ICBA® 2021 CAPITAL SUMMIT

CLOSE INDUSTRIAL LOAN COMPANY LOOPHOLE

INDUSTRIAL LOAN COMPANIES: "BANKS" OWNED BY COMMERCIAL COMPANIES

Industrial loan companies (ILCs) are the functional equivalent of full-service banks. They engage in commercial and consumer lending as well as deposit taking and have access to the Federal Reserve payments system. A loophole in the Bank Holding Company Act allows commercial companies to own or acquire ILCs, subject only to approval by the FDIC. Federal law prohibits all other full-service banks, whether federal or state chartered, from being owned by commercial companies.

The ILC charter historically been limited and may be issued by only a handful of states, though it grants the power to operate nationwide. Prior to 2020, the FDIC had not approved deposit insurance for a new ILC for more than 10 years. Since 2020, the FDIC has approved two new ILCs and an additional six applications are pending, including one from Rakuten, the "Amazon of Japan." Absent Congressional intervention, we expect a flood of new applications with the potential to fundamentally shift the American economic landscape.

Given what's at stake, ILC policy should be debated and deliberated in Congress, not left to the discretion of the FDIC.

MIXING BANKING AND COMMERCE FLOUTS LONG-STANDING AMERICAN ECONOMIC POLICY

The prohibition on mixing banking and commerce was first established in the 1930s in response to concerns about concentration of economic power. Mixing banking and commerce inevitably creates market distortions and leads to cross-sector consolidation.

In the age of big data, social media and e-commerce conglomerates, this threat is greater now than it was in the 1930s. We should be cautious before giving these companies yet more reach into the economic life of Americans by allowing them to leverage ownership of bank-like ILCs. The integration of technology and banking firms would not only result in an enormous concentration of financial and technological assets but also would pose conflicts of interest in our banking system and privacy concerns for consumers.

What will happen when social media giants extend their reach into our financial lives? Access to Americans' personal, financial data—monthly paycheck direct deposits, account balances, expense patterns, political contributions, history of late fees, transaction records, etc.—would create a whole new level of targeted marketing and analytics-based price manipulation.

A BLIND SPOT IN FINANCIAL SUPERVISION

Commercial companies that own ILCs are not subject to federal consolidated supervision. This leaves a dangerous gap in safety and soundness oversight, described as a "blind spot" in a GAO report.

The Bank Holding Company Act provides for consolidated supervision by the Federal Reserve of the holding company and its affiliates as a group. This is important because, according to the Fed, "financial trouble in one part of an organization can spread rapidly to other parts of the organization." Only consolidated supervision allows for risk monitoring across corporate boundaries. Because ILCs are exempt from the BHCA, ILC parent companies are not subject to consolidated supervision. This creates an unacceptable level of risk.

MESSAGES FOR YOUR MEMBERS OF CONGRESS

- Commercial ownership of ILCs has the potential to change the American financial services landscape.
- Such a far-reaching change must be debated in Congress, not left to the discretion of the FDIC.
- Support legislation to address the ILC loophole, such as the "Close the ILC Loophole Act," sponsored by Rep. Jesús "Chuy" García.

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