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Comptroller of the Currency  
Administrator of National Banks

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Washington, DC 20219

**Conditional Approval #284**  
**September 1998**

August 14, 1998

Mr. Bruce Rigelman  
Lead Attorney  
Legal Department  
Bank One, National Association  
100 East Broad Street  
Columbus, Ohio 43271-0158

Re: Operating Subsidiary Application of Bank One, N.A., Columbus, Ohio ("Bank One")  
Application Control Number: 98-ML-08-0010

Dear Mr. Bennett:

This is in response to Bank One's June 15, 1998 application to acquire, through an operating subsidiary, Banc One Investment Advisers Corporation ("BOIA"), an indirect non-controlling minority interest in a de novo limited liability company, Pacholder & Co., LLC ("LLC"). LLC will engage in certain investment advisory activities. For the reasons set forth below, we approve the establishment and acquisition of LLC by BOIA, subject to certain conditions.<sup>1</sup>

***I. Background***

Bank One proposes to establish and acquire an indirect non-controlling 49 percent interest in a de novo limited liability company, LLC. Bank One proposes to hold its interest in LLC through its wholly-owned subsidiary, BOIA. LLC will be organized by an incorporated group of management investors, Pacholder Associates, Inc. ("Group"), and LLC will serve as investment advisor to an existing investment fund. In addition, LLC may also engage in other investment advisory and related activities that are permissible for national banks.

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<sup>1</sup> In addition to Bank One's interest in LLC, you also indicated in your letter Bank One's intention to hold a 51 percent indirect interest in Banc One High Yield Partners, LLC ("Newco"), a limited liability company that also will engage in investment advisory and related activities. Because of Bank One's majority interest in Newco, Newco will qualify as an operating subsidiary under OCC regulations. *See* 12 C.F.R. § 5.34(d)(2). A bank may acquire or establish a new operating subsidiary without filing any application if the new subsidiary's activities are limited to those previously reported by the bank in establishing or acquiring a prior operating subsidiary that was deemed permissible by the OCC. *See* 12 C.F.R. § 5.34(e)(4). The new subsidiary's activities must continue to be deemed permissible by the OCC and be conducted in accordance with any conditions previously imposed in approving the prior subsidiary's conduct of those activities. *Id.* Since Bank One and Newco will be in conformity with these regulations, no application or notice to the OCC is required.

LLC will be established under Ohio law and governed by an operating agreement between Bank One and Group. Among other things, the terms of the operating agreement provide that LLC will not engage in any activities that are not permitted for national banks or entities in which national banks may invest, and that Bank One will elect two of the four managers of LLC. Also, under the terms of the agreement, members of LLC that are national banks, such as Bank One, will have the authority to veto activities or withdraw from LLC in the event that LLC engages in activities otherwise impermissible for national banks.

## ***II. Discussion***

### ***A. National Bank Express and Incidental Powers (12 U.S.C. § 24(Seventh))***

Bank One's plan to purchase and hold a 49 percent interest in LLC through BOIA raises the issue of the authority of a national bank to hold--indirectly through an operating subsidiary--a non-controlling interest in an enterprise such as LLC. A number of recent OCC letters have analyzed the authority of national banks, either directly or through their subsidiaries, to own a non-controlling interest in a limited liability company.<sup>2</sup> These letters each concluded that the ownership of such an interest is permissible provided four standards, drawn from OCC precedents, are satisfied.<sup>3</sup> They are:

- (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;
- (2) The bank must be able to prevent the entity or enterprise from engaging in activities that do not meet the foregoing standard, or be able to withdraw from 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 factors is discussed below and applied to your proposal.

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<sup>2</sup> *E.g.*, Conditional Approval Letter No. 269, (January 13, 1998); Interpretive Letter No. 694 (December 13, 1995), *reprinted in* [1995-1996 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 81-009; Interpretive Letter No. 692 (November 1, 1995), *reprinted in* [1995-1996 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 81-007.

<sup>3</sup> *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.

**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 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 business of banking.<sup>4</sup>

LLC will provide investment advisory and related administrative services to an investment fund. This activity is permissible for national banks under 12 U.S.C. § 24(Seventh). *See, e.g.*, 12 C.F.R. § 5.34(e)(3)(ii)(D) which authorizes national banks, under an expedited review process, to establish operating subsidiaries that will serve as investment adviser for investment companies, and 12 C.F.R. §§ 5.34(e)(2)(ii)(C) and (I) which authorize national banks, under a notice process, to establish operating subsidiaries that provide financial advice and consulting for the bank or its affiliates and to act as an investment or financial adviser (not involving the exercise of investment discretion) or provide financial counseling.

As discussed above, Bank One has represented that LLC will engage in acting as an investment advisor to an investment fund. In addition, LLC may also engage in other investment advisory and related activities that are permissible for national banks.

Thus, we conclude that the activities to be conducted by LLC are 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.***

This is an obvious corollary to the first standard. 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.

Several provisions in the LLC Agreement (“the Agreement”) are designed to satisfy the requirement that LLC’s activities remain part of, or incidental to, the business of banking. The Agreement provides that LLC will engage only in activities that are legally permissible for national banks and for which all required regulatory consents or approvals have been obtained and all required regulatory notices have been filed. Moreover, any member who is a national bank will have the right to veto or withdraw from LLC in the event that LLC

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<sup>4</sup> *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).

engages in activities otherwise impermissible for national banks or for which any national bank member has not obtained all required regulatory approvals. Thus, with respect to LLC, this standard is met.

**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. As a legal matter, investors in an Ohio limited liability company do not incur liability with respect to the liabilities or obligations of the limited liability company solely by reason of being a member or manager of the limited liability company. Ohio Rev. Code Ann. § 1705.48(B). In addition, the LLC Agreement specifies that LLC broadly indemnifies the members of LLC from any proceeding against or resulting from the actions or omissions of LLC or the other members of LLC. Thus, Bank One's loss exposure for the liability of LLC is limited by statute and by the Agreement establishing LLC. Moreover, Bank One is further protected from liability since its interest in LLC is held by its subsidiary, BOIA.

*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 20-50 percent ownership share of investment in a limited liability company 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). *See also* Interpretive Letter 692, *supra*.

As previously stated, Bank One will hold through BOIA a 49 percent ownership interest in LLC. Bank One believes that the appropriate accounting treatment for BOIA's investment is the equity method. Thus Bank One's losses from an accounting perspective would be limited to the amount invested in LLC and Bank One will not have any open-ended liability for the obligations of LLC. In addition, as noted above, Ohio law generally would limit members' losses to their capital investment. Therefore, with respect to LLC, 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.***

A national bank's investment in an enterprise or entity 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." *See Arnold Tours, Inc. v. Camp*, 472 F.2d 427, 432 (1st Cir. 1972). Therefore, a consistent thread running through our precedents concerning stock ownership is that it must be convenient or useful to *that bank's* banking business. The investment must benefit or facilitate that business and cannot be a mere passive or speculative investment.<sup>5</sup>

This standard is met here. Bank One's investment in LLC is an extension of the investment advisory business that is currently conducted in BOIA. By working with Group, Bank One hopes to benefit from additional access to Group's expertise in the management of various types of investment funds and assets. Moreover, the LLC Agreement requires Bank One's active participation in LLC through the election of managers, the setting of policies, and the approval of new initiatives by LLC.

For these reasons, the investment in LLC is convenient and useful to Bank One in carrying out its business and is not a mere passive investment. 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 Bank One may acquire, through BOIA, an indirect non-controlling minority interest in LLC. Our approval is subject to the following conditions:

- (1) LLC will engage only in activities that are part of, or incidental to, the business of banking;
- (2) Bank One, through BOIA, will have veto power over any activities and major decisions of LLC that are inconsistent with condition number one, or will withdraw from LLC in the event it engages in an activity that is inconsistent with condition number one;

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<sup>5</sup> *See e.g.*, Conditional Approval Letter No. 248, (June 27, 1997); Conditional Approval Letter No. 200, *supra*; Interpretive Letter No. 543 (February 13, 1991), *reprinted in* [1990-1991 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 83-225.

- (3) Bank One through BOIA will account for the investments in LLC under the equity method of accounting; and,
- (4) 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.

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

If you have any questions, please contact John A. Soboeiro, Senior Attorney, at (202) 874-5300 or Licensing Manager Richard Erb, at (202) 874-5060.

Sincerely,

/s/

Raymond Natter  
Acting Chief Counsel