June 30, 2020

Via Email

Mr. Robert E. Feldman
Executive Secretary
Attention: Comments
Federal Deposit Insurance Corporation
550 17th Street NW
Washington, D.C. 20429

Re: Request for Comments Regarding the Notice of Proposed Rulemaking entitled "Parent Companies of Industrial Banks and Industrial Loan Companies" (RIN 3064-AF31)

Dear Mr. Feldman:

EnerBank USA (EnerBank or we) is grateful for the opportunity to provide comments and recommendations to the Federal Deposit Insurance Corporation (FDIC) regarding its Notice of Proposed Rulemaking on "Parent Companies of Industrial Banks and Industrial Loan Companies" (RIN 3064-AF31) (Proposed Rule).

As the FDIC knows, EnerBank is a Salt Lake City-based industrial bank (IB) that provides unsecured home improvement loans to consumers throughout the nation who work with EnerBank's strategic business partners and independent construction contractors. Our strategic business partners include manufacturers, distributors, franchisors, and major retailers of home improvement, remodeling, and energy-efficiency products and services. Since our founding on June 1, 2002, EnerBank has originated unsecured home improvement loans to approximately one million consumers. We are able to assist these consumers in large part because of our structure as an IB and the FDIC's effective regulation and oversight of the IB industry.

We write in support of the Proposed Rule because we believe it will reinforce the existing comprehensive regulatory regime for IBs by formalizing important standards and promoting additional transparency. To minimize any unintended consequences, we respectfully submit the recommendations below. In particular, we encourage the FDIC to, among other things, harmonize the meaning of "control" with the Federal Reserve Board's framework under the Bank Holding Company Act; preserve the existing majority rule limitation on an IB parent company's board representation; and tailor examination and certain approval requirements based on size and maturity, rather than apply a one-size-fits-all approach.

These proposals are intended to tailor slightly certain aspects of the Proposed Rule to address risk while minimizing disruptions to corporate governance for existing and prospective IBs and their parent companies. We appreciate the FDIC's work on this Proposed Rule and we look forward to serving as a resource, where helpful, as the FDIC finalizes the proposal.

The Proposed Rule Will Formalize Important Existing Requirements and Processes, and Promote Transparency

We support the Proposed Rule as a means of formalizing important existing requirements and processes the FDIC has implemented for IBs and their parent companies. By doing so, the Proposed Rule will also promote more transparency into the licensing and supervisory components of the IB regulatory regime. This greater transparency will instill even more confidence in IBs and provide existing and prospective institutions a uniform understanding of the rules of the road.

IBs and their parent companies are subject to a rigorous and effective regulatory regime that promotes safety and soundness. The FDIC imposes numerous safety and soundness standards on IBs, such as strictly regulating IBs' ability to engage in transactions with affiliates, mitigating conflict of interests between IBs and their parents, and, in certain circumstances, restricting dividend distributions. The FDIC also requires IBs' parent companies to ensure independent audits of their IB subsidiaries are performed annually, and to provide capital and liquidity support to their subsidiary IBs as needed, among other requirements.

Furthermore, an important aspect of the existing framework is the application of Sections 23A and 23B of the Federal Reserve Act to IBs. These two sections impose restrictions on an IB's ability to fund the operations of its affiliated commercial entities. The intermingling of banking and commerce is a common critique of IB subsidiaries owned by non-financial parent companies. Sections 23A and 23B mitigate this risk by appropriately regulating IBs' activities.

To enforce these and other regulations, the FDIC conducts rigorous examinations of IBs. To correct errors or to sanction misconduct, the FDIC utilizes its enforcement power. Pursuant to that power, the FDIC is authorized to issue cease and desist orders and consent orders; levy civil money penalties; and prohibit individuals from exercising control or influence over an IB, among other tools. As a result, very few IBs fail or negatively impact the market or the Deposit Insurance Fund (DIF).

The Proposed Rule would formalize various requirements the FDIC has applied to IBs and their parent companies for a long time through the rulemaking process, thereby creating more transparency and uniformity. By doing so, the Proposed Rule will enable the FDIC to conduct even more effective oversight. Making these expectations formalized in law will also provide clear rules of the road for prospective charter applicants, thereby facilitating charters for qualified, well-informed candidates. Promoting a sound, clear, and uniform yet tailored regulatory framework for IBs is beneficial to the economy as it promotes competition within the banking industry, expands access to credit to consumer and businesses, and reduces the price of credit.

Recommendations

Given the important role IBs play in our economy, maintaining an effective and well-tailored regulatory framework is essential. To that end, we propose for the FDIC's consideration a few recommendations that we believe will tailor certain aspects of the Proposed Rule to minimize operational and administrative challenges. We offer these recommendations in response to specific questions included in the Proposed Rule

> *Question 1: Should the proposed rule apply only prospectively, that is, to industrial banks that become a subsidiary of a parent company that is a Covered Company? Or should the proposed rule also apply to*

> *all industrial banks that, as of the effective date, are a subsidiary of a parent that is not subject to Federal consolidated supervision by the FRB? What are the concerns with each approach?*

To avoid confusion and to ensure the smooth continuance of operations by existing IBs, we recommend that the finalized rule expressly state that existing IBs and their parent companies as of the effective date of this Proposed Rule are not subject to this rule. As the FDIC notes in the Proposed Rule, the proposal is to formalize and strengthen existing processes and policies with which currently operating IBs and their parents comply. As these institutions have demonstrated a long track record of sound operations pursuant to the existing framework and supervision by the FDIC, grandfathering them into the finalized rule would promote the FDIC's stated intent. Moreover, an unambiguous statement that existing IBs and their parent companies comply with the rule would minimize uncertainty within the existing IB marketplace.

> *Question 7: Are the definitions clear in their meaning and application? Should any other terms used in the proposed rule be defined?*

As written, the Proposed Rule defines the term "control" in the same manner as the Change in Bank Control Act (CIBCA). We encourage the FDIC to revise the definition to incorporate the framework for determining control that the Board of Governors of the Federal Reserve (Board) has implemented.

In response to the Board's request for comment about the meaning of control under the Bank Holding Company Act (BHCA) under its proposed rule ("Control and Divestiture Proceedings" (RIN 7100-AF59)), EnerBank informed the Board that the differences between the meaning of control under the CIBCA and the BHCA resulted in confusion by investors which ultimately discouraged them from investing in EnerBank's parent company. In the past, CMS Energy had a large mutual fund shareholder that wanted to increase its ownership above ten percent but was advised against it by its legal counsel due to concerns about application of the Volcker Rule. The shareholder's counsel correctly noted that a control threshold was triggered by exceeding ten percent but failed to note that triggering the CIBCA's disclosure requirements did not preclude the shareholder from rebutting a presumption of control for the Volcker Rule to apply. There is a meaningful concern that many more investors have been and are deterred from increasing their investment about which CMS Energy has no knowledge. CMS Energy is likely not unique because institutional investors tend to avoid increasing their investment in the non-financial parents of IBs above ten percent to avoid the perceived risk of becoming subject to the Volcker Rule.

Aligning the FDIC's definition of control with the Board's new regulatory framework would help minimize confusion and would create a more uniform system based on which banks and their investors can make market-driven decisions rather than regulatory-based decisions.

> *Question 11: The proposed rule would limit board of directors (or similar body) representation to 25 percent of the members of the board of directors (or similar entity). The FDIC has chosen this threshold with the idea that 25 percent is a key threshold for control purposes. Is another threshold more appropriate? If so, what and why?*

While we appreciate the FDIC's interest in ensuring that IBs maintain independent leadership that acts in the best interest of the bank entity, we believe the FDIC's existing majority rule approach is effective and, thus, need not be modified. Currently, IBs' parents are not allowed to control a majority of the board of directors of their IB subsidiaries.

The proposed 25 percent limit, however, would not improve materially the operations or independence of IBs, but it could make the size of boards of directors unworkable. Requiring three outside directors for every insider would require an IB subsidiary to have a 13-person board in order to have just three insider directors. Such large boards would lead to managerial inefficiencies and are inconsistent with corporate governance best practices.

With respect to corporate governance concerns, this provision could further disrupt management when one of the independent members of a smaller board resigns. In the case of a five-member board, the IB would not be in compliance with the rule. As a result, there is risk (or uncertainty, at the least) that the inside director would be forced to cease participating on the board until a new outside director is elected. Such a result would impose unnecessary and harmful disruptions to the IB's operations. Given the success of the existing framework, we believe the operational challenges posed by this requirement would render immaterial any benefits over the existing system. We believe the costs would outweigh any marginal benefits.

Rather than impose a 25 percent limitation, we encourage the FDIC to formalize the existing practice of limiting a parent company's control to less than a majority of the board. Formalizing the majority limitation also recognizes the independence requirements and safeguards already built into the system. For instance, IBs must have an independent management team and a majority of outside directors on its board of directors so they are sufficiently protected from undue influence by their parent companies. Overall, the existing requirements for independent leadership enable smooth corporate governance while allowing IBs to operate under efficient and effective management.

> *Question 12: If there is an individual who is the dominant shareholder of a Covered Company, should that individual be required to commit to the maintenance of appropriate capital and liquidity levels?*

AND

> *Question 17: Should the FDIC retain the authority to require additional written agreements, commitments, or conditions on or by an industrial bank or Covered Company after the nonobjection to a change in bank control, approval of a merger transaction, or a grant of deposit insurance by the FDIC? Should the FDIC retain the power to require additional written agreements, commitments, or conditions on or by an industrial bank or parent company of an industrial bank that became a subsidiary of a parent company that is not subject to Federal consolidated supervision by the FRB prior to the effective date?*

EnerBank recognizes the FDIC's mandate to protect the Deposit Insurance Fund and the attendant need to ensure that financial institutions do not "engage in high-risk or other inappropriate activities." In that effort, certain restrictions are more appropriately tailored according to an institution's size given the risk, complexity, and cost of compliance. For instance, the proposed requirement that all applicants adopt a complex, multi-scenario contingency plan would impose more administrative challenges and costs on low-risk small IBs than it would produce benefits.

Complex dissolution requirements are appropriate for large complex IBs as they have significant assets and obligations and could pose material risks to the DIF. In contrast, the smallest IBs do not pose similar risks or require the same level of complex planning; thus, the costs of the requirement could exceed the benefits. We are encouraged by the FDIC's stated goal of tailoring the contents of a contingency plan and, in certain cases, to tailor

such a plan based on the IB's size, complexity, and other factors. It is important that these factors are applied so that the smallest institutions are not saddled with a significant regulatory burden that does not address material risks. At a minimum, the standard applied to IBs should be the same as the standards to comparable institutions because IBs do not inherently pose more risk to the financial system than other depository institutions. Their contingency planning obligations, therefore, should not be more stringent than other FDIC-insured depository institutions.

Similarly, the proposed requirements in section 354.5 should only apply to IBs during their *de novo* stage rather than throughout their lifetime because the requirements are designed to ensure proper oversight when the IB is building out its operations. For instance, the proposed requirement that an IB obtain prior approval from the FDIC to make a material change to its business plan after it becomes a subsidiary of a Covered Company, irrespective of that IB's historical performance and the sophistication of its leadership, is not tailored adequately to address risk. Such a requirement may be appropriate for *de novo* entities as such institutions are immature. Material changes to such institutions' operations may merit prior review and oversight as the FDIC and the institution are calibrating the risk the institution can absorb. Mature institutions do not pose such problems even when the parent company changes. Equal treatment among depository institutions is also important in this instance as similar restrictions do not apply perpetually to other depository institutions. Mature IBs do not pose a heightened risk that would merit such specialized supervisory oversight.

Additionally, to strike the balance between rigorous oversight and administrative cost and efficacy, we recommend modifying the Proposed Rule to limit examinations to only the holding company subsidiaries that engage in transactions with the affiliated IB. Many holding companies own a significant number of subsidiaries in addition to their IB subsidiary and many of these subsidiaries do not engage with the IB. Examining every subsidiary would impose logistical challenges and costs for the FDIC and regulated entities without resulting in material benefits to either. While additional disclosure and transparency may be appropriate, oversight should be limited to those affiliates with direct interactions with the depository institution.

Conclusion

We are generally supportive of the Proposed Rule because we believe it would reinforce the existing robust regulatory framework for IBs and promote transparency within the examination and supervisory process. As a result, it would help expand access to credit at lower prices by encouraging more applicants to seek and obtain IB charters. We share and support the FDIC's mission to promote the safety and soundness of the banking industry while fostering economic growth. Please do not hesitate to contact me if we can be helpful.

Sincerely,

Charlie Knadler
President and Chief Executive Officer
EnerBank USA