Federal Deposit Insurance Corporation
550 17th Street NW, Washington, D.C. 20429-9990
Legal Division

MEMORANDUM TO: The Board of Directors

FROM: Sandra L. Thompson
Acting Director
Division of Supervision and Consumer Protection

Douglas H. Jones
Acting General Counsel

SUBJECT: Moratorium On Deposit Insurance Applications And Change In Bank Control Notices Submitted By, Or With Respect To, Industrial Loan Companies

RECOMMENDATION

Staff recommends that the Board impose a six-month moratorium on any FDIC action to: (i) accept, approve, or deny any application for deposit insurance by an industrial loan company, industrial bank, and similar institution (collectively referred to as "ILCs"), or (ii) accept, disapprove, or issue a letter of intent not to disapprove any notice of change in bank control filed with respect to any ILC. In addition, we recommend that during the period of the moratorium all other applications and notices filed by, or with respect to, any ILC be brought to the Board of Directors for review and determination. We also recommend that the Board limit the application of the moratorium when the Board determines with respect to a particular case(s) that (i) the moratorium would present a significant safety and soundness risk to any FDIC-insured institution or a significant risk to the deposit insurance fund, or (ii) an emergency exists requiring expeditious action, or (iii) failure to act would otherwise impair the mission of the FDIC.

Recently, the growth of the ILC industry, the trend toward commercial company ownership of ILCs, and the nature of some ILC business models have raised questions about the risks of ILCs to the deposit insurance fund and whether their commercial relationships pose any safety and soundness risks. These issues also have been raised by the public, academics, other Federal agencies, and members of Congress. While ILCs to date have not presented undue risks or safety and soundness concerns, and current supervisory controls have been effective, it is appropriate for the FDIC to carefully evaluate these developments and assess whether statutory, regulatory, or policy changes should be made in its oversight of ILCs. A moratorium would give the FDIC the opportunity to further evaluate the various issues, facts, and arguments raised in connection with the ILC industry and to assess whether statutory or regulatory changes or revised standards and procedures for ILC applications and supervision are needed to protect the deposit insurance fund.

I. BACKGROUND

ILCs were first chartered in the early 1900's as small loan companies for industrial workers. Over time the chartering states have gradually expanded the powers of their ILCs to the extent that ILCs now generally have the same powers as state commercial banks.[1]

While ILCs are "banks" under the FDI Act, they are not "banks" under the Bank Holding Company Act (BHCA). One result of this difference in treatment is that a company that owns an ILC could engage in commercial activities and may not be subject to Federal consolidated supervision. By contrast, domestic bank holding companies and financial holding companies that are subject to Federal consolidated supervision are prohibited from engaging in commercial activities. As a result of these differences, some of the companies that own ILCs are not subject to Federal consolidated supervision. Recently, there has been an increase in applications for, and interest in, ILCs that will be affiliated with commercial concerns or other companies that will not have a Federal consolidated supervisor. As the ILC industry has continued to evolve, the FDIC has been evaluating the impact of these developments on the safety and soundness of individual institutions and the risk they may pose to the deposit insurance funds. Some members of Congress, the Government Accountability Office, the FDIC's Office of Inspector General, and members of the public have expressed concerns regarding the lack of Federal consolidated supervision, the potential risks from mixing banking and commerce and the potential for an "unlevel playing field".

ILCs are state-chartered banks, and all of the existing FDIC-insured ILCs are "state nonmember banks" under the FDI Act. As a result, their primary Federal banking supervisor is the FDIC. The FDIC generally exercises the same supervisory and regulatory powers over ILCs that it does over other state non-member banks. The only material exceptions to the FDIC's authority over ILCs are that the cross-guarantee liability provisions, the golden parachute provisions, and the management interlocks provisions are not applicable to ILCs, their affiliates or holding companies. Legislation to make these provisions applicable to ILCs is currently pending.

II. DEVELOPMENTS IN THE INDUSTRY

The ILC industry has evolved since ILCs were excluded from the BHCA by the Competitive Equality Banking Act (CEBA) in 1987. As of year-end 1987, there were 105 ILCs with aggregate total assets of $4.2 billion and aggregate total deposits of $2.9 billion. The reported total assets for these ILCs ranged from $1.0 million to $411.9 million, with the average ILC reporting $40.0 million in total assets and $27.3 million in total deposits.

As of March 31, 2006, there were 61 insured ILCs with aggregate total assets of $155.1 billion and total deposits of $110.9 billion. Only 14 of the current 61 ILCs were insured during 1987 or prior years. ILCs owned by four financial services firms, including Merrill Lynch & Co., Inc.;

[1] If an ILC is authorized to, and does, in fact, offer demand deposits, any company that owns such an ILC may be required to register as a bank holding company. As a result, most of the ILCs have chosen not to offer demand deposits.

UBS, AG; Lehman Brothers Holdings, Inc.; and Morgan Stanley, accounted for 63 percent of the growth in ILC assets since 1987. These firms which all operate under consolidated supervision by the Federal Reserve Board (FRB), the Office of Thrift Supervision or the Securities and Exchange Commission account for 61.4% of the total ILC industry assets as of March 31, 2006. Reported total assets of all ILCs, as of March 31, 2006, ranged from $2.7 million to $62.0 billion.

As of July 24, 2006, 48 of the 61 existing ILCs were chartered in Utah or California. ILCs also operate in Colorado, Hawaii, Indiana, Minnesota and Nevada. Currently, nine applications for deposit insurance for ILCs are pending before the FDIC. The FDIC has also received five notices of change in bank control to acquire an ILC. Recent deposit insurance applications and change in control notices regarding ILCs have more often involved potential owners that would not qualify as a bank holding company or financial holding company. Attached is a list of these pending ILC deposit insurance applications and change in control notices.

III. RECOMMENDED MORATORIUM

As a result of the continued evolution of the ILC industry and the various issues and concerns expressed regarding the ILC industry mentioned above, and as detailed in the attached Federal Register Notice of the Imposition of a Moratorium, it is appropriate for the FDIC Board to further evaluate (i) industry developments, (ii) the various issues, facts, and arguments raised with respect to the ILC industry, (iii) whether there are emerging safety and soundness issues or policy issues involving ILCs or other risks to the insurance fund, and (iv) whether statutory, regulatory, or policy changes should be made in the FDIC's oversight of ILCs in order to protect the deposit insurance fund or important Congressional objectives regarding the statutory structure applicable to depository institutions.

Consequently, staff proposes the imposition of a six-month moratorium on (i) all acceptances, approvals, and denials of applications for deposit insurance submitted by ILCs, and (ii) all acceptances of, disapprovals of, and issuances of letters of intent not to disapprove all change in control notices with respect to ILCs.

During the moratorium, the FDIC would not "accept" applications for deposit insurance for any ILC or notices of change in control with respect to any ILC, regardless of whether the deposit insurance applications or change in control notices is substantially complete. The moratorium would include all pending ILC applications for deposit insurance and notices of change in control with respect to an ILC in order to maintain the status quo. In that way the FDIC would be able to focus carefully and comprehensively on further evaluating the developments, facts, issues, and arguments mentioned above, and to ensure that no new ILCs will be insured and no new changes in control will be permitted that would be inconsistent with the FDIC's findings and conclusions.

During the moratorium, all ILC applications and notices other than those subject to the moratorium will be considered and acted upon by the FDIC's Board of Directors.

The moratorium would provide an exception for the Board of Directors to act on an ILC application or notice, on a case by case basis, in the event that the moratorium would present a significant safety and soundness risk to any FDIC-insured institution or a significant risk to the deposit insurance fund, if an emergency exists requiring expeditious action, or if failure to act would otherwise impair the mission of the FDIC.

In circumstances similar to the FDIC's, courts have recognized that agencies have authority to impose a moratorium on agency actions or approvals. In situations similar to this one, courts have consistently upheld a moratorium where it was necessary to achieve or preserve the broad statutory objectives of the agency's governing statute and the agency's decision to impose the moratorium was reasonable under the circumstances.[2] Challenges to agency moratoriums by applicants have been uniformly unsuccessful where the agency imposed the moratorium to evaluate its understanding of emerging issues and standards for dealing with those issues.

By imposing this moratorium the FDIC Board is not implementing any new standards, but rather seeks to maintain the status quo while the FDIC evaluates its standards in light of its statutory objectives and congressional policies and conducts the other evaluations described above. Such a moratorium therefore would be essentially procedural in nature, rather than substantive, and may be imposed without notice-and-comment rulemaking.[3]

Staff Contacts

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Attachments

[2] See, e.g., *Western Coal Traffic League v. Surface Transportation Board*, 216 F.3d 1168, 1173 (D.C. Cir. 2000).
[3] *Western Coal*, 216 F.3d at 1176; *Neighborhood TV Co., Inc. v. FCC*, 742 F.2d 629, 638 (D.C. Cir. 1984).

Pending Applications for Deposit Insurance					
Insured	Institution	Total Assets	Total Deposits	State	Parent
NA	COMDATA BANK	NA	NA	UT	Ceridian Corporation
NA	DAIMLERCHRYSLER BANK US	NA	NA	UT	DaimlerChrysler
NA	CAPITALSOURCE BANK	NA	NA	UT	CapitalSource, Inc.
NA	WAL-MART BANK	NA	NA	UT	Wal-Mart
NA	MARLIN BUSINESS BANK	NA	NA	UT	Marlin Business Services, Corp.
NA	AMERICAN PIONEER	NA	NA	UT	Cargill Financial Services and First City Financial
NA	HEALTHBENEFIT BANK dba BLUE HEALTHCARE BANK	NA	NA	UT	Blue Cross/Blue Shield
NA	BERKSHIRE HATHAWAY BANK	NA	NA	UT	Berkshire Hathaway
NA	FIFTH STREET BANK	NA	NA	NV	Security National Master Holding Company

Pending Notices of Change in Bank Control					
Insured	Target Institution	Total Assets	Total Deposits	State	Acquiring Entity
8/2/2004	GMAC AUTOMOTIVE BANK	3,060.6	2,573.1	UT	Cerberus
9/22/1997	MERRICK BANK	736.2	551.8	UT	CompuCredit
8/26/1988	SILVERGATE BANK	412.4	180.5	CA	WESCOM Credit Union
6/3/2002	ENERBANK	91.3	77.7	UT	The Home Depot
5/1/2000	VOLVO COML CREDIT CORP OF UTAH	2.8	0.5	UT	NHB Holdings, Inc.