Comptroller of the Currency
Administrator of National Banks

Washington, DC 20219

Conditional Approval #327
September 1999

September 14, 1999

Mr. John G. Martines
President
LA Bank, N.A.
LA Bank Financial Center
Oppenheim Building
409 Lackawanna Avenue, Suite 201
Scranton, PA 18503

Re: Application by LA Bank, N.A., Lake Ariel, Pennsylvania, to expand the activities of an existing operating subsidiary by acquiring and holding a non-controlling interest in a limited partnership to provide title insurance agency and loan closing management services

Application Control Number: 1999 NE 08 0032

Dear Mr. Martines

This responds to the application filed by LA Bank, N.A., Lake Ariel, Pennsylvania ("Bank"), to expand the activities of an existing operating subsidiary, Ariel Financial Services, Inc. ("Subsidiary") by acquiring and holding a non-controlling interest in a limited partnership that will provide title insurance agency and real estate loan closing management services that have been found to be permissible for national banks in prior OCC letters. For the reasons set forth below, the application is approved subject to the conditions set forth below.

Proposal

The Subsidiary proposes to become a 50 percent limited partner in a limited partnership known as Premier Realty Settlement Services ("Premier"). The other 50 percent interest will be that of the general partner, Wyoming Group, Inc ("Wyoming"), which is owned by partners of the law firm of O'Malley & Harris, P.C. The Subsidiary and Wyoming will each contribute 50 percent of the initial capital. Profit and losses will be allocated and distributed equally between the Subsidiary and Wyoming.

Premier will operate pursuant to a limited partnership agreement ("Partnership Agreement"). In accordance with the Partnership Agreement, Wyoming will be responsible for the exclusive

control and management of Premier. However, the Subsidiary will have the right to prevent Premier from engaging in any activity if that activity is not a part of, or incidental to, the business of banking. Furthermore, the Subsidiary has the right to withdraw from Premier at any time.

Premier will sell title insurance and provide real estate loan closing management services. Services typically available through title insurance agencies will be provided by Premier, and will conform to the principles enunciated in Interpretive Letter No. 753, *reprinted in* [1996-1997 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 81-107 (November 4, 1996) (the "First Union Letter"). Although Premier will act as a title insurance agency, in no event will it become obligated as a title insurer.[1]

The closing management services proposed to be provided are the same as those described in Conditional Approval No. 276 (May 8, 1998). When a creditor finds it inconvenient or impossible to close a loan at its office or using its employees or when special expertise or documents are required, creditors typically engage a closing agent to conduct the closing. Often title insurance agencies perform closing services as the functions may overlap, *e.g.*, recording of mortgages and preparation of HUD-1 settlement statements. In some cases, closing services will include the disbursement of proceeds. When such closings occur, Premier will ensure that disbursement is made in compliance with the OCC's interpretive rulings regarding the origination and making of loans at banking and other than banking offices.

Premier will be licensed as a title insurance agency by the Commonwealth of Pennsylvania, and all title examiners employed by Premier will be licensed to the extent required by Pennsylvania law. Premier will have its registered office and principal place of business in Lake Ariel, Pennsylvania, where the Bank has its main office. As of the last decennial census, the population of Lake Ariel did not exceed 5000 persons.

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[1]Some of Premier's proposed activities will qualify as "settlement services" under the Real Estate Settlement Procedures Act, 12 U.S.C. § 2601 *et seq*. ("RESPA"). As such, the referral of services among the Bank, the Subsidiary and Premier are subject to the restrictions relating to "Affiliated Business Arrangements" as defined in RESPA. The Bank has represented that the Bank and Premier will comply with all applicable requirements of RESPA, including the Affiliated Business Arrangement rules. Specifically, neither the Bank nor Premier will require a consumer to purchase settlement services from Premier as a condition of obtaining a loan from the Bank, unless expressly authorized by RESPA. In addition, the Bank has represented that consumers will be provided with an Affiliated Business Arrangement notice in the circumstances required by RESPA. Premier will observe and abide by RESPA's rules regarding the payment of a thing of value within the Affiliated Business Arrangement setting. The Bank and Premier will also comply with the anti-tying restrictions found in the Bank Holding Company Act, 12 U.S.C. § 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 that are part of or incidental to the business of banking by means of an operating subsidiary. *See* 12 C.F.R. § 5.34(d)(1).[2] Further, the OCC has permitted national banks to own, either directly or indirectly through an operating subsidiary, a non-controlling interest in an enterprise. The enterprise might be a limited partnership, a corporation, or a limited liability company. In recent interpretive letters, the OCC has concluded that national banks are legally permitted to make a non-controlling investment in an enterprise, provided that four criteria or standards are met.[3] 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;

(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 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.

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[2]*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.

[3]*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 non-controlling investment in a limited partnership. Earlier OCC letters permitted national banks to make non-controlling 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).

Our precedents on non-controlling ownership have recognized that the enterprise in which the bank holds an interest must confine its activities to those that are part of, or incidental to, the business of banking.[4] Twelve U.S.C. § 92 authorizes a national bank located and doing business in a place having a population of 5000 or fewer persons to act as the agent for fire, life, or any other insurance company. Premier will be located in the place where the Bank has its main office, a town with fewer than 5000 persons.

The OCC has previously concluded that the proposed title insurance agency activities are permissible under section 92, and the loan closing management activities are part of, or incidental to, the business of banking. *See, e.g.*, Conditional Approval No. [to be published] (July 30, 1999) (title insurance agency and loan closing management activities); Corporate Decision No. 99-06 (January 29, 1999) (title insurance agency, loan closing and other loan-related activities); Interpretive Letter No. 842, *reprinted in* [1998-1999 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 81-297 (September 28, 1998) (title insurance agency and loan closing activities); and Conditional Approval No. 276 (May 8, 1998) (title insurance agency, loan closing and other loan-related services). The Bank has represented that Premier will conduct its title insurance activities in a manner consistent with section 92 and the principles set forth in the First Union Letter.

Accordingly, 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 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.[5]

The Partnership Agreement gives the Subsidiary the right to dissolve, liquidate or terminate Premier in the event that Premier ever conducts business not part of, or incidental to, the

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[4]*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).

[5]*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).

business of banking. Further, the Partnership Agreement provides that the Subsidiary has a continuing and unconditional right to withdraw from Premier at any time.

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.

The Partnership Agreement provides that the Subsidiary is not individually liable for any of the debts, obligations or losses of Premier beyond the Subsidiary's limited partnership interest. Consequently, the Bank's loss exposure for the liabilities of Premier will be limited to the Subsidiary's capital contribution to Premier.

b. Loss exposure from an accounting standpoint

The OCC has not objected to a bank utilizing the equity method of accounting in reporting an investment through an operating subsidiary on an unconsolidated basis when the ownership share or investment is between 20 and 50 percent. Under the equity method of accounting, 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.[6]

The Bank has represented that it will account for the Subsidiary's investment in Premier under the equity method of accounting. Therefore, losses by the Bank and the Subsidiary from an accounting perspective will be limited to the amount invested in Premier, and the Bank and Subsidiary will not have open-ended liability for the obligations of Premier.

Accordingly, for both legal and accounting purposes, the Bank's potential loss exposure will be limited to its investment in Premier. 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.

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[6]*See generally*, Accounting Principles Board, Op. 18 § 19 (1971) (equity method of accounting for investments in common stock). Interpretive Letter No. 692, *supra*.

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 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."[7] 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.[8]

The services are of the types routinely purchased or performed by the Bank when engaged in the business of making mortgage loans and, as proposed to be conducted by Premier, will provide a convenient and useful source of these essential services that are ancillary to extending credit secured by real estate. Conducting the services through Premier 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.

Conclusion

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

(1) Premier will engage only in activities that are part of, or incidental to, the business of banking;

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

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

[8] *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*.

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

(4) Premier 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, 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 Bank representatives.

If you have any further questions, you may contact Jason D. Redwood, Senior Attorney, at (212) 790-4010, or Nina Lipscomb, Analysis Specialist, at (212) 790-4055.

Sincerely,

/s/

Julie L. Williams
Chief Counsel