Comptroller of the Currency
Administrator of National Banks

Washington, DC 20219

March 20, 2000

Conditional Approval #371
April 2000

Mr. Philip O. Farr
Vice President
Grange National Bank
101 Main Street
Post Office Box 56
Laceyville, PA 18623

Re: Application by Grange National Bank, Laceyville, Pennyslvania, to expand the activities of its operating subsidiary to make a noncontrolling investment in a limited liability partnership that will engage in title insurance sales.
Application Control No.: 2000 NE 08 0001

Dear Mr. Farr:

This responds to the application filed by Grange National Bank, Laceyville, Pennsylvania ("Bank"), pursuant to 12 C.F.R. § 5.34(e) to expand the activities of its operating subsidiary, Grange National Insurance Agency ("Grange Subsidiary"), by acquiring and holding a noncontrolling interest in a limited partnership that will sell title insurance. For the reasons set forth below, the application is approved subject to the conditions set forth below.

Proposal

The Grange Subsidiary will become a 50 percent limited partner in a limited liability partnership ("LLP") established under the laws of Pennsylvania. The other 50 percent interest will be that of the general partner, Mt. Laurel Abstract Co. ("Mt. Laurel"), a Pennsylvania corporation. The Grange Subsidiary and Mt. Laurel will each contribute 50 percent of the initial capital. Profit and losses will be allocated and distributed equally between the Grange Subsidiary and Mt. Laurel.

The LLP will operate pursuant to a limited partnership agreement ("Partnership Agreement"). In accordance with the Partnership Agreement, Mt. Laurel will be responsible for the exclusive control and management of the LLP. However, the Grange Subsidiary will have the right to prevent the LLP from engaging in any activity that is not permissible for a national bank.

Furthermore, the Grange Subsidiary has the right to withdraw from the LLP if the LLP engages in any such activity.

The LLP will be licensed to sell title insurance by the Pennsylvania Department of Insurance, and all title examiners employed by the LLP will be licensed to the extent required by Pennsylvania law. The LLP will have its registered office and principal place of business in Tunkhannock, Pennsylvania. Although the LLP will act as a title insurance agency, in no event will it become obligated as a title insurer. The Bank has represented that it and all its affiliated parties mentioned in its application letter will act in compliance with all applicable laws, including the restrictions related to "Affiliated Business Arrangements" as defined in the Real Estate Settlement Procedures Act, 12 U.S.C. 2601 and the anti-tying restrictions found in the Bank Holding Company Act, 12 U.S.C., section 1972, to the extent applicable.

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 permissible for a national bank by means of an operating subsidiary that engages solely in activities that national banks are permitted to engage in directly and are conducted subject to the same terms and conditions that govern the conduct of such activities by national banks. *See* Section 121 of the Gramm-Leach-Bliley Act ("GLBA").[1] Further, the OCC has permitted national banks to own, either directly or indirectly through an operating subsidiary, a noncontrolling interest in an enterprise. The enterprise might be a limited partnership, a general partnership, a corporation, a limited liability corporation, or other entity permitted under applicable state law. In recent interpretive letters, the OCC has concluded that national banks are legally permitted to make a noncontrolling investment in an enterprise, provided certain criteria or standards are met:[2]

(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 (or otherwise authorized for a national bank);

(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;

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[1] Pub. L. No. 106-102, 113 Stat. 1338 (1999).

[2] *See* Interpretive Letter No. 705, *reprinted in* [1995-1996 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 81,020 (October 25, 1995), permitting national banks to make a noncontrolling investment in a limited partnership. Earlier OCC letters permitted national banks to make noncontrolling investments in limited liability companies and other enterprises. *See* Interpretive Letter No. 692, *reprinted in* [1995-1996 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 81,007 (November 1, 1995); Interpretive Letter No. 694, *reprinted in* [1995-1996 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 81,009 (December 13, 1995); and Interpretive Letter No. 697, *reprinted in* [1995-1996 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 81,012 (November 15, 1995).

(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 and useful to the bank in carrying out its business and not merely a passive investment unrelated to that bank's banking business.

Based upon the facts presented, the Bank's proposal satisfies these four standards.

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 (or otherwise authorized for a national bank).

Banks may make noncontrolling investments in an enterprise that confines its activities to those that are permissible for a national bank.[3] Sales of title insurance are expressly authorized for national banks by section 303 of the GLBA. The Bank may therefore hold an interest in the title insurance LLP.

Section 303(b)(1) of the GLBA provides that:

> *Notwithstanding any other provision of law* (including section 104 of this Act), in the case of any State in which banks organized under the laws of such State are authorized to sell title insurance as agent, a national bank may also sell title insurance as agent, but only in the same manner, to the same extent, and under the same restrictions as such State banks are authorized to sell title insurance as agent in such State. (emphasis added).

Section 303(b)(1) is entitled "nondiscriminatory parity exception" to the prohibition in section 303(a) on title insurance activities by national banks, and is clearly designed to ensure parity between national and state banks. This exception makes it clear that sales of title insurance by a national bank are subject to the same restrictions on the sales of title insurance by a state bank. The authority of section 303(b) applies "notwithstanding any other provision of law." The plain language of this section clearly permits sales of title insurance without regard to the geographic limits of 12 U.S.C. § 92. Therefore, a national bank may sell title insurance from a place of any size in a particular state if a state bank may sell title insurance in the state.

In 1997, the Pennsylvania legislature amended its insurance laws to specifically provide that "financial institutions"[4] may be licensed to sell insurance anywhere in the state provided certain

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[3] *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).

[4] A "financial institution" is defined as "any federal or state-chartered bank, bank and trust company, savings bank,

conditions are met concerning disclosure, physical location, customer privacy and anti-tying. *See* Act of June 25, 1997, P.L. 349, No. 40 ("1997 Act"). Pennsylvania law contains express provisions that permit financial institutions to be licensed to sell insurance from any place in Pennsylvania without any geographic restrictions. Pa. Cons. Stat. Ann. tit. 40 § 286(b) (Purdon 1999). The law provides that: "[a] financial institution, and any officer, employee or agent thereof, that sells insurance shall be licensed in accordance with the provisions of this Act and regulations promulgated under this Act." *Id*. The following restrictions are applicable to the sale of insurance (except credit insurance) by financial institutions and agents and brokers thereof:

(a) [such sales] shall take place in a location that is distinct from the area where deposits are taken and loan applications are discussed and accepted. Signs or other means shall be used to distinguish the insurance or annuities sales area from the deposit taking and lending areas. The Insurance Commissioner shall exempt a financial institution from the requirements of this section if the number of staff or size of the facility would prevent compliance.

(b) Compliance by a financial institution with the setting and circumstances requirements set forth in the "Interagency Statement on Retail Sales of Nondeposit Investment Products" issued February 15, 1994, by the Board of Governors of the Federal Reserve System, the Federal Deposit Insurance Corporation, the Office of the Comptroller of the Currency, and the Office of Thrift Supervision, shall satisfy the requirements of subsection (a).

Pa. Cons. Stat. Ann. tit. 40 § 287 (Purdon 1999), *see also Id* at § 288 (customer privacy) and § 275(b) (anti-tying).

Therefore, state-chartered banks are authorized to sell title insurance anywhere in the state.[5] Accordingly, pursuant to section 303(b) of the GLBA, national banks are authorized to sell title insurance in the same manner, to the same extent, and under the same restrictions as such state banks. Thus, 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 the investment.

The activities of the enterprise in which a national bank may invest must be permissible for a national bank 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.[6]

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savings and loan association, trust company or credit union." Pa. Cons. Stat. Ann. tit. 40 § 231 (Purdon 1999).

[5] The Bank has represented that its planned sales of title insurance are consistent with applicable state law.

[6] *See, e.g.*, Interpretive Letter No. 711, *reprinted in* [1995-1996 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 81-026 (February 23, 1996); Interpretive Letter No. 625, *reprinted in* [1993-1994 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 83,507 (July 1, 1993).

The Partnership Agreement gives the Grange Subsidiary the right to prevent the LLP from engaging in any activity if that activity does not comply with the above standard. Furthermore, the Grange Subsidiary has the right to withdraw from the LLP if the LLP engages in any activity that does not comply with that standard. 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. Normally, this is not a concern when a national bank invests in a corporation, for shareholders are not liable for the debts of the corporation, provided proper corporate separateness is maintained.[7] In the present case, the Bank and the Grange Subsidiary are separate corporations distinct from each other and from the LLP.

A limited partner in a limited liability partnership established under Pennsylvania law will not incur liability with respect to the certain liabilities or obligations of the limited liability partnership that arise from any negligent or wrongful acts or misconduct committed by another partner or other representative of the partnership. Pa. Cons. Stat. Ann. tit. 15 § 8204 (Purdon 1999). This limited liability feature is what differentiates limited liability partnerships from general partnerships, where all partners are generally liable for all the liabilities or obligations of the partnership, including those that arise from any negligent or wrongful acts or misconduct committed by another partner or other representative of the partnership; and from limited partnerships, which must have at least one general partner who is personally liable for the all the liabilities or obligations of the partnership, including those that arise from any negligent or wrongful acts or misconduct committed by another partner or other representative of the partnership.

Furthermore, the Partnership Agreement provides that the Grange Subsidiary is not liable for any express liabilities or obligations of the LLP. Consequently, the Bank's loss exposure for the liabilities of the LLP will be limited to the Grange Subsidiary's capital contribution to the LLP.

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 investment in an entity is to report it as an unconsolidated entity under the equity method of accounting. Under this method,

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[7] *See* 1 William M. Fletcher, Fletcher Cyc. Corp. § 25 (Perm. Ed. 1999).

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 shown on the investor's books.[8]

The Bank has represented that it will account for the Grange Subsidiary's investment in the LLP under the equity method of accounting. Therefore losses by the Bank and the Grange Subsidiary from an accounting perspective will be limited to the amount invested by the Grange Subsidiary.

Accordingly, for both legal and accounting purposes, the Bank's potential loss exposure will be limited to its investment in the LLP. 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 the 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 and 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."[9] Our precedents on bank noncontrolling 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.[10]

The services provided by the LLP are the types routinely required by the Bank when engaged in the business of making mortgage loans and will provide a convenient and useful source of these services that are ancillary to extending credit secured by real estate. Offering these services through the LLP will enhance the ability of the Bank to offer mortgage loans more efficiently and capably to the public from a one-stop source, while generating additional revenue for the Bank. For these reasons, the investment is convenient and useful to the Bank in carrying out its lending business and is not a mere passive investment. Accordingly, the fourth standard is satisfied.

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[8] *See generally* Accounting Principles Board, Op. 18 § 19 (1971) (equity method of accounting for investments in common stock).

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

[10] *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.*

Conclusion

Based upon the information and representations that you have provided, and for the reasons discussed above, we conclude that the Bank may, through the Subsidiary, acquire and hold a noncontrolling interest in the LLP, subject to the following conditions:

(1) the LLP will engage in activities that are permissible for a national bank;

(2) the Bank will have veto power over any activities and major decisions of the LLP that are inconsistent with condition (1) above, or will withdraw from the LLP in the event that it engages in an activity that is inconsistent with condition (1);

(3) the Bank will account for its investment in the LLP under the equity method of accounting; and,

(4) the LLP will be subject to OCC supervision and examination, subject to the limitations and requirements of 12 U.S.C.§ 1831v.

Please be advised that the conditions of this approval are deemed to be "condition(s) 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 the Bank's representatives. If you have any further questions, you may contact James Vivenzio, Senior Attorney, at (212) 790-4010, or Nina Lipscomb, Analysis Specialist, at (212) 790-4055.

Sincerely,

-signed-

Julie L. Williams
First Senior Deputy Comptroller
and Chief Counsel