



**NCRC Statement on Industrial Loan Companies
Submitted to the House Financial Services Committee
July 10, 2006**

The National Community Reinvestment Coalition (NCRC) greatly appreciates the opportunity to submit a comment for the public record concerning Industrial Loan Companies (ILCs). NCRC agrees with several members of Congress that the ILC loophole needs to be closed completely.

NCRC is the voice for 600 community organizations members representing millions of low- and moderate-income consumers across America. We are the nation's economic justice trade association dedicated to increasing access to credit and capital for minority and working class families.

Banking & Commerce Do Not Mix

By allowing ILCs (industrial loan company) to exist, federal regulators would let companies like Wal-Mart have the same privileges as a regular bank without the same rigorous regulatory oversight. Unlike other banks, ILCs fly under the radar of federal regulating agencies. They are exempt from the Bank Holding Company Act (BHCA), which requires safety and soundness examinations of banks and their parent companies. Without these protections, the U.S. banking system and taxpayers who fund the federal safety net for banks and ILCs are put at serious risk. Major corporate scandals, such as Enron and Worldcom, highlight potential financial failures that Wal-Mart could similarly engender. If Enron had been an ILC, the U.S. banking system and American taxpayers would have had to foot the bill. Imagine the implications given that Wal-Mart does more business than Target, Sears, Kmart, JC Penney, Safeway and Kroger combined.

Mixing banking and commerce imperils safety and soundness because it eliminates a bank's impartiality. A bank with a commercial affiliate will not base its lending decisions on sound underwriting criteria. Instead, it will favor its affiliate and cut off credit for its competitors. The bank will also be tempted to finance its affiliate's speculative and risky ventures. With a bank the size of Wal-Mart or Home Depot, the end result is a significant reduction in credit for independent small businesses, and an increase in financing for the bank's affiliate, regardless of the risk it produces.

Victims of predatory lending have also fallen prey to abusive home improvement loans. The business model proposed by Home Depot would create incentives for contractors to aggressively market home improvement loans to unsuspecting customers, thereby exacerbating current predatory lending and home improvement scams. Current ILC loopholes do not provide comprehensive oversight to address these potential issues.

While many ILCs start as special purpose banks processing credit cards, they can quickly amass a sizable amount of profits and capital. Where would a Wal-Mart invest these profits and capital? It is likely these investments would be anti-competitive and could also be risky.

While companies like Wal-Mart may point out that they are not alone in their attempts to establish ILC's, this does not rectify the fact that they exploit an outdated and already abused loophole. NCRC and other consumer advocate organizations support the complete elimination of the ILC loophole and have petitioned Congress to close the loophole as it considers regulatory relief provisions.

ILCs were never intended to be large, nationwide banks that offered services indistinguishable from commercial banks. In 1987, Congress granted an exception to the BHCA for ILCs because they were sporadically chartered in a small number of states, held very few assets, and were limited in the lending and services they offered. In fact, the exception applied only to ILCs chartered in five states (Utah, California, Colorado, Nevada, and Minnesota) which either have assets of \$100 million or do not offer checking services. Yet since that time, everything about ILCs has grown: the number that exist, the amount of assets and federally insured deposits in them, and services and lending products they can offer.

According to the General Accounting Office (GAO), ILC assets grew from \$3.8 billion to over \$140 billion (over 3,500%) between 1987 and 2004. Of the 180 largest financial institutions in the country, in 2004, six were ILCs with \$3 billion each in assets. According to the Federal Reserve, the majority of ILCs had less than \$50 million in assets in 1987, with assets at the largest ILC valuing less than \$400 million. By contrast, in 2003, one ILC owned by Merrill Lynch had more than \$60 billion in assets (and more than \$50 billion in federally insured deposits).

It is time to shut down this parallel banking system, and disallow its further expansion. The Federal Reserve Board has also recommended that the ILC exemption be eliminated. NCRC and its members strongly urge the FDIC to reject pending applications to establish ILCs, and call on Congress to close the ILC loophole permanently.

Conclusion

Today, with the existing loophole, the world's largest retail corporation could gain banking privileges that Congress never intended for it to have; it would be given insufficient regulatory oversight due to an exemption from the Bank Holding Company Act, and it would only need to meet the bare minimum obligations to low- and moderate-income communities under the Community Reinvestment Act. As a result, American taxpayers and the U.S. banking system will be put at risk. The health of community banks, small businesses, and the product choices they offer consumers would be jeopardized.



Office of Thrift Supervision
Department of the Treasury

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John M. Reich
Director

July 11, 2006

The Honorable Spencer Bachus
Chairman
Subcommittee on Financial Institutions
and Consumer Credit
Committee on Financial Services
U.S. House of Representatives
Washington, D.C. 20515

Dear Mr. Chairman:

As you evaluate the structure and supervision of the industrial loan company (ILC) segment of the financial services industry, it is important to clarify the Office of Thrift Supervision's (OTS) existing supervisory authority in this area.

Some have suggested that ILC's and their holding companies are unregulated and that ILC's in holding company structures pose potential risks arising out of the relationship, transactions and activities between the ILC and its parent holding company. It has been further suggested that these risks may only be managed by subjecting the corporate parent of an ILC to supervision as though it were a bank holding company. In fact, there is a regulatory structure already in place in which a number of ILC holding companies are currently subject to holding company oversight.

In any instance where an ILC and a savings association are affiliated in a corporate structure, the holding company is a savings and loan holding company subject to regulation by the OTS. In such cases, the state is the primary regulator of the ILC, the FDIC is the appropriate federal banking agency for the ILC, and the OTS is the appropriate federal banking agency for the ILC holding company, as well as the affiliate savings association.

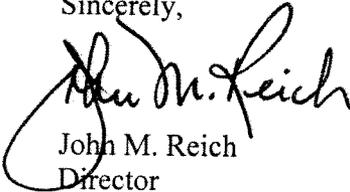
The notion that only a bank holding company framework provides rigorous holding company oversight is mistaken. The OTS has long exercised broad and effective oversight of complex holding company structures that own savings associations. OTS currently supervises 481 thrift holding companies with aggregate assets of \$7.5 trillion. Eight of these companies also own an ILC and, as such, are subject to OTS holding company jurisdiction and oversight. These OTS-supervised holding companies control approximately 70 percent of the total ILC assets nationwide, and include Merrill Lynch, Morgan Stanley, USAA, American Express, Lehman Brothers and General Electric.

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Authority for OTS to supervise these depository holding company structures under the Home Owners Loan Act is comprehensive. This authority is recognized not only domestically, but also internationally by the European Union, which has recognized OTS as a consolidated coordinating supervisor for General Electric, an OTS-supervised holding company conglomerate that operates in the EU.

As you consider legislation involving oversight of the ILC industry, please feel free to contact us with any questions you may have with respect to OTS's experience, holding company supervisory authority and oversight. My staff and I are also available to assist you in any manner regarding legislation in this area. Thank you.

Sincerely,

A handwritten signature in black ink, appearing to read "John M. Reich". The signature is fluid and cursive, with a large initial "J" and "R".

John M. Reich
Director

cc: Members of the Subcommittee on
Financial Institutions and Consumer Credit