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Comptroller of the Currency  
Administrator of National Banks

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Washington, DC 20219

## **Conditional Approval #577 February 2003**

### **DECISION OF THE OFFICE OF THE COMPTROLLER OF THE CURRENCY ON THE APPLICATION TO CHARTER CHARLES SCHWAB BANK, NATIONAL ASSOCIATION, RENO, NEVADA February 4, 2003**

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#### **I. DESCRIPTION OF THE PROPOSAL**

On May 31, 2002, a group of organizers (“Organizers”) filed an application with the Office of the Comptroller of the Currency (“OCC”) to charter a new national bank. The proposed bank will be headquartered in Reno, Nevada, and will be titled Charles Schwab Bank, National Association (“bank”). The bank has applied to the Federal Deposit Insurance Corporation (“FDIC”) for deposit insurance and will apply to become a member of the Federal Reserve System. No public comments were received with respect to the application during the comment period.

The application is sponsored by The Charles Schwab Corporation (“Schwab”), San Francisco, California, an existing, publicly traded company that provides securities brokerage, banking, and investment related services to customers throughout the United States and overseas. Schwab is also a registered financial holding company under the Bank Holding Company Act of 1956, as amended. The bank will be a direct 100% owned subsidiary of Schwab. As of December 31, 2001, Schwab and its subsidiaries provided financial services to 7.8 million active accounts. Client assets under management in these accounts aggregated approximately \$846 billion. Significant subsidiaries of Schwab include Charles Schwab & Co., a securities broker-dealer with approximately 395 domestic offices in 48 states, as well as branches in the Commonwealth of Puerto Rico and the U.S. Virgin Islands; U.S. Trust Corporation, a domestic bank holding company that provides investment management, fiduciary and private banking services in 12 states; Charles Schwab Europe, a retail securities brokerage firm located in the United Kingdom; Charles Schwab Investment Management, Inc., the investment advisor for Schwab’s proprietary mutual funds; Schwab Capital markets L.P., a market maker in NASDAQ and other securities

providing trade execution services to broker-dealers and institutional clients; and CyberTrader, Inc., an electronic trading technology and brokerage firm providing services to highly active online investors. As of December 31, 2001, Schwab reported consolidated net income for the year of \$199 million, with revenues of \$4,353 million, and total stockholders equity of \$4,163 million.

The bank will be headquartered in Reno, Nevada, and the head office will have public access. No branch offices are planned at this time. However, the Organizers expect that the bank will service the vast majority of its customers by alternative delivery systems including the telephone, mail, a transactional Internet website, and other electronic means such as ATMs.

The bank will offer a full range of deposit products, including interest and non-interest bearing checking accounts, statement savings accounts, certificates of deposit, money market deposit accounts, and individual retirement accounts (IRAs). The bank will also offer retail loan products, including overdraft lines of credit, home equity lines of credit, residential mortgage loans for home purchase and refinance, and personal loans. The bank's products and services will be marketed to new customers and existing Schwab customers, who are expected to provide a strong base, consistent with the federal fair lending laws. In addition, as noted herein, the bank is also expected to target lending efforts in its Reno assessment area to low-and moderate-income neighborhoods. The bank will not make commercial or small business loans, or offer credit cards. The Schwab core strategy involves cross marketing of banking and securities products and services of the bank and its U.S. broker-dealer affiliates. The bank does not intend to register as a broker-dealer, but will work with the principal registered U.S. broker-dealer affiliates of Schwab.

Execution of this strategy will rely upon internal resources of the Schwab family of companies, as well as the services of outside service providers. Many of the customer service functions of the bank are to be provided by a newly established service company, Business Services Company ("BSC"), which will be a wholly owned subsidiary of Schwab. The organizers have committed that all of the bank's vendors, including its affiliates, will comply with its comprehensive vendor management program, which was developed in accordance with OCC guidance on managing such third-party relationships (OCC Bulletin 2001-47 (November 1, 2001)). The OCC reviewed the bank's efforts in this regard during our field investigation evaluating the application's merit, and determined that the bank's vendor management processes should be satisfactory. The OCC will further review the bank's vendor management program during our pre-opening examination.

The bank will perform some key operational functions internally while contracting with third-party service providers for the provision of other functions. Bank staff will perform business and strategic planning, marketing, investment and funds management, credit analysis of generated or purchased loans, and regulatory compliance. Many other activities will be outsourced to non-affiliated companies, such as deposit and loan processing, mortgage originations, home equity loan originations, overdraft lines of credit, ACH, ATM processing, information technology, and websites. Other functions, including customer service via phone, internal audit, and administrative support, will be integrated with Schwab affiliates.

The bank has contracted with a nationally known mortgage and home equity loan vendor (“Mortgage Vendor”) to provide mortgage services whereby the bank will book mortgage loans subject to pre-established credit criteria set by the bank. The Mortgage Vendor will handle originations, servicing, and collections. Home equity lines of credit will also be originated and serviced by the Mortgage Vendor. Mortgages will consist of conventional 30 and 15 year fixed rate, adjustable rate, and a smaller volume of shorter-term fixed rate loans. The Organizers represent that the business plan contemplates that the bank will make only prime loans. Management affirmed the bank would maintain direct control over products and services delivered through affiliated and non-affiliated third party service providers. Management provided documentation of the proposed vendor management program that includes measurable service level requirements, and the metrics that will be used to monitor performance on an ongoing basis. Management will maintain control of loan originations through establishment of Mortgage Vendor’s underwriting requirements and process monitoring. OCC Bulletin 2001-47, “Third Party Relationships,” also specifically discusses the OCC’s expectations concerning due diligence and oversight of the use of such third party provider relationships. Prior to the bank’s opening, the OCC will review the systems and controls used to oversee and manage the activities of all affiliated and non-affiliated service providers including the loan servicing arrangements and the bank will not be permitted to open until the OCC has determined that it has no supervisory objection to such systems and controls.

## II. LICENSING FACTORS

### A. Policy Considerations

Under its Corporate Activities regulations (12 C.F.R. § 5.20), the OCC considers whether the proposed bank: (A) has organizers who are aware of, and understand, national banking laws and regulations; (B) has competent management, including the board of directors, with ability and experience relevant to the types of services to be provided; (C) has capitalization that is sufficient to support the projected volume and type of business; (D) can reasonably be expected to achieve and maintain profitability; and (E) will be operated in a safe and sound manner.

In evaluating this charter proposal, the OCC performed a thorough assessment of the Organizers and the proposed business plan. This included a field investigation comprised of interviews with the Organizers and proposed officers and directors; investigation and review of affiliated Schwab’s business record; review of proposed operations; and evaluation of its proposed information system architecture and approach to security and controls. We also conducted a detailed financial and business plan analysis using regulatory and industry data and research.

#### *Organizers and Management*

The OCC concluded that the organizers and proposed management and directorate have knowledge of, and understand, national banking laws and regulations and safe and sound operations. Of the five organizers, four will serve on the board of directors. Three additional

individuals will also serve on the seven-member board<sup>1</sup>. The organizers and directors, as a group, have significant prior banking and financial experience that should serve the bank well in implementing the business plan and overseeing the operations of the bank. Each director understands the role and responsibilities of a national bank director.

The Organizers have assembled a competent management team with satisfactory experience to run the proposed operations in a safe and sound manner. The proposed President and Chief Executive Officer is Richard F. Kenny, who has over 20 years of banking experience, much of which was in executive level positions. He possesses the necessary attributes to implement the operating plan.

Satisfactory candidates have been hired for the positions of Senior Loan Officer, Chief Financial Officer, and executive officer positions for compliance, marketing, loan production, operations, and technology. The OCC reviewed the qualifications of these individuals and has no objection to them serving in their proposed positions.

### *Capital Considerations*

Proposed capital is sufficient to support the projected volume and type of business. Schwab plans to provide initial capital to the bank of at least \$275 million in cash. Based upon the bank's growth and earnings projections, the initial capitalization should ensure that the Tier 1 leverage ratio never falls below 8 percent throughout the first three years of operations. The projections also evidence risk-based capital ratios that are well in excess of the minimum regulatory requirements.<sup>2</sup> Schwab, the parent company, should have the requisite financial capacity, including access to public and private capital sources, to provide capital support to the bank if necessary.

### *Earnings Considerations*

The bank can reasonably be expected to achieve and maintain profitability. The financial projections show the bank becoming profitable in the first year using realistic growth, income, and expense assumptions. It is reasonable to expect that the proposed bank can achieve and maintain profitability in line with these projections. The Organizers supported the profit prospects of this proposal through a comprehensive business plan submitted as part of the national bank charter application. The business plan included an analysis of the competitive landscape, a marketing analysis and plan, a yield and cost analysis of the proposed assets and liabilities, and an overhead expense breakdown. Both deposit and loan growth projections appear well researched and conservative. Deposit growth projections are based on deriving the majority of deposits from the Charles Schwab customer base. Their assumptions were based on

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<sup>1</sup> The five organizers are: William L. Atwell, Richard F. Kenny, J. Scott Rhoades, Bryce R. Lensing, and Hugh E. Westermeyer. Additional directors are: Charles R. Schwab, Geoffrey J. Penney, and David R. Martin.

<sup>2</sup> See 12 C.F.R. Part 3.6

actual experience with similar Schwab products such as the “Schwab One Brokerage” account and “Schwab Access” account that both have banking related features.

The OCC concludes the proposed directors and management team, with the support of the Schwab organization, have the ability to properly monitor implementation of the proposed business plan, and make necessary strategic adjustments should they be necessary.

### *Safety and Soundness Considerations*

The OCC is satisfied that the bank can be operated in a safe and sound manner. Based upon preliminary review, the Organizers have established a good foundation of personnel, policies, and controls that will be adopted by the bank. The OCC will confirm this during the preopening examination that will be broad in scope and conducted by an interdisciplinary team. This examination will include an evaluation of the bank’s final plans to identify, monitor, and control all relevant risks, notably transaction risk stemming from the bank’s use of technology and other operational factors, credit risk, interest rate risk, liquidity risk, strategic risk, reputation risk, and compliance risk.

As part of the business plan, the proposed bank has developed a description of its information systems architecture. This includes a discussion of the technologies used and key elements for the security policies, internal controls, and audit procedures. Based upon our review of the plans, the OCC is satisfied with the plans to date, but will undertake further review during the organizational phase of the bank. Prior to receiving final charter approval, we are requiring the bank to submit the final information systems and operations architecture and the information systems risk assessment and management plan for our review and approval. The bank must also successfully undergo a comprehensive security review by an objective and qualified source. This review should demonstrate that the information system has adequate physical and logical protection against unauthorized internal and external access. The bank should adhere to current and future OCC issuances on technology risk management.<sup>3</sup> In addition, at our preopening examination, the OCC will review the bank’s Internet web pages for compliance with applicable disclosure regulations, including 12 C.F.R. § 328, to assure customers are not confused as to which products and services are being provided by the bank, and which are being provided by other Schwab affiliates or third-parties.<sup>4</sup>

The bank will also develop and implement comprehensive Bank Secrecy Act and anti-money laundering policies and procedures, including any requirements of the USA PATRIOT Act. Pursuant to one of the special preopening requirements outlined below, we will ensure that the

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<sup>3</sup>See “Internet Banking,” Comptroller’s Handbook (October 1999), “Risk Management of Outsourcing Technology,” Advisory Letter 2000-12 (August 28, 2000), “Guidelines Establishing Standards for Safeguarding Customer Information,” OCC Bulletin 2001-8 (February 15, 2001), and “Third-Party Relationships: Risk Management Principles,” OCC Bulletin 2001-47 (November 1, 2001).

<sup>4</sup> The bank represents that it will comply with all provisions of applicable law and precedent concerning the retail sale of non-deposit investment products. See also recently enacted 12 CFR 7.5010 regarding electronic activities.

bank has developed and implemented satisfactory policies, procedures, systems and controls in this area prior to its opening.

As discussed above, the bank has submitted draft plans to perform some key operational functions internally while contracting with third-party service providers for the provision of other functions. Prior to receiving final charter approval, we are requiring the bank to finalize such plans and establish acceptable policies and procedures for vendor management, including with respect to operational oversight and quality assurance. The primary outsourcing is to the Charles Schwab Corporation, its affiliates, the deposit services vendor (Deposit Vendor), and the Mortgage Vendor. We considered whether corporate governance issues exist due to the structure of the bank. We considered the level of accountability and control over risk management exerted by bank management. We also considered outsourcing and management control given the outsourcing.

We concluded through the field investigation and application analysis that the outsourcing risks are mitigated by bank and corporate management structure; strong internal audit and controls; a strong vendor management program; and carefully crafted contracts that protect the bank. We have also included conditions to our approval on the outsourcing and corporate governance issues that mitigates these risks.

The bank will draft and adopt a comprehensive privacy policy.<sup>5</sup> The Organizers represent that the bank's policy and related procedures will address the collection and use of personal information, maintenance of accurate information, information security, limited employee access to personal information, third-party disclosure restrictions, and other matters. The bank will maintain internal controls, including technological firewalls, to preclude unauthorized access to or disclosure of customer information. In addition, management will be involved in privacy policy development, and the bank is expected to develop and implement procedures, including audits, to ensure that employees and third parties understand and adhere to its stated policy. The bank will implement and maintain policies, procedures, and controls for ensuring compliance with consumer protection laws and regulations. The bank's policies and procedures also must comply with current and future guidance and regulations issued by the OCC or the FFIEC with respect to customer privacy, consumer protection, and electronic banking.<sup>6</sup>

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<sup>5</sup>The OCC has issued guidance for national banks on examples of effective practices for informing customers about bank policies for the collection and use of personal information. The guidance discusses examples of effective practices for the development of bank privacy policies and measures for ensuring adherence to those policies. *See* "Guidance to National Banks on Web Site Privacy Statements," OCC Advisory Letter 99-6, May 4, 1999 and "Privacy of Consumer Financial Information," OCC Bulletin 2001-26, (May 25, 2001). *See also* OCC Bulletin 2000-6 (Privacy of Financial Information), March 2, 2000.

<sup>6</sup>*See* OCC Bulletin 98-31 (FFIEC Guidance on Electronic Financial Services and Consumer Compliance), OCC Bulletin 98-38 (Technology Risk Management: PC Banking), and OCC Advisory Letter 99-3 (Fair Credit Reporting Act).

Finally, the Organizers represent that the bank will not indicate in any of its marketing efforts or materials that the OCC has approved or endorsed the security, functionality, or effectiveness of the bank's products or services.

### *Community Reinvestment Act (CRA) Considerations*

Under the Community Reinvestment Act ("CRA") and its implementing regulations, the OCC must take into account a proposed insured national bank's description of how it will meet its CRA objectives. (See 12 U.S.C. §§ 2902(3) and 2903(a)(2) and 12 C.F.R. § 25.29(b)). Twelve C.F.R. § 5.20(h)(5)(ii) requires an organizing group to submit a CRA statement that demonstrates its plans to achieve CRA objectives as part of its proposed operating plan. The bank has provided a business plan that includes such a description. The bank will be evaluated initially as a large bank for CRA purposes because it will be affiliated with a holding company that has total banking and thrift assets greater than \$1 billion. As a large bank, its CRA performance will be evaluated under the lending, investment and service tests set forth at 12 C.F.R. §§ 25.22 through 25.24. Because it will be evaluated as a large bank under CRA, the bank will collect and report the data required by 12 C.F.R. § 25.42.

As set forth in 12 C.F.R. § 25.41(c)(2), the bank must delineate assessment areas that "include geographies in which the bank has its main office, its branches, and its deposit-taking ATMs, as well as the surrounding geographies in which the bank has originated or purchased a substantial portion of its loans . . ." The bank's main office will be located in Reno, Nevada, and it will not have any branches or deposit-taking ATMs outside the Reno, Nevada area. As such, the bank's plan to designate the Reno, Nevada Metropolitan Statistical Area ("MSA") as the assessment area is appropriate.<sup>7</sup> The bank may also consider a strategic CRA plan within 18 months.

Overall, the bank plans to help meet the credit needs of its assessment area through lending activities, qualified investments, and retail and community development banking services. The bank recognizes that it will be a new entrant into the market and will need time to establish operations, identify community development loan and investment opportunities within its assessment area, and establish appropriate contacts. The bank also recognizes that, as a bank with a national marketing scope, it will likely be limited in the number of loans originated within its defined assessment area. Accordingly the bank plans to devise lending policies that address the needs of all geographies and income groups within its assessment area and will aggressively pursue community development lending and qualified investment opportunities in the Reno MSA.<sup>8</sup>

The bank expects that a substantial portion of loans made within its assessment area will be made within low-to-moderate income (LMI) census tracts and LMI borrowers. The bank intends to work with mortgage brokers and bankers to identify these loans. The bank will also seek to identify assessment area loans through other community outreach efforts and local marketing. In

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<sup>7</sup> The Reno MSA consists of Washoe County.

<sup>8</sup> Among other things, the bank is exploring CRA-related lending, investment, and service opportunities on Indian reservations in Washoe County.

addition, the bank will offer housing products through Fannie Mae's Homeownership for People with Disabilities and Community Home Buyer's programs. Bank management has also committed to continue exploring lending opportunities through meetings and discussions with the City of Reno Redevelopment Agency, the City of Reno Community Development Agency, the Community Services Agency, Reno Housing Authority, and other Washoe County based community organizations.

The bank will offer residential mortgage loans, home equity loans, personal loans, and overdraft lines of credit.<sup>9</sup> Since the bank will not offer commercial or small business loans, it plans to originate community development loans that benefit the Reno MSA or a broader statewide or regional area. The bank has set goals for the level of community development lending in the Reno MSA and for home purchase and refinance loans targeted to low- and moderate-income ("LMI") borrowers. The bank established goals for community lending development loans. It also provided targets for borrowers in low-and-moderate-income tracts to purchase or refinance homes in Reno. The plan also includes an acceptable goal for qualified investments. All of the goals are based on a projected level of loans and deposits and will be appropriately adjusted based on any deviations in volume from the projections. In addition, the bank may seek CRA consideration for certain home mortgage and community development loans originated outside its assessment area.<sup>10</sup>

For consideration under the investment test, the bank intends to make qualified investments that benefit the Reno MSA or the broader statewide or regional area that includes its assessment area. Such investments may include CRA-qualifying general obligation bonds and other securities of state and local housing authorities that support affordable housing projects. In addition, the bank will seek to make community development grants and may seek credit for qualified investments made by affiliates.<sup>11</sup>

The bank will operate only one office located on the south side of Reno near Meadowood Mall, which will be easily accessible and open convenient hours. In addition, the bank will offer services by telephone, by mail, and on-line banking via the Internet. For additional consideration under the service test, the bank intends to provide educational programs, much like the ones its parent company has for promoting financial literacy. The bank will also donate personal computers and provide free Internet access to appropriate organizations serving LMI communities and tribal entities. The bank may also seek credit for community development

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<sup>9</sup> The bank plans to participate in affordable housing programs such as those offered through Fannie Mae.

<sup>10</sup> Pursuant to CRA Q&A § \_\_.22(b)(2) & (3)—4 at 66 Fed. Reg. 36,633 (July 12, 2001), consideration will be given for loans to LMI individuals outside an institution's assessment area(s), provided the institution has adequately addressed the needs of borrowers within its assessment area(s).

<sup>11</sup> Pursuant to CRA Q&A §§ \_\_.12(i) & 563.12(h)-5 at 66 Fed. Reg. 36626-7 (July 12, 2001), as long as an institution has adequately addressed the community development needs of its assessment area(s), it will also receive consideration for community development activities if they benefit geographies or individuals located somewhere within the broader statewide or regional area that includes the institution's assessment area(s), even if those activities do not benefit its assessment area(s).



services provided in the broader statewide or regional area. As noted above, management has also committed to continue exploring lending opportunities through meetings and discussions with the City of Reno Redevelopment Agency, the City of Reno Community Development Agency, the Community Services Agency, Reno Housing Authority, and other Washoe County based community organizations.

Given that the bank will have national operations, while it is only required under CRA regulations to treat the Reno MSA as its assessment area, the OCC has an interest in the full scope of the bank's CRA related activities, and will be requiring the bank to provide additional information on CRA qualifying loans, investments and services provided by the bank outside of its assessment area. The bank will be required, annually, to provide the OCC with the number, type and amount of loans and investments made in LMI geographies outside its assessment area as discussed in the conditions below.

## B. Legal Considerations

### 1. Chartering authority

The OCC charters a national bank under the authority of the National Bank Act of 1864, as amended, 12 U.S.C. § 1 *et seq.*, and 12 C.F.R. § 5.20. The OCC has conducted a thorough review of this application in light of the factors set forth in these statutory and regulatory provisions and has determined that there is no impediment under applicable laws and regulations to granting preliminary charter approval.<sup>12</sup>

### 2. Authority over vendors

As discussed, the bank has indicated in its application that it will outsource to various vendors deposit and loan processing, mortgage originations, home equity loan originations, overdraft lines of credit, ACH, ATM processing, information technology, and websites. The process of subcontracting activities that the bank would otherwise perform for itself implicates the requirements of the Bank Service Company Act, 12 U.S.C. § 1861 *et seq.* ("BSCA").<sup>13</sup> In particular, 12 U.S.C. § 1867(c) states, in part, that

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<sup>12</sup> With regard to chartering a national bank, the National Bank Act requires that: articles of association and an organization certificate must be drafted and filed with the OCC, 12 U.S.C. §§ 21-23; the required amount of capital must be paid in, 12 U.S.C. § 53; certain requirements relating to directors must be satisfied, 12 U.S.C. §§ 71-73; and the OCC must be notified when these things have been accomplished, 12 U.S.C. § 26. As is typical with new charter proposals, these requirements will be satisfied after the OCC grants preliminary approval. We note that the bank also must obtain deposit insurance from the FDIC and the Federal Reserve System under the Bank Holding Company Act must approve Schwab's establishment of the bank. The bank has filed an application for deposit insurance with the FDIC, and has filed its bank holding company application with the Federal Reserve Bank of San Francisco.

<sup>13</sup> The BSCA requires that the bank notify the OCC of the existence of the service relationship within thirty days after the making of such service contract or the performance of the service, whichever occurs first. 12 U.S.C. § 1867(c)(2).

[n]otwithstanding subsection (a) of this section, whenever a bank that is regularly examined by an appropriate Federal banking agency, or any subsidiary or affiliate of such a bank that is subject to examination by that agency, causes to be performed for itself, by contract or otherwise, any services authorized under this chapter, whether on or off its premises - (1) such performance shall be subject to regulation and examination by such agency to the same extent as if such services were being performed by the bank itself on its own premises....

Pursuant to this statute, services performed for the bank by contract or otherwise, will be subject to the examination and regulation of the OCC. The bank has represented that it will notify potential vendors, in writing, of the OCC's examination and regulatory jurisdiction should they contract with the bank. Moreover, BSC, which will provide many of the customer service functions of the bank, will be required to acknowledge that the OCC has the legal authority to examine its activities under the BCSA.<sup>14</sup>

OCC Bulletin 2001-47, Third Party Relationships also specifically addresses the OCC's expectations concerning due diligence and oversight of third party vendors. Pursuant to this bulletin, the OCC expects the bank to have in place a risk management process that includes:

- Risk assessment to identify the bank's needs and requirements;
- Proper due diligence to identify and select a third-party providers;
- Written contracts that outline duties, obligations, and responsibilities of the parties involved; and,
- Effective ongoing oversight of third parties and third-party activities.

### 3. Other legal matters

There are no branching issues raised in this application. As noted above, the bank will have only one office, located in Reno, Nevada. Personnel at the offices of Charles Schwab Corporation may perform ministerial acts of providing information about deposit accounts or loans to prospective customers, and helping customers complete application forms and related documents. These activities do not cause these locations to be a branch.<sup>15</sup>

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<sup>14</sup> To the extent that elements of the services to be provided to the bank are performed by MSC or any other subsidiary of Schwab, these services will constitute activities pursuant to the BSCA. To the extent that such third-party vendors perform these services for the bank through Schwab, the third-party vendors will be subject to federal banking regulation and examination to the same extent as if such services were being performed by the bank itself. Similarly, to the extent that Schwab itself performs services for the bank, those services will be subject to regulation and examination pursuant to the BSCA.

<sup>15</sup> See Interpretive Letter No. 721, *reprinted in* [1995-1996 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 81,036 (Mar. 6, 1996); Interpretive Letter No. 691, *reprinted in* [1995-1996 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 81,006 (Sep. 25, 1995); Interpretive Letter No. 638, *reprinted in* [1993-1994 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 83,525 (Jan. 6, 1994); Interpretive Letter No. 634, *reprinted in* [1993-1994 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 83,518 (Jul. 23, 1993).

With respect to affiliate transactions, the bank has represented that all transactions with its affiliates will comply with sections 23A and 23B of the Federal Reserve Act, 12 U.S.C. §§ 371c and 371c-1.

Before permitting the bank to open the OCC also will review the policies and procedures the bank has developed to assure that they address compliance with anti-tying standards that are applicable to the bank pursuant to 12 U.S.C. § 1972.

### III. PREOPENING REQUIREMENTS AND SUPERVISORY CONDITIONS

In all cases, following review of a new bank charter application, the OCC decides whether to grant preliminary approval, preliminary conditional approval, or disapproval to the request. Preliminary approval (or preliminary conditional approval) indicates permission to proceed with the organization of the bank according to the plan set forth in the application. The organizational steps of a new national bank generally include hiring management and staff, establishing premises, purchasing computers and other equipment, selecting vendors, developing and implementing policies, procedures, and controls, and raising capital. Preliminary approval is not an assurance, however, that the OCC will grant a new national bank charter. Once the OCC grants preliminary approval to a charter proposal, the organizing group must satisfy certain procedural requirements and, in some cases, special requirements before the OCC will grant final charter approval. In addition, the OCC sometimes imposes conditions that will remain in place after the bank opens.

In response to this proposal, the OCC grants preliminary conditional approval subject to several preopening requirements and on-going conditions. These requirements and conditions supplement the procedural requirements for a new national bank referenced in the transmittal letter to the bank's spokesperson. The preopening requirements provide a framework for steps that the proposed bank must successfully complete before the OCC can render a decision on final charter approval. The on-going conditions establish certain checks and safeguards to ensure that the bank, once open, will maintain adequate capital and liquidity and operate in an overall safe and sound manner. The OCC will monitor the bank's future actions and performance through the normal supervisory process.

This preliminary conditional approval is subject to the conditions listed below:

1. The bank: (i) shall give the OCC's San Francisco Field Office at least sixty (60) days prior written notice of the bank's intent to significantly deviate or change from its business plan or operations<sup>16</sup> and (ii) shall obtain the OCC's written determination of no objection before the bank engages in any significant deviation or change from its business plan or operations. For the first three years of operation, the bank also must provide a copy of such written notice to the FDIC's San Francisco Regional Office.

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<sup>16</sup> If such deviation is the subject of an application filed with the OCC, no separate notice to the supervisory office is required.

2. Prior to opening, the bank shall engage an independent, external auditor to perform an audit according to generally accepted auditing standards of sufficient scope to enable the auditor to render an opinion on the financial statements of the bank. The audit period shall commence on the date that the organizing group forms a body corporate and may end on any calendar quarter-end no later than 12 months after the bank opens. Such audits shall be performed annually thereafter.
3. The bank shall implement an independent internal audit function that is appropriate for its size and for the scope of its activities that satisfies applicable OCC guidance on internal audit. The internal audit function must be supervised by a full time employee of the bank with sufficient expertise to identify the risks inherent in the bank's operations and to assess the effectiveness of internal controls. In addition, the bank must comply with any applicable requirements of 12 CFR 363 regarding Annual Independent Audits and Reporting Requirements.
4. The board of directors shall establish policies and procedures for contracts and transactions with affiliated companies to assure that the bank's interests are independently assessed and appropriately protected when its parent company or an affiliated company provides services to or engages in transactions with the bank. The board of directors shall thereafter periodically and at least annually review such contracts and transactions to insure that they comply with the established policies and procedures, and review such policies and procedures to ensure that they continue to provide the foregoing assurance.
5. The bank must notify all potential technology related vendors in writing of the OCC's examination and regulatory authority under 12 U.S.C. § 1867(c)<sup>17</sup>. All final vendor contracts must stipulate that the performance of services provided by the vendors to the bank is subject to the OCC's examination and regulatory authority.
6. The bank shall establish and maintain a comprehensive risk management function satisfactory to the OCC that is staffed by full time employees of the bank. The bank functions included in the risk management function should include but not be limited to internal audit, loan review, and compliance
7. The Board shall implement a program to ensure the risks and issues associated with third party outsourcing are appropriately addressed as outlined in OCC Bulletin 2001-47; Third Party Relationships. The program shall properly address credit risk, reputation risk, compliance risk and transaction risk as discussed in the guidance. This will include proper controls to make certain the contracted services do not permit third parties to implement product programs that are not under the proper control of the bank and within its business plan. The program should be updated regularly and reviewed annually by the board of directors.
8. The bank shall provide a report annually to the OCC on its lending and investment activity outside the Reno assessment area as follows:

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<sup>17</sup> The OCC has the authority to assess the bank for the cost of examining a service provider. See 12 C.F.R. § 8.6.

- It will identify the top ten metropolitan statistical areas (“MSAs”) by total number of loans and the top ten MSAs by total dollar amount of loans in which the bank has made mortgage, consumer, small business, or small farm loans. The report will provide the following data by loan type for up to twenty MSAs: A summary of the loans made in each MSA including data on the borrower income characteristics (e.g. low, moderate, middle, upper), racial characteristics (for those loan types where the bank maintains that information), and geographic income characteristics.
- It will also identify the top ten MSAs by total numbers of community development loans and qualified investments combined and identify the top ten MSAs by total dollar amount of community development loans and qualified investments<sup>18</sup> combined. The bank will provide a summary of the community development activities, (i.e., CD loans, qualified investments, and CD services) for up to twenty MSAs that includes the dollar and number of these activities, and categorizes each activity according to the definition at 12 CFR 25.12(h).

The above-listed conditions of this approval shall be deemed to be “condition[s] imposed in writing by the agency in connection with the granting of any application or other request” within the meaning of 12 U.S.C. § 1818(b)(1).

In addition to the standard requirements for all new national banks, the following special requirements must be satisfied before the OCC will grant final charter approval:

1. The bank must submit to the OCC’s San Francisco Field Office for review and prior written determination of no supervisory objection a complete description of the bank’s final information systems and operations architecture as well as the information systems risk assessment and management plan. In addition, the bank must provide the bank’s technology vendor selections, including copies of the loan and/or mortgage servicing company contract. The information should include a schematic drawing and discussion of the following items:

Vendor due diligence and contracts; electronic banking security mechanisms and policies; information systems personnel; internal controls; audit plans; and operating policies and procedures, including, but not limited to, vendor management, weblinking, customer authentication and verification, and business resumption contingency plans.

2. The bank must have performed an independent security review and test of its electronic banking platform. The bank must have this review performed regardless of whether the platform is operated in-house or by one or more third-party service providers. If the bank outsources the technology platform, it can rely on testing performed for the service provider to the extent that it satisfies the scope and requirements listed herein. The review must be conducted by an objective, qualified independent source (Reviewer). The scope should cover:

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<sup>18</sup> You may include appropriate affiliate community development loans and qualified investments in your report.

- All access points, including the Internet, Intranet, or remote access.
- The adequacy of physical and logical protection against unauthorized access including individual penetration attempts, computer viruses, denial of service, and other forms of electronic access.

By written report, the Reviewer must confirm that the security measures, including the firewall, have been satisfactorily implemented and tested. For additional guidance, see "The Internet and the National Bank Charter" booklet of the *Comptroller's Licensing Manual*, pages 37-38 and 74-75. The booklet may be found at the Publications section of the OCC's Web site: <http://www.occ.treas.gov/netbank/letters.htm>.

3. The bank must have a security program in place that complies with the "Interagency Guidelines Establishing Standards for Safeguarding Customer Information" specified at 12 CFR 30, Appendix B.
4. A letter must be submitted to the Western District Office at least 45 days before the bank is scheduled to open, notifying the OCC that all conditions and requirements necessary to receive a national bank charter have been met, requesting a preopening examination, and providing the anticipated opening date.
5. The bank's initial Tier 1 capital, net of any and all organizational and preopening expenses, must be no less than \$275 million on opening day.
6. The organizers must obtain FDIC insurance for the bank, and receive any other regulatory approvals, including any applicable approvals from the Federal Reserve for the related bank holding company application.
7. The OCC must conclude that it has no supervisory objection to the bank's program of systems and controls to address the risks and issues associated with third party outsourcing as outlined in OCC Bulletin 2001-47; Third Party Relationships.
8. The OCC must conclude that it has no supervisory objection to the bank's program to address compliance with the anti-tying standards of 12 U.S.C. § 1972.

The OCC poses no objection to the proposed executive officers as proposed in the application as follows:

President and Chief Executive Officer:	Richard F. Kenny
Chief Financial Officer:	J. Scott Rhoades
Chief Operating Officer:	Mark J. Watson
Chief Credit Officer:	Patricia A. Kenny
Chief Information Officer:	Hugh E. Westermeyer
Chief Compliance Officer:	Julianne Gray

Chief Marketing Officer:

Christina C. Polizzotto

Prior to the bank's opening, the bank must obtain the OCC's prior written determination of no objection for any additional organizers or executive officers, or directors appointed or elected before the person assumes the position. For a two-year period after the bank commences business, the bank must file and the OCC issue a letter of no objection to any new executive officer or director prior to that person assuming such position.

The OCC poses no objection to the following persons serving as directors as proposed in the application:

Charles R. Schwab, William L. Atwell, Richard F. Kenny, J. Scott Rhoades, Bryce R. Lensing, Geoffrey J. Penney, and David R. Martin.

The OCC also grants your request to waive the residency requirements of 12 USC 73 for the majority of the bank's board of directors. This waiver is granted based upon a review of all available information, including the filing and any subsequent correspondence and discussions, and the bank's representation that this waiver will not affect the board's responsibility to direct the bank's operations in a safe, sound, and legal manner. The OCC reserves the right to withdraw or modify this waiver and, at its discretion, to request additional information at any time in the future.

## V. CONCLUSION

The charter proposal satisfies the applicable statutory requirements of the National Bank Act and the policy standards of the OCC, as set forth in 12 C.F.R. § 5.20. For the reasons set forth above, including the representations and commitments made by the Organizers, the application is hereby preliminarily approved, subject to the requirements and conditions in this Decision and the transmittal letter.<sup>19</sup>

*/s/ Julie L. Williams*

*February 4, 2003*

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Julie L. Williams  
First Senior Deputy Comptroller and  
Chief Counsel

\_\_\_\_\_  
Date

Application Control Number: 2002-WE-01-0006

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<sup>19</sup> The preliminary conditional approval, and the activities and communications by OCC employees in connection with the filing, do not constitute a contract, express or implied, or any other obligation binding upon the OCC, the United States (U.S.), any agency or entity of the U.S., or any officer or employee of the U.S., and do not affect the ability of the OCC to exercise its supervisory, regulatory and examination authorities under applicable law and regulations. The foregoing may not be waived or modified by any employee or agent of the OCC or the U.S.

