Comptroller of the Currency
Administrator of National Banks

Washington, DC 20219

Corporate Decision #2000-07
June 2000

May 10, 2000

Donald W. Smith, Esquire
Kirkpatrick & Lockhart LLP
1800 Massachusetts Avenue, NW, 2nd Floor
Washington, DC 20036-1800

Re: Mellon Bank, National Association, Pittsburgh, Pennsylvania
Application to Acquire a Limited Liability Company as an Operating Subsidiary
Application Control No. 2000-NE-08-0016

Dear Mr. Smith:

This is in response to the March 23, 2000 operating subsidiary application ("Application") you submitted on behalf of Mellon Bank, National Association, Pittsburgh, Pennsylvania ("Bank"), to the Office of the Comptroller of the Currency ("OCC").

The Bank proposes to acquire as an operating subsidiary MPAM Private Equity, LLC, a limited liability company ("LLC") that serves as general partner to a limited partnership used as an investment vehicle for Bank clients. The Bank would have the sole membership interest in the LLC. Based on the information and representations concerning the LLC's activities contained in the application and subsequent telephone conversations with your office, and for the reasons discussed below, the Application is approved.

I. Background

The LLC serves as the sole general partner of MPAM 1999 Private Equity Fund, LP ("Fund"), a Delaware limited partnership that is used as an investment vehicle for Bank clients. The LLC also will be the Fund's "tax matters partner," as provided in the limited partnership agreement. The LLC contributed $1,000 to the partnership's capital and shall not be required to make any additional capital contributions. The $1,000 investment is deposited in a non-interest-bearing bank account, and the LLC does not have any beneficial interest in any other partnership property. This status will not allow the LLC, for its own account, to participate or have a financial interest in the Fund's investments or investment returns.

The Fund's goal is to achieve long-term capital appreciation, and to this end it may invest in bank-impermissible investments. The Fund intends to invest in a portfolio of three to seven "Investment Partnerships" managed by unaffiliated investment managers. These partnerships will make investments in early- and later-stage venture capital, middle-market private equity, and leveraged buyout funds.[1]

As general partner, the LLC executed an "Investment Management and Administration Agreement" on behalf of the Fund with the Bank pursuant to which the Bank acts as investment manager and administrator for the Fund.[2] The LLC delegated to the Bank substantially all of its powers and obligations to conduct the operations of the Fund. At the Fund's expense, the Bank, as investment manager, also will provide or obtain recordkeeping, accounting, tax preparation, and related services for the Fund.

The Bank also acts as placement agent for the Fund's limited partnership interests. The Bank invested, and expects to continue investing, in the Fund on behalf of clients for which the Bank acts as fiduciary.[3] The Bank will not invest in the Fund for its own account, and its indirect interest through the LLC would not provide any financial interest in the Fund. Under the agreement, the Bank will receive management, placement, performance,[4] and special redemption fees with respect to most investors' investments in the Fund.

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[1] Pending the Fund's investments in, and distribution of amounts received from, Investment Partnerships, the Fund may invest in short-term debt securities, money market instruments, and interests in one or more investment companies or funds that invest in comparable investments. The Fund also may invest in short-term investments for liquidity purposes and in order to pay the annual management fees and other fund expenses.

[2] The Bank will act through Mellon Private Asset Management, the brand name under which the Bank and its affiliates offer trust and investment products and services to private clients.

[3] Eligible investors include high net worth individuals, trusts, corporations, foundations, pension plans, and other eligible investors that qualify as "accredited investors" under SEC Regulation D and who are also "qualified purchasers" as that term is defined in the Investment Company Act. *See* Investment Company Act, § 2(a)(51)(A); 17 C.F.R. § 230.501(a). The Bank may purchase interests in the Fund on behalf of fiduciary client accounts meeting the criteria set forth above and in the subscription agreement.

[4] After an investor receives aggregate distributions equal to his capital contribution, the Bank, as investment manager, will receive a fee equal to 5% of all distributions payable to that investor in excess of his contribution (*i.e.*, the bank will share in the profits). *See* Confidential Private Placement Memorandum at 6. 12 C.F.R. § 9.15(a) provides that "[i]f the amount of a national bank's compensation for acting in a fiduciary capacity is not set or governed by applicable law, the bank may charge a reasonable fee for its services." The Bank represents that the use of a performance fee and the amounts of the fees are within accepted standards of fiduciary law. The fee will be disclosed in the governing documents, and accepted by the parties who would correspond to beneficiaries under

The Bank has not guaranteed any of the liabilities of the LLC or the Fund. The LLC's investment in the Fund will be limited to the $1,000 the LLC contributes to the Fund in order to serve as its general and tax matters partner. The Bank asserts that the limited partnership agreement limits the liability of the LLC as the general partner, and of the Bank as the investment manager, respectively.[5] The limited partnership agreement also includes comprehensive provisions for the Fund indemnifying the LLC and the Bank in both capacities.

II. Analysis

A. Applicable Law

As part of the business of banking, a national bank may exercise trust powers pursuant to 12 U.S.C. § 92a (a), which states in pertinent part:

> The Comptroller of the Currency shall be authorized and empowered to grant by special permit to national banks applying therefor, when not in contravention of State or local law, the right to act as trustee, executor, administrator, registrar of stocks and bonds, guardian of estates, assignee, receiver, . . . or in any other fiduciary capacity . . . .[6]

12 U.S.C. § 24(Seventh) provides, in relevant part:

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conventional bank fiduciary relationships.

[5] The Limited Partnership Agreement provides that (1) the general partner shall have no personal liability for the validity or sufficiency thereof or the return of any limited partner's capital contribution, and (2) the general partner and the investment manager shall not be liable, responsible, or accountable to any limited partner or the Fund for any act or failure to act on the Fund's behalf, unless that act or failure to act resulted from the general partner's or investment manager's willful misconduct, bad faith, gross negligence, or reckless disregard of its obligations and duties to the Fund. That same agreement also provides that (1) the LLC shall have none of the rights and obligations applicable to the limited partners in the Fund, including rights to allocations of income and loss and to distributions, as a result of this contribution, (2) that the LLC's contribution shall be deposited in a non-interest-bearing bank account, (3) that the LLC, as general partner, shall not have any beneficial interest in any of the Fund's other property, and (4) that the term "limited partner" shall not be construed in any way to include the LLC, as the Fund's general partner.

[6] The term "fiduciary capacity" includes acting as "trustee, executor, administrator, registrar of stocks and bonds, transfer agent, guardian, assignee, receiver, or custodian under a uniform gifts to minors act; investment adviser, if the bank receives a fee for its investment advice; any capacity in which the bank possesses investment discretion on behalf of another; or any other similar capacity that the OCC authorizes pursuant to 12 U.S.C. 92a." 12 C.F.R. § 9.2(e).

> [A national bank shall have power] [t]o exercise by its board of directors or duly authorized officers or agents, subject to law, all such incidental powers as shall be necessary to carry on the business of banking . . . .

A national bank may conduct in an operating subsidiary activities that are permissible for a national bank to engage in directly either as part of, or incidental to, the business of banking or under other statutory authority.[7] OCC regulations and precedents recognize a national bank's authority to establish or acquire an LLC as an operating subsidiary.[8] An operating subsidiary may exercise investment discretion on behalf of customers or provide investment advice for a fee if the parent national bank has prior OCC approval to exercise fiduciary powers pursuant to § 5.26.[9]

B. Discussion

The Bank may purchase the LLC as an operating subsidiary to serve as general partner of a limited partnership used as an investment vehicle for Bank clients. Operating subsidiaries of national banks may enter into general partnerships that engage in bank-permissible activities[10] where the corporate veil of the subsidiary corporation protects the bank from the potentially open-ended exposure associated with a direct partnership investment.

An operating subsidiary may be a general partner of a partnership.[11] In Interpretive Letter No. 411, the OCC stated that a national bank could establish an operating subsidiary whose sole purpose was to

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[7] *See* 12 C.F.R. § 5.34(e)(1), *reprinted in* 65 Fed. Reg. 12,905, 12,911 (March 10, 2000). The Gramm-Leach-Bliley Act ("GLBA"), 113 Stat. 1378, § 121(g)(3), acknowledges the authority of national banks to have "a subsidiary that [ ] engages solely in activities that national banks are permitted to engage in directly and are conducted subject to the same terms and conditions that govern the conduct of such activities by national banks[.]"

[8] *See* 12 C.F.R. § 5.34(e)(2), *supra*; Interpretive Letter No. 669 (October 14, 1994), *reprinted in* [1994-95 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 83,617 (bank may convert an existing operating subsidiary into an LLC that provides mortgage banking services to its customers); Interpretive Letter No. 645 (April 29, 1994), *reprinted in* [1994 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 83,554 (bank may establish an LLC to originate and service residential real estate mortgage loans).

[9] *See* 12 C.F.R. § 5.34(e)(5)(vii), *supra*.

[10] *See, e.g.*, Corporate Approval No. 243 (May 9, 1997).

[11] *See Merchants' National Bank v. Wehrmann*, 202 U.S. 295 (1906); Interpretive Letter No. 289 (May 15, 1984), *reprinted in* Fed. Banking L. Rep. (CCH) ¶ 85,453. Prior OCC partnership decisions are based on the principle that the prohibition on national banks' entry into general partnerships is based exclusively on the unlimited liability exposure of a general partner, and, therefore,

invest as a general partner in a partnership that engages in bank-permissible activities.[12] The partnership made bridge loans to finance merchant banking transactions. The OCC considered this a lending activity within national banks' express lending authority under Section 24(Seventh). The activities of the operating subsidiary were part of or incidental to the business of banking and, therefore, permissible. An operating subsidiary also may act as managing general partner of a limited partnership.[13] In Interpretive Letter No. 423, the OCC permitted a national bank to establish an operating subsidiary to invest in real estate mortgage-related assets. The OCC concluded that the bank, through its subsidiary, entered into the partnership as a means of developing and performing its lawful banking activities, and not merely as an investment.

The LLC will be engaged in activities permissible for national banks.[14] The LLC will act as investment adviser to the Fund. Acting as an investment adviser is permissible for either a bank or its operating subsidiary.[15] A national bank investment adviser may delegate investment management functions.[16] As

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is inapplicable where a bank's operating subsidiary enters into general partnership because the bank would generally be shielded from partnership liability by its subsidiary corporation.

[12] Interpretive Letter No. 411 (January 20, 1988), *reprinted in* [1988-89 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 85,635.

[13] Interpretive Letter No. 423 (April 11, 1988), *reprinted in* [1988-89 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 85,647.

[14] The Bank possesses trust powers. A national bank may exercise its trust powers by means of its operating subsidiary. *See* 12 C.F.R. § 5.34(e)(5)(vii), *supra*, and Letter from James M. Kane, District Counsel, Central District, to James J. Gregory (March 28, 1989) (Unpublished) ("Therefore, if the Bank has been granted fiduciary powers by the OCC pursuant to 12 U.S.C. § 92a, its subsidiary may exercise those powers.").

[15] *See, e.g.*, Conditional Approval No. 284 (August 14, 1998) (acting as investment adviser is a permissible activity of national banks, and may be carried on through an LLC as part of and incidental to the business of banking); *see also* 12 C.F.R. § 5.34(e)(5)(v)(I), *reprinted in* 65 Fed. Reg. 12,905, 12,912 (March 10, 2000).

[16] *See, e.g.*, Trust Interpretation No. 169 (August 5, 1988), *reprinted in* Fed. Banking L. Rep. (CCH) ¶ 84,936 (a national bank may employ an affiliate to provide services in the conduct of its fiduciary activities, provided such employment is consistent with the governing law, is in the best interest of the bank's fiduciary clients, and compliance with 12 C.F.R. part 9 is maintained); Interpretive Letter No. 850 (January 27, 1999), *reprinted in* [1998-99 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 81-307 (a national bank may enter into arrangements with a registered investment adviser for the provision of investment advice); Letter from William B. Glidden, Assistant Director, Legal Advisory Services Division (January 30, 1989) (Unpublished) (a national bank may delegate investment discretion to individuals who are not employed by the bank or a bank affiliate provided the bank directors retain responsibility for supervising the delegated authorities to the same extent the directors supervise such

noted above, the LLC, as general partner of the Fund, executed an "Investment Management and Administration Agreement" with the Bank pursuant to which the Bank currently acts as investment manager and administrator for the Fund. Thus, the general partner delegated to the Bank substantially all of its powers and obligations to manage the operations of the Fund.[17]

The LLC and the Bank will not hold investments in the Fund for themselves. The Bank holds various types of investments for its fiduciary customers pursuant to its trust powers authority. Under this proposal, the LLC would hold investments in the Fund for the limited partners. Although the Fund may make bank-impermissible investments, both the LLC and the Bank have no financial interest for their own accounts in these investments. Instead, all risks and rewards of the Fund's underlying investments are allocated to the limited partners, who are fiduciary clients of the Bank.[18] Functionally, the LLC's position as the general partner of the Fund is the same as the Bank's role in maintaining common trust funds and other pooled accounts that hold investments for its fiduciary customers.[19] The Bank may acquire the LLC as an operating subsidiary because the LLC will conduct only activities permissible for a national bank.

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delegation of authority to bank employees).

[17] Pursuant to its authority under Section 24(Seventh) and its authority to exercise fiduciary powers under 12 U.S.C. § 92a, the Bank currently engages in the offering of its services as investment adviser. The Bank's proposed advisory activities are consistent with that business. Conducting this activity through the LLC will allow more of the Bank's investment management clients to participate in private equity investments at lower investment levels and thus, will enhance the Bank's ability to offer its investment management services more efficiently and capably, and in a format employed by nonbank competitors.

[18] Interests in the limited partnership will be offered for sale to fiduciary accounts for which the bank has investment discretion. The Bank serves as the investment manager and placement agent for the limited partnership and receives various initial and continuing fees for its services from the partnership. The Bank's simultaneous roles as a fiduciary for discretionary accounts and investment manager and placement agent for the limited partnership create an interest that might affect the exercise of the best judgment of the Bank in making investment decisions for its discretionary fiduciary accounts. The Bank may not make investments for its discretionary fiduciary accounts in the limited partnership unless applicable law specifically authorizes such investment. *See* 12 C.F.R. §§ 9.12(a)(1) and 9.2(b). The Bank has represented that it will comply with Section 9.12(a) by disclosing all aspects of the relationship and, as appropriate, acquiring the necessary consent of applicable parties prior to purchasing interests in the partnership for its discretionary fiduciary accounts.

[19] The Fund will be analogous to the operation by a bank of a proprietary investment company. The Bank represents that to the extent that customers who have fiduciary relationships at the Bank are invested in the Fund, the arrangements will be in compliance with 12 C.F.R. Part 9. Fiduciary funds will not be commingled for the purpose of acquiring individual limited partnership interests in the Fund.

The Bank's loss exposure will be limited, and it will not have open-ended liability for the obligations of the LLC. Investors in an LLC generally will not incur liability with respect to the liabilities or obligations of the LLC.[20] Even if the LLC were found to be liable for acts or omissions in connection with its service as the Fund's general partner and such liability were not indemnifiable, the statute pursuant to which the LLC was formed expressly provides that "no member or manager of a limited liability company shall be obligated personally for any . . . debt, obligation or liability of the limited liability company[, whether arising in contract, tort or otherwise,] solely by reason of being a member or acting as a manager of the limited liability company."[21] Thus, the corporate veil of the subsidiary LLC protects the Bank from open-ended exposure.

Furthermore, the Bank has not, directly or indirectly, invested any assets for its own account in the Fund, nor guaranteed any of the liabilities of the LLC or the Fund. The LLC's investment in the Fund will be limited to the $1,000 the LLC contributes to the Fund in order to serve as its general and tax matters partner. The limited partnership agreement limits the liability of the LLC as the general partner, and of the Bank as the investment manager, respectively.[22] The limited partnership agreement includes comprehensive provisions for indemnifying both the general partner and the investment manager. Thus, the liabilities of both the Bank and the LLC are limited with respect to the limited partnership.

III. Conclusion

Based upon the information and representations you have provided, and for the reasons discussed above, we conclude that the Bank may purchase the LLC and that the Application is approved.

If you have any questions, please contact J. Christopher Jackson, Attorney, Securities and Corporate Practices Division, at (202) 874-5210.

Sincerely,

-signed-

Julie L. Williams
First Senior Deputy Comptroller and Chief Counsel

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[20] Under specified circumstances and depending upon the law of the state under which the LLC is organized, managers and managing members may be held personally liable for monetary damages if that individual's breach or failure to perform duties resulted in, for example, a violation of criminal law and either the individual is culpable to an extent or the individual derived an improper personal benefit. Otherwise, the limit of liability generally is the individual's capital contributions to the LLC.

[21] Delaware Limited Liability Company Act, 6 Del.C. § 18-303.

[22] *See supra* note 5.