



Comptroller of the Currency
Administrator of National Banks

Washington, DC 20219

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January 2000
12 USC 24(7)

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127 Public Square
Cleveland, Ohio 44114-1306

Dear Mr. Kopek:

This responds to your request for confirmation that Key Bank USA, National Association, Cleveland, Ohio (“Bank”) may lawfully acquire and hold a non-controlling, minority interest in Econex LLC (“Econex”), a limited liability company that will provide certain Internet-related services to merchants, and that it is legally permissible for Key Merchant Services, LLC (“KMS”), a limited liability company in which the Bank holds a non-controlling, minority interest, to expand its activities to include the Internet-related services to merchants. Based upon the information and representations provided, we conclude that the Bank’s proposed investment in Econex and KMS’s proposed expansion of activities are permissible.

I. BACKGROUND

A. Structure

The proposed owners of Econex, a Georgia limited liability company, will be the Bank, NOVA Corporation (“NOVA”), FirstEnergy Corp. (“FirstEnergy”), and David Scantling (“Scantling”). NOVA is a provider of merchant debit/credit card processing services. FirstEnergy is a utility company headquartered in Akron, Ohio. Scantling is founder and first president of Econex. The proposed owners will acquire their interests in Econex in accordance with a four-phase investment plan. Phase I of the investment plan has been completed, resulting in NOVA, Scantling, and FirstEnergy owning 57.14%, 28.57%, and 14.29% of Econex, respectively. Under Phase II, the Bank proposes to acquire new units of Econex that will result in a 28.57% interest in the company. As a consequence of the Bank’s investment (and a concurrent additional investment by FirstEnergy), the ownership interests of NOVA and Scantling will be diluted. The resulting ownership interests in Econex after Phase II will be 28.57% for the Bank, 28.57% for NOVA, 28.57% for FirstEnergy, and 14.29% for Scantling. Under Phase III, NOVA has the right, but not the obligation, to acquire additional units of Econex such that its interest in the company will increase to 51%. If NOVA exercises its option under Phase III, the Bank’s and

FirstEnergy's interests will be diluted to 19.6% each, and Scantling's interest will be diluted to 9.8%. Under Phase IV, Econex would convert to a Delaware corporation.¹

An Operating Agreement currently governs Econex and its members. As part of Phase II this Operating Agreement will be amended to, among other things, include the Bank as a party to the agreement. The Bank represents the First Amended and Restated Operating Agreement ("Amended Agreement") will be adopted once it makes its investment in Econex. Section 2.79(b) of the Amended Agreement includes a provision that precludes Econex from engaging in any business that would constitute a new activity within the meaning of applicable banking law, rules, and regulations, and that would make the Bank's investment in Econex impermissible, without first giving the Bank notice of Econex's intent to engage in the new activity and allowing the Bank an opportunity to obtain regulatory approval for such new activity (the "Veto Right"). In the event that the Bank cannot obtain the appropriate regulatory approval, the Amended Agreement prohibits Econex from engaging in that new activity without the written consent of the Bank.

Section 14.1 of the Amended Agreement requires the unanimous consent of all Econex investors for any amendment to the Amended Agreement that would adversely affect the rights and obligations of any of the members. Section 2.7(d) further provides that upon conversion to a corporation, the Econex investors will execute legal documents, including a certificate of incorporation, by laws, and a shareholders' agreement, with terms, conditions, equity ownership, and governance rights, that are consistent with the Operating Agreement in effect at that time. Moreover, in Section 2.7(d) the members of Econex acknowledge and agree that the Bank's Veto Right will be incorporated into the shareholders' agreement upon the conversion to a corporation.

The Bank currently owns a 49% interest in KMS. The remaining 51% is owned by NOVA. KMS currently engages in the business of merchant credit and debit card processing and the leasing of point-of-sale terminals to merchants. KeyBank N.A., Cleveland, Ohio ("KBNA"), an affiliate of the Bank, initially received OCC approval to acquire a 49% indirect interest in KMS through an operating subsidiary, Key Payments Services Inc ("KPSI").² The Bank acquired its 49% interest in KMS from KPSI as a result of an internal corporate reorganization that was effective April 1, 1999. Except for changes attendant to the transfer in ownership, the relevant facts about the structure and operating agreement of KMS as described in OCC Conditional Approval No. 269 remain the same.

¹ The conversion of Econex from a limited liability company to a corporation would occur at such time that Econex enters into an agreement with one or more underwriters for an initial public offering.

² See OCC Conditional Approval No. 269 (January 13, 1998).

B. Proposed Activities

Econex and KMS propose to provide services to merchants to facilitate the sales of goods and services over the Internet. Econex and KMS propose to offer merchants a package of electronic services (“Internet Services”) that bundle payment processing services with ancillary support necessary for merchants to have retail web sites that will be linked to a “virtual mall” web site. Additionally, Econex will provide these services to other financial institutions on a wholesale basis so that those institutions may offer similar Internet services to their merchant customers.

KMS will seek to sell these Internet Services to merchants to which it currently provides debit and credit card processing services, as well as to other merchants.³ KMS will provide merchants with software needed to create their own web sites on the Internet, and the merchant may select a web site template from a series of available templates, or opt to have KMS custom build the web site.⁴ KMS also will help merchants maintain their web sites.⁵ KMS will provide sales tax calculations on the products and services sold to merchants who request that information, will register merchants with a number of Internet search engines, and will obtain an Internet web site address known as a Universal Resource Locator (“URL”) for the merchant.

There will be links between KMS’s web sites and the web sites of the merchants that sign up for KMS’s Internet Services, thus forming a type of “virtual mall.” There also will be links between the KMS web site and the Bank’s web site, so that a person visiting the Bank’s web site will be able to access the KMS virtual mall web site.⁶

³ KBNA is a party to the contracts KMS currently has with merchants to provide debit and credit card processing services. Under these three-party contracts between the merchant, KMS and KBNA, KBNA is the sponsoring bank that provides access to the payments networks. These contracts will be assigned by KBNA to the Bank. Furthermore, the Bank will be a party to the contracts with merchants that KMS signs up for the Internet Services. These contracts will likewise be three-party contracts between the merchant, KMS and the Bank under which the Bank provides access to the payments networks as sponsoring bank. KMS currently has a services agreement with KBNA pursuant to which KBNA provides clearing, settlement, marketing, and other related services to KMS. This agreement will also be assigned by KBNA to the Bank after which the Bank will provide those services to KMS.

⁴ The merchant purchasing the Internet Services will make all decisions as to what information will be presented on its web site and how that information will be presented.

⁵ Such maintenance will include ongoing maintenance and support of the web site’s host servers, as well as providing merchants with reports on transaction volume and other data relating to the purchase of products and services from their web sites. Each merchant, however, is responsible for maintaining and updating the store and product information contained on their web site.

⁶ The KMS home page will include a disclosure stating that the Bank and its affiliates do not guarantee, endorse or provide any of the goods or services available through the third-party web sites linked through the KMS site. The user agreement of the Bank’s web site will include a similar disclosure. The merchants’ web sites will not carry any indication that they are being hosted or supported by the Bank, KMS or Econex. The Bank’s logo or other references to the Bank, KMS or Econex will not appear on a merchant’s web site, except as may be necessary to effect the payments processing component. Bank, through KMS and Econex, will also limit its reputation risk by

Econex will provide to KMS the aforementioned software and web site hosting services that KMS will then re-sell to the merchants, will contract directly with merchants to provide the web site building, software, and hosting services, and will market to other financial institutions the same web site software and hosting services that it provides to KMS so that these other financial institutions will be able to re-sell those services to merchants that they sign up.

Econex and KMS, via the Internet, will provide an electronic communications pathway between the merchant and its potential customers through which product orders and payment information flow.⁷ Thus, customers who wish to purchase products or services from the merchants through their web sites can also pay for those purchases through the Internet by debit or credit card, electronic checks, or other means of electronic payment. When a potential customer submits a purchase order at a merchant's web site, the order, along with payment and shipping information will be transmitted electronically to the merchant. The merchant will be able to electronically confirm payment authorization before shipping any goods. Econex will directly or indirectly provide the payment authorization and processing for these payment transactions. Econex and KMS also will provide merchants with electronic bill presentment services whereby the Econex and KMS will electronically present bills to customers who have previously ordered goods or services from these merchants.

Merchants who sign up for the Internet Services will be charged various fees, including a licensing or start-up fee when they initially sign up for the services, monthly maintenance and hosting fees, and transaction fees in connection with processing credit and debit card transactions or other payment transactions. Neither KMS or Econex will receive any referral fee when a consumer links to a merchant's web site from the KMS virtual mall web site.

The proposed activities involve risks associated with the processing of debit and credit card transactions and other payment transactions. These risks are the same types of risk that banks already assume when providing merchant debit and credit card processing services for business customers. The risks associated with accepting and authorizing payments through a merchant's web site are identical to those

reserving the right to prohibit offensive or indecent material from hosted sites. Finally, the Bank has committed to ensure that KMS complies with the FFIEC Interagency Statement on Nondeposit Investment Products ("FFIEC Statement") if the OCC determines that the FFIEC Statement is applicable. *See* OCC Banking Circular 274 (February 16, 1994).

⁷ In connection with the services it provides, KMS may have access to personal information of its customers. In this regard, KMS has adopted a statement of policy concerning the treatment of personal customer information in the conduct of its business that recognizes customer expectations for privacy and provides standards for the use, collection and retention of such information. KMS's policy states that if personally identifiable consumer information is provided to a third party, KMS insists that the third party adhere to strict privacy guidelines that provide for keeping such information confidential. KMS further represents that it maintains security standards and procedures intended to preclude unauthorized access to customer information. KMS's privacy statement will be accessible via link from each page of its web site.

Econex initially will not be dealing directly with merchants' customers. However, since data will be stored on servers it owns or leases, Econex may have access to personal information of customers. Bank management involved in the Econex project has represented that Econex has no intention of selling customer data to which they might have access to third parties.

already assumed when banks enable an established web site to receive debit and credit card orders or other forms of electronic payments. To the extent that Econex and KMS contract with other service providers, notably technology firms, to provide any of the necessary products and services to offer the Internet Services to merchants, they will manage its indirect risk exposure to the activities of the service providers.

II. DISCUSSION

A. *National Bank Express and Incidental Powers (12 U.S.C. § 24(Seventh))*

The OCC has traditionally recognized the authority of national banks to organize and perform any of their lawful activities in a reasonable and convenient manner not prohibited by law. A national bank may engage in activities that are part of or incidental to the business of banking by means of an operating subsidiary.⁸ Further, the OCC has permitted national banks to own, either directly or indirectly through an operating subsidiary, a non-controlling interest in an enterprise. The enterprise might be a limited partnership, a corporation, or a limited liability company.⁹ In interpretive letters, the OCC has concluded that national banks are legally permitted to make a non-controlling investment in a limited liability company or corporation provided four criteria or standards are met.¹⁰ These standards, which have been distilled from our previous decisions in the area of permissible non-controlling investments for national banks and their subsidiaries, are:

- (1) the activities of the entity or 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 or entity 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; and
- (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.

⁸ See 12 C.F.R. § 5.34(d)(1).

⁹ See also 12 C.F.R. § 5.36(b). National banks are permitted to make various types of equity investments pursuant to 12 U.S.C. § 24(Seventh) and other statutes.

¹⁰ See Corporate Decision No. 97-54 (June 26, 1997); OCC Interpretive Letter No. 711, *reprinted in* [1995-1996 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 81-026 (Feb. 23, 1996); OCC Interpretive Letter No. 692, *reprinted in* [1995-1996 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 81,007 (November 1, 1995), and No. 694, *reprinted in* [1995-1996 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 81,009 (December 13, 1995); OCC Interpretive Letter No. 705, *reprinted in* [1995-1996 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 81,020 (October 25, 1995).

Based upon the facts presented, the Bank's proposal satisfies these four standards.¹¹

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

Our precedents on non-controlling ownership have recognized that the enterprise in which the bank holds an interest must confine its activities to those that are part of, or incidental to, the conduct of the banking business.¹²

In the present case, Econex and KMS will provide a package of Internet-related services linked with merchant debit and credit card processing and other electronic billing and payment services. Additionally, Econex will provide these services to other financial institutions on a wholesale basis so that those institutions may offer similar Internet Services to their merchant customers. As discussed below, these proposed activities are part of, or incidental to, the business of banking.

The OCC has already addressed Internet services and related order and payment processing services, similar to those proposed by Econex and KMS, and has found that they are part of, or incidental to the business of banking and, therefore, authorized for national banks under 12 U.S.C. § 24(Seventh).¹³ We have previously determined that a national bank may provide a "package" of Internet-based services to retail merchants which included the following: hosting merchants' web sites on its server; registering merchants with search engines and obtaining URLs; providing an electronic communications pathway for product ordering and payment; maintaining merchants' data associated with the web sites on its server (e.g., price information, product descriptions, and images); providing merchants with software to create web sites; providing reports on transactions, web site "hits," and sales data; and processing credit card transactions. Econex and KMS propose to provide all of these previously approved activities.

In our previous decisions, we concluded that the hosting of commercial web sites, registering merchants with search engines and obtaining URLs, providing an electronic communications pathway for product ordering and payment, and electronically storing and retrieving the data set for a merchant's on-line

¹¹ In OCC Conditional Approval No. 269, the OCC determined that KBNA's indirect investment in KMS met all four of the noncontrolling minority investment standards. The proposed expansion of KMS's activities impact only the first and fourth standards. Except for changes attendant to KBNA's transfer of its indirect ownership of KMS to the Bank, the relevant facts about the structure and operating agreement of KMS as described in OCC Conditional Approval No. 269 remain the same. Accordingly, we do not re-evaluate the Bank's investment in KMS relative to the second and third standards herein.

¹² See, e.g., OCC Interpretive Letter No. 380, *reprinted in* [1988-1989 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 85,604 n.8 (December 29, 1986) (since a national bank can provide options clearing services to customers it can purchase stock in a corporation providing options clearing services); Letter from Robert B. Serino, Deputy Chief Counsel (November 9, 1992) (since the operation of an ATM network is "a fundamental part of the basic business of banking," an equity investment in a corporation operating such a network is permissible).

¹³ OCC Interpretive Letter No. 856 (March 6, 1999).

catalog are forms of finder activities authorized for national banks.¹⁴ The finder function has long been recognized as a permissible 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 transactions that the parties themselves negotiate and consummate."¹⁵ Providing information to prospective buyers about the products or services of prospective sellers is also one of the fundamental activities of a finder.¹⁶ By hosting merchants' web sites, Econex and KMS will be bringing potential customers and merchants together for a transaction that the parties themselves negotiate and consummate, and providing potential customers with information about those merchants' goods and services. Accordingly, we conclude that the components of Econex's and KMS's proposed Internet Services package that involve hosting of commercial web sites, registering merchants with search engines and obtaining URLs, and electronic storage and retrieval of the data set for a merchant's on-line catalog are permissible finders activities authorized for national banks pursuant to 12 U.S.C. § 24(Seventh).

We have also previously determined that a national bank engaged in permissible web site hosting activity may provide merchants with software that will enable them to design their web sites. The software is "necessary" to use or fully enjoy the permissible service and, thus, is either part of the service (if limited

¹⁴ See also OCC Corporate Decision No. 97-60 (July 1, 1997) (national bank operating subsidiary maintaining and operating an Internet web site which provides information on pre-owned automobiles to potential buyers); OCC Conditional Approval No. 221, (Dec. 4, 1996) (national bank making a minority investment in a company that provides an electronic "gateway" through which customers of bank will be able to obtain home banking and other financial services from their respective financial institutions through various electronic access devices); OCC Interpretive Letter No. 611, *reprinted in* [1992-1993 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 83,449 (Nov. 23, 1992) (national bank linking non-bank service providers to its communications platform of smart phone banking services).

¹⁵ 61 Fed. Reg. 4863 (Feb. 9, 1996) (codified at 12 C.F.R. 7.1002(b)).

12 C.F.R. § 7.1002 provides in its entirety:

- (a) General. A national bank may act as a finder in bringing together a buyer and seller.
- (b) Qualification. Acting as a finder includes, without limitation, identifying potential parties, making inquiries as to interest, introducing or arranging meetings of interested parties, and otherwise bringing parties together for transactions that they themselves negotiate and consummate. Acting as a finder does not include activities that would characterize the bank as a broker under applicable federal law.
- © Advertisement and fee. Unless otherwise prohibited, a national bank may advertise the availability of, and accept a fee for, the services provided pursuant to this section.

Earlier OCC decisions regarding finder activities cite 12 C.F.R. § 7.7200. OCC interpretive rulings at 12 C.F.R. Part 7 were revised and renumbered effective April 1, 1996. Interpretive ruling § 7.1002 (1996) replaced former interpretive ruling § 7.7200.

¹⁶ See OCC Interpretive Letter No. 653, *reprinted in* [1994-1995 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 83,601 (Dec. 22, 1994).

function) or incidental thereto (if full function).¹⁷ Thus, Econex's and KMS's provision to merchants of software to enable them to design their web sites is permissible under 12 U.S.C. § 24(Seventh).

The processing of payments resulting from orders received through a merchant's bank-hosted web site is clearly part of the business of banking.¹⁸ Econex and KMS will process payments resulting from orders received from a merchant's web site in several ways. The two entities will process purchases made over the Internet with debit and credit cards. Merchant debit and credit card processing services generally involves verifying credit card authorizations at the time of purchase, processing card transactions, settlement of card transactions, and depositing funds in merchants' accounts. Econex and KMS will also process electronic checks and other means by which a purchaser electronically authorizes payment for the purchase of goods or services. This payment processing activity will include verifying authorizations, processing transactions, settlement of transactions, and depositing funds in merchants' accounts. The fact that the debit and credit card and other electronic payment transactions will involve purchases of goods or services over the Internet does not change the nature of the services that will be provided. Thus, the proposed payments processing activities of Econex and KMS are part of the business of banking.

Econex and KMS also propose to provide merchants with monthly reports on empirical data such as site "hits" and transaction volume arising from their web sites, including number and types of products sold. Again, we have previously concluded that to the extent those reports involve the processing and transmittal of information relating to specific payment transactions the bank handles for the merchant, it is part of the payment processing function and not a separate service.¹⁹ Additionally, we have determined that a bank's calculation of sales taxes owed by the merchants on their Internet sales is an activity incidental to the payments processing services and is thus permissible.²⁰

¹⁷ OCC Interpretive Letter No. 856. *See also* Conditional Approval No. 221(Dec. 4, 1996) (providing full-function web browser software is a permissible incidental activity when a national bank is offering a home banking system based on web server technology using "Internet compatible" browser software).

¹⁸ OCC Interpretive Letter No. 856. *See also* OCC Conditional Approval No. 289 (October 2, 1998) (national banks may acquire a minority interest in a firm that, among other things, provides accounts receivable processing and accounts payable processing); Conditional Approval Letter No. 248 (national bank operating subsidiary may acquire a minority interest in an entity that provides merchant credit and debit card processing services), OCC Conditional Approval No. 282 (July 7, 1998) (national bank may acquire an interest in a firm that would, among other things, engage in payments processing for the health care firms); and OCC Interpretive Letter No. 731, *reprinted in* [1995-1996 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 81,048 (July 1, 1996) (national banks as part of the banking business may collect and process accounts in relating to an electronic toll collection system).

¹⁹ OCC Interpretive Letter No. 856. *See also* OCC Interpretive Letter No. 731, *supra* and OCC Interpretive Letter No. 732, *reprinted in* [1995-1996 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 81,049 (May 10, 1996) (design, development, marketing, and maintenance of a network for electronic funds transfer and electronic data interchange permissible for a national bank). *Cf.* Letter from Julie L. Williams, Chief Counsel, October 2, 1996 (unpublished) (national bank acting as finder could maintain a database of transactions resulting from its finder activities was "integral" to the finder function).

²⁰ OCC Interpretive Letter No. 856. *See also* *Clement Nat'l Bank v. Vermont*, 231 U.S. 120 (1913).

Finally, we have concluded that the bank could, as part of its proposed web site hosting services, provide the merchants with more general information and reports relative to their web sites.²¹ We have long held that as part of the business of banking, national banks may collect, transcribe, process, analyze, and store for itself and others banking, financial, or related economic related data.²² Here, Econex and KMS propose to provide similar types of information and reports to the merchants as part of their Internet Services package. Accordingly, those proposed activities of Econex and KMS also are permissible.

Econex and KMS also propose to provide billing services, to provide links from their web sites to the web sites of merchants that have subscribed to the Internet Services package, to provide the Internet merchant hosting services on a wholesale basis to other financial institutions to enable those institutions to resell the services to its merchant customers, and to build the merchants' web sites at the merchant's option.

We have previously found that electronic bill presentment is part of the business of banking.²³ Thus, the proposed billing services of Econex and KMS are permissible activities pursuant to 12 U.S.C. § 24(Seventh).

We also have previously determined that providing links to third party vendors' web sites, in the manner proposed by Econex and KMS, is a finder activity and, thus, part of the business of banking.²⁴ By providing links to the merchant' web sites, KMS introduces two parties who may engage in a transaction.

²¹ OCC Interpretive Letter No. 856. *See also* OCC Interpretive Letter No. 653, *supra* (national bank acting as a finder for insurance could also keep financial and other records relating to the client agency sales, receipts and disbursements); OCC Interpretive Letter No. 741, *supra* (national bank acting as finder for automobile dealers may also maintain a comprehensive system that allows dealers to track information on customers referred and to generate market statistics such as buying trends and cycles).

²² 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, the "analytical framework" embodied in the ruling remained the same. 49 Fed. Reg. 11157 (Mar. 26, 1984). There was no intent to narrow or restrict the substantive effect of the rule. OCC Interpretive Letter No. 677, *reprinted in*, [1994-1995 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 83,625 (June 28, 1995). *See also*, OCC Interpretive Letter No. 737, *supra* (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 (Dec. 22, 1994) (national bank may act as an informational and payments interface between insurance underwriters and general insurance agents); and OCC Interpretive Letter No. 346, *reprinted in* (1985-1987 Transfer Binder) Fed. Banking L. Rep. (CCH) ¶ 85,516 (July 31, 1985) (national banks may maintain records on commodities transactions).

²³ *See e.g.*, OCC Conditional Approval No. 304 (March 5, 1999) (electronic bill payment and presentment services over the Internet); OCC Interpretive Letter No. 731, *reprinted in* [1995-1996 Transfer Binder] Fed. Banking Law. Rep. (CCH) ¶ 81-048 (July 1, 1996) (operation of electronic toll collection system); OCC Interpretive Letter No. 836, *reprinted in* [1996-1997 Transfer Binder] Fed. Banking Law. Rep. (CCH) ¶ 81-290 (March 12, 1996) (data processing and electronic data interchange system to assist in the billing and collection for medical services).

²⁴ *See* OCC Conditional Approval No. 221 (December 4, 1996).

Any further negotiations will then occur between the customer and the merchant. At that point, KMS'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.

Providing the Internet merchant hosting services to other financial institutions for their resale to their merchant customers also qualifies as a modern correspondent banking function. The OCC has long permitted national banks to offer correspondent services as part of the business of banking.²⁵ More specifically, the OCC has allowed national banks as a permissible correspondent activity to provide data processing and other computer-related services to other financial institutions.²⁶

Moreover, the OCC has permitted a national bank to market specially designed computerized "smart phones" to other financial institutions as a correspondent banking function.²⁷ Like the Internet merchant hosting services package here, the "smart phones" enabled customers to communicate with their banks and with other service providers through a supporting network of computers and software to conduct various financial transactions (e.g., bill paying, point-of-sale, and credit card transactions).

Econex's proposal to provide the Internet merchant hosting services package to financial institutions is functionally equivalent to providing them with the data processing services and the electronic gateways and communication devices referred to above. Hence, we conclude that providing Internet merchant hosting services packages that meet the banking needs of financial institution merchant customers is a valid correspondent banking service and, therefore, part of the business of banking.

Finally, Econex and KMS propose to build web sites for merchants as part of the Internet merchant hosting services package. Both entities have presented convincing evidence that the ability to build the web sites for the participating merchants as part of Internet Services package is critical to the successful

²⁵ See e.g., OCC Interpretive Letter No. 811, *reprinted in* [1997-1998 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 81-259 (Dec. 18, 1997) (permitting national bank to offer printing services to other financial institutions as correspondent service); Corporate Decision No. 97-79 (July 11, 1997) (federal flood hazard determinations).

²⁶ See OCC Interpretive Letter No. 516, *reprinted in* [1990-1991 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 83,220 (July 12, 1990) (authorizing national bank to provide other financial institutions with electronic "gateways" to communicate and receive financial information and to conduct transactions); OCC Interpretive Letter No. 346, *reprinted in* [1985-1987 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 85,516 (July 31, 1985) (bank operating subsidiary may provide electronic information and transaction services and linkage for financial settlement services).

²⁷ OCC Interpretive Letter No. 611, *reprinted in* [1992-1993 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 83,449 (Nov. 23, 1992).

marketing of the package.²⁸ We therefore find that the proposed building of web sites by Econex and KMS for those merchants desiring that service is incidental to the business of banking.

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.²⁹ We 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:

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 service of building the merchants web sites is needed to successfully market Econex's and KMS's Internet Services package. Without the web site building component, Econex's and KMS's Internet Services package will not fully satisfy customer demand, thus putting them at a competitive disadvantage relative to other providers of Internet commerce and web site hosting services.

Econex and KMS have demonstrated that there is strong merchant demand for a web site building component in the package of Internet Services supported by the LLC. There is also clear evidence that competitors of Econex and KMS are and will be offering such a feature. Finally, the Internet access feature will be only a minor part of the entire package offered by Econex and KMS (on average over the next five years, projected gross profits from web site building will be less than 30% of the projected gross

²⁸ In designing the Internet Services package to be offered by Econex and KMS, Econex conducted a survey of 1,000 randomly-selected small merchants. The results of this survey suggest that those merchants overwhelmingly demand that the proposed Internet Services include the building of the web site. Of the 455 merchants that responded to the survey question about whether they would develop their web site in-house or outsource it, approximately 83 percent said they desire total outsourcing. *See also* Jennifer Kingson Bloom, *Vendor Groups Woo Banks into Net Services*, Am. Bankr., May 27, 1999, at 14 (reporting that vice president of the National Retail Federation says merchants of all sizes prefer to outsource the building of virtual stores). In light of this indicia of consumer demand, Econex and the LLC assert that they need to include the building of web sites as part of their package of Internet Services in order to successfully market that package.

The marketplace apparently agrees. To enhance marketability and reduce costs to merchants, the firms that will compete with Econex and KMS in providing Internet commerce products and services are now offering complete packages to merchants which include the building of the web sites. *See e.g.*, Bloom, *supra*; Steven Marjanovic, *First Data to Buy Stake in iMall, a Software Firm*, Am. Bankr., Nov. 9, 1998, at 17; Tami Luhby, *Wells Fargo Opens Door to Web for Small Business*, Am. Bankr., Sept. 15, 1998. Experts say that without these packages, most smaller companies lack the budget and manpower to do a thorough job of creating and maintaining a commerce-enabled web site. Bloom, *supra*.

²⁹ OCC Interpretive Letter No. 742, *reprinted in* [1996-1997 Transfer Binder] Fed. Banking. L. Rep (CCH) ¶ 81-106 (Aug. 19, 1996) (the "Apollo Letter").

profits of the entire Internet Services package).³⁰ Under these circumstances, we find the web site building services to be incidental to the other Internet Services, and therefore authorized.

Thus, we conclude that all the proposed activities to be conducted by Econex and KMS are part of, or incidental to, the business of banking. Therefore, the first standard is met.

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.*

The activities of the enterprise in which a national bank may invest must be part of, or incidental to, the business of banking not only at the time the bank first acquires its ownership, but for as long as the bank has an ownership interest. This standard may be met if the Bank is able to exercise a veto power over the activities of the enterprise, or is able to dispose of its interest.³¹

The Amended Agreement precludes Econex from engaging in any business that would constitute a new activity within the meaning of applicable banking law, rules, and regulations, and that would make the Bank's investment in Econex impermissible, without first giving the Bank notice of Econex's intent to engage in the new activity and allowing the Bank an opportunity to obtain regulatory approval for such new activity. In the event that the Bank cannot obtain the appropriate regulatory approval, the Amended Agreement prohibits Econex from engaging in that new activity without the written consent of the Bank (the "Veto Right"). Moreover, the Amended Agreement requires the unanimous consent of all Econex investors for any changes to the Amended Agreement that would adversely affect the rights and obligations of any of the members. Thus, the Bank would have the right to block any changes to its Veto Right.

The Amended Agreement further provides that upon conversion to a corporation, the Econex investors will execute legal documents, including a certificate of incorporation, by laws, and a shareholders agreement, with terms, conditions, equity ownership, and governance rights, that are consistent with the

³⁰ 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, *reprinted in* [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, *reprinted in* [1996-1997 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 81-120 (Nov. 6, 1996). 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.

³¹ See, e.g., Interpretive Letter No. 711, *reprinted in* [1995-1996 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 81-026 (February 3, 1996); Interpretive Letter No. 625, *reprinted in* [1993-1994 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 83,507 (July 1, 1993).

Operating Agreement in effect at that time. In Section 2.7(d) the members of Econex acknowledge and agree that the Bank's Veto Right will be incorporated into the shareholders agreement upon the conversion to a corporation. In the event that a decision is subsequently made not to incorporate the Bank's Veto Right in the incorporation documents, and Econex undertakes to engage in a new activity that is not permissible for national banks, the Bank represents it will sell its interest in Econex.³² Therefore, the second standard is satisfied.

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.*

- 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 the national bank's investment not expose it to unlimited liability.

Initially, Econex will be a Georgia limited liability company. As a legal matter, investors in an Georgia limited liability company do not incur liability with respect to the liabilities or obligations of the limited liability company solely by reason of being a member or manager of the company.³³ Furthermore, the Amended Agreement includes a provision which states that no member, manager, agent or employee of Econex shall be liable for any debt, obligation or liability of the Econex solely by reason of being a member, manager, agent or employee.

Econex may, in the future, convert to a Delaware corporation. A corporation is an entity distinct from its shareholders.³⁴ It is generally accepted that shareholders are protected by the "corporate veil" from liability for the debts and obligations of the corporation provided proper corporate separateness is maintained.³⁵

Thus, the Bank's loss exposure for the liabilities of Econex, as limited liability company or as a corporation, will be limited.

- b. *Loss exposure from an accounting standpoint*

³² Section 10.1 of the Amended Agreement provides that during the 18 month period following the Bank's investment in Econex, any member of the Econex may sell its interest in the company only with the consent of all other members. The Bank represents that if the conversion to a corporation occurs during that 18 month period, it will not agree to leave its Veto Right out of the incorporation documents unless this restriction on transfer is also left out of the incorporation documents. Thus, the Bank would be in a position to sell its interest in Econex without having to obtain the consent of the other investors.

³³ See Ga. Code Ann. § 14-11-303.

³⁴ 1 Fletcher, Cyclopedia of the Law of Private Corporations § 25 (rev. perm. ed. 1990).

³⁵ *Id.*

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 20-50 percent ownership share of investment in a limited liability company is to report it on an unconsolidated basis. Under the equity method of accounting, unless the bank has extended a loan to the entity, guaranteed any of its liabilities or has other financial obligations to the entity, losses are generally limited to the amount of the investment shown on the investor's books.³⁶

The Bank will account for its investment in Econex under the equity method of accounting. Thus, the Bank's loss from an accounting perspective will be limited to the amount invested in Econex, and the Bank will not have any open-ended exposure to the liabilities of Econex.

Therefore, for both legal and accounting purposes, the Bank's potential loss exposure relative to Econex should be limited to the amount of its investment. Thus, the third standard is satisfied.

4. *The investment must be convenient and 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 must also 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 constitute a mere passive investment unrelated to that bank's banking business. 12 U.S.C.

§ 24(Seventh) gives national banks incidental powers that are "necessary" to carry on the business of banking. "Necessary" has been judicially construed to mean "convenient or useful."³⁷ Our precedents on bank non-controlling investments have indicated that the investment must be convenient or useful to the bank in conducting *that bank's* business. The investment must benefit or facilitate that business and cannot be a mere passive or speculative investment.³⁸

The Bank's proposed investment in Econex, and its continued investment in KMS after it expands its activities as proposed, will meet this standard. KMS and Econex will market the Internet Services to customers for which the Bank is providing merchant processing services. The Bank anticipates that providing these Internet Services through KMS and Econex will help retain existing and attract new merchant customers. Furthermore, by undertaking these proposed activities through joint ventures involving NOVA and FirstEnergy, the Bank believes the investment in technology needed to make the venture successful will be ensured. Thus, the investments are convenient and useful to the Bank in carrying out its business and is not a mere passive investment. Thus, the fourth standard is satisfied.

³⁶ See generally, Accounting Principles Board, Op. 18 § 19 (1971) (equity method of accounting for investments in common stock). Interpretive Letter No. 692, *supra*.

³⁷ See *Arnold Tours, Inc. v. Camp*, 472 F.2d 427, 432 (1st Cir. 1972).

³⁸ See, e.g., Interpretive Letter No. 697, *supra*; Interpretive Letter No. 543, *reprinted in* [1990-1991 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 83,255 (February 13, 1991); Interpretive Letter No. 427, *reprinted in* [1988-1989 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 85,651 (May 9, 1988); Interpretive Letter No. 421, *reprinted in* [1988-1989 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 85,645 (March 14, 1988); Interpretive Letter No. 380, *supra*.

III. CONCLUSION

Based upon the information and representations you have provided, and for the reasons discussed above, we conclude that the Bank may acquire and hold a non-controlling minority interest in Econex in the manner and as described herein, and continue to hold a non-controlling minority interest in KMS, subject to the following conditions:

1. Econex and KMS will engage only in activities that are part of, or incidental to, the business of banking;
2. the Bank will have veto power over any activities and major decisions of Econex and KMS that are inconsistent with condition number one, or will withdraw from Econex or KMS in the event the entity engages in an activity that is inconsistent with condition number one;
3. the Bank will account for its investment in Econex and KMS under the equity method of accounting; and
4. Econex and KMS will be subject to OCC supervision, regulation, and examination.

Please be advised that the conditions of this approval are deemed to be “conditions 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 and, as such, may be enforced in proceedings under applicable law.

This approval is granted based on a thorough review of all information available, including the representations and commitments made in the Bank letters and by Bank representatives.

Sincerely,

/s/

Julie L. Williams
First Senior Deputy Comptroller and Chief Counsel