

The Industrial Loan Company Loophole

The United Food and Commercial Workers International Union represents 1.3 million workers in North America, primarily in the grocery, retail, and meatpacking industries.

If Industrial Loan Companies (ILCs) are not properly regulated? and we believe that today they are not? the financial safety of working people and all Americans is put at risk. This is particularly true for ILCs owned by commercial entities, which are not subject to consolidated oversight by the Federal Reserve. The growth of commercial ownership of ILCs only makes these risks more acute. The list of risks is long, including everything from reduced consumer protections to insolvency, which can directly affect all of us.

The UFCW was one of the founding members of a diverse group of organizations known as the Sound Banking Coalition. In addition to the UFCW, the members of the coalition include the Independent Community Bankers of America, the National Association of Convenience Stores, and the National Grocers Association. The coalition was created early in 2003 when there were few commercial applicants for ILC charters.

The attempt by some commercial entities to add banking to their corporate portfolios reminds us of the lesson and the reasons for the long-standing policy separating banking and commerce in the United States. Separation of the financial from the commercial spheres has proven to be sound economic policy, and it has benefited consumers and workers who might otherwise find themselves at the mercy of a single large firm for not only the goods and services they need, but for their very financial welfare. It has also allowed for the development of a vibrant and competitive financial services industry that offers a multitude of products and services to consumers. The fact that so many commercial firms are now trying to circumvent this bedrock economic policy through a loophole in the law is troubling. We should not allow decades of good policy to be undone through an inadvertent backdoor mechanism.

Commercial ownership of banks creates the potential for two specific and very troubling problems. First, ILCs and their parent companies are not subject to consolidated supervision at the holding company level. Holding companies that own banks in this country are subject to consolidated regulation by the Federal Reserve Board. The Fed examines a bank holding company and all of its subsidiaries to ensure that neither the holding company nor any of the subsidiaries create solvency risks for the bank. More than simply avoiding risk, however, a bank holding company is supposed to be a source of financial strength for its bank subsidiaries, which can be a critical factor for banks that face financial difficulties. The Fed oversees bank holding companies whether the bank itself is a state-chartered bank or a national bank. Non-U.S. bank holding companies can be an exception to this rule, but only if those foreign firms are subject to similar, consolidated supervision in their home countries.



We should not hold ILCs to standards lower than those required of bank holding companies and foreign banks. Our obligation to protect people's funds should be the same. Indeed, on one level it is the same: ILC funds are, after all, protected by the same FDIC insurance that covers deposits in all other banks. And the problems with a failure can be just as devastating. During the savings and loan crisis, no one who lost money was comforted by the fact that the institution that failed was called an S&L rather than a bank. For the same reason, calling something an ILC should not change prudent financial regulatory policy. If consolidated supervision is needed for other banks? which we endorse and current law requires? then it should be required for ILCs.

The other key regulatory concept is the mixing of banking and commerce. Banks are supposed to be neutral arbiters of capital, providing financing to customers on an unbiased basis, unencumbered by commercial self-interest and competition. If those banks are owned by commercial companies, the conflicts of interest can skew loan decisions and lead to systemic problems. The potential distortion of the market is harmful both to the businesses (who may be competitors) as well as for consumers.

The FDIC has extended a moratorium on ILC applications submitted by commercial entities. The moratorium, which has now expired, was a short-term, stop gap measure. Fundamental policy decisions need to be made. We urge the Obama-Biden administration to close the ILC loophole and prevent the commercial firms from owning Industrial Loan Companies.