



Office of Thrift Supervision

Department of the Treasury

1700 G Street, N.W., Washington, DC 20552 • (202) 906-6000

April 14, 1997

Re: Proposed Internet Access to be Provided by

Dear []:

This responds to your letter dated January 9, 1997, in which you asked for our views regarding the authority of [] ("Savings Bank") through a newly-created wholly-owned subsidiary, [] ("Subsidiary"): (1) to offer Savings Bank customers banking services via an Internet connection to the Savings Bank's home banking system; and (2) to afford access to the Internet for non-banking purposes to customers and others living in the Savings Bank's service area. As discussed below, we conclude that the proposed activities are permissible for a Federal association to offer through a service corporation or an operating subsidiary, provided that Internet accounts for non-Savings Bank customers are provided as part of a safe and sound implementation strategy acceptable to the appropriate regional office.

Background

The Savings Bank operates in the [] area through three offices. The Savings Bank proposes to form the Subsidiary, which would provide data processing and computer services to the Savings Bank, offer electronic banking services to customers of the Savings Bank, and offer Internet access to customers of the Savings Bank and others in the Savings Bank's market area. The Subsidiary has not yet finalized its pricing arrangements for customer billing. As an Internet service provider, the Subsidiary would use state-of-the-art security, routers, encryption, and "firewalls"¹ to protect servers from unauthorized access. Incoming calls would arrive over local telephone lines to the Subsidiaries' bank of modems. Two computers would process information, service the Savings Bank's website, and provide redundancy as part of the Savings Bank's disaster recovery plan. Behind a "firewall," the Subsidiary's third computer would supply word-processing and other

¹ A firewall is a system or combination of hardware and software solutions that enforce a boundary between two or more networks.

computer needs of the Subsidiary. A T1 telecommunications line would connect the system to the Internet through the out-going routers. The Savings Bank's computers would not be part of or connected to the Subsidiary's computers.

Savings Bank customers would access their account information and perform transactions through the Subsidiary's Internet-available home page with a hyperlink² to the Savings Bank's home page. The Savings Bank's home page would display information about Savings Bank products and services (on the Subsidiaries' server), including rates on deposit accounts and certain types of credit. A hyperlink would connect the customer to a transparent out-of-state FISERV account from which the customer could access personal bank account information. FISERV is an unrelated data processing company that supplies such information over secure Internet connections to various financial institutions around the country using its own set of approved encryption and other security measures not the subject of this letter. Through the Subsidiary-to-FISERV Internet-accessible connection, customers would be able to perform various banking activities, including verifying account balances, transferring funds among accounts (including making loan payments from existing accounts), and paying bills electronically.

Savings Bank customers with Internet access to their bank account through the Subsidiary would automatically have access to other Internet sites without any computer software enhancements being made. Internet sites now number in the hundreds of thousands and enable those with access to conduct a wide range of personal business activities -- such as retail purchases, investments, and travel planning -- that complement the financial business that may be conducted at the Savings Bank's website. Savings Bank customers with their own Internet access could also access their accounts at the Savings Bank's Internet-accessible web site. The Subsidiary expects initial start-up costs of approximately \$250,000 to buy computer equipment, software, furniture, fixtures and office equipment. While the Savings Bank would need all of the subject equipment to provide their customers with Internet access to their bank accounts in the manner described, you represented that offering Internet access to persons who are not Savings Bank customers would require only setting up new accounts and no substantial computer software enhancements or additional costs. The equipment purchased for the Subsidiary would, you have advised us, enable the Subsidiary to provide Internet access to a total of approximately 500 persons.

The Savings Bank states that its feasibility study for the proposed Internet banking service showed that to help offset the initial costs of supplying Internet services to Savings Bank customers, the Savings Bank could cover part of its start-up costs by selling general Internet

² A hyperlink is an area on an Internet web page which, when selected by a computer user, transmits a command to the computer to connect the user to a specific web page, the address of which is preprogrammed in the link.

access to the Savings Bank's customers and the general public. The non-customer fees will both help defray the cost of the new technology equipment and serve as a marketing tool to introduce potential customers to the Savings Bank, all without jeopardizing service to the Savings Bank customers. Further, the Savings Bank predicts that selling Internet access to non-customers living in the Savings Bank's market area would result in some Internet customers establishing banking relationships with the Savings Bank. Eventually, the Savings Bank's Internet access capacity will be used entirely by approximately 500 banking customers. (The Subsidiary will purchase additional equipment to provide Internet access as the number of bank customers requesting such access exceeds 500. You have represented the Savings Bank will not purchase additional equipment solely for the purpose of providing Internet access to non-customers.) You have said that the Savings Bank has no intention to become a large-scale Internet access provider and will limit the scope of its non-customer Internet services as the Savings Bank customer usage increases. At no time will non-bank customers represent more than 50 percent of the Internet customers. All Internet customers will sign a user agreement that limits the provider's liability to the amount paid for such Internet access.

Discussion

Offering Bank Services on the Internet

The Savings Bank is authorized to provide the proposed banking services to customers under the OTS's home banking services regulation,³ and under the OTS's data processing services regulation.⁴

The home banking services regulation permits Federal savings associations to use any electronic technology to provide their customers with home banking services, i.e., the transfer of funds or financial information or the performance of other transactions initiated by a customer by a home computer or other specified means.⁵ Here, the Savings Bank would use an electronic technology, the Internet, to enable Savings Bank customers to access their accounts from their own computers from their homes. The Savings Bank proposes to offer existing Savings Bank customers Internet access to their accounts to obtain account information, transfer funds and conduct other banking activities. Accordingly, the proposed provision of home banking services is well within the scope of the home banking regulation.

The data processing services regulation permits Federal associations to engage, inter alia, in any permissible activity or

³ 12 C.F.R. § 545.142 (1996).

⁴ 12 C.F.R. § 545.138 (1996).

⁵ 12 C.F.R. § 545.142 (1996).

service by using data processing equipment and technology.⁶ The data to be processed under this authority must be financial, economic, or related to thrift, home financing, or the activities of depository institutions, and the Federal association must provide the data processing and transmission services primarily for itself, other depository institutions (including the parent or a subsidiary of either), and persons with whom the Federal association has established a loan or deposit relationship.⁷

Federal associations clearly may enable customers to conduct banking services, such as verifying account balances, transferring funds among accounts, and paying bills. The services in question would be provided to customers with whom the Savings Bank has a loan or deposit relationship, and the data in question, relating to accounts with the Savings Bank, would clearly be financial in nature. Accordingly, the proposed services are authorized by sections 545.138(a) and (b) of the OTS data processing regulations.

Operating subsidiaries of Federal savings associations may conduct any activity that the Federal association may conduct directly.⁸ In addition, OTS regulations provide that service corporations of Federal associations may conduct any activity that a Federal association may conduct, other than deposit-taking, on a pre-approved basis.⁹ Accordingly, the Savings Bank would be permitted to conduct the proposed activities through the Subsidiary regardless of whether the Savings Bank designates the Subsidiary as an operating subsidiary or a service corporation.

General Access to the Internet

Savings Bank Customers. The Subsidiary's provision of Internet access to the Savings Bank's customers through the Savings Bank's website also would afford customers general access to the Internet. This access would not require special software enhancement, modification, or expense. Indeed, the Subsidiary would incur additional expense if it were to try to limit the Internet access of the Savings Bank's customers to only the Savings Bank's website or other specific banking websites.

Section 545.138(c)(1) provides that "[a]s an incident" to providing data processing and transmission services under section 545.138(b), a Federal savings association may market certain by-products of the services, provided that the by-products are not designed, created, or

⁶ 12 C.F.R. § 545.138(a) (1996).

⁷ 12 C.F.R. § 545.138(a), (b) (1996).

⁸ 61 Fed. Reg. 66572 (Dec. 18, 1996), to be codified at 12 C.F.R. § 559.3(e)(1).

⁹ 61 Fed. Reg. 66,572 and 66,575 (Dec. 18, 1996), to be codified at 12 C.F.R. §§ 559.3(e)(2), and 559.4(a), respectively. The OTS has permitted service corporations of Federal associations to accept deposits on a case-by-case basis.

substantially enhanced for marketing purposes. In this case, access to the World Wide Web is inseparable from the access to the Savings Bank that the Subsidiary will provide to the Savings Bank's customers. Access to the Savings Bank is not enhanced by virtue of general Internet access, and the Subsidiary would bear additional expense if it were to try to sever access to the Savings Bank from access to other websites. In our view, therefore, general access to the Internet is a by-product of the Savings Bank access provided by the Subsidiary and may appropriately be marketed under section 545.138(c)(1).

Additionally, providing general access to the Internet as part of providing access to a savings association's customers' bank accounts would be within a thrift's "incidental powers," as this agency has defined that term in previous opinions.¹⁰ Enabling customers to check balances and pay bills while also, and at no additional expense to the Savings Bank or the Subsidiary, providing those customers with access to other data transmission services such as the Internet, complements the Savings Bank's functions. Because, with broad Internet access, customers may conduct personal business in addition to their business with the Savings Bank, such access will widen the Savings Bank's role as a financial intermediary. Providing such access also will enable the Savings Bank to compete more effectively in the modern economy, particularly given the increased role of the Internet in the economy. Finally, the effect of providing Internet access is to place the Savings Bank in an electronic stream of commerce that is the functional equivalent of a decision to place a physical branch in a commercial area. Thus, providing Internet access is substantially identical to the permissible decisions that a Federal savings bank may make about where to conduct its business.

Accordingly, it is our view that the Savings Bank may provide general access to the Internet to customers with whom the Savings Bank has a loan or deposit relationship. In addition, for the reasons discussed in the case of Internet banking services, given that the Savings Bank may conduct the proposed activity itself, it may conduct the activity through the Subsidiary regardless of whether it classifies the Subsidiary as an operating subsidiary or a service corporation.

Non-Savings Bank Customers. Section 545.133(c)(2) permits a Federal savings association to market the excess capacity of its data processing facilities provided that the involvement (1) is limited to furnishing access to its facilities and providing the necessary operating personnel, and (2) the association has not artificially created excess capacity by acquiring equipment or facilities with substantially greater capacity than that necessary to accommodate its present or expected future needs for providing permissible data processing services.

¹⁰ See, Op. Chief Counsel (OTS) (Oct. 17, 1994); Op. Chief Counsel (OTS) (Mar. 25, 1994).

Our discussion with the Savings Bank indicates that the Subsidiary plans to acquire an amount and type of equipment that is appropriate to launch the Internet banking access and meet the foreseeable needs of the Savings Bank's customers. The proposed equipment can support a maximum number of approximately 500 accounts for Internet access, and the Savings Bank expects the number of its customers using the Internet access will increase from approximately 250 to 500 over the next few years. Thus we believe that the Savings Bank has met the requirement of paragraph (c)(2) that it not artificially create excess capacity. The Savings Bank claims no intention to develop a major Internet access business and will restrict access to persons in its market area by offering a local access number only.¹¹

Accordingly, it is our view that the proposed type of service is legally permissible for Federal associations under Section 545.138 provided such Internet accounts for non-Savings Bank customers are provided as part of a safe and sound implementation strategy acceptable to the appropriate regional office.

Again, for the reasons discussed in the case of Internet banking services, given that the Savings Bank may conduct the proposed activity itself, it may conduct the activity through the Subsidiary regardless of whether it classifies the Subsidiary as an operating subsidiary or a service corporation.

Other Matters

Pursuant to Section 559.1(a), the OTS may limit or prohibit any subsidiary activity for supervisory, legal, or safety and soundness reasons. The circumstances of a specific thrift or subsidiary application may raise such concerns. To pursue the proposed activity, the Savings Bank must file an appropriate application or notice with the appropriate OTS Regional Office and obtain approval.

In reaching the conclusions set forth herein, we have relied upon the representations contained in your letter, supplemented by oral representations from the Savings Bank, as summarized herein. Our conclusions depend upon the accuracy and completeness of those representations. Any material change in circumstances from those described herein might require different conclusions.

¹¹ The proposal is clear that in offering Internet access to non-customers of the Savings Bank, the Subsidiary would provide only the necessary access to its computer facilities and would support its facilities with appropriate operating personnel, thus satisfying the other requirement of paragraph 545.138(c)(2).

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If you have any questions regarding this response, please contact Kevin A. Corcoran, Assistant Chief Counsel, at (202) 906-6962 or Paul D. Glenn at (202) 906-6203.

Sincerely,

/s/

Dwight C. Smith III
Deputy Chief Counsel

cc: Regional Director
Regional Counsel
[
David A. Sjogren, Corporate Activities Division]