October 10, 2006

Robert E. Feldman
Executive Secretary
Federal Deposit Insurance Corporation
550 17th Street, NW
Washington, DC 20429

Attention: Comments

Re: Notice and Request for Comment, Industrial Loan Companies and Industrial Banks

Dear Mr. Feldman:

The undersigned members of the Sound Banking Coalition – the Independent Community Bankers of America, the National Association of Convenience Stores, the National Grocers Association and the United Food and Commercial Workers International Union – have a strong interest in the regulation and operation of industrial loan companies (ILCs). We are greatly concerned about the tremendous growth of this industry, its impact on the insurance fund, its effect on competition among banks, and the consumer protection implications of these changes. We appreciate the FDIC's thoughtful consideration of this matter and of the views of the public. To that end, we submit the following in response to your Notice and Request for Comment, as published in the Federal Register on August 23, 2006.

Regulation of ILCs is a momentous public policy decision. Currently, the FDIC does not have sufficient regulatory power to adequately oversee these institutions. To properly address this, the FDIC should:

- Extend the ILC moratorium at least six months, until mid-2007, to allow time for Congress to act on the issue. Congress has shown significant interest in this issue this session, although final action has not been taken. With the time pressures imposed by the fall elections, it is clear that no further action will take place this year. Realistically, Congress will need at least six months next year to move on the issue.

- Hold public hearings on the issue. It is critical that the FDIC get as much public input on this issue as possible before making any final decisions. We applauded the agency for holding hearings on the Wal-Mart ILC application for just that reason. The over-arching policy issues that will provide the guidelines for FDIC going forward deserve at least the same amount of careful public deliberation.

- Endorse congressional legislation that would bolster regulatory authority over ILCs and limit or eliminate the ability of commercial entities to own ILCs. Representatives Gillmor and Frank have introduced legislation that would allow limited commercial activities, while Representative Leach is sponsoring a bill calling for a complete ban; both bills augment the authority of regulators to supervise these institutions and their parent companies.

These issues are vitally important. You have also raised several key questions in your request for comments. We answer those questions, in turn, below.

1. Have developments in the ILC industry in recent years altered the relative risk profile of ILCs compared to other insured depository institutions? What specific effects have there been on the ILC industry, safety and soundness, risks to the Deposit Insurance Fund, and other insured depository institutions? What modifications, if any, to its supervisory programs or regulations should the FDIC consider in light of the evolution of the ILC industry?

Since the ILC loophole was adopted in 1987, the ILC industry has grown dramatically in assets and powers, it has seen a great deal of consolidation, and the mixing of banking and commerce has become more common in the industry as more commercial entities have purchased ILCs. Assets in these institutions grew 3500 percent between 1987 and 2004. As the number of ILCs has declined due to consolidation, the average size of ILC's has grown to over \$2.5 billion. According to the Government Accountability Office (GAO), three of the six ILC charters issued since June 2004 are owned by commercial entities.[1] All these factors affect the safety and soundness profile of the ILC industry and, because most of these institutions are insured by the FDIC, these developments increase the risk ILCs pose to the Deposit Insurance Fund (the Fund). Moreover, the potential for adding more banking authority to the current powers of ILCs threatens to exacerbate those risks.

The Federal Reserve on numerous occasions has opined on the threat posed by ILCs to the banking system and the insurance fund. In testimony before the House Financial Services Committee in February of this year, Federal Reserve Board Chairman Ben Bernanke urged Congressional review and action with respect to the regulation of ILCs. The following month, Federal Reserve Governor Donald L. Kohn testified to the Senate Committee on Banking, Housing and Urban Affairs that, "the Board continues to believe that Congress should *not* grant this new (de novo) branching authority to ILCs unless the corporate owners of these institutions are subject to the same type of consolidated supervision and activities restrictions as the corporate owners of other full-service insured banks."

The Board's current policy is clearly consistent with the views of former Board Chairman Alan Greenspan. In a letter to Representative James Leach (R-IA) on January 6, 2006, Chairman Greenspan described the current and growing threat to the nation's financial system posed by ILCs.

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1 Government Accountability Office. 2005. "Recent Asset Growth and Commercial Interest Highlight Differences in Regulatory Authority." GAO-05-621, September 2005 (GAO Report).

> When this exemption was adopted in 1987, ILCs were mostly small locally owned institutions that had only limited deposit-taking and lending powers. However, much has changed since 1987 and recent events and trends highlight the potential for this exemption to undermine important general policies established by Congress that govern the banking system and to create an unlevel competitive playing field among banking organizations. The total assets held by ILCs have grown by more than 3,500 percent between 1987 and 2004, and the aggregate amount of estimated insured deposits held by ILCs has increased by more than 500 percent since 1999.
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> The character, powers and ownership of ILCs have changed materially since Congress first enacted the ILC exemption. These changes are undermining the prudential framework that Congress has carefully crafted and developed for the corporate owners of other full-service banks. Importantly, these changes also threaten to remove Congress' ability to determine the direction of our nation's financial system with regard to the mixing of banking and commerce and the appropriate framework of prudential supervision. These are crucial decisions that should not be made through the expansion and exploitation of a loophole that is available to only one type of institution chartered in a handful of states.

We agree that the FDIC does not currently have sufficient regulatory authority to comprehensively oversee these growing and complex institutions. Bank holding companies are subject to consolidated holding company supervision to ensure that the holding company and its subsidiaries do not create solvency risks for the bank and to ensure that the holding company can be a source of strength for the bank. Unlike the Federal Reserve or the Securities and Exchange Commission, which have consolidated oversight authority, the FDIC does not have the power to examine an ILC holding company or affiliate except in connection with the ILC's relationship with the parent or affiliate. This deprives ILCs of the basic protections afforded other banks and leaves the Deposit Insurance Fund susceptible to the vagaries of the commercial marketplace. According to the GAO, even this limited authority appears to be circumscribed. The GAO has stated that "questions remain about whether FDIC's supervisory approach and authority over … holding companies and their non-bank subsidiaries address all risks to the ILC from these entities."[2]

The lack of consolidated supervision of ILCs and the mixing of banking and commerce that occurs when a commercial entity owns a bank threaten some of the basic underpinnings of

2 GAO Report, p.7.

banking regulation in the United States and could have a significant impact on SBC members, consumers, and the financial services marketplace as a whole. The FDIC needs increased authority to supervise these entities. That is why we believe congressional action is necessary. There are currently two bills in Congress that address these important issues. The Industrial Bank Holding Company Act of 2006, introduced by Representatives Paul Gillmor (R-OH) and Barney Frank (D-MA), would bolster the FDIC's supervisory authority over ILC holding companies and thereby reduce risks to the Deposit Insurance Fund. The bill also limits the amount of commercial activity in which an ILC holding company may engage, thus greatly reducing the threats posed by the banking/commerce mix. Legislation introduced by Representative Leach would ban commercial entities from owning ILCs, and would subject owners of ILCs to the same type of consolidated regulatory supervision as bank holding companies. We urge the FDIC to work with Congress to pass such legislation.

2. Do the risks posed by ILCs to safety and soundness or to the Deposit Insurance Fund differ based upon whether the owner is a financial entity or a commercial entity? If so, how and why? Should the FDIC apply its supervisory or regulatory authority differently based upon whether the owner is a financial entity or a commercial entity? If so, how should the FDIC determine when an entity is "financial" and in what way should it apply its authority differently?

The ownership of an ILC, specifically whether the owner is a commercial or financial entity, can affect the risks to the institution's safety and soundness and to the Deposit Insurance Fund. Commercial entities pose greater safety and soundness risks than financial entities because they tend to be riskier businesses, more entrepreneurial, and less regulated. This is generally desirable in a commercial entity from a policy perspective because we want to encourage creativity, experimentation, and increased productivity. This creates wealth and is good for the economy.

Banks are different and for good reason. We want banks to be more cautious and maintain strong safety and soundness protections because of their important role in securing and growing capital for depositors. For these reasons, banks are subject to comprehensive regulatory oversight, part of which requires them to maintain sufficient capital reserves to cover their risks. In contrast, rather than holding cash in reserve, commercial entities are generally designed to invest excess dollars in research and development, new products, investments, or other activities that will improve the company's bottom line. The implications of this difference can be great for ILCs. If a commercially-owned ILC is in trouble, there is no guarantee that its parent will be a "source of strength" and have the resources to assist. Moreover, if the commercial parent of an ILC is in trouble, it might look to the ILC for a capital infusion when that might not be in the best interest of the ILC.

We believe the FDIC should apply its supervisory and regulatory authority in a consistent manner across the board. Having said that, however, we believe there is a need for more comprehensive regulatory oversight when an ILC is owned by a commercial entity that is not subject to the Bank Holding Company Act, as opposed to one that is owned by a financial entity already subject to consolidated supervision by the Federal Reserve or holding company regulation by the Securities and Exchange Commission or other federal or state regulators. Simply stated, commercial entities that own ILCs need greater supervision. All of these factors require enactment of the Gillmor-Frank legislation discussed above.

3. Do the risks posed by ILCs to safety and soundness or to the Deposit Insurance Fund differ based on whether the owner is subject to some form of consolidated Federal supervision? If so, how and why? Should the FDIC assess differently the potential risks associated with ILCs owned by companies that (i) are subject to some form of consolidated Federal supervision, (ii) are financial in nature but not currently subject to some form of consolidated Federal supervision, or (iii) cannot qualify for some form of consolidated Federal supervision? How and why should the consideration of these factors be affected?

We believe that safety and soundness and the Fund face the least risk from an ILC that is owned by an entity that engages in activity that is financial in nature and is subject to consolidated federal supervision. As stated above, banks are generally more cautious in nature, avoiding risks that commercial entities must take to remain competitive. In addition to the nature of the institutions, consolidated federal supervision ensures that the ILC parent is healthy and that interactions between parent and the ILC, and between the ILC and other subsidiaries, are legitimate and not detrimental to the financial health of the institution.

As stated above, although ILCs are subject to FDIC oversight, the FDIC has more limited regulatory powers with respect to holding companies and affiliates than does the Federal Reserve. The Bank Holding Company Act (BHCA) provides the Federal Reserve with the authority to examine the bank holding company itself and any of its non-bank subsidiaries at any time, while the FDIC has only limited examination authority, and is unable to examine affiliates of banks unless necessary to disclose the direct relationship between the bank and affiliate and the effect of the relationship on the bank.[3]

Moreover, the Federal Reserve is entitled to establish consolidated capital requirements to ensure that bank holding companies are a source of financial strength for the subsidiary bank. This source of strength doctrine has been codified in Regulation Y, which specifies that a bank holding company parent should be ready to provide capital to its bank subsidiary when needed. Failure to provide such assistance would enable the regulator to take enforcement action to protect the bank. In contrast, corporate parents of ILC's are not subject to these capital requirements.

[3] Letter to Senator Tim Johnson from Alan Greenspan, Chairman of the Board of Governors of the Federal Reserve System, June 25, 2003, at 4.

Finally, the Federal Reserve has broad enforcement authority under the BHCA, and can issue cease and desist orders, impose civil penalties, and order a holding company to divest non-bank subsidiaries if it determines that ownership of the subsidiary presents a risk to the financial safety, soundness, or stability of an affiliated bank and is inconsistent with sound banking principles or the purposes of the BHCA.[4] The Federal Reserve is the only federal agency authorized to take such actions against bank holding companies.

Some financial institutions – insurance companies, for example – are not subject to consolidated supervision. Despite this, these entities generally present less risk to a subsidiary's safety and soundness and to the Fund than commercial institutions because they are regulated in their own right. That is, unlike a commercial entity that is not likely to be subject to any oversight, an insurer or other financial institution that is not subject to consolidated supervision remains subject to the regulatory oversight of its primary regulator. Thus, the financial institution/parent would be subject to FDIC oversight with respect to its relationship with its ILC subsidiary, and to direct regulation in areas such as solvency, consumer protection, and so forth.

The safeguards such as those provided by the Federal Reserve and other financial regulators are necessary to protect the Fund against the potential risks presented by ILCs. Without these safeguards, it may be impossible for problems to be identified and managed in time to prevent deficiencies and damage to the federal safety net.

4. What features or aspects of a parent of an ILC (not already discussed in Questions 2 and 3) should affect the FDIC's evaluation of applications for deposit insurance or other notices or applications? What would be the basis for the FDIC to consider those features or aspects?

As discussed further in our response to question 5 below, the FDIC has broad statutory authority to evaluate applications for deposit insurance and changes in control. Using this authority as the basis for its evaluation, there are several features of an ILC parent that the FDIC should review including the size of the entity, its market reach/market penetration, its behavior in the marketplace, the impact on the entity's competition in both commercial and financial matters, and the character of the applicant. All of these features of the parent company can affect the safety and soundness of the ILC, the risk posed to the Fund, the adequacy of the institution's capital structure, and the impact on the community.

5. The FDIC must consider certain statutory factors when evaluating an application for deposit insurance (see 12 U.S.C. 1816), and certain largely similar statutory factors when evaluating a change in control notice (see 12 U.S.C. 1817(j)(7)). Are these the only factors FDIC may consider in making such evaluations? Should the consideration of these factors be affected based on the nature of the ILC's proposed owner? Where

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4 *Id.* at 5.

an ILC is to be owned by a company that is not subject to some form of consolidated Federal supervision, how would the consideration of these factors be affected?

The FDIC, pursuant to the Federal Deposit Insurance Act, has broad discretion to evaluate and rule on a bank's application for federal deposit insurance.[5] The FDIC is required to consider seven factors to determine whether to approve a bank's application. Those factors are: (1) the financial history and condition of the depository institution; (2) the adequacy of the depository institution's capital structure; (3) the future earnings prospects of the depository institution; (4) the general character and fitness of the management of the depository institution; (5) the risk presented by such depository institution to the Deposit Insurance Fund; (6) the convenience and needs of the community to be served by such depository institution; and (7) whether the depository institution's corporate powers are consistent with the purposes of the Act.[6]

An application decision by the FDIC is valid if: (1) it is based on the factors prescribed by the Act; and (2) there is a reasoned path from the facts before the FDIC and its decision on the application.[7] These statutory factors and case law make clear that FDIC has ample discretion to do what is right in evaluating these applications. That includes properly looking into the nature of the institution and whether it is subject to consolidated supervision

Courts review an application decision by the FDIC under § 706 of the Administrative Procedure Act to determine if the decision is, "arbitrary, capricious, an abuse of discretion or otherwise not in accordance with law."[8] An FDIC application decision will withstand judicial review if the agency "examined the relevant data and articulated a satisfactory explanation for its action including a 'rational connection between the facts found and the choice made."[9] For instance, in *Anderson v. FDIC*, the Sixth Circuit upheld the FDIC's denial of a bank's application based on one of the bank officer's alleged past improper banking actions.[10]

In *Anderson*, organizers of the Bank of Michigan filed an application for federal deposit insurance with the FDIC. The bank's principle officer, Stanford Stoddard, had previously been subject to an administrative proceeding by the Office of the Comptroller of the Currency ("OCC") for allegedly breaching his fiduciary duties and engaging in unsafe and unsound banking practices while working for another bank. The OCC action against Mr. Stoddard was dismissed by the D.C. Circuit on procedural grounds.[11] The FDIC, however, reexamined the

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5 12 U.S.C. § 1815(a) (2000).

6 12 U.S.C. § 1816.

7 *Anderson v. FDIC*, No. 96-2574, 1997 U.S. App. LEXIS 22507, at *9 (6th Cir. Aug. 19, 1997).

8 *Id.*; 5 U.S.C. § 706(2)(A)

9 *Anderson*, 1997 U.S. App. LEXIS 22507, at *9 (quoting *Simms v. National Highway Traffic Safety Admin.*, 45 F.3d 999, 1004-1005); *See also*, *Motor Vehicle Mfrs. Ass'n v. State Farm Mut. Auto. Ins. Co.*, 463 U.S. 29, 43 (1983) (quoting *Burlington Truck Lines, Inc. v. United States*, 371 U.S. 156, 168 (1962)).

10 *Anderson* 1997 U.S. App. LEXIS 22507, at *10-12.

11 *See*, *Stoddard v. Board of Governors of the Fed. Reserve Sys.*, 868 F.2d 1308, 1310-12 (D.C. Cir. 1989).

charges brought by the OCC against Mr. Stoddard and concluded that as a result of the allegations the bank failed to satisfy the statutory requirements regarding the "general character and fitness of the management of the depository institution" and "the risk presented by such depository institution to the Deposit Insurance Fund."[12] The Sixth Circuit held that the past allegations provided sufficient evidence for the FDIC to reach its conclusions and deny the bank's application for federal deposit insurance.[13]

Thus, based on the caselaw, it is clear that, when the FDIC is reviewing an application, it has the authority, indeed is required, to consider all of the seven factors listed above – including the "character and fitness" factor – in the broadest possible way.[14] The nature of the proposed owner – commercial or financial – is as integral part of the FDIC's determination as the fitness of the institution. With respect to the financial fitness of an institution, the FDIC should consider more than simply the information provided by the applicant. The lack of consolidated supervision of ILCs must be considered as a major factor in determining the financial condition, the capital structure, and the risk to the Fund posed by an applicant. The FDIC must consider how this lack of oversight will affect the entity going forward. Moreover, the FDIC must consider all comments received in connection with an application, and, importantly, has the discretion to reject an application. Furthermore, the courts are to give deference to the FDIC's decision.

6. Should the FDIC routinely place certain restrictions or requirements on all or certain categories of ILCs that would not necessarily be imposed on other institutions (for example, on the institution's growth, ability to establish branches and other offices, ability to implement changes in the business plan, or capital maintenance obligations)? If so, which restrictions or requirements should be imposed and why? Should the FDIC routinely place different restrictions or requirements on ILCs based on whether they are owned by commercial companies or companies not subject to some form of consolidated Federal supervision? If such conditions are believed appropriate, should the FDIC seek to establish the underlying requirements and restrictions through a regulation rather than relying upon conditions imposed in the order approving deposit insurance?

We do not object to the FDIC placing restrictions or requirements on all or certain categories of ILCs but not on others. Having said that, however, we do not believe the imposition of such restrictions is an effective way to permanently control the behavior of an ILC or ILC parent, nor is it an effective way to protect for safety and soundness or prevent risk to the

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12 *Id.*

13 *Id.* at 13.

14 It is clear, for example, that the questions raised about "character and fitness" in the Anderson care are far less substantial than those raised about a current applicant – Wal-Mart. While the allegations against Stoddard were dismissed in court, Wal-Mart has been subject to large and repeated penalties for legal violations in areas ranging from employment to immigration. These violations are precisely the type of thing the FDIC must consider according to the Sixth Circuit.

Fund. The FDIC has consistently maintained that it could reconsider restrictions on an approval at a future date – such as after three years. That does not provide sufficient protection. If the FDIC wishes to place effective restrictions on an applicant, the restrictions must actually be permanent. If the FDIC does not have authority to do this, it should seek statutory authority to do so.

7. Can there be conditions or regulations imposed on deposit insurance applications or changes of control of ILCs that are adequate to protect an ILC from any risks to safety and soundness or to the Deposit Insurance Fund that exist if an ILC is owned by a financial company or a commercial company? In the interest of safety and soundness, should the FDIC consider limiting ownership of ILCs to financial companies?

As stated in our response to question 6, we question the effectiveness of such restrictions because they can be changed in the future. As opposed to relying on such restrictions, we believe legislation such as the Gillmor-Frank bill or the Leach bill should be enacted to provide regulators with the clear authority to more closely oversee ILC parent companies and to exclude entities that are commercial from owning an ILC.

8. Is there a greater likelihood that conflicts of interest or tying between an ILC, its parent, and affiliates will occur if the ILC parent is a commercial company or a company not subject to some form of consolidated Federal supervision? If so, please describe those conflicts of interest or tying and indicate whether or to what extent such conflicts of interest or tying are controllable under current laws and regulations. What regulatory or supervisory steps can reduce or eliminate such risks? Does the FDIC have authority to address such risks in acting on applications and notices? What additional regulatory or supervisory authority would help reduce or eliminate such risks?

Mixing banking and commerce increases the opportunity and likelihood that conflicts of interest will arise. In the U.S. system, banks are meant to be neutral arbiters of capital. They lend based on economic fundamentals, leading to more efficient economic development. Allowing a commercial company to own and operate a bank risks skewing that role. The temptation for an entity active in the commercial marketplace to withhold loans from its competitors and steer funds toward firms with which it does business is likely to be overwhelming. That conflict of interest would threaten – not enhance – commercial competition in the marketplace in which such a bank would operate.

This is not a hypothetical concern. The Home Depot's application for deposit insurance in connection with its acquisition of EnerBank USA illustrated the serious questions about tying bank products with commercial sales that can arise when a commercial entity owns a bank.

The Notice submitted to the FDIC by Home Depot clearly states that EnerBank and the company "share a common focus on the home improvement market." Further, the document notes that the bank's relationships with contractors and trade professionals "fits with The Home Depot's desire to expand its relationships with contractors and trade professionals – especially the local, small contractors that are core to The Home Depot's business." Although the Notice states that no bank loan will be tied to purchases from the company, it remains unclear exactly how this relationship will work without leading to consumer confusion regarding the status and identity of the lender. The scheme risks significant consumer confusion as to where the division between the bank and the company lies. Although the Notice does not provide details about the company's statement that no EnerBank loan will be tied purchases at Home Depot stores, it seems reasonable to assume that borrowers might feel some pressure from contractors who do business with the company to borrow from EnerBank. In addition, although the company forswears explicitly tying loans with product purchases, there is no discussion in the Notice as to whether there will be other incentives for borrowers to become Home Depot customers or vice versa.

That is one of the primary reasons Congress traditionally drew a line between banking and commerce – a line that has been upheld by Republicans and Democrats alike. Indeed, that line was reinforced with the enactment of the Gramm Leach Bliley Act (GLBA) in 1999. GLBA recognized the interrelationship between banking and other financial services and strengthened the line of separation between banking and commerce by ending the unitary thrift loophole, which had previously allowed commercial firms to get into banking.

Greater mixing of commerce and banking could lead to the following scenarios:

- **In small towns, businesses may have no choice but to seek bank services from an ILC owned by a competitor, which may be reluctant to grant loans to retailer competitors of its parent company.** If competitor banks are destroyed, surviving local businesses would be forced to go to their competitor for deposits and loans, providing the parent company with an even greater competitive advantage in both retail and banking, effectively restricting access to capital for local businesses – especially in smaller communities where there may be few banking alternatives for small retailers. This would bring to life the nightmare scenario that is a key reason for the longstanding U.S. policy prohibiting the mixture of banking and commerce.

- **An ILC might require confidential business information from a loan applicant before providing financing.** If an ILC is owned by a competitor of a loan applicant, the conflict of interest inherent in the commerce/ banking mix could force local retailers to essentially provide their business plans to their competition (the ILC parent).

- **To secure a loan, local businesses may be forced to alter business plans.** The conflict of interest could also lead local retailers to change business plans, pricing structures and markets in order to secure financing. These changes might be required by the "lender" and thus inherently suspect, or they might be steps taken by the loan applicant in order to smooth the way to secure financing. Either way, it would be a distortion of the market and potentially very harmful to the business prospects for the small business.

- **Costs to bank customers could increase.** Finally, loss of competition could, ultimately, lead to increased costs for consumers. According to a 2001 report by PIRG, average rates for checking account and other depository services are 15% lower at small banks than at large, multi-state banks. An ILC owned by a giant commercial entity would only exacerbate this difference.

Keeping commercial entities out of the banking business is the key way to resolve these problems. While some argue that some of these influences on ILC lending would be illegal, we all know that people are sometimes willing to break the law for monetary gain. The problem is that many of these abuses will be exceedingly hard to detect. For the FDIC, what is essential is ensuring that there are rules in place that best protect against known dangers like these – by stopping the situations that foster them and allowing regulators more opportunity to detect them if they do occur.

The FDIC's limited authority to review transactions between a parent and ILC – and not the entire relationship between the ILC and the holding company and affiliates, and not the financial health of the entire entity – puts the agency at a distinct disadvantage in reducing/eliminating the conflicts of interest that could arise with the mixing of banking and commerce. Again, we believe the Gillmor-Frank bill, with its limitation on the extent to which a parent company may engage in commercial activities and its bolstering of FDIC authority, would go a long way in reducing these risks.

9. Do ILCs owned by commercial entities have a competitive advantage over other insured depository institutions? If so, what factors account for that advantage? To what extent can or should the FDIC consider this competitive environment in acting on applications and notices? Can those elements be addressed through supervisory processes or regulatory authority? If so, how?

ILCs owned by commercial entities are advantaged over ILC's owned by financial entities in a number of ways:

- Less comprehensive regulation at the holding company level, leaving the ILC free to engage in more/different activities that might be prohibited for financial institutions;

- Use of capital: commercial entities have more freedom to use their capital as they please because they are not subject to reserve requirements that financial institutions must satisfy under the consolidated supervision rules;

- Concentration of capital: banks use capital for lending – spreading access to capital to non-financial institutions, thus growing the economy. Commercial entities may choose to concentrate capital rather than lend to their competitors, thus harming those seeking loans and the economy as a whole; and

- Cross marketing, tying, etc: commercial entities have a built-in opportunity to cross market financial products with commercial products. For example, lending a customer the funds to purchase a commercial item from the parent company.

These amount to substantial financial and market advantages for ILCs owned by commercial, as opposed to financial, entities, and they provide similar benefits to the parent companies. In addition to raising questions of fairness and equal treatment, these "advantages" could pose risks to the safety and soundness of ILCs and to the Fund because the current regulatory framework is unable to adequately oversee these institutions.

10. Are there potential public benefits when a bank is affiliated with a commercial concern? Could those benefits include, for example, providing greater access to banking services for consumers? To what extent can or should the FDIC consider those benefits if they exist?

Expansion of banking opportunities is critical for the health and growth of the economy and for individual consumers and businesses to succeed financially. We do not believe, however, that expansion of banking access requires – or benefits from – commercial ownership of banks. Such affiliations are not only detrimental in the long-run, they are not necessary. Today, there are thousands of community bank branches doing business inside commercial businesses – supermarkets, for example. These arrangements offer the benefits of consumer access but suffer from none of the conflicts of interest or unfair competition problems that would face a bank owned by the commercial entity. This is the preferred model and ought to be fostered by preventing commercial ownership of ILCs rather than squelched by allowing huge commercial companies to take over ILCs and put these community banks out of business.

11. In addition to the information requested by the above questions, are there other issues or facts that the FDIC should consider that might assist the FDIC in determining whether statutory, regulatory, or policy changes should be made in the FDIC's oversight of ILCs?

As the FDIC considers whether statutory, regulatory or policy changes should be made with respect to ILC oversight, we urge you to consider the original purpose of ILCs and of the ILC loophole in the BHCA. As former Federal Reserve Chairman Alan Greenspan noted in his letter to Representative Leach in January 2006, "When this exemption was adopted in 1987, ILCs were mostly small locally owned institutions that had only limited deposit-taking and lending powers." ILCs were intended to be small institutions that address specific market/ consumer needs. Ownership of ILCs by large commercial institutions turns this purpose on its head. The FDIC should look with some unease at the dramatic change in the ILC industry – and the potential for further change – by the entrance of huge commercial companies. This could fundamentally change the character of the loophole as written by Congress, which is further reason for the FDIC maintaining the moratorium until Congress has had an opportunity to act.

12. Given that Congress has expressly excepted owners of ILCs from consolidated bank holding company regulation under the Bank Holding Company Act, what are the limits on the FDIC's authority to impose such regulation absent further Congressional action?

Congressional action in this area – either the Gillmor-Frank model, Leach model or another model – is needed. But the FDIC can and should play a leading role. First, FDIC should extend the moratorium to give Congress time to act. As we stated at the outset, Congress has shown significant interest in this issue this session. With the time pressures imposed by the fall elections, however, it is clear that no further action will take place this year. Realistically, Congress will need at least six months to move on the issue. Thus, we urge an extension of the moratorium to mid-2007 at the earliest. Second, FDIC should hold public hearings to further flesh out the issues raised in this comment letter and in the submissions of other interested parties. Third, FDIC ought to voice its support for legislation that will provide additional regulatory powers enabling comprehensive regulation of ILCs and their parent companies.

Thank you for your consideration of our views.

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