



Comptroller of the Currency
Administrator of National Banks

Washington, DC 20219

Conditional Approval #456
April 2001

March 10, 2001

Sterling A. Spainhour
Senior Vice President and
Associate General Counsel
Wachovia Bank, N.A.
100 North Main Street
Winston-Salem, North Carolina 27101

Re: Application by Wachovia Bank, N.A., Winston-Salem, North Carolina, to Acquire An Operating Subsidiary That Holds a Non-Controlling Interest in a Corporation That Engages in Professional Employee Organization Services -- Application Control No. 2000-SE-08-0062.

Dear Mr. Spainhour:

I. Background

The Bank proposes to acquire 51 percent of Davis Baldwin Enterprise Solutions (“DBES”), a Florida limited liability company, which means that DBES will be an operating subsidiary of the Bank. DBES, in turn, owns a small interest in Agency Solutions International (“ASI”), a Florida corporation.¹

ASI is a holding company that provides, by means of subsidiaries, human resources and employment-related administrative services to client businesses. The services performed include acting as a co-employer of the clients’ workers, employment benefits management, human resource management, workers’ compensation management, compliance administration, and

¹ DBES holds its interest through a limited partnership, ASI Partners, Ltd. (“ASI Partners”). DBES owns 3.57% of the limited partnership units of ASI Partners, which in turn owns 33.75% of the shares of ASI. This means, in effect, that DBES holds less than a 2% interest in ASI. ASI Partners is merely a vehicle for holding shares in ASI, and engages in no other activity.

safety-risk management and training. Collectively, these are known as professional employee organization or “PEO” services.

ASI engages in no activities itself, but provides these services through ten wholly-owned subsidiaries. Six of these subsidiaries provide PEO services in various states. This structure is advantageous due to differences in state laws and regulations. Of the other four subsidiaries, one provides payroll services for ASI and its subsidiaries; one purchases employer liability and worker’s compensation insurance for ASI and its subsidiaries; one is inactive; and one serves as the general partner of ASI Partners. The Bank will have an indirect, non-controlling interest in each of these subsidiaries to the same extent as its interest in the parent company, ASI.

DBES, in addition to its ownership of a small interest in ASI, helps to market the PEO services of one of the subsidiaries of ASI, AdvanTech Solutions I, Inc. (“AdvanTech”), in consideration for the payment by ASI of commission income to DBES. AdvanTech is a Florida corporation that provides PEO services in the states of Georgia, Florida, and Texas. Through DBES, the Bank will market these PEO services to its small- and medium-sized customers. The Bank will thus be able to offer a service to its customers while generating fee income for itself.

II. Analysis

A. Acquisition of an Operating Subsidiary

The Bank will acquire 51 percent of the membership interests in DBES from existing members. Thus, the ownership requirements of 12 C.F.R. § 5.34 are met.

DBES will do two things. It will own a small, indirect interest in ASI. As explained below, this is a permissible non-controlling investment. In addition, DBES will perform finder activities for a subsidiary of ASI. This, too, is permissible.

DBES will market AdvanTech’s services to the Bank’s customers and other potential prospects. ASI, AdvanTech’s parent, will compensate DBES by payment of referral fees or commissions for generating new business and renewing existing business. The Bank represents that DBES will not be responsible for or take part in the acceptance of any subscriber by AdvanTech, or take part in the consummation or execution of any professional employee contract between AdvanTech and a subscriber of its services. Therefore, the Bank states that DBES will act only as a finder, bringing together potential buyers and sellers of AdvanTech’s professional employee organization services.

The OCC has long recognized the finder function as a permissible banking activity that includes “without limitation, identifying potential parties, making inquiries as to interest, introducing or arranging meetings of interested parties, and otherwise bringing parties together for a transaction that the parties themselves negotiate and consummate.”² Indeed, an operating subsidiary's activities as a finder are eligible for after-the-fact notice under 12 C.F.R. § 5.34(e)(5)(v)(R) so

² 12 C.F.R. § 7.1002.

long as they are in accordance with published OCC precedent and 12 C. F. R. § 7.1002. The proposed referral and compensation arrangements of DBES and ASI are consistent with OCC precedents.³

B. Non-controlling Investment in a Corporation Providing PEO Services

In a variety of circumstances, the OCC has permitted national banks to own, either directly, or indirectly through an operating subsidiary, a noncontrolling interest in an enterprise, provided four criteria or standards are met. These standards, which have been distilled from our previous decisions in the area of permissible non-controlling investments for national banks and their subsidiaries, 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 (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.
- 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.
- 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.

In the interest of clarity and simplicity, the following analysis applies this four-part test to ASI. However, since ASI is simply a holding company, the activity discussion in reality applies to ASI's subsidiaries. Based upon the facts presented, we conclude, as discussed below, that the Bank's investment in ASI, indirectly through DBES, satisfies these 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).*

The Bank, through its operating subsidiary, DBES, proposes to make a non-controlling investment in ASI, which engages in activities through its subsidiaries. Six of these subsidiaries

³ See, e.g., Interpretive Letter No. 824, *reprinted in* [1997-1998 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 81,273 (Feb. 27, 1998) (referral in connection with insurance sales); Conditional Approval No. 221 (Dec. 4, 1996) (non-controlling investment through an operating subsidiary in a LLC that will provide Internet links to third party vendors' websites); Interpretive Letter No. 607, *reprinted in* [1992-1993 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 83,445 (Aug. 24, 1992) (referral of trust business); Interpretive Letter No. 472, *reprinted in* [1989-1990 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 83,008 (Mar. 2, 1989) (referral of bank mortgage loan customers to providers of homeowners insurance).

will engage exclusively in providing PEO services to customers, an activity that the OCC has previously determined is permissible for national banks.⁴

Of the four other subsidiaries, one performs payroll processing, and another purchases employer's liability and worker's compensation insurance on behalf of the six PEO subsidiaries of ASI. These activities have also been found permissible for national banks.⁵ Another subsidiary is inactive, and the only activity of the last subsidiary is to serve as the general partner of ASI Partners which, as explained in note 1, *supra*, conducts no activities of its own. All it does is hold an interest in ASI. Therefore, the last subsidiary simply holds an indirect interest in the other subsidiaries, whose activities are bank-permissible. Accordingly, the Bank's indirect investment in this subsidiary is also permissible.⁶

Since the activities of ASI, performed through its subsidiaries, have all been determined to be permissible for national banks and their subsidiaries, the first standard is satisfied.⁷

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 the national bank will invest must be part of, or incidental to, the business of banking not only at the time the bank first acquires its ownership interest, 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.

In this instance, the Bank will hold a very small interest in ASI and its subsidiaries. Minority shareholders in a corporation do not possess a veto power over corporate activities as a matter of law. Accordingly, the Bank lacks the ability to restrict the activities of ASI and its subsidiaries to only bank-permissible activities. However, the Operating Agreement governing DBES provides specific procedures to govern a member's sale of its interest in DBES when the member desires to discontinue participation in the company's business.⁸ The Bank represents that should ASI commence any activity that is not part of or incidental to the business of banking, or

⁴ This includes acting as co-employer of the employees of nonbanking companies. Conditional Approval No. 384 (April 25, 2000).

⁵ *Id.*

⁶ *See, e.g.*, Conditional Approval No. 336 (Nov. 2, 1999); Conditional Approval No. 317 n.5 (July 19, 1999).

⁷ Similarly, since ASI Partners simply serves as a vehicle for the Bank's investment in ASI, investment in ASI Partners through DBES is also legally permissible. See note 6, *supra*.

⁸ *See* First Amendment to the Operating Agreement of Davis Baldwin Enterprise Solutions, LLC, §§ 7.11, 7.13.

otherwise permissible for a national bank, the Bank will divest its interest in DBES, or otherwise divest its interest in ASI, within one year.⁹ 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 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 a national bank's investment not expose it to unlimited liability. In this instance, the Bank's minority investment will be held by an operating subsidiary. Florida law provides that members and managers of a limited liability company are not personally liable for the debts or obligations of the LLC. Fla. Stat. Ann. § 608.4227 (West Cum. Supp. 2001). Therefore, the Bank will be insulated from any potential liability arising from ASI, and its loss exposure is limited to the amount of its investment in ASI through the operating subsidiary.

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 less than 20 percent ownership share or investment in an entity is to report it as an unconsolidated entity under the equity or cost method of accounting. Under either method, unless the investor has extended a loan to the entity, guaranteed any of its liabilities, or has other financial obligations, the investor's losses are generally limited to the amount of the investment shown on the investor's books.¹⁰ You have represented that the Bank will account for its investment under the equity method.

Therefore, for both legal and accounting purposes, the Bank's potential loss exposure arising from its investment in ASI should be limited to the amount of its investment. Because 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 that bank's banking business.*

Twelve U.S.C. § 24 (Seventh) gives national banks incidental powers that are "necessary" to carry out the business of banking. "Necessary" has been judicially construed to mean "convenient" or "useful."¹¹ Therefore, OCC precedents on non-controlling investments have indicated that the investment must be convenient or useful to the bank in conducting that bank's

⁹ The OCC previously allowed reasonable periods, not exceeding two years, for the divestiture of nonconforming assets. *See, e.g.*, Conditional Approval No. 319 (July 26, 1999); Conditional Approval No. 259 (October 31, 1997).

¹⁰ *See, e.g.*, Conditional Approval No. 371 (March 20, 2000) (equity method); Conditional Approval No. 333 (Oct. 19, 1999) (cost method).

¹¹ *Arnold Tours, Inc. v. Camp*, 472 F. 2d 427, 432 (1st Cir. 1972).

business. The investment must benefit or facilitate that business and cannot be a mere passive or speculative investment.

In this instance, the Bank's investment in ASI is not passive or speculative. The investment allows the Bank to expand its business into a new area of banking, PEO services. Through DBES, the Bank will market these PEO services to its small- and medium-sized customers, thus providing a service to its customer base while generating fee income. DBES will also act as finder for potential new clients. The Bank's small investment in ASI will enable it to gain knowledge about and experience with the delivery of PEO services without having to acquire control of a professional employee organization at this time. Thus, the fourth standard is satisfied.

III. Conclusion

Based upon the information and representations you have provided, and for the reasons discussed above, we conclude that the Bank may acquire and hold DBES as an operating subsidiary. We further conclude that the Bank may hold an indirect, non-controlling interest in ASI in the manner and as described herein, subject to the following conditions:

- (1) ASI (including its subsidiaries) will engage only in activities that are part of, or incidental to, the business of banking;
- (2) In the event ASI (including its subsidiaries) engages in an activity that is inconsistent with condition number one, the Bank will either divest its interest in DBES, or otherwise divest its interest in ASI, in accordance with Section II-B of this letter;
- (3) The Bank will account for its investment in ASI under the equity or cost method of accounting; and
- (4) ASI (including its subsidiaries) will be subject to OCC supervision and examination, subject to the limitations and requirements of 12 U.S.C. § 1831v.

Please be advised that these conditions 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 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 questions, please contact Debra Burke, Licensing Analyst, Southeastern District, at (404) 588-4525.

Sincerely,

-signed-

Julie L. Williams
First Senior Deputy Comptroller and Chief Counsel