

United States House of Representatives
Committee on Financial Services
Washington, D.C. 20515

August 25, 2017

The Honorable Martin Gruenberg
Chairman
Federal Deposit Insurance Corporation
550 17th Street, NW
Washington, DC 20429

Dear Chairman Gruenberg,

I am writing to request that the Federal Deposit Insurance Corporation (“FDIC”) hold at least one public hearing on Social Finance, Incorporated’s (“SoFi”) application to establish an industrial loan company (“ILC”) to provide FDIC-insured Negotiable Order of Withdrawal (“NOW”) accounts and credit card products. As you know, because *de novo* ILC formations have been affected by regulatory and statutory moratoria for several years, the FDIC has not approved a deposit insurance application for a new ILC charter for some time. Since the enactment of the Dodd-Frank Wall Street Reform and Consumer Protection Act (“Dodd-Frank Act”), changes in the financial regulatory regime and financial services industry justify a public hearing to examine the policy and legal implications of granting Federal deposit insurance to ILCs generally, as well as to obtain greater input on the unique risks posed by granting it to a financial technology (“fintech”) company like SoFi, a number of which I will discuss in more detail below.

In addition, the small number of comment letters submitted on SoFi’s application, despite the high level of past public and congressional opposition to the ILC applications submitted by Walmart and Home Depot, calls into question whether there is adequate public awareness about this pending application and, by extension, also strengthens the case for why a public hearing on SoFi’s application is needed. Notwithstanding the fact that the short time period for public comment on SoFi’s application has expired, I believe that the FDIC’s decision on this application should be conducted in the most deliberative, transparent manner possible and, in order to do so, a public hearing is needed. While FDIC regulations appear to leave the determination of whether to hold a public hearing to the discretion of the regional director, I urge you to exercise your authority as Chairman to require that a public hearing be held on this ILC application to ensure that all external stakeholders and members of the public have adequate opportunity and time to provide input on this landmark application.

I. Concerns with regulatory oversight of ILCs generally and concerns with allowing fintech companies to be approved as federally-insured ILCs

Appropriate regulatory oversight of any ILC is an essential prerequisite to approving any application for deposit insurance backed by taxpayers. The FDIC has previously acknowledged the importance of strong oversight of any insured bank and its parent company when discussing oversight of ILCs.¹ In reaction to a number of concerns previously raised on the regulation of

¹ See Mindy West, FDIC Senior Examination Specialist, *The FDIC’s Supervision of Industrial Loan Companies: A Historical Perspective* (June 2004), https://www.fdic.gov/regulations/examinations/supervisory/insights/sisum04/industrial_loans.html (“Monitoring

ILCs, the FDIC even went so far as imposing several moratoria on its ability to approve ILC applications for deposit insurance in 2006 and 2007 to, in the words of former FDIC Chairman Sheila Bair in testimony before the House Financial Services Committee, “allow the FDIC to carefully weigh the safety and soundness concerns that have been raised regarding commercially-owned ILCs. At the same time... the moratorium provides an opportunity for Congress to consider the important public policy issues regarding the ownership of ILCs by commercial companies.”²

In 2007, the U.S. House of Representatives passed H.R. 698, the Industrial Bank Holding Company Act of 2007,³ which would have enhanced the regulation of the parent companies of industrial banks, restored the traditional separation between banking and commerce, prevented branch banking by some commercially-owned ILCs, prohibited the FDIC from granting new charters to commercial companies seeking to start or acquire ILCs, and bolstered the examination and enforcement authorities of the FDIC as an ILC regulator. The bipartisan bill was sponsored by former Reps. Paul Gilmor (R-OH) and Barney Frank (D-MA), and was approved by the House by a 371-16 vote. While the Senate did not act on the measure, a bipartisan companion bill was introduced in the Senate.⁴

In addition, others have made recommendations to improve regulatory oversight of ILCs. As Congress deliberated and drafted the Dodd-Frank Act in 2009 and 2010, the Treasury Department made the following recommendation:

“All companies that control an insured depository institution, however organized, should be subject to robust consolidated supervision and regulation at the federal level by the Federal Reserve and should be subject to the nonbanking activity restrictions of the BHC Act. The policy of separating banking from commerce should be re-affirmed and strengthened. We must close loopholes in the BHC Act for ... industrial loan companies....”⁵

and controlling the relationship between an insured entity and its parent company is an important part of the banking agencies' approach to supervision.”).

² Statement of Sheila C. Bair, Former FDIC Chairman, before the House Financial Services Committee on H.R. 698, The Industrial Bank Holding Company Act of 2007 (Apr. 25, 2007), <http://archives.financialservices.house.gov/hearing110/ht042507.shtml>.

³ <https://www.congress.gov/bill/110th-congress/house-bill/698>

⁴ S.1356, the Industrial Bank Holding Company Act of 2007 introduced by Sen. Sherrod Brown (D-OH) and former Sen. Wayne Allard (R-CO), <https://www.congress.gov/bill/110th-congress/senate-bill/1356>.

⁵ Department of the Treasury, *Financial Regulatory Reform – A New Foundation: Rebuilding Financial Supervision and Regulation* (June 17, 2009) page 34, <https://www.treasury.gov/press-center/press-releases/Pages/20096171052487309.aspx>. (On page 35, Treasury further explains: “Congress added the ILC exception to the BHC Act in 1987. At that time, ILCs were small, special-purpose banks that primarily engaged in the business of making small loans to industrial workers and had limited deposit-taking powers. Today, however, ILCs are FDIC-insured depository institutions that have authority to offer a full range of commercial banking services. Although ILCs closely resemble commercial banks, their holding companies can avoid the restrictions of the BHC Act – including consolidated supervision and regulation by the Federal Reserve – by complying with a BHC exception. Formation of an ILC has been a common way for commercial companies and financial firms (including large investment banks) to get access to the federal bank safety net but avoid the robust governmental supervision and activity restrictions of the BHC Act. Under our plan, holding companies of ILCs would become BHCs.”)

In the interim, Section 603 of the Dodd-Frank Act imposed a three-year moratorium on the FDIC's ability to approve deposit insurance for ILCs and required the U.S. Government Accountability Office ("GAO") to study the issue.⁶ GAO had previously studied ILCs and recommended that Congress consider improving supervision and oversight of ILCs to allow for broader supervision akin to the supervision of bank holding companies.⁷ GAO published its statutorily required report in January 2012, finding that,

"[t]he Bank Holding Company Act of 1956 (BHC Act) establishes the legal framework under which bank holding companies—that is, companies which own or control banks—operate and restricts the type of activities that these companies may conduct. The BHC Act excludes from these restrictions certain companies because the financial institutions they own are exempt from the BHC Act definition of "bank". However, these exempt institutions are eligible for FDIC insurance raising questions about continuing to exempt their holding companies from BHC Act requirements.... These institutions vary by size, activities, and risks. Larger institutions such as ILCs provide banking services similar to those of commercial banks and carry many of the same risks.... OCC officials and representatives of exempt institutions viewed the current oversight was sufficiently robust. FDIC officials indicated that supervision of the exempt institutions themselves was adequate, but noted that consolidated supervision authorities provide important safety and soundness safeguards. Officials from the Federal Reserve and Department of the Treasury stated that the exemptions should be removed, given that exempt institutions have access to FDIC insurance and the holding companies of most types of exempt institutions are not subject to consolidated supervision. The implications of subjecting exempt institutions and their holding companies to the BHC Act vary."⁸

Additionally, pursuant to Section 620 of the Dodd-Frank Act, Federal banking regulators issued a report to Congress and the Financial Stability Oversight Council in which the Board of Governors of the Federal Reserve System recommended, among other things, that Congress, "repeal the exemption that permits corporate owners of industrial loan companies (ILC) to operate outside of the regulatory and supervisory framework applicable to other corporate owners of insured depository institutions."⁹

The aforementioned concerns highlighted by the Federal Reserve and others regarding whether ILCs should be required to comply with the BHC Act have also been raised by stakeholders

⁶ See S. Rept. 111-176, the Restoring American Financial Stability Act of 2010, at page 83, <https://www.congress.gov/111/crpt/srpt176/CRPT-111srpt176.pdf>.

⁷ See GAO, *Industrial Loan Corporations: Recent Asset Growth and Commercial Interest Highlight Differences in Regulatory Authority*, (Sep. 15, 2005), <http://www.gao.gov/products/GAO-05-621>. ("Industrial loan corporations (ILC) emerged in the early 1900s as small niche lenders that provided consumer credit to low and moderate income workers who were generally unable to obtain consumer loans from commercial banks. Since then, some ILCs have grown significantly in size, and some have expressed concern that ILCs may have expanded beyond the original scope and purpose intended by Congress. Others have questioned whether the current regulatory structure for overseeing ILCs is adequate.... GAO is not recommending executive action but believes Congress should consider strengthening the regulatory oversight of ILCs...")

⁸ GAO, *Bank Holding Company Act: Characteristics and Regulation of Exempt Institutions and the Implications of Removing the Exemptions* (Jan. 19, 2012), <http://www.gao.gov/products/GAO-12-160>.

⁹ Board of Governors of the Federal Reserve System, FDIC and the Office of the Comptroller of the Currency, *Report to the Congress and the Financial Stability Oversight Council Pursuant to Section 620 of the Dodd-Frank Act* (Sep. 2016), page 28, <https://www.federalreserve.gov/newsevents/pressreleases/files/bcreg20160908a1.pdf>.

commenting on SoFi's application. For example, in the Independent Community Bankers of America ("ICBA")'s comment letter on SoFi's application, the group wrote,

"[f]or safety and soundness reasons and to maintain the separation of banking and commerce, the FDIC should deny SoFi Bank's application and impose a moratorium on future ILC deposit insurance applications. SoFi should be subject to the same restrictions and supervision that any other bank holding company of a community bank is subject to. Furthermore, Congress should close the ILC loophole because it not only threatens the financial system but creates an uneven playing field for community banks....Congress should immediately address this issue and permanently close the ILC legal loophole before it is too late and we have huge commercial or technology firms like Amazon, Google or Wal-Mart owning FDIC-insured ILCs and operating them without adequate holding company supervision and without any restrictions on the types of activities in which the holding company or the ILC's affiliates can engage."¹⁰

These concerns regarding the regulation of ILCs generally, and concerns about extending the existing regulatory framework of ILCs to fintech companies, should be carefully considered, including whether it is appropriate for firms like SoFi to have access to Federal deposit insurance by simply establishing a state-chartered ILC. Holding a public hearing on SoFi's application would provide an additional opportunity to weigh these concerns before acting on the application.

II. Shortcomings of existing regulatory authority for fintech companies

While some experts have touted the possibility that fintech firms can help promote financial inclusion, others have underscored the challenges posed for our current regulatory regime to oversee these types of companies and have underscored the need for policymakers to carefully evaluate the consequences of allowing them access to deposit insurance and the Federal Reserve discount window¹¹. Thus, Federal regulators have taken a varying degree of actions focused on fintech companies and services. For example, while the Office of the Comptroller of the Currency ("OCC"), under its "Responsible Innovation" initiative, has proposed a Special

¹⁰ ICBA letter to FDIC, (July 18, 2017). *Also see* Letter from Americans for Financial Reform (AFR) to FDIC, *RE: 20170820 - SoFi Bank - Deposit Insurance (New Bank)*, (July 18, 2017).

¹¹ See U.S. Department of the Treasury, *Opportunities and Challenges in Online Marketplace Lending*, (May 10, 2016), <https://www.treasury.gov/connect/blog/Pages/Opportunities-and-Challenges-in-Online-Marketplace-Lending.aspx>; National Economic Council, *A Framework for FinTech* (Jan. 13, 2017), <https://obamawhitehouse.archives.gov/blog/2017/01/13/framework-fintech>; and Congressional Research Service, *Marketplace Lending: Fintech in Consumer and Small-Business Lending*, (Sep. 6, 2016), ("Some observers assert that marketplace lending may pose an opportunity to expand the availability of credit to individuals and small businesses in a fair, safe, and efficient way. Marketplace lenders may have lower costs than traditional lenders, potentially allowing them to make more small loans than would be profitable for traditional lenders. In addition, some observers believe the accuracy of credit assessments will improve by using more data and advanced statistical modeling, as marketplace lenders do through their automated algorithms, leading to fewer delinquencies and write-offs. They argue that using more comprehensive data could also allow marketplace lenders to make credit assessments on potential borrowers with little or no traditional credit history. Other observers warn about the uncertainty surrounding the industry and the potential risks marketplace lending poses to borrowers, loan investors, and the financial system. The industry only began to become prevalent during the current economic expansion and low-interest-rate environment, so little is known about how it will perform in other economic environments. Many marketplace lenders do not hold the loans they make themselves and earn much of their revenue through origination and servicing fees, which potentially creates incentives for weak underwriting standards. Finally, some observers argue that lack of oversight may allow marketplace lenders to engage in unsafe or unfair lending practices.").

Purpose National Bank Charter for fintech companies (“fintech charter”)¹² questions have been raised about whether the benefits to consumers for this new charter will be widely and fairly shared, and whether there is adequate legal authority, let alone a clearly defined and modern regulatory framework, for such a fintech charter.¹³ Indeed, a lawsuit has been filed by state banking regulators challenging the OCC’s authority.¹⁴ As should be the case with the OCC and its proposal to use its authority to federally charter fintech companies, the FDIC should thoroughly consider the implications of offering access to the deposit insurance fund for ILCs that will result in expanding the type of institutions to it, like fintech firms. Fintech firms, whose operations cross state and international boundaries, and may exist entirely online, were undoubtedly beyond original congressional intent in permitting ILCs to access deposit insurance and it is appropriate for stakeholders to weigh in on whether it is appropriate for these firms to have this access without proper oversight of their parent companies.

SoFi was established six years ago¹⁵ as “a new kind of finance company taking a radical approach to lending and wealth management.”¹⁶ Granting SoFi’s application would set a precedent that a wide variety of other fintech companies may choose to follow even though concerns related to financial inclusion, consumer benefits, supervision, and regulation of such entities are still unresolved. Thus, the FDIC should carefully consider these concerns when reviewing SoFi’s application, and in doing so, hold a public hearing to allow for a fuller vetting of the advantages and disadvantages of extending an outdated regulatory framework for ILCs to fintech companies, and the potential implications for the broader financial system. Importantly, the public hearing could also shed more light on whether it may be more prudent for the FDIC to work with Congress to design a Federal regulatory framework for fintech companies. I would welcome your input for such an undertaking.

III. Consumer protection concerns

The chartering of a fintech company as an ILC also raises a number of consumer protection concerns that the FDIC should consider. For example, the California Reinvestment Coalition (“CRC”) has opposed SoFi’s application on the basis of concerns with the institution’s Community Reinvestment Act (“CRA”) plan, as well as its intended approach to financial inclusion, fair lending, and consumer protection.¹⁷ CRC notes that SoFi’s business model targets “students from elite universities that have strong earnings and wealth potential,” and offers products and services “designed to exclude working class households.” CRC also notes that SoFi’s CRA plan is grossly inadequate, considering that: (1) SoFi’s assessment area will be limited to areas in Utah, but the company will accept deposits and operate nationally; (2) SoFi’s

¹² <https://occ.gov/topics/responsible-innovation/index-innovation.html>

¹³ See OCC, *Public Comments on Exploring Special Purpose National Bank Charters for Fintech Companies*, <https://www.occ.gov/topics/responsible-innovation/fintech-charter-comments.html>, including comments from the Independent Community Bankers Association, Conference of State Bank Supervisors, National Consumer Law Center and National Community Reinvestment Coalition.

¹⁴ <https://www.csbs.org/news/press-releases/pr2017/Pages/042617.aspx>

¹⁵ Ann Carns, *SoFi Tapping Alumni to Help With Student Loans*, NEW YORK TIMES (Apr 3, 2012), <https://bucks.blogs.nytimes.com/2012/04/03/sofi-tapping-alumni-to-help-with-student-loans/>.

¹⁶ SoFi, *Our Story*, <https://www.sofi.com/our-story/>, (accessed on Aug. 7, 2017).

¹⁷ CRC letter to Kathy Moe, Regional Director, FDIC, *RE: CRC opposition to application by SoFi for an industrial bank charter* (July 18, 2017). CRC’s comment letter also notes that the Consumer Financial Protection Bureau’s complaint database includes 42 complaints by SoFi’s customers over the past two years related to improper fees, poor customer service, and loan fees; *see also*, National Community Reinvestment Coalition (“NCRC”) letter to FDIC, *RE: NCRC Comment Letter on SoFi Charter Application* (July 18, 2017).

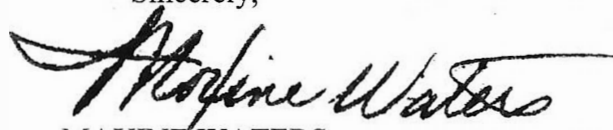
current core products are not designed to serve the “convenience and needs” of low- and moderate-income (“LMI”) communities in which the bank would operate,¹⁸ but rather are focused on serving SoFi’s members; and (3) SoFi’s CRA plan does not encompass measurable commitments to lending, investments, and services for LMI communities. CRC wrote:

“[t]he proposed bank’s CRA plan is woefully inadequate in terms of which communities will be served, and how they will be served. Perhaps most significantly, the Bank undermines the goals of the CRA by proposing to lend and take deposits nationally, but reinvest only locally, in the Salt Lake City area. The intent of the CRA is to ensure that banks, which benefit from various federal government subsidies, protections and rules, meet community credit needs by reinvesting deposits back into the communities from which they originated. Most likely, Salt Lake City and environs will comprise only a miniscule portion of the would-be bank’s deposits.... The Bank will be focusing on its existing SoFi members, and SoFi indicates that these members live in the top 10 metropolitan areas within the USA. It can be assumed that a plurality of SoFi deposits will come from these 10 metro areas. The Bank should clearly accept these 10 metro areas as part of its CRA assessment area.”¹⁹

Although companies are free to offer products and services based on their market choices, institutions must follow the law and should not be able to benefit from Federal deposit insurance if they are deliberately choosing to not provide financial services to the most vulnerable, underserved, and underbanked individuals in the country. The FDIC should gather more evidence regarding the financial inclusion, fair lending, and consumer protection concerns that arise from SoFi’s application by convening a public hearing.

In conclusion, there are a number of important policy and legal issues at stake with SoFi’s application that warrant the FDIC holding a public hearing.

Sincerely,


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¹⁸ *Id.* CRC letter. CRC notes that SoFi’s CRA plan identifies lending to LMI consumers through credit cards that “charge a much higher interest rate north of 20% percent.” CRC also stated “the fact that the bank’s main CRA loan product is a high interest rate credit card is unacceptable.”

¹⁹ *Id.* CRC Letter; *see also*, NCRC letter.