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**Edward Horowitz**

(left) of CitiGroup, which is still waiting for its Internet payoff. **Matthew Lawlor** (right) has helped small banks cash in cheaply.



## DEALS & DEAL MAKERS

# Smaller Institutions Make Inroads On the Internet Via Outsourcing

By

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MCLEAN, Va. -- Let the banking behemoths pour in hundreds of millions of dollars as they try to develop online-banking services.

F&M Bank-Northern Virginia, meanwhile, has invested a mere \$5,000 -- and is seeing promising results.

The community lender, a unit of F&M National Corp. , Winchester, Va., boasts all the basics in Web banking-fund transfers, bill payment, instant statements, even a 24-hour customer-service phone line for F&M's online customers. The service isn't as broad as that of big rivals, but most depositors just want the basics. So while its big rivals raise the stakes, F&M says \$5,000 is all it will ante for now.

Rather than pump millions of dollars into a Web system, F&M outsourced. There to help was entrepreneur Matthew Lawlor, a former big-bank executive and now chairman and chief executive of Online Resources & Communications Corp. , which helps banks offer customers home-banking options. For a start-up fee and monthly service charges, Online Resources, McLean, Va., designed F&M's Web site and runs it.

At a high-security central processing room, Mr. Lawlor's team monitors all the clicks of F&M's online clients -- and those of 430 other small-financial clients from Massachusetts to California -- making sure bills get paid or funds get transferred as ordered. One floor below is a 24-hour customer-support center, designed to answer computer-related questions.

Online Resources even arranged to have envelopes stuffed for F&M with fliers touting the bank's online service. "They had us ready to go in four or five months," says F&M's chief financial officer, Ramona Rodriguez. "We could never have done that on our own."

Many are betting on online banking and are vying to be the choice of banks trying to get up and running. The likes of Jack Henry & Associates Inc., Monett Mo., CheckFree Corp., Norcross, Ga., and S1 Corp. , Atlanta, are competing to provide banks with services allowing remote banking through the Internet.

For these entrepreneurs, small banks are a huge and untapped market. Two-thirds of the nation's deposits are held at several thousand small institutions with \$10 billion in assets or less. For example, Mortgage.com Inc., a Plantation, Fla., provider of mortgages handled online, recently decided to refocus its business from individual borrowers to financial institutions seeking to outsource online housing loans.

"The big growth area are small- to medium-size banks," says Seth Werner, Mortgage.com's president and chairman. "The question for these institutions is no longer 'Should we have an Internet strategy?' The question now is 'What should our 'Net strategy be?'"

Five years ago, technology seemed to auger the demise of community banking. Big banks with large budgets and national brands were poised to invest heavily in Internet banking and thus threatened to shut out small banks. Online-banking clients tend to be wealthy, and small banks risked losing such coveted customers.

The costs of developing such a system in-house can break a small bank. However, if they are able to go online on the cheap, the playing field could become more level. The solution: outsourcing. "These big banks are very aggressive advertisers, and our customers noticed. They wanted online services and were asking for it," F&M's Ms. Rodriguez says. "Now we have something that is competitive. It's a defensive measure. And, yes, it's cheap."

Cutting costs is crucial because online-banking services, while necessary, don't pay for themselves. First Manhattan Consulting Group says that 70% of investments that financial institutions are making in online services are unprofitable. "I haven't heard of any bank really making money online yet," says Avivah Latin, an analyst with Gartner Group.

Web banking remains cumbersome for consumers. Most online bill-paying services, for example, require a depositor to register the account number of whomever they are trying to give money to before they pay. Furthermore, nobody yet has found a way to get cash out of the computer terminal. Analysts say online-banking systems will take time to perfect. They note that ATMs were considered cumbersome two decades ago, and today they are taken for granted.

Mr. Lawlor -- once with Chemical Bank, which has been merged with Chase Manhattan -- is investing heavily in improving the service. His company, which went public on the Nasdaq Stock Market in 1999, hopes to turn a profit sometime during the next two or three years.

The Harvard Business School graduate with rumpled suits and thick glasses, quit as director of venture capital at the former Chemical Bank to become an entrepreneur in 1980-long before "dot-comming" became a fashion. He wanted to bring banking into the home and developed a series of systems that never took off.

In the process, he found an angle that has shown to be invaluable: Use the network of ATMs to give small bank customers instant access to their accounts from the home. Mr. Lawlor, 52 years old, patented the idea, and it is one reason why his service is quick and cheap: "They use railroad tracks that are already in place," Ms. Rodriguez says.

The system is best used for bill payment. Many rival systems still process orders by sending checks in the mail on the behalf of customers -- a process that takes days. Through Online Resources, small banks such as F&M use the ATM network to immediately tap the customer account and credit the newspaper carrier or phone company electronically. Big banks, which have shown interest in using the same technology, haven't been happy about the patent. Citibank sued Online Resources and won the right to use the ATM system as part of a settlement.

Mr. Lawlor quietly is expanding the array of services it offers. Online Resources recently announced an alliance with Engineering Enterprise Inc., New York, that will allow Online Resources customer banks to offer their depositors online-trading services. In another deal meant to help small banks service corporate customers online, Online Resources has partnered with Politzer & Haney, Newton, Mass., the leading outsourcer of cash-management services.

Again, no bank is making much money with these products, but few are willing to risk not being ready as the Web-banking market grows. "If you want your financial institution to be part of the future," Ms. Rodriguez says, "you've got to have somebody like Online Resources."

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