part of, or incidental to, the business of banking.*

OCC precedents on non-controlling ownership have recognized that the enterprise in which a national bank holds an interest must confine its activities to those that are part of, or incidental to, the business of banking. The Services to be provided by the LLC have previously been authorized for national banks as activities that are a part of, or incidental to, the business of banking.

(1). Title Insurance Agency

The sale of general insurance as agent from a place the population of which is less than 5,000 is permitted by 12 U.S.C. § 92. The OCC has previously authorized the Bank to conduct general insurance agency activities from such a place, and the Operating Subsidiary was established pursuant to this authority.<sup>5</sup> The LLC will be located in Pineville, North Carolina, a place of less than 5,000, in which the Bank operates a branch. The OCC has previously authorized national banks to conduct title insurance agency activities through joint ventures with title insurance vendors.<sup>6</sup> The LLC will be operated according to the principles outlined in the First Union Letter.

(2). Appraisal Management

The OCC has permitted national banks to perform real estate appraisals both for themselves and for other lenders.<sup>7</sup>

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<sup>5</sup> Interpretive Letter No. 753, *reprinted in* [1996-1997 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 81-107 (Nov. 4, 1996) ("First Union Letter"). *See also Barnett Bank of Marion County, N.A. v. Nelson*, 517 U.S. 25 (1996); Interpretive Ruling 7.1001, 12 C.F.R. § 7.1001.

<sup>6</sup> *See, e.g.*, Conditional Approval No. 276 (May 8, 1998) (authorizing 50-percent investment through an operating subsidiary in a limited partnership engaged in title insurance and related activities) ("Mellon Letter"); Interpretive Letter No. 842, *reprinted in* [1998-1999 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 81-297 (Sept. 28, 1998) (same, direct investment).

<sup>7</sup> Mellon Letter, *supra* note 6; Interpretive Letter No. 467, [1988-1989 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 85,691 (Jan. 24, 1989) (national bank operating subsidiary to offer real estate appraisal services for the bank

(3). Closing Management

It has long been recognized that national banks or their operating subsidiaries may conduct loan closing services both for themselves and for other lenders.<sup>8</sup> Loan closing services may include the disbursement of loan proceeds. You have represented that loan closings in North Carolina will take place at the offices of attorneys, as required by North Carolina law, while loan closings outside of North Carolina will take place at the offices of unaffiliated third parties. This will ensure compliance with the OCC's regulations and interpretive rulings regarding the origination and making of loans at banking and other than banking offices. See Interpretive Rulings 7.1003, 7.1004, and 7.1005, 12 C.F.R. §§ 7.1003, 7.1004 and 7.1005. Thus, the LLC's office will not be a branch of the Bank since loan proceeds will not be disbursed there.

(4). Flood Insurance

The OCC has previously authorized an operating subsidiary to perform flood insurance services.<sup>9</sup>

(5). Credit Reporting

The OCC has previously authorized an operating subsidiary to engage in credit reporting activities, including operation of a credit-reporting bureau.<sup>10</sup>

(6). Property Inspections

The OCC has previously authorized an operating subsidiary to engage in property inspections in connection with lending activities.<sup>11</sup>

(7). Property Preservation

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and other financial institutions); see 12 C.F.R. § 5.34(e)(3)(ii)(G) (operating subsidiaries engaging in real estate appraisal activities qualify for expedited approval).

<sup>8</sup> Mellon Letter, *supra* note 6; see Interpretive Letter No. 776, *reprinted in* [1997 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 81-203 (Mar. 18, 1997) (closing loans is among the essential activities associated with the lending function); Interpretive Letter No.368, *reprinted in* [1985-1987 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 85,538 (July 11, 1986) (describing duties of closing agent and noting that banks close loans for customers).

<sup>9</sup> Mellon Letter, *supra* note 6; Corporate Decision No. 97-79 (July 11, 1997).

<sup>10</sup> Mellon Letter, *supra* note 6; letter of John E. Shockey, Deputy Chief Counsel (May 18, 1976) (unpublished).

<sup>11</sup> Mellon Letter, *supra* note 6; Interpretive Letter No. 806, *reprinted in* [1997-1998 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 81-253 (Oct. 17, 1997) (property inspections in conjunction with net leases of real estate to Muslims who, because of religious beliefs, cannot obtain traditional mortgages).

The acquisition, holding and managing of real property as OREO is permitted by 12 U.S.C. § 29 and 12 C.F.R. Part 34, Subpart E. OCC regulations expressly authorize national banks to expend funds to maintain and preserve OREO.<sup>12</sup>

(8). Loan Document Preparation

The OCC has previously found that the preparation of loan-related documents is an integral part of the lending function and a logical outgrowth of that function, and thus legally permissible.<sup>13</sup> The LLC will not assume greater risks of inaccuracy or deficiencies in preparation of loan documents than the risks already assumed by the Bank with respect to preparing loan-related documents itself.

(9). Census Tract Information

The OCC has found that gathering census tract and related information for purposes of complying with HMDA is legally permissible, as it is a logical outgrowth of the lending function and convenient and useful to a bank's compliance with HMDA's requirements.<sup>14</sup> The LLC will not assume greater risks of inaccurate data entry than the risks already assumed by the Bank with respect to its HMDA compliance.

(10). Portfolio Audit

The OCC has found that loan portfolio audit is a logical outgrowth of, as well as convenient and useful to, the making of loans which are subject to the FDPA, and therefore legally permissible.<sup>15</sup> An effective audit of a bank's portfolios will also help assure that borrowers receive the insurance protections should a flood occur. By engaging in this service, the LLC will be assuming the same risks as the Bank, which is already subject to the FDPA.

(11). Real Estate Tax Services

The OCC has found that assuring the payment of local real estate taxes is legally permissible since it is an integral part of, or a logical outgrowth of, the lending function.<sup>16</sup> It also relieves borrowers of making

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<sup>12</sup> Property preservation (maintenance) activities are governed by 12 C.F.R. § 34.86(b)(1). *See also* Mellon Letter, *supra* note 6 (authorizing title insurance joint venture to perform property preservation services).

<sup>13</sup> Mellon Letter, *supra* note 6.

<sup>14</sup> *Id.*

<sup>15</sup> *Id.*

<sup>16</sup> *Id.*



regular tax and insurance payments. Such tax services are also typically required in order for a loan to be sold into the secondary mortgage market. By performing this service, the LLC will be assuming the same risks that the Bank has assumed in acting as escrow agent for tax and insurance payments.

(12). Finder for an Intermediary in Like-Kind Exchanges

Interpretive Ruling 7.1002, 12 C.F.R. § 7.1002, permits national banks to act as finders. The Bank's investment in the LLC and the resulting relationship with the Vendor will enable the Bank to provide finder services for owners of investment property. As required by the Interpretive Ruling, the LLC will not become involved in the negotiation or consummation of the transaction.

Accordingly, the first standard is satisfied.

2. *The bank must be able to prevent the enterprise from engaging in activities that do not meet the foregoing standard, or be able to withdraw its investment.*

The Bank's investment in the LLC will be consistent with prior OCC interpretive letters relating to a national bank's minority investment, which require the right to veto any proposed activity that is not permissible for national banks, or the ability to withdraw from the investment. The Operating Agreement provides that the LLC shall only engage in activities that are permissible for national banks, and gives the Operating Subsidiary the right to veto any proposed new activities that are not bank-permissible.

Accordingly, the second standard is satisfied.

3. *The bank's loss exposure must be limited, as a legal and an accounting matter, and the bank must not have open-ended liability for the obligations of the enterprise.*

- a. Loss exposure as a legal matter

A primary concern of the OCC is that national banks should not be subjected to undue risk. Where an investing bank will not control the operations of the entity in which it holds an interest, it is important that the bank's investment not expose it to unlimited liability. The Bank's losses will be limited, both as a legal and as an accounting matter.

As a legal matter, the Bank's losses are limited by statute and the governing documents of the LLC. With respect to liabilities of the LLC, Delaware law provides that the debts, obligations and liabilities of a limited liability company, whether arising in contract, tort or otherwise, shall be solely the debts, obligations and liabilities of the limited liability company; and no member or manager of a limited liability company shall be obligated personally for any such debt, obligation or liability solely by reason of being

a member or acting as a manager of the limited liability company.<sup>17</sup> In addition, the Operating Agreement provides that no member shall be liable for the debts, liabilities, or obligations of the LLC or other members without prior written consent.

The Bank will also be protected by the corporate veil of the Operating Subsidiary, a North Carolina corporation. North Carolina law provides that a shareholder is not liable to the corporation or its creditors except to pay the consideration for which the shares were issued.<sup>18</sup> You have represented that both the LLC and the Operating Subsidiary will comply with corporate formalities in order to maintain corporate separateness from the Bank.

b. Loss exposure as an accounting matter

In assessing a bank's loss exposure as an accounting matter, the OCC has previously noted that the appropriate accounting treatment for a bank's 20- to 50-percent ownership share in a limited liability company is to report it as an unconsolidated entity under the equity method of accounting. Under this method, unless the bank has extended a loan to the entity, guaranteed any of its liabilities, or has other financial obligations to the entity, losses are generally limited to the amount of the investment shown on the investor's books.<sup>19</sup> You have advised that the Bank's investment in the LLC will be accounted for as an unconsolidated subsidiary under the equity method of accounting.

Accordingly, the Bank's potential losses will be limited for both legal and accounting purposes. Since that exposure will be quantifiable and controllable, the third standard is satisfied.

4. *The investment must be convenient or useful to the bank in carrying out its business and not a mere passive investment unrelated to the bank's banking business.*

Twelve U.S.C. § 24(Seventh) gives national banks incidental powers that are "necessary" to carry on the business of banking. "Necessary" has been judicially construed to mean "convenient or useful."<sup>20</sup> Accordingly, our precedents on bank non-controlling investments have indicated that the investment must be convenient or useful to the investing bank's business activities, and not constitute a mere

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<sup>17</sup> Del. Code Ann. tit. 6 § 18-303(a) (Michie Supp. 1998). However, Delaware law also allows a member or a manager to enter into an agreement to be personally liable for the debts, obligations and liabilities of a limited liability company. *Id.* tit. 6 § 18-303(b). You have represented that the Operating Subsidiary will not enter into such an agreement.

<sup>18</sup> N.C. Gen. Stat. § 55-6-22 (1990).

<sup>19</sup> *See generally* Accounting Principles Board, Op. No. 18 § 19 (1971) (equity method of accounting for investments in common stock).

<sup>20</sup> *Arnold Tours, Inc. v. Camp*, 472 F.2d 427, 432 (1st Cir. 1972).

passive investment unrelated to that bank's banking business. The investment must benefit or facilitate that business and cannot be a mere passive or speculative investment.

The LLC will benefit the Bank's business by providing the Bank's real estate lending operations with a reliable, high-quality resource for the placement of title insurance and settlement services on a national scale at a competitive price. In addition, the Vendor brings a high level of practical experience and professionalism necessary to oversee the day-to-day operations of a title insurance agency.

Accordingly, the fourth standard is satisfied.

### III. CONCLUSION

Based upon the foregoing facts and analysis, and the representations and commitments made by the Bank in connection with this application, we conclude that the Bank may hold a 50-percent interest in the LLC, and perform the stated activities, in the manner described in this letter. This approval is subject to the following conditions:

1. The Operating Subsidiary and the LLC may engage only in activities that are part of, or incidental to, the business of banking;
2. The Bank, through the Operating Subsidiary, will have effective veto power over any activities or major decisions of the LLC that are inconsistent with condition (1), or will withdraw from the LLC in the event it engages in an activity inconsistent with condition (1);
3. The Bank will account for its minority investment in the LLC under the equity method of accounting; and
4. The LLC will be subject to OCC supervision, regulation, and examination.

Please be advised that the conditions of this approval are deemed to be "conditions imposed in writing by the agency in connection with the granting of any application or other request" within the meaning of 12 U.S.C. § 1818.

If you have any further questions, you may contact Richard Erb, Licensing Manager, Bank Organization and Structure Division, at (202) 874-5060, or Christopher C. Manthey, Senior Attorney, Bank Activities and Structure Division, at (202) 874-5300.

Sincerely,

/s/

Julie L. Williams  
Chief Counsel