Comptroller of the Currency
Administrator of National Banks

Washington, DC 20219

Corporate Decision #97-54
July 1997

June 26, 1997

Daniel R. Stolzer
Senior Vice President & Senior Managing Counsel
KeyCorp
127 Public Square
Cleveland, Ohio 44114

Re: Application of KeyBank National Association, Cleveland, Ohio to Acquire an Operating Subsidiary which has Invested in Corporations, Limited Partnerships and a General Partnership which Engage in Leasing Activities. Application Control Number: 97-CE-08-018

Dear Mr. Stolzer:

This is in response to your letter dated May 12, 1997, supplemented by a letter dated June 5, 1997, by which KeyBank National Association ("Bank") applied pursuant to 12 C.F.R. § 5.34(e)(1)(i)(B) to acquire Leasetec Corporation ("Leasetec") and Leasetec's direct and indirect interests in various corporations, limited partnerships, and a general partnership. Leasetec and its interests engage in originating and administering leases of equipment to commercial entities. We have now completed our review and it is our opinion that this transaction is legally permissible in the manner and as described herein. Accordingly, for the reasons given below, your application is hereby approved.

BACKGROUND

The Bank proposes to purchase 80 percent of the issued and outstanding stock of Leasetec. Leasetec holds 100 percent of the voting interest in Mitel Capital Corp., StorageTek Financial Services Corporation, Technology Leasing Solutions, Inc., and Unisys Leasing Corporation (collectively the "Leasing Subsidiaries") and Leasetec Funding Corp. I, Leasetec Funding Corp. II, and Leasetec Funding Corp. III (collectively the "Funding Subsidiaries"). Leasetec also owns 19.8 percent limited partnership interests in Ascot Leasing Partners, Ltd., Brentford Leasing Partners, Ltd., Holborn Leasing Partners, Ltd., Kent Leasing Partners, Ltd., and Sutton Leasing Partners, Ltd., and a 19.5 percent limited partnership interest in Bear Peak Limited Partnership ("Bear Peak") (each a "Leasing Vehicle"). The Leasing Vehicles were organized under the laws of Colorado. After being acquired by the Bank, Leasetec will not form any additional Leasing Vehicles in which it will invest as a limited partner.

Leasetec also owns 50 percent of Juniper Hill, Inc. ("JH"), a corporation which is the sole general partner of Bear Peak. GATX Capital Corporation ("GATX") owns the other 50 percent of JH. Leasetec and GATX have entered into an Agreement Among Shareholders ("Shareholders Agreement") to govern their relations with respect to the management of JH. In accordance with this Agreement, there is an even number of directors on the JH board of directors, and Leasetec and GATX each have the right to appoint one-half of the directors. With one exception,[1] a deadlock among the directors results in no action being taken by JH.[2]

Leasetec, the Leasing Subsidiaries, and the Leasing Vehicles engage in the business of leasing personal property.[3] Leasetec established the Funding Subsidiaries to facilitate the securitization of its leasing receivables.[4] All leases entered into by Leasetec, the Leasing Subsidiaries, and the Leasing Vehicles are net leases. In addition, Leasetec acts as agent in conducting each Leasing Vehicle's leasing activities under a service agreement ("Service Agreement") with each of the Leasing Vehicles. Leasetec provides the following services to the Leasing Vehicles under these Service Agreements: locating lessees, remarketing equipment upon termination, arranging with third parties to recondition and maintain equipment, paying expenses incurred in connection with structuring lease transactions on behalf of the Leasing Vehicle, supervising delivery and installation of leased property, general administration including billing and collecting rents, arranging for storage and transportation of unleased equipment, and arranging for insurance for risk of loss with respect to the equipment.[5] Leasetec receives a monthly fee for providing these services.

DISCUSSION

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[1] If the directors are deadlocked on a vote to terminate the service agreement between Bear Peak with Leasetec, the deciding vote is to be cast by a director appointed by GATX

[2] At the time of the application, Leasetec also owned a number of foreign entities that engage in personal property leasing activities. Prior to the Bank's acquisition of Leasetec, the ownership of these foreign entities will be transferred to Leasetec Corporation International ("LSI"), a subsidiary of Leasetec. The Bank has filed an application with the Board of Governors of the Federal Reserve System to establish LSI as an "Agreement corporation" and to invest in LSI and its subsidiaries. *See* 12 U.S.C. §§ 601 - 604a; Regulation K, 12 C.F.R. § 211.

[3] National banks and their operating subsidiaries may engage in personal property leasing activities under 12 U.S.C. §§ 24(Seventh), 24(Tenth), 12 C.F.R. §§ 23, and 5.34(e)(2)(ii)(M).

[4] National banks and their operating subsidiaries may negotiate evidences of debt and borrow money under 12 U.S.C. § 24(Seventh). *See* Interpretive Letter No. 415, *reprinted in* [1988-89 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 85,640 (February 16, 1988) (leases); Interpretive Letter No. 417, *reprinted in* [1988-89 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 85,641 (February 17, 1988) (mortgage assets).

[5] National banks and their operating subsidiaries are authorized to engage in personal property leasing and activities incidental thereto under 12 U.S.C. §§ 24(Seventh), 24(Tenth), 12 C.F.R. §§ 23.3 and 5.34(e)(2)(ii)(M).

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

The Bank's application raises the issue about the authority of a national bank to hold, through an operating subsidiary organized as a corporation, a non-controlling 50 percent interest in a corporation (i.e., JH), an indirect 50% interest in the general partner of a limited partnership (i.e., Bear Peak) and non-controlling, minority interests in limited partnerships (i.e., the Leasing Vehicles) that engage in personal property leasing activities.[6] A number of recent OCC Interpretative Letters have analyzed the authority of national banks, either directly or through their subsidiaries, to own a non-controlling interest in an enterprise. *See, e.g.*, Interpretative Letter No. 697, *reprinted in* [1995-1996 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 81-013 (November 15, 1995); Interpretative Letter No. 732, *reprinted in* [1995-1996 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 81-049 (May 10, 1996). These letters each concluded that the ownership of such an interest is permissible provided four standards, drawn from OCC precedents, are satisfied.[7] 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 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 and 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.

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.

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[6] The OCC recently amended its operating subsidiary rule, 12 C.F.R. 5.34, as part of a general revision of Part 5 under the OCC's Regulation Review Program. Operating subsidiaries in which a national bank may invest include corporations, limited liability companies, or similar entities if the parent owns more than 50 percent of the voting interest. Here, the Bank will own 80 percent of Leasetec. Thus, the Bank's investment in the operating subsidiary (Leasetec) is permissible.

[7] *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.

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 . *See, e.g.*, Interpretative 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); Interpretive Letter No. 694, *reprinted in* [1995-1996 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 81-009 (December 13, 1995) (national bank permitted to take non-controlling, minority interest in a limited liability company that purchases secured home improvement loans and resells them in the secondary market); Interpretive Letter No. 711, *reprinted in* [1995-1996 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 81-026 (February 23, 1996) (national bank to take minority equity interest in mortgage banking company).

It is clear that the proposed activities of JH, Bear Peak, and the other Leasing Vehicles -- personal property leasing activities -- are permissible for national banks and their subsidiaries. *See* 12 U.S.C. § 24(Seventh) and (Tenth); 12 C.F.R. §§ 23 and 5.34(e)(2)(ii)(M); *M. and M. Leasing Corporation v. Seattle First National Bank*, 563 F. 2d 1377 (1977), *cert. denied*, 436 U.S. 956 (1978). Therefore, the first standard is satisfied.

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. *See, e.g.*, Interpretive Letter No. 711, *reprinted in* [1995-1996 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 81-026 (February 3, 1996); Interpretative Letter No. 625, *reprinted in* [1993-1994 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 83,507 (July 1, 1993). This ensures that the bank will not become involved in impermissible activities.

Leasetec and GATX each own 50 percent of JH. In accordance with the Shareholder Agreement, Leasetec and GATX each have the right to appoint one-half of the directors of JH. A majority vote of the JH board is required for major business decisions. As a result, Leasetec, in effect, has veto power with respect to major business decisions of JH. Thus, Leasetec will have the right to veto any proposed activities of JH that it considers to be impermissible for national banks. Furthermore, since JH is the sole general partner of Bear Peak, Leasetec (through JH) will also be able to veto proposed activities of Bear Peak that are impermissible for national banks.

With respect to the Leasing Vehicles, the Bank (through Leasetec) will exercise considerable control over each of the Leasing Vehicles through the Service Agreements. Under each Service Agreement, Leasetec acts as agent for the Leasing Vehicle in all matters concerning equipment owned and leased by the Leasing Vehicles. By virtue of these Service Agreements, the Bank believes Leasetec will be able to restrict the activities of the Leasing Vehicles to those permissible for national banks. Further, the Bank commits that in the event that any Leasing Vehicle in which the Bank or one of its subsidiaries is a limited partner were to engage in an activity impermissible for a national bank, the Bank would cause that Leasing Vehicle to cease such activities or divest its partnership interest as promptly as prudently practicable.

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, such as JH, for it is generally accepted that a corporation is an entity distinct from its shareholders, with its own separate rights and liabilities, provided proper corporate separateness is maintained. 1 W. Fletcher, Cyclopedia of the Law of Private Corporations § 25 (rev. perm. ed. 1990). The same is generally true when a national bank invests in a limited partnership. Under Colorado law governing limited partnerships, Leasetec will not be liable for the general liabilities of the Leasing Vehicles beyond the extent of its investment in the limited partnerships. *See* Colo. Rev. Stat. Ann. § 7-62-303 (West 1986).

National banks are not permitted to be partners in general partnerships due to the potential unlimited liability for the acts of other partners within the scope of the partnerships. *Merchants National Bank v. Wehrmann*, 202 U.S. 295 (1906). However, the OCC permits operating subsidiaries of national banks to enter into general partnerships that engage in bank-permissible activities because the corporate veil of the subsidiary corporation protects the bank from the potentially open-ended exposure associated with a direct partnership investment. Interpretative Letter No. 289, *reprinted in* [1983-1984 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 85,453 (May 15, 1984). Such is the case here, where the general partner of Bear Peak is JH, a corporation that is 50 percent owned by Leasetec, another corporation.

b. *Loss exposure from an accounting standpoint*

From an accounting standpoint, the loss exposure of the Bank will also be limited. The Bank states that its indirect interests in JH, Bear Peak, and the other Leasing Vehicles will be accounted for on the books of the Bank and Leasetec under the equity or cost methods of accounting.[8] Under either method, losses recognized by the investor will not exceed the amount of its investment (including extensions of credit or guarantees, if any) shown on the investor's books. *See generally,* Accounting Principles Board, Op. 18, ¶ 19 (1971).

Therefore, for both legal and accounting purposes, the Bank's potential loss exposure relative to the corporation and the general and limited partnerships should be limited to the amount of its investment in those entities. Since that exposure will be quantifiable and controllable, 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 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). The provision in 12 U.S.C. § 24(Seventh) relating to the purchase of stock, derived from section 16 did not authorize speculative investments in stock. 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. *See, e.g.*, Interpretative Letter No. 697, *supra*; Interpretative Letter No. 543, *reprinted in* [1990-1991 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 83,255 (February 13, 1991); Interpretative Letter No. 427, *reprinted in* [1988-1989 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 85,651 (May 9, 1988); Interpretative Letter No. 421, *reprinted in* [1988-1989 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 85,645 (March 14, 1988); Interpretative Letter No. 380, *supra*.

The Bank is currently engaged in personal property leasing activities, and will continue to actively participate in this line of business together with Leasetec, JH, and the Leasing Vehicles. JH and the Leasing Vehicles permit the Bank, through Leasetec, to participate in leasing transactions with other entities. These other entities, like GATX, can contribute expertise, experience and resources to the partnerships, thus benefitting Leasetec and the other investors. Moreover, JH and the Leasing Vehicles provide the Bank an opportunity to limit

[8] The Bank will consolidate results of Leasetec, its operating subsidiary, with parent company results in accordance with generally accepted accounting principles.

the resources it commits to any one entity and, thus, diversify its risk. These will not be passive investments for the Bank; Leasetec will continue to be very involved in the ongoing operation of these entities by virtue of the Service Agreements with the Leasing Vehicles.

For these reasons, the investments in JH, Bear Peak, and the other Leasing Vehicles are convenient and useful to the Bank in carrying out its business and are not mere passive investments. Thus, the fourth standard is satisfied.

B. General Partnership Issues

Some features of the general partnership interest in Bear Peak have already been touched upon in discussing other issues. Certain other points about the partnership should also be briefly mentioned. Since the OCC considers a general partnership to be an activity of the partner operating subsidiary, and since we reserve the right to supervise and examine operating subsidiaries under 12 C.F.R. § 5.34(d)(3), the Office requires that it have the right to supervise and examine general partnerships involving operating subsidiaries. *See, e.g.*,Interpretative Letter No. 625, *supra*; Interpretative Letter No. 381, *reprinted in* [1988-1989 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 85,605 (May 5, 1987). Counsel for the Bank has represented that the Bank will permit the OCC to supervise and examine the Bear Peak partnership.

The OCC has not required any minimum ownership level when operating subsidiaries participate in general partnerships. A search of our precedents will reveal a wide range of equity levels, including minority interests. *See, e.g.*, Letter of Vernon E. Fasbender, Director for Analysis, Southeastern District (December 6, 1990) (bank operating subsidiary to own 60 percent of partnership); Interpretative Letter No. 369, *reprinted in* [1985-1987 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 85,539 (September 25, 1986) (51 percent); Interpretative Letter No. 625, *supra* (50 percent); Interpretative Letter No. 381, *supra* (33 1/3 percent). Accordingly, the Bank's 50 percent interest in the corporation (JH) which is the general partner of Bear Peak, is permissible.

C. Branching Issues

Under the McFadden Act, any bank office that performs certain "core" banking activities, including lending money, is a branch and is subject to locational restrictions. 12 U.S.C. § 36(j). Leasing conducted by a national bank under the authority of 12 U.S.C. § 24(Seventh) is the functional equivalent of lending money. *See M&M Leasing Corp. v. Seattle First National Bank*, *supra.* As a result, the OCC has determined that section 24(Seventh) leasing must be conducted at a branch or main office location. However, the OCC also concluded that leases authorized by section 24(Tenth), *i.e.*, CEBA leases, are not equivalent to lending and therefore need not be restricted to permissible branch locations. *See* Letter from Peter Liebesman, Assistant Director, Legal Advisory Services Division (June 15, 1989) (unpublished) ("Liebesman Letter"). Here, the Bank represents that Leasetec and its

interests will engage in leasing activities authorized for national banks under section 24(Seventh) or section 24(Tenth).[9]

The locations of Leasetec and its interests will not be branches of the Bank within the meaning of section § 36(j), in either case, however. The operations of an entity in which a national bank has a non-controlling, minority interest are not ordinarily attributed to the bank for branching purposes. *See* Interpretive Letter No. 711, *supra*. Accordingly, the leasing activities of the Leasing Vehicles will not be considered activities of the Bank for branching purposes. Further, the Bank has represented that Leasetec and its majority-owned subsidiaries will not conduct section 24(Seventh) leasing in a manner which constitutes branching from locations that are not approved branches. *See* 12 C.F.R. §§ 7.1003 (defining where money is lent within the meaning of section 36(j)), 7.1004 (origination of loans at other than banking offices), and 7.1005 (credit decisions at other than banking offices); Interpretive Letter No. 634, *reprinted in* [1993-94 Transfer Binder] Fed. Banking L. Rep. ¶ 83,518 (July 23, 1993) (concluding that the office of the bank's leasing subsidiary was not a branch for the purpose of section 36).

CONCLUSION

Based upon the information and representations you have provided, and for the reasons discussed above, we conclude that the Bank may acquire Leasetec (including its interests in the Leasing and Funding Subsidiaries) and Leasetec may continue to hold non-controlling investments in a corporation, a general partnership, and limited partnerships in the manner and as described herein, subject to the following conditions:

1. Leasetec, JH, and the Leasing Vehicles (including Bear Peak) will engage only in activities that are part of, or incidental to, the business of banking;

2. the Bank, through Leasetec, will have veto power over any activities and major decisions of JH and the Leasing Vehicles that are inconsistent with condition number one, or will withdraw from JH or any of the Leasing Vehicles in the event they engage in an activity that is inconsistent with condition number one;

3. the Bank will account for the investment in JH and the Leasing Vehicles under the equity or cost methods of accounting; and

4. Leasetec, the Leasing Subsidiaries, the Funding Subsidiaries, JH, and the Leasing Vehicles will be subject to OCC supervision, regulation, and examination.

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[9] Twelve C.F.R. 23.5 requires national banks to maintain separate records to distinguish section 24(Seventh) and section 24(Tenth) leases. The Bank is not certain at this time the extent to which the leases will be section 24(Tenth) type leases.

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 and by the Bank's representatives.

If you have any questions, please contact Carolina Ledesma, Licensing Analyst, at (312) 360-8867 or Christopher Sablich, Senior Attorney, at (312) 360-8805.

Sincerely,

/s/

Julie L. Williams
Chief Counsel