BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM
WASHINGTON, D. C. 20551

ADDRESS OFFICIAL CORRESPONDENCE
TO THE BOARD

August 23, 2006

Mr. Justin McClinton
Tennessee Department of Financial Institutions
511 Union Street
Fourth Floor
Nashville City Center
Nashville, TN 37219

Dear Mr. McClinton:

This responds to your e-mail to the Federal Reserve Bank of Atlanta dated March 21, 2006, in which you request a Board staff opinion on the eligibility of "single member limited liability companies" ("SMLLCs") to maintain an account of the type described in 12 U.S.C. § 1832 ("NOW account").

Section 1832 of Title 12 of the United States Code authorizes depository institutions (as defined in that section) "to permit the owner of a deposit or account on which interest or dividends are paid to make withdrawals by negotiable or transferable instruments for the purpose of making transfers to third parties." 12 U.S.C. § 1832(a). This authorization extends, however, only to certain accounts or deposits, namely those "which consist solely of funds in which the entire beneficial interest is held by one or more individuals or by an organization which is operated primarily for religious, philanthropic, charitable, educational, political, or other similar purposes and which is not operated for profit, and with respect to deposits of public funds by an officer, employee, or agent of the United States, any State, county, municipality, or political subdivision thereof, the District of Columbia, the Commonwealth of Puerto Rico, American Samoa, Guam, any territory or possession of the United States, or any political subdivision thereof." 12 U.S.C. § 1832(b). In summary, Section 1832 authorizes depository institutions to offer interest-bearing checking accounts to individuals, certain nonprofit organizations, and domestic governmental units.

According to the National Conference of Commissioners on Uniform State Laws ("NCCUSL"), which promulgated a Uniform Limited Liability Company Act ("ULLCA") in 1994, a limited liability company "is a single business entity which provides limited liability protection for the partners, as well as providing all the owners of the business with federal partnership taxation."[1] The Tennessee Limited Liability

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[1] Cf. http://www.nccusl.org/Update/uniformact_factsheets/uniformacts-fs-ullca.asp.

Company Act was enacted in 1994, with the Tennessee Revised Limited Liability Company Act being enacted in 1995 and effective as of January 1, 2006. Tenn. Code Ann. §§ 48-201-101 et seq. (1994); Tenn. Code Ann. §§ 48-249-101 et seq. (2005).

The Board has long held that for-profit entities are prohibited by statute from maintaining NOW accounts.[2] The only business-related entities that have been permitted to maintain NOW accounts are sole proprietorships and individuals operating unincorporated businesses, "because the funds of the business are the funds of the individual and are not the funds of a separate legal entity such as a corporation or partnership. Additionally, it could prove to be burdensome to separate the funds of a sole proprietorship into those that are used for personal expenses and those that are used for business purposes."[3] Accordingly, Board staff has opined that a "one-man corporation" may not maintain a NOW account because "[e]ven though a corporation may be owned by one person, a corporate entity does not qualify as an 'individual' under the statute [12 U.S.C. § 1832(a)]."[4] Board staff similarly opined that subchapter S corporations may not maintain NOW accounts: "[a]lthough some subchapter S corporations may have only one shareholder, and thus may be taxed as a sole proprietorship, they are legally incorporated organizations under state law and have an existence independent of the individual shareholder. . . . Therefore, the mere fact that a subchapter S corporation may be in the same position as sole proprietorships with regard to taxes does not blur the clear legal distinctions between the two types of entities."[5]

Board staff believes that an SMLLC is in the same position as a "one-man corporation" or a subchapter S corporation with a single shareholder for purposes of determining NOW account eligibility. The SMLLC has a legal existence independent of its individual shareholder. It is not only possible therefore to distinguish between funds of the individual in his individual capacity and the funds of the SMLLC, but one of the purposes of establishing such an entity is to distinguish legally between the individual and the SMLLC. Accordingly, Board staff believes that unless an SMLLC is "operated

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[2] See, e.g., Board letter dated July 2, 1981: "Profit-making entities such as corporations are not permitted by statute to maintain NOW accounts. Since partnerships are regarded as separate legal entities, the Board and the other Federal agencies have long held that they should be treated in a manner similar to that accorded corporations. Consequently, partnerships organized for profit are not permitted to maintain NOW accounts." Id. at 1.

[3] Id. at 2. Recognizing that this interpretation created disparate treatment of businesses operated as sole proprietorships and businesses operated as closely-held corporations, the Board in 1981 proposed categorizing sole proprietorships as ineligible to maintain NOW accounts. Cf. Board Press Release (Apr, 14, 1981). The Board did not adopt the proposal in light of negative comments received.

[4] Board staff opinion dated April 27, 1981.

[5] Board staff opinion dated February 23, 1981.

primarily for religious, philanthropic, charitable, educational, political, or other similar purposes and . . . is not operated for profit," the SMLLC is not eligible to maintain a NOW account.

I hope this information is useful.

Sincerely,

Stephanie Martin
Associate General Counsel

c: Alaina Gimbert, Esquire
Mr. Gary Louis
Federal Reserve Bank of Atlanta