
**Board of Governors of the Federal Reserve System
Federal Deposit Insurance Corporation
Office of the Comptroller of the Currency
Office of Thrift Supervision**

**Report to the Congress
on Review of Regulations Affecting
Online Delivery of Financial Products and Services**

November 2001

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Submitted to the Congress pursuant to section 729 of the Gramm-Leach-Bliley Act

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Introduction

The Board of Governors of the Federal Reserve System (Board), Federal Deposit Insurance Corporation (FDIC), Office of the Comptroller of the Currency (OCC), and Office of Thrift Supervision (OTS) (collectively, the Agencies), jointly issue this report about banking regulations that affect the online delivery of financial products and services. The Agencies prepared the report pursuant to section 729 of the Gramm-Leach-Bliley Act (the GLB Act or Act).¹

The Agencies' report consists of several parts: Part I summarizes the statutory mandate and the methods the Agencies used to conduct the studies and prepare this report; Part II discusses the Agencies' review of the regulations that the Agencies must administer jointly; and Parts III – VI describe each Agency's review of the regulations that it solely administers.

Summary of Conclusions

This report concludes that the Agencies' regulations generally accommodate online banking and lending. The report outlines those few areas that the Agencies plan to consider further for possible modifications.

The Agencies will continue to monitor developments in banking practices and technology. The Agencies are committed to updating their respective regulations and guidance as the need arises, both individually and in conjunction with each other and the Federal Financial Institutions Examination Council (FFIEC). In doing so, the Agencies will continue to seek to minimize impediments to the electronic delivery of financial products and services even as other regulations may be required to ensure the lawful uses of those products or services, such as the provisions that will be implemented under the Uniting and Strengthening America by Providing Appropriate Tools Required to Intercept and Obstruct Terrorism Act of 2001 (USA PATRIOT ACT). The Agencies will foster growth of these activities in a manner that is safe and sound and helps ensure consumer acceptance and protection.

¹ Pub. L. 106-102, 113 Stat. 1338, 1476 (1999).

Part I

Background and Methodology

A. Background

Section 729 of the GLB Act requires the Board, FDIC, OCC, and OTS to conduct a study of banking regulations regarding the delivery of financial products and services. Section 729 further requires the Agencies to report their recommendations on adapting existing legislative or regulatory requirements to online banking and lending.

Even prior to the enactment of section 729 of the GLB Act, each Agency had undertaken several initiatives to adapt its regulations to facilitate and support the online delivery of financial products and services. Moreover, following the Act, the Agencies jointly developed regulations and guidance that are designed to facilitate the electronic delivery of financial products and services. For example, the Agencies recently issued the Interagency Guidelines Establishing Standards for Safeguarding Customer Information, under section 501 of the Act, that accommodate the needs for financial institutions to adopt new electronic technologies to provide financial products and services to their customers.² In addition, through the FFIEC, the Agencies issued guidance on authentication in the electronic banking environment.³

Finally, on June 30, 2000, the President signed into law the Electronic Signatures in Global and National Commerce Act (E-Sign Act),⁴ which was designed to encourage the continued expansion of electronic commerce. The E-Sign Act generally provides that a record or signature will not be invalid solely because it is in electronic form, rather than in a paper or customarily handwritten form. In addition, the E-Sign Act provides that maintaining electronic records may satisfy record retention requirements, provided that those records meet certain conditions. The E-Sign Act also contains special rules applicable to some consumer disclosure requirements that permit the use of electronic records. The E-Sign Act is

² 66 Fed. Reg. 8616 (Feb. 1, 2001). These guidelines implement the requirements of section 501(b) of the GLB Act, 113 Stat. at 1436-37, *codified at* 15 U.S.C. § 6801.

³ Board of Governors' Division of Banking Supervision and Regulation, SR Letter 01-20 (SUP) (Aug. 15, 2001), FDIC FIL-69-2001 (Aug. 24, 2001), OCC Advisory Letter No. 2001-8 (July 30, 2001), OTS CEO Memorandum No. 143 (Aug. 8, 2001).

⁴ Pub. L. 106-229, 114 Stat. 464 (2000), *codified at* 15 U.S.C. § 7001 *et seq.*

enforceable by its own terms; implementing regulations are not required. In fulfilling their obligations under other statutes, including the promotion of safe and sound banking practices, the Agencies will act consistent with the terms and purposes of the E-Sign Act.

B. Methodology

To satisfy the requirements of section 729 of the Act, each Agency conducted a full review and analysis of its regulations that could affect the online delivery of financial services. Each of the Agencies separately reviewed its regulations and certain supervisory policies that relate to the delivery of financial products or services to assess their suitability for transactions that are conducted through electronic media. The Agencies jointly reviewed interagency regulations.

To assist this review, each Agency published in the *Federal Register* a request for comment on a wide range of issues that bear on delivering financial products and services over the Internet to assess whether any of its respective regulations should be amended to facilitate online banking and lending.⁵ In addition, the Agencies sought comment on how particular statutory provisions affect the online delivery of financial products and services.

After reviewing their respective regulations, the Agencies determined that the report should focus on those regulations (or other supervisory policies) that present issues with respect to the online delivery of financial products or services to individual or business customers. In this way, the Agencies have endeavored to tailor the report to address key issues, common problems raised by the comments, and other aspects of banking regulations with respect to the electronic delivery of financial products and services, instead of a wide-ranging examination of all of the Agencies' regulations. Furthermore, the Agencies determined that, absent any compelling issues raised by the comments, the report should not address other

⁵ 65 Fed. Reg. 4895 (Feb. 2, 2000) (OCC); 66 Fed. Reg. 27,912 (May 21, 2001) (Board); 66 Fed. Reg. 31,186 (June 11, 2001) (OTS); 66 Fed. Reg. 34,855 (July 2, 2001) (OCC); 66 Fed. Reg. 37,029 (July 16, 2001) (FDIC). The Appendix includes copies of the *Federal Register* publications. The Board also solicited comments relating to the section 729 study and report as part of its publication of interim final rules to establish uniform standards for the electronic delivery of disclosures to consumers under the consumer financial services regulations administered by the Board (Regulations B, E, M, Z and DD). 66 Fed. Reg. 17,779; 66 Fed. Reg. 17,786; 66 Fed. Reg. 17,322; 66 Fed. Reg. 17,329; 66 Fed. Reg. 17,795 (Mar. 30 and Apr. 4, 2001).

regulations, such as those that will be issued under the recently enacted USA PATRIOT ACT, that will be the subject of a future rulemaking proceeding.

Part II

Jointly Administered Regulations

A. Appraisal Standards for Federally Related Transactions

Under title XI of the Financial Institutions Reform, Recovery, and Enforcement Act of 1989, 12 U.S.C. § 3331 *et seq.*, the Agencies promulgated regulations that provide protection for federal financial and public policy interests in real estate-related transactions by requiring appraisers to perform written real estate appraisals in accordance with uniform standards.⁶ For the sake of simplicity in this report, we refer to the rule as the “Appraisal Rule.” Under the rule, appraisers must demonstrate competency and their professional conduct must be subject to effective supervision. The Appraisal Rule applies to all federally related transactions entered into by the Agencies or by institutions regulated by the Agencies. The Appraisal Rule generally:

- Identifies the real estate-related financial transactions that require the services of an appraiser;
- Prescribes the categories of federally related transactions that a State certified appraiser must appraise and the categories a State licensed appraiser must appraise; and
- Prescribes minimum standards for the performance of real estate appraisals in connection with federally related transactions under the jurisdiction of the Agencies.

1. Analysis

Some commenters recommended that the Agencies exempt from the written appraisal requirement loans processed using an automated underwriting system selected pursuant to an institution’s required board-approved real estate lending policy. Commenters also asserted that the \$250,000 threshold for requiring the use of state licensed or certified appraisals is outmoded. However, under existing rules, any loan underwritten to standards established by Fannie Mae and Freddie Mac is exempt. Moreover, a commenter who has studied the industry commented

⁶ 12 C.F.R. parts 34 (OCC), 225 (subpart G) (Board), 323 (FDIC), and 564 (OTS).

that simply switching from a paper-based format to an automated, paperless one would not solve all appraisal issues about whether the current system of appraisals is the optimal one.

2. Conclusion

The Agencies have not identified any provisions of the Appraisal Rule that impede online banking or that need amendment to facilitate online banking.

B. Community Reinvestment

In 1977, Congress enacted the Community Reinvestment Act (CRA), 12 U.S.C. § 2901 *et seq.*, to encourage federally insured banks and thrifts to help meet the credit needs of their entire communities, including low- and moderate-income neighborhoods, consistent with safe and sound banking practices. The Agencies' joint rule implements the CRA.⁷

1. Analysis

In connection with this study and report, a few commenters noted that the CRA regulations have implications for online banking and lending. For example, one commenter observed that geographical proximity to a financial institution's service facility, such as an institution's branch, may not serve as an appropriate criterion for evaluating whether the institution is able to serve the credit needs of a particular group of consumers.

On July 19, 2001, the Agencies issued a Joint Advance Notice of Proposed Rulemaking (ANPR) as part of their review of the CRA regulations.⁸ The Agencies sought public comment on a wide range of issues concerning the CRA, including suggestions for revising the CRA regulations and on other steps the Agencies might undertake instead of, or in addition to, revising the regulations. One of the issues discussed in the Joint ANPR is how to define the assessment areas.

The CRA regulations provide that an assessment area is the geographic area in which the Agencies evaluate an institution's record of meeting the credit needs of

⁷ See 12 C.F.R. parts 25 (OCC), 228 (Board), 345 (FDIC), and 563e (OTS).

⁸ 66 Fed. Reg. 37,602.

its community under the CRA. An institution's assessment area generally consists of one or more metropolitan statistical areas or one or more contiguous political subdivisions, and includes geographies where the institution has its main office, branches, and deposit-taking ATMs, as well as surrounding geographies where the institution has originated or purchased a substantial portion of its loans. Through the Joint ANPR, the Agencies sought comment on whether the assessment area provisions provide a reasonable and sufficient standard for designating the communities within which the institution's activities will be evaluated during an examination. The Agencies noted that members of the public have questioned the continued appropriateness of delineating geographically defined assessment areas in light of the increasing use of channels such as the Internet to serve widely dispersed markets and to gather deposits and deliver products and services without using deposit-taking branches or ATMs.

2. Conclusion

The Agencies are addressing CRA issues, including the appropriate standards for defining assessment areas, in the separate CRA rulemaking. Accordingly, the Agencies make no recommendation about regulatory or legislative changes to the CRA in this report. Such recommendations, if any, may emerge as a result of the CRA rulemaking.

C. Consumer Protections for Depository Institution Sales of Insurance

Section 305 of the GLB Act generally requires the Agencies to prescribe customer protection regulations that govern the retail sales practices of any insurance product by a depository institution or any person engaged in insurance sales at an office of or on behalf of the institution. The Agencies implemented section 305 of the GLB Act through regulations that were jointly developed and issued in consultation with the National Association of Insurance Commissioners (NAIC).⁹ The Agencies' respective rules are substantively identical; for the sake of simplicity in this report, we refer to the rule as the "Insurance Rule."

⁹ 65 Fed. Reg. 75,821 (Dec. 4, 2000). The Agencies' rules are codified at 12 C.F.R. parts 14 (OCC), 208 (subpart H) (Board), 343 (FDIC), and 536 (OTS) respectively.

1. Analysis

The Insurance Rule prohibits any institution, or anyone acting on its behalf (a “covered person”), from engaging in any practice that could mislead someone or otherwise cause a reasonable person to reach an erroneous belief about:

- The uninsured nature of any insurance product or annuity;
- The investment risk associated with certain products; and
- The fact that the approval of a credit extension cannot be conditioned on the purchase of an insurance product or annuity from the financial institution, and that the consumer is free to purchase the insurance product or annuity from another source.

The Insurance Rule requires that the covered person provide appropriate insurance disclosures before the completion of the initial sale of an insurance product or annuity to the consumer, as well as a credit disclosure at the time the consumer applies for an extension of credit in connection with which insurance is solicited, offered, or sold. The covered person must obtain from the consumer a written acknowledgment of receipt of the disclosures at the time the consumer receives the disclosures or before the initial purchase of an insurance product or annuity by the consumer. Disclosures must be made orally and in writing, except that oral disclosures are not required for applications received or sales conducted by mail. Similarly, any disclosures provided by electronic media do not have to be provided orally.

The rule specifically authorizes the covered person to provide disclosures electronically, subject to the requirements of section 101(c) of the E-Sign Act, if the consumer affirmatively consents and the covered person makes the disclosures in a format that allows the consumer to retain the disclosures or obtain them later.

2. Conclusion

The Agencies believe that no change to the Insurance Rule is necessary to adapt its requirements to online banking and lending. In the notice of proposed rulemaking, the Agencies specifically invited comment on issues of sales, disclosure, and acknowledgment of receipt of disclosure by electronic means. After considering the comments submitted with respect to those issues, the Agencies addressed those issues in the Supplementary Material published with the final rule and in the rule

itself.¹⁰ The GLB Act mandates that the regulations include requirements to provide disclosures and obtain an acknowledgment by the consumer and permits the Agencies to adjust those requirements to suit transactions conducted in electronic media. The Agencies believe that, in accordance with the statute, the final rule contains appropriate adjustments to the disclosure and acknowledgment requirements to facilitate online banking and lending as discussed above.

D. Loans in Areas Having Special Flood Hazards

Pursuant to the National Flood Insurance Act of 1968 and the Flood Disaster Protection Act of 1973, as amended, the Agencies promulgated regulations that prohibit financial institutions from making certain loans if the collateral is located in a special flood hazard area unless the collateral is covered by flood insurance.¹¹ The Agencies' regulations also prescribe requirements about how a financial institution must inform a borrower of the insurance requirement for the loan.

1. Analysis

The Agencies' flood insurance regulations expressly permit a financial institution to use a computerized or electronic flood hazard determination form. Similarly, an institution may deliver electronically the notice of changes in servicer to the insurance company issuing the flood insurance policy, if acceptable to the insurance company. However, the regulations require the institution to provide the borrower with a written, physical copy of the notice of special flood hazards.¹²

The Agencies note that the requirement to provide a written notice of special flood hazards to a borrower is affected by the E-Sign Act. That statute, by its own force, permits a financial institution to satisfy that notice requirement by providing the notice in electronic form in lieu of a physical, written copy. Before the financial institution may do so, it must comply with the provisions of section 101(c) of the E-Sign Act. Among other requirements, section 101(c) mandates that the

¹⁰ 65 Fed. Reg. at 75,827-29; *see, e.g.*, 12 C.F.R. § 14.40(c)(4).

¹¹ 42 U.S.C. § 4104a. The Agencies' regulations are codified at 12 C.F.R. parts 22 (OCC), 339 (FDIC) and 572 (OTS) and § 208.25 (Board), respectively.

¹² Notwithstanding this requirement with respect to the borrower, the lender may provide the *servicer* an electronic copy of the notice of special flood hazards.

consumer must have “affirmatively consented” to the use of an electronic record in lieu of a physical, written notice.

2. Conclusion

The Agencies have determined that, at this time, the flood insurance regulations do not impose any undue burden that limits a financial institution’s ability to provide loans or other financial products or services on line. Nevertheless, the Agencies may consider amending the interagency rule to clarify the conditions for providing an electronic, instead of written, notice of special flood hazards to a borrower.

E. Management Official Interlocks

The Agencies jointly implemented regulations under the Depository Institutions Management Interlocks Act. 12 U.S.C. § 3201 *et seq.* The Agencies’ respective rules are substantively identical; for the sake of simplicity in this report, we refer to the rule as the “Management Interlocks Rule.”¹³

1. Analysis

The Management Interlocks Rule generally prohibits a management official of a depository organization from serving as a management official of an unaffiliated depository organization if the depository organizations in question or its affiliate have offices in the same community or relevant metropolitan statistical area. *See, e.g.*, 12 C.F.R. § 212.3(a). The rule defines a “community” as “a city, town, or village, and contiguous and adjacent cities, towns, or villages.” *See, e.g.*, 12 C.F.R. § 212.2(c). Similarly, the rule defines a “relevant metropolitan statistical area” as a primary or consolidated metropolitan statistical area, as defined and applied by the Office of Management and Budget.

One commenter noted that the definitions of “community” and “relevant metropolitan statistical area” are predicated on conceptions of geography. The commenter suggested that the Agencies should consider revising these geographic limitations to suit financial institutions that deliver products and services through the Internet.

¹³ *See* 12 C.F.R. parts 26 (OCC), 212 (Board), 348 (FDIC), and 563f (OTS).

2. Conclusion

The Agencies recognize that the Management Interlocks Rule is based upon conceptions of geography, as mandated by the statute, that may not apply to financial institutions engaged in online banking and lending. Nevertheless, the Agencies believe that the geographic limitations have a minimal impact, if any, upon the online delivery of financial products and services. The Agencies believe that the Management Interlocks Rule sufficiently suits the purpose of preventing anti-competitive practices as determined by customary measures of banking products and services in a local market. Because an alternative analysis of the competitive effects of institutions that offer financial products and services over the Internet has not been developed, the Agencies believe that it would be premature to consider changes to the Management Interlocks Rule that would apply to a competitive environment that includes online banking and lending. Accordingly, the Agencies have determined that amendments to the statute or the rule would be unnecessary at this time.

F. Privacy of Consumer Financial Information

The Agencies implemented the privacy provisions of Subtitle A of Title V of the GLB Act through regulations that were jointly developed and issued in coordination with the National Credit Union Administration, the Federal Trade Commission, and the Securities and Exchange Commission. The Agencies' respective rules are substantively identical; for the sake of simplicity in this report, we refer to the rule as the "Privacy Rule."¹⁴

1. Analysis

The GLB Act generally requires a financial institution to provide notices to its consumers that describe its privacy policies and practices and, where applicable, allow a consumer to opt out of disclosures of nonpublic personal information to nonaffiliated third parties. The GLB Act requires that a financial institution provide notices "in writing or in electronic form or other form permitted by the regulations." *See, e.g.*, 15 U.S.C. § 6803(a). The Privacy Rule facilitates the electronic delivery of financial products and services by allowing a financial institution to deliver its notices online, provided that it satisfies certain conditions.

¹⁴ *See* 12 C.F.R. parts 40 (OCC), 216 (Board), 332 (FDIC), and 573 (OTS).

In particular, the Privacy Rule generally allows a financial institution to deliver the applicable notices electronically only if the consumer agrees.

The Agencies received several comments regarding the Privacy Rule; we address those issues below.

a. Providing “clear and conspicuous” notices over the Internet

Section 503 of the GLB Act (15 U.S.C. § 6803) requires a financial institution to deliver a notice of its privacy policies and practices to a consumer at the time of establishing a customer relationship and annually thereafter. The Privacy Rule refers to these notices as an “initial notice” and “annual notice,” respectively.

Section 502 (15 U.S.C. § 6802) generally prohibits a financial institution from disclosing nonpublic personal information about a consumer to any nonaffiliated third party unless the institution provides the consumer with an initial notice and a reasonable opportunity to opt out of that disclosure. The privacy regulation refers to the notice that describes the consumer’s right to opt out of disclosures to nonaffiliated third parties as an “opt out notice.”

The Privacy Rule mandates that the initial, annual, and opt out notices be “clear and conspicuous,” and defines that requirement as “reasonably understandable and designed to call attention to the nature and significance of the information in the notice.” This provision does not prescribe specific requirements for written or online notices. Rather, several examples illustrate how a financial institution may comply in various media, such as the use of a “plain-language heading to call attention to the notice” and the use of “distinctive type size, style, and graphic devices, such as shading or sidebars” when the notice is combined with other information. The rule also includes an example that is tailored to notices that a financial institution provides on its web site(s).¹⁵

¹⁵ Section __.3(b)(2)(iii) of the Agencies’ Privacy Rule provides: “If you provide a notice on a web page, you design your notice to call attention to the nature and significance of the information in it if you use text or visual cues to encourage scrolling down the page if necessary to view the entire notice and ensure that other elements on the web site (such as text, graphics, hyperlinks, or sound) do not distract attention from the notice, and you either: (A) Place the notice on a screen that consumers frequently access, such as a page on which transactions are conducted; or (B) Place a link on a screen that consumers frequently access, such as a page on which transactions are conducted, that connects directly to the notice and is labeled appropriately to convey the importance, nature, and relevance of the notice.”

Several commenters urged the Agencies to modify the “clear and conspicuous” standard to accommodate the delivery of financial products and services via non-traditional computing devices, such as wireless handheld computers. Relative to standard desktop computers, handheld devices have smaller screens that require information to be displayed in smaller or altered formats. One commenter believed that the Agencies should clarify the Privacy Rule to state where notices are available to consumers via customary personal computers, a financial institution should not have to ensure that secondary access through wireless devices meets the same standard of “clear and conspicuous” as would apply to notices that are accessed via a personal computer.

As noted above, the Privacy Rule does not prescribe specific requirements for written or online notices. Nevertheless, the Agencies may consider providing guidance to illustrate how the standard of “clear and conspicuous” applies to delivering notices over smaller computing devices.

b. Applicability of the E-Sign Act

One commenter asked the Agencies to address whether the consumer consent provisions of the E-Sign Act apply to the notices required under the privacy provisions of the GLB Act. The commenter asserted that “[s]ome confusion” has arisen over whether an institution must comply with the E-Sign Act when it is required to provide a notice under the GLB Act and the Privacy Rule. The commenter urged the Agencies to amend the Privacy Rule to expressly state that the E-Sign Act does not apply to any notices required under the GLB Act that are delivered electronically in accordance with the Privacy Rule.

The provisions of the E-Sign Act that regulate disclosures to consumers apply “if a statute, regulation, or other rule of law requires that information relating to a transaction or transactions in or affecting interstate or foreign commerce be provided or made available to a consumer in writing.” 15 U.S.C. § 7001(c). After gathering more experience implementing the Privacy Rule, the Agencies will be prepared to assess whether any additional actions would be appropriate to clarify the applicability of the E-Sign Act to the privacy provisions of the GLB Act.

2. Conclusion

Based upon the review of the privacy provisions of the GLB Act and the Privacy Rule, and the comments submitted in connection with this study, the Agencies conclude that none of the provisions of the GLB Act or the regulation impose any

undue burden that limits a financial institution's ability to provide financial products or services on line. The Agencies may consider including additional examples or issuing other guidance that aims to clarify how a financial institution may satisfy its obligations under the Privacy Rule through various electronic media.

Part III

Regulations Administered by the Board of Governors of the Federal Reserve System

A. Electronic Delivery of Disclosures under Various Consumer Financial Services Regulations Administered by the Board

1. Overview

As early as the mid-1990s, the Board recognized the potential benefits of electronic commerce to both consumers and the financial services industry. In 1996, the Board amended Regulation E (Electronic Fund Transfers) to permit electronic authorizations for preauthorized debits from consumers' deposit and other asset accounts. Since that time, the Board has exercised its authority under the consumer financial services laws that it administers to permit electronic delivery of certain disclosures. For example, in 1997, the Board interpreted the written-disclosure requirement under Regulation CC (Expedited Funds Availability) to permit electronic disclosures, and interpreted Regulation Z (Truth in Lending) to permit the electronic delivery of periodic statements. In 1998, the Board issued an interim rule permitting all disclosures under Regulation E to be provided electronically and, in 1999, the Board issued an interim rule under Regulation DD (Truth in Savings) permitting deposit account disclosures on periodic statements to be provided electronically.

In August 1999, the Board issued proposed rules permitting electronic delivery of *all* disclosures (for example, via e-mail or at a web site) that under the Board's consumer financial services regulations are required to be in writing. The proposals required institutions to obtain consumers' consent to receive electronic disclosures by requiring a standardized consent form identifying the types of disclosures to be delivered electronically, how to access them, and other information deemed necessary for consumers to make informed decisions about electronic delivery.

The E-Sign Act, which became law in June 2000, established the legal validity and enforceability of electronic signatures, contracts, and other records (including consumer disclosures). The E-Sign Act superseded much of the Board's rulemakings but contained a consent requirement similar to that proposed by the Board. The E-Sign Act authorizes the electronic delivery of written records

required by law to be provided or made available to a consumer if an institution obtains the consumer's consent in accordance with the E-Sign Act's requirements.

In March 2001, the Board published interim final rules under Regulations B, E, M (Consumer Leasing), Z, and DD to incorporate the requirements of the E-Sign Act by reference. Under the interim final rules, financial institutions, creditors, lessors, and others may use electronic disclosures if they obtain consumers' consent in accordance with the requirements of section 101(c) of the E-Sign Act. The Board's interim final rules also establish uniform requirements for satisfying the timing and delivery requirements of the consumer financial services laws when electronic disclosures are used.

Under the interim final rules, electronic disclosures may be provided by e-mail or they can be made available at another location, such as an institution's web site. If a disclosure—such as an account statement or a notice of a change in account terms—is provided at a web site, an institution must notify the consumer of the disclosure's availability by e-mail. The disclosure must remain available for 90 days, not necessarily at the same location, to allow consumers adequate time to access and retain the information. In addition, when a disclosure sent by e-mail to a consumer is returned undelivered, the interim rule requires the institution to take reasonable steps to attempt redelivery using the information in its files. This requirement is satisfied if, for example, the institution sends the disclosure or notice to a different e-mail or postal address that the institution has on file.

2. Analysis

In connection with the March 2001 interim final rules, the Board also requested comment on whether other regulatory or legislative changes are needed to facilitate online banking and lending. Only a few comments were received on the study, which mostly focused on the Board's interim final rules. In May, the Board solicited comments specifically on the section 729 study. The Board received approximately twenty-five comment letters; most of the comments concerning the Board's consumer financial services regulations focused on the March 2001 interim final rules and mirrored the comments received earlier.

The Board's consumer financial services regulations generally require that institutions "send," "provide," or "deliver" disclosures to consumers as opposed to merely making the disclosures available. The requirement typically is satisfied by mailing disclosures to a postal address designated by the consumer. Where

disclosures are provided electronically, sending disclosures to a consumer's e-mail address would satisfy this requirement.

The Board has recognized, however, that because of security and privacy concerns associated with data transmissions, institutions may choose to make the disclosures available at their web sites, where consumers may retrieve them under secure conditions. The Board's rulemakings on electronic disclosures, therefore, have not required institutions to send the required disclosures by e-mail, but have also allowed institutions to make the disclosures available at another location, such as an Internet web site.

In allowing disclosures to be made available in this manner, the Board also considered whether additional rules might be necessary to ensure their effective delivery. For example, the Board believes that consumers should not be required to initiate a search of the web site of each financial institution with which an account is held to determine whether a disclosure has been made available. Consumers who receive disclosures by accessing an institution's web site should be alerted when the information is first available in order to ensure that they have the opportunity to access the information before it is removed.

Accordingly, to ensure effective delivery, when disclosures are not sent to the consumer's e-mail address, a notice alerting the consumer of the disclosures' availability must be sent to the consumer's e-mail address in a timely fashion. The consumer's e-mail address is defined as a location where the consumer can also receive messages from parties other than the institution.

a. Alert notices

Several commenters objected to the interim final rules' requirement that alert notices be sent to the consumer's e-mail address when disclosures are posted on a web site. Commenters that were opposed to the alert notice requirement asserted that some consumers do not have an e-mail address (and may not want to sign up for one, due to cost or other reasons), or they may have an e-mail address but prefer not to receive account information there. Commenters were also concerned that some consumers would not update their e-mail address on file with the institution when their address changes, causing problems with attempts to send disclosures or notices via e-mail. Some commenters thought that the costs of developing an e-mail system for alert notices could be prohibitive for certain institutions. Some large institutions, however, have stated that they already use e-mail to send notices and disclosures to consumers.

Several commenters believe the requirement for sending alert notices when disclosures are made available at a web site is inconsistent with the E-Sign Act because it imposes an additional requirement for using electronic disclosures. They also believe that alert notices are unnecessary where a consumer receives a disclosure at the time the consumer completes an online transaction such as consummating a loan or opening a credit card or deposit account.

b. Redelivery requirement

A related area of concern was the requirement to redeliver a disclosure sent to a consumer's e-mail that was returned undelivered. The institution must take reasonable steps to attempt redelivery using the information in its files. Some commenters believe that institutions should not be required to send disclosures to another address on file that has not been designated by the consumer for that purpose. These commenters also stated that if the only other address on file is a postal address, the interim rule would result in a requirement for paper disclosures, which they believe is inconsistent with the E-Sign Act.

Other commenters expressed the view that the burden should rest with the consumer to ensure that the institution has the consumer's correct e-mail address and that financial institutions should be allowed to rely on procedures that allow consumers to provide the updated address information. At a minimum, commenters urged the Board to clarify that financial institutions may make a second attempt to deliver the disclosure to the same e-mail address because the e-mail service could have been temporarily unavailable.

c. "Reasonable demonstration"

The Board's interim final rules permit financial institutions to deliver disclosures electronically, provided that the consumer consents in accordance with the E-Sign Act's requirements. Under the E-Sign Act, the consumer must consent electronically, or confirm his or her consent electronically, in a manner that "reasonably demonstrates" that the consumer can access the electronic record in the format used by the institution. One commenter requested that the Board provide additional clarification of the E-Sign Act's "reasonable demonstration" requirement. The commenter believes that the need to ensure that the consumer can access electronic disclosures should not create undue burdens that might discourage consumers from obtaining financial products and services online. Another commenter observed that the requirement for consumers to reasonably demonstrate that they have the ability to access the disclosures is counter to the E-

Sign Act's premise that electronic and paper disclosures should be treated the same. Accordingly, this commenter suggested that the Congress delete this requirement.

d. Preemption

Several commenters urged the Board to confirm that financial institutions that comply with the E-Sign Act do not need to comply with additional or different requirements imposed under state law when providing electronic disclosures under the Board's consumer financial services regulations. Commenters also asked the Board to clarify that where the Board has determined that the E-Sign Act's consumer consent provision (§ 101(c)) does not apply to certain disclosures (*e.g.*, disclosures in connection with advertisements, or credit and charge card applications and solicitations), state law may not require consumer consent with respect to those disclosures. They believe that uniform federal law would promote electronic commerce.

One commenter noted that section 102(a) of the E-Sign Act grants limited authority to states, with respect to their own laws, to enact their own electronic writing and signature requirements under certain conditions. This commenter believes that this authority could result in state law requirements that create significant impediments for institutions that conduct electronic transactions in multiple states that have varying writing and signature requirements.

3. Conclusion

In general, comments received on the section 729 study have raised the same issues that were raised in connection with the March 2001 interim final rules and request for comment. The Board lifted the October 1, 2001 mandatory effective date for compliance with the interim final rules in response to comments received on the March 2001 rules stating that additional time was needed to make operational changes. Furthermore, the Board may consider adjustments to the rules to provide additional flexibility. Financial institutions may continue to provide electronic disclosures under their existing policies and practices (in accordance with the E-Sign Act), or they may follow the interim final rules until permanent final rules are issued.

With respect to the preemption issues raised, the Board believes that it is premature to make any recommendation concerning whether Federal law should preempt State law in these areas.

B. Regulation B (Equal Credit Opportunity) and Regulation C (Home Mortgage Disclosure)

1. Overview

Regulation B prohibits discrimination in any aspect of a credit transaction on the basis of national origin, marital status, religion, gender, color, age, race, receipt of public assistance funds, and exercise of any right under the Consumer Credit Protection Act.

Regulation C requires mortgage lenders in metropolitan areas to disclose to the public data about home purchase and home improvement loans (including refinancings) that lenders originate or purchase and about the disposition of applications for such loans. Lenders collect and report data about each application or loan, each applicant or borrower (including national origin or race, gender, and annual income), and each property (including occupancy status and location).

2. Analysis

Section 202.13 of Regulation B generally requires a creditor that receives an application for credit for the purchase or refinancing of a consumer's primary residence to collect as part of the application certain information about the applicant (*e.g.*, national origin or race, marital status, and gender). Similarly, section 203.4 of Regulation C generally requires financial institutions to collect data about the national origin, gender, and race of applicants for home purchase and home improvement loans. The commentaries for both regulations provide that if an application is taken over the phone, creditors need not collect monitoring information under Regulations B and C. If an application is taken by mail, the creditor must request the information, but the applicant need not provide it. One commenter noted that if online credit applications are treated like mail or telephone applications, then information about applicant characteristics may not be reported and thus it will be more difficult to identify discriminatory lending practices.

The collection of monitoring information is essential in enhancing the transparency of creditor lending practices. As more applications are being taken by telephone, by mail, and over the Internet, however, less information about applicant characteristics is being provided by consumers, while at the same time, lenders cannot make visual observations. In August 1999, as part of a comprehensive review of Regulation B, the Board proposed to treat online credit applications similarly to applications taken by mail. Therefore, a creditor would have to request

monitoring information on the online application form, but if the consumer chose not to provide the information, the creditor would not be required to make an additional request to the applicant. (This interpretation is consistent with the current interpretation under Regulation C.) No final action has been taken on this rulemaking.

3. Conclusion

The Board will monitor developments in online credit applications for both Regulations B and C reporting requirements and will consider adjustments to the rules where appropriate.

C. Regulation E (Electronic Fund Transfer Act), Regulation Z (Truth in Lending Act), and Regulation DD (Truth in Savings Act)

1. Overview

Regulation E establishes rules about the disclosure of terms and conditions of electronic fund transfer (EFT) services; limitations on a consumer's liability for unauthorized use of debit cards; restrictions on the unsolicited issuance of debit cards; documentation of EFTs by means of receipts and periodic account activity statements; and procedures for error resolution. The regulation covers transactions at automated teller machines, point-of-sale terminals in stores, telephone bill-payment plans, and preauthorized transfers to and from a customer's account, such as direct deposit of salary and social security benefits.

Regulation Z promotes the informed use of consumer credit by requiring disclosures about its terms and cost. The regulation also gives consumers the right to cancel certain credit transactions that involve a lien on a consumer's principal dwelling, regulates certain credit card practices, and provides a means for fair and timely resolution of credit billing disputes.

Regulation DD requires institutions to disclose yields, fees, and other terms concerning deposit accounts to consumers at account opening, upon request, when changes in terms occur, and in periodic statements. The regulation also covers advertising for deposit accounts and prohibits certain methods of calculating interest.

2. Analysis

In responding to the Board's request for comment on whether additional legislative or regulatory changes are needed to further facilitate the electronic delivery of consumer financial services, many commenters raised issues that apply to more than one regulation. For example, many commenters addressed requirements for periodic statements and advertising under Regulations Z and DD. To streamline the discussion on issues that apply to multiple regulations, the discussion of Regulations E, Z, and DD has been consolidated in this subsection. Where appropriate, comments received on issues that are unique to a specific regulation are also addressed.

a. Periodic statements under Regulations E, Z and DD

The Board specifically solicited comment on whether the rules for periodic account activity statements on deposit and credit accounts should be modified for online banking and lending. Several commenters stated that it was not necessary at this time to modify the rules for periodic statements to specifically apply to the electronic environment. One commenter noted that periodic statements perform multiple functions in addition to providing transaction summaries which are typically available online. This commenter stated, for example, that it would be difficult to manage the error resolution process under Regulations E and Z without actual statement cycle dates and beginning and ending balances. In addition, it would be unclear how an annual percentage yield earned under Regulation DD could be calculated if beginning and ending balances were not provided on a statement cycle basis.

In contrast, a few commenters urged the Board to modify or eliminate the rules for periodic statements when institutions provide transaction information on a daily basis. These commenters believed that the value of providing disclosures based on a particular "statement period" or beginning and ending dates is questionable when customers can view their account and transaction history online at any time.

Other commenters suggested that it would be appropriate to permit financial institutions to deliver modified periodic statements electronically that provide links or access instructions to disclosures that are continuously available. For example, to comply with periodic statement requirements under Regulations E and Z, a financial institution could provide links to error resolution disclosures that are posted on a continuous basis on a web site. Similarly, a link between a daily transaction summary and the periodic statement could be used. In addition, one

commenter recommended that consumers should have a legal right to waive delivery of periodic statements if they already have this information available in their online banking history.

Two commenters argued that the Board's periodic statement requirements under Regulation E are hindering the development of certain electronic products and services such as stored-value cards, account aggregation services, and electronic/Internet cash exchange. In particular, these commenters argue that the periodic statement requirements in connection with these services presented unnecessary technical and compliance burdens that have slowed the development and maintenance of these emerging products and services.

The Electronic Fund Transfer Act (EFTA) requires the Board in issuing regulations to take into account, and allow for, the continuing evolution of electronic banking services and the technology used in such services. The Board is aware that the application of certain provisions of the EFTA and Regulation E, including the requirement to provide periodic account activity statements, could impose significant compliance costs and impact the development of electronic payment products, such as stored-value cards. The Board has modified Regulation E periodic statement and other requirements to accommodate the development of specific EFT services, such as electronic benefit transfer accounts.

The Board does not believe that there is a need to modify the general statutory requirements under Regulations E, Z, and DD concerning disclosures in periodic statements at this time. The daily transaction summaries that consumers may access online are not adequate substitutes for the periodic statements required by statute. These disclosure statements provide uniform information to consumers about the overall costs of credit, EFT services, or interest earned on an account for a particular period and thus allows consumers to evaluate, for example, whether a particular credit card or deposit account continues to suit their financial needs.

In recent rulemakings, the Board has provided guidance on the electronic delivery of periodic statements. The Board will provide additional guidance in this area as necessary and provide additional flexibility as warranted.

b. Error resolution and preauthorized transfers under Regulation E

Commenters addressed issues concerning error resolution and liability for unauthorized transfers. The EFTA and section 205.11 of Regulation E sets out detailed error-resolution procedures. Several commenters observed that any new

kinds of statements and electronic methods of delivering statements might require an adjustment to the error resolution timing requirements. For example, one commenter suggested that for online banking, it may be appropriate to begin the time period by which a consumer would be required to notify his or her financial institution of a billing error or unauthorized transfer after some reasonable period of time in which the consumer would be expected to view his or her daily online statements.

Section 205.10(b) of Regulation E requires a consumer's financial institution or payee to provide advance notice to the consumer whenever a preauthorized EFT from the consumer's account will vary in amount from the previous transfer under the same authorization or from the preauthorized amount. The consumer may have the option, however, of receiving notice only when a transfer falls outside an agreed-upon range or when a transfer differs from the most recent transfer by more than an agreed-upon amount.

One commenter believes that this notice requirement may impede electronic initiatives. The commenter asks the Board to consider revising the rule to allow institutions to debit a consumer's account based on a computable amount or percentage, as opposed to a specific dollar amount or range of dollar amounts, or by reference to the entire balance or the total amount currently due.

The Board believes that the rule currently provides sufficient flexibility for financial institutions. The Board has not observed a significant compliance problem to date with the current provisions of the rule, but will consider this issue as part of a future review of the regulation.

c. Issues that apply to Regulation Z

1) “Clear and conspicuous” and format requirements for electronic credit card solicitations

Section 226.5a of Regulation Z requires credit card issuers to provide clear and conspicuous disclosures of the terms of the credit account on or with a card solicitation or application. Some commenters observed that it was unclear how to meet certain of the provision's format requirements in an electronic environment. In particular, section 226.5a(b)(1) requires the annual percentage rate for purchases to be disclosed in at least 18-point type to the consumer. These commenters noted that because creditors have no control over how disclosures will appear on the consumer's computer screen, they should not have a duty to ensure that a

consumer views the disclosures in the context of the format and type size requirements.

The Board has addressed this concern in a prior rulemaking. *See* 65 Fed. Reg. at 58,906 (Oct. 3, 2000). The Board's official staff commentary to Regulation Z generally provides that disclosures transmitted electronically satisfy the clear and conspicuous standard based on the form in which the disclosures are provided. Thus, a creditor may satisfy the clear and conspicuous standard by displaying the disclosures in a credit card solicitation at its web site in a large type size, regardless of the size of the device used by a consumer to view the disclosures.

2) Prompt crediting of payments

Section 226.10 of Regulation Z requires a creditor to credit a payment to a consumer's account as of the date of receipt. The rule permits a creditor to specify the requirements for making payments, including setting a cut-off hour for payments to be considered received on a particular day. Given the emerging technologies for processing electronic payments, the Board may in the future consider whether adjustments to the rule for crediting payments are necessary.

3) Advertising

Regulations Z and DD contain provisions that ensure that advertisements are not misleading or inaccurate, with regard to the account terms actually offered by the institution. For example, the regulations specify that if an advertisement contains certain account terms, then the advertisement must also include other specified terms. There are special rules permitting abbreviated disclosures for broadcast media advertisements to account for time and space restrictions.

Some commenters urged the Board to extend the rules for broadcast media advertising to Internet advertisements. Several commenters cautioned against applying the advertising requirements to disclosures accessed by hand-held wireless devices because of the potential cost and the difficulty in presenting the disclosures in an easy to read format. One commenter believes that because Internet technology allows institutions to provide a wealth of information to consumers, the Board should amend its advertising regulations to require institutions to provide more information about terms in advertisements.

More generally, one commenter urged the Board to publish a compliance guide containing the rules for electronic advertising that would apply to all the consumer financial services regulations administered by the Board.

The Board has considered certain aspects of electronic advertisements in connection with its interim final rules on electronic delivery of disclosures. For example, the Board has previously determined that rules for broadcast media advertisements in Regulation DD do not apply to web sites. 66 Fed. Reg. 17,795 (Apr. 4, 2001). Nevertheless, additional guidance on aspects of electronic advertisements not covered in the proposals may be appropriate for future regulatory reviews. For disclosures provided on hand-held wireless devices, however, the Board notes that it would be difficult to streamline the required disclosures for such devices without diminishing the effectiveness of the disclosures.

D. Regulation D (Reserve Requirements of Depository Institutions)

1. Overview

Regulation D implements section 19 of the Federal Reserve Act.¹⁶ Regulation D generally requires depository institutions to distinguish between “transaction accounts” and “savings deposits” and to maintain reserves against transaction accounts. Reserve requirements aid in the conduct of open market operations for monetary policy purposes by helping to ensure a stable, predictable demand for reserves, thereby increasing the Board’s control over short-term interest rates. Regulation D also defines “demand deposit” for the purposes of the prohibition of paying interest on demand deposits under Regulation Q.

2. Analysis

Regulation D requires depository institutions to hold reserves against their transaction accounts, generally defined as accounts from which the depositor is permitted to make payments or transfers to third parties.

Depository institutions are not required to hold reserves against savings deposits. Regulation D defines a “savings deposit,” in part, as a deposit or account from which the depositor is limited to no more than six preauthorized, automatic, or telephonic transfers or withdrawals, or combination thereof, per calendar month or

¹⁶ 12 CFR part 204; 12 U.S.C. § 461.

statement cycle. In addition, the regulation provides that “no more than three of the six such transfers may be made by check, draft, debit card, or similar order made by the depositor and payable to third parties.”

Regulation D permits unlimited transfers or withdrawals from savings deposits when such transfers or withdrawals are made by mail, messenger, automated teller machine, in person, or by telephone (via check mailed to the depositor).¹⁷

Commenters noted that the regulation limits the number of transactions from a savings account that a customer may initiate on line because this exception applies only to postal, ATM, or physical means of transfer or withdrawal rather than electronic means, such as a transfer or withdrawal initiated through a bank’s web site. One commenter explained that customers who maintain the bulk of their funds in savings accounts are constrained by Regulation D from making online transfers to transaction accounts to cover possible overdrafts or meeting other unexpected expenses paid to third parties from the transaction accounts.

3. Conclusion

The Board recognizes that Regulation D imposes limitations on the extent to which depositors may make transfers or withdrawals from their savings accounts using online services. To implement section 19 of the Federal Reserve Act, however, the Board must distinguish between transaction accounts and savings accounts. It has made this distinction based on the ease with which the depositor may transfer funds to third parties. The Board recognizes that depository institutions are generally able to offer more attractive interest rates to consumers on savings accounts than on transaction accounts because depository institutions do not have to maintain reserves on savings accounts. (Currently, business customers that are not eligible for NOW accounts are not able to obtain interest-bearing transaction accounts.)

The Board believes that the interest-rate differential between transaction accounts and savings accounts could be reduced by legislation that would permit the payment of interest on reserve and clearing balances held by depository institutions at Federal Reserve Banks. The Board has long supported such a change. In addition, the Board has also long advocated repeal of the prohibition against payment of interest on demand deposits, which would permit businesses to obtain interest-bearing transaction accounts. Legislation is currently pending before the Congress that would accomplish both of these changes.

¹⁷ 12 C.F.R. § 204.2(d)(2).

E. Regulations T and U (Securities Margin Lending)

1. Overview

Regulations T and U implement section 7 of the Securities Exchange Act of 1934.¹⁸ Regulation T applies to extensions of credit by brokers and dealers. Regulation U applies to persons other than brokers and dealers who extend credit for the purpose of buying or carrying margin stock if the credit is secured directly or indirectly by margin stock. The regulations impose, among other obligations, initial margin requirements and payment rules on certain securities transactions.

2. Analysis

Regulation T provides, in general, that every extension of credit shall be deemed to be purpose credit unless the creditor “accepts in good faith from the customer a written statement that it is not purpose credit.”¹⁹ Presently, the Board requires a creditor to collect (and validate) a purpose statement (form T-4).

Regulation U similarly requires a lender that extends credit secured by margin stock to collect and validate a purpose statement. Presently, the Board requires a creditor to file a purpose statement (form U-1 or G-3). Unlike Regulation T, which requires a “written statement,” Regulation U does not specify how that statement must be executed.

3. Conclusion

The Board may consider amendments to Regulation T and U to clarify the purpose statement requirements of the respective regulations under the E-Sign Act.

F. Regulation CC (Availability of Funds and Collection of Checks)

1. Overview

Regulation CC implements the Expedited Funds Availability Act.²⁰ Regulation CC requires a bank to make funds deposited into transaction accounts available for

¹⁸ 12 C.F.R. parts 220 and 221; 15 U.S.C. § 78g.

¹⁹ 12 C.F.R. § 220.6(e)(2).

²⁰ 12 C.F.R. part 229; 12 U.S.C. §§ 4001-10.

withdrawal in accordance with prescribed schedules. The regulation also sets forth rules that govern the collection and return of checks by banks, same-day settlement for certain checks, and liability of banks for failure to comply with its provisions.

In the request for comment, the Board noted that laws or regulations that contain concepts of time may not be relevant in an online environment. The Board asked whether the provisions of Regulation CC that define a “banking day” are appropriate in the context of a customer that opened an account and performs all banking functions online.

2. Analysis

a. Schedule of funds availability and the definition of “banking day”

Regulation CC generally requires funds deposited or received for deposit to be available on specified business days after the “banking day” on which the funds are deposited or received. The term “banking day” is defined as that part of any business day on which an office of a bank is open to the public for carrying on substantially all of its banking functions.²¹ Several commenters agreed with the Board’s suggestion that the term “banking day” may be incompatible with services that may be obtained electronically at any time and on any day. One commenter contended that traditional accounting principles, including definitions of time, may require modification as financial institutions develop continuous processing systems. Nevertheless, customers’ demands for services that would require such continuous processing systems have not emerged at this time. Because re-engineering computer systems to implement continuous processing will be costly, particularly in view of customers’ current expectations about banking services, commenters urged the Board to retain the regulatory provisions that define time. Commenters explained that the definition of “banking day” allows institutions to schedule certain banking functions, such as batch processing of ACH transactions, in a manner that efficiently uses their available resources.

b. Disclosure requirements

Regulation CC contains several provisions that require depository institutions to provide notices to their customers. For example, section 229.16 requires a bank to provide a notice that describes the bank’s policy as to when funds deposited in an

²¹ 12 C.F.R. § 229.2(f).

account are available for withdrawal. Under the general requirements, contained in section 229.15, a bank must provide most notices in writing and in a form that the customer may keep. The commentary to section 229.15 explains that a bank “satisfies the written-disclosure requirement by sending an electronic disclosure that displays the text and is in a form that the customer may keep, if the customer agrees to such means of disclosure.”²² Other notice requirements, such as the notice to a customer when the bank receives a returned check or a notice of nonpayment of a check under section 229.33(d), do not specify the form of the notice.

3. Conclusion

The Board believes that changes to the regulatory definition of “banking day” are not appropriate at this time. Although certain online banking services may be available outside the hours of a normal banking day, most banks are generally not open to the public for carrying on substantially all of their banking functions on a 24-hour basis. Furthermore, most banks have not upgraded to continuous processing systems that would accommodate a more expansive definition of “banking day.” Accordingly, the Board concludes that, at this time, such an amendment is not warranted. The Board will continue to monitor developments in banking practices and technology that may affect such issues. In addition, the Board may consider clarifications to Regulation CC or its commentary regarding the interaction of the regulation’s notice provisions and the E-Sign Act.

The report also summarizes the few suggestions of commenters that certain provisions of the Board’s consumer financial services regulations be modified to better accommodate online lending and banking. The report states that the Board will continue to provide compliance guidance and will consider additional flexibility in the rules as appropriate.

²² 12 C.F.R. part 229, App. E, at IX.A.1., FRRS 9-190.

Part IV

Regulations Administered by the Federal Deposit Insurance Corporation

As required by section 729 of the GLB Act, the FDIC has reviewed all of its regulations that could affect the online delivery of financial services to ensure that they do not impede online or other forms of electronic banking. As part of this review, on July 16, 2001, the FDIC published in the *Federal Register* a request for comment on how its banking regulations affect the online delivery of banking services. 66 Fed. Reg. 37,029. (See Appendix B.) The FDIC asked the public to respond to certain general questions:

- Are there specific regulations the FDIC should modify because they impede the use of a new technology that would allow financial institutions to offer improved products or services in a more efficient manner and at a lower cost?
- Are there areas where financial institutions would benefit from additional clarification of rules or guidance concerning the risks associated with electronic banking activities?
- Are there specific areas in which regulatory changes are needed to enhance consumer acceptance of, confidence in, or access to, electronic banking?

In addition, the FDIC specifically asked for comments on hyperlinking; whether certain terms in its regulations regarding physical location requirements, such as the definition of a bank “branch,” should be revised to deal with electronic banking; whether regulations involving appraisals should be amended to provide for the possibility of online appraisals; and whether the FDIC should promulgate regulations or publish guidance setting forth standards for the use of electronic signatures and records.

The FDIC received comments from 3 associations of financial services providers, 6 financial services firms, a firm that provides software to financial services firms, 3 individuals, and the Conference of State Bank Supervisors (CSBS). Some of the submissions also responded to requests for comment by the other Federal banking agencies, and addressed regulations that the other agencies have that the FDIC does not.

Most commenters cautioned the FDIC not to amend or issue new regulations until this developing area of financial activity has had more time to develop on its own. Only two commenters suggested changes to specific FDIC-only rules. One commenter suggested that the FDIC should amend part 303 of the FDIC's rules to exclude online banking services from the definition of "branch" in 12 C.F.R. § 303.41(a). CSBS recommended that the FDIC work on a joint interagency basis to clarify where a depository institution's Internet banking operations are located. CSBS believes that such an approach would maintain competitive equality among all depository institutions.

In addition, commenters suggested that guidance, or as one commenter termed it, "practical information resources," be issued in certain areas. Commenters cited, as examples of existing helpful guidance, the FDIC's June 4, 2001 Bank Technology Bulletin On Outsourcing (FIL-50-2001) and the FFIEC's July 30, 2001 guidance on Authentication in an Electronic Banking Environment (*see* FDIC FIL-69-2001, Aug. 24, 2001).

As commenters have suggested, electronic banking is a dynamic area that needs an opportunity to develop as much as possible without formal regulation. This has been a guiding principle in the FDIC's review of its regulations, and in the FDIC's approach to electronic banking, predating the enactment of the GLB Act. When the FDIC has been required to issue or amend regulations, the FDIC has tried to structure them so as to avoid obstacles to the growth of online and electronic banking. Otherwise, the FDIC has tried to foster online banking through the training of its own employees and, when necessary, by issuing non-regulation guidance. The purpose of such guidance is to ensure that electronic banking does not engender unreasonable risks without creating impediments to its development. The FDIC issued electronic banking examination procedures in January 1997 and implemented an electronic banking subject matter expert program in April 1997. The Division of Supervision created an Electronic Banking Branch to focus attention on electronic banking supervisory issues in September 2000. In addition, the FDIC has issued a variety of written guidance concerning risks and appropriate procedures for electronic banking. *See, e.g.*, FIL 81-2000, Risk Management of Technology Outsourcing (Nov. 29, 2000); FIL 77-2000, Bank Technology Bulletin, Internet Domain Names (Nov. 9, 2000); FIL 72-2000, Electronic Signatures in Global and National Commerce Act (Nov. 2, 2000); FIL 67-2000, Security Monitoring of Computer Networks (Oct. 3, 2000); FIL 63-2000, Online Banking (Sept. 21, 2000); FIL 131-97, Security Risks Associated with the Internet (Dec. 18, 1997).

The FDIC has not identified any of its rules that would, by its terms, impede online banking. When rulemaking is required, the FDIC will continue to craft rules to avoid unnecessarily impeding online banking, and in individual cases, such as the review of applications, the FDIC will attempt to find interpretations of its rules that will accommodate legitimate activities while fulfilling the rule's purpose. In addition, the FDIC will continue to issue guidance, individually or in conjunction with the other Federal banking agencies and the FFIEC, as necessary to foster online banking without interfering with its safe and sound growth.

Part V

Regulations Administered by the Office of the Comptroller of the Currency

Prior to enactment of section 729, the OCC had made a concerted effort to facilitate and support online delivery of financial services. Recognizing that uncertainty over permissible electronic bank activities could hinder the delivery of online financial services, the OCC sought to provide clear guidance on the scope of these activities through its decisions on bank licensing applications and its legal interpretive letters. The OCC has approved a number of activities involving innovative uses of new technology, including the establishment of transactional Web sites, virtual marketplaces, Internet access services, and electronic payment systems. The OCC has also permitted national banks to provide digital certification, electronic correspondent banking services, and electronic safekeeping. These opinions and decisions are summarized and are made available on the OCC web site.²³

Further, to ensure that electronic banking activities are conducted consistent with bank safety and soundness and to reduce uncertainty over supervisory expectations on the delivery of online financial services, OCC has issued guidance addressing supervisory issues relating to banks' use of technology.²⁴ With the other Federal banking agencies, the OCC recently issued guidelines prescribing information security standards that implement the requirements of the GLB Act²⁵ and guidance on authentication in the electronic banking environment.²⁶ The OCC also issued a comprehensive handbook on Internet banking that discusses business and technical issues associated with providing banking services via the World Wide Web, the risks presented by these activities, and the OCC's procedures for Internet-related

²³ The OCC established a web site that contains information relating to electronic banking activities. See www.occ.treas.gov/netbank/netbank.htm (Electronic Banking web site). The site includes a listing of opinions, approval letters, supervisory guidance, and other issuances on this subject and provides links to the documents listed.

²⁴ See, e.g., OCC Bulletin 98-3, Technology Risk Management – Guidance for Bankers and Examiners (Feb. 4, 1998).

²⁵ 66 Fed. Reg. 8616 (Feb. 1, 2001) (information security guidelines issued jointly by the OCC, the Board, the FDIC, and OTS). These guidelines implement the requirements of section 501(b) of the GLB Act, 113 Stat. at 1436-37 *codified at* 15 U.S.C. 6801.

²⁶ OCC Advisory Letter No. 2001-8 (July 30, 2001).

examinations.²⁷ In addition, the OCC issued “The Internet and the National Bank Charter,” as part of the Comptroller’s Corporate Manual (Jan. 2001) and guidance on weblinking activities and aggregation activities.²⁸ These and other issuances, including Internet-related regulatory updates, are available on OCC’s Electronic Banking web site.

Finally, the OCC has conducted a comprehensive review of the OCC’s regulations with a view toward removing impediments to national banks’ use of technology. In an advance notice of proposed rulemaking (ANPR) published on February 2, 2000,²⁹ the OCC invited public comment on issues involving Internet banking and other uses of electronic technology. (*See* Appendix C.) Specifically, the ANPR focused on three issues:

- How should the OCC adapt its regulations and supervisory policies to facilitate national banks’ use of electronic technology consistent with bank safety and soundness?;
- What statutes can the OCC interpret more flexibly to accommodate new technologies?; and
- How can the OCC enhance the operational flexibility of banks engaging in electronic banking consistent with bank safety and soundness?³⁰

The OCC received 16 comments on the ANPR, including 7 from banks, 6 from trade associations, 2 from individuals, and 1 from a company that provides information processing management, outsourcing services, and application software to banks. The commenters strongly supported the OCC’s initiative, emphasizing that outdated and inflexible regulations are one of the largest obstacles banks face as they attempt to adopt new technologies. The comments offered suggestions in each of the three areas identified in the ANPR and raised a variety of additional issues.

²⁷ Comptroller’s Handbook, Other Income Producing Activities: Internet Banking (Oct. 1999).

²⁸ “Weblinking,” OCC Bulletin 2001-31 (July 3, 2001) and “Bank-Provided Account Aggregation Services,” OCC Bulletin 2001-12 (Feb. 28, 2001).

²⁹ 65 Fed. Reg. 4895 (Feb. 2, 2000).

³⁰ The ANPR also solicited suggestions that would be helpful in formulating recommendations for legislative action or for actions that may be appropriately undertaken on an interagency basis.

After reviewing these comments, the OCC developed a proposed rule to update its regulations to reflect national banks' use of new technology. On July 2, 2001 the OCC published in the *Federal Register* a notice of proposed rulemaking (NPRM) that would provide simpler and clearer guidance for national banks using electronic and developing technologies to conduct their activities and, also, would codify positions that the OCC has taken previously in published interpretive letters to national banks.³¹ (See Appendix C.) The NPRM also solicited additional suggestions under section 729 either for legislative action or for actions that may be appropriately undertaken on an interagency basis.

The proposed rule would create a new subpart E to part 7 of the OCC's regulations to house these and other OCC provisions related to the conduct of national bank activities through electronic means. Among its most significant provisions, the proposed rule would:

- Codify recent OCC interpretative letters approving the use of the finder authority by national banks to engage in several new activities made possible by technological developments. The proposed regulation includes examples, both in the electronic banking context and in the non-electronic banking context, illustrating the range of finder activities that the OCC has authorized.
- Set forth the factors the OCC considers in determining whether an electronic activity is part of, or incidental to, the business of banking. These factors are based on OCC and Federal judicial precedent and will provide better guidance to national banks seeking to engage in new electronic activities.
- Clarify that State law applies to a national bank's conduct of activities electronically only to the same extent it would apply if the activity were conducted through traditional means.
- Codify OCC interpretations that permit national banks as part of a digital signature transaction to act as a certification authority that issues certificates verifying the *identity* of the certificate holder. The proposal also requested comments on whether this authority should include the ability of a national bank to issue a digital certificate that verifies that the holder has certain *authority* or the *financial capacity* to make a purchase or engage in a transaction, how these activities will be structured, and whether these activities present unique risks.

³¹ 66 Fed. Reg. 34,855.

- Codify OCC interpretations that permit a national bank to collect, process, transcribe, analyze and store banking, financial and economic data for itself and its customers as part of the business of banking. The proposal also requested comments on whether the OCC should issue a rule on incidental data processing that would recognize that a national bank may generally derive a certain specified percentage of its *total* annual data processing revenue from processing non-financial data as incidental to its financial data processing services.
- Clarify that a national bank will not be considered “located” in a state simply because it maintains technology, such as a server or an automated loan center, in that state or because customers in that state electronically access a bank’s products and services.
- Require, as a matter of safety and soundness, that banks that share co-branded web sites or other electronic space with affiliated or unaffiliated third parties take reasonable steps to enable customers to distinguish between products and services offered by the bank and those offered by the third party. National banks must disclose their limited role with respect to the third party product or service, and ensure that these disclosures are conspicuous, simple, direct, readily understandable, and designed to call attention to the fact that the bank does not provide, endorse, or guarantee any of the products or services available.

The comment period on the proposed rule closed on August 31, 2001. OCC received 26 comments. The comments included 16 from financial institutions, 8 from trade and government associations, 1 from an individual, and 1 from a law firm. The comments were generally supportive of the proposed rule, but suggested some refinements. The OCC is currently studying these comments and may issue a final rule before the end of this year.

The OCC also stated in the NPRM that it is considering whether to further revise its regulations in light of the E-Sign Act³² in a separate project, and that any such

³² Shortly after the ANPR was published, Congress passed the E-Sign Act, which was enacted on June 30, 2000. Among other provisions, the E-Sign Act establishes certain uniform Federal rules concerning the use of electronic signatures and records in commercial and consumer transactions and establishes certain requirements for making disclosures to consumers electronically. Although it does not require implementing regulations, the E-Sign Act gives the OCC (and other Federal and state regulatory agencies) authority to interpret the E-Sign Act’s requirements with respect to the statutes they administer, subject to specified limitations.

revisions would be undertaken in a separate rulemaking. To that end, the OCC has completed an initial review of the regulations and statutory provisions administered by the OCC that require banks: (1) to provide signatures or written documents to (or obtain them from) consumers or other third parties or (2) to give notices or disclosures to consumers or other third parties. The OCC is considering various actions to clarify the effect of the E-Sign Act on these regulations and provisions, including the possibility of commencing a rulemaking project or issuing guidance. In this context, the OCC is consulting with other federal banking agencies to determine how to interpret and apply various words and phrases in OCC administered regulations and laws that arguably appear to contemplate written documents or signatures. These words and phrases include “execute,” “written agreement,” “agreement,” “form,” “instrument,” “copy,” “make available,” “notice,” “legend,” “notify,” “inform,” “report,” “publish,” “post,” “inform,” “mail,” and “by mail.” Likewise, OCC is consulting with the other agencies on how to administer provisions that require information to be posted in a particular place or locality, for example in a lobby or in an office.

Part VI

Regulations Administered by the Office of Thrift Supervision

OTS makes the following conclusions based upon its review:

A. Summary of Conclusions

There is not a need, at this time, for legislative amendments to the statutes that OTS's regulations implement in order to adapt requirements to online banking and lending. Nor is there a need, at this time, for OTS to revise its regulations in order to adapt requirements to online banking and lending.

As discussed in more detail in subpart C below, OTS already has a very flexible regulatory framework that permits savings associations to conduct banking and lending electronically. *See* 12 C.F.R. part 555. OTS also reviewed its other regulations but found none that would impede electronic delivery of products or services.

OTS has established processes for periodically reviewing the need for new legislation and legislative amendments, as well as regulatory changes. OTS will consider the information learned through this study as part of those processes.

OTS is committed to updating its regulations and guidance as the need arises, both individually and in conjunction with the other Federal banking agencies and the FFIEC. In doing so, OTS will continue to avoid impediments to online banking and lending. OTS will foster growth of these activities in a manner that is safe and sound and helps ensure consumer acceptance and protection.

B. Report Methodology and Information Learned

An interdisciplinary team OTS established in April 2001 derived the above conclusions. Representatives from OTS's Offices of Supervision Policy, Compliance Policy, Technology Risk Management, and Chief Counsel comprised the team. This team used three methods, described below, to contribute to its thorough review of its regulations on the delivery of financial services for this study: (1) a request for public comment published in the *Federal Register*; (2) a survey of OTS examiners; and (3) a headquarters review of OTS regulations.

1. Request for Comment on Study of Banking Regulations Regarding the Online Delivery of Financial Services

On June 11, 2001, OTS published in the *Federal Register* a request for comment on a variety of issues relating to the electronic delivery of financial products and services by savings associations.³³ (See Appendix D.) OTS received eight comments. Three were from trade associations: America's Community Bankers (ACB), American Bankers Association (ABA), and Electronic Financial Services Counsel (EFSC). The others were from MasterCard International (MasterCard), VISA U.S.A. (VISA), JPMorganChase (JPM), a law firm, and an appraiser. The OTS interdisciplinary team reviewed the public comments.

ACB, ABA, EFSC, MasterCard, and VISA commented against further federal restrictions on electronic transactions, including in the area of Internet link arrangements. ACB and MasterCard urged OTS to continue to provide flexible guidance rather than mandates. ACB and EFSC specifically discouraged OTS from issuing regulations or guidance on the E-Sign Act. MasterCard specifically discouraged OTS from providing guidance on the application of Most Favored Lender rules to electronic banking. These commenters asserted that action by OTS in these areas would be premature and unnecessary.

ACB, EFSC, MasterCard, and VISA encouraged OTS to help ensure that states do not impose a patchwork of requirements burdening electronic commerce. EFSC raised specific concerns about state privacy legislation, state licensing provisions for banking and other financial products and services, and state requirements that financial service providers maintain offices in state or employ local residents. ABA raised the issue of the extent to which the E-Sign Act may preempt state law.

ABA, MasterCard, and the law firm advocated greater flexibility to provide disclosures electronically under federal consumer protection statutes and regulations. VISA argued that if an institution provides disclosures on a web site, the federal banking agencies should not also require the institution to e-mail the disclosure to the consumer. VISA specifically asked the agencies to revise their Privacy rules so as not to require consumer consent before providing privacy notices electronically instead of on paper. A few commenters addressed regulations under the purview of other agencies. JPM focused on disclosures

³³ *Request for Comment on Study of Banking Regulations Regarding the Online Delivery of Financial Services*, 66 Fed. Reg. 31,186 (June 11, 2001).

under Regulations E, DD, and Z, VISA focused on Regulations E and the Truth in Lending Act (TILA), and MasterCard also focused on TILA, all of which are under the Board's purview. The law firm focused on the Real Estate Settlement Procedures Act (RESPA), which is under the Department of Housing and Urban Development's purview.

ACB urged the agencies to allow automated underwriting systems to substitute for the written appraisals currently required for certain real estate loans, an alternative EFSC also suggested the agencies consider through a separate process. ACB also encouraged OTS to raise the current \$250,000 regulatory threshold for loans requiring the use of state licensed or certified appraisers to the conforming GSE loan limit (now \$275,000 for most parts of the country). In contrast, the appraiser who commented urged OTS to retain the written appraisal requirement, arguing that appraisals are necessary to ensure that the collateral for mortgage loans is sufficient. VISA also called for some increased flexibility in using electronic appraisals.

ACB encouraged OTS to consider how to address "location" under the CRA, management interlocks, and branching. It suggested that OTS allow use of something like a CRA strategic plan for management interlocks and branching but did not provide further elaboration on how this option would work. In contrast, ABA and VISA advised the agencies not to revise rules with geographic or time components.

Consistent with the comments, this report does not recommend any new federal restrictions on electronic transactions. Part II of this report, which discusses jointly administered regulations, addresses Appraisal Standards (Part II.A), CRA (Part II.B), and Management Official Interlocks (Part II.E). In Part III of this report, the Board discusses providing disclosures electronically under a variety of federal consumer protection statutes and regulations.

2. Examiner Survey

During July and August 2001, OTS surveyed examiners who are directly involved in examining our savings associations that offer electronic banking and lending services. The questions pertained to the following:

- Examiners' observations of associations and customers that encounter difficulties or barriers with online banking and lending arising from OTS regulations or guidance.

- Whether there are specific regulatory requirements in an association's delivery of financial services, including those regulations that assume person-to-person contact, that OTS should adapt to online banking and lending.
- Whether OTS lacks, or could improve upon, guidance or regulation of online banking and lending.

The interdisciplinary team reviewed the examiners' survey responses. The examiners provided insightful responses regarding their examination experience with online banking and lending. OTS will consider the information learned from the examiners' responses in ongoing agency efforts to ensure that examinations are conducted in a thorough and efficient manner and to enhance employee guidance and training.

3. Interdisciplinary Headquarters Review

The OTS interdisciplinary team, in addition to participating in the interagency review of joint regulations as discussed in this report, also reviewed OTS-specific regulations. In performing this review, the team consulted with those OTS staff most familiar with particular regulations.

The first step of the review was to review all of OTS's regulations to determine which regulations address the delivery of financial services, including those regulations that may assume that there will be person-to-person contact during the course of a financial transaction, as indicated in section 729(a).

The second step was to identify in what way the assumption manifested itself in the particular regulation. For example, some regulations require that certain information be provided in writing through the mail or designate certain types of activities to be provided in separate areas of an office from where other activities are conducted. *See, e.g.*, 12 C.F.R. § 563b.3 (conversions) and § 563.76 (securities sales).

The third step was to identify whether any of the regulations, or the statutes they implement, would need to be revised to adapt the requirements to online banking and lending so as not to impede the electronic delivery of financial products and services. The review uncovered no statutes or regulations impeding the electronic delivery of financial products and services.

C. OTS's Previous Initiatives

Through the end of the 1990's, OTS periodically revised its regulations to better enable savings associations to use new technologies for electronic banking and lending. In 1998, OTS streamlined and updated its regulations relating to electronic operations to make it easier for Federal savings associations to develop new ways of delivering products and services through the prudent and innovative use of emerging technology.³⁴ (*See* Appendix D.) The revised rule permits Federal savings associations to use, or participate with others to use, electronic means or facilities to perform any function, or provide any product or service, as part of an authorized activity. The rule also requires each savings association (federally chartered or state-chartered) to notify OTS 30 days before it establishes a transactional web site. It provides that savings associations that present supervisory or compliance concerns may be subject to additional procedural requirements.

In promulgating the rule, OTS emphasized the importance of enabling regulations in this area. At the same time, OTS designed its regulations to help ensure that it would have sufficient information to understand developing technologies, to provide appropriate guidance on these technologies, and to supervise electronic operations effectively. OTS designed the final rule to provide both the industry and the agency with the appropriate amount of flexibility to adapt to changing conditions.

The preamble to the final rule noted that the agency had issued, and would continue to issue, guidance as electronic operations evolve. This guidance has taken the form of letters to chief executive officers of savings associations, interagency examiner guidelines, revisions to the Thrift Activities and Compliance Activities Handbooks, conditions on the approval of applications, and responses to requests for legal interpretations.³⁵ Since the publication of the final rule, OTS has

³⁴ *See* 63 Fed. Reg. 65,673 (Nov. 30, 1998).

³⁵ *See, e.g.*, Memorandum from Richard M. Riccobono, Deputy Director, for Chief Executive Officers (Nov. 3, 1998) (Policy Statement on Privacy and Accuracy of Personal Customer Information); Memorandum from Richard M. Riccobono, Deputy Director, for Chief Executive Officers (July 23, 1998) (Interagency Guidance on Electronic Financial Services and Consumer Compliance); Memorandum from John Downey, Executive Director, Supervision, for Chief Executive Officers (June 23, 1997) (Statement on Retail On-Line Personal Computer Banking); Thrift Activities Regulatory Handbook, Section 341, Information Technology (Oct. 1997)

continued to provide additional guidance in this area and post it on its web site at <www.ots.treas.gov>.³⁶

(Regulatory Bulletin 32-6, Oct. 15, 1997); Federal Financial Institutions Examinations Council (FFIEC) Information Systems Examination Handbook (1996); OTS Order No. 95-88 (May 8, 1995) (application approval of Internet bank); OTS Op. Chief Counsel (Oct. 1, 1998) (authority of federal savings associations to provide payroll processing services); OTS Op. Chief Counsel (July 1, 1998) (preemption of state ATM restrictions); OTS Op. Chief Counsel (Sept. 19, 1997) (establishment of automated loan machines).

³⁶ *See, e.g.*, Memorandum from Richard M. Riccobono, Deputy Director, for Chief Executive Officers (June 10, 1999) (Transactional Web Sites); OTS Op. Chief Counsel (Dec. 7, 1999) (San Francisco ATM fee ordinance); OTS Op. Chief Counsel (Nov. 22, 1999) (preemption of local ATM fee restrictions); OTS Op. Chief Counsel (Jan. 15, 1999) (New York State ATM Safety Act); OTS Mem. Chief Counsel (Dec. 22, 1998) (Massachusetts Electronic Branch Restrictions).

APPENDICES

Relevant Federal Register Publications