Comptroller of the Currency
Administrator of National Banks

Washington, DC 20219

Conditional Approval #316
July 1999

June 30, 1999

Mr. Michael E. Bleier
General Counsel
Mellon Bank
One Mellon Bank Center
Pittsburgh, Pennsylvania 15258-0001

Mr. Donald Davis
First Independence National Bank of Detroit
44 Michigan Avenue
Detroit, Michigan 48226

Mr. Louis E. Prezeau
City National Bank of New Jersey
900 Broad Street
Newark, New Jersey 07102

Mr. Walter Grady
Seaway National Bank of Chicago
645 East 87th Street
Chicago, Illinois 60619

Re: Application and requests for approval to acquire and hold non-controlling interests in a limited liability company engaged in personal property leasing activities
Application Control Number: 99-NE-08-0014

Dear Messrs. Bleier, Davis, Prezeau, and Grady:

This is in response to your application and letters to the Office of the Comptroller of the Currency ("OCC"), seeking approval to acquire and hold directly or indirectly through a wholly-owned operating subsidiary, non-controlling interests in a limited liability company. By application dated April 6, 1999,

Mellon Bank, N.A., Pittsburgh, Pennsylvania ("Bank"), requested approval to acquire and hold through a wholly-owned subsidiary, Mellon Leasing Corporation ("Subsidiary"), a forty (40) percent non-controlling interest in a joint venture ("LLC"), a Michigan limited liability company.[1] By letters, dated April 20 and June 2, 1999, First Independence National Bank of Detroit, Detroit, Michigan, requested confirmation to make a direct fifteen (15) percent non-controlling investment in the LLC and to abide by the conditions OCC imposes on national banks making these types of non-controlling minority investments. By letters, dated May 18, 1999, and June 11, 1999, City National Bank of New Jersey, Newark, New Jersey, and Seaway National Bank of Chicago, Chicago, Illinois, respectively, also requested confirmation to make a direct fifteen (15) percent non-controlling minority investment in the LLC. (The three national bank investors and a fourth state bank investor in the LLC hereinafter referred to as the "Participants").[2] The Participants or their parent entities are minority-owned or -controlled businesses.

The LLC will conduct personal property leasing activities and provide various personal property leasing services in compliance with 12 C.F.R. Part 23. Subsidiary currently engages in the personal property leasing business.

For the reasons set forth below, we conclude that through Subsidiary, the Bank and the Participants may acquire an interest in the LLC, subject to the conditions set forth below.[3]

PROPOSAL

Articles of Organization will be filed in Michigan to create the LLC, and the Bank's Subsidiary and each Participant will enter into an Operating Agreement to govern the activities of the LLC. Subsidiary will hold a forty (40) percent interest and each Participant will directly or indirectly hold a fifteen (15) percent interest in the LLC. The LLC will provide various personal property leasing services in compliance with the OCC's leasing regulations set forth at 12 C.F.R. Part 23.

When businesses have a need to lease equipment and other personal property, it is contemplated they will contact the LLC, describe their particular leasing needs, complete the requisite documentation to apply for approval to lease the desired equipment and, if approved, execute lease agreements and ancillary documents.

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[1] The OCC had approved the Bank's engaging in personal property leasing activities through an operating subsidiary in 1976.

[2] The fourth Participant in the LLC is Liberty Bank and Trust Company, New Orleans, Louisiana. Liberty Bank and Trust Company is a Louisiana-chartered commercial bank not subject to OCC supervision, and not required to inform the OCC of its intention to invest in the LCC.

[3] The national bank Participants each are permitted to make direct non-controlling minority investments in the LLC, to acquire and hold its respective fifteen (15) percent interest, subject to the same conditions that apply to the Bank.

The LLC will be structured so as to qualify as a Minority Business Enterprise certified by the Michigan Minority Business Development Council.[4] The Bank and the national bank Participants believe that their joint ownership in the LLC will further the minority business goals of the Michigan Minority Business Development Council. Participation in the joint venture will provide a number of benefits to the minority-owned or -controlled banks; it will provide an opportunity for these banks to engage in the personal property leasing business, further developing each banks' leasing services expertise and providing expanded product lines and services to its customers. The Participants will use their investment in the LLC as a means of offering customers and potential customers personal property leasing services that the Participants could not as economically or effectively offer directly as a start up product line. In this way, the investment enhances the banks' ability to provide a complete line of banking and bank related services to a broader range of customers, and to compete more effectively by efficiently and capably offering these specialized services.

The LLC will provide equipment leasing services initially to Ford Motor Company,[5] and ultimately to other companies. The LLC will both originate equipment leasing transactions for its own account as well as operate as a lease advisor/broker, originating transactions which will be sold to other lessors. It is expected that the LLC will hold for its own account approximately twenty (20) percent of the transactions it originates and will sell the remainder to other lessors. The originated leases will cover various types of personal property, including high technology equipment, leased under operating leases.

With respect to transactions held by the LLC for its own account, financing will principally be in the form of either non-recourse loans from other financial institutions to the LLC or the sale of receivables (with the residual investment in the transactions retained by the LLC). In both cases, the lender or receivables purchaser will be assigned, or granted a security interest in, the leased equipment and the related lease documents. Transactions not retained by the LLC for its own account will be sold in their entirety (lease rentals and residual position in the leased equipment) to other lessors.

When providing lease advisory services, the LLC will consult with its leasing customer, determine what the customer's equipment leasing needs are, and then attempt to obtain and/or provide the best lease terms available for the desired equipment. When it plans to assign a lease after closing, the LLC will

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[4] Among other things, such a certification is predicated upon the fact that the Participants or their parent entities, as the case may be, are minority-owned or -controlled businesses. Each Participant will represent and warrant in the constituent documents of the LLC that it is a qualified Minority Business Enterprise, certified by, or acceptable to, the Michigan Minority Business Development Council and that it will maintain such status as long as it remains a Participant in the LLC.

[5] Ford Motor Company will also derive a benefit from this arrangement. As a company that transacts significant business with the federal government, it must provide certain business opportunities to minority-owned businesses.

first identify potential lessors of the equipment, taking into consideration pricing, expertise and lease servicing capacity; typically, several potential lessors will be considered. When a vendor and equipment are selected, the LLC will arrange for the purchase and leasing of the equipment.[6]

Toward the end of the lease term, the LLC will advise its leasing customers with respect to evaluating the residual value of the leased equipment; this will help the customer appropriately and more accurately to make plans with respect to the retention or return of the equipment at the end of the lease term. The LLC also will maintain records of the equipment it leases and will keep its customers, including those whose leases are assigned by the LLC, informed of approaching lease termination dates. This will enhance the customers' planning and decision-making with respect to lease terminations, purchase options and continuing equipment needs.[7]

The LLC will be capitalized in cash by Subsidiary and the Participants in direct proportion to their relative ownership interests. The management of the LLC will be directed by a board of managers comprised of eight members: three members from Subsidiary; one member from each of the four Participants; and the chief executive officer of the LLC. The board of managers will have full and complete authority, power and discretion to manage and control the business, affairs and properties of the LLC, subject to terms of the Operating Agreement.

Initially, the LLC will have six employees: a chief executive officer, an account executive, two leasing specialists, a controller, and a manager of operations.[8] In addition, Mellon US Leasing, a division of Subsidiary, will provide the LLC with certain lease administration services, pursuant to a Services Agreement between the LLC and Mellon US Leasing. The Bank will provide lockbox services relative to the receipt and disbursement of lease payments, including both leases retained by the LLC as well as leases it assigns to others.

ANALYSIS

The OCC has traditionally recognized the authority of national banks to organize and perform any of their lawful activities in a reasonable and convenient manner not prohibited by law. A national bank may engage in activities that are part of or incidental to the business of banking by means of an

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[6] When the lease is to be assigned, the LLC will structure its equipment financing in conjunction with the evaluation and selection of the lease assignee/servicer. In such cases, the LLC will coordinate the acquisition process, including the collection of invoices, payment of the vendor, etc. Typically, the assignment of the transaction will occur prior to the purchase of the equipment; thus, the assignee lessor will actually purchase the equipment from the vendor. When the LLC will not assign the lease to another lessor, the leasing process is simplified somewhat in that an assignee lessor will not have to be approved and selected.

[7] Subsidiary currently provides all of the foregoing services to Ford Motor Company.

[8] The account executive and two leasing specialists are currently employed by a division of Subsidiary.

operating subsidiary. *See* 12 C.F.R. § 5.34(d)(1). Further, the OCC has permitted national banks to own, either directly or indirectly through an operating subsidiary, a non-controlling interest in an enterprise. The enterprise might be a limited partnership, a corporation, or a limited liability company.[9] In recent interpretive letters, the OCC has concluded that national banks are legally permitted to make a non-controlling investment in a limited liability company provided the following four criteria or standards are met:[10]

> (1) The activities of the entity or 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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> (2) The bank must be able to prevent the enterprise or entity from engaging in activities that do not meet the foregoing standard or be able to withdraw its investment;
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> (3) The bank's loss exposure must be limited, as a legal and accounting matter, and the bank must not have open-ended liability for the obligations of the enterprise; and
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> (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.

Based upon the facts presented, the Bank's proposal satisfies these four standards with respect to the Bank and to each of the national bank Participants.

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

Our precedents on non-controlling ownership have recognized that the enterprise in which the bank holds an interest must confine its activities to those that are part of, or incidental to, the conduct of the business of banking.[11]
The LLC will conduct personal property leasing activities that are authorized by 12 U.S.C.

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[9] *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.

[10] *See* Interpretive Letter No. 692, *reprinted in* [1995-1996 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 81,007 (November 1, 1995), and No. 694, *reprinted in* [1995-1996 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 81,009 (December 13, 1995). In other recent letters, the OCC has permitted national banks to make a non-controlling investment in an enterprise other than an LLC, provided the investment satisfies these four standards. *See, e.g.*, Interpretive Letter No. 697, *reprinted in* [1995-1996 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 81,012 (November 15, 1995); Interpretive Letter No. 705, *reprinted in* [1995-1996 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 81,020 (October 25, 1995).

[11] *See, e.g.*, Interpretive Letter No. 380, *reprinted in* [1988-1989 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 85,604 n.8 (December 29, 1986) (since a national bank can provide options clearing services to customers it can purchase stock in a corporation providing options clearing services); Letter from Robert B. Serino, Deputy Chief Counsel (November 9, 1992) (since the operation of an ATM network is ?a fundamental part of the basic business of banking,? an equity investment in a corporation operating such a network is permissible).

§§ 24(Seventh) or 24(Tenth) and in compliance with the requirements of 12 C.F.R. Part 23. The Operating Agreement by which Subsidiary and the Participants will be bound will clearly state that the LLC shall not engage in any activity not permissible for national banks. Accordingly, we conclude that the activities to be conducted by the LLC are part of, or incidental to, the business of banking and, therefore, the first standard is met.

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 activities of the enterprise in which a national bank may invest must be part of, or incidental to, the business of banking not only at the time the bank first acquires its ownership, but for as long as the bank has an ownership interest. This standard may be met if the Bank is able to exercise a veto power over the activities of the enterprise, or is able to dispose of its interest.[12]

Pursuant to the LLC Operating Agreement, the LLC may only engage in activities that are part of, or incidental to, the business of banking, as such phrase is interpreted by the OCC. Furthermore, the LLC Operating Agreement authorizes the Subsidiary and the national bank Participants to withdraw from the LLC by selling their interests to a third party, thus satisfying the second standard.[13]

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

a. Loss exposure from a legal standpoint

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 the bank holds an interest, it is important that the national bank's investment not expose it to unlimited liability. As a legal matter, investors in a Michigan limited liability company will not incur liability with respect to

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[12] *See, e.g.*, Interpretive Letter No. 711, *reprinted in* [1995-1996 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 81-026 (February 3, 1996); Interpretive Letter No. 625, *reprinted in* [1993-1994 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 83,507 (July 1, 1993).

[13] The Operating Agreement shall provide that if a Participant or Subsidiary desires to sell its interest in the LLC to a party not affiliated with the selling entity, the LLC shall have the right of first refusal to purchase such interest; if the LLC does not exercise the right, then the individual Participants will be granted the right of first refusal. If neither the LLC nor the remaining Participants exercise such right, the selling member will be free to sell its interest to a third party. With the exception of a sale by Subsidiary, the purchasing entity must be a minority business enterprise as defined by the Michigan Minority Business Development Council. The OCC has concluded that the second minority investment factor is satisfied even if the provisions regarding the right to transfer an investment are complex, provided that transfers of ownership interests to other parties can be accomplished. *See* Conditional Approval No. 202 (April 25, 1996).

the liabilities or obligations of the limited liability company solely by reason of being a member or manager of the limited liability company.[14] The LLC will be adequately capitalized by the Bank, through Subsidiary, and by Participants. At all times, the Bank, Subsidiary, the LLC and each of the Participants will adhere to corporate and other applicable formalities to ensure all the entities maintain their corporate existences separate from the LLC. None of the constituent documents of the LLC, including the Articles of Incorporation and the Operating Agreement, will provide for any liability on the part of the Bank, Subsidiary, or Participants for the obligations of the LLC. Nor will the Bank, Subsidiary, or Participants guarantee or otherwise assume any liabilities of the LLC. Additionally, in the case of Subsidiary, the operating subsidiary structure itself inherently provides some limitations on liability. Thus, the Bank's, the Subsidiary's and each Participant's loss exposure for the liabilities of the LLC will be limited solely to each entity's capital contribution.

b. Loss exposure from an accounting standpoint

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 of investment in a limited liability company is to report it on an unconsolidated basis. Under the equity method of accounting, 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.[15]

The Bank will account for its forty (40) percent investment in the LLC under the equity method of accounting. Thus, the Bank's loss from an accounting perspective would be limited to the amount invested in the LLC, and the Bank will not have any open-ended exposure to the liabilities of the LLC.

Some of the Participants may choose to use the cash or cost method of accounting for their fifteen (15) percent investments. Under the cost method of accounting, the investor records an investment at cost, dividends are the basis for recognition of earnings (although in the case of a limited liability company, dividends are generally not issued), and losses recognized by the investor are limited to the extent of the investment. Regardless of whether the Participants use the cost or equity method of accounting, each national bank Participant's maximum risk of loss should be limited to the amount of its respective investment in the LLC (plus potentially, the amount of any additional extensions of credit).[16] In either case, its exposure is quantifiable and controllable and, thus, the national bank Participants will not have open-ended liability for the liabilities of the LLC.

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[14] *See* MICH. COMP. LAWS § 450.4501 (1998).

[15] *See generally,* Accounting Principles Board, Op. 18 ¶ 19 (1971) (equity method of accounting for investments in common stock). Interpretive Letter No. 692, *supra.*

[16] First Independence National Bank of Detroit and City National Bank of New Jersey have indicated each will exert sufficient control to use the equity method of accounting.

Therefore, for both legal and accounting purposes, the Bank's and each national bank Participant's potential loss exposure relative to the LLC should be limited to the amount of its investment. Thus, the third standard is satisfied.

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

A national bank's investment in an enterprise or entity that is not an operating subsidiary of the bank must also satisfy the requirement that the investment have a beneficial connection to the bank's business, *i.e.*, be convenient or useful to the investing bank's business activities, and not constitute a mere passive investment unrelated to that 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."[17] Our precedents on bank non-controlling investments have indicated that the investment must be convenient or useful to the bank in conducting *that bank's* business. The investment must benefit or facilitate that business and cannot be a mere passive or speculative investment.[18]

The services to be provided by the LLC are currently performed by Subsidiary when engaging in the personal property leasing business. By means of the LLC, the Bank will provide another delivery channel for that business. The LLC will contract with a division of Subsidiary to perform certain lease administration services and the Bank will provide lockbox services to the LLC, generating additional revenues to the Bank and Subsidiary. In addition, each national bank Participant will be able to engage in the equipment leasing business, further developing its expertise and providing expanded product lines and services to its customers. The Bank and the national bank Participants believe that their joint ownership in the LLC will contribute to, and facilitate, the objectives of the Michigan Minority Business Development Council and will leverage that experience and expertise for its own benefit and that of its customers. For these reasons, the investment is convenient and useful to the Bank and the national bank Participants in carrying out their respective banking businesses and is not a mere passive investment. Thus, the fourth standard is satisfied.

CONCLUSION

Based upon the information and representations the Bank and the national bank Participants have

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[17] *See Arnold Tours, Inc. v. Camp*, 472 F.2d 427, 432 (1st Cir. 1972).

[18] *See, e.g.*, Interpretive Letter No. 697, *supra*; Interpretive Letter No. 543, *reprinted in* [1990-1991 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 83,255 (February 13, 1991); Interpretive Letter No. 427, *reprinted in* [1988-1989 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 85,651 (May 9, 1988); Interpretive Letter No. 421, *reprinted in* [1988-1989 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 85,645 (March 14, 1988); Interpretive Letter No. 380, *supra.*

provided, and for the reasons discussed above, we conclude that the Bank and the national bank Participants may make the direct or indirect investments to acquire and hold non-controlling minority interests in the LLC in the manner and as described herein, subject to the following conditions:

1. The LLC will engage only in activities that are part of, or incidental to, the business of banking;

2. The Bank and the national bank Participants will have veto power over any activities and major decisions of the LLC that are inconsistent with condition number one, or will withdraw from the LLC in the event they engage in an activity that is inconsistent with condition number one;

3. The Bank and the national bank Participants will account for their investments in the LLC under the equity or cost 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 and, as such, may be enforced in proceedings under applicable law.

This approval is granted based on a thorough review of all information available, including the representations and commitments made in the application and by Bank representatives.

Sincerely,

/s/

Julie L. Williams
Chief Counsel