Comptroller of the Currency
Administrator of National Banks

Central District Office
One Financial Place, Suite 2700
440 South LaSalle Street
Chicago, Illinois 60605

December 2, 1997

Interpretive Letter #815
January 1998
12 U.S.C. 24(7)68
12 U.S.C. 24(7)81

Dear [ ],

This responds to your letter of September 3, 1997, requesting confirmation that the [ ] ("*Bank*"), [*City, State*], may lawfully retain its minority, noncontrolling interest in [ ] ("*TC*"), [*City, State*], a state-chartered trust company.

Based on the information and representations provided and for the reasons set forth below, I agree with your conclusion that [*Bank*] may retain its interest in [*TC*].

I. BACKGROUND

[*Bank*], a nationally-chartered trust company and wholly-owned subsidiary of [ ] Corporation, a holding company, currently manages over $1.4 billion in assets in more than 1,500 accounts. On September 16, 1997, [*Bank*] acquired a 15% interest in [*TC*], a trust company chartered under the laws of Indiana. [*TC*] was owned by three shareholders prior to [*Bank*]'s purchase. Two of the shareholders, [*Mr. 1*] and [*Mr. 2*], are also in key management positions. The third shareholder is not active in the operation of [*TC*]. [*TC*] currently has approximately $250 million in assets under management in more that 600 accounts.

Pursuant to a Stock Acquisition Agreement entered into between [*Bank*], [ ] Corporation, [*TC*] and the [*TC*] shareholders, [*Bank*] purchased newly-issued common stock of [*TC*] equal to a 15% interest in [*TC*]. As of the closing on the purchase of these shares, a Shareholders' Agreement was entered into governing the operation of [*TC*], establishing three positions on [*TC*]'s seven-person Board of Directors as [*Bank*]-appointed directors and establishing voting provisions at the shareholder and director level which provide [*Bank*] with veto power over major transaction or management decisions relating to [*TC*].

The Acquisition Agreement further states that [*Bank*] will ultimately acquire the remainder of [*TC*] in a single transaction. Closing on the acquisition of [*TC*]'s remaining shares is anticipated to occur by June 30, 2002. Between June 30, 2000, and June 30, 2002, there will be a revenue valuation confirmation period during which the two organizations will work together for [*Bank*]'s purchase of [*TC*]'s remaining shares. Prior to its closing on those remaining shares, [*Bank*] will notify and seek approval of the Office of the Comptroller of the Currency for its acquisition of [*TC*] through a merger pursuant to 12 U.S.C. § 215a.

The Acquisition Agreement also provides for various contingencies during the nearly five-year period from the initial purchase of the newly issued shares in September 1997 through the closing on the remaining shares in 2002. If any adverse change occurs with respect to [*TC*], [*Bank*] would be relieved of any obligation to acquire the remaining shares and would be entitled to have the newly-issued shares repurchased by the [*TC*] shareholders. Adverse changes include a material adverse change in the financial condition of [*TC*]; a material adverse change in the customer base of [*TC*]; the conviction of any Shareholder of a felony; a revocation, withdrawal, suspension or termination by banking regulators or other governmental authorities of [*TC*]'s authority to conduct operations in the ordinary course of business; or the death and/or disability of [*TC*]'s two key officers prior to June 30, 2000, or within twelve months of each other.

II. ANALYSIS

[*Bank*]'s purchase of a 15% interest in [*TC*] initially raises the issue of the authority of a nationally-chartered trust company to hold a minority, noncontrolling interest in a corporation. In a variety of circumstances the OCC has permitted national banks to own, either directly, or indirectly through an operating subsidiary, a minority interest in an enterprise. In several recent interpretive letters, the OCC concluded that national banks are legally permitted to make a minority, noncontrolling investment in an entity provided that four standards are satisfied. *See* Comptroller Interpretive Letters No. 737 (August 19, 1996), reprinted in [1996-1997 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 81,101; No. 732 (May 10, 1996), reprinted in [1995-1996 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 81,049; No. 694 (December 13, 1995), reprinted in [1995-1996 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 81,009; and No. 692 (November 1, 1995), reprinted in [1995-1996 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 81,007. These standards, which have been distilled from our previous decisions in the area of permissible minority, noncontrolling investments for national banks and their subsidiaries, are:

(1) the activities of the enterprise in which the bank invests must be limited to activities that are part of, or incidental to, the business of banking;

(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 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.

Each of these standards is discussed below and applied to [*Bank*]'s investment.

1. The activities of the enterprise in which the bank invests must be limited to activities that are part of, or incidental to, the business of banking.

Our precedents on minority, noncontrolling stock ownership have recognized that the enterprise in which the bank takes an equity interest must confine its activities to those that are part of, or incidental to, the conduct of the banking business. See, e.g., Comptroller Interpretive Letter No. 380 (December 29, 1986), reprinted in [1988-1989 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 85,604 n.8 (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 (Nov. 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).

You have represented that [*TC*] provides trust and fiduciary services, including the normal and customary services associated with administering trusts and estates, managing agency accounts, providing custodial and safekeeping services, serving in various fiduciary capacities, and providing pension and employee benefit services. It is well established that national banks may engage in trust activities. 12 U.S.C. § 92a.

Thus, the activities performed by [*TC*] are activities that are part of, or incidental to, the business of banking, and 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 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. *See,* *e.g.*, Interpretive Letter No. 711 (February 3, 1996), reprinted in [1995-1996 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 81-026; Interpretive Letter No. 625 (July 1, 1993), reprinted in [1993-1994 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 83,507. This ensures that the bank will not become involved in activities which are not part of, or incidental to, the business of banking.

A number of provisions governing the relationship between [*Bank*] and [*TC*] will cause [*TC*] to restrict its activities to those that are part of, or incidental to, the business of banking. First, [*TC*]'s articles of incorporation will be amended to limit its activities to those that are part of, or incidental to, the business of banking. Second, the Acquisition Agreement provides for [*Bank*] to be relieved of any obligation to acquire the remaining shares and entitles it to have the newly-issued shares repurchased by the [*TC*] shareholders in the event of an adverse or material change in [*TC*]. Third, the Shareholders' Agreement provides for the Board of Directors of [*TC*] to have seven (7) members, including the three (3) [*TC*] shareholders, one (1) individual chosen by those three shareholders, and three (3) additional directors to be chosen by [*Bank*]. The Shareholders' Agreement further provides that the affirmative vote of 80% of [*TC*]'s Board of Directors is required for major decisions and transactions, including adding a new line of business or making any changes in the scope or nature of the business of [*TC*].[1] Thus, [*Bank*] has the veto power to prevent [*TC*] from engaging in any activities that are not part of, or incidental to, the business of banking.

Through the revised articles of incorporation, Acquisition Agreement, and the [*Bank*]-designated positions on the [*TC*] Board of Directors, [*Bank*] can assure that [*TC*] does not engage in activities that are not a part of, or incidental to, the business of banking. Therefore, the second standard is satisfied.

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. In

---

[1]Although the Shareholders' Agreement does not provide for [*Bank*]'s withdrawal from its investment if [*TC*] engages in activities that are not part of, or incidental to, the business of banking, the Agreement does require the unanimous vote of the Shareholders to amend [*TC*]'s Articles of Incorporation. Since [*TC*]'s articles of incorporation will provide that it will not engage in activities that are not part of, or incidental to, the business of banking, [*Bank*] will be able to enforce such provision.

Indiana, trust companies are defined as "corporations,"[2] and, as a legal matter, "a shareholder of a corporation is not personally liable for the acts or debts of the corporation." Ind. Code Ch. 23-1-26-3(b) (1993). *See also* Aronson v. Price, 644 N.E.2d 864, 867 (Ind. 1994) ("corporate shareholders sustain liability for corporate acts only to the extent of their investment"). Thus, [*Bank*]'s loss exposure for the liabilities of [*TC*] is limited by statute.

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 minority investment is to report it as an unconsolidated entity under the equity method of accounting. Under this method, unless the bank has guaranteed any of the liabilities of the entity or has other financial obligations to the entity, losses are generally limited to the amount of the investment, including loans and other advances shown on the investor's books. *See generally*, Accounting Principles Board, Op. 18 § 19 (1971) (equity method of accounting for investments in common stock). Interpretive Letter No. 692, *supra.*

[*Bank*] has a 15 percent ownership interest in [*TC*], and will account for its investment under the equity method. [*Bank*]'s loss exposure is initially limited to the amount of its investment and is subject to certain rights to have its shares repurchased upon the occurrence of adverse changes in circumstances. Further, [*Bank*]'s obligation to proceed with the purchase of the remaining shares is conditioned upon [*TC*]'s continued financial and operational performance.

Therefore, for both legal and accounting purposes, [*Bank*]'s potential loss exposure relative to [*TC*] should be limited to the amount of its investment. Since that exposure is 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 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." *See* Arnold Tours, Inc. v. Camp, 472 F.2d 427, 432 (1st Cir. 1972). 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. *See, e.g.* OCC Conditional Approval No. 186 (Nov. 15, 1995) (National bank may indirectly own a 25 percent interest in a trust company.)

From your statements, it appears that [*Bank*] has valid business reasons for its investment in [*TC*]. You state that this investment allows [*Bank*] to extend its trust business into a new market through [*TC*], an established trust provider. For this reason, [*Bank*]'s investment

---

[2] Ind. Code Ch. 28-1-5-1(a)(1993).

benefits and furthers its banking business by enabling [*Bank*] to gain new trust customers through [*TC*]. In addition, [*Bank*]'s investment is intended to provide a vehicle for the orderly acquisition of [*TC*]. Thus, it is not merely a passive or speculative investment. Accordingly, the fourth standard is satisfied.

III. *CONCLUSION*

This opinion is based on a thorough review of all information available, including representations and commitments submitted by [*Bank*], and by its representatives. Based on these representations and for the reasons outlined above, we conclude that the Bank may legally retain its investment in [*TC*], subject to the following conditions:

1. [*TC*] will engage only in activities that are part of, or incidental to, the business of banking;

2. [*Bank*] will have veto power over any activities and major decisions of [*TC*] that are inconsistent with condition number one, or will withdraw from [*TC*] in the event that it engages in an activity that is inconsistent with condition number one;

3. [*Bank*] will account for its investment in [*TC*] under the equity method of accounting; and

4. [*TC*] will be subject to OCC supervision, regulation, and examination.

These conditions are conditions imposed in writing by the OCC in connection with its action on the request for a legal opinion confirming that [*Bank*]'s investment is permissible under 12 U.S.C. § 24 (Seventh) and, as such, may be enforced in proceedings under applicable law.

If you have any questions, please contact me or Giovanna Cavallo, Attorney, at (312) 360-8805.

Sincerely,

/s/

Coreen S. Arnold
District Counsel