



**Comptroller of the Currency
Administrator of National Banks**

Washington, D.C. 20219

**Conditional Approval #221
December 1996**

December 4, 1996

Gerald P. Hurst, Esquire
Associate General Counsel
NationsBank Corporation
NationsBank Corporate Center
NC1-007-20-01
Charlotte, NC 28255

Re: Bank of America National Trust and Savings Association; NationsBank, National Association; KeyBank National Association; Bank One, Columbus, National Association; Mellon Bank, N.A.; Barnett Bank, National Association; First Bank National Association; PNC Bank, National Association; Michigan National Bank; The First National Bank of Chicago; Comerica Bank - Ann Arbor, National Association; and Fleet National Bank: Notice of Intent to Establish Operating Subsidiaries Pursuant to 12 C.F.R. § 5.34 to Become a Member of a Limited Liability Company to Provide Data Processing for Home Banking and Other Electronic Financial Services.
Application Control Numbers: 96-WO-08-0011 and 96-WO-08-0014 through -0024

Dear Mr. Hurst:

This is in response to your operating subsidiary notice pursuant to 12 C.F.R. § 5.34¹ submitted on behalf of Bank of America, National Trust and Savings Association, Charter Number 13044 ("Bank of America"), NationsBank, National Association, Charter Number 14448 ("NationsBank"), KeyBank National Association, Charter Number 14761 ("KeyBank"), Bank One, Columbus, National Association, Charter Number 7621 ("Bank One"), Mellon Bank, N.A., Charter Number 6301 ("Mellon"), Barnett Bank, National Association, Charter Number 9049 ("Barnett"), First Bank National Association, Charter Number 710 ("First Bank"), PNC Bank, National Association, Charter Number 1316 ("PNC"), Michigan National Bank,

¹ The OCC recently amended its operating subsidiary rule , 12 C.F.R. 5.34, as part of general revision to Part 5 ("Rules, Policies and Procedures for Corporate Activities") under the OCC's Regulation Review Program. See 61 Fed. Reg. 60342 (November 27, 1996). However, the amended rule does not take effect until December 31, 1996. Accordingly, this application was decided under the current rule. 48 Fed. Reg. 48454 (October 19, 1983) as amended at 50 Fed. Reg. 1440 (January 11, 1985); 53 Fed. Reg. 18547 (May 24, 1988); and 55 Fed. Reg. 997 (January 11, 1990).

Charter Number 16660 (“Michigan National”), The First National Bank of Chicago, Charter Number 8 (“FNBC”), Comerica Bank - Ann Arbor, National Association, Charter Number 21527 (“Comerica”), and Fleet National Bank, Charter Number 1338 (“Fleet”) (collectively, the “Banks”) to establish new, or to engage in new activities in existing, operating subsidiaries (collectively, the “Operating Subsidiaries”). The purpose of the Banks' establishment of, or conduct of new activities within, the Operating Subsidiaries is to invest in a joint venture arrangement (the “Joint Venture”) to form a Delaware limited liability company under the name of Integriion Financial Network, L.L.C. (the “LLC”), which will provide home banking and other electronic financial services.

For the reasons discussed below, we approve, subject to certain conditions, the establishment or expansion of such operating subsidiaries by the Banks because we find that the proposed investment by the operating subsidiaries in the LLC would be permissible for national banks under 12 U.S.C. § 24(Seventh). Please note that our response is solely directed to the question stated above. At this time, we will not address how other federal and state laws and regulations will or might apply to the Banks' activities in connection with the LLC, or to the LLC's operations, nor do we address the important supervisory or consumer protection considerations that will arise when the LLC actually commences operations. The LLC is still in the planning stage with some significant operational details still undecided. The OCC will work closely with the LLC so that supervisory and consumer matters are addressed, as appropriate, as the LLC's plans and actual operations develop.

A. *Background*

The LLC essentially will act as an electronic distribution channel for financial institutions to provide electronic financial services to their customers. More specifically, the LLC will establish an electronic "gateway" through which customers of the Banks will be able to obtain home banking and other financial services from their respective financial institutions through various electronic access devices, including telephone, personal computer, interactive television, etc. After the initial introduction of these home banking and other financial services, it is contemplated that other value-oriented services (such as stock quotations) will be offered to the financial institutions' customers by third party providers through the gateway. It is contemplated that the gateway eventually will be available, for a fee, to financial institutions that are not members of the LLC.

Each of the Banks (as well as several other financial institutions)² (collectively, the "Member Financial Institutions") has entered into a subscription agreement pursuant to which the Member Financial Institutions will make equal investments of up to [\$\$] in the LLC.

² The other financial institutions include Norwest Corp., Royal Bank of Canada, ABN AMRO North America, Inc. On December 2, 1996, the Board of Governors of the Federal Reserve granted the necessary regulatory approvals under section 4(c)(8) of the Bank Holding Company Act (12 U.S.C. 1843(c)(8)) for the investments by these institutions in the Integriion system. The Royal Bank of Canada, Montreal, Canada, __ Fed. Res. Bull. __, Order of December 2, 1996. See also, 61 Fed. Reg. 54441 (October 18, 1996). Washington Mutual, Inc., which is a thrift holding company regulated by the Office of Thrift Supervision (“OTS”), has filed with OTS its notice of intent to invest in the Integriion system.

International Business Machines Corporation ("IBM"), has entered into a substantially similar subscription agreement. The investment in the LLC by the Member Financial Institutions and IBM is pursuant to a Private Placement Memorandum, dated March 20, 1996, as amended (the "Private Placement Memorandum"). The Private Placement Memorandum contemplates that each investor enter into a Limited Liability Company Agreement (the "LLC Agreement") providing for the management and operation of the LLC upon receipt of all regulatory approvals and satisfaction of certain other conditions.³

Each of the Banks contemplates that its investment in the LLC will be made through its wholly owned Operating Subsidiary. The LLC will be a Delaware limited liability company. The purpose of the Banks' Operating Subsidiaries will be to own an interest in, and to participate in the management of, the LLC.

1. Proposed Activities of the LLC

In establishing and operating an electronic distribution channel for providing electronic financial services to customers of participating financial institutions, the LLC will design, develop, license and market services to financial institutions⁴ (the "LLC Services") comprised of software⁵, transaction processing, and direct network access that together will form an electronic gateway to the Member Financial Institutions, enabling the Member Financial Institutions to offer their customers a broad array of financial services delivered under individual financial institution brand names. Members using the LLC Services will be able to provide consumers full electronic access to their accounts through various devices, including personal computers, touch-tone telephones and, ultimately, other state-of-the-art devices such as personal digital assistants, screen phones, and interactive television. The LLC will use the IBM Global Network ("IGN"), which provides users with levels of network, application and transaction security beyond that currently available on the public Internet.⁶

³ Pursuant to the Private Placement Memorandum and the LLC Agreement, the total number of Member Financial Institutions may not exceed 18. To date, 16 financial institutions (i.e., each of the Banks, as well as Norwest Corp., Washington Mutual, Inc., ABN AMRO North America, Inc., and Royal Bank of Canada) have agreed to participate.

⁴ The LLC will not itself provide any services directly to the customers of the Member Financial Institutions. Instead, the services will be provided to financial institutions. The LLC's role will be transparent to the customer and will be limited to establishing the electronic gateway through which the customers may obtain the LLC supported services from their respective Member Financial Institutions or from third parties.

⁵ The LLC will provide a variety of software. For example, it will provide Member Financial Institutions with software to be distributed to customers so the customers can access and navigate the LLC's gateway. Because of the design of the LLC's system, the browser and dialer software required to access the LLC gateway is the same type of software required to access the public Internet. The LLC will provide other software to third party service providers that will enable a provider to gain access to, and operate within, the LLC gateway.

⁶ Within the United States, electronic communications and host services will be provided by Advantis, a subsidiary of the IGN. In exchange for the LLC's agreement to certain usage commitments, IBM will grant the LLC certain exclusive domestic rights to a transaction processing platform (the "IFS Platform") that will serve as the basis for providing the LLC with transaction processing compatibility. The platform will facilitate

Initially, the LLC Services will be limited to facilitating certain banking services offered by the Member Financial Institutions to their customers. These core LLC Services will support traditional home banking and financial service activities, including remote banking and bill payment services, as well as certain customer service functions (such as check ordering, two-way customer service e-mail with the bank, and electronic statements).

Within one year, the Joint Venture intends to expand the scope of the LLC's Services to support additional home banking and financial service functions (such as on-line bill paying) through Internet protocol-style browsers (such as Netscape's Navigator), account access for inquiries and transfer, linkage to PC-based financial software (such as MECA's Managing Your Money, Microsoft's Money, and Intuit's Quicken), on-line statements, as well as enhanced customer service e-mail. Subsequent phase functions will include electronic bill presentment, interactive loan applications, and account opening services. Eventually, the LLC contemplates allowing customer access to other on-line services through the LLC's gateway. To the extent that these other on-line services are not permissible for a national bank, these on-line services would be made available through third party providers rather than by the Member Financial Institutions.⁷ The LLC also contemplates that, eventually, the LLC's gateway function will be made available to other financial institutions.

Customers will be able to access the LLC gateway in two ways. First, customers who have a separate Internet access service provider will be able to access the LLC gateway through the Internet using the home page of a participating bank. Second, customers can access the LLC gateway through a private network using a local interface gateway ("LIG") that will be furnished to the LLC by IBM.⁸ Financial institutions that subscribe to the LLC Services will also be able to use the LLC platform interface as a means of enabling their customers to access the public Internet for non-banking purposes. While the LLC will receive a modest fee

connections and compatibility between the customer's access device (e.g., a PC) and the bank's existing systems. It will consist of web servers for each participating financial institution. It will also contain certain core applications like bill payment and presentment. The Banks commit that in the agreement between the LLC and IBM, IBM will commit to preserve the confidentiality of bank customer information. The LLC Services performed for national banks directly or indirectly by the IGN or Advantis will be subject to OCC examination under 12 U.S.C. § 1867(c).

⁷ Essentially, the LLC will provide a link via its web server to the Internet home page of the third party service provider. Specifically, the LLC will modify its web server architecture to link the customer directly with the party provider's Universal Reference Locator (i.e., Internet address) ("URL"). Thus, a customer desiring third party services will merely click on an icon on the LLC menu of services and will be connected with the third party's home page. The LLC will not provide any other form of data or transaction processing service to the third parties. The Banks will ensure that the appropriate disclosures are made by the third party vendors to make it clear that the nonbanking services are being offered by the nonaffiliated third party vendors and not by the Banks, and that the Banks are not responsible for such services. In addition, the Banks contemplate that the amount of nonbanking services made available through the LLC gateway will remain relatively small in relation to the amount of banking services.

⁸ Eventually, the LLC will also enable customers to access the gateway using their own personal financial management software and third party online service providers (e.g., American On-line, Prodigy and CompuServe).

for enabling Internet access (in the form of hourly user fees and fees for the sale of browser and dialer software), the Banks assert that providing Internet access will entail little additional expense and that less than 10% of the LLC's total net income will be attributable to providing public Internet access.

2. *Structure of the LLC*

As noted above, pursuant to the subscription agreements, the Operating Subsidiaries (and IBM and the remaining Member Financial Institutions) will acquire, subject to regulatory approval, interests in the LLC. The Banks will contribute approximately [\$\$] in cash to each of their respective Operating Subsidiaries (unless the funds are currently available with respect to those Operating Subsidiaries that are already in existence). In turn, the Operating Subsidiaries will each invest the cash in the LLC. The other Member Financial Institutions and IBM also will, directly or indirectly, invest up to [\$\$] each in the LLC.

Pursuant to the Article III of the LLC Agreement, the LLC will be managed by a 13-member Board of Managers (the "Board"). The Chief Executive Officer of the LLC will be given a permanent seat on the Board, and IBM will be given a permanent right to appoint a Manager to the Board. For the first four years of operations, the remaining 11 Manager positions will be allocated as follows: (i) the nine "founding" financial institutions⁹ will each be entitled to appoint a Manager to the Board; and (ii) two Managers will be "at-large" positions, selected for two-year terms by the remaining Member Financial Institutions not otherwise represented on the Board.

After the first four years, the nine Managers will be appointed by those nine Member Financial Institutions having the largest LLC revenue contribution, and will serve a term of four years. The other two "at large" Managers will be selected by the remaining Member Financial Institutions and will serve a term of two years. The LLC Board will appoint the executive management of the LLC and will oversee and approve the activities of the LLC in accordance with parameters set forth in the LLC Agreement.

3. *Other Material Terms of the LLC Agreement*

Under the LLC Agreement, the LLC may not engage in any activity that is not a permissible activity for a national bank or an operating subsidiary thereof and will cease any activity that the OCC formally opines to be an impermissible activity. Section 2.8(b). Further, the LLC will obtain OCC approval, to the extent required, prior to the commencement of any new activity. Id. Members may withdraw from the LLC without the consent of the other Members if, *inter alia*, the Member reasonably determines that the LLC is engaged in activities that are not permissible for a national bank or an operating subsidiary thereof. Section 8.2 Under the LLC Agreement, the interests in the LLC are subject to restrictions on transferability. Basically, a Member may not transfer all or a part of its interest without the

⁹ The eight founding financial institutions include Bank of America, NationsBank, Key Bank, Bank One, Royal Bank of Canada, Barnett, FNBC, and Fleet.

prior written consent of a super majority of the Members and a majority of the members holding percentage interests. *Id.* After a Member is admitted, its mandatory additional capital contributions to the LLC cannot exceed an aggregate amount of [\$\$]. Section 4.2. Finally, the LLC Agreement acknowledges that the LLC will be subject to the examination, supervision and regulation by the OCC. Section 10.13.

B. Discussion

A national bank may engage in activities that are part of or incidental to the business of banking by means of an operating subsidiary. 12 C.F.R. § 5.34. Your letter raises the issue of the authority of a national bank to make indirectly a non-controlling investment in a limited liability company. In a variety of circumstances, the OCC has permitted national banks to own, either directly, or indirectly through an operating subsidiary, a minority interest in an enterprise.¹⁰ The enterprise might be a limited partnership, a corporation, or in more recent examples, a limited liability company. In two recent interpretive letters, the OCC concluded that national banks are legally permitted to make a minority investment in an LLC provided four criteria or standards are met. See Interpretive Letter No. 692, reprinted in [Current] Fed. Banking L. Rep. (CCH) ¶ 81,007 (November 1, 1995), and OCC Interpretive Letter No. 694, reprinted in [Current] Fed. Banking L. Rep. (CCH) ¶ 81,009 (December 13, 1995). These standards, which have been distilled from our previous decisions in the area of permissible minority investments for national banks and their subsidiaries, are: (1) The activities of the 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. (4) The investment must be convenient or useful to the bank in carrying out its business and not a mere passive investment unrelated to that bank's banking business. We conclude, as discussed below, that the proposed indirect investment by national banks in the LLC satisfies these four criteria.

1. *The activities of the enterprise in which the investment is made must be limited to activities that are part of or incidental to the business of banking*

The National Bank Act, in relevant part, provides that national banks shall have the power:

[t]o exercise ... all such incidental powers as shall be necessary to carry on the business of banking; by discounting and negotiating promissory notes, drafts, bills of exchange, and other evidences of debt; by receiving deposits; by buying and selling exchange, coin, and bullion; by loaning money on personal security; and by obtaining, issuing, and circulating notes ...

¹⁰ See, e.g., OCC Conditional Approval Letter No. 219 (July, 15, 1996). Such investments are permissible if they meet the requirements for direct minority investments by national banks.

12 U.S.C. § 24(Seventh).

The Supreme Court has held that the powers clause of 12 U.S.C. § 24(Seventh) is a broad grant of power to engage in the business of banking, including but not limited to the enumerated powers and the business of banking as a whole. See NationsBank of North Carolina, N.A. v. Variable Life Annuity Co., 115 S. Ct. 810 (1995) (“VALIC”). Judicial cases reflect three general principles used to determine whether an activity is within the scope of the “business of banking”: (1) is the activity functionally equivalent to or a logical outgrowth of a recognized banking activity; (2) would the activity respond to customer needs or otherwise benefit the bank or its customers; and (3) does the activity involve risks similar in nature to those already assumed by banks. See, e.g., Merchants’ Bank v. State Bank, 77 U.S. 604, 648 (1871) (certification of checks has grown out of the business needs of the country and involves no greater risk than a bank giving a certificate of deposit); M&M Leasing Corp. v. Seattle First Nat’l Bank, 563 F.2d 1377, 1382-83 (9th Cir. 1977), cert. denied, 436 U.S. 987 (1978) (personal property lease financing is “functionally interchangeable” with the express power to loan money on personal property); American Ins. Assoc. v. Clarke, 865 F.2d 278, 282 (D.C. Cir. 1988) (standby credits to insure municipal bonds is “functionally equivalent” to the issuance of a standby letter of credit)(“AMBAC”). Further, as established by the Supreme Court in VALIC, national banks are authorized to engage in an activity if it is incidental to the performance of the five enumerated powers in section 24(Seventh) or if it is incidental to the performance of an activity that is part of the business of banking.

In the present case, the LLC's activities will be limited to the development, licensing and marketing of services comprised of software development, data processing, and data transmission, enabling participating financial institutions to offer their customers the various services supported by the LLC through the LLC’s electronic gateway. It is contemplated that the LLC gateway will enable customers of participating financial institutions to obtain other financially related services from third party provider firms. As will be developed below, these proposed activities are part of or incidental to the business of banking.

a. Providing an Electronic Gateway to Support the Provision of Home Banking and Financial services

The LLC will offer participating financial institutions an electronic gateway by which those institutions may provide their own customers with home banking and other electronic financial services. Initially, the gateway will support traditional home banking and financial services such as remote banking and bill paying. Eventually, the gateway will be expanded to support account inquiries and transfers, electronic bill presentment and on-line loan applications. To support these underlying consumer services, the LLC gateway will provide participating institutions with transaction and information processing, communications services, and supporting software. These are permissible activities for national banks.

It is well established that a national bank may use electronic means to perform services expressly or incidentally authorized to national banks.¹¹ The OCC Interpretive Ruling setting forth this authority was recently revised, in recognition of the rapid advancement of technology, to authorize a national bank to “perform, provide, or deliver through electronic means and facilities any activity, function, product, or service that it is otherwise authorized to perform, provide, or deliver.” 61 Fed. Reg. 4849 (1996) codified at 12 C.F.R. § 7.1019.

The LLC’s information and transaction processing for participating institutions will involve banking, financial, or related economic data and, thus, is part of the business of banking. An earlier version of 12 C.F.R. § 7.1019 stated that “as part of its banking business and incidental thereto, a national bank may collect, transcribe, process, analyze, and store for itself and others, banking, financial, or related economic data.” Interpretive Ruling 7.3500, 39 Fed. Reg. 14195 (Apr. 22, 1974). Although in its 1984 revision of the ruling, the OCC deleted this statement because it believed that “specific examples [of permissible electronic activities] are inappropriate given the imprecision of terms and rapid pace of change in the data processing industry”, 49 Fed. Reg. 11157 (Mar. 26, 1984), the “analytical framework” embodied in the ruling remained the same. *Id.* There was no intent to narrow or restrict the substantive effect of the rule.¹²

Similarly, the OCC has found that, as part of the business of banking, national banks may provide for the transmission of banking, financial, or related economic data and thereby establish communication or data networks that support banking and financial transactions. In OCC Interpretive Letter No. 732, reprinted in [Current] Fed. Banking L. Rep. (CCH) ¶ 81-049 (July 1, 1996), the OCC permitted a national bank to assume a minority ownership in a company engaged in the design, development, and marketing of a network for electronic funds transfer and electronic commercial data interchange.¹³

¹¹ See OCC Interpretive Letter No. 677, reprinted in [1994-1995 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 83,625 (June 28, 1995); OCC Interpretive Letter No. 284, reprinted in [1983-1984 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶85,448 (March 26, 1984); and OCC Interpretive Letter No. 449, reprinted in [1988-1989 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 85,673 (August 23, 1988).

¹² OCC Interpretive Letter No. 677, supra. See also, OCC Interpretive Letter No. 737 (August 19, 1996) (to be published) (national bank may provide transaction and information processing services to support an electronic stored value system); OCC Interpretive Letter No. 653, reprinted in [1994-1995 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 83,601 (December 22, 1994) (national bank may act as an informational and payments interface between insurance underwriters and general insurance agents); OCC Letter No. 346, reprinted in [1985-1987] Transfer Binder] Fed. Banking Law. Rep. (CCH) ¶ 85,516 (July 31, 1985) (national banks may maintain records on commodities transactions).

¹³ See also, OCC Interpretive Letter No. 653, supra (national bank may establish a network to act as an informational and payments interface between insurance underwriters and their agents); OCC Interpretive Letter No. 516, reprinted in [1990-91 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶83,220 (July 12, 1990) (national bank may provide electronic communications channels for persons participating in securities transactions); OCC Interpretive Letter No. 513, reprinted in [1990-91 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶83,215 (June 18, 1990) (national bank may provide an electronic network for the transmission of visual, voice and data communications for other financial institutions); OCC Interpretive Letter No. 346, supra (national bank may establish an electronic gateway for financial settlement services).

Finally, the LLC will provide two types of software in connection with its gateway service. First, it will provide participating institutions with software to be distributed to customers so they can access and navigate the LLC's gateway. Second, the LLC will provide software to third party service providers that will enable a provider to gain access to, and operate within, the electronic gateway. Both are clearly incidental to the business of banking; the distribution of this software is necessary to the functioning of the LLC's gateway. A national bank can sell software where the software will enable the bank customer to receive or utilize other services from the bank such as a specialized payment service or informational services.¹⁴ In this case, the software is a necessary adjunct to the gateway service and, thus, is incidental thereto.¹⁵

b. Providing Links to Third Party Vendor Websites

The LLC plans to allow customers of participating institutions to access the Internet home pages of other on-line services through an Internet link provided on the LLC's gateway. Providing links to third party vendors' websites, in the manner proposed by the LLC, is both part of the business of banking and, under the facts of this case, incidental to the business of banking.

The linkage to third party vendors' websites is part of the business of banking because it is a use of modern technology to provide a recognized banking function: acting as a "finder." The finder function is a well recognized banking activity that includes, "without limitation, identifying potential parties, making inquiries as to interest, introducing or arranging meetings of interested parties, and otherwise bringing parties together for a transaction that the parties

¹⁴ See OCC Interpretive Letter No. 516, supra (a national bank that is providing customers with a permissible database service of information relating to financial instruments can also provide software that enables the customers to download and analyze the information) and OCC Interpretive Letter No. 419, reprinted in [1988-89 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶85,643 (February 16, 1988) (a national bank that is providing customers with a permissible electronic transactional and information service can provide software that enables customers to participate in the system).

¹⁵ The fact that the browser and dialer software provided by the LLC can also be used for other purposes, e.g., to access the public Internet, does not undercut this conclusion. The LLC's gateway system is based upon web server technology and, thus, uses "Internet-compatible" browser software. The OCC has long held that national banks have an incidental authority to provide electronic products or services that can be used for both banking and non-banking functions as part of a package of banking related products or services where the full function products or services are not an excessive amount of the total package. OCC Interpretive Letter No. 742 (August 19, 1996) (to be published) (Internet access service); OCC Interpretive Letter No. 611, reprinted in [1992-1993 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 83,449 (Nov. 23, 1992) (sale of computerized telephone "smart phone" is incidental to banking even though the phone can be used for non-banking functions). The LLC will sell the dialer and browser software to the participating institutions at cost and, thus, it clearly will be a minor and incidental portion of the entire package. See OCC Interpretive Letter No. 754 (November 6, 1996) (to be published).

themselves negotiate and consummate.” 61 Fed. Reg. 4849, 4863 (Feb. 9, 1996) (codified at 12 C.F.R. § 7.1002).¹⁶

Even though earlier OCC staff opinions sometimes characterized the finder function as an incidental powers activity,¹⁷ it is actually part of the business of banking. Prior to VALIC, the courts and the OCC frequently blurred or combined the “business of banking” and “powers incidental to the business of banking” concepts. Under the now superseded Arnold Tours test,¹⁸ all non-enumerated powers tended to be characterized as “incidental powers” even though some activities held to be incidental clearly fell within the “business of banking”, e.g., an activity that is the functional equivalent of an established power such as lending. See, e.g., M & M Leasing, 563 F.2d 1382-83. Compare, American Ins. Assoc. v. Clarke, 656 F. Supp. 404 (D.D.C.), aff’d 865 F. 2d 278 (D.C. Cir. 1988). However, in light of VALIC, it is now clear that the incidental activities are activities that are permissible for national banks not because they are part of the “business of banking”, but rather because they are “convenient” or “useful” to an activity that is part of the business of banking. In contrast, activities that are part of the business of banking are permissible without reference or connection to any other banking activity.

Clearly, the OCC has treated the finder activity as an activity that is permissible without reference to any other banking activity. OCC letters opining that the finder activity permissible have not been based upon any determination that the finder activity was somehow

¹⁶ See also, Letter from J.T. Watson, Deputy Comptroller of the Currency, February 26, 1969 (unpublished); Letter from John M. Miller, July 26, 1977 (unpublished); Letter from Paul Allan Schott, Chief Counsel, May 9, 1988 (unpublished); Letter from Elizabeth Corey, May 18, 1989 (unpublished); OCC Interpretive Letter No. 238, reprinted in [1983-1984 Transfer Binder], Fed. Banking L. Rep. (CCH) ¶ 85,402 (February 9, 1982); OCC Interpretive Letter No. 472, reprinted in [1989-1990 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 83,008 (March 2 1989); Letter from Lee Walzer, Attorney, Securities, Investments and Fiduciary Practices Division, August 24, 1992 (unpublished) and Letter from Julie L. Williams, Chief Counsel, October 2, 1996 (not yet assigned a number; to be published).

¹⁷ See e.g., Letter from Christopher Manthey, Senior Attorney, March 2, 1989 (unpublished) Letter from Elizabeth Corey May 18, 1989 (unpublished), Letter from Richard V. Fitzgerald, Director, May 29, 1979 (unpublished), Letter from Roberta Walsh Boylan, Assistant Director, October 17, 1980 (unpublished).

¹⁸ Before VALIC, the standard used to determine whether an activity was “incidental” had been developed by the First Circuit Court of Appeals in Arnold Tours, Inc. v. Camp, 472 F.2d 427 (1st Cir. 1972). In Arnold Tours, the court held that “incidental” activities must be convenient or useful to one of the activities expressly enumerated or listed in 12 U.S.C. 24(Seventh). However, the VALIC decision clearly mandates that this aspect of the Arnold Tours test be modified to accommodate VALIC’s flexible definition of the “business of banking.” VALIC requires that the test be rephrased as follows: An activity is validly “incidental” if it is convenient or useful to the “business of banking” including, but not limited to, one of the powers specifically enumerated in the National Bank Act. Thus, we must distinguish analytically between activities that are part of the “business of banking” and those that are “incidental to the business of banking.”

“necessary” to another banking activity.¹⁹ Thus, the finder activity is more accurately characterized as part of the business of banking, rather than as incidental thereto.

The means that national banks use to act as finders for their customers have evolved due to technological advancements. Where banks once performed this service for their customers via newsletters and personal contacts, they presently conduct the activity with computer technology.²⁰ The LLC will merely use another new technology: the Internet and the LLC’s web server architecture. Customers after having accessed their financial institution’s webserver will be presented a menu and can select a third party vendor’s icon appearing on screen to be linked to that vendor’s URL. By providing links to third party vendors’ websites, the LLC merely introduces two parties who may engage in a transaction. Any further negotiations will then occur between the customer and the vendor. At that point, the LLC’s role in the transaction is complete. Thus, the process of providing hypertext links in the manner proposed is acting as a finder and is a new way of conducting this aspect of the business of banking. See M&M Leasing Corp., 563 F.2d at 1382-1383.

Further, and independent of the prior analysis, the LLC’s links to third party vendors’ websites is incidental to the business of banking because it is a permissible use of the LLC’s excess capacity acquired in good faith. It is well established that a national bank, under its incidental authority, may market and sell excess electronic capacities acquired or developed by the bank in good faith for banking purposes. 12 C.F.R. § 7.1019. See also OCC Interpretive Letter No. 742, supra, and OCC Interpretive Letter No. 677, supra. Thus, a national bank, under its incidental authority, may utilize the excess capacity inherent in the electronic media it uses to communicate with its customers. Banks have been permitted to include non-banking financial information as “statement stuffers” in envelopes containing a regularly scheduled mailings to customers. See OCC Interpretive Letter No. 316, reprinted in [1985-87 Transfer Binder] Fed. Banking Rep ¶85,486 (December 28, 1984). Providing links to non-banking vendors, in the manner proposed, is the use of a new technology to provide the equivalent of including written information in bank customers mailings since customers now receive the same information through links to the third party vendors’ websites.

¹⁹ See Letter from John D. Gwin, Deputy Comptroller of the Currency, May 22 1968 (unpublished) (national bank may act as a finder for target or acquiror industrial corporations); Letter from Kenneth W. Leaf, Chief National Bank Examiner, June 8, 1973 (unpublished) (national bank may act as finder for computer programs); Letter from James M. Kane, District Counsel, October 24, 1985 (unpublished) (permitting national bank to act as a finder for insurance products) OCC Interpretive Letter No. 472, supra (national banks may provide finder services for homeowners insurance); OCC Interpretive Letter No. 653, supra (national bank may act as finder for insurance products); Letter from Julie L. Williams, Chief Counsel, October 2, 1996, supra (permitting a national bank to conduct finder activities for a variety of third party products and services).

²⁰ See 12 C.F.R. § 7.1019. See also OCC Interpretive Letter No. 346, supra (national banks may act as a finder through electronic means for commodities transactions); OCC Interpretive Letter No. 516, supra (national banks may utilize computer channels to act as a finder for securities or other financial instruments); OCC Interpretive Letter No. 611, supra (national banks may provide finder service through connecting third party vendors to their home banking platform) and OCC Interpretive Letter No. 741 (August 19, 1996) (to be published) (permitting national banks to act as a finder for automobile sales and financing through database and call center services).

A bank that has in good faith acquired excess data processing capacity sufficient for website links need not allow that capacity to go unused. The specific server configuration necessary to provide banking services in the manner proposed by the LLC will legitimately have capacity in excess of that required to provide banking services. The LLC will establish logical separate web servers for each bank configured to permit URL links and possessing sufficient random access memory (“RAM”) to tolerate varying customer banking traffic needs. Thus, this server architecture will have excess RAM sufficient for URL links to third party vendor’s websites. Execution of these links, enabling customers to access other services, will require an insignificant amount of computer resources, and will not result in the LLC incurring additional costs. Providing links to other vendors’ websites enables the LLC to benefit from the excess capacity resulting from the establishment of the banking web servers.

The LLC does not face significant additional risks by providing links to third party vendors in the manner proposed. The risks faced are similar to those associated with the permissible activities of providing banking services via electronic means generally. Acting as a finder does not pose any increased risks to the LLC since its role is limited to providing a link -- introducing the parties to the transaction. The links merely expedite users’ navigation to other vendors websites.²¹

c. Providing Internet Access

Finally, the LLC will enable participating institutions to offer their customers access to the public Internet from the LLC platform. The LLC believes that the ability to enable participating banks to offer Internet access as part of package of home financial services is critical to the successful marketing of the package supported by the LLC. For the reasons below, we agree and therefore find that the LLC’s wholesaling of Internet access to participating institutions is incidental to the business of banking.

In designing the package of consumer services to be supported by the LLC, some of the Banks and others conducted a survey in April 1996 of almost 600 consumers who either currently use or would consider using electronic financial services. This survey found that those consumers overwhelmingly demand public Internet access as part of a package of electronic financial management services. The survey, which rated consumer demand for more than 40 different services that might be included in a home financial services package, was based on a scale of 1 to 5 (with a “5” indicating that the consumer is extremely likely to use a service and a “1” indicating that the consumer is not at all likely to use the service). The consumer respondents assigned public Internet access a rating of 4.3, making it the second most important feature overall; 79.8% of the respondents rated Internet access as either a “4” or “5” in importance. Surprisingly, consumers rated public Internet access as more important than several traditional home banking functions such as account transfer and loan application functions. In light of this strong indicia of consumer demand, the LLC and participating

²¹ The LLC will conduct this activity in conformance with 12 C.F.R. § 7.1002. Further, the Banks will ensure that third parties make the disclosures mentioned in footnote 6 and that the nonbanking services made available through the LLC gateway remain relatively small in proportion to the banking transactions conducted.

Banks assert that they need to include public Internet access as part of their package of consumer services in order to successfully market that package.

The marketplace apparently agrees. To enhance marketability, many consumer products and services are now being bundled with Internet access. Newspapers, which frequently post their content on Internet home pages, are now beginning to offer free and full Internet access service to their subscribers. See Mills, Newspapers Offer Free Internet to Subscribers, Washington Post, October 16, 1996 at C12, col. 2. Similarly, the largest telecommunications companies are offering their customers reduced cost Internet access as a marketing incentive for their telephone service. See Flanagan, AT&T Invades Internet with "Free" Service, 30 ASAP 5 (May 1996); Swett, MCI Matches AT&T Free Internet Offer, Sacramento Bee, March 19, 1996 at D1. Most significantly, the firms that will compete with the LLC in providing home banking networks also offer reduced cost public Internet service as part of their package of consumer financial services. Intuit, Inc., which will be one of the LLC's most significant competitors, operates the "Quicken Financial Network" ("QFN"), an area on the World Wide Web containing information on the Quicken financial software, the financial world, and the institutions that provide on-line financial services through Intuit. Users of the Quicken financial software gain free Internet access to the portion of the Internet housing the QFN. Intuit also offers its customers the option to purchase full Internet access at a reduced fee.²²

Recently, the OCC determined that a national bank subsidiary may provide home banking services via an Internet connection to the bank's home banking system and, incidental to that service, may also provide Internet access to customers and non-bank customers in the bank's service area. OCC Interpretive Letter No. 742, supra (the "Apollo" letter). The OCC based this conclusion in part upon a finding that, under the facts of that case, providing full Internet access created a package of related services needed to satisfy consumer demand and enable the bank to successfully market its home banking services. The OCC said:

OCC precedent has established that the provision of such ancillary non-banking services is permissible as incidental to the business of banking when needed to successfully package and promote other permissible banking services.
[Citations omitted.]

Here, the full Internet access service is needed to successfully provide and market the Bank's Internet banking service. Limiting the Bank's gateway services, to block non-banking use, would create a hobbled home banking product unlikely to meet consumer demand. Customers in the midst of an

²² Intuit informs its customers that:

[Y]ou can upgrade to full Internet access for a low monthly fee. This upgrade gives you access to the World Wide Web, electronic mail, and newsgroups. ... Full Internet access through QFN is economical. Our exclusive offer for Quicken users entitles you to very low access fees.

Intuit, Quicken User's Guide: Version 5 for Windows at p. 24 (1995).

Internet session wanting to view their account information would need to end the Internet session, then connect directly to the Bank. Such a cumbersome structure would not fully meet customer needs, causing them to search for more useful banking products offered by other institutions.

OCC Interpretive Letter No. 742, supra. See also, OCC Interpretive Letter No. 611, supra, (bank selling home banking service can also provide customer access to non-banking services “to increase the customer base and the usage of the program”); OCC Interpretive Letter No. 653, reprinted in [1994-1995 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 83,601 (December 22, 1994) (national banks may offer non-banking products as part of larger product or service when necessary, convenient and useful to bank permissible activities). Cf., National Courier Ass’n v. Board of Governors, 516 F. 2d 1229, 1240 (D.C. Cir. 1975) (incidental powers of holding companies to provide specialized courier services when service necessary to obtain full benefit of data processing services).

The facts in this case are somewhat different than in the Apollo letter.²³ Nevertheless, the LLC has made a strong showing of consumer demand for an Internet access feature in the package of services supported by the LLC. There is also clear evidence that competitors of the LLC will be offering such a feature. Finally, the Internet access feature will be only a minor part of the entire package offered by the LLC (less than 10% of total net income)²⁴ and will entail little additional expense for the LLC. Under these circumstances, we find the Internet access feature to be validly incidental to the other LLC Services.

2. *The Banks must be able to prevent the LLC from engaging in activities that do not meet the foregoing standard, or be able to withdraw their investment*

This is an obvious corollary to the first standard. It is not sufficient that the LLC’s activities are permissible at the time the bank initially purchases LLC membership shares; they must also remain permissible for as long as the bank retains an ownership interest in the LLC.

²³ For example, here the LLC will not be using excess capacity to provide public Internet access.

²⁴ Full function products provided as an incidental part of a package of banking services cannot dominate the banking services being provided. See OCC Interpretive Letter No. 737, supra; OCC Interpretive Letter No. 516, supra; Letter from Michael J. O’Keefe, District Counsel, Midwestern District (July 13, 1987) (unpublished); OCC Interpretive Letter No. 345, [1986-1987 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 77,799 (July 9, 1986). The OCC has two alternative tests for determining when sale of full function products as part of a package of banking services is “incidental” to those services. The older OCC test is whether the cost of the full function product is less than 30% of the cost of the entire package. OCC Interpretive Letter No. 742, supra. As an alternative to the cost test, a recent letter adopted a test based on the percentage of “gross profits” (sales less cost of goods sold) that is derived from the sale of the hardware. OCC Interpretive Letter No. 754, supra. Specifically, this letter held that where the gross profits generated by a full function product provided in connection with a banking service do not exceed thirty percent of the total gross profits from that service, the sale of the full function product is incidental to the permitted banking service. Here, the LLC has expressed the percentage in terms of net income rather than gross profits. However, under the facts in this case, the difference between gross profits and net income is not material.

The LLC Agreement provides that the LLC will only engage in activities permissible for national banks. In addition, Members may withdraw from the LLC without the consent of the other Members if, *inter alia*, the Member reasonably determines that the LLC is engaged in activities that are not permissible for a national bank or an operating subsidiary thereof. As a result, the Banks will be able, on an ongoing basis, to prevent the LLC from engaging in new activities that may be impermissible for national banks.

3. *The Banks' loss exposure must be limited, as a legal and accounting matter, and the Banks 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 a bank's investment not expose it to unlimited liability. This is the case here. As a legal matter, investors in a Delaware LLC will not incur liability beyond their investment in the LLC because of being a member or manager of the LLC -- even if they actively participate in the management or control of the business. Del. Code Ann. Tit. 6, § 18-303(a) (1994). Additionally, the LLC Agreement does not expose the Banks to unlimited liability due to their investment in the LLC.

b. *Loss exposure from an accounting standpoint*

In assessing a bank's loss exposure as an accounting matter, the OCC has previously noted that the appropriate accounting treatment for a bank's less than 20 percent ownership share or investment in an LLC is to report it as an unconsolidated entity under the equity method or cost of accounting. Under the equity method of accounting, unless the investor has extended a loan to the entity, guaranteed any of its liabilities, or has other financial obligations, the investor's losses are generally limited to the amount of the investment shown on the investor's books.²⁵ Similarly, under the cost method of accounting, the investor records an investment at cost, dividends, or distributions from the entity are the basis for recognition of earnings, and losses recognized by the investor are limited to the extent of the investment. In sum, regardless of which accounting method is used, the investing bank's potential loss is limited to the amount of its investment. The Banks will meet this requirement.

²⁵ See generally, Accounting Principles Board, Op. No. 18 § 19 (1971). Under the equity method, the investor records the initial investment at cost and, then, adjusts the carrying amount to recognize the investor's pro rata share of subsequent earnings or losses in the LLC. When losses equal or exceed the carrying amount of the investment plus advances, the investment is reduced to zero value and no further losses need be recognized unless the investor has guaranteed obligations of the LLC or is otherwise committed to provide further financial support of the LLC. In contrast, under the cost method, the investor records the initial investment at cost and, then, adjusts the carrying amount to recognize dividends actually received. Operating losses are recognized if a series of losses or other factors indicate that a decrease in the value of the investment has occurred which is other than temporary. However, losses under the cost method are generally recognized only to the extent of the adjusted carrying amount of the investment.

4. *The investment must be convenient or 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 that is not an operating subsidiary of the bank also must 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 be a mere passive investment unrelated to that bank's business activities.

"Necessary" has been judicially construed to mean "convenient or useful." See Arnold Tours, 472 F.2d at 432. The provision in 12 U.S.C. § 24(Seventh) relating to the purchase of stock, derived from section 16 of the Glass-Steagall Act, was only intended to make it clear that section 16 did not authorize speculative investments in stock. See OCC Interpretive Letter No. 697, reprinted in [Current Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 81-102 (November 15, 1995). Therefore, a consistent thread running through our precedents concerning stock ownership is that it must be convenient or useful to the bank in conducting that bank's banking business. The investment must benefit or facilitate that business and cannot be a mere passive or speculative investment.

That requirement is met here. The LLC will be providing services to the investing Banks that will enable the Banks to offer their customers a competitive package of home banking and financial services.

C. Conclusion

On the basis of the representations specified in your notification letter and other submitted materials, the OCC finds that the Banks may operate subsidiaries that will invest in the LLC and that the notification should be and is approved subject to the following conditions:

1. the LLC may engage only in activities that are part of or incidental to the business of banking;
2. the Banks will withdraw from the LLC in the event it engages in an activity that is inconsistent with condition # 1;
3. the Banks will account for their investment in the LLC under the equity or cost method of accounting; and
4. the LLC will be subject to OCC supervision, regulation, and examination.²⁶

Please be advised that all conditions of this approval are "conditions imposed in writing by the agency in connection with the granting of any application or other request" within the

²⁶ In the future, the nature and scope of the LLC's activities might be so substantially enhanced that the methodology the OCC uses to compute the Banks' assessment will need to be adjusted to cover adequately the expense of supervising and examining the LLC.

meaning of 12 U.S.C. § 1818.

Sincerely,

/s/

Julie L. Williams
Chief Counsel