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POWERS OF MINNESOTA STATE CHARTERED BANKS

A Financial Examinations Division Publication

July 2008 (Fifth Edition)

MINNESOTA DEPARTMENT OF COMMERCE

This pamphlet outlines some of the powers that are available to Minnesota state-chartered banks. The powers described are not intended to be an exhaustive list, but rather a summary of the more common items that may be of interest to community bankers.

This is not intended to be a comprehensive summary of state law, nor is it a substitute for the advice of competent legal counsel. We hope you find this information useful. Perhaps it will focus your attention on one or more opportunities you may have overlooked.

The pamphlet will be periodically updated. Your comments or suggestions are welcome.

For your convenient reference:

- *Minnesota Statutes are available on the Internet at:
<https://www.revisor.leg.state.mn.us/statutes/?view=part&start=46&close=59>*
- *Minnesota Rules are available at: <https://www.revisor.leg.state.mn.us/rules/?agency=120>*
- *Applications forms can be found on the Department of Commerce web site:
www.commerce.state.mn.us*
 - 1. Click on Licenses, Registration, Certification*
 - 2. Click on Banks, Credit Unions, Trusts from the list of industries in the left column.*
 - 3. Click on Banks for applications and other forms for conversions, mergers, relocations, etc.*

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Branch Offices

(Reference: Minn. Stat. § 47.52)

Branch offices are generally referred to as detached facilities under Minnesota law. A bank may establish a detached facility in the municipality where the main office is located, within 5,000 feet (as the crow flies) of the main office, in a municipality where there is not a main office of another bank, or in a municipality having a population of at least 10,000 people. A detached facility may be established in a community with less than 10,000 population if all the banks having a main office in that municipality consent in writing to the new detached facility. There may be alternatives to the establishment of a detached facility, however. (See “Relocation of Offices,” discussed below.)

Establishment of a detached facility in a township requires a special act of the legislature.

A detached facility may not be closer than 50 feet to another bank’s detached facility or closer than 100 feet to another bank’s main office. Distances are measured as the crow flies. This requirement does not apply if the other banks consent in writing.

A bank can operate a part-time deposit taking office at a school located within the same municipality as its main office or a detached facility. These offices must be approved by the school administration and be established in connection with student education programs.

There is no limit on the number of detached facilities that a bank may establish.

Establishment of a detached facility requires an application to the commissioner and publication of notice in a local newspaper. Prior notice publication requirements and other restrictions may be waived in the case of a failing bank.

Application forms to establish a detached facility are available via Internet at the Department’s web page.

Any bank with a main office within three miles of a proposed detached facility may object in writing to a proposal.

A bank may close a detached facility with 60 days’ prior written notice to the commissioner. Federal regulatory agencies may have different notice requirements.

Investments in branch offices are subject to the dollar limits described under the heading Investments in Bank Premises elsewhere in this discussion.

Interstate Banking

(Reference: Minn. Stat. §§ 48.90, 49.411)

A Minnesota state bank may operate a branch office in another state if the branch office is acquired by interstate merger. De novo interstate branching is not permitted.

Senior Citizen Banking Facilities

(Reference: Minn. Stat. § 47.52(d))

The 1999 banking bill added a provision which permits banks to operate part-time locations at nursing homes and senior citizen housing facilities located within the municipality where the main office or a detached facility is located. The 2000 banking bill expanded this authority—a bank with a main office or detached facility in the seven-county metropolitan area may operate part-time locations at nursing homes or senior citizen facilities anywhere in the seven-county metro area. A letter application to the commissioner is required.

Emergency Closing of Bank Offices

(Reference: Minn. Stat. § 47.0151)

In the event of an emergency, or an impending emergency, a bank's officers may decide to close or not open one or more of the bank's offices. No office shall remain closed for more than 48 hours without approval by the commissioner. Emergency is defined broadly.

The commissioner may authorize banks to close offices or relocate offices in an emergency.

Other Offices or Locations

(Reference: Minn. Stat. §§ 47.51, 48.892)

A bank may perform clerical services (broadly defined back room operations) for itself at an off-premise location. Assurances must be provided to the commissioner that these activities are subject to regulation and examination to the same extent as at the main office or detached facilities. Acquisitions of real or personal property for these locations are subject to the restrictions on investments in bank premises discussed under that heading.

A bank may establish a drive-in or walk-up facility located within 1,500 feet (as the crow flies) of the main banking house or a detached facility. No application is necessary.

An unstaffed after-hour depository drop box can be established anywhere within the municipality where the bank's main office or detached facility is located. No application is necessary.

Loan Production Offices

(Reference: Minn. Stat. § 48.15)

State banks may apply to the commissioner to establish loan production offices. The authority comes from Minn. Stat. § 48.15, subd. 2, and the Comptroller of the Currency's interpretation of 12 USC 36. A letter application to the commissioner should include a resolution by the bank's board authorizing the activity under the provisions of Minn. Stat. § 48.15, subd. 2, and the Comptroller's interpretive ruling; the location of the loan production office, proposed staffing, occupancy terms and hours of operation; a letter of assurance that all records of activities, including leases, employment records, advertising and loan application information relating to the loan production office, will be maintained at the main banking house for inspection by Commerce Department examiners. If a loan production office is proposed in another state, please submit documentation of the authority and basis on which the other state's applicable official or agency has either approved or issued a no action letter. This includes evidence that any corporate or foreign corporation laws or rules have been complied with; amendment to the bank's lending policy incorporating the specific activities authorized at any loan production office and any special considerations should the borrower or any real estate taken as collateral be located outside the bank's normal lending territory. ATMs may be installed at a loan production office.

Investments in Bank Premises

(References: Minn. Stat. § 47.10; Minn. Rules, Part 2675.2110)

The net book value of investment in land, buildings and leasehold improvements (including parking lots) is limited to 50 percent of a bank's capital stock and paid-in surplus (without commissioner approval).

Investments in property and improvements, including nonadjacent property for future expansion, may be made up to 100 percent of capital stock and surplus with the prior written consent of the commissioner. The previous limit of 75 percent was increased to 100 percent by the 2001 banking bill, effective April 30, 2001.

The absolute limit on investment in land, buildings and improvements is 100 percent of capital stock and surplus.

Acquisition of or investment in adjacent property (including property across the street, alley or public thoroughfare) which will result in total investment in land, buildings and improvements under 50 percent of capital stock and surplus does not require the approval of the commissioner.

Real property lease arrangements between a bank and its managers or owners require the prior written approval of the commissioner.

Purchases or leases of real property, personal property, improvements or equipment in excess of \$25,000 from stockholders and other insiders require the prior written approval of the commissioner.

For insider transactions under \$25,000, the bank must maintain records that demonstrate the commercial reasonableness of the transaction.

Property for Future Expansion

(References: Minn. Stat. § 47.10; Minn. Rules, Part 2675.2110)

Prior written approval by the commissioner is required for the acquisition of nonadjacent real property or improvements acquired for future expansion. The aggregate investment in premises and improvements must be less than 100 percent of capital stock and surplus.

Acquisition of adjacent property does not require prior approval if total investment in premises and improvements is under 50 percent of capital stock and surplus.

Relocation of Offices

(References: Minn. Stat. §§ 47.101, 47.56)

Relocation of a detached facility outside of a three-mile radius requires an application and approval by the commissioner, much the same as establishing a new detached facility.

Relocation of a detached facility within a three-mile radius requires a prior notice to the commissioner because it involves acquisition of nonadjacent property.

Relocation of a bank's main office requires an application to and approval by the commissioner. An application to relocate a main office a distance greater than three miles or out of the municipality will be processed using the standards applicable to a new charter application. New charters require, among other things, a finding that there is reasonable public demand for a bank and that the probable volume of business is sufficient to insure and maintain the solvency of the new bank and the solvency of existing banks in the locality without endangering the safety of those bank(s). Rather than establish a detached facility in a community with home office protection, the courts have ruled that a bank may relocate its main office to that community under the provisions of Minn. Stat. § 47.101 and designate its former main office as a detached facility.

Other Real Estate

(Reference: Minn. Stat. §§ 48.21 and 500.24; Minn. Rules, Part 2675.2170)

Minn. Rules, Part 2675.2170 sets forth the requirements for the handling of Other Real Estate by a bank. Other Real Estate (ORE) is defined as 1) real estate obtained through foreclosure or for debt previously contracted; 2) property no longer used in the banking business due to a relocation of an office; or 3) real estate acquired for future expansion when the plans to use the property have been abandoned.

While the rule requires that the other real estate obtained through foreclosure be designated as ORE at the end of the redemption period, call report instructions require it to be reported as ORE when the bank has “control” of the property. With respect to the timing of booking ORE, we recommend that banks follow the call report instructions. Please refer also to the FDIC’s Financial Institution Letter 62-2008 dated July 1, 2008.

Under the Minnesota rule, within 60 days of acquiring title to the property (after expiration of the redemption period or upon obtaining a deed in lieu of foreclosure), the bank must obtain an independent qualified appraisal. At that time, any remaining book value above the appraised value must be charged off. The appraisal must be part of the ORE file along with an attorney’s opinion or equivalent evidence of ownership. Insurance must be maintained, if necessary, and real estate taxes must be kept current. Under the Minnesota rule, the bank can hold ORE for five years without taking any further charge off. Starting with year six, the ORE balance must be charged off at 20 percent per year so that it is off the books at the end of 10 years as required by Minn. Stat. § 48.21. Under Minn. Stat. § 500.24, agricultural land can only be held for five years unless leased to the preceding former owner. In that case, the bank can hold the land for 10 years but must sell by the end of the 10 years. Reasonable attempts must be made to dispose of all ORE by sale.

Expenditures approved by the board for permanent improvements to ORE can be capitalized up to 10 percent of the appraised value and further; however, the carrying value cannot exceed the appraised value determined after acquisition of title.

Trust Powers

(Reference: Minn. Stat. § 48.36)

A bank may apply to the commissioner of commerce for permission to exercise trust powers.

Trust Offices

(Reference: Minn. Stat. §§ 48A.14 and 48A.15)

Any bank or trust company which is authorized to exercise trust powers may establish a trust representative office with limited trust activity. Establishment requires 30 days' prior notice to the commissioner.

Any trust company or bank which is authorized to exercise trust powers may establish a trust service office at any office of another bank in this state. Establishment of a trust service office requires 30 days' joint notice to the commissioner by both the provider of trust services and the host bank. Any trust business that may be conducted at the provider's principal office may be provided at a trust service office.

Lending Limits

(Reference: Minn. Stat. § 48.24; Minn. Rules, Chapter 2675)

The basic lending limit to any one borrower is 20 percent of a bank's capital stock and surplus accounts. Capital stock and surplus is narrowly defined and does not include undivided profits or capital notes and debentures. In calculating capital stock and surplus, goodwill and other intangibles carried on the asset side of the bank's balance sheet are netted out first against undivided profits and to the extent that they exceed the balance of the undivided profits account, they would reduce capital stock and surplus in calculating the lending limit.

One borrower is defined broadly and includes an individual's liability as endorser or guarantor and the liability of any majority-owned corporation or limited liability company. It also includes the liabilities of the general partners of a partnership and the liabilities of the several members of an unincorporated association. It does not include the liabilities of the limited partners in a partnership. It does include the liabilities of majority-owned/controlled subsidiaries of a corporation.

There are several exceptions to the lending limits.

An additional 25 percent of capital and surplus over and above the basic limit can be loaned to one borrower if the 25 percent is secured by U.S. Treasury or U.S. government guaranteed bonds with market value of at least 110 percent of the loan balance at inception.

An additional 25 percent of capital and surplus can be loaned if secured by first real estate mortgages on improved property in Minnesota or adjacent states where the loan to value ratio is not more than 50 percent. Multiple exempt first mortgages can be made, but the aggregate first mortgage exemptions per customer cannot exceed 25 percent of capital and surplus.

An additional 30 percent of capital and surplus may be loaned via conditional sales contracts or leases discounted and guaranteed by one person or entity.

Also, where adequate financial data is on file and based on the written certification of an officer that the bank is relying primarily on the purchaser or lessee, conditional sales contracts may be purchased subject only to the basic 20 percent of capital stock and surplus limit. Sufficient documentation is obviously important in these cases.

Loans guaranteed by various state and federal agencies are exempt from the lending limit.

Loans fully secured by own bank deposits are exempt from the lending limit.

Daily Fed funds transactions with other banks are not subject to the lending limit.

The uninsured portion of certificates of deposit issued by another bank and held as an asset of your bank must not exceed the basic 20 percent lending limit.

An additional 20 percent of capital and surplus over and above basic limit can be loaned if secured by unencumbered feeder livestock with a market value not less than 115 percent of the loan balance. See also Minn. Rules, Part 2675.0500 for additional requirements.

A bank may advance additional funds over and above the lending limit that may be necessary to avoid a loss on a loan or investment.

An additional 10 percent of capital and surplus over and above the basic lending limit may be loaned on a perfected first lien on stored grain with a market value of over 115 percent of the loan balance. A perfected assignment of a forward contract for the sale of the grain with a recognized broker within 270 days is also required, along with insurance on the grain. This provision was added by the 1999 banking bill.

The lending limit statute and related rules are complex and reference thereto is recommended. The above discussion is not intended to be all inclusive.

Loan Documentation Fee

(Reference: Minn. Stat. § 47.59, subd. 6(d))

A one-time loan administration fee not exceeding \$25 may be charged on closed-end loans where the original principal balance of the loan is \$4,320 or less. If the customer pays the loan prior to maturity, the loan administration fee is considered part of the finance charge for the purposes of calculating refunds. Refer also to Minn. Stat. § 47.59, subd. 3(f).

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Qualified Subchapter “S” Subsidiary Earnings Distribution

(Reference: Minn. Stat. § 48.09, subd. 3)

In addition to dividend distributions on prior year’s retained earnings, a qualified subchapter “S” bank may apply to the commissioner for approval of a plan and agreement for a distribution of earnings to the shareholders of the bank for payment by shareholders of estimated taxes. The plan of distribution once approved becomes automatic unless modified or rescinded by the commissioner with 90 days’ prior notice to the bank. The distributions should be periodically adjusted to correspond to changes in tax rates.

Dividends

(References: Minn. Stat. § 48.09; Minn. Rules, Part 2675.2240)

A bank may pay dividends with the written approval of the commissioner in an amount up to 100 percent of the bank’s net income for the three most recent calendar years. Dividend forms are mailed out to banks at the end of each calendar year to facilitate the approval process. The forms are available on the Commerce Department’s internet web site. Dividends meeting certain criteria are automatically approved after a 15-day waiting period.

Wild Card Statute

(Reference: Minn. Stat. § 48.15, subd. 2)

The commissioner may authorize banks organized under the laws of this state to engage in any banking activity in which banks subject to the jurisdiction of the federal government may be authorized to engage by federal legislation, ruling, or regulation.

Debt Cancellation Products

(Reference: Minn. Stat. § 48.15, subd. 2)

The Office of the Comptroller of the Currency (OCC) has taken the position that debt cancellation/suspension products are not insurance products and exempt from the state regulatory requirements associated with credit insurance products. The Commerce Department has determined that a state bank may make application under the “wild card” statute to engage in the sale of debt cancellation products. State banks selling debt cancellation products must comply with all the disclosure, consumer protection and safety and soundness requirements set forth in OCC regulation 12 CFR 37.

Leasing

(Reference: Minn. Stat. § 48.152)

A state bank may acquire and lease or participate in the acquisition and leasing of personal property. Acquisition of personal property for leasing to customers is limited to 200 percent of the bank's capital and surplus if the leases are not full payout leases.

Investments

(Reference: Minn. Stat. § 48.61)

In addition to the investments permitted under Minn. Rules, Part 2675, a bank may make the following investments:

- Up to 20 percent of capital stock and surplus in the capital stock of an agricultural credit corporation organized under the laws of this state, and entitled to discount privileges with any federal intermediate bank organized under the laws of the United States.
- Up to 5 percent of capital stock and surplus in shares of stock in small business investment companies organized under the provisions of the small business investment act.
- Up to 10 percent of capital stock and surplus in bank or bank holding company stock if the stock is (1) owned exclusively by banks or bank holding companies and (2) at least 51 percent of the voting stock is owned or controlled by bank holding companies or banks authorized to do business in the state of Minnesota.
- Up to 5 percent of capital stock and surplus in debt or equity investment in a partnership, limited liability company, corporation or project designed primarily to promote community welfare, such as rehabilitation or development of economically depressed residential, commercial, or industrial areas. Aggregate investment in all such organizations is limited to 10 percent of capital and surplus.
- Up to the greater of 10 percent of capital stock and surplus or the amount of qualifying shares in stock of the Federal Agricultural Mortgage Corporation created pursuant to the Agricultural Credit Act of 1987.
- Investments permitted as direct investments may also be purchased indirectly via mutual funds that are registered under the Federal Securities Act of 1933. Mutual funds whose portfolios contain investments subject to other limits under state law or rule are limited to 20 percent of capital stock and surplus. There is no limit on mutual funds that contain only securities that a bank

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could purchase directly without limitation. Mutual fund shares must be carried at the lower of cost or market value and adjusted to market quarterly.

- A state bank can invest in any securities authorized for national banks as of May 27, 1989, subject to the same restrictions that apply to national banks. The commissioner may authorize investments in securities that become eligible for national banks after May 27, 1989.

Subsidiaries

(Reference: Minn. Stat. § 48.61, subd. 7)

A bank may organize, acquire or invest in subsidiaries in Minnesota for the purposes of engaging in one or more of the following activities:

- Any activity (except receiving deposits and paying checks) that is permitted for state banks under state or federal law or rule unless prohibited by Minnesota law;
- Any activity that a bank clerical service corporation can engage in under Section 48.89;
- Any activity authorized for a national bank, a bank holding company, a subsidiary of a national bank or a bank holding company and approved by the commissioner.

A subsidiary is defined as a corporation of which more than 20 percent of the voting stock is owned by a bank. Subsidiaries are subject to examination and regulation the same as a bank.

For example, one Twin Cities state bank has a community development subsidiary which provides consulting services, grants and entrepreneurship classes for inner city residents starting small businesses. Another bank has a majority-owned subsidiary which owns an office building which is used as a banking office and rental property.

Subsidiary activities require an application to the commissioner.

The aggregate amount of funds invested in equity or loans to all subsidiaries of a bank is limited to 50 percent of capital stock and surplus.

The 2001 banking bill increased the amount that can be loaned to or invested in a subsidiary. The definition of subsidiary was changed to a corporation owned at least 20 percent by a bank, down from the previous 50 percent. The change enables more than one bank to invest in the same subsidiary.

Retirement and Medical Savings Accounts

(Reference: Minn. Stat. § 48.15, subd. 4)

A state bank may act as trustee or custodian of a self-employed retirement plan under the Federal Self-Employed Individual Tax Retirement Act of 1962, or a medical savings account under the Federal Health Insurance Portability and Accountability Act of 1996.

Interbank Customer Service Agreements

(Reference: Minn. Stat. § 47.78)

A state-chartered bank may contract with a national bank, federal savings association, federal credit union having its main office in this state, or a bank, savings bank, savings association or credit union established and operating under the laws of this state to render services to customers. Services include accepting and receiving deposits, honoring and paying withdrawals, issuing money orders, cashiers checks, traveler's checks or similar instruments, cashing checks or drafts, receiving loan payments, receiving or delivering cash and instruments and securities, disbursing loan proceeds by machine, and any other transactions authorized through an electronic financial terminal.

A bank may enter into this type of contract with a bank located in another state, provided that the arrangement is permissible under the laws of the other state.

The establishment of these agreements requires a prior notice filing with the commissioner.

Reverse Mortgages

(Reference: Minn. Stat. § 47.58)

A bank may make a loan to a borrower where the committed principal amount is paid to the borrower in installments over a period of years. The loan is due when the committed principal amount has been fully paid, the property sold, death of the last surviving borrower, or termination of homestead status.

Preferred Stock

(Reference: Minn. Stat § 48.055)

A bank may issue preferred stock of one or more classes with or without voting rights. Approval of the commissioner is required and the amount of preferred stock cannot exceed 50 percent of the total common stock and surplus of the bank.

Sale of Insurance and Non-Deposit Investment Products

(Reference: Minn. Stat. § 48.15)

With approval from the commissioner of commerce and proper licensure, a bank located in a town of less than 5,000 population may offer insurance products to its customers.

The federal Gramm-Leach-Bliley Act passed in late 1999 permits banks in both large and small communities to engage in insurance agency activities through a subsidiary.

With approval from the commissioner of commerce, a bank may affiliate with a securities broker-dealer for the purpose of offering non-deposit investment securities to its customers.

School Banking

(Reference: Minn. Stat. § 47.52)

A bank can operate a part-time deposit taking office at a school located within the same municipality as its main office or a detached facility. These offices must be approved by the school administration and be established in connection with student education programs.

Electronic Funds Transfer Facilities

(Reference: Minn. Stat. § 47.62)

A bank may establish and maintain one or more electronic financial terminals, or automated teller machines (ATMs). The requirement that the Department be notified prior to the establishment of an ATM was eliminated by the 2007 banking bill.

Employee Stock Ownership Plan

(Reference: Minn. Stat. § 48.605)

A state bank may grant options to purchase, sell or enter into agreements to sell shares of its capital stock to its employees.

Banks May Issue Notes and Debentures

(Reference: Minn. Stat. § 48.62)

With the approval of the commissioner of commerce, a state bank may issue and sell capital notes or debentures.

Off-Premises Data Processing/Storage Facility

(Reference: Minn. Stat. § 47.10)

A state bank may acquire real and personal property subject to Minn. Stat. § 47.10 for the purpose of establishing a data processing and storage center.

Reverse Stock Split

(Reference: Minn. Stat. § 48.056)

The 1999 banking bill added a provision which permits a bank to effect a reverse stock split by reducing the number of outstanding shares. Approval by the commissioner is required. Minority shareholders who would be eliminated in the reverse stock split who object to the transaction may apply to the district court for the appointment of appraisers to determine the value of the disputed stock. Costs of the appraisals are shared by the bank and the shareholder.

Many believe that the reverse stock split is a simpler way to eliminate minority shareholders than a phantom bank merger.

Pledging Assets

(Reference: Minn. Stat. § 48.16 and Ch. 118A)

Banks may not pledge assets except to the state, to secure public deposits, to secure bankruptcy funds, to secure borrowings, to finance real estate acquisitions, and for repurchase agreements, and to a counterparty in an interest rate swap agreement. In 1999, American Indian Tribal entities were added to the list of government entities in Chapter 118A whose deposits in excess of FDIC insurance must be covered by either surety bonds or pledged collateral.

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