May 17, 2022

The Honorable Maxine Waters
Chairwoman
Committee on Financial Services
U.S. House of Representatives
Washington, D.C. 20515

The Honorable Patrick McHenry
Ranking Member
Committee on Financial Services
U.S. House of Representatives
Washington, D.C. 20515

Re: H.R. 5912 (Garcia), *The Close the ILC Loophole Act* -- Support

Dear Chairwoman Waters and Ranking Member McHenry,

The undersigned organizations, which together represent a cross-section of civil rights, financial reforms groups, and consumer protection organizations, write today to strongly urge Congress to promptly close the industrial loan company (ILC) loophole in current law by passing H.R. 5912 (Garcia), *The Close the ILC Loophole Act*.

ILCs operate under a special exemption in federal law that permits any type of organization—including a large technology company or commercial firm—to control a full-service FDIC-insured bank *without* being subject to the same oversight and prudential standards, or limitations on the mixing of banking and commerce, that Congress has established for the U.S. financial system. When this exception was initially created, ILCs were typically small financial institutions, and companies used the charter for the limited purpose of providing small loans to industrial workers who could not otherwise obtain credit. However, since that time, large commercial companies have used the ILC charter to gain access to the U.S. financial system and control entities that have essentially all of the powers of a full-service commercial bank, including the ability to accept deposits, make consumer and commercial loans, and effectuate payments.[1]

Currently, ILCs of any size can collect FDIC-insured savings from retail customers and offer mortgages, credit cards, and consumer loans, which enable them to operate as full-service banks. Although ILCs have the powers of a commercial bank, their corporate owners—unlike the owners of commercial banks--are not subject to consolidated supervision and regulation by a federal banking agency, which can allow risks to build up in the organization outside the view of any federal supervisor. Simply put, this regulatory loophole creates safety and soundness risks for the institution, risks to the financial system, and additional risks for consumers and taxpayers.

The risks to consumers and the financial system from ILCs are not theoretical. It should come as no surprise that several large companies that used the loophole to acquire ILCs, evading the type of consolidated supervision meant to ensure soundness and regulatory compliance, then required public bailouts during the 2007-2008 financial crisis.[2]

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[1] See Testimony of Scott G. Alvarez, General Counsel, Board of Governors of the Federal Reserve System, before the Committee on Banking, Housing, and Urban Affairs, U.S. Senate, October 4, 2007, available at https://www.federalreserve.gov/newsevents/testimony/alvarez20071004a.htm.

[2] Professor Art Wilmarth, "The FDIC Should Not Allow Commercial Firms to Acquire Industrial Banks, " May 2020. Pg 5.

Furthermore, ILCs provide non-bank lenders an easy path to federal preemption of state interest rate caps. Today, First Electronic Bank–an ILC– engages in a "rent-a-bank" scheme whereby it is being used by high-cost lender Personify Financial to make high-cost installment loans of $1,000 to $10,000 at APRs as high as 179.99% in 22 states whose laws do not allow that rate for a non-bank lender.[3] ILCs can "export" their state's interest rate to consumers in other states when providing credit– a privilege primarily given to nationally chartered banks closely supervised by the federal banking regulators. As a result, many ILCs that are chartered in Utah are able to lend at exorbitant rates because Utah has no state usury cap.[4]

High-cost lending only fuels financial exclusion. We deeply object to attempts to justify preemption of state interest limits with claims that they lead to a more inclusive market, particularly for communities of color. We heard the same claims about predatory subprime mortgage lending until the foreclosure crisis ravaged neighborhoods of color and only widened the racial wealth gap. The suggestion that high-cost lending offers a path toward upward mobility insults those of us who understand that our communities deserve better. For this reason, we look forward to the GAO report this bill mandates to gain greater insight into how ILCs affect the cost of credit in minority and low-income communities.

Moreover, the loophole provides a way for technology firms offering a wide variety of services to acquire a full-service bank along with all of the privileges of a bank--even though Congress has generally prohibited the mixing of banking and commerce. These technology firms thereby gain access to FDIC-insured deposits and, potentially, a vast trove of consumer financial information, all without being subject to the information security and prudential standards that apply to regulated bank holding companies. In addition, because the corporate owners of ILCs are not considered bank holding companies, they also evade the limitations imposed by Congress on the ability of banking organizations to expand into new activities if their insured depository institution subsidiaries have a less than Satisfactory record of performance under the Community Reinvestment Act.[5]

We recognize that some firms have previously acquired an ILC in reliance on the exception and may continue to operate as such, subject to appropriate safeguards that permit the ILC's federal supervisor to protect the safety and soundness of the FDIC-insured ILC, the financial system, and consumers. However, any of these pre-existing ILCs should *not* be permitted to essentially sell that status to an unaffiliated third party without restrictions, thereby allowing a new company to take advantage of the exception after the loophole is closed by Congress. Permitting unencumbered transfers would allow, for example, a technology firm to evade Congress's action to close the ILC loophole by simply acquiring one of the several dozen ILCs that operate under the exception today. After doing so, unless restricted, the company could alter the institution's business strategy, product set, and geographic scope to make it unrecognizable to its former self and greatly expand—rather than constrict—the risks posed by the exception.

ILC owners should not have the ability to sell their status rights to the highest bidder and therefore exploit consumer data, undermine trust in our banking system and otherwise put our financial system at risk. To put it more simply, allowing existing ILCs to easily transfer their rights to an unaffiliated party

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[3] Center for Responsible Lending. "Industrial Loan Company Charters Pose Risks to Consumers and the Economy." July 2020

[4] Utah's Department of Financial Institutions

[5] See 12 U.S.C. § 1843(*l*).

would be the legislative equivalent of attempting to close the barn door but leaving the side of the barn wide open.

The time is now for Congress to close the ILC loophole before it is further exploited by firms seeking to gain all of the advantages of an FDIC-insured bank charter without the concomitant supervision and regulation that Congress has established for the corporate owners of full-service insured banks. H.R. 5912, *The Close the ILC Loophole Act*, introduced by Representatives Chuy Garcia (D-IL) and Lance Gooden (R-TX), addresses these concerns and is a comprehensive solution to closing the ILC loophole once and for all. As civil rights groups, financial reform groups, and consumer advocates, we fully support this important legislation and encourage the Financial Services Committee to pass it quickly.

Respectfully,

20/20 Vision DC
Action Center on Race & the Economy
Arthur E. Wilmarth, Jr. Professor Emeritus of Law, George Washington University Law School
California Reinvestment Coalition
Citizens Action Coalition of IN
Consumer Action
Consumer Federation of America
Delaware Community Reinvestment Action Council, Inc.
Fair Housing Center of Central Indiana, Inc.
HomesteadCS
Hoosier Action
Hoosiers for Responsible Lending
Indiana Association of Area Agencies on Aging
Indiana Catholic Conference
Indiana Coalition Against Domestic Violence, Inc.
Indiana Community Action Association, Inc.
Indiana Community Action Poverty Institute
Indiana Friends Committee on Legislation
Indiana State Conference NAACP
Indianapolis Urban League
MCCOY (Marion County Commission on Youth, Inc.)
New Jersey Citizen Action
Open Markets Institute
Opportunity Finance Network
Public Citizen
Take on Wall Street
The Democracy Collaborative
The Leadership Conference
The Military / Veterans Coalition of Indiana
Thrive Alliance
UnidosUS

United Way of Allen County
Virginia Organizing
VOICE (Voices Organized in Civic Engagement) OKC
Woodstock Institute

cc: Members of the House Financial Services Committee