



Comptroller of the Currency
Administrator of National Banks

Washington, DC 20219

Conditional Approval #317
August 1999

July 19, 1999

Mr. Larry P. Cole
First Tennessee National Corporation
165 Madison Avenue
Memphis, TN 38103

Re: Application of First Tennessee Bank, N.A., Memphis, Tennessee, to participate in a joint venture providing real estate tax reporting and management services -- Application Control No. 99-SE-08-021

Dear Mr. Cole:

This is in response to your application dated April 21, 1999, which incorporated your earlier letter dated April 9, 1999, and was later supplemented by your letter dated April 23, 1999, by which First Tennessee Bank, N.A. ("FTBNA"), applied to participate, through two operating subsidiaries and one direct investment, in a joint venture providing real estate tax reporting and management services maintained in connection with first mortgage purchase and refinanced loans. For the reasons set forth, the Office of the Comptroller ("OCC") approves FTBNA's application to conduct the proposed activities in the manner described, subject to the conditions set forth below.

Background

As described in your letters, FTBNA contributed equity to FT Real Estate Information Mortgage Solutions Holdings, Inc. ("Holdings"), a Delaware "C" corporation. FTBNA formed Holdings for the sole purpose of holding a one hundred percent (100%) ownership interest in FT Real Estate Information Mortgage Solutions, Inc. ("Mortgage Solutions"), also a Delaware "C" Corporation. Holdings contributed the equity it received from FTBNA to Mortgage Solutions, which then contributed the equity to Total Mortgage Solutions, L.P. ("Total"), a Delaware limited partnership, in exchange for a forty-nine and one half percent (49.5%) interest in Total.

Total is a joint venture among Mortgage Solutions, First American Real Estate Flood & Tax Solutions, L.L.C. ("First"), and JV Mortgage Solutions, L.L.C. ("JV"), a Delaware limited liability company. JV is a joint venture between FTBNA and First American Real Estate Solutions, L.P. ("First American"),

in which FTBNA and First American each own a fifty (50%) interest. FTBNA contributed equity directly into JV. JV, controlling a one percent (1%) interest, is the general partner of Total. Mortgage Solutions and First are the limited partners, each controlling a forty-nine and one-half (49.5%) percent interest. First American has a one hundred percent (100%) interest in First. First American is not affiliated with FTBNA and FTBNA does not have a financial interest in First American.

Total will provide real estate tax reporting and management services maintained in connection with first mortgage purchase and refinanced loans. Initially, Total will only provide services for FTBNA, its subsidiaries, and its affiliates. In the future, Total may market its services to unaffiliated banks, thrifts, and credit unions. Total may also market its services to unaffiliated mortgage or finance companies that are the subsidiaries of banks or their holding companies, thrifts or their holding companies, or credit unions. Total will not provide tax advice to any person or entity.

Analysis

FTBNA's application raises both operational and structural issues: (1) whether the activities are legally permissible for a national bank and its operating subsidiaries; and (2) whether a national bank has authority to hold--directly or indirectly through an operating subsidiary--an equity interest in the various proposed structures.

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 under 12 U.S.C. § 24(Seventh) by means of an operating subsidiary.¹ A national bank, through its operating subsidiary, has also been authorized to be a general partner. Similarly, the OCC has permitted national banks, directly or indirectly through operating subsidiaries, to be limited partners in partnerships.

In its application, FTBNA proposes to establish two structures. Under the first structure, FTBNA would establish two operating subsidiaries, Holdings and Mortgage Solutions. Holdings and Mortgage Solutions are qualifying subsidiaries as defined in 12 C.F.R. § 5.34(d)(2) because FTBNA owns one hundred percent (100%) of the two subsidiaries. Mortgage Solutions would acquire a 49.5% interest as a limited partner in Total through equity provided by Holdings. The issue presented by this structure is whether FTBNA, indirectly through its operating subsidiaries, may hold a noncontrolling interest in Total.

Under the second structure, JV would acquire a 1% interest as a general partner in Total through equity provided by FTBNA and First American. This structure raises two issues: (1) whether FTBNA may hold a noncontrolling interest in JV; and (2) whether JV may hold a noncontrolling interest in Total.

¹ 12 C.F.R. § 5.34(d)(1).

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 entity. The entity may take different forms, including a limited partnership, a corporation, or a limited liability company.² The OCC has concluded that minority, noncontrolling investments are legally permitted if four standards are met. These standards 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 the bank's banking business. Each of these standards is discussed below and applied to the three issues.

(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.

OCC precedents have recognized that the enterprise in which a national bank takes an equity interest must confine its activities to those that are part of, or incidental to, the business of banking.³ National banks have long been permitted to service the loans that they make and servicing frequently entails the assurance that local real estate taxes are paid on time, particularly when such loans involve tax escrow accounts. Such tax service is an integral part or logical outgrowth of the lending functions. Initially, Total will only provide services for FTBNA, its subsidiaries, and its affiliates. In the future, Total may market its services to unaffiliated banks, thrifts, and credit unions. Total may also market its services to unaffiliated mortgage and finance companies that are the subsidiaries of banks or their holding companies, thrifts or their holding companies, or credit unions. The OCC has previously recognized that providing tax reporting services to affiliates and other lenders is part of, or incidental to, the business of banking.⁴

² See Interpretive Letter No. 737, *reprinted in* [1996-1997 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 81,101 (Aug. 16, 1996); Interpretive Letter No. 732, *reprinted in* [1995-1996 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 81,049 (May 10, 1996); Interpretive Letter No. 694, *reprinted in* [1995-1996 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 81,009 (Dec. 13, 1995); and Interpretive Letter No. 692, *reprinted in* [1995-1996 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 81,007 (Nov. 1, 1995).

³ See Interpretive Letter No. 711, *reprinted in* [1995-1996 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 81,026 (Feb. 23, 1996); Interpretive Letter No. 694, *supra* note 1 (national bank permitted to take non-controlling, minority interest in LLC that purchases secured home improvement loans and resells them in secondary market).

⁴ Conditional Approval No. 276 (May 8, 1998).

Total will provide services that are part of, or incidental to, the business of banking. Therefore, the first standard is met for all three issues.⁵

(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 an enterprise in which a bank invests must be part of, or incidental to, the business of banking not only at the time the bank initially acquires its ownership, but they must remain so for as long as the bank has an ownership interest. This standard may be met if the bank is able to exercise a veto or is able to dispose of its interest.⁶ This ensures the bank will not become involved in activities that are not part of, or incidental to, the business of banking.

You have represented that safeguards will be in place with respect to Holdings, Mortgage Solutions, JV, and Total to ensure that they only conduct activities permissible for national banks or their operating subsidiaries. Section 5.3(e) of the Agreement of Limited Partnership of Total Mortgage Solutions, L.P. (“Total Agreement”) restricts the General Partner from doing any act that is not permitted of a national bank. JV is the General Partner and the Limited Liability Company Agreement of JV Mortgage Solutions, LLC (“JV Agreement”) also restricts JV from engaging in activities not permitted of national banks.

The Agreements permit JV to withdraw from Total and FTBNA to withdraw from JV should the entities engage in activities not permitted of national banks. Section 8.6 of the Total Agreement also permits Mortgage Solutions to withdraw as a Limited Partner from Total should it engage in activities that a national bank may not engage in. The agreements also submit JV and Total to the jurisdiction, supervision, and examining authority of the OCC.

By these means, FTBNA will be able to ensure that Holdings, Mortgage Solutions, JV, and Total only conduct activities that are part of or incidental to the business of banking, or that the respective entity may withdraw from a given entity in the event that it is not able to prevent such activities from taking place.

⁵ The activities of Holdings, Mortgage Solutions, and JV are limited to investing either directly or indirectly in Total. Therefore, since Total will only be conducting activities that are part of, or incidental to the business of banking, they will be limited to conducting activities that are part of, or incidental to the business of banking.

⁶ Interpretive Letter No. 711, *supra* note 2; Interpretive Letter No. 694, *supra* note 1.

(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 not be subjected to undue risk, especially where an investing bank will not control the operations of the entity in which the bank holds an interest. 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

Similarly, investors in a LLC generally will not incur liability with respect to the liabilities or obligations for the LLC. The Delaware Limited Liability Company Act provides:

[T]he 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 of the limited liability company solely by reason of being a member or acting as a manager of the limited liability company.⁸

Thus, FTBNA's losses for its investment in JV will be limited by statute. The OCC has previously recognized that a LLC statute provides a national bank acquiring a fifty percent non-controlling interest in a LLC adequate loss exposure from a legal standpoint.⁹ FTBNA's investment in JV satisfies this standard.

As a general matter of partnership law, a general partner has unlimited liability for the obligations of a partnership. A general partner in a limited partnership has analogous liability.¹⁰ The OCC has permitted operating subsidiaries of national banks to enter into general partnerships that engage in bank-permissible activities when the corporate veil of the operating subsidiary corporation protects the

⁷ 1 William M. Fletcher, *Fletcher Cyclopedia of the Law of Private Corporations* § 25 (perm. ed. rev. vol. 1990).

⁸ Del. Code Ann. tit. 6, § 18-303 (1999).

⁹ Interpretive Letter No. 819, *reprinted in* [1997-1998 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 81,268 (Jan. 20, 1998).

¹⁰ *See* Del. Code Ann. tit. 6, § 17-403 (1999).

bank from the potential open-ended exposure associated with a direct partnership investment.¹¹ Similar legal safeguards exist where a LLC, in which a bank has an interest, acquires a general partnership interest in a limited partnership that will engage in bank-permissible interests.

In your letter, you represented that JV and Total will at all times adhere to applicable formalities so that FTBNA will maintain its separate corporate existence from JV and Total. The Agreements do not provide for FTBNA to have any liability for the obligations of JV or Total. Consequently, sufficient legal safeguards exist for JV to hold a general partnership interest in Total.

National banks are permitted, directly or indirectly through operating subsidiaries, to become limited partners in partnerships engaging in activities permissible for national banks.¹² Delaware law limits the liability of a limited partner in a limited partnership.¹³ Additionally, section 6.3 of the Total Agreement limits the liability of Mortgage Solutions to its capital contribution and distributions, if any. Therefore, Mortgage Solutions may hold a limited partnership in Total as it will engage in permissible activity provided the entities adhere to the requisite corporate formalities.

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 noncontrolling investment is to report it as an unconsolidated entity under the cost or equity method of accounting.¹⁴ Under these methods, 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.

You have represented that FTBNA will use the equity method of accounting in reporting an investment in both JV and Total on an unconsolidated basis. FTBNA will neither guarantee nor assume any liabilities for either JV or Total. Therefore, the equity method of accounting will limit FTBNA's liability. Accordingly, for both legal and accounting purposes, FTBNA's potential loss exposure should be limited to the amount of its investment. Because the Bank will not have open-ended liability and its potential liability will be quantifiable and controllable, the third standard is satisfied.

¹¹ Conditional Approval No. 276 (May 8, 1998); Interpretive Letter No. 517, *reprinted in* [1990-1991 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 83,228 (Feb. 23, 1996); Interpretive Letter No. 289, *reprinted in* [1983-84 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 85,453 (May 15, 1984).

¹² Interpretive Letter No. 617, *reprinted in* [1992-1993 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 83, 457 (Mar. 4, 1993) (national bank may purchase limited partnership units in a partnership which will be formed and licensed as a Small Business Investment Company).

¹³ Del. Code. Ann. tit. 6, § 17 (1999).

¹⁴ Conditional Approval No. 304 (Mar. 5, 1999) (approving the use of both the cost and equity methods of accounting in connection with noncontrolling equity investments).

(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.*

Under 12 U.S.C. § 24(Seventh), a national bank is given all incidental powers that are necessary to carry on the business of banking. Courts have construed "necessary" to mean "convenient or useful."¹⁵ A national bank's investment in an enterprise or entity, whether through an operating subsidiary or not, 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 be a mere passive investment unrelated to its business activities.¹⁶

You have represented that Total will provide services of the types routinely purchased or performed by lenders when engaged in the business of making mortgage loans. Total would provide a useful and convenient source of these essential services that are ancillary to extending credit secured by real estate. Total will enhance FTBNA's ability to offer its mortgage loans more efficiently and capably to the public while generating additional revenues for FTBNA. Accordingly, this standard is satisfied.

Conclusion

Based upon the information and representations you have provided, and for the reasons discussed above, it is our opinion that FTBNA is legally permitted to make the investments as described herein, subject to the following conditions:

- (1) JV and Total will engage only in activities that are part of, or incidental to, the business of banking;
- (2) FTBNA, either directly or indirectly, will have veto power over any activities and major decisions of JV and Total that are inconsistent with condition (1) or it, or the relevant entity in which it directly or indirectly invested, will withdraw from JV and Total in the event they engage in an activity that is inconsistent with condition (1);
- (3) FTBNA will account for its investments in JV and Total under the cost or equity method of accounting; and

¹⁵ *Arnold Tours, Inc. v. Camp*, 472 F.2d 427, 432 (1st Cir. 1972).

¹⁶ Interpretive Letter No. 697, *reprinted in* [1995-1996 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 81,012 (Nov. 15, 1995); Interpretive Letter No. 543, *reprinted in* [1990-1991 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 83,255 (Feb. 13, 1991); Interpretive Letter No. 427, *reprinted in* [1988-1989 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 851,651 (May 9, 1988); Interpretive Letter No. 421, *reprinted in* [1988-1989 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 85,645 (Mar. 14, 1988).

- (4) JV and Total will be subject to OCC supervision, regulation, and examination.

Accordingly, this application is approved subject to the above conditions. 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.

If you have any further questions, you may contact Louis Gittleman, Senior Corporate Analyst, Southeastern District, at (404) 588-4525, or Stephen Lybarger, NBE/Licensing Expert, Bank Organization and Structure Division, at (202) 874-5060.

Sincerely,

/s/

Julie L. Williams
Chief Counsel

Application Control Number 99-SE-08-021