

## FDIC – Industrial Loan Companies (ILC) Final Rule

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


The purpose of the proposed rule is to codify existing practices utilized by the FDIC to supervise ILC and their parent companies, to mitigate undue risk to the DIF [Deposit Insurance Fund] that may otherwise be presented in the absence of Federal consolidated supervision of an ILC and its parent company, and to ensure that the parent company that owns or controls an ILC serves as a source of financial strength for the ILC, consistent with Section 38A of the FDI [Federal Deposit Insurance] Act. With the exception of the added reporting for systems for PII, the balance of the revisions, although modest, were in the ILC applicant's favor. The rule provides a clearer process regarding expectations and should make the approval process clearer in which to comply.


### Key Changes


1. The final rule is largely consistent with the proposed rule, with the exception of a) Revises the commitment of each parent company to limit its representation on the ILC's board to less than 50 percent from no more than 25 percent b) Subsidiary ILC to obtain the FDIC's prior approval to add or replace a member of the board of directors, or to add or replace a senior executive officer of the ILC only for a period of three-year period as opposed to perpetual basis c) Additional reporting requirement on systems for protecting the security, confidentiality, and integrity of consumer and nonpublic personal information
2. The rule rules applies to institutions prospectively
3. The FDIC defends the regulatory framework around ILCs drawing parallels to state non-member banks and making it clear they have the tools to govern / manage both non-financial and financial ILCs and affiliate relationships
4. Provides clarity to the approval process of what tools the FDIC has
5. The FDIC does not wade into the debate on non-financial ILCs, makes it clear that they will apply the law as it stands
6. April 1, 2021 Effective Date - While this is a fairly long time for an effective date, the FDIC has made it clear they will continue to be processing "pending" deposit insurance applications. This appears to mean that applications that have been received and are in pending status will be processed in a similar manner to past ILC application, such as Square and Nelnet. Additional clarity is needed regarding how applications submitted between 12/15/20 and 4/1/21 will be processed. It is likely they will still be processed, but not submitted to the FDIC Board for approval.


### FDIC considers ILC Bank similar to other Charter Types

- The FDIC has not found that ILCs pose unique safety and soundness concerns based on the activities of the parent organization.
- ILCs are subject to all of the same restrictions and requirements, regulatory oversight, and safety and soundness exams as any other kind of insured depository institution. As such, the risks posed are substantially similar to those of all other charter types.
- At year-ends 2009 through 2011, ILCs maintained a median tier 1 leverage capital (T1LC) ratio between 13.1 percent and 15.4 percent, whereas, other insured institutions maintained a median T1LC ratio between 9.3 percent and 9.7 percent. The capital and earnings ratios for ILCs is reflective of the higher degree of risk inherent in their business models
- When compared to other insured institutions, ILCs typically maintain a lower volume of liquid assets and rely more heavily on non-core liabilities to fund longer- term earning assets. As a result, while still satisfactory, the liquidity posture for ILCs was considered slightly lower both during and subsequent to the 2008-09 financial crisis. In the FDIC's experience, asset quality has been comparable between ILCs and other insured institutions.

Themes	Potential Impact	Potential Impact Description
<p><b>Minor Clarification:</b> Timing Update and wording clarification</p>	 Low	<p>The proposed rule would have divided the rule into two temporal states, on or before the effective date on the one hand, and after the effective date on the other hand. The final rule amends the dividing line so that the relevant timeframes would be before the effective date and on or after the effective date. FDIC has made it clear they will continue to be processing “pending” deposit insurance applications. This appears to mean that applications that have been received and are in pending status will be processed in a similar manner to past ILC application. Additional clarity is needed regarding how applications submitted between 12/15/20 and 4/1/21 will be processed. It is likely they will still be processed, but not submitted to the FDIC Board for approval.</p> <p>Minor wording clarifications have been made (e.g., explicit use of language to state applicability related to nonfinancial commercial firms)</p>
<p><b>Flexibility:</b> Board— Independence Threshold flexibility</p>	 High	<p>Limited the Covered Company's direct and indirect representation on the board of directors or board of managers, as the case may be, of each subsidiary ILC to less than 50 percent of the members (from no more than 25%) of such board of directors or board of manager. The revision aligns with ILC business models and support flexibility in including members with direct experience with bank operations.</p>
<p><b>Additional Reporting:</b> Reporting Requirement</p>	 High	<p>In response for covered companies that are not engaged in financial services that are not covered by GLBA, the rule added reporting on Systems for protecting the security, confidentiality, and integrity of consumer and nonpublic personal information. This likely will have more of an impact on covered companies that are non-financial in nature and not covered by GLBA</p>
<p><b>Flexibility:</b> Requirements removed related to additional commitment/restrictions</p>	 High	<p>Removed the requirement related to additional commitments required by a Covered Company or by an individual who is a controlling shareholder of a Covered Company. This was removed in response to concerns regarding the FDIC having the ability to have open-ended authority over covered companies or controlling shareholders and provides flexibility to the banks.</p> <p>Additionally, also removed requirement around imposing additional restrictions on the activities or operations of an ILC that is controlled by a Covered Company to avoid confusion that the FDIC would unilaterally impose additional commitments/restrictions.</p>
<p><b>Flexibility:</b> Three Year Limitation on requirement of FDIC approval on add or replace a member of the board of directors/ senior executive officer</p>	 High	<p>Revised to include a three-year limitation on the requirement of written approval to employ of a senior executive officer who is, or during the past three years has been, associated in any manner (e.g., as a director, officer, employee, agent, owner, partner, or consultant) with an affiliate of the ILC to allow ILCs flexibility to appoint directors and officers in a timely manner. A three-year limitation was added representing the de novo period to allow ILCs the flexibility to appoint directors and officers in a timely manner since FDIC approval would not be needed outside of the three-year period.</p>

 **High Impact** – Results in some process changes and additional effort required (Reporting)

 **Medium Impact** – Results in some process changes but no additional effort required (25% & 3-year)

 **Low Impact** – Results in no direct impact and no additional effort (Effective date, FDIC authority)

## Written Commitments

No ILC may become a subsidiary of a Covered Company unless the Covered Company enters into one or more written agreements with both the FDIC and the subsidiary ILC, which contain commitments by the Covered Company to comply with the requirements listed below.

#	Written Commitments
1	Each Covered Company must provide an initial listing of all of the Covered Company's subsidiaries and update such list annually;
2	Provide Consent to the examination by the FDIC of the Covered Company and each of its subsidiaries to permit the FDIC to assess compliance with the provisions of any written agreement, commitment, or condition imposed; the FDI Act; or any other Federal law for which the FDIC has specific enforcement jurisdiction against such Covered Company or subsidiary, and all relevant laws and regulations.
3	Submit to the FDIC an annual report describing the Covered Company's operations and activities, in the form and manner prescribed by the FDIC, and such other reports as may be requested by the FDIC to inform the FDIC as to the Covered Company's: (i) financial condition; (ii) systems for identifying, measuring, monitoring, and controlling financial and operational risks; (iii) transactions with depository institution subsidiaries of the Covered Company; (iv) systems for protecting the security, confidentiality, and integrity of consumer and nonpublic personal information and (v) compliance with applicable provisions of the FDI Act and any other law or regulation.
4	Maintain records as the FDIC deems necessary to assess the risks to the ILC and to the DIF .
5	Use an independent audit of each subsidiary ILC to be performed annually.
6	Limit its direct and indirect representation on the ILC's board of directors to less than 50% percent of the members of the board, or board of managers, in the aggregate, and, in the case of a subsidiary ILC that is organized as a member-managed limited liability company, limit the Covered Company's direct and indirect representation as a managing member to less than 50 percent of the managing member interests of the subsidiary ILC , in the aggregate.
7	Maintain the capital and liquidity of the subsidiary ILC at such levels as the FDIC deems appropriate, and take such other actions as the FDIC deems appropriate to provide the subsidiary ILC with a resource for additional capital and liquidity including, for example, pledging assets, obtaining and maintaining a letter of credit from a third-party institution acceptable to the FDIC, and providing indemnification of the subsidiary industrial ban.
8	Execute a tax allocation agreement with its subsidiary ILC that expressly states that an agency relationship exists between the Covered Company and the subsidiary ILC with respect to tax assets generated by such ILC, and that further states that all such tax assets are held in trust by the Covered Company for the benefit of the subsidiary ILC and will be promptly remitted to such ILC. The tax allocation agreement also must provide that the amount and timing of any payments or refunds to the subsidiary ILC by the Covered Company should be no less favorable than if the subsidiary ILC were a separate taxpayer.
9	Outside of the 8 commitments, The FDIC may require such Covered Company and ILC to commit to provide to the FDIC, and, thereafter, implement and adhere to, a contingency plan subject to the FDIC's approval that sets forth, at a minimum, recovery actions to address significant financial or operational stress that could threaten the safe and sound operation of the ILC and one or more strategies for the orderly disposition of such ILC without the need for the appointment of a receiver or conservator.

#	Restrictions on ILC subsidiaries of Covered Companies
1	Without the FDIC's prior written approval, an ILC that is controlled by a Covered Company shall not: (a) Make a material change in its business plan after becoming a subsidiary of such Covered Company; (b) Add or replace a member of the board of directors, board of managers, or a managing member, as the case may be, of the subsidiary ILC during the first three years after becoming a subsidiary of such Covered Company; (c) Add or replace a senior executive officer during the first three years after becoming a subsidiary of such Covered Company; (d) Employ a senior executive officer who is, or during the past three years has been, associated in any manner (e.g., as a director, officer, employee, agent, owner, partner, or consultant) with an affiliate of the ILC; or (e) Enter into any contract for services material to the operations of the ILC (for example, loan servicing function) with such Covered Company or any subsidiary thereof.

For additional details on Banking Charter options and services related to applying, implementing and standing up digital banking operations, refer to: [Business model strategy for financial services.](#)

# Appendix:

## FDIC ILC Proposed Rule Changes

[This link compares the FDIC's ILC Proposed and Final Rule, in regard to Parent Companies of ILCs and Industrial Loan Companies.](#)

## FDIC ILC Final – How it effects Procedures Manual Supplement for Non-Bank Applicant

[Potential impact of revisions from the Proposed to Final rule related to Procedures Manual Supplement.](#)

## Sources

Fact Sheet: [https://www.fdic.gov/news/fact-sheets/ilc-12-15-20.pdf?source=govdelivery&utm\\_medium=email&utm\\_source=govdelivery](https://www.fdic.gov/news/fact-sheets/ilc-12-15-20.pdf?source=govdelivery&utm_medium=email&utm_source=govdelivery).

1. Statement by FDIC Chairman Jelena McWilliams on the Final Rule for Parent Companies of ILCs and Industrial Loan Companies at the FDIC Board Meeting: [https://www.fdic.gov/news/speeches/spdec1520c.html?source=govdelivery&utm\\_medium=email&utm\\_source=govdelivery](https://www.fdic.gov/news/speeches/spdec1520c.html?source=govdelivery&utm_medium=email&utm_source=govdelivery).
2. Statement by FDIC Board Member Martin J. Gruenberg on the Final Rule: Parent Companies of ILCs and Industrial Loan Companies at the FDIC Board Meeting : [https://www.fdic.gov/news/speeches/spdec1520e.html?source=govdelivery&utm\\_medium=email&utm\\_source=govdelivery](https://www.fdic.gov/news/speeches/spdec1520e.html?source=govdelivery&utm_medium=email&utm_source=govdelivery).
3. Final Rule : [https://www.fdic.gov/news/board/2020/2020-12-15-notice-dis-b-fr.pdf?source=govdelivery&utm\\_medium=email&utm\\_source=govdelivery](https://www.fdic.gov/news/board/2020/2020-12-15-notice-dis-b-fr.pdf?source=govdelivery&utm_medium=email&utm_source=govdelivery).
4. Press Release : [https://www.fdic.gov/news/press-releases/2020/pr20137.html?source=govdelivery&utm\\_medium=email&utm\\_source=govdelivery](https://www.fdic.gov/news/press-releases/2020/pr20137.html?source=govdelivery&utm_medium=email&utm_source=govdelivery)

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